



Hybrid mismatches: clarification of penalty protection documentation contents, deadlines and methodology

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A Ministerial Decree of 6 December 2024 (the “Decree”) has clarified the rules on documentary evidence of analyses conducted in order to apply hybrid mismatch rules and obtain protection against penalties for incorrect income tax returns (the “Documentation”). It defines the contents of the Documentation and how and when it should be prepared and reported. The Decree, which is of undoubted interest, even clarifying certain substantive aspects of the rules, allows taxpayers to “shield” fiscal years prior to 2024 by preparing Documentation no later than the filing date for the 2024 income tax return (31 October 2025, for calendar-year taxpayers). For the 2020-2022 fiscal years only, it is necessary to prepare Documentation with a time stamp by 30 June 2025.

The Documentation

The Decree implements article 61 of Legislative Decree no. 209/2023, which, by adding paragraph 6-bis to article 1 of Legislative Decree no. 471/1997, introduced special penalty protection for hybrid mismatches. More specifically, in the event of a dispute about hybrid mismatch rules that results in higher tax or a lower tax credit, no penalty will be applied if, during the search, inspection, audit or other investigation, the taxpayer presents the Italian Revenue Agency with appropriate documentation enabling it to verify that the rules neutralising hybrid mismatches have been applied. The Decree, which comprises 13 articles and three annexes, indicates which taxpayers are subject to the rules and the analytical approach to identifying relevant transactions (or homogeneous sets of relevant transactions). It also defines the structure, format, contents and validity of the Documentation, as well as the deadlines by which it must be prepared and delivered. There are specific Documentation rules for the transitional period and for taxpayers who have adhered to the cooperative compliance program.

Who the rules apply to

The anti-hybrid-rules apply to all parties liable to IRES corporate income tax (both residents and - if they have a PE in Italy - non-residents) that have cross-border transactions, irrespective of the sector in which they operate (financial or industrial). Therefore, the Documentation can be prepared by any party resident or established in Italy. With the declared intent of “limiting the administrative burden associated with the Documentation”, the Decree allows multinational groups to delegate the preparation and reporting of the Documentation to a single taxpayer (the “appointee”).

Criteria for identifying relevant hybrid mismatches

The Decree stipulates that, in identifying transactions that generate or are reasonably likely to generate a “relevant hybrid mismatch”, it is necessary to describe the process of analysis used. The process must mirror that described in Annex B of the Decree and the description must provide the information and essential details indicated in Annex A. It is important to note that the Decree allows analyses to be conducted for “homogenous sets” of relevant transactions, a “homogeneous set” being a set of transactions that (i) take place in the same fiscal year with the same party/different parties, related to the taxpayer or otherwise, and (ii) have an identical or substantially identical legal and economic impact on the taxpayer, and (iii) receive the same treatment under anti-hybrid rules. Purely by way of example, the explanatory report identifies the following homogeneous sets: AT1s, convertible bonds, subordinated loans, interest-free loans and zero coupons.

Structure, content and form of the Documentation

Documentation, presented for a single fiscal year, must provide relevant information about the transactions which the taxpayer intends to shield from penalties. The structure of the Documentation is described in Annex A of the Decree (see table below).

1. Information on the multinational group <ul style="list-style-type: none">- The multinational group- The enterprises in the multinational group- Tax status of the enterprise, other than a permanent establishment, in the jurisdiction of incorporation or tax residence and in the jurisdiction where the shareholders or investors are resident- Permanent establishment- Tax group
2. Taxpayer <ul style="list-style-type: none">- The taxpayer's particulars- Tax residence- Tax status of the enterprise, other than a permanent establishment, in Italy and in the jurisdictions where its shareholders or investors are resident- Recognition of a permanent establishment in Italy- Recognition of a permanent establishment abroad
3. Description of the process
4. Relevant transactions <p><i>Relevant transaction no. [•]</i></p> <ul style="list-style-type: none">- Parties involved in the relevant transaction- Relevant hybrid mismatch- Analysis and identification of, and reaction to, the relevant hybrid mismatch- Documentary evidence <p><i>Relevant multiple transaction</i></p> <ul style="list-style-type: none">- Description of the multiple relevant transaction- Parties involved in the relevant multiple transaction- Analysis and identification of, and reaction to, the relevant hybrid mismatch- Documentary evidence

The Documentation must be prepared in Italian and electronically signed by the taxpayer's legal representative (or appointee) with a time stamp that must be affixed no later than the filing deadline for the income tax return of the fiscal year covered by the Documentation, or the later deadline for a supplementary return. An exception is made for the fiscal year in progress on 29 December 2023 (FY 2023, for calendar-year taxpayers). In this case, the deadline for preparing, signing and time stamping the Documentation is the filing deadline for the fiscal year in progress on the date the Decree comes into force (FY 2024, for calendar-year taxpayers), whereas for the 2020-2022 fiscal years the deadline is 30 June 2025. The Documentation must be in electronic format and reach the Italian Revenue Agency within 20 business days of request. Moreover, the taxpayer must report to the Italian Revenue Agency that it possesses the Documentation by flagging this in the income tax return for the fiscal year covered by the Documentation.

Documentation for FYs 2020, 2021, 2022 and 2023 must be reported in the 2025 income tax return (for FY 2024).

Penalty protection

The preparation and reporting of Documentation to the Italian Revenue Agency protects **the taxpayer against penalties for an incorrect return**, in respect of the relevant transactions or sets of transactions. Failure to include a relevant transaction in the Documentation, or its inadequate description in the Documentation, does not invalidate the Documentation in respect of the other transactions included in it. As emphasised by the explanatory report accompanying the Decree, "this allows the taxpayer, in respect of Relevant Transactions that may give rise to so-called direct hybrid mismatches, to select transactions for penalty

protection", this protection not being conditional on the identification and description of all the taxpayer's relevant transactions.

The Documentation for one or more periods prior to 29 December 2023 will give penalty protection for hybrid mismatches if (a) it has been prepared and time stamped within the filing deadline for the FY 2024 return, and (b) the taxpayer has not been notified of any violation of the hybrid mismatch rules in connection with the relevant transactions (or sets of transactions) included in the Documentation, and (c) no search, inspection, audit or other inquiries about those transactions have begun and have been formally brought to the attention of the originator or co-obligors of the transactions.

Cooperative compliance taxpayers

The Decree includes certain specific provisions applicable to cooperative compliance taxpayers. In particular, it makes the preparation and reporting of the Documentation part of a cooperative compliance taxpayer's duties. Essentially, in their case, preparation and reporting become "compulsory" when relevant transactions above the materiality threshold are detected. Vice versa, if there are no relevant transactions above the materiality threshold, preparation and reporting of the Documentation remain optional, provided that the Tax Risk & Control Matrix (TRCM) includes suitable mechanisms to identify, measure and manage the risks associated with the relevant transactions.

Documentation will also give penalty protection to relevant transactions (or sets of transactions) below the materiality threshold, even if they are not included in the Documentation. This is provided that the TRCM maps the business processes that can identify relevant transactions for the purposes of anti-hybrid rules.

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