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Changes of international taxation in Italy and Europe:
Custom Duty, Transfer Pricing and Dual Residence
Issues

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ABSTRACT

Con questa tesi mi sono prefisso l'obiettivo di capire a fondo i meccanismi e le variabili che influiscono sulla tassazione internazionale dando particolare attenzione al punto di vista italiano.

Nel primo capitolo si parla della storia dei dazi doganali dall'età romana alla moderna organizzazione dell'unione europea dando qualche sintetico richiamo macroeconomico.

Segue nel secondo capitolo l'analisi e i vari metodi dei prezzi di trasferimento negli scambi internazionali.

Il terzo capitolo riassume e mette in correlazione gli argomenti trattati precedentemente analizzando i punti di vista dei vari soggetti coinvolti (autorità fiscali, doganali e privati).

Il quarto ed ultimo capitolo è il cuore della tesi in cui si analizzano le varie problematiche legate alla doppia tassazione ed alla definizione della residenza fiscale. Ho deciso di studiare in particolare modo le novità legate all'art.4 dell'OECD model e dare il mio punto di vista sull'approccio del legislatore italiano su questo delicato argomento.

INDEX:

INTRDUCTION

CHAPTER ONE: Custom duty

- 1.1. A general overview
- 1.2. The history of custom duty in Italy
- 1.3. A Briefly macro-economic recall
- 1.4. Modern age development
- 1.5. The down of Europe and role of Itlay
- 1.6. A Single Market
- 1.7. Consequences of Brexit on custom duty

CHAPTER TWO: Transfer pricing

- 2.1. A general overview
- 2.2. History of Transfer Pricing
- 2.3. The OECD
- 2.4. Arm's length
- 2.5. OECD Transfer Pricing Guidelines
- 2.6. Method of Transfer Price Application.
- 2.7. Italian legislation for the selection of Transfer Price method

CHAPTER THREE: THE RELATION BETWEEN TRANSFER PRICING AND CUSTOM DUTY

- 3.1. A general overview
- 3.2. New authorities' collaborations
- 3.3. A view from the private sector

CHAPTER FOUR: CHANGES IN TAX RESIDENCE

- 4.1. A general overview
- 4.2. The project Base Erosion and Profit Shifting.
- 4.3. The art.4 of OECD model.
- 4.4. Adjustments of art.4
- 4.5. Italian law on transfer of tax residence
- 4.6. Tax residence in conventions: particular situations
- 4.7. Memorandum Italy – China

CONCLUSIONS

BIBLIOGRAPHY

WEB SOURCES

RINGRAZIAMENTI

INTRODUCTION

In a period that is expiring what a global and total market is, with all its nuances, its advantage and issues, human being is remain attached to some of the more solid pillars of society: Trade and Taxes.

From the mists of time in order to increase their own wellness, individual before and societies after trade with other entities with the aim of rise and rich higher economic conditions.

In this thesis I will discuss about the connection among Custom Duties and Transfer Pricing and how, thanks to a modern and interconnected environment, that topic has become crucial not only for the economy of multinational enterprises but also for the relationships between Sovereign States.

The aim of this work is to understand which relationship exist between Custom Duties and Transfer Pricing, why we arrive at the current situation in Europe, and which will the future scenario with particular attention at the role of Italy.

On the first chapter I will mainly concentrate on the history of custom duty and how the policy related to it changed across the centuries. Particularly attention has been given to the Italian and European History. After some macro-economic

consideration the first chapter close with a reflection about the situation in UK and the reason of Brexit related to the custom issues.

The second chapter will be mainly focus on Transfer pricing. Will be deeply analysed how it works, which are the procedures, the methods and the variables that have to be taken into account during an international transaction.

In the third chapter I will describe the issue that raised from the interaction of tax and custom authorities, their point of view and the one of the private sector.

The thesis will conclude with an analysis of where a private or juridical subject has to pay the taxes when there are residential disputes. Particular attention is given to the recent changes of the art.4 of the OECD model and to the position of Italy regarding the dual residence issue.

CHAPTER I

CUSTOM DUTY

1.1. A general overview

Since trade between Nations, Empires or other form of Social Organizations exist, Custom Duty represents the amount of taxes imposed on the goods or services transferred among those entities.

Custom duty is the most ancient form of trade policy.

There are several reasons for which sovereign States can apply tariff over the import or export of specific items. Generally speaking, the first and most obvious reason are exactly the same of the great part of the other taxes: generate revenues.

E.g. in the USA before the introduction of income taxation the revenue generate from custom duty was the great part of the national income.

Then, if on one hand Nations have a direct gain on custom duty on the other hand enterprises have to face a relevant cost that can orient their business strategies and horizons. So here the second goal of custom duty: protect specific industrial domestic sector and also the own economy the entry of under-priced goods or from an aggressive foreign policy of other nations. The level of protection is expressed in a rate with the price that would be set in a situation of free trade.

Generally speaking, a duty generate a gap between the price for which a good and service is exchanged within national adage (internal price) and the one for which is exchanged internationally (external price). So, fixing a duty on a specific good has an effect to rise its price on the country that want to import that good and decries for the country that want to export.

Immediately after the end of the second world war the new born Nations stared to protect they industrial sector with custom duty on manufactured goods.

At the turn of the 20 and 21 centuries was drastically decreased, chiefly since government usually preferred to protect their own economy through protectionist policies based on non-tariff barriers (NTB) as – quotas to the import set a limits to the amount of goods importable in a country or export restriction.

There are basically two different types of custom duty.

The first one called *specific* represents a fixed amount of money - based on the characteristics of the items -linked to each transaction that take place between a nation and another.

The second one is called *ad valorem* and is a certain percentage linked to the whole value of the goods or service shared.

The duty we are heard about and that are consistently rising in importance in the last year are the latter.

All the concept of commercial war subsisting mainly between USA and China but that also involves the European Union and other nations are based mostly on the application of *ad valorem*¹ custom.

The slogan “America first” is the emblem to an economic policy vote to reduce the trade deficit of a nation moving the national trade policy from multilateral free trade agreements to bilateral trade deals.

1.2.The history of custom² duty in Italy

The History of Custom duty in Italy start with the declaration of Italian Kingdom in 1861 or to be more precise the following year when the reign adopt in its new territory the custom duty of the former Sardinia Kingdom and had replaced the rules of the pre-unification States.

Reading and searching information I went deep in the History and I know that could sound strange to start the analysis of Italian History from the really beginning and so from the Roman Empire but I found several similarities with the actual situation that I would like to highlight.

¹ Today great part of the custom duty are *ad valorem*.

² In the different languages in Europe the name of the “custom office” came from the name of the fee that had to be paid to cross the border between two nations.

Since from the republican age, Rome adopted for its reign the Greek system for custom duty was used to apply *ad valorem* taxation.

Corps responsible for collecting taxes was private and nominated through contracts.

We will see later on in the history that the alternance between private and public corps for the administration of custom duty is recurrent and that has a central role in the development of our Nation.

The fundamental Laws that had regulated that area could be found in the “*Digesto Romano*³”. Here it is possible to read the first custom duty legislation and the definition of a custom duty *ad valorem*.

As I wrote previously at the beginning all the issues regarding taxation, both internal and external, were carried out by private subjects.

That was the cause of several issues for the Republica before and for the Empire after especially for public order and smuggling problems. That is the reason why during the reign of Emperor Claudio among 41 and 54 A.D the administration of taxes and custom duty fell into the responsibility of the public entities.

At the beginning and during his richest moment along the borders of the empires were found very different levels of custom duty. While at the end of its history there was a unique custom duty rate.

³ D.XXXIV, IV De publicanis, et vectigalibus, et commissis; D. XL IX, XIV De iure fisci; D. LXVII De regulis iuris, De fisco.

I personally found really interesting that the level of the initial custom duty, that correspond with the period in which Rome has known its maximum splendour, was about 2.5% - 5% and that correspond at the level that today the industrialized country applies on average⁴. The same similarity could be found with the tax level set in the last and economically weak period of the empire where the rate was around 12% and correspond to the hodiern rate present in the under developed nations.

After the desegregation of the Roman Empire the multitude of small kingdom crate a quantity of different custom duty that almost paralyzed trade among state.

Immediately the turn back to *specific* custom and quite protectionist policy.

The situation radically changed after the discovery of America.

The following period denominate modern - eval experienced an exponentially grow of international trade lead to the new colonial discovery and as a consequence the consolidation of huge territorial agglomeration and big National State.

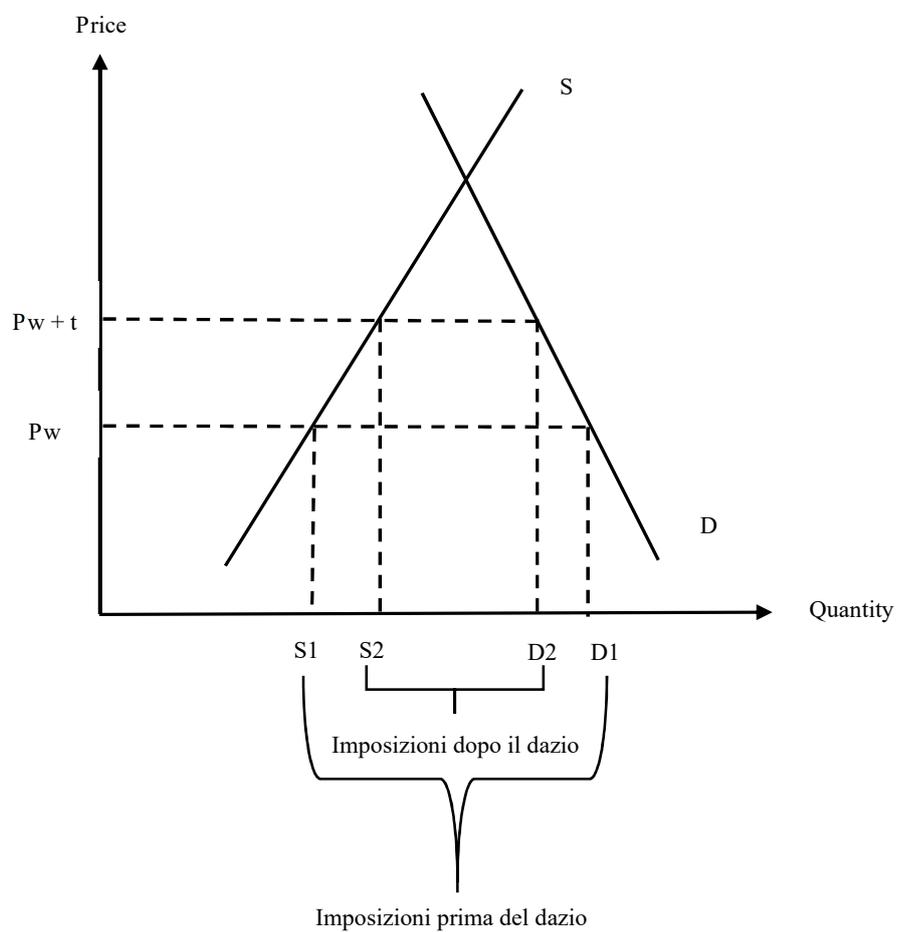
During this period Portugal, Spain, England, Netherland and French rise their economically condition. That doesn't happen in Italy and it could be an interesting point to analyse the inefficiency of custom duty set by small States.

⁴ At the end of the 20th centuries the custom duty set by the major industrialised drastically decrease. Between 1990 and 2010 the duty on their import decreased on average about 6 percentage point.

1.3. A Briefly macro-economic recall

Generally speaking, the effect of a custom duty is cut down the quantity exchanged among two powerful state and to increase the price of the item in the country that set a custom duty for the importation and rise the same price for the one that want to export. But this commercial policy work only if the Nation that set the custom duty is big or powerful enough to influence the quantity exchanged in the market.

If is not the only effect is that the imposition of a custom duty on an imported good do not influence its international price. Therefore, the price of the good rise from P_w (price of the world market) to P_w+t (price of the world market plus the entity of the custom duty). The obvious effect is that the only consequence is that the quantity imported from the state fall down.



Where: D=demand; S=supply; P_w (world price of a specific good); t =level of custom duty

That is why the influence that the little State in Italy during the moder-evale was basically null.

They didn't have any power to influence the price and though, even if the quality component of reign as Repubblica di Venezia or Genova was superior, the remained cut out from the political and economic development of that period.

That was the main reason way city as Livorno introduce the ex-work policy thank to what become and still one of the major ports for the transit of goods from and to the new world/USA.

1.4. Modern age development

Along all the period after the end of the Roman Empire the administration of custom duty was under private company or institution.

Only in 1791 French govern decide to take back the direct control of it⁵. That new policy was immediately more efficient and generally recognised.

When, under the Napoleon era, the French domain arrived in Italy, bring with it the new custom policy in both the direct⁶ and indirect⁷ annex region.

Those French models leave everywhere a benchmark of professionalism and efficiency that also during the Risorgimento the new born State of Italy decide to maintain that structure.

⁵ This bodies was called "*Service actif des douanes*".

⁶ Piemonte, Liguria, Ducati di Piacenza, Parma and Guastalla, Tuscany, Lazio and Umbria

⁷ Italian reign, and Naples reign

Regarding which tariff was adopted it need to wait the 1859 when the one used in the reign of Sardinia become also the one used in all the country.

Different part of the new state reacts in different way to that uniform tariff from the moment there were several economy absolutely not at the same level and in which the economies were based on different types of product and so different trade with other nations.

The new born State of Italy found itself immediately at a crossroad. In one hand it has the necessity to integrate its economy within an international contest, where a liberalism organization of a trade was growing up, in the other hand there were also the need to protect the industry and other sector of an economy that was quite young.

On the base of that environment some decision was taken. There were a reduction of custom duty for the import of several goods as – cotton, wool and silk and the right of exporting cereals was revoked. In the same period the first bilateral agreements start to broke up into the international environment.

In particular I am going to talk about bilateral and multilateral agreement later on in the following chapters.

After the two world war during which Sovereign state comply close to a protectionism policy, and to be more precise to war policy⁸ that doesn't allow any commercial activity with the opponent nations, the situation in Italy Europe and also at a world level start a long, radical and historical change at international trade level.

Especially Europe start to talk about a united market again after thousands of years.

A central role on the reorganization of the world market was played by the Unites States for obvious reason. Starting with the Bretton Wood economic strategy⁹ and though a progressive liberalization of the world trades, America pushed the international and globalized market up. During these years the history of custom duties in Italy become day by day more attached and linked to the evolution, or maybe is better to talk about “revolution” of the Euro – Zone.

1.5. The down of Europe and role of Italy

So as discussed in the previous chapter is after the end of the second world war and with the support of USA that the transformation process of an historical

⁸ Regio Decreto n.1415 of 08.07.1938

⁹ Bretton Woods established a system of payments based on the dollar, which defined all currencies in relation to the dollar, itself convertible into gold, and above all, "as good as gold" for trade. U.S. currency was now effectively the world currency, the standard to which every other currency was pegged.

multinational market as the one it used to be in Europe in a unique and strong area had taken off.

The first step is to take over the existence of several multilateral agreements. The first institution in that area was the International Trade Organization (I.T.O) that was a simple predecessor of the General Agreement on Tariff and Trade better known as G.A.T.T.

G.A.T.T. was subscribed by 23 Countries and entered in force in 1948. Four were the pillars where were found its principals:

- Reduction of tariff barriers;
- Disposal of quantitative restriction;
- Easy establishment of the clause within the nations;
- G.A.T.T. actions were carried on by general sessions.

Moving forward rapidly along the years we arrive at 1950 when France proposed the foundation of CECA (comunità europea del carbone e dell'acciaio) a new multilateral agreement in which Italy immediately took part and that opened our nation to a liberalization of its commercial politics. It is curious that UK was strongly against the CECA that could be considered the very first image of European Union and today, 31 January 2020, Great Britain is also the first country to leave the united market.

Going back to Italy and Europe the turning point was the 1957 when: Belgium, German Republic, French, Italy, Luxemburg and Netherland subscribe the Treaty of Rome that officially established the E.E.C (European economic community).

The goal of E.E.C. was to create a single market within:

- The custom duty barriers had to be removed;
- Quantitative restriction within state had to be removed as well;
- Set of a common custom duty towards external country.

From now to then in Europe we are not talking about Custom Duty of singular nation anymore but of a Euro – Zone as a whole.

1.6. A Single Market

The 1° July 1968 become effective the Common Custom Duty¹⁰. This tariff had two prerogatives. First it showed the General Rules and Special disposition, secondly it establish the level that had been set for custom duty.

All the customs duties and restrictions were lifted among the 6 countries of the European Economic Community and calculated on the average value of the previous custom duties.

¹⁰ Issued with regulations C.E.E n.950 of 26.06.1968

So, the national customs duties on goods were replaced by a shared custom tariff from the rest of the world. That definitely allows the trade between European Country to multiply faster and to take off. In a really short period investment from external country and for member state rise and with them also the whole economy.

Ten years after in 1987 a Single Administrative Document replaces hundreds of national customs declaration forms.

In the same year was created a shared and common transit system for goods. All those steps pave the way to build common characteristic among goods producers within European borders and beyond.

1992 was the year of the Maastricht Treaty and, also the time in which EU adopt a Community Custom Code. That job behind that code had a fundamental importance for the simplification of traders and customs within the internal market. It put together for the very first time in a unique code the rules and provisions of customs legislation that until that moment were divided in a huge number of Community regulations and Directives.

From 1993 the free movement of goods become a reality. That radically changed our continent not only from an economically point of view. Not only had repercussion on Custom duties regulation or similar but also on the aspect of EU and the behave of people. The regimentation of Custom duties literally changes the shape of Europe. There were no more long queues at the frontier for

commercial vehicles that had needed before to be control just only to cross the border from a country to another.

In 1994 the tariff of European Union start to be daily upload thanks to the new digital format of TARIC.

Just to be more specific TARIC is the Integrated Tariff of the European Union.

It is basically a multilingual database that integrate all the measures linked to the EU custom duty tariff, commercial and agricultural legislation. That tools was and still fundamental for member state in order to have a clear view on imported goods into the EU or exporting goods from EU.

The TARIC system become more and more efficient thanks also to the exploit of IT technologies and of the digital database.

With the new millennium several revolutions took place in the market.

First of the creation of a new common coin in 2002. That obviously made the nations even closer than before by far.

In 2004 ten new country join the EU. That highlight the amazing result reached in the previous year form this organization. With these new dimension and awareness of the market new tools was needed. Just set the level of custom duties was not sufficient anymore. That is why in 2005 was launched a Custom risk Management system that allows more than 800 customs offices of different nation to share data and information about risk and irregularities lead to several trade through a digital platform.

The principal goal of Custom security was to control the security of supply chain and trades from and to the EU borders.

Along the years the relative young EU has adjusted its organization under huge number of factor and variables.

In the las 52 years past from 6 to 28 members and today the European Union is currently the largest trading block in global terms.

That has as consequence that its custom union has a central role in the international trade. Recalling the previous chapter in which I talk about the inefficiency of a commercial policy of a little state, it is easy to understand why the European union was the only way to remain competitive at global level from a commercial point of view. From the moment that we must face with economical power as USA and new Asiatic market the EU negotiating position thus outweighs that of any single Member State acting on its own.

Thanks to several turning point along the history we understand how aggregation of nation and the reduction of custom duties just leave the market rise and work better.

As well as the use of *ad valorem* custom duty is often related to a healthy society and that national administration of the tariff is better that the private one by far because naturally reduce the phenomena of smuggling and reach higher and cost efficiency performances.

In the last part of this first chapter I will analyse the peculiarity situation created by the Brexit and the possible consequence for UK.

1.7. Consequences of Brexit on custom duty

As it was explained in the previous paragraph UK was never hundred percent convince to join the EU union. Since the foundation of EEC when it was already in contrast with the policy carried on by French and the other nation.

So is not that astonishing that UK is also the first country to leave the Union. I am talking about that here because one of the principal reasons of this event is linked to the fiscal European policy and precisely to the Custom policy.

During the politic debate the principal argumentation of pro-Brexit as Daniel Hannan start from the conflict between the parliamentary stature of single nation and the ruling of Brussels institution. The latter in fact most of the time has the precedence on the national decision.

From their point of view the governance of the union, since the foundation of the ECC, was more concentrated on political and welfare aspect then on economical one by far.

Hannan and the other supporter of Brexit was not a free-trade area but a custom union. Generally speaking, this is a positive aspect but they underline a technical difference that is the very central reason of “leaving the UE”.

If free-trade areas remove barriers between member and tend to make participants wealthier, a Custom Union, by contrast, erect a common barrier around its edge who surrender the right to strike individual trade deals.

That situation it particularly tough for the Great Britain because differently from the other 28 member states it commerce and trade more with the rest of the world then to the other countries of the Union. That is why, in their opinion, the EU's Common External Taxes were particularly penalising for the Britain economy.

Pro-Brexit had declared that from the day UK will leave the Union on, it will be the EU's single biggest export market. That why during all the last period of negotiating they had tried to achieve agreement similar to the once hold by Switzerland, where the can enjoy the free trade with the Euro zone but at the same time are free to sign bilateral agreement with external country.

Then after the official communication its intention to withdraw from the European union in 2017 and following approval of this extension in 2019 from the UE countries, from the first of February 2020, the United Kingdom finally reach its goal. It will non longer be a member of the European Union. There will be a transaction period from that day until the end of the year (December 31th 2020) in which the EU law will continue to apply in the UK. So, during the current year nothing is going to change for the citizen and business of the nation.

After this transition period if a no withdrawal agreement will be reached then Great Britain will be perceived from the Euro zone as a third party. As a consequence, Brexit will be particularly tough for all those businesses that only have trade within the Single Market without cross – border interaction. Enterprises that will start or carry on previous business with UK will need to engage in procedures which are mandatory for trade with third countries. Those enterprises have to start to inform themselves about these matters and obtain information on what trade with non-EU countries means and on which documentation is needed to trade goods and services in cross-border interactions.

Below are some of the principal aspects of trade with third countries:

- Custom declaration and related authorizations granted by customs authorities;
- Customs value, commodity codes and potential customs duty;
- Import and export restrictions.

Another point that must be considered is related to transfer pricing that I will analyse in the following chapter.

CHAPTER II

TRANSFER PRICING

2.1. A general overview

Transfer pricing refers to the determination of the price and other conditions for the transfer¹¹ of goods, services or assets between affiliated companies situated in different tax jurisdiction.

Thanks to the exponential growth of international trade that the world is experience since the 20 centuries the subject of transfer pricing is becoming crucial for the multinational enterprises (MNE)¹². Anytime that goods, assets or intangible services need to cross a border in order to move form one part of a company to another transfer pricing becomes a relevant issue both for the taxpayers and for the national tax and custom authorities which have the responsibility to manage these cross-border flows.

When we talk about transfer price we must to consider the arm's length principle that said that the price for a trade among different party of the same multinational

¹¹ An indicator of this characteristic is the ability to set transfer price that differ from market price. The market price is a price set in the marketplace for transfers of goods and services between unrelated person (B.J.Arnold, M.J:McIntyre; 2002).

¹² Multinational enterprise group (MNE Group): A group of associated companies with business establishments in two or more countries. (OECD transfer Pricing Guidelines, 2010).

enterprises as to be set as the agreement was between two unrelated parties in free market condition.

In fact, the main problem is that MNE use transfer pricing with the aim of minimize the paid taxes.

Often related body avoid the income taxes of a country thanks to the manipulation of transfer pricing activities.

A short explanation of transfer pricing following:

A Multinational enterprise is operating in two different country, let's say country X and country Y, where X has a high tax rate while country Y has really low, almost null, tax rate. E.g. subsidiary A might avoid paying income taxes in country X by setting a price on the sale of its goods to Subsidiary B that will have a little or no profit. If the actual tax rate in country Y is lower than the effective tax rate the tax X, then the total tax burden of the affiliated companies A and B would be reduced through the use of inappropriate transfers prices. Furthermore, if country Y is a Tax Haven, then the affiliated companies would pay a very low level or worse none taxes.

To summarise for tax purposes, the transfer pricing determines the amount of income that each party earns and thus, the level of income tax that is due in both country of export and the nation that import that specific good or service.

A higher transfer price may reduce the taxable income in the country of importation and increase the taxable income in the country of export. A lower transfer price has the opposite effect.

Aim of this chapter is in the first part to give a general recall at the history beyond transfer pricing, understand the different techniques to apply transfer pricing, the arm's length principle and in the second part start to make several considerations between the correlation existing between transfer pricing and custom duties.

2.2. History of Transfer Pricing

Since 1917 the Internal Revenue Service (IRS) in the USA was allowed to allocate income and deduction among linked corporations. IRS commissioners were authorized to make adjustments into accounts of related parties with the aim of avoiding and ensuring the regular and true declaration of taxable income.

As early as 1935 regulations have adopted the arm's length standard as the tool to reach the provision. Transfer pricing regulations enforced in 1968 provided more guidance on the application of the arm's length standard, including pricing methods and additional rules for certain intercompany transactions.

The United States has strongly helped build an international consensus in favour of the arm's length standard. Generally speaking, one reason could be that since the

Bretton Woods policies was the nations the push a rise of international trade the most and secondly because the multinational enterprises that more were using transfer pricing tools were American.

All the 50 current income tax treaties of USA (except the one with the nations that were under the control of Soviet Union) contain articles that talks about mutual application of the arm's length principle with the goal of find agreement on transfer pricing disputes.

The organization of Economic Cooperation and Development (OECD) similar adopted the arm's length principle as the foundation of its report in 1979 (transfer pricing and multinational enterprises) and also in its guidelines in 1995(transfer pricing guidelines for multination enterprises and tax administrations).

2.3. The OECD

Talking about OECD I will spend a paragraph just to clarify what this organization is.

It was founded in 1948 with the name of OEEC (we already talk about it in the previous chapters) from French for the European country, with the aim of helping the Marshall Plan in its administration aspect. The name changed in 1961 o in Organization for Economic Co-operation and Development (OECD) and it was extended also to non – European nations.

Along the years other countries have joined this organization or stipulate treaties with it.

OECD has as a principal aim the regulation of taxes. In fact, it publishes and updates tax model convention that has to be used as a template for allocating taxation rights between different countries. In general OECD tend to allocate the principal right to tax to country from which capital investment originates rather than the country in which the investment is made.

The aspect that interest this thesis the most is the Transfer Pricing Guidelines that was published by OECD in 1995. Those Guidelines serve as a template for profit allocation of transactions within multinational enterprises to county. The earlier version, of July 2017, incorporates the approved action developed under the Base Erosion and Profit Shifting (BEPS) project initiated by the G20.

2.4. Arm's length

Going back to the arm's length topic its standard call for an evaluation of the functions performed, asset used, and risks assumed in controlled taxpayer in internal transaction of a MNE.

While the arm's length character of controlled transactions is verifying through comparison with comparable uncontrolled transactions, it is recognised that

uncontrolled taxpayers who engage in comparable transaction under comparable circumstances do not always achieve identical results.

Then the IRS or OECD will not allocate taxable income where results are within an arm's length range.

In recent years, some countries have sought to reach agreement with their taxpayers on the methodologies to be used in setting transfer prices before a transfer pricing dispute can even arise. This kind of agreement is called "advance pricing agreement" APA.

Nevertheless, conflict and a dispute among countries on tax topics and so on transfer pricing issues still be common.

In 2008 were updated new rules from OECD to the Model Treaty¹³ in order to bind the arbitration of nations in setting prices for trade. Thus, the paper was focused on transfer pricing rules used in the EU member states and had the goal of avoid taxpayers from shifting income to related bodies located in tax havens or in countries where they can pay a lower level of taxes.

Generally speaking Nations should take care of own tax revenues through using transfer pricing rules. That can surely help in cut off the erosion of the tax base in their country.

¹³ OECD Model Treaty forms the basis of bilateral tax treaties involving OECD member countries and an increasing number of non – member countries.

2.5. OECD Transfer Pricing Guidelines

The transfer Pricing Guidelines provide explanation regarding the application of arm's length principle¹⁴ to the pricing of cross-border transaction between different bodies of the same multinational enterprise.

As I said in the introduction nowadays the global economy see the greatest part of its trad operated by MNE and so National Governments have to careful that those MNE do not shift out their income to tax paradise and at the same moment enterprises have to be sure not to pay taxes more than once for each transaction.

In other worlds, for taxpayers it is essential to limit the risk of a double taxation that can be lead to a dispute among two country regard the arm's length remuneration for their cross – borders transaction.

The authoritative statement of the arm's length principle is found in paragraph 1 of Article 9 of the OECD Model Treaty. The hart of the arm's length principle is the comparability analysis that actually is the examination of controlled and uncontrolled transaction.

Unfortunately, there are several situations in which that principle is difficult and complicated to apply, e.g. in multinational enterprises that are dealing with brand new products or services or intangible items. Particularly difficult is those situations

¹⁴ Numerous countries use also the terms "market price" or "fair market price".

where associated enterprises may engage in transaction that independent enterprises will never going through.

2.6. Method of Transfer Price Application.

So, as I said arm's length principle is generally based on comparability analysis that in a nutshell is a comparison of the conditions in a controlled transaction with the conditions in transaction between independent enterprises (uncontrolled transaction). In order to be consider comparable the economical characteristic of a specific transaction have to be comparable too.

When determining whether or not there are any differences between the transactions being compared that effectively impact on the exanimated conditions there are five comparability factors that the OECD Transfer Pricing Guidelines identify as important to consider:

1. Contractual Terms that will influence the allocation of functions and risk between independent parties and, therefore, the price charged, and margins earned. About the contractual term is fundamental to verify that the contract are actually adhered to in practice and are in line with the conduct of the parties.
2. Functional analysis which involves an analysis of functions performed, risk assumed and assets employees, may be considered a cornerstone of the

comparability analysis. The remuneration of a party, and though its profit potential, will be correlated with the functions it performs, the risks it bears and the assets that it employs. In a nutshell simply performing more functions, getting greater risk, and employing greater asset is not lead to high profitability. On the contrary bearing great risk increase the possibility of a follow in term of profitability or even losses. A functional analysis plays an important role in accurately delineating the transaction though determining how the transfer prices should be set.

3. Characteristics of the good or service impact directly upon the value attributed to it in the open market. So consideration on characteristics is required in order to determinate if there are any differences that can impact the analysed condition and, where there is, which adjustment can be apply to eliminate the impact. Those characteristics can regard: tangible property(physical features, quality and reliability, availability and volume of supply); services (nature and extent of the services) and the intangible property.

4. Economic circumstances among a transaction can have a significant influence on its pricing. E.g. the price paid for the same goods or services can differ

significantly as between geographic locations or the industry in which they take place.

Some circumstances that could be interesting to take into consideration are:

- Geographic location;
- Market size,
- Barriers to entry;
- Existence and availability of substitute products;
- Government regulations;
- Economic, business or product cycles

5. Business strategies also can influence a lot the price of a transaction. Such strategies may include: market penetration, market expansion, market maintenance and diversification of the strategies.

The comparability factors explained before are referred to the guidance of most countries with established transfer pricing rules. To stress of the accuracy of that , recent version of OECD Transfer Pricing guidelines highlight the importance of accurate delineation of transaction in comparability analysis and the data that a take into consideration.

Generally, the analysis follows a specific journey.

Starting from the preliminary analysis of the condition of the controlled transaction, through the identification and seek of potential comparable situation, the selection of the proper transfer pricing method and finally the declaration of the results.

There are 5 different methods that are possible to apply for the analysis of the arm's length: comparable uncontrolled price, resale price, cost plus, comparable transactional net margin and transactional profit split method.

- *Comparable uncontrolled price method (CUP)*

With this method the transfer price in a controlled trade of a tangible property is evaluated a comparison to the price in a comparable uncontrolled transaction. Where the prices differ, this may be an indication that the conditions in the controlled transaction were not arm's length. The Comparable Uncontrolled price method could be internal or external, depending on the characteristic of the parties that took place in the transaction. If it takes place between two third parties it is an external CUP, otherwise if it is between one of the related parties and a third party it is an internal CUP. This method fits perfectly in a situation in which:

- Internal comparables already exist (tangible goods, services, royalty rates);
- Commodities transactions, particularly where information on market prices for homogeneous or standardised commodities exist;

- Financial transaction (interest rates on loans);
- Are analysed common intangibles (royalty rates, licence fees).

CUP method could also be apply when an exact comparison is not possible but in that case the reliability of the analysis is reduced.

- *Resale price method (RP)*

This method start with taking into account the price at which the analysed good or service of the controlled transaction is resold (resale price). In other words it is the evaluation of the gross profit margin earned in the controlled transaction by referring to the gross profit margin realized in comparable uncontrolled transaction.

The resale price method is concentrated on the value of the reselling functions, so while similarity in fuctions, risks and contractual terms is significant, comparability in this method in not so lead to the characteristics and possible similarity of the product like in the CUP.

$$\text{Arm's length price} = \text{Resale price} \times (1 - \text{Resale price Margin})$$

Below three situation in which the resale price method could be successful:

- Situation where a reseller purchases different products for resale from associated parties and independent parties, but because of those differences the CUP method can not be applied;
- Purchases of products from associated parties for resale by a reseller that does not add significant value by making physical modification, contribution of valuable intangible property, significant marketing activities;
- Commissionaires and agents.

This method is not particularly used when the analysed taxpayer uses its intangible property to add an extra - value to the good resold.

- *Cost plus method (CP)*

This method is really similar to the first one CUP but instead of focusing on the resale price and thus on the gross profit mark-up, the cost-plus method focalizes on the value of the production functions. First aspect to take into account in this process is the cost faced from the supplier of the good or service of the controlled transaction, that are is then marked up by a coherent mark-up in order to determine an arm's length price. The fair cost-plus

mark-up is determinate by the gross margins earned in comparable uncontrolled transaction.

Arm's length price = Cost base x (1+Cost Plus Mark-up)

The costs to be taken into account are the direct and indirect costs of producing the good or service except the operating costs.

Below some situation in which the Cost Plus method is perfectly work:

- Whenever a supplier of goods or services in the controlled transaction provide also similar items to independent parties, but due to the differences in the products or services the CUP method can not be applied;
 - When the manufacturer does not add valuable intangibles or assume substantial risk;
 - Intra-group services;
 - Contract research and development arrangements.
-
- *Transactional net margin method*
This method (TNMM) consider an appropriate financial indicator that is based on the profit, that the tasted party realizes in controlled transactions, and compares it with that realized in comparable uncontrolled transactions.

If an financial indicator is appropriate or not depend on the facts, circumstances and the selection of the tested party.

A great strength of TNMM is that since the condition being examined is at the net margin level there is a greater pool of potential comparable information available than in the CUP, Resale Price and Cost Plus methods. It is also really flexible during the application. In fact the net margin can be compared to several bases depending on the financial indicator selected.

In some country, especially in the USA, there is a slightly different version of this method that is referred to the *comparable profits method(CPM)*.

Below some example in which the TNMM is successfully applied:

- Sales of tangible products to distributors where the data is not available to use the resale price method;
- Sales of tangible products by manufacturers where data is not available to use the cost plus method;
- Where gross margin data is available but is not reliable because of differences in the accounting
- Intra-group services, including contract research and development arrangements.

- *Transactional profit split method*

It is a particular method. After the selection of the relevant profit or losses arising from the controlled transaction those profit have to be split between the associated enterprises which are party jto those transactions on an economically valid basis. For this method there are three possible way to split the profits between parties.

The first possibility is the *comparable profit split* where relevant profit or loss is split by reference to comparable splits of profit studied between independent enterprises in comparable transaction.

Second option is the *contribution analysis* where the relevant profits or losses from the controlled transaction are allocated between the associated parties based on their relative contributions.

The last patter applicable is called *residual analysis*. It is an approach in which firstly allocates profits to a routine activity of the associated parties and then split the residual profit or losses on an economically valid basis.

Below three situations where the profit split method is used:

- When the parties give unique and valuable contribution to the transaction;
- When the controlled transaction is highly integrated and therefore can not be considered in separate basis;

- Where the parties of the transaction share the economically significant risks lead to those transactions.

Now that those five methods had been explained a question a question rises spontaneous.

Which factor influence the method decision process?

The first aspect that has to be taken into account is the domestic law requirements if there are any. For example, domestic law may dictate a hierarchy of appropriate method to the circumstances of the method or guidelines regarding the appropriate method to specific circumstances.

Also, the OECD TPG provide a guidance on the selection fo the most appropriate method. As follow several points to consider according to those guidelines:

- The respective strengths and weaknesses of the methods;
- The value of the method considered related to the nature of the controlled transaction;
- The result of the previous functional analysis;
- The availability of the needed data and information
- The degree of comparability between the controlled and uncontrolled transactions.

2.7. Italian legislation for the selection of Transfer Price method

As explained on the previous paragraph every fiscal legislation provides rules concerning Transfer Pricing, with the goal of limiting the shifting of internal revenue abroad.

In order to be closer to the OECD model against the double taxation¹⁵, the Italian legislation has known hug development in the last years. Nevertheless, Italy still remain attached on the fundamental rule of fiscal regulation (comm.7 art.110 TUIR) that basically describe the Arm's length standards. So basically, on the commercial relationship with foreign non-independent bodies, the value and level of transaction have to be with the one of the market.

The Legislative decree MEF of May 14th 2018 fix the specific rules for the determination of transfer pricing. The article 3 of this decree describe when two transaction could be considered comparable and is exactly the same rule described in the previous chapter. In the same way the needed parameters for the comparability analysis are the same of the OECD Guidelines.

Also, the 5 method are the same.

¹⁵ Double taxation may be juridical (taxation of the same income in the hands of one person by more than one state) or economic (taxation of the same income in the hands of two different persons).

The Italian decree allow the possibility of applying different method in situations in which:

- None of the standard method could find a reasonable application based on a specific transaction;
- The apply of this alternative method provide a result that must to me coherent with the once of independent comparable transaction.

Obviously, every method has its strength and weakness but, even if the OECD it is not strict anymore on a application hierarchy, the Italian legislator still recommend, whenever is possible, to choose the Cost Plus Method.

Where the analysis process is correctly conducted the legislator declares as follow:

- During it inspection, Fiscal Administration must follow the method chosen by the contributor;
- Every value obtained within the range of value obtained through the chosen method, is a value acceptable for the arm's length principle

Furthermore, in order to simply the analysis process the legislator had specified that all the cost that do not represent the core business of the related bodies could be consider as a single cost with the addiction of a profit mark-up of 5%.

In order to be considered not small cost the following characteristics must be respected:

- Are not core cost or support costs;
- Do not require the use of unique immaterial goods and do not help in the creation of those goods or services;
- Do not represent a risk for the provider of the service.

Finally, the decree specifies that the documentation regarding the chosen transfer price method is adequate when it provides the needed data to operate the analysis, with no influence from the possibility of different choices of the Finance Administration in the future.

PART III

THE RELATION BETWEEN TRANSFER PRICING AND CUSTOM

DUTY

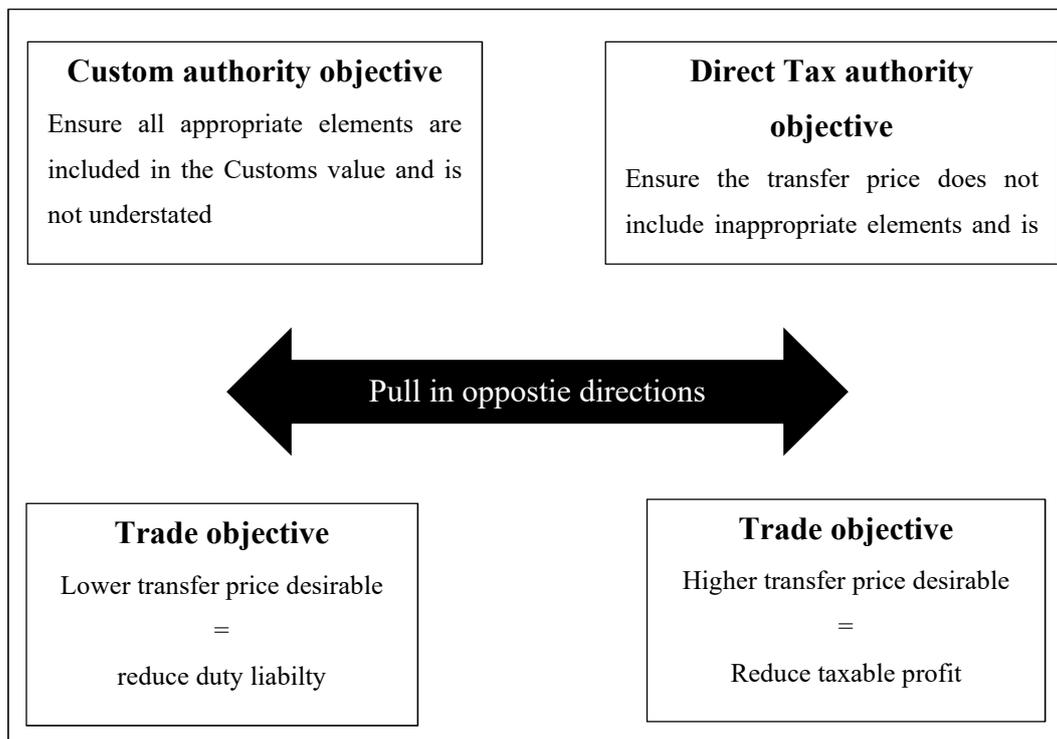
3.1. A general overview

Following the acquired notions of the previous chapter, it can be seen how the goal of Custom valuation and calculation of Transfer Pricing is quite similar. If customs are establishing whether or not a price has been influenced by the relationship between prices, the aim of tax regulation is to seek an fair price through the arm's length principle.

In both situation the price is set as the parties were not related and as they had been negotiated in a normal business condition.

It has been noticed that there are huge similarities between the WTO and OECD method for custom valuation and transfer pricing. For example if we take into account the WTO deductive method, it is based on the resale price of a good or services as is the OECD resale price method. The same applies to the plus profit that is similar to the OECD cost plus method.

Having identified the similar concepts, it can be observed that goal and aim of each approach are specular.



So direct tax authorities tend to follow the arm's length principle and the OECD TP Guidelines for set the price for transaction of the multinational enterprises.

Custom Authorities apply the relevant provisions of the WTO Customs Valuation Agreement.

However there huge difference are fundable in the application of those two principle, for example regarding policy objective, operational functioning, timing

of valuation, valuation method, documentation requirements and dispute resolution mechanisms. It is not unusual that more than one national authorities operate on the same topic or particular situation but in that case some different variables must to be considered.

On a specific import transaction, a Customs officer tend to give more importance in checking whether or not the value declared by the importer is under-estimated from the moment that is goal is to collect more duties. On the contrary the revenue authority will naturally try to understand is the import value was over – estimated or not because a revenue officer would be interested in limiting what would be regarded as an excessive tax-deductible amount in his jurisdiction.

3.2. New authorities' collaborations

Over recent years, it had been discussed about the possibility of sharing the information between the Authorities. In fact, transfer pricing studies may also be of use to customs auditors from the moment that the information provided by this body can also give useful information regarding related party transactions of imported goods. This potentially can reduce the waste of time in looking twice for the same information. This does not mean however that customs must rely solely on transfer pricing documentation. It could be just an additional evidence to consider as part of an audit enquiry.

In order to better understand this topic, in 2006 WCO and OECD have initiated a series of joint conference. There qualified person from Customs, Tax administration and private sector discussed about several viewpoints and give proposal regarding issues such as the scope for greater alignment and other technical aspects.

After the second meeting in 2007 start to be clear that such harmonization was very tough to realize especially because of the application of the methodology contained in the WTO Valuation Agreement is an obligation for a WTO Member country is was not expected in the medium – long term.

So, the new challenge was to find something within the constrain of the existing WTO agreement provisions.

3.3. A view from the private sector

The International Chamber of Commerce (ICC), that represent the world business organization that interacts with the national authorities for the enterprises, has produced a policy statement in which are showed a series of comments and proposal regarding the trade view on the relationship between transfer pricing and custom value.

They want to highlight how the enterprises face lots of difficulties in the evaluation of goods within the international trade. Those kinds of issue born

because the transaction between related parties have to respond to a double examination, one from the custom authorities and another one from the fiscal one, that have different and contradictory rules and interest.

From their point of view this dichotomy create uncertainty and slow down the economic globalization. It is also lead to the rise of implementation and compliance costs, absence of flexibility in the conduct of business operations and perhaps even more important creates a significant risk of penalties.

PART IV

CHANGES IN TAX RESIDENCE

4.1 A general overview

Until now we have analysed how the custom duty and the transfer pricing evolve and developed along the history and how they are interconnect.

Especially in PART III I had described which type of issue are raised by the interconnection between the respective authorities. We had a look at all the different point of view: the one of the custom duty authorities, the tax one and finally the point of view of the private sector.

What I have never really focused on, and that I will do in this final part, is where a single person or a private company have to pay the taxes. What determinate how the amount of fee an enterprise has to pay which are the variables to be taken into account.

Finally, I will describe how in Italy, some changes are taking place during the last years especially on the topic of the residence of physical person with the particular attention on the several mutual agreement with some nations.

To conclude I will describe the last and new agreement subscribed with China Republic.

On November 27th 2017 an new Convention Model against the double taxation was approved. With its actuation OECG have introduced significant changes that give a deeper explanation to the guide lines that was already discussed on the matter of BEPS (*Base Erosion and Profit Shifting*) developed along 15 actions.

In particular this new model try to implement the specific *actions*:2,6,7 and 14.

4.2. The project Base Erosion and Profit Shifting.

For Base Erosion and Profit Shifting it meant the set of tax strategies that some enterprises use in order to erode the taxable base and tough subtract tax (cash box) to the taxman.

Profit shifting form country having an high tax burden to the one that instead have a lower or null one it is already one of those strategies. It is possible to apply these types of strategies in areas with a high technology grade. Often the “flexibility” of enterprises revenue is much higher then the one of the tax systems. That allow company to find new way to evade taxation.

Before 2015 the international fiscal was based on principles that was been developed in 1920. This critical issue was faced for the first time during the G20 of 18-19 June of 2012 and start the journey until the apportion of BEPS guidelines of 2015.

In this paragraph I will analyse only the actions relevant for the new convention model against the double taxation, so as specified before the *actions*:2,6,7 and 14.

The actions from 2 to 14 are developed on three pillars:

- I. Confer consistency to national tax systems in the of transnational activities;
- II. Implement the substantive requirements essential for the current international standard, pursuing a realignment of taxation (and tax regimes) with the substantial localization of production activities and the creation of value;
- III. Increase transparency, exchange of information and improve conditions of legal certainty both for the business world and for governments.

- *Action 2: Hybrid Mismatch Arrangements*

It is part of the first pillar and has as an object the one to neutralise the effect of the so called hybrid mismatch arrangements. Generally speaking, we are talking about “double not taxation”. It’s a set of tools act to take advantage of asymmetries among different national legislations.

- *Action 6: Treaty abuse*

It is part of the second pillar and tries to prevent, through specific treaty abuse, the granting of benefits in inappropriate circumstances, by virtue of what is allowed by the conventions against double taxation. It is referred especially to the specific situation of the so called “treaty shopping” that takes place when a subject that is not located in nor of the two nations that have stipulate a treaty tries to take advantage of this treaty. These activity are carried on thanks to the creation of fictitious companies called “letterboxes” or “shell companies”.

- *Action 7: Permanent established status*

It is part of the second pillar and has as a goal void the technique for which by substituting the distributors with "commissionaire arrangements" a company shift the profit to another country.

- *Action 14: Dispute resolution mechanisms*

It is part of the third pillar. This final action tries to grow the effect of dispute resolution mechanisms, also in consideration of the fact that the changes introduced by the BEPS project could be likely to lead to uncertainty in the short term, with possible repercussions in terms of increased litigation.

As I said in the previous paragraph the new OECD model against the double taxation have brought several changes. But before to analyse in particular which of these changes has in particular interested the art.4 let describe what the article 4 was and in part is still about.

4.3. The art.4 of OECD model.

The Convention Model describe the concept of tax residence of physical person in the art.4, that describe the definition of *conventional residence*, and has a list of criteria, the *tie breaker rules*, that have to be apply in the hierarchical order in which they appear, in the situation of *dual residence*.

The resolution of tax residence conflicts of individual represents a central aspect within what concern the convention model. First of all, gives the possibility to identify the Nation that will have the right to subdue full tax liability the revenue of a specific subject.

The growing mobility of people, driven by personal needs (such as the search for a better standard of living), work and investment, as well as the contrast to the fictitious “abroad-residence” phenomena by the tax administrations have done nothing but increase the number of subjects which could potentially be involved in residence issues.

The criteria for the determine the tax residence on the OECG model convention are as follows:

- 1 Permanent home available;
- 2 Centre of vital interests;
- 3 Habitual adobe;
- 4 Nationality;
- 5 Mutual agreement procedure.

Permanent home available: following the firs criteria the residence coincides with the place where the taxpayer owns or has a permanent home. On this topic the *commentario* gives a further explanations and in particular clarify that the home:

- It can be owned in any capacity, even for rent;
- Must has an sufficient organization that allow the taxpayer a long term and not occasional permanence.

In Italy as concept of residence it has to be consult the art.43 of Codice Civile.

Centre of vital interests: this second criteria takes into account the place in which the personal relationships and economical network are *closer*.

As specified by the *commentario*, in order to find the centre of vital interests, not only the social and familiar relationships of the taxpayer must to be considered but also the political, cultural activities (or others). Also the where his/her work location and where her/his administers the company have to be considered.

All these characteristics have to be analysed as a hole considering the specific of singular taxpayer.

Sometimes is not that easy to apply these criteria because e.g. the family is in a country while the economic interest are in another. The Italian legislator confer more importance here to the family interests.

Habitual adobe: The *commentario* does not provide a clear point of view on the requirements that have to be verified in order to find which minimum time lapse required is needed to be verified the habitual adobe.

It just says “a sufficient length of time”.

Nationality: It clarifies that if the habitual residence is identifiable in both Contracting States or, it is not in either of them, the person will be considered resident in the Contracting State of which he has the nationality;

Mutual agreement procedure: Finally, if the taxpayer has the nationality of both Contracting States or does not have the nationality of either of them, the competent authorities of the two countries will determine the residence with an amicable procedure, indicated in article 25 of the same OECD Model.

On the specific the art.4 is divided in three parts. The first and the third one are those interested by the changes of 2017.

Below the old version of art. 4.

RESIDENT

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority

thereof. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.

1. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:

a) he shall be deemed to be a resident only of the State in which he has a permanent

home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests);

b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode;

c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national;

d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

3. Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated.

4.4. Adjustments of art.4

The new convention's model introduces a relevant change referred to the criteria for the determination of the tax residence. In fact the third paragraph of the art.4, in its latest formulation, says that for the legal entities, that the tax residence in a specific country of a taxpayer instead of being determined by the direct application of the tie-breaker rule of Place of effective management, it has to be defined by an appropriate mutual agreement between the two competent authorities of the involved nations. This type of approach is called *case by case*, and is based on the concrete analysis of every single case.

Here the Country involved will have to define together the effective tax residence of the taxpayer, taking into account a series of variables described and illustrated in the *commentario*.

This analysis has to be developed along the following factors that can be linked to the place in which:

- the meetings of the board of directors are regularly held;
- the CEO make their principal functions;
- managers exercise the functions of ordinary administration;
- the head office is located;
- where the accounting documentation is kept.

The new *commentario* underlines that Nations can continue in following the original criteria of PoEM. Generally speaking the new model just required to the states to follow the principal element.

Thus, the real new is represented by the mechanism of collaboration between States that have to determine the tax residence of di entities different from physical person through a mutual agreement. This facilitated a lot to clarify the situation of *dual residence*.

A further new elements is about the notion of *habitual abode* in the terms of residence of physical persons. First of all, the new *commentario* specify that in all the hypothesis in which the property has been leased or rented and so the owner can not directly use it, that property should not be taken into consideration for the habitual abode.

There are three new elements to identify the habituality of a tax payers, as follows they are:

- the frequency of stays;
- the stay's duration;
- the regularity of stays.

These elements join the previous elements as the stays period duration in the year (183 days).

To conclude this paragraph I would like to highlight how the new *commentario* specify how the period of time spent in a country for reason like a divorce or other external factor must not be taken into consideration.

Below the changes at the first and the third part of the art.4 are in **bold**:

Replace paragraph 1 of Article 4 by the following:

1. For the purposes of this Convention, the term “resident of a Contracting State” means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any

other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof **as well as a recognised pension fund of that State**. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.

Replace paragraph 3 of Article 4 by the following:

2. Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, ~~then it shall be deemed to be a resident only of the State in which its place of effective management is situated.~~ **the competent authorities of the Contracting States shall endeavour to determine by mutual agreement the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention, having regard to its place of effective management, the place where it is incorporated or otherwise constituted and any other relevant factors. In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by this Convention except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States.**

Before to start to analyse the several mutual agreements of Italy and the lasts news regarding the approach of our country with the OECD model convention I will add now some information that I consider important about some news about the *Mutual Agreement Procedure*.

The art. 25 of model convention establishing an amicable procedure and an arbitration procedure for the resolution of interpretative issues, and for the

particular case of double taxation where the other dispositions of the Convention can not arrive at solution.

In the version the model says that the taxpayers can consult non only the competent authorities of hiw/her own nation or stat of residence but also the once of the other State.

4.5. Italian law on transfer of tax residence

Important clarification about the evaluation of the residence on the Italian soil of physical person and about the relation between national law and the convention against the double taxation, has been made from the response to the request for a request for a reply to question no.203, published in June 25th 2019 from the *Agenzia delle Entrate*.

It express itself on the subject highlighting that if for the great part of the taxable period are satisfy at the same moment one of the expected requirements of the art.2 of TUIR and the current requirement in the other country, the conflict determined by “double” residence must be solved based on the double taxation conventions.

The tax agency has specified in the scenario of legislature conflicts between two country legislations they should be solved according to the criteria established in the paragraph 2 of the art.4 of OECD model. Thus, following the tie breaker rules.

These clarifications from our tax agency has given the possibility to overcome, where is needed, the way of operating that until now had been express be the jurisprudence of *Cassazione*, that had confirmed several time how only the inscription to the Italian registry office was enough to be considered to established also the tax residence in Italy.

The evaluation of residence, in the specific case of a physic person employed in a foreign company have a huge importance. In in one hand a non-resident subject is never under the Italian taxation for the revenue eared abroad, a resident person I taxed in Italy even if he eared his/her revenue abroad.

4.6. Tax residence in conventions: particular situations

As it is specified before these conventions are useful overcome issue related to the double tax residence.

There are anyway some situation that differ from the general guide lines. These particular situations in some case provide a different formulation of the law.

They can give another point of view to the tie breaker rules.

As follow some of these particular conventions:

- *Convention Italy – Japan:*

This particular convention against the double taxation does not provide nay provision regarding any criteria act to cut down the tax residence issue. Here the eventual problem goes directly on charge of the competent authority of the two nation s that every time have to decide where a person is officially residence from a tax point of view.

From a practical point of view is often quit tough to start these procedure. Then most of the time if a subject is not registered at AIRE¹⁶ it doesn't matter if he/she has moved in japan. He/She will continue in paying taxes in Italy.

¹⁶ The Registry of Italians residing abroad, better known by the acronym AIRE, is the register of Italian citizens residing abroad

The new model have made also the following change to the *commentario*:
Japan reserves the right to omit the phrase “except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States” in paragraph 3.

- *Convention Italy – Bulgaria:*

The article 1 of the convention between Italy and Bulgaria is peculiar. Here the first test of *permanent home* it does not expected. The article one only takes into consideration the personal relationship to determinate the tax residence. If this is not possible to determinate the two state will find a mutual agreement.

- *Convention Italy – Ireland*

This convention is particularly interesting because modify the time of permanence that an individual have to spend in the other nation to incur in the change of residence.

The convention underline if an Italian spend more then 91 day on the Ireland soil he/her will be considered resident there from a fiscal point of view.

- *Convention Italy – Germany*

This convention focus on the situation of change residence along the year. Here is specified that if an individual move form Italy to Germany or vice versa he will start to pay taxes in the other country from the moment that he/she move his/her residence.

4.7. Memorandum¹⁷ Italy – China

This is one of the last conventions and for sure one of the more discuss in 2019.

I personally think that is good example to show how the directive of OECD influence the new treaty or help country in found a way to established or as in this specific case renew international agreement.

The *Memorandum* is not only a fiscal agreement but for sure the fiscal aspect has a huge influence on the treaty as a whole.

The principal aim of this treaty is to enforce the political, economic and direct relationship between the two country. The inclusion of every region of both Italy and China is compulsory.

The subjects of collaboration are several, starting from the political dialogue until the transport, logistic and infrastructure affairs passing through the connectivity of people and the cooperation for a sustainable development.

¹⁷ Memorandum of Understanding was signed by the political leader of the Italian's giallo-verde government Giuseppe Conte and the Chinese President Xi Jinping. It had made official the accession of Italy to the "Belt and Road Initiative.

But the two aspects that have relevant importance for this thesis are the following.

- *Commerce* where the parts are going to work in order to rise the number of investment a trade flow in both the directions. As well as will be implemented the bilateral industrial collaboration and the collaboration in external country.
- *Financial collaboration* where the part will enforce the communication and bilateral coordination in the subject of fiscal policies.

As I said the *memorandum* is the update of the obsolete agreement signed the 31 of October 1986. This updating has been made following especially the requirement of the new recommendations of the project OECD/G20 and BEPS in the subject of artificial shifting of profit aimed to the tax base erosion.

The first three article of *memorandum* are particularly related to residence argumentation of the OECD model.

The *art.1* set the boundaries of the juridical competence area of the treaty, that include both juridical and physical person resident in one or both of the states. The text is the same of the one adopted in the OECD model.

The *art. 2* defines the objective scope of the agreement by identifying the taxes included. In Italy they are IRPEF, IRES and IRAP while for china individual income tax and enterprise income tax are included.

The *art. 3* describe the general definition, following the guidelines of OECD and the current contention, of the conventions stipulated by Italy regarding the double taxation.

The *art. 4* defines the status of residence and identify the criteria in the tie – breaker rules of OECD convention.

CONCLUSIONS

When I start to write this thesis, I had clear in mind which one had to be the conclusion. Through the explanation of several variables that influence the international tax environment my idea was to identify a reason that can support the decision of the Italian tax authorities in supporting the tie breaker rules when there a situation of dual residence is rising.

Actually, having in mind the history of custom duty and international taxation I was quite convince that, follow the new version of art. 4 of OECD model and more in general, an international rules for address and solve the problem of dual residence, should represent the only way to be attached with the world economy and the exponential grow and development of the market.

But from the day that I start that journey until February 21th 2020 unpredictable events happened in the Italian courts.

As I explained in paragraph 4.5 *Agenzia delle entrate* published in June 25th 2019 the respond n.203 that finally had changed our old personal interpretation of dual residence based only on the registration on the registry office on a particular case where Denmark.

But what happened then? Just a month after, the same Italian authority change its previous behave when it was analysing a dual residence in which UK were involved.

In July 18th 2019 *Agenzia delle entrate* with the respond n.270 step back to the previous and old method to define residence of individuals.

In my personal opinion History teach us that we'd better to be align with the international convention especially in a time where even these international authorities have to face huge issue in understanding market, trade, movement of people and as a consequence do define the most appropriate tax strategies.

Probably in order to able to remain attached to the European and world evolution in this theme, the only patter in to "force" our self starting from the Current Italian legislation.

I know that it is a strong position, but in my opinion change the comma.2 - art.2 of TUIR where the registration at registry office is still named could be a solution in order to solve dual residence issue. It is here that Italian legislation have to provide a single and united interpretation on the subject with the OECD model art.4 paragraph.2

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