

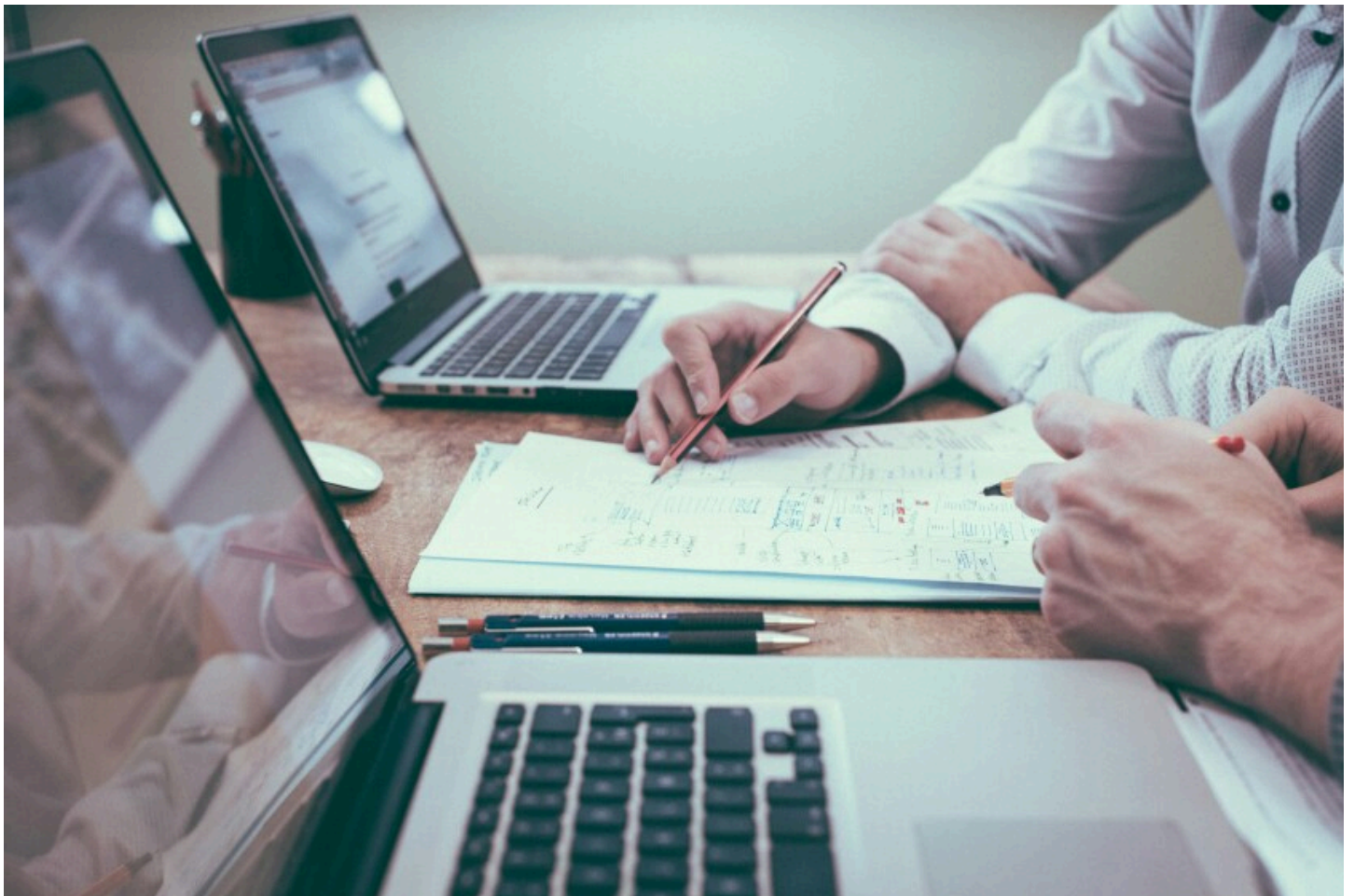
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# Italian Supreme Court decision confirms stance on intercompany services

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*By Federico Vincenti, Carola Valente* May 10, 2024



## **Federico Vincenti and Carola Valente of Valente Associati GEB Partners/Crowe Valente suggest what documentation can demonstrate the reasonableness of the costs of an intra-group transaction, and the benefits for a subsidiary**

The Italian Supreme Court, with judgment No. 6584 of March 12 2024, has again ruled on the issue of intra-group costs allocation and specifically on the conditions for deductibility of management fees charged by the parent company to the subsidiary.

The court, consistent with its prior jurisprudence, has established that the deductibility of intra-group costs is subject to the actual provision of services and the relevance and reasonableness of the costs in relation to the business activities carried out by the subsidiary, as well as the real benefit derived by the latter.

To determine whether the service has been provided, the Italian legislation, following [the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations](#), outlines the so-called benefit test: the activity performed is deemed to be a service and chargeable if it has economic or commercial value, or if it enhances the recipient's commercial position, and therefore an independent enterprise in comparable circumstances would have been willing to pay for such an activity or would have performed the activity in-house for itself.

The actual provision of the services, and the related benefits, should be demonstrated through proper documentation.

With regard to the proper documentation for intercompany service charges, it is also recommended to refer to the Operational Manual for the Prevention of Tax Evasion and Fraud issued by the Italian Tax Police (*Guardia di Finanza*) with Circular No. 1/2018, Volume III.

The assessment of the deductibility of the costs incurred by the service recipient must take into account the probative value of the documentation submitted or otherwise acquired (e.g., during an audit) with regard to all the subjective and objective elements of the service, which must also be considered in light of the general principles for determining business income, including those of inherent nature, certainty, and determinability.

In this context, an audit would focus on the following:

- As a preliminary matter, the existence of a written contract with a proven date shall be established;
- Alternatively, whether the transaction is objectively supported by documentation that is consistent (internal and external), reliable, and specific (it may be useful to compare the data and elements that can be found in the contract, in the 'memoranda' or files that preceded the agreement, in the correspondence between the parties, in the relevant invoices, and in the resulting accounting records).

The Supreme Court confirmed that the taxpayer (the service recipient) must provide evidence of the existence and relevance of the costs incurred. However, merely presenting the contract for services

provided by the parent company to the subsidiary and the corresponding invoices is not sufficient. Rather, specific elements are required to determine the actual or potential benefits obtained by the taxpayer.

In the case at hand, the existence of a benefit for the Italian subsidiary was demonstrated by a written agreement specifying the details of the services and a fair allocation criterion. Additionally, the subsidiary's organisational structure was not suitable for independently performing the services received from the parent company.

## Key takeaways: supporting an intercompany service transaction

Based on the above, it is advisable to support an intercompany service transaction through making available the following qualitative and quantitative information that generally could be requested by the tax authorities during tax audits:

- The taxpayer should provide a description for each category of services, the identity of the beneficiaries, the reasons for providing the services within the multinational enterprise group's business environment, the benefits received or expected, the allocation criteria chosen, and the reasons why these criteria are expected to produce results that reasonably reflect the benefits received.
- Service contracts – the taxpayer should prepare the written contracts or agreements relating to the provision of services and any amendments thereto, demonstrating the consent of the parties involved to the application of the chosen allocation criteria. Such written contracts or agreements may also consist of contemporaneous documents, relating to the period under consideration, identifying the parties involved, indicating and describing the nature of the services, and the contractual terms under which such services are provided.
- Evaluation of the transactions – the taxpayer should document and illustrate the calculations showing how the aggregate of direct and indirect costs associated with the provision of the services and the profit margin applied are determined, with a detailed representation of all categories and the amounts of the relevant costs, including the costs related to any service provided exclusively to a single member of the multinational group.
- Calculations – the taxpayer should provide, also in the form of spreadsheets, the calculations showing how the allocation criteria set have been applied.

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