

Italy enacts EU Tax Dispute Resolution Mechanisms

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Executive summary

On 10 June 2020, the Italian Government published Legislative Decree n. 49 (Decree) - enacting Directive (EU) n. 2017/1852 on tax dispute resolution mechanisms in the European Union (Directive) - *Official Gazette*.¹

The Decree implements new rules to resolve disputes between Italian and other European Union (EU) tax authorities on the interpretation and application of agreements and conventions for the avoidance of double taxation (Mutual Agreement Procedure or MAP). It introduces the possibility for Italian taxpayers to request the institution of an Advisory Commission and extends the procedure to disputes other than those related to transfer pricing and permanent establishments (PEs) by consequently allowing individuals and non-multinational enterprises to access the procedure.

The Decree applies to MAPs filed as of 1 July 2019 with reference to fiscal years starting from 1 January 2018 onwards.

Detailed discussion

The Decree implements the new rules on tax dispute resolutions set forth by Council Directive 2017/1852 of 10 October 2017 which established significant improvements to resolve cross-border tax disputes, as they ensure that

businesses and individuals can resolve disputes related to the interpretation and application of tax treaties more swiftly and effectively.

The new rules also cover issues related to double taxation which occurs when two or more countries claim the right to tax the same income or profits of a company or individual. This can happen, for example, due to a mismatch in national rules or different application of transfer pricing rules in by the local tax administrations.

There are currently around 900 double taxation disputes in the EU and they are estimated to be worth about €10.5 billion.

Main structure of the Decree

The main structure of the Decree resembles and builds on the existing EU arbitration convention,² according to which the taxpayer shall file a specific request, the competent tax administrations evaluate and assess the admissibility of the request, the tax administrations undertake to reach an agreement in a two-year timeframe and, if no agreement is reached, an arbitration process may be initiated with the appointment of an advisory commission.

However, the Directive, as implemented by the Decree, provides for very significant innovation as, for example:

- ▶ The scope is no longer confined to transfer pricing matters and attribution of profits to a PE but is now extended to further double taxation issues that may stem from the application of tax treaties, for instance: tax residency of individuals and legal entities, assessment on the existence of a (hidden) PE, flows of dividends, interest and royalties.
- ▶ It introduces new mechanisms that may ensure the resolution of tax disputes in situations where the involvement of tax administrations does not seem to be effective or even possible. Those mechanisms involve arbitration phases and the possibility for the taxpayer to bring the case in front of national tax courts.

Filing of the request: Terms, conditions and impact on tax litigation proceedings

A request for a MAP may be started before the commencing of tax litigation or also pending any other tax administrative procedure.

The request is submitted simultaneously to each of the competent tax authorities (i.e., the Italian, *Agenzia delle entrate*, and the foreign ones) within three years after:

- ▶ The date when the taxpayer was notified with the tax assessment deed (or equivalent administrative document); or
- ▶ The date when the measure giving rise to the controversial double taxation issue takes place.

A simplified procedure is established for individual and small-medium companies that are not part of a large multinational enterprise group. Those subjects may file a request with the Italian Tax Authorities (ITA) only, who will then take care of transmitting it to the other tax administration(s) involved.

The Decree clarifies that the request can also be filed in situations where:

- ▶ The tax liability has not been finally settled (one of the main innovations).
- ▶ The ITA and the taxpayer reached a pre-litigation administrative settlement on the tax issue.
- ▶ The taxpayer already payed the higher tax assessed by the tax administration, renouncing to file an appeal against the tax assessment deed.

The request cannot be filed if the taxpayer voluntarily settled a tax violation before any inspection or audit activity is initiated by the tax administration.

The Decree expressly sets out that the taxpayer is not bound to start litigation proceedings before filing the request. At the same time, the taxpayer keeps the right to file an appeal against the tax assessment deed after having filed the request; in this case, the taxpayer is entitled to ask for the suspension of the judicial proceedings.

However, the request cannot be filed if a judgment has become final or the parties (ITA and taxpayer) reached an agreement in the course of the judicial proceedings (*conciliazione giudiziale*).

Multilateral Agreement Procedure

The ITA shall decide if the taxpayer's request can be accepted within six months from the day when the request is received. If the request is rejected, the ITA shall explain the reasons of its decisions.

If the ITA does not provide an answer within the six-month term, the request is considered as formally accepted.

The taxpayer is expressly entitled to file an appeal against the rejection decision in front of the competent tax court.

Once the request is accepted, the MAP is opened. The ITA and the tax administration(s) of the other Member State(s) are under an obligation to resolve the issue within two years from the date when the taxpayer is notified with the formal acceptance of the request.

The term can be postponed by another year if additional information is required.

In the case of pending domestic tax litigation on the matter, such domestic procedure is suspended upon the taxpayer's request. The suspension of the litigation also implies the suspension of the provisional tax collection until the finalization of the MAP.

Within six months from the receipt of the request, the ITA may decide for a unilateral resolution, without the involvement of the tax administration(s) of the other Member State(s) - for instance by providing a tax refund or eliminating a previously issued tax assessment deed.

Possibility for an arbitration phase

The Advisory Commission

If the request to start a MAP is rejected, or after a period of two years (three in case of postponement) during which the tax administrations have not been able to reach an agreement, the taxpayer can file a further request to open the arbitration phase by the setting up of an Advisory Commission.

The ITA is entitled to object to the taxpayer's request to set up the Advisory Commission if: (i) criminal sanctions are served for the relevant tax violations; or (ii) the debated issue does not give rise to a double-taxation situation; or (iii) the controversy has been finally decided by a judicial statement or settled in the framework of a litigation procedure (*conciliazione giudiziale*).

If the request from the taxpayer is not rejected, the Advisory Commission shall be formed within 120 days following the taxpayer's filing of its request.

The Advisory Commission shall rule on the taxpayer's request within six months from the day it is established.

The alternative dispute resolution mechanism

As an alternative to the establishment of the Advisory Commission, the Decree leaves to the tax administrations the possibility to opt for an Alternative Dispute Resolution Mechanism (ADRM).

The tax administrations involved would be able to adopt other dispute resolution processes, including the so-called "final offer" arbitration process (otherwise known as "last best offer" arbitration) to solve the dispute in a binding manner. The tax administrations involved are free to agree on the method according to which they intend to solve the issue.

Outcome of the arbitration phase

After the Advisory Commission or the ADRM mechanism provide for a solution, the tax administrations involved shall agree to resolve the controversy within six months. The outcome of the arbitration phase is not binding on the tax administrations involved, which could agree on a solution to the dispute different from the one determined by the Advisory Commission or by the ADRM mechanisms. However, if no agreement is reached, then the issue shall be solved according to the outcome of the arbitration phase (i.e., according to the outcome of the Advisory Commission or of the ADRM).

Relationship with other multilateral agreement procedures

The Decree determines the case when a MAP is requested on a multiple legal basis, i.e., on the basis of the Directive, of the EU Arbitration Convention or of the applicable double tax treaty. In such cases, the procedure will take place under the framework provided by the Directive, which will prevail over the others.

Then, if a (i) MAP was already activated under a different legal basis; and (ii) the tax administrations involved were not able to reach an agreement; and (iii) the legal framework under which the MAP was activated does not include an arbitration phase, the taxpayer is entitled to file a further request to start the arbitration phase (Advisory Commission or ADRM).

Enforcement of the solution agreed by the tax authorities

The Decree sets out the rules to implement the decision reached after the MAP or the arbitration phase (Advisory Commission or ADR mechanism).

The ITA shall implement the decision either by: (a) collecting the higher tax due; (b) granting a tax refund; or (c) granting a relief for the higher tax previously assessed.

In the first case (collection of the higher tax), the ITA shall apply administrative penalties (if applicable) plus late-payment interest starting from the date when the final decision was adopted.

However, if the taxpayer had already paid administrative penalties in the context of a pre-litigation tax settlement, then the ITA could collect only the higher tax amount (and interest) but not penalties.

In the second case (tax refund), the Decree clarifies that the refund shall also include any amount of tax penalties already paid by the taxpayer.

The resolution of the issue between the tax administrations can be enforced provided that the taxpayer accepts it in written form within sixty days and, contextually, renounces any litigation procedure (if any).

Only for the purposes of the enforcement of the arbitration outcome, the ordinary statute of limitations is doubled (i.e., generally extending to 10 years).

Procedural instructions will be issued in the next months by the *Agenzia delle entrate*.

Endnotes

1. *Italian Official Gazette n. 146.*
2. 90/436/EEC90/436/EEC: Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, ratified and executed by Italy with Law n. 99 of 22 March 1993.

For additional information with respect to this Alert, please contact the following:

Studio Legale Tributario, International Tax and Transaction Services, Milan

- ▶ Marco Magenta marco.magenta@it.ey.com
- ▶ Savino Tatò savino.tato@it.ey.com
- ▶ Simone De Giovanni simone.de-giovanni@it.ey.com
- ▶ Davide Bergami, *Transfer Pricing* davide.bergami@it.ey.com

Studio Legale Tributario, Financial Services Office - Tax, Milan

- ▶ Marco Ragusa marco.ragusa@it.ey.com
- ▶ Paolo Zucca paolo.zucca@it.ey.com
- ▶ Antonfortunato Corneli antonfortunato.corneli@it.ey.com
- ▶ Giancarlo Tardio giancarlo.tardio@it.ey.com
- ▶ Alberto Giorgi alberto.giorgi@it.ey.com

Studio Legale Tributario, Rome

- ▶ Daniele Ascoli, *ITTS* daniele.ascoli@it.ey.com
- ▶ Livio Zallo, *FSO - Tax* livio.zallo@it.ey.com

Studio Legale Tributario, Tax Controversy, Milan - Rome - Bologna

- ▶ Maria Antonietta Biscozzi maria-antonietta.biscozzi@it.ey.com
- ▶ Pasquale Cormio pasquale.cormio@it.ey.com
- ▶ Enrico Ceriana enrico.ceriana@it.ey.com
- ▶ Michela Antonella Prencipe michela-antonella.prencipe@it.ey.com
- ▶ Andrea Daglio andrea.daglio@it.ey.com
- ▶ Raffaele Sgambato raffaele.sgambato@it.ey.com
- ▶ Umberto Iannarilli umberto.iannarilli@it.ey.com

Studio Legale Tributario, Bologna

- ▶ Mario Ferrol, *ITTS* mario.ferrol@it.ey.com
- ▶ Gianluca Zanella, *Tax Controversy* gianluca.zanella@it.ey.com

Ernst & Young LLP (United Kingdom), Italian Tax Desk, London

- ▶ Domenico Borzumato dborzumato@uk.ey.com

Ernst & Young LLP (United States), Italian Tax Desk, New York

- ▶ Emiliano Zanotti emiliano.zanotti2@ey.com
- ▶ Andrea Ajovalasit andrea.ajovalasit1@ey.com
- ▶ Luigi Caltagirone luigi.caltagirone1@ey.com

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