

Italian tax agency clarifies transfer pricing adjustments and VAT

The Italian Revenue Agency has clarified the VAT treatment of transfer pricing (TP) adjustments via a tax ruling on November 2 2018. Antonella Della Rovere and Federico Vincenti of Crowe Valente / Valente Associati GEB Partners explain the details.

November 07, 2018

Related to [News](#), [Correspondent](#) & [Italy](#)

The case in the tax ruling referred to transfer pricing adjustments made to permit the applicant enterprise to reach the minimum profit level provided in the group TP policy. Specifically, the applicant company provided goods and services to a related company. According to an agreement between them, the former received remuneration from the latter for the difference between the amount of profit actually realised and the amount of profit at arm's length. The question raised was whether or not such remuneration was relevant for VAT purposes.

The ruling clarified that the adjustment cannot be qualified as "remuneration for a specific supply transaction" because it is essentially a remuneration for a financial risk assumed, to ensure that the applicant was remunerated for the goods supplied at arm's length. Hence, what needs to be determined is whether the adjustments were practically modifying the prices paid for the supply of goods/services and, therefore, the VAT taxable base of the transactions between the two companies. To this purpose, the tax authority examined if there was a direct link between such amounts and the supplies of goods/services, in line with the European Commission's Working Paper No. 923/28.02.2017.

In this working paper, the VAT committee considered the potential VAT-related implications of the TP rules provided in direct taxation, including if TP adjustments (by enterprises or tax authorities) should be considered payment for goods or services. It was clarified that such adjustments may have an impact on the VAT taxable base on the following conditions:

- There is consideration, i.e. some kind of compensation monetary or in kind for the adjustment;
- The transactions for the provision of goods or services to which the consideration refers are duly identified; and
- There is a direct link between the transactions and the consideration.

Thus, an adjustment following application of the transactional net margin method (TNMM) to align the company's operational margin with its target margin evaluated at arm's length would be relevant for VAT purposes, if it could be linked to specific transactions. Such linking would be easier in cases where the comparable uncontrolled price (CUP) method is used because the adjustments refer to specific transactions.

From the working paper, it arises that although the arm's-length principle is generally applicable according to the TP rules in direct taxation, the VAT Directive (2006/112/EU) seems to outline a narrower area of application. In essence, the application of such rules is at member states' discretion, and only for the purpose of preventing tax avoidance and evasion in specific cases. Such cases are exhaustively listed in Article 80 of the VAT Directive and hence, according to the Court of Justice (*C-142/12* and joined cases *C-621/10* and *C-129/11*), member states cannot deviate therefrom, providing for additional cases.

In light of the above, the ruling did not identify a direct link between the TP adjustments and the supply of goods and services. As a result, such adjustments could not be considered to lead to a modification of the VAT taxable base in relation to these transactions.



Antonella Della Rovere
Partner
a.dellarovere@crowevalente.it



Federico Vincenti
Tax manager
f.vincenti@crowevalente.it