

European Business Initiative on Taxation (EBIT)

Comments on the OECD's Discussion Draft on

**BEPS ACTION 10: PROPOSED MODIFICATIONS TO CHAPTER VII
OF THE TRANSFER PRICING GUIDELINES RELATING TO LOW
VALUE-ADDING INTRA-GROUP SERVICES**

At the time of writing this submission, EBIT Members included: AIRBUS, BP, CATERPILLAR, DEUTSCHE LUFTHANSA, DIAGEO, INFORMA, JTI, LDC, MTU, NUTRECO, REED ELSEVIER, ROLLS-ROYCE, SAMSUNG ELECTRONICS, SCA, SCHRODERS and TUPPERWARE.

EBIT Comments on BEPS ACTION 10: Proposed modifications to Chapter VII of the Transfer Pricing Guidelines relating to low value-adding intra-group services

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Submitted by email to: TransferPricing@oecd.org

Brussels, 14 January 2015

Dear Andrew,

EBIT is grateful for this opportunity to provide comments on the OECD Public Discussion Draft entitled BEPS ACTION 10: Proposed modifications to Chapter VII of the Transfer Pricing Guidelines relating to low value-adding intra-group services (hereinafter “the Discussion Draft”).

General comments

EBIT welcomes this overall rather well-written, even-handed and nuanced Discussion Draft as a very good basis for revision of Chapter VII of the Transfer Pricing Guidelines in respect of low value-adding intra-group services, and in our view the OECD is on the right track here.

We also support in principle the proposed elective simplified transfer pricing methodology for low value-adding intra-group services but there are some practical issues.

EBIT Members believe that for this approach to really work, it is essential that all BEPS-44 will implement this elective approach for companies and in a consistent manner.

Specific comments

B.1.2 Shareholder activities

7.10-7.11: EBIT welcomes further clarification of the distinctions drawn between shareholder activities, stewardship activities and other direct and indirect services that are provided within a group.

B.1.3. Duplication

7.12: EBIT generally supports the OECD’s proposed additions regarding the possible duplication of services.

B.1.6 Form of remuneration

7.19: The OECD should preferably clarify the seeming contradiction between paragraphs 7.19 and 7.61: the latter requires “written contracts or agreements for the provision of services” whereas in paragraph 7.19 it is mentioned that “the absence of payments or contractual

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agreements does not automatically lead to the conclusion that no intra-group services have been rendered”.

B.2.1. Determining an arm’s length charge in general

7.20: EBIT urges the OECD to add a specific reference that random limitations on deductibility of intra-group service charges should be avoided by tax administrations.

B.2.2.1 Direct-charge versus indirect charge methods

7.22-7.27: EBIT does not necessarily agree with the OECD’s assertion in the Discussion Draft that the direct-charge is the default method and to be preferred. EBIT is concerned about the prescriptive language in the following sentence:

“indirect-charge methods (...) should be allowable provided sufficient regard has been given to the value of the services to recipients and the extent to which comparable services are provided between independent enterprises. These methods of calculating charges would generally not be acceptable where specific services that form a main business activity of the enterprise are provided not only to associated enterprises but also to independent parties.”

EBIT strongly believes that MNCs should be free to decide the best method for their group structure, i.e. either one of the direct or the indirect charge methods, as long as they adhere to the agreed OECD guidance. There is simply not a “one size fits all” or default method that is suitable for all MNCs.

C. Examples of intra-group services – R&D

7.43: From our practical experience, contract R&D is part and parcel of commercial relationships between third parties operating at arm’s length, even though it may result in the value creation of an intangible owned by the IP owner who contracts out the R&D.

D2 Simplified determination of arm’s length charges for low value-adding intra-group services

7.51-7.54: EBIT in principle supports the proposed elective simplified transfer pricing methodology for low value-adding intra-group services, but at this stage of the Discussion Draft it is hard to determine whether it would be practical and beneficial. We understand that there is no consensus on this proposed methodology apparently for the moment. It is however extremely important for companies to know whether all or most tax authorities will actually implement it and whether this will be done in a consistent manner because otherwise it would defeat its purpose. EBIT is of course willing to assist the OECD in making the methodology beneficial for both business and tax administrations.

EBIT Members are concerned based on their experience that payee tax administrations sometimes allege that more of the costs incurred by MNCs in relation to management fees in the top company location(s) should be recharged to affiliates, and at higher margins, whereas their counterparts in payer jurisdictions sometimes contend that part or the entire recharged amount should be disallowed.

In addition, some of our Members have experienced that even after domestic disallowance, tax authorities in some jurisdictions have tried to brand the payment for services as ‘other income’ and therefore have imposed withholding tax on the payment. We would argue that if the expense in question is a valid business expense, in principle it seems fair that all of such costs should be able to be recharged and should be able to be deducted somewhere either at the shareholder level, or in individual subsidiaries. Further, withholding tax should be limited to the tax deductible amount.

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From our experience most of these charges are insignificant in relation to the total revenues and profits of groups yet still a huge amount of effort and cost is very often wasted to seeking agreement between payer and payee jurisdictions about relatively small amounts of tax, which should not be. EBIT would welcome more guidance by the OECD to limit the costs of compliance for companies related to this approach. There is in our view at this embryonic stage of the Discussion Draft still a big risk that companies would still have to justify their costs to tax authorities in detail even after having submitted all documentation in line with the simplified approach.

D.2.2. Allocation of low value-adding services

7.55 and 7.56: EBIT believes that the number of allocation keys needs to be small. Allocation keys are closely aligned to services, which is not satisfactory for practical purposes.

D.2.3 Profit mark-up

7.57: EBIT generally welcomes the OECD's apparent intention to provide a clear safe-harbour with a profit mark-up to all costs in the pool of 2-5%. There might be a risk that payee tax jurisdictions will assume that the upper limit proposed is the default mark-up to be used, and the payer country tax administrations will assume the opposite. This might create unwelcome uncertainty where services are provided to many jurisdictions, or for establishing a mark-up that includes all payer jurisdictions.

Guidance is therefore needed for showing that the agreed margin is consistently applied by a MNC to all low value-added services and that tax authorities do not seek to unreasonably challenge the 2-5% mark-up.

Pass-through costs should have no mark-up in our view.

EBIT members trust that the above comments are helpful and will be taken into account by the OECD in finalising its work in this area. EBIT is committed to a constructive dialogue with the OECD.

Yours sincerely,

European Business Initiative on Taxation – January 2015

For further information on EBIT, please contact its Secretariat via Bob van der Made:
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