Italy

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Supreme Court Decision on Transfer Pricing: Burden of Proof, Anti-Avoidance Interpretation and Abuse of Law Principle

The Italian Supreme Court recently issued its ruling in a case concerning the arm's length value of transactions between companies belonging to an international group. This decision focused on the true nature of the domestic transfer pricing rules and whether the taxpayer or the tax authorities bear the burden of proof with regard to transfer pricing issues.

1. Issues

A recent decision of the Italian Supreme Court (*Corte di Cassazione*)[1] deals with a key international tax law concept, namely the arm's length value of transactions between companies belonging to an international group. In this case, the tax authorities asserted that the price paid by an Italian company to its foreign affiliates was higher than the arm's length value. As a result, the tax authorities assessed increased profits to the Italian company under the transfer pricing provision of former Art. 76, Para. 5[2] of Presidential Decree 917 of 22 December 1986 (the Income Tax Code or ITC).

The Supreme Court decision focused on (1) the true nature of domestic transfer pricing rules and (2) which party bears the burden of proof with regard to transfer pricing issues (the taxpayer or the tax authorities). In considering the second issue, the Supreme Court referred to the concept of "abuse of law" as stated in recent decisions of the European Court of Justice (ECJ).[3]

2. The case

2.1. Facts

The Italian company is part of an international automotive group that produces and sells vehicles around the world. The parent company is located in the United States, while the main plants are located across Europe (namely in Germany, Spain and the United Kingdom) and the production is carried out through affiliated companies located therein. The Italian company operates as a distributor of vehicles purchased from affiliated companies.

In 1967, the US parent company issued a directive to all its affiliates under which:

- the costs of maintenance and repairs, as well as liability for damages from the use of the vehicles, remained with all affiliated companies in charge of the distribution and sale of the vehicles to costumers; and
- the price fixed by the manufacturers should have taken into account these additional costs suffered by the distributing companies.

Thus, under this directive, the expenses related to maintenance, repairs and liability for damages from the use of the vehicles remained with the Italian company.

In their assessment, the tax authorities argued that the price paid by the Italian company to its foreign affiliates was not arm's length, as the former did not receive any compensation for the maintenance and repair obligations, while, under Art. 1490 of Civil Code, such obligation would remain with the manufacturers. The tax authorities concluded that because the price paid by the Italian company was in excess of the arm's length value that should have been calculated under the transfer pricing provisions set out in Art. 110(7) of the ITC, the extra costs incurred unlawfully reduced the Italian company's taxable income to the benefit of its foreign affiliates.

2.2. The decision

At the outset, the Supreme Court pointed out that the reference to Italian civil law was improper, as the relevant transactions fall within the scope of international transactions subject to the provisions of the Vienna Convention of 11 April 1980.[4]

Second, the Supreme Court rejected the arguments raised by the tax authorities regarding the form of the agreements entered into by the Italian company and the foreign manufacturers. Indeed, according to the tax authorities, the agreement was based on the 1967 directive that had been issued in a "proper form". The Supreme Court relied on Art. 11 of the Vienna Convention, under which "[a] contract of sale need not be concluded in or evidenced by writing and is not subject to any other requirement as to form. It may be proved by any means, including witnesses". Based on the above, the Supreme Court reasoned that the transactions were properly concluded under international law and that the 1967 directive must be considered valid. The Supreme

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1. Court of Cassation decision 22023, 13 October 2006.
2. Currently Art. 110, Para. 7.
3. See e.g. *Halifax plc et al. v. Customs and Excise Commissioners* (*Halifax*), C-255/02.
4. Ratified by Law 765 of 11 December 1985 and entered into force on 1 January 1988.

Court acknowledged that the 1967 directive also contained a clause under which the costs of maintenance and repairs, as well as the liability for damages, rested with the distributor. Then, the 1967 directive contained guidelines for determining the arm's length price, such that the fixed price should have been reduced by an amount equal to the presumed future costs shifted to the distributing company. In this regard, the Supreme Court ruled that in order to successfully adjust the taxable income, (1) the tax authorities should have proved that this clause was in fact violated and that (2) this violation was due to the primary goal of obtaining a tax advantage. Indeed, the Italian taxpayer unlawfully reduced its taxable income.

Furthermore, the Supreme Court interpreted the transfer pricing rules contained in Art. 110(7) of the ITC as an anti-avoidance provision aimed at preventing the situation where, through intra-group transactions, taxable income is shifted from Italy to a country with a lower tax burden. In this regard, the Court reasoned that the transfer pricing rules must be regarded as anti-avoidance provisions because they have their source in the Community law doctrine of abuse of law,[5] as well as in other areas of domestic anti-avoidance legislation (i.e. Art. 10 of the Law 408/90). The Court, citing some of its previous judgments,[6] ruled that insofar as the transactions are aimed at obtaining anything other than the creation of a tax advantage, the burden of proof rests with the tax authorities. To this end, the Court also referred to the 1995 OECD Transfer Pricing Guidelines (1995 OECD Guidelines), which provide that should the relevant jurisdiction place the burden of proof on the tax authorities, "the taxpayer need not to prove the correctness of its transfer pricing in such cases unless the tax administration makes a prima facie case showing that the pricing is inconsistent with the arm's length principle".[7]

Based on the above, the Supreme Court, in ruling in favour of the taxpayer, held that:

- the tax authorities should have first proved that the overall tax burden, at that point in time existing in Italy, was greater than the effective tax burden in the countries in which the transactional counterparties were located (i.e. Germany, Spain and the United Kingdom); and
- the tax authorities should have recalculated the arm's length value of the transfers.

As the tax authorities did not prove either of the above, there were no grounds for the Supreme Court to accept the assessment.

3. Domestic Law

Transfer pricing provisions are currently embodied in Art. 110(7) of the ITC, which stipulates that:

> ...the business income components derived from transactions with companies not resident in the territory of the State and which, because of their direct or indirect relationship with the enterprise are subject to its dominant influence or have a dominant influence on it, shall be valued, if it derives an increase of the income, on the basis of the normal value of goods transferred, services performed and goods and services received. The provision also applies when the enterprise and the non-resident are subject to the dominant influence of the same person...[8]

The concept of normal value, as defined by Art. 9(3) of the ITC, constitutes the statutory basis for the determination of the arm's length value of an intra-group transaction:

> Normal value means the average price or consideration paid for goods and services of the same or similar type, in free market conditions, at the same level of commerce, at the time and place at which the goods or services were purchased or performed, or, if no such criteria are available, at the time and place nearest thereto. In determining normal value, reference must be made – to the extent possible – to price lists or tariffs of the party which has supplied the goods or services or, if necessary, to the indices and price list of the Chamber of Commerce and to professional tariffs, taking normal discounts into account. For goods and services subject to price control, reference must be made to the regulation in force.[9]

In order to provide guidance on the concept of normal value, the Ministry of Finance issued a circular letter (the Circular)[10] in which it analytically indicated the methods to be used for each type of transaction, based on the arm's length principle. The Circular was expressly aimed at implementing the criteria for determining transfer prices as set out in the 1979 OECD Report.[11]

Despite not being legally binding, the Circular is acknowledged by the tax authorities and by taxpayers, and is deemed to be the main point of reference for the interpretation of transfer pricing issues. In this regard, both the 1979 OECD Report and the 1995 OECD Guidelines[12] have become significant tools for interpreting transfer pricing matters.[13]

4. Commentary

The Court's ruling is noteworthy for various reasons, as this is the first time that the Supreme Court has issued a decision in a transfer pricing case that involves both procedural and substantial issues.[14]

5. The Supreme Court expressly cited the ECJ decision in *Emsland-Stärke GmbH v. Hauptzollamt Hamburg-Jonas* (*Emsland-Strake GmbH*), C-110/99.
6. Including Decision 4317/03.
7. See 1995 OECD Guidelines, Para. 5.2, Chap. 5.
8. The application of Art. 110(7) of the ITC may give rise to a decrease of the resident company's taxable income only envisaged under a mutual agreement between Italy and the treaty partner.
9. *The Tax Treatment of Transfer Pricing* (Amsterdam: IBFD, online and loose-leaf publication), G. Maisto, Italy chapter, at 2.1.
10. Circular Letter 9/22667 of 22 September 1980. On 12 December 1981, the Ministry of Finance issued Ministerial Circular 42, which implemented some minor amendments to the relevant legislation.
11. *Transfer Pricing and Multinational Enterprises* (Paris: OECD, 1979).
12. The 1995 OECD Guidelines have not yet been implemented in Italy.
13. In a recent decision (17206 of 26 July 2006) dealing with the recharacterization of an Italian company as a permanent establishment of a Panamanian company, the Italian Supreme Court explicitly stated that it refused to strictly follow the interpretation introduced at the OECD level and contained in the new commentary to Art. 5 of the OECD Model Treaty. The Court pointed out that the commentary represents a mere recommendation and that Italy has voiced a reservation to the new commentary (and made it clear that it is willing to follow the jurisprudence of its own national courts on this matter).
14. This recently published case has already drawn the attention of some Italian scholars. See D. Bergami, "Onere della prova a carico dell'amministrazione nel transfer pricing", *Corr. Trib.* (2006), at 3732; A. Ballancin, "La disciplina italiana del transfer price tra onere della prova, giudizi di fatto e l'(in)esistenza di obblighi documentali", *Rass. Trib* (2006), at 1982.

4.1. Burden of proof on the tax authorities

From a procedural perspective, the Supreme Court concluded that the burden of proof rests with the tax authorities. Therefore, the latter had to prove the grounds on which the assessment of increased taxable income was based (e.g. must have proved that the transfer prices were not arm's length) and should have calculated the arm's length value.

Despite the fact that the authors agree with the outcome of this case, the grounds on which this decision is based, are questionable. In fact, the Supreme Court ruled that the burden of proof remains with the tax authorities, as the transfer pricing rules are regarded as anti-avoidance provisions. In this regard, the authors maintain that (1) a number of valid arguments exist which may lead to the same result without the need to interpret Art. 110(7) of the ITC as a general anti-avoidance provision and (2) it is doubtful whether the interpretation of the Italian judges is consistent with the true scope of the domestic transfer pricing provision.

Art. 2967 of the Civil Code states the general principle that "[o]ne who asserts a right in judicial proceedings must prove the facts on which the right is based. One who asserts the invalidity of such facts, or claims that the right has been modified or extinguished, must prove the facts on which the defence is based". Neither the ITC nor Presidential Decree 600 of 29 September 1973 on the Assessment of Direct Taxes include a provision that clarifies which party should bear the burden of proof. The judges could have merely made use of the general civil law principle endorsed in Art. 2967, under which the party that asserts a claim in judicial proceedings must prove the facts on which the claim is based.[15] Therefore, the burden of proving that the inter-company transactions have been carried out other than at arm's length still would rest with the tax authorities,[16] merely applying the general civil law principle.[17]

4.2. Transfer pricing rules as pure anti-avoidance provisions

Italian tax law does not contain a general anti-avoidance provision. Rather, tax avoidance is dealt with through specific provisions, such as:
- Art. 37-*bis* of Presidential Decree 600 of 29 September 1973,[18] under which the tax authorities may disregard single or connected acts, facts and transactions intended to circumvent obligations and limitations provided under tax law aimed at obtaining tax savings or refunds otherwise not due in the absence of valid economic reasons;[19]
- CFC legislation, contained in Art. 167 of the ITC, the application of which may be avoided if (1) the resident person proves that the foreign entity predominantly carries on an actual industrial or commercial activity in the state or territory in which it is located or (2) the resident person proves that the participation in the foreign entity does not achieve the localization of income in tax haven countries or territories. In both cases, the taxpayer must apply to the Ministry of Finance for an advance ruling;
- anti-tax-haven legislation, contained in Art. 110(10) and (11) of the ITC, which limits the deductibility of expenses related to transactions carried out with enterprises based in low-tax jurisdictions, unless the resident person proves that the non-resident enterprise carries on a real business activity, or the relevant transactions had a real business purpose and actually took place;[20] and
- Art. 73(3) and (4) of the ITC, under which non-resident trusts and companies are deemed to be resident in Italy for tax purposes if a number of requirements are met, unless the taxpayer provides evidence of the contrary.

Although a detailed analysis of each specific anti-avoidance provision is beyond the scope of this article, it is important to highlight that in all of the above situations (1) the burden of proof is shifted on the taxpayer, other than in case of Art. 37-*bis* and (2) reference to "valid economic reasons", the existence of an "industrial or commercial activity" and "real business" activity is always made. Moreover, the anti-avoidance rules seem to establish narrow boundaries for the taxpayer, as they apply by way of a legal presumption unless the taxpayer meets the requirements provided under the relevant legislation.[21]

15. Some scholars have already made it clear that Art. 2967 of the Civil Code governs the burden of proof in the case of tax assessments. See e.g. G. Falsitta, *Manuale di Diritto Tributario* (Padova, 2005), at 660; G. Cipolla, "L'onere della prova", *Giurisprudenza sistematica di diritto tributario*.
16. See Maisto note 9, at Para. 7.4.2.
17. For the sake of completeness, one must bear in mind that the Supreme Court indirectly upheld the principle according to which upon the notification of a tax assessment providing indicia of the non-existence of costs or the denial of their deductibility to the taxpayer, the burden of proof rests with the taxpayer, whereas the tax authorities must prove the grounds for an assessment of increased taxable income.
18. This provision replaced Art. 10 of Law 408/90, which was cited by the Supreme Court in its findings. With Art. 37-*bis* a different approach was taken in that tax avoidance transactions would no longer be identified by a mere list of specific types of transactions taken one by one. Rather, reference should be made to the purpose of the overall scheme (i.e. existence of valid economic reasons) and connected series of acts, facts and transactions.
19. Art. 37-*bis* applies only to the transactions listed therein, namely (1) transformations, mergers, divisions, voluntary liquidations and distributions to the shareholders other than profit distributions, (2) contributions of capital to companies and transactions concerning branches of activity, (3) transfers of credits, (4) transfers of excess tax credits, (5) operations covered by the legislation implementing the Merger Directive, (6) classifications on the balance sheet, (7) operations concerning transfers and valuations of participations and transfers of securities, foreign currencies and precious metals and transactions in derivative instruments, (8) payments of interest and royalties eligible for the exemption under the Interest and Royalties Directive (2003/49/EC), if made to a person directly or indirectly controlled by one or more persons established outside the European Union and (9) transactions between resident entities and their affiliates resident in tax havens and concerning the payment of amounts as a penalty or compensation (*clausola penale, multa, caparra confirmatoria o penitenziale*). With regard to all other transactions not listed above, this anti-avoidance rule does not apply.
20. The Provincial Tax Court of Milan, in a case concerning deductibility of costs charged by a foreign coordination centre to an Italian resident controlled company, confirmed this view. For a comment on the ruling, see N. Saccardo, *Provincial Tax Court Decision on Documentation Supporting Cost Sharing Agreement* 2 (2006), at 92.
21. See C. Rotondaro, "The application of transfer pricing rules and the definition of associated enterprises", 6 *International Transfer Pricing Journal* 6 (1999), at 260.

The current wording of the domestic transfer pricing rule does not include reference to the shifting of the burden of proof to the taxpayer, nor to the existence of valid business reasons.[22] Art. 110(7) of the ITC merely governs cross-border inter-company transactions and sets the "normal value" as the principle constituting the statutory basis for the determination of the arm's length value.

In light of the above, it seems difficult to share the outcome reached by the Supreme Court in holding that Art. 110(7) of the ITC is a pure anti-avoidance provision; rather it is should be seen mainly as a provision related to the valuation of business income items aimed at properly ascertaining the taxable base. In the meantime, the authors are of the opinion that transfer pricing provisions might be used as an anti-avoidance tool aimed at tackling abusive practices by means of shifting income to foreign jurisdictions.[23]

Such an interpretation seems to be supported by the 1995 OECD Guidelines, which stipulate that the arm's length principle, as endorsed in transfer pricing regulations, serves the dual objective of "…securing the appropriate tax base in each jurisdiction and avoiding double taxation…".[24] Thus, the Guidelines do not emphasize a true anti-avoidance meaning in transfer pricing provisions, although both the taxpayer and the tax authorities "should endeavour to make a good faith showing that their determinations of transfer pricing are consistent with the arm's length principle regardless of where the burden of proof lies".[25] As a further remark, the 1995 OECD Guidelines note that " transfer pricing issues originally arose in dealings between associated enterprises operating within the same tax jurisdiction".[26] In some countries, transfer pricing provisions still apply also to domestic transactions[27] and not only to transactions between a resident taxpayer and a non-resident related party.[28]

It is also peculiar that the Court concluded that in order to successfully adjust the taxpayer's taxable income, the tax authorities should have proved that the effective tax burden in the country in which the income was shifted was less than that in Italy at the time when the transaction occurred. The Court's decision reveals that this conclusion is based on the Supreme Court's interpretation of Art. 110(7) of the ITC as an anti-avoidance provision. For the time being, the tax authorities have disregarded the validity of a transaction for anti-avoidance purposes if the transaction is carried out with the sole purpose of achieving undue tax advantages in the absence of valid economic reasons. Then, this analysis has always been carried out by looking only at the domestic effects, irrespective of the result achieved in the other jurisdiction involved.[29]

This gives rise to the questions of whether the Supreme Court's conclusion should be upheld in interpreting the transfer pricing rule as an anti-avoidance provision, such that the tax authorities need to verify the effective tax burden in the countries of residence of the other group companies in order to increase the taxable income for transfer pricing purposes or to disallow tax advantages achieved through avoidance schemes. For transfer pricing purposes, the tax authorities may increase the taxable income of a taxpayer on the basis of the arm's length value, if the arm's length value is greater than that agreed in the relevant transactions, regardless of the effective tax burden in the country of residence of the counter-party. Furthermore, the Supreme Court did not clarify what constitutes a lower effective tax burden, and the interpretation of this concept can become very difficult. If one considers the case at hand, the counterparties involved were resident in Germany, Spain and the United Kingdom, which in principle cannot be regarded as countries having an effective tax burden lower than Italy. Therefore, it is difficult to understand the true implications of the Supreme Court's decision.

If the view of the Supreme Court is interpreted as a development of more fundamental principles applicable to anti-avoidance, it should be seen as a first step towards an overall approach[30] rather than a per-country approach.[31,32] These two approaches are currently under debate following recent ECJ cases.

4.3. Abuse of law

The Italian Supreme Court referred to the concept of abuse of law as stated in recent ECJ decisions,[33] particularly *Emsland-Starke GmbH*.[34] In the authors' opinion, reference to the concept of abuse of law is not relevant to the case at hand, as transfer pricing rules do not have their source in Community law.

In *Centros*,[35] as cited in the Advocate-General's conclusion in *Halifax*, clarification was provided regarding the

22. With regard to the transactions subject to transfer pricing rules, it is assumed that valid economic reasons exist and that the issue is the value at which such commercial transactions have been carried out.
23. See G. Zizzo, "Le regole generali per la determinazione del reddito di impresa", *Giurisprudenza sistematica di diritto tributario*, *Imposta sul reddito delle persone fisiche*, *II* (Torino, 1994), at 378.
24. OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines), 1995-2000, Preface, Para. 7.
25. See Para. 5.2, Chap. 5, OECD Guidelines.
26. Para. 12 OECD Guidelines.
27. In this regard, see G. Maisto, IFA General Report 1992 Cancun, "Transfer pricing in the absence of comparable market prices".
28. In this regard, the Italian Supreme Court expressly stated that transfer pricing provisions do not apply to intra-group domestic transactions.
29. In this regard, as far as the CFC rules go, anti-tax haven legislation and the presumption of residence in Italy of trusts apply on the assumption that entities in low-tax jurisdiction are involved.
30. E.g. in *Finanzamt Köln-Altstadt v. Roland Schumacker*, C-279/93 (regarding personal tax allowances), *Marks & Spencer v. David Halsey (HM Inspector of Tax)* (*Marks & Spencer*), C-446/03 (regarding foreign losses of a multinational) and Advocate-General Léger's opinion in *Hans-Jürgen Ritter-Coulais and Monique Ritter-Coulais v. Finanzamt Germersheim* (*Ritter*), C-152/03 (regarding source-based deductions) the ECJ did consider the tax treatment in more than a single Member State (referred to as the overall approach).
31. See *Fokus Bank v. The Norwegian State* (*Fokus Bank*), Court of the European Free Trade Association, E-1/04, 23 November 2004.
32. See Dennis Weber, "In search of a (New) Equilibrium Between Tax Sovereignty and the Freedom of Movement Within the EC", 34 *Intertax* 12 (2006), at 585.
33. See e.g. *Halifax*, note 3; *Centros Ltd v. Erhvervs- og Selskabbstyrelsen* (*Centros*), C-212/97; *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd* (*Inspire Art*), C-167/01 and *X and Y v. Riksskatteverket*, C-436/00.
34. Note 5.
35. Note 33.

context in which the concept of abuse has been utilized by the ECJ, namely when Community law provisions are:

– abusively invoked in order to evade national law; or
– abusively relied upon in order to gain advantages in a manner that conflicts with the purposes and aims of those same provisions.

A general principle that can be drawn from *Centros*, is that Community law may not be relied upon for abusive or fraudulent purposes. However, this broad principle is not, by itself, a useful tool for determining whether a right arising from a specific provision of Community law is being exploited abusively. As a consequence, the Advocate-General in *Halifax* pointed out that:

> [the] Court has developed the parameter according to which that assessment is to be made at national level. First, the assessment of the abuse must be based on objective evidence. Second, and most importantly, it must be made in conformity with the purpose and objectives of the provision of Community law allegedly relied upon in an abusive way. In this regard, in so far as the determination of such a purpose is a matter of interpretation, the Court has in several cases expressly excluded the existence of an abuse.[36]

In *Emsland Starke*, cited by the Italian Supreme Court, the ECJ went a step further in formulating a more developed Community law doctrine of abuse. In particular, the ECJ in *Emsland Starke* noted that two elements must be present in order to establish the existence of an abuse of Community law in this area. The first corresponds to the subjective element, interpreted as it aims at ascertaining the purpose of the activities in question. That purpose is to be objectively determined on the basis of the absence of any other economic justification for the activity than that of creating a tax advantage. The second element corresponds to the objective element, whereby the purpose and objectives of the Community rules allegedly being abused are compared with the purpose and results achieved by the activity at issue. As the Advocate-General in *Halifax* pointed out:

> this second element is important, not only because it provides the standard upon which the purpose and results of the activity in question are to be assessed. It also provides a safeguard for those instances where the sole purpose of the activity might be to diminish tax liability but where that purpose is actually a result of a choice between different tax regimes that the Community legislature intended to leave open. Therefore, where there is no contradiction between recognition of the claim made by the taxable person and the aims and results pursued by the legal provision invoked, no abuse can be asserted.[37]

The concept of abuse of law would no longer be relevant where the economic activity carried out may have some justification other than the mere attainment of tax advantages over the tax authorities.

Other relevant considerations in this context include the following:

– the statement of the Advocate-General in *Zhu and Chen*[38] indicates that in order to conclude that there has been an abuse of a particular right, it must be ascertained whether the person concerned, by invoking the Community provision which grants the right in question, is betraying its spirit and scope. The test for the abuse is therefore, essentially, whether or not there has been a distortion of the purposes and objectives of the Community provision which grants the right in question;[39]
– in *Centros*, the ECJ noted that national courts may, on a case-by-case basis and based on objective evidence, take account of abusive or fraudulent conduct of the persons concerned in order (where appropriate) to deny them the benefit of the provisions of Community law on which they seek to rely. However, the national courts must nevertheless assess such conduct in light of the objectives pursued by those provisions;[40] and
– in *Emsland Starke*[41] the ECJ referred to a combination of objective circumstances in which, despite formal compliance with the conditions specified under the Community rules, the purpose of those rules has not been achieved.

In all of the above circumstances, the concept of abuse of law operates as a principle governing the interpretation of Community law as stated by the Commission in its written observations[42] and expressly shared by the Advocate-General in *Halifax* case.[43] Therefore, in the authors' opinion, the reference made by the Italian Supreme Court to the Community concept of abuse of law is not appropriate in the case at hand, as there is neither Community law to be interpreted (even in connection with a domestic law), nor a violation of a principle stated in a Community law based on the wording of the Italian Supreme Court decision.

On the other hand, if the position of the Supreme Court is to apply indirectly the domestic anti-avoidance provisions to transactions which are not expressly listed in such provisions (i.e. those contained in Art. 37-*bis* of Presidential Decree 600/73) on the basis of the broader concept of abuse of law (as it does not refer to a number of listed transactions, but is a general principle), it is doubtful whether such an interpretation can be justified. In fact, even if abuse of law is a general principle and, as such, may be utilized as a guideline for interpreting or implementing domestic provisions,[44] such a concept of

36. See Para. 65, statement of the Advocate-General Mr Maduro, in *Halifax*, note 3.
37. See Para. 88, statement of the Advocate-General Mr Maduro, in *Halifax*, note 3.
38. *Zhu and Chen v. Secretary of State for the Home Department*, C-200/02, statement of Advocate-General, point 114.
39. Id., point 116.
40. *Centros*, note 33, at point 25.
41. Note 34, at point 52.
42. See to that effect A. Kjellgren, "On the Border of Abuse", *European Business Law Review* (2000), at 192.
43. *Halifax*, note 3, at Sec. 69.
44. In this regard, see Advocate-General Maduro at point 90 of his statement in *Halifax*. ("This, however, will require the adoption of appropriate national legislative measures. Mere interpretation will not suffice. Such measures might include more general anti-abuse provisions of the kind adopted in some Member States, that are applicable inter alia to VAT, which may differ, either in their scope, modus operandi or effects, from the operation in the field of VAT of the interpretative Community law principle of the prohibition of abuse. In any case, such legislation must comply with the Article 27 procedure and the limits laid down in that regard by the Court".)

abuse of law may be cited by judges in interpreting domestic provisions that do not have their source in Community law.

With regard to the Italian case at hand, the principle found in domestic anti-avoidance legislation, as provided for by Art. 37-*bis* of Presidential Decree 600/73, is very close to the interpretation of abuse of law given by the ECJ. However, as previously noted, the Italian legislature chose to apply this provision only to a number of transactions expressly listed in Para. 3 of Art. 37-*bis*, amongst which commercial transactions carried out between affiliated companies, as those at issue, are not included. Therefore, the Supreme Court should not make reference to the ECJ concept of abuse of law to classify Art. 110(7) of the ITC as an anti-avoidance provision, while, from a legislative perspective, the choice was made not to include the relevant transaction for purposes of Art. 110(7) of the ITC in the domestic anti-avoidance provision.

5. Conclusion

The last few years have seen a growing trend of tax auditing and litigation with regard to both anti-abuse and international tax matters. This trend has led to an increasing number of Supreme Court decisions, the outcome of which has sometimes surprised scholars and practitioners, and has opened room for further debate (and tax litigation) on some general issues, such as tax residence of companies and individuals; permanent establishments; the relationship between domestic legislation and EU directives; the application of anti-avoidance principles in an international context and in treaty situations; and reliance on OECD principles in interpreting domestic tax rules. The decision of the Italian Supreme Court is a notable example of this trend. The Supreme Court affirmed that transfer pricing rules have an anti-avoidance nature, and from that the Court has drawn two main conclusions: (1) the burden with regard to proof in transfer pricing disputes rests with tax authorities and (2) the tax authorities must prove that the prices agreed upon by the parties have led to an overall tax saving, considering both Italian and foreign taxes and taking into account taxes due by both parties, rather than by the Italian taxpayer only.

Quite surprisingly, however, such far-reaching conclusions derive from a principle (the anti-abusive nature of transfer pricing rules), which is assumed without in-depth motivations. In the long run, this attitude situation is welcome, since it obliges scholars to a more critical analysis on matters that until few years ago were given for granted; in the short run, however, this leads to a significant uncertainty on taxpayers. The trend is traced but the impression is that some of the assumptions and conclusions of the Supreme Court will further be modelled in the future, maybe by the Supreme Court itself.[45]

45 See Supreme Court decisions 12302 of 24 May 2006; 12301 of 24 May 2006; 22932 of 14 November 2005; 22932 of 14 November 2005; and 20398 of 26 October 2005.