CIRCULAR LETTER NO. 21 /E

Central Assessment Directorate

Rome, 5 June 2012

SUBJECT: Settlement of International Tax Disputes.
The Mutual Agreement Procedures.

TABLE OF CONTENTS

INTRODUCTION

The last three years witnessed a substantial and steady increase of international tax disputes connected with mutual agreement procedures initiated to provide relief to instances of double taxation.

As a result, the Revenue Agency stepped up its efforts in providing technical assistance and support towards the Department of Finance – the body in charge for tax treaty policy and the management of mutual agreement procedures – in order to settle Italy's position with respect to its foreign counterparts.

Against this background, an increased involvement of the regional and provincial offices of the Agency plays a key role as far as the sharing of customary practices and the participation in the procedural phases instrumental to the satisfactory outcome of a mutual agreement procedure is concerned.

Based on the above, the current Circular clarifies a number of issues relating to the management of tax disputes in the framework of a mutual agreement procedure (hereinafter referred to as "MAP"), with a view to provide adequate consistency between the administrative action and the principles endorsed by international tax laws.

To this end, the Circular distinguishes between the different features of MAP proceedings established pursuant to either a Double Tax Convention in force between Italy and the Treaty partners (hereinafter referred to as "bilateral Convention" or "DTC") or the Convention 90/436/EEC of 23 July 1990 on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (hereinafter referred to as "Arbitration Convention" or "AC").

Moreover, the Circular outlines the various stages of the procedure, with reference to the interplay between MAPs and the remedies available under domestic law. Finally, the Circular provides certain clear ground rules with respect to the subjective and objective requirements and the steps to be followed in order to successfully initiate a MAP.

It is worth pointing out that instances of double taxation arising from adjustments to profits of associated enterprises based on domestic transfer pricing legislation[1] are amongst the most frequent ones leading to MAPs. This is due to the circumstance that the evaluation of the consistency with the arm's length conditions of transactions carried out between associated enterprises features a high level of complexity and technicality.

As a result, irrespective of the fact that the Circular applies to all the instances falling within the scope of the supranational provisions involved, the clarifications provided herewith focus, in particular, on the main issues relating to MAPs initiated following a transfer pricing adjustment.

1. INTERNATIONAL LEGAL BASIS

As already mentioned in the introduction, the relevant international sources are either the bilateral Conventions for the avoidance of double taxation or the Arbitration Convention.

DTCs, as well as containing dedicated provisions aimed at preventing or mitigating instances of international double taxation, provide a specific tool allowing resolution of disputes potentially arising amongst States: the mutual agreement procedure provided for by Article 25 of the OECD Model Tax Convention on Income and on Capital (hereinafter referred to as "OECD Model") and its Commentary[2].

MAP is an instrument of direct consultation between the tax administrations of Contracting States, establishing a dialogue by means of their respective "competent authorities" – through the communication channels that they consider more appropriate - for the purpose of reaching an agreement on the case at stake. To this end, MAP represents the instrument for the resolution of

[1] In particular, reference is made, respectively, to (i) the provisions contained in Article 110, para.7 of the Income Tax Code approved with the Presidential Decree No. 917 of December 22, 1986 applicable to transactions between legal entities, businesses, permanent establishments or, more in general, other entities part of the same multinational group; or (ii) to the provisions contained in articles 7 and 9 of DTC and that of article 4 of the AC.

[2] OECD Committee on Fiscal Affairs, *Model Tax Convention on Income and on Capital, [as they read on 22 July 2010]*.

international tax disputes in cases where a taxpayer resident in one of the two Contracting States considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of the Convention.

Italy has entered into a substantial amount of DTCs for the elimination of juridical and economical double taxation by means of allocating the taxing power amongst the Contacting States[3]. Each of those contains a provision equivalent to Article 25 of the OECD Model with regard to MAP.

In order to facilitate the effective and transparent management of MAPs, as of 2004 the OECD began a project aimed at improving the mechanism for the settlement of international tax disputes. This project led to the release of a *"Manual on Effective Mutual Agreement Procedures"* (hereinafter referred to as "*MEMAP*")[4] for an effective management of MAPs. The Manual provides to both tax administrations and taxpayers the key information for the functioning of a MAP, identifying some best practices to which countries should adhere to the maximum extent possible.

Chapter IV of the OECD Transfer Pricing Guidelines[5] as well, examining the administrative approaches to avoid and resolve transfer pricing disputes, contains a specific section regarding MAPs. In there, the general features of MAPs are highlighted as well as the key issues surrounding corresponding adjustments to carry on once a primary transfer pricing adjustment has been carried out.

Besides bilateral Conventions the abovementioned Arbitration Convention applies to cases of economic double taxation arising from transfer

---

[3] Juridical double taxation arises when one item of income (e.g., dividends or interest) is taxed twice or more in the hands of the same taxpayer in two or more States. Economic double taxation arises where two or more different taxpayers are taxed by two or more States in respect of the same income. See the Commentary to Article 23 A and B of the OECD Model, paragraphs. 1 e 2.

[4] OECD – Centre for Tax Policy and Administration, *Manual on Effective Mutual Agreement Procedures (MEMAP) - February 2007 Version*, available online at www.oecd.org/ctp/memap.

[5] *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, the latest version of which has been approved by the OECD Council on 22 July 2010.

pricing adjustments to profits of associated enterprises resident in the European Union.

As regards the application of the Arbitration Convention, it is also necessary to refer to the recommendations included in the *"Revised Code of Conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises"*, adopted by the Council of the European Union on 22 December 2009[6] (hereinafter referred to as the "Code of Conduct").

2. DOMESTIC LEGAL BASIS

As regards the domestic legal system, the relevant provisions to properly establish a MAP may be found, respectively, in the DTCs entered into by Italy[7] – all ratified by law - and in the Arbitration Convention[8], ratified by Law No. 99 of 22 March 1993.

Moreover, with regard to Italian tax legislation an express reference to MAP is included in Article 110, paragraph 7, second sentence, of the Income Tax Code, laying down "*General Provisions concerning valuations*". In particular, Article 110 stipulates that the provision concerning the application of the arm's length principle "*also applies if the result is a downward adjustment to taxable income, but only insofar as it is the outcome of binding agreements concluded with the competent authority of a contracting state pursuant to a mutual agreement procedure provided for by international tax treaties*". As a result, the above mentioned article shows, in particular, the interaction between domestic transfer pricing provisions and DTCs.

---

[6] Published on the Official Journal of the European Union n. 322/1 of 30 December 2009. It is the revision of the Code of Conduct approved in 2006 by the Council of the European Union (2006/C 176/02).

[7] An updated list of the bilateral Conventions is available in the web site of the Department of Finance, www.finanze.it

[8] The Arbitration Convention, entered into force on 1 January 1995, expired on 1 January 2000. The relevant Protocol amending the Convention, ratified in Italy by law 28 April 2004, No. 132, entered into force on 1 November 2004 , effective from 1 January 2000.

3. STATUTORY BODIES INVOLVED

The statutory bodies overseeing the management and discussions of MAPs are the Ministry of Economics and Finance – Department of Finance – acting as Italy's competent authority, and the Revenue Agency.

From a general standpoint, the term "competent authority" identifies the body representing a Contracting State in the international relations arising from a DTC. With specific reference to MAP, the competent authority is the body representing the Contracting State with respect to both the internal relations with its taxpayer and the external relations with the other Contracting State involved in the MAP.

The competent authority guarantees the application in good faith of the DTC, trying to reach solutions with the other Contracting State sticking to the principles of equity and transparency.

Based on this, the Revenue Agency provides to Italy's competent authority the technical support and the proper co-operation throughout the entire duration of the MAP, in particular during the procedural phase connected with the drafting of the *"position paper"*[9] and with the exchange of correspondence with the competent authority of the other Contracting State regarding the factual and juridical elements underlying the case falling into the scope of the MAP. The Agency's role is relevant also in light of the need of guaranteeing consistency between the technical position expressed within the MAP and those arising in other contexts, such as interpretation of tax legislation, auditing and dispute prevention [10].

[9] The term "*position paper*" refers to the document whereby each tax administration outlines the legal and technical issues underlying its claim to uphold its view.

[10] As regards dispute prevention measures, express reference is made to the "International Standard ruling" instrument, introduced in Italy by article 8 of Decree Law No. 269 of 30 September 2003, converted with amendments by Law No. 326 of 24 November 2003 and implemented with Regulations of the Director of the Revenue Agency of 23 July 2004.

4. ARTICLE 25 OF THE OECD MODEL TAX CONVENTION

As already mentioned, all DTCs entered into by Italy include a provision equivalent to Article 25 of the OECD Model endorsing the recourse to MAPs.

Based on paragraphs 1 and 2 of Article 25 of the OECD Model, MAP is a remedy available to taxpayers claiming to be actually or potentially subjected to taxation not in accordance with the provisions of the DTC.

Moreover, pursuant to paragraph 3 of Article 25 of the OECD Model a MAP may be initiated directly by either of the competent authority of each Contracting State.

The two circumstances are discussed separately.

4.1. MAP initiated by the competent authorities

The first sentence of paragraph 3 of Article 25 of the OECD Model provides for that a MAP is initiated by the competent authorities in order to resolve by mutual agreement problems relating to the interpretation or application of the Convention.

The paragraph refers to general difficulties encompassing categories rather than single taxpayers, although any such difficulty may arise in respect of individual cases falling into the scope of paragraphs 1 and 2 of Article 25.

Moreover, the second sentence of paragraph 3 enables the competent authorities to deal also with such cases of double taxation as do not come within the scope of the provision of the DTC. For instance, this is the case of an enterprise resident of a third State having permanent establishments in both Contracting States.

As a result, in addition to having recourse to a MAP aimed at resolving instances of double taxation arising in connection with the violation of any provision of a DTC, a MAP may also be carried out upon the impulse of the competent authorities themselves in order to resolve difficulties of interpretation or application of a DTC or to resolve cases falling outside the scope of a Convention.

The agreement reached by the competent authorities in the context of a MAP activated pursuant to paragraph 3 of Article 25 of the OECD Model affects a wide number of taxpayers. Accordingly, it has to be subjected to proper forms of disclosure.

4.2. MAP initiated by the taxpayer

4.2.1. Subjective scope

Paragraph 1 of Article 25 of the OECD Model stipulates that in the event a person considers that he has been or will be subjected to taxation not in accordance with the Convention, he is entitled to submit the case to the competent authority of his State of residence or, in the event paragraph 1 of Article 24 (*Non-discrimination*) of the OECD Model would apply, to the competent authority of the State of which he is a national.

It has to be pointed out that not all the DTCs entered into by Italy contain reference to the notion of “nationality”, in addition to that of “residence”. As as result, should the taxpayer decide to invoke the non-discrimination provision, he has to make a direct reference to the DTC applicable in the case at stake in order to determine whether or not he is entitled to activate a MAP.

For the sake of clarity, the term “person” encompasses individuals, legal entities, enterprises and any other association or entity liable to tax and resident for tax purposes in the jurisdiction of either Contracting State.

Moreover, it is not necessary that double taxation has already occurred. It is sufficient, in order for the taxpayer to set the procedure in motion, that he does establish that the actions of one or both of the Contracting States will likely result in double taxation.

4.2.2. Objective scope

Article 25, paragraph 1 and 2 of OECD Model covers all cases of juridical and economical double taxation suitable to affect both individuals, enterprises and other entities to which the Convention applies.

As regards individuals, a category of cases may concern, for example, double tax residence, an improper application of a withholding tax on dividends, interest and royalties, a conflict of qualification regarding the employment income received by a taxpayer etc.

As regards taxpayers other than individuals, other cases generally involve the existence of a permanent establishment, the proper allocation of profits to associated enterprises part of a multinational group, the qualification of income either as business profits or as particular class of income falling within the scope of a dedicated provision of a DTC etc.

4.2.3. Terms for MAP submission

In order to properly identify the final term within which the taxpayer may submit his MAP opening request it is necessary to refer to the timing provided for by the single DTC applicable to the case at stake

Indeed, although the OECD Model sets a three year time limit from the date of the first notification of the action resulting in taxation not in accordance with the provisions of the Convention, most of the DTCs entered into by Italy provide for a shorter time limit (generally two years).

In this respect, the notion of "*first notification of the action resulting in taxation not in accordance with the provisions of the Convention*" has to be construed in the most favorable manner to the taxpayer, pursuant to the interpretation provided for by paragraph 21 of the Commentary to Article 25 of the OECD Model.

It is therefore necessary to distinguish (i) the situation in which the taxation not in accordance with the provisions of a DTC claimed by the taxpayer arises from the application of a domestic tax or withholding tax (e.g., withholding taxes applied on dividends, interest and royalties) from (ii) the case where taxation not in accordance with the provisions of a DTC is triggered by adjustments carried out by the tax administration (e.g. audits, notifications or transfer pricing adjustments to profits of associated enterprises).

As regards the case *sub* (i) the term for a valid submission of a MAP request runs either from the date of notification by the tax administration of the refund denial submitted with respect to the application of a withholding tax; or from the ninetieth day following the submission of the refund's request without a decision by the Agency, pursuant to Article 37, second paragraph, and Article 38 of the Presidential Decree No. 602 of 29 September 1973[11].

As regards the case *sub* (ii) – consistently with the position expressed by Italy in adhering to the Code of Conduct for the effective implementation of the Arbitration Convention, the initial term of the period within which the taxpayer may submit his case concurs, for the purpose of a bilateral MAP as well, with the date of notification of the formal assessment triggering taxation not in accordance with the provisions of the DTC.

However, it has to be pointed out that the taxpayer is entitled to submit the request before he has been notified with a formal assessment: it is possible, for instance, for the taxpayer to submit the MAP opening request following the notification of an audit report (so-called "*processo verbale di constatazione*"). In the latter case, the MAP is deemed to be opened from the date in which the competent authority has received the request together with the minimum set of information instrumental to set the procedure in motion.

4.2.4. Contents and submission of a MAP request

In principle, the taxpayer has to submit a MAP request directly to the competent authority of his State of residence for tax purposes.

With specific reference to transfer pricing adjustments, the MAP opening request has to be submitted, by the resident enterprise recipient of the assessment notice, to the State which has released the act leading to double taxation. However, against this background the MAP request can be validly submitted by the foreign associated enterprise as well, which has been already

[11] In this regard, non resident taxpayers are obliged to submit their request to the Pescara Operational Centre.

taxed in respect of the profits corresponding to the primary transfer pricing adjustment. In this case, the foreign associated enterprise deals with the competent authority of its State of residence to claim relief from double taxation arising within the group.

It is worth noting that, in addition to the subjects entitled to legally represent taxpayers other than individuals, the MAP can be set in motion by the general or special taxpayer's attorney. In particular, the proxy has to be conferred pursuant to the procedure established by Article 63 of the Presidential Decree No. 600 of 1973.

In the event the MAP request is submitted by a taxpayer resident for tax purposes in Italy, it has to be drafted in free form and sent via letter with advice of delivery to Ministero dell'Economia e delle Finanze, Dipartimento delle Finanze – Direzione Relazioni Internazionali, or it can be directly hand-delivered to the above mentioned Office with receipt of the copy of the first page of the request with secretary's stamp and date of receipt. It is possible – as well as advisable in case of hefty documentation - to submit an electronic version of the supporting documentation regarding the MAP request.

The submission of a MAP request is free of charge.

In order to accelerate the evaluation process and the establishment of subsequent contacts with the foreign competent authority, the request must preferably contain the following pieces of information:

1. the taxpayer's data (i.e. name, address and tax identification number);
2. the tax domicile of the taxpayer or of any legitimate recipient to which the tax administration can address any communication regarding the state of the MAP;
3. an illustration of the facts and circumstances of the case, with a specific reference to the tax years in which double taxation occurred or might occur;

4. a description of any administrative or legal proceeding undertaken in Italy, such as a request for a tax settlement (e.g. so-called "*accertamento con adesione*") or the submission of a legal appeal;
5. a description of the remedies, if any, activated in the other Contracting State to eliminate the double taxation;
6. a copy of the tax documents which resulted, or that might result, in taxation not in accordance with the provisions of the bilateral Convention (in particular, a copy of the notice denying the refund or, in case of an implied denial, a copy of the refund claim submitted pursuant to Article 37, second paragraph, and 38 of the Presidential Decree No. 602 of 1973); and
7. any other form of documentation instrumental to ease the scrutiny by the competent authorities involved in the MAP.

Finally, the request must include the formal commitment of the taxpayer to answer in a timely and exhaustive manner to any query from the competent authority, as well as to make available any additional documentation that might be necessary to carry on the procedure.

With specific reference to MAPs arising from a transfer pricing adjustment, reference is made to the guidance provided for by point 5.5 of this Circular with respect to the steps for presenting a MAP on the basis of the AC.

4.2.5. Interplay with domestic legal proceedings

Paragraph 1 of Article 25 of the OECD Model stipulates that a MAP request can be validly submitted by a taxpayer "*irrespective of the remedies provided by the domestic law of those States*". In this respect, most of the DTCs entered into by Italy contain, in their accompanying Protocol, an interpretative provision regarding the MAP article whereby the expression "*irrespective of the remedies provided by the domestic law"* shall be construed so that "*the mutual agreement procedure is not alternative to the national contentious proceedings*

which shall be, in any case, preventively initiated, when the claim is related to an assessment of Italian tax not in accordance with the Convention" (or equivalent).

Generally, next to a MAP activated in Italy on the basis of a DTC, a court appeal proceeding exists pursuant to domestic law. In this respect, the opportunity to file a complaint to a tax judge aims at avoiding that, pending the MAP, the tax assessed in Italy becomes final without the possibility of being modified under the agreement potentially reached by the competent authorities involved.

However, the parallel progress of a MAP and a domestic court appeal leaves room to a potentially conflicting outcome between the domestic court judgment and the agreement achieved by the competent authorities involved. Within this scenario, the tax administration might find itself unable to comply with the international obligation arising from the mutual agreement.

As a result, should the competent authorities agree to eliminate double taxation before a judgment is issued by an Italian court, the taxpayer can accept this agreement, but he has to renounce to the proceeding in order to give execution to the agreement.

In the opposite scenario, i.e. where a judgment intervened before the competent authorities reached an agreement pending the MAP, the Italian competent authority will inform its foreign counterpart of the outcome of the domestic litigation. In this case, should the judgment not eliminate double taxation, the latter may not be avoided unless the foreign competent authority concurs with the position expressed by the Italian tax court.

Pending the MAP, it will be up to the taxpayer to decide whether or not to require the suspension of the domestic court appeal. To date, recent experience shows that tax courts have granted the suspension of the litigation proceeding waiting for the outcome of the negotiations between the competent authorities. Should the latter not be able to reach an agreement, the taxpayer is entitled to re-activate the litigation.

Lastly, it is worth noting that in the event an adjustment occurred in the other Contracting State, the court appeal potentially opened in the foreign jurisdiction does not preclude the opening and progress of the MAP insofar as the foreign tax administration shares the same view.

4.2.6. Arbitration clause

The essential feature of the MAP opened on the basis of a DTC is that the competent authorities are not committed to an "obligation of result" as far as the elimination of double taxation is concerned. Under a mere "obligation of diligence" the two tax administration "*shall endeavor*" to eliminate by mutual agreement taxation not in accordance with the Convention.

Within this line of reasoning, paragraph 37 of the Commentary to Article 25 of the OECD Model clarifies the above mentioned concept by stating that "*Paragraph 2 no doubt entails a duty to negotiate; but as far reaching mutual agreement through the procedure is concerned, the competent authorities are under a duty merely to use their best endeavours and not to achieve a result*".

In practice, this entails that the case submitted to the competent authorities of the Contracting States may not be resolved.

More in detail, it is worth recalling the amendments introduced in 2008 to the text of Article 25 of the OECD Model, where paragraph 5 provides for a mandatory arbitration phase in the event the competent authorities are unable to reach an agreement within two years.

The new paragraph 5 of Article 25 is applicable only insofar as its inclusion is negotiated (or re-negotiated) in the new (or existing) DTCs. This depends on the willingness of the States involved in the negotiation, that may opt for the inclusion of the clause in DTCs concluded with certain treaty partners by taking into account a number of factors.

It goes without saying that a DTC containing a provision equivalent to paragraph 5 of Article 25 of the OECD Model enhances the effectiveness of a MAP.

To date, Italy has entered into thirteen DTCs with other treaty partners containing an arbitration clause[12]. Such a clause, included by Italy in DTCs negotiated before the introduction of the arbitration clause in the OECD Model, allows for the activation of an arbitration procedure only upon the mutual consent of both the Contracting States as well as the taxpayer. As a result, the Contracting States have no obligation (mandatory arbitration) to enter into arbitration in the event the controversy has not been mutually agreed. In some instances, the effectiveness of the clause has been subjected to the prior condition of the exchange of diplomatic notes amongst the Contracting States[13]. The exchange of notes, as well as showing the willingness of the Contracting States to implement the arbitration clause, aims at defining the operational terms of the arbitration (such as the criteria for establishing the arbitration commission, those relating to the members' selection, the sharing of costs, the selection of the working language etc.).

4.2.7. Suspension of tax collection

There are no dedicated procedures aimed at the suspension of tax collection pending MAPs activated on the basis of a DTC. However, it is acknowledged the possibility for the taxpayer to get access to the remedies ordinarily available to the taxpayer, such as the administrative suspension or the suspension granted by a tax court, respectively provided for by Article 39, paragraph 1, of the Presidential Decree No. 602 of 1973 and by Article 47 of the Legislative Decree No. 546 of 31 December 1992.

4.2.8. Procedural phases

Paragraph 2 of Article 25 of the OECD Model stipulates that, in the event the competent authority considers that the taxpayer's claim is justified, but

[12] To date, the States with which Italy has entered into DTC containing an arbitration clause are: Armenia, Canada, Croatia, Georgia, Ghana, Jordan, Kazakhstan, Lebanon, Moldova, Slovenia, Uganda, Uzbekistan and United States of America.

[13] To date, see the current DTCs: Canada, Ghana, Kazakhstan, United States of America and Uzbekistan.

is not able to unilaterally achieve a satisfactory solution, it shall endeavor to resolve the case by mutual agreement with the competent authority of the other Contracting State. As a result, it is possible to identify two different phases in the mutual agreement procedure.

In the first phase, the competent authority which has received the taxpayer's claim has to decide whether or not the submission is receivable. To this end, the competent authority must evaluate that the subjective and objective requirements to open a MAP are properly fulfilled. In particular, the competent authority has to assess whether the taxpayer has properly submitted the arguments whereby the actions of one or both the Contracting States result or will result in taxation not in accordance with the DTC. In the event the MAP is related to the refund of taxes collected not in accordance with a DTC provision, the competent authority jointly with the Revenue Agency ponders the validity of the submission and ascertains that a legitimate request for refund was filed as well as that the refund was denied or the terms elapsed for the creation of the so-called "silence-denial".

Should the MAP request by the taxpayer be deemed legitimate, the competent authority must first evaluate whether grounds exist for resolving unilaterally the situation of taxation not in accordance with the DTC. In the opposite scenario, the taxpayer's request will be notified to the competent authority of the other Contracting State to set the procedure in motion.

Based on the above, once the Ministry of Economy and Finance, Finance Department receives the taxpayer's submission for opening the MAP, it will evaluate – based on the information at its disposal – the validity of the request (in the above terms of subjective and objective requirements) and will involve the Revenue Agency for its advice on controversial issues where necessary.

Moreover, in this phase the competent authority can invite the taxpayer to provide any supplementary information and documentation instrumental for setting the procedure in motion. Furthermore, the competent authority will solicit

the taxpayer to submit its refund request based on Article 37 and 38 of the Presidential Decree No. 602 of 1973 in the event he has not done it already.

The competent authority will also inform the taxpayer whether or not the request has been accepted and the procedure properly set in motion.

Should double taxation arise from an assessment notice issued by the Revenue Agency, the latter will consider whether – *prima facie* – there are any grounds for a unilateral elimination of double taxation, i.e. by way of "self-tutelage" pursuant to the Law Decree No. 564 of 30 September 1994, converted with amendments by Law No. 656 of 30 November 1994. On the same footing, should double taxation arise from an assessment notice issued by a foreign tax administration, the Revenue Agency will consider whether room exist to grant a refund or tax relief to the resident taxpayer, as the foreign assessment is clearly consistent with the DTC provision at stake.

Instead, in the event the feasibility of a unilateral elimination of double taxation be excluded, Italy's competent authority will promptly inform its foreign counterpart and the Revenue Agency of its decision of setting the MAP in motion.

The opening date of the MAP concurs with the date where the taxpayer's request was submitted together with the required documentation, unless the filing of supplementary documentation is necessary. In the latter case, the MAP is deemed open from the date of the filing of the supplementary documentation.

Should the MAP request be submitted by an associated enterprise in the other Contracting State involved in the procedure (in the event of a transfer pricing adjustment), the opening date is the one promptly communicated by the foreign competent authority.

In case of a MAP opened according to a DTC, the Italian tax administration aims at following – as much as possible – the timing and procedural recommendations contained in the Code of Conduct for the effective

implementation of the Arbitration Convention. See point 5.8 of this Circular for more details.

The relationship between the competent authorities instrumental for dispute resolution in cases of double taxation generally takes place via the exchange of written position papers and the organization of meetings amongst the parties, where necessary. As a rule of thumb, the first competent authority sending its position paper is the one representing the Contracting State which has adopted the measure leading to double taxation. Generally, English language is adopted for drafting the position papers.

4.2.9. The role of the taxpayer

The MAP is a dispute resolution mechanism between Contracting States in the exercise of their tax sovereignty. The sole parties involved in the procedure are the competent authorities of the two Contracting States, which are entitled to sign the bilateral agreement potentially reached.

Notwithstanding the above, the taxpayer is invited to assume a proactive role, in particular with respect to the need of supplying a thorough and accurate description of the case at stake in order to provide all the relevant information as necessary to an exhaustive scrutiny. Accordingly, the taxpayer is required to assume a co-operative, transparent behavior in accordance with the principle of good faith.

On the other hand, the taxpayer is entitled to be informed about the development of the procedure. In particular, pursuant to the recommendations contained in the *MEMAP* (see Section 3.3.3. and the *best practice* No. 14) the taxpayer should be timely informed by the competent authority on the stage of the procedure and he may require to discuss his position with reference to the dispute.

In the event the MAP has been opened following a transfer pricing adjustment, paragraph 40, letter (c) of the Commentary to Article 25 of the OECD Model contains the further recommendation whereby the taxpayers

concerned should be given every reasonable opportunity to present the relevant facts and arguments to the competent authority both in writing and orally.

As a rule, the above mentioned practices are observed by the Italian tax administration. The facts and arguments presented may be jointly considered by the Finance Department and the Revenue Agency.

4.2.10. Conclusion of a MAP

In general, if the competent authorities reach an agreement the one who received the opening request will inform the taxpayer about the outcome of the negotiation. In the meanwhile, the Revenue Agency will execute the agreement and provide, if the case, either for the refund or the relief on the tax not due as well as interest and penalties applied. In case the MAP is triggered by a transfer pricing adjustment, generally the Italian competent authority informs the resident taxpayer of the outcome of the negotiations also in the event the MAP request was submitted to the foreign competent authority by the non-resident taxpayer.

Should the agreement be reached pending a domestic court appeal, the taxpayer may opt to either accept the agreement reached within the MAP or reject it and proceed with the domestic litigation. In any event, the taxpayer is obliged to inform both the competent authority and the Central Assessment Directorate of the Revenue Agency regarding the choice he opted to pursue.

4.2.11. Extension of the MAP outcomes

Within the exclusive scope of the DTCs and pursuant to the evaluation of the competent authorities, the effects of the agreement reached within the MAP may be prolonged to the tax years immediately subsequent to those in dispute on the assumption that the set of facts and circumstances subject of the MAP have remained unchanged.

Such a scenario often arises for MAPs set in motion to resolve disputes regarding income qualification matters with respect to one of the categories

provided for by a DTC in order to properly allocate the taxing rights amongst the Contracting States,

As a result, following the successful conclusion of the negotiations within the procedure and subject to the condition that the legal and factual circumstances remained unchanged also during the taxable years subsequent to those falling within the scope of the mutual agreement, Italy's competent authority may consider, together with the other Contracting State, to prolong the effects of the agreement, insofar as the taxpayer gives his explicit consent.

5. THE EU ARBITRATION CONVENTION

The Arbitration Convention, signed by the Member States on 23 July 1990, was adopted with the aim of ensuring – at least at the EU level – certainty with respect to the resolution of disputes arising from transfer pricing adjustments and the subsequent elimination of double taxation within a reasonable time frame.

The provisions contained in the AC, although originating in part from the OECD Model, have full autonomy in that, in order to be effective they neither refer nor need to be supplemented by the corresponding provisions of the DTC entered into by the Member States.

Pursuant to Articles 1 and 4 of the AC, the Convention applies when on the basis of the arm's length principle a Contracting State makes an upward adjustment to profits of a resident enterprise by including profits that have been already taxed in the hands of an associated enterprise resident of another Contracting State. Within this scenario, should the two enterprises and the other Contracting State reject the adjustment, Article 5 provides for the possibility that a MAP is set up pursuant to Article 6 of the AC.

Moreover, pursuant to paragraph 1 of Article 7 of the AC, in the event the competent authorities concerned fail to reach an agreement that eliminates double taxation within two years of the date on which the case was first submitted, they shall set up an advisory commission charged with delivering its

opinion on the elimination of double taxation in question. Article 12 of the AC stipulates that the competent authorities shall act in accordance with the advisory commission's opinion or shall jointly take a decision which deviates from the advisory commission's opinion as far as this decision will eliminate double taxation.

Accordingly, under the AC there is an obligation to resolve the dispute, whereas Article 25 of the OECD Model provides the sole duty of using the best endeavors and not to achieve a result.

Hereinafter this Circular provides a detailed description of the implementation of a MAP under the AC. To this end, the Italian tax administration acts consistently with the recommendations of the previously mentioned Code of Conduct of 22 December 2009. See the Code of Conduct itself for more details.

5.1. Subjective scope

The taxpayers entitled to submit a MAP request to Italy's competent authority are:

a. the resident enterprises, with respect to their interest ownership[14] existing with enterprises resident in another Member State of the European Union; and

b. the permanent establishments in Italy of enterprises resident in another Member State.

These categories of taxpayers may present their request insofar as the Italian tax administration or that of another Member State adjusted or will adjust

[14] Pursuant to article 4 of the AC, an interest ownership exists between the Italian resident enterprise and the enterprise resident in another Member State when:

i. the resident enterprise participates, directly or indirectly, in the management, control or capital of the enterprise resident in another Member State;
ii. the enterprise resident in another Member State participates, directly or indirectly, in the management, control or capital of the resident enterprise;
iii. the same persons (resident either in Italy or in a foreign State, the latter being either a EU or a third State) participate, directly or indirectly, in the management, control or capital of the Italian enterprise and the one resident in another Member State.

the profits of associated enterprises resident in their jurisdiction or those of permanent establishments situated therein.

5.2. Objective scope

Article 4 of the AC lays down the arm's length principle. Article 1 outlines the scope of the AC, whereby "*this Convention shall apply where, for the purposes of taxation, profits which are included in the profits of an enterprise of a Contracting State are also included or are also likely to be included in the profits of an enterprise of another Contracting State on the grounds that the principles set out in Article 4 and applied either directly or in corresponding provisions of the law of the State concerned have not been observed*".

The above entails that in the event the Revenue Agency adjusts upwards the profits of an associated enterprise, the only relevant domestic rules entitling the taxpayer to have access to the AC are the transfer pricing rules provided for by Article 110, paragraph 7, and Article 9, paragraph 3, of the Income Tax Code.

In other words, taxpayers who have grounded their MAP requests based on claims other than those referred to the violation of transfer pricing rules (including those regarding the so-called "inherency" of costs based on Article 109, paragraph 5 of the Income Tax Code) will be denied access to the procedure. Within this scenario the competent authority – after having obtained the opinion of the Agency – informs the taxpayer about the exact scope of the items falling within the MAP, limiting the discussions solely to transfer pricing adjustments.

5.3. Serious penalties

As regards the legal grounds preventing a MAP from being opened, Article 8, paragraph 1 of the AC stipulates that "*the competent authority of a Contracting State shall not be obliged to initiate the mutual agreement procedure or to set up the advisory commission referred to in Article 7 where legal or administrative proceedings have resulted in a final ruling that by actions giving*

rise to an adjustment of transfers of profits under Article 4 one of the enterprises concerned is liable to a serious penalty".

Moreover, paragraph 2 of the latter provision adds that "*where judicial or administrative proceedings, initiated with a view to a ruling that by actions giving rise to an adjustment of profits under Article 4 one of the enterprises concerned was liable to a serious penalty, are being conducted simultaneously with any of the proceedings referred to in Articles 6 and 7, the competent authorities may stay the latter proceedings until the judicial or administrative proceedings have been concluded*".

With respect to this issue, Italy has taken the view (by means of a unilateral declaration attached to the AC) that: "*the term 'serious penalties' means penalties laid down for illicit acts, within the meaning of the domestic law, constituting a tax offence*".

In this connection, the Code of Conduct recommends Member States – in light of the practical experience acquired on the issue – to clarify/amend "*their unilateral declarations … in order to better reflect that a serious penalty should only be applied in exceptional cases like fraud*".

Against this background, it is worth noting that reference in the unilateral declaration to penalties applicable for tax offences has been construed in practice in exactly the same way as suggested by the Code of Conduct, i.e. by considering only the exceptional cases of a fraudulent behavior, generally not arising in transfer pricing cases.

Exceptional instances where access to MAP is precluded (a situation not occurred so far in Italy) mainly include cases where a fraudulent and/or fictitious behaviour arose, as described by Articles 2 (*Fraudulent Tax Return by means of invoices or other documents regarding non-occurred transactions*) and 3 (*Fraudulent Tax Return via other devious means*) of the Legislative Decree No. 74 of 10 March, 2000. In the above-mentioned situations the alleged transaction did not occur and/or the alleged price was not the one actually agreed amongst the parties. As a result, the focus is towards cases concerning the use of fictitious

invoices or other documents referring to “material facts” other than those actually occurred, and beyond any valuation of the consistency of the prices with the arm’s length principle. In the latter regard, it is useful to recall the Supreme Court’s judgment No. 14772 of 2002 where the judges, in holding the criminal liability of taxpayers charged with tax fraud, held that any reference to “pricing” was inappropriate as the transactions amongst the taxpayers themselves did never occur.

As regards in particular Article 3 (*Fraudulent Tax Return via other devious means*), such a behaviour in principle should be excluded as far as transfer pricing is concerned, considering that inconsistency with the arm’s length principle should involve neither a fictitious accounting representation nor it could be possible to deem fraudulent behaviours those that are ordinarily documented by taxpayers.

As a result, transfer pricing issues – although a judicial prosecutor is always entitled to evaluate whether the topic is relevant for criminal purposes - would fall out of the scope of application of Articles 2 and 3 of the Legislative Decree No. 74 of 2000. Yet, it seems theoretically possible that inconsistency with the arm’s length principle – reflected in the accounting/tax returns – would fall in the “residual” scope of Article 4 (*Unfaithful Tax Return*) of the above mentioned Decree.

However, the Legislative Decree No. 74 of 2000 is clearly focused on tax crimes related with the process leading to the determination of the taxable base and the tax due. As also derives from the relevant governmental report attached to it, the Decree does not even exclude the valuation processes as such, although transfer pricing methods are deemed to be really complex tools in terms of arm’s length valuation as well as of great consequence for the amounts involved.

Nevertheless, the above-mentioned provision of Article 4 should be tested against Article 7 (*Accounting and Balance-Sheet Records*) of the Legislative Decree No. 74 of 2000, which stipulates the exclusion of criminal

liability for valuation assessments, such as those applying to transfer pricing cases as well. In this regard, the governmental report accompanying the Legislative Decree No. 74 of 2000 clarified that the provision "*aims at avoiding that the new legislation on tax crimes applies too strictly and involves 'criminal risk' also with respect to taxpayers that are not acting with the purpose of evading tax, since the topic of valuation is very much uncertain both from a statutory and a factual standpoint.*"; the newly introduced provisions "*may be deemed as causes of exclusion, iuris et de iure, of a willful criminal tax behavior*".

It stems from the above that Italy's choice to limit the application of Article 8 of the AC to tax offences – without extending its scope to administrative penalties as well – is deemed to be construed consistently with the recommendation of the Code of Conduct suggesting to limit its enforceability to fraudulent behaviours only (i.e. in principle not arising in transfer pricing cases) or to the exceptional circumstances of wilful tax evasion by the taxpayer, actually not occurred yet in Italy's experience.

5.4. Terms for MAP submission

Pursuant to Article 6, paragraph 1, of the AC, "*The case must be presented within three years of the first notification of the action which results or is likely to result in double taxation within the meaning of Article 1*".

The expression "*first notification of the action*" must be construed in the most favorable way to the taxpayer. This entails that the three-year period within which the request must be submitted elapses from the date in which the tax assessment leading to economic double taxation was notified.

The taxpayer may opt to present the MAP opening request prior to the date where the assessment notice has been notified, e.g. where the audit report has been delivered. In any event, in a manner consistent to what is stated in paragraph 5, (b) of the Code of Conduct, the initial term of the two-year period for completing the procedure will start on the latest of the following dates: (i) the

date of the tax assessment notice; (ii) the date on which the competent authority receives the request and the minimum information to work the MAP.

Should the MAP request be submitted by the other associated enterprise in the other Contracting State interested by the procedure, it will be relevant the date promptly communicated by the foreign competent authority.

5.5. Contents and submission of a MAP request

In the event a MAP has been initiated by a taxpayer resident in Italy under the AC, the opening request has to be submitted in free form and sent via letter with advice of delivery to the Ministry of Economy and Finance, Finance Department – International Relations Directorate, or hand-delivered to the same Directorate with receipt of a copy of the first page of the request stamped by the secretariat and bearing the date of receipt. It is allowed and advised to submit relevant documentation supporting the request in an electronic format.

It is also confirmed that, in addition to the advisors representing taxpayers other than individuals, the procedure may be activated by the general or special taxpayer's attorney. Within this scenario, the proxy must be conferred pursuant to what is provided for by Article 63 of the Presidential Decree No. 600 of 1973.

The submission of the request for activating the mutual agreement procedure does not require the payment of a fee, in a manner pursuant to the recommendation contained in paragraph 6.1, (e) of the Code of Conduct.

Under paragraph 5, (a) of the Code of Conduct, the MAP request must contain at least the following information:

1. identification (such as name, address, tax identification number) of the enterprise that presents its request and of the other parties to the relevant transactions;
2. details of the relevant facts and circumstances of the case, including details of the trade relations between the enterprise and the other parties to the relevant transactions;

3. identification of the tax periods concerned by the procedure;
4. copies of the tax assessment notice, tax audit report or equivalent leading to the alleged double taxation;
5. details of any appeals and litigation procedures initiated by the enterprise or the other parties to the relevant transactions (e.g. enterprises part of a tax consolidation group, associated enterprises etc.) and any court decisions concerning the case;
6. an explanation by the enterprise of why it considers that the principles set out in Article 4 of the Arbitration Convention have not been observed, with specific reference to: a description of the transactions incurred between associated enterprises subject to adjustments and the transfer pricing method adopted by the enterprise involved, including the underlying reasons upon which the enterprise considers that the methodology adopted leads to results consistent with the arm’s length principle;
7. an undertaking that the enterprise shall respond as completely and quickly as possible to all reasonable and appropriate requests made by the competent authority and have documentation at the disposal of the competent authorities; and
8. any specific additional information requested by the competent authority within two months upon receipt of the taxpayer's request;
9. an indication – if the case may be – that the transactions falling within the scope of the MAP have been properly documented either pursuant to Article 26 of the Law Decree No. 78 of 31 May 2010, converted with amendments by Law No. 122 of 2010 or pursuant to equivalent documentation requirements imposed by the domestic legislation of the other Member State.

5.6. Interplay with domestic legal proceedings

Article 7, paragraph 1, second part, of the AC stipulates that "…*where the case has so been submitted to a court or tribunal, the term of two years referred to in the first subparagraph shall be computed from the date on which the judgment of the final court of appeal was given*".

However, paragraph 3 of the said article states that: "*Where the domestic law of a Contracting State does not permit the competent authorities of that State to derogate from the decisions of their judicial bodies, paragraph 1 shall not apply unless the associated enterprise of that State has allowed the time provided for appeal to expire, or before a decision has been delivered*".

As Italy is one of those jurisdictions where administrative authorities cannot deviate from the decision of a judicial body, Article 7, paragraph 1 of the AC does not apply in the event a decision of a judicial authority occurred. In other words, within this scenario access to the arbitration phase is prevented.

The arbitration phase may be activated only and insofar as the associated enterprise has allowed the time provided for the appeal to expire, or has withdrawn any such appeal before a decision has been delivered. Moreover, should the request for opening the procedure be submitted before withdrawing from the judgment, the term of two years - pursuant to what is established in Article 7, paragraph 1, second period, and paragraph 3 - runs from the date in which the enterprise has withdrawn from the first grade of appeal.

Accordingly, in the event the taxpayer simultaneously submit a MAP opening request and carry on the appeal against the assessment notice (regarding elements thereof pertaining to the adjustments leading to double taxation), the existence of a litigation proceeding does not prevent the mutual agreement procedure to begin and/or the competent authorities to exchange views regarding the case or information on the pending judicial proceeding.

However, in the event a judicial decision occurred and yet double taxation has not been eliminated, the latter will not be removed unless the foreign

competent authority signs a mutual agreement consistent with the domestic judicial decision.

In any case the taxpayer can appeal on issues other than those falling into the scope of the mutual agreement procedure.

In this regard, it is necessary to recall the legal grounds of the appeal concerning the application of tax penalties, somehow linked to the transfer pricing adjustments falling into the scope of the MAP.

In particular, the possibility granted for the taxpayer to carry on the domestic legal proceeding is excluded insofar as the legal ground of the appeal is based upon the illegitimacy arising from the application of the penalties as a result of the alleged unreasonableness of the adjustments. In the latter case, the challenge is strictly intertwined with that related to the legitimacy of the adjustment subject of discussions in the MAP. Accordingly, the taxpayer must dismiss this legal ground as well.

Notwithstanding the above - and with sole reference to the application of tax penalties - the taxpayer may carry on the judicial proceeding in the event the legal grounds substantiating his appeal relate to; (i) the unlawfulness of the penalties charged because of the mistaken application of Article 1, paragraph 2-*ter*, of the Legislative Decree No. 471 of 1997 (by means of which penalties connected with transfer pricing adjustments do not apply whenever, in the course of a visit/examination/audit, the taxpayer hands over to the Tax Administration appropriate documentation, compliant with the relevant Regulations of the Director of the Revenue Agency, instrumental to prove the consistency of the methodology adopted with the arm's length principle); (ii)) the unlawfulness of the penalties charged because of the uncertain conditions concerning the scope and application of Article 110, paragraph 7 of the Income Tax Code, pursuant to Article 10, paragraph 3 of Law No. 212 of 27 July 2000 (laying down the so-called "Taxpayer's Chart").

With respect to these legal grounds, although the challenges are linked with the main claim concerning transfer pricing, yet they are referring to elements other than those falling into the scope of the MAP. As a result, they do not trigger the consequence for the taxpayer of being forced to withdraw from the appeal. Indeed, the taxpayer would be interested in upholding his claims during the appeal in order to avoid the application of penalties in case Italy would be attributed the taxing rights upon conclusion of the MAP.

5.7. Suspension of tax collection

Based upon Article 3, paragraph 2, of Law No. 99 of 1993 which ratified the AC, pending both the agreement procedure and the potential arbitration phase, the Revenue Agency may authorize the suspension either of the tax collection or of any other enforcing act regarding the amount of greater taxes assessed on the basis of Article 110, paragraph 7 of the Income Tax Code and related interest and penalties.

The administrative suspension procedure is strictly intertwined with the acceptance of the MAP opening request submitted by the taxpayer under the AC.

The suspension request must be submitted to the Revenue Agency – Central Assessment Directorate – via the Office responsible for the issue of the assessment notice, copying also the Ministry of Economy and Finance, Finance Department - International Relations Directorate.

The request must contain the following elements:

a) identification (name, address and tax identification number) of the taxpayer;

b) express reference to the submission of a MAP opening request, and subsequent acceptance by the Ministry of Economy and Finance, Finance Department;

c) detailed information regarding any potential litigation in which the assessed taxpayer or any related party thereof is involved, such as the consolidating enterprise;

Moreover, in light of the timing regarding the tax collection procedure, the request should preferably contain, in an Annex to the request:

a) copy of the MAP opening request;

b) copy of the note with which the Ministry of Economy and Finance informs the taxpayer of the opening of the procedure;

c) copy of the enforcing acts, if any.

The act authorizing for the suspension of the tax collection or any other enforcing decree is signed by the Commissioner of the Revenue Agency and transmitted to the competent Regional or Provincial Directorate for the issuance of the formal suspension of the tax collection. The Regional or Provincial Directorate will be responsible for evaluating the need of a proper warranty to pledge the tax amount due.

As concerns the identification of the final term related to the effectiveness for the suspension of the tax collection, it normally corresponds to the date in which the AC procedure is concluded.

It must be highlighted that in the event the taxpayer is carrying on at the same time an appeal against the same items falling into the scope of the MAP, the authorization to the suspension of the tax collection or any other enforcing act is granted on condition that the taxpayer withdraws from the appeal.

The underlying rationale of the above requirement is that the AC procedure is taken into consideration as a whole, on the basis of what is stated in Article 3, paragraph 2, of Law No. 99 of 1993, which ratified the AC. In other words, the AC procedure is construed from a “dynamic viewpoint”, i.e. as a procedure aimed at settling controversies outside the domestic judicial system and the remedies provided thereof, including in particular those allowing the suspension of the tax collection in the event certain requirements are met.

Within the context of the AC procedure, the suspension is provided for by the above-mentioned Article 3, which must be read - in conjunction with the MAP within which the suspension request is submitted – as an alternative to the domestic appeal and to the suspension of the tax collection granted in the context

of a judicial proceeding pursuant to Article 47 of the Legislative Decree No. 546 of 1992.

What has been stated so far is consistent with EU law – which takes into account national tax legislations that cannot be derogated – and in particular the Code of the Conduct, which recommends "… *to take all necessary measures to ensure that the suspension of tax collection during cross-border dispute resolution procedures under the Arbitration Convention can be obtained by enterprises engaged in such procedures, under the same conditions as those engaged in a domestic appeals/litigation procedure*…"

With reference to the procedural alternative above, relevant domestic legislation is grounded in paragraph 3 of Article 7 of the AC and in the considerations included in the prior point 5.6 of the current Circular.

In other words the act of suspension of the tax collection - according to the domestic provision conferring the discretionary power to grant it – is structured jointly with the AC MAP, within which the request may be submitted, but as an alternative to the ordinary procedures to be pursued for the judicial or administrative suspension of the tax collection.

5.8. Procedural phases

The Ministry of Economy and Finance, Finance Department – International Relations Directorate, acknowledges receipt of a taxpayer's request to initiate a mutual agreement procedure within one month from the receipt of the request, carrying out in the meantime an evaluation of the subjective and objective admission criteria, potentially involving the Revenue Agency by asking for its advice on controversial issues.

Consistently with the recommendations set out in the Code of Conduct, the Italian competent authority will inform the taxpayer within two months from the submission of the opening request as either to its acceptance or the need for providing additional information. In the first scenario the opening date of the procedure corresponds with that in which the request was duly submitted with

minimum documentation attached, whereas in the other case it corresponds with the date in which the additional requested documentation was submitted.

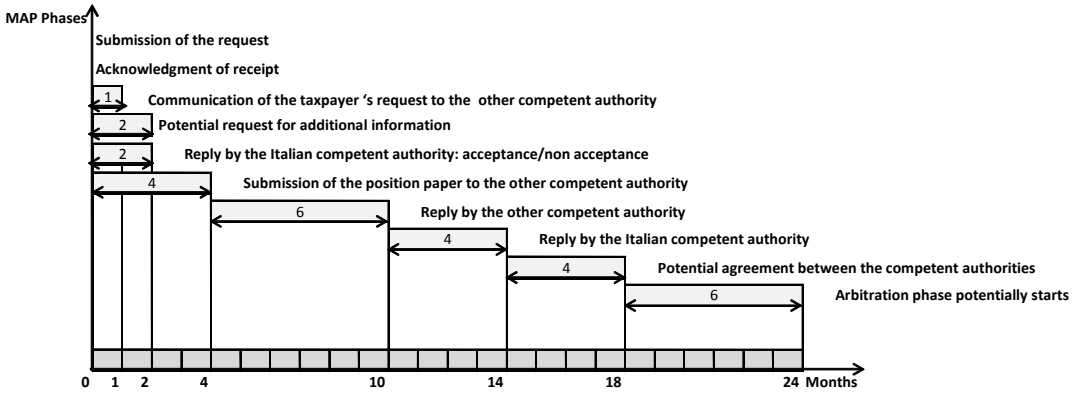
In the event the request appears to the competent authority to be well-founded but it is not itself capable of eliminating double taxation, it will inform the other Contracting State of its decision to open a MAP after receiving the advice of the Revenue Agency

The Revenue Agency, once being informed of the opening of the procedure, will move on by issuing the relevant acts within its areas of discretion (first and foremost, the act granting the suspension of the tax collection or of the enforcing act).

In the two years following the opening of the MAP (or subsequent to the taxpayer's withdrawal from the tax appeal) the competent authorities of the two States shall endeavor to reach an agreement for the elimination of double taxation. Should the two authorities not be able to settle the controversy within the envisaged timeframe, an advisory commission must be established for the initiation of the arbitration phase.

Therefore, it is apparent the need for speedy consultations once one of the two competent authorities has accepted the MAP opening submission by the taxpayer. In this latter regard as well, the Italian tax administration aims at being consistent to the fullest possible extent with the procedural and time recommendations contained in the Code of Conduct, as illustrated in the chart below:

TIMELINE OF THE TWO-YEAR TIMEFRAME OF A MAP



However, it is important to pinpoint to a number of factors which at times may hamper the respect of the above described timeframe, such as, e.g., the different approach that the competent authority of the other State may follow in analyzing the issue at stake in the procedure, in particular with reference to the most complex ones.

The relationship between the competent authorities, aimed at resolving instances of double taxation, is conducted via the written exchange of position papers and, where necessary, with the organization of face-to-face meetings (let alone the role of the taxpayer as described in the following point 5.9 of the current Circular). As a rule, the competent authority of the country in which the tax assessment has been made which result in double taxation, will first send the position paper to the competent authority of the other Contracting State involved in the case.

The language ordinarily used for the drafting of the position papers is English, which is also admitted for documentation attached to the MAP opening request as well as for additional documentation submitted where necessary.

5.9. The role of the taxpayer

The same analysis carried out at point 4.2.9 with respect to mutual agreement procedures opened on the basis of a bilateral tax treaty is applicable here.

This entails that the taxpayer is not directly involved in the dialogue between the competent authorities, although he is required to be co-operative by describing thoroughly the case at stake and promptly providing additional information, if any.

Moreover, in light of the complexity embedded in transfer pricing issues the taxpayer is entitled to take the initiative and submit to the competent authority facts and arguments concerning the case at stake, which may be jointly evaluated by the Finance Department and the Revenue Agency.

Furthermore, pursuant to the recommendation contained in paragraph 6.3 (b) of the Code of Conduct, the taxpayer will be kept informed of all significant developments during the course of the procedure.

5.10 Conclusion of a MAP

The MAP is concluded by:

a. the agreement between the competent authorities reached within two years from the initiation of the procedure or within a greater term as agreed between the competent authorities and the taxpayers involved; or

b. the agreement between the competent authorities reached within six months following the issuance of an opinion by the advisory commission, pursuant to it or in derogation on the base of Article 12, paragraph 1, of the AC.

The agreement is notified to the taxpayer by the competent authority. The Revenue Agency is promptly informed and, if the case, provides any relevant information concerning the submission by the taxpayer of a tax refund or relief request, plus penalties and interest.

Pursuant to Article 3, paragraph 1, of Law No. 99 of 1993, on request by the taxpayer the Commissioner of the Revenue Agency will formally authorize the refund or relief regarding the amount of tax not due as a result of the conclusion of the MAP or arbitration procedure.

6. THE ROLE OF THE REVENUE AGENCY

In light of what has been stated so far, the Revenue Agency supports the Italian competent authority in the various stages of the international dispute, irrespective of whether the MAP has been started based upon a DTC or according to the AC.

In particular, the Revenue Agency provides the legal and technical support during the initial stage of establishing the position of the Italian competent authority *vis-à-vis* the foreign counterpart. Afterwards, the Agency will stand next to the competent authority in the negotiation stage, by submitting a proposal instrumental to reach a potential bilateral agreement. This holds true also where the outcome of the agreement struck by the competent authorities would result in a downward adjustment of the taxable income. Finally, during the arbitration phase, the Agency gathers all the relevant information required and carries out the analysis requested by the advisory commission.

From an operational standpoint, the Agency is responsible for the procedures regarding the suspension of the tax collection or the enforcement measures triggered as a result of assessment notices adopted by the Italian tax administration. By the same token, the Agency puts in place all the measures necessary for a consistent implementation of the mutual agreement achieved with a foreign competent authority at the end of a MAP or an arbitration procedure.

Based on this premise - and in light of the increasing number of MAPs in which Italy is involved, either initiated by resident taxpayers or by foreign enterprises via their respective competent authorities - it is expected a greater involvement of the territorial bodies of the Agency and at the same time it is

necessary to clarify their specific role with the view of assuring their full participation in the management of international disputes.

To this end, the following remarks highlight the different circumstances in which the Regional and Provincial Directorates may be involved by the central structures of the Agency in dealing with mutual agreement procedures.

In this regard, it is necessary to distinguish between MAPs originating from an assessment notice issued by the Italian tax administration and MAPs triggered as a result of an upward adjustment carried out by a foreign tax administration.

In the first case, it is apparent that the Tax Office that carried out the assessment has at its disposal all the relevant information and documentation (e.g. assessment notice, audit report, further documentation gathered in the course of the audit) instrumental to the drafting – by the relevant Tax Office itself – of a report where the underlying rationale of the administrative action leading to the upward adjustment is laid down. The report must also evaluate the legitimacy of the arguments put forward by the taxpayer in filing a MAP opening request. In other words, such a report should be instrumental to smoothen the finalization of the position paper by the Italian competent authority.

Moreover, pending the MAP the relevant Tax Office might be requested to carry out further analysis as necessary to answer to requests for clarifications or to reply to some specific questions posed by the foreign competent authority.

Afterwards, it could be necessary an overall re-examination of the case at stake, in particular in the event the MAP would end into arbitration, as the advisory commission generally instructs the case as from the beginning.

On the other hand, should double taxation arise from a foreign tax assessment, the relevant Tax Office of the Regional or Provincial Directorate must gather all relevant information and documentation necessary to properly instruct the case. This generally entails the performance of visits and inspections or, at least, the submission – to the taxpayer involved – of questionnaires

instrumental to assess the facts upon which the claim by foreign tax administration is grounded as well as its legitimacy.

In the latter scenario as well, based on the information collected, the relevant Office will draft a report as comprehensive as possible so as to be directly used by the Italian competent authority to reply to the position paper of the foreign counterpart.

Lastly, a further relevant scenario to be taken into account is related to instances where double taxation occurs as a result of the express or implied denial against a refund request filed on the basis of a Double Tax Convention. Such a scenario is particularly relevant - from a procedural standpoint – in the event the foreign taxpayer filed to its competent authority the request for the elimination of the double taxation arising because of the refusal of the refund of withholding taxes or tax credits. Within this context, the Operational Centre of Pescara ("*Centro Operativo di Pescara*") is the responsible Unit within the Agency dealing with refund issues to non-resident taxpayers.

Accordingly, the Operational Centre of Pescara is responsible for drafting the report containing the legal grounds underlying the denial, accompanied by any relevant information and documentation available.

7. MAP AND DOMESTIC TAX SETTLEMENTS

As regards the interplay between MAP and remedies available for taxpayers to settle the controversy under Italian legislation (such as, mainly, the so-called "*accertamento con adesione*", "*mediazione tributaria*" and "*conciliazione giudiziale*") the following remarks are carried out, keeping in mind the different approach to be pursued depending on the legal basis deployed (i.e. MAP based on a DTC and MAP based on the AC).

7.1. Double Tax Convention

In the event a MAP request has been filed according to a DTC, it is relevant first to recall what has been clarified at paragraph 4.2.5 concerning the

interplay with domestic appeals. To this end, therein an express reference to paragraph 1 of Article 25 of the OECD Model is contained, whereby the procedure may be activated "*irrespective of the remedies provided by the domestic law*". Furthermore, many of the Double Tax Conventions entered into by Italy contain a Protocol where it is clarified that the expression "*irrespective of the remedies provided by the domestic law*" shall be construed so that "*the mutual agreement procedure is not alternative to the national contentious proceedings which shall be, in any case, preventively initiated, when the claim is related to an assessment of Italian tax not in accordance with the Convention*".

Against this background, in case the taxpayer does not challenge the findings of the assessment notice, the effects deriving therefrom will render the tax assessed final, i.e. it will not be possible to re-negotiate the amount of it within a MAP and in the context of the agreement potentially reached by the competent authorities involved. The same consequences (i.e. the tax due being final and no longer negotiable) will arise in the event the taxpayer agrees to settle with the Agency before going to court via the so-called "*accertamento con adesione*" - pursuant to Legislative Decree No. 218 of 19 June 1997 or by means of either tax mediation ("*mediazione tributaria*") or judiciary conciliation ("*conciliazione giudiziale*"), provided for respectively by Article 17-bis and Article 48 of Legislative Decree No. 546 of 1992. This will entail that the MAP, once opened, cannot be aimed at revising the tax settled by means of the above instruments. However, the competent authority of the other Contracting State may explore the possibility of a unilateral corresponding downward adjustment in order to eliminate double taxation.

The underlying rationale of the domestic tax settlements is twofold, as they reduce the amount of domestic litigations and they are also appealing because of the reduction of any applicable tax penalty. In the context of a MAP, the effect triggered by leveraging on the above-described remedies is equivalent to that produced by the taxpayer not challenging the assessment, i.e. what is defined in the domestic settlement becomes final and not negotiable.

As concerns, in particular, the "*accertamento con adesione*", Article 2, paragraph 3, of Legislative Decree No. 218 of 1997 stipulates that the settlement act can neither be appealed nor be modified or amended by the relevant Tax Office, unless the conditions of paragraph 4 of the same provision are met, concerning additional assessment activities leading to a higher taxable basis. As a consequence, given the terms of the tax settlement as agreed and crystallized between the taxpayer and the Agency, in the absence of new assessment items, the settlement is deemed final, triggering the above said effects on the mutual agreement procedure .

In conclusion, recourse to the *"accertamento con adesione"*, *"mediazione tributaria"* and *"conciliazione giudiziale"* (involving a qualified willingness to settle the case) trigger the conclusion of the controversy between the parties involved, preventing the Agency from renegotiating the position agreed domestically with the taxpayer in the context of a MAP, also in light of the legal instruments and the resources deployed by the tax administration in achieving the tax settlement with the taxpayer.

7.2. Arbitration Convention

What has been described above with respect to the effects produced by the domestic settlement instruments can be confirmed as well in the event of MAP filings under the AC, although some major differences exist due to the different legal nature of the AC itself.

In this respect, the key feature arising from the combined reading of Articles 6 and 7 of the AC is the alternative approach between the mutual agreement procedure and the domestic litigation appeal system, that is; within the AC the MAP is an alternative to the judicial proceedings and involves the obligation to eliminate double taxation: in the event the competent authorities are not capable of reaching an agreement an arbitration phase will be initiated (the details of which have been described in paragraph 5 and ss. of this Circular).

Within this scenario, the settlement of tax disputes aims at closing any claim by the Agency, even though the perspective of an international dispute may be undertaken.

The fact that the taxpayer decided to settle the controversy does exclude the possibility of reopening the discussions in the context of a MAP: the option between domestic and international litigation is no longer available as any dispute has already been settled, again also in light of the legal instruments and the resources deployed by the tax administration in achieving the tax settlement with the taxpayer.

Although the tax has become final, which precludes any re-negotiation within a MAP based upon the AC, the competent authority of the other Contracting State may explore the possibility of a unilateral corresponding downward adjustment in order to eliminate double taxation. This possibility, however, can be granted only insofar as the enterprise has also submitted a MAP request on the basis of a Double Tax Convention as well.

Unlike tax settlements, the will not to challenge the assessment notice before the domestic court does not prevent the taxpayer from initiating a mutual agreement procedure under the AC. On the contrary, the act of not challenging the assessment, together with the submission of a MAP opening request, proves the taxpayer’s willingness to re-discuss an re-examine the issue at stake in the alternative context of a MAP and of the arbitration phase, pursuant to the different terms and timeframe established by the AC and by means of the involvement of the competent authorities of the relevant Contracting States.

Both the Regional and Provincial Directorates are invited to closely monitor the circulation of and compliance with the current Circular.

THE COMMISSIONER

Attilio Befera