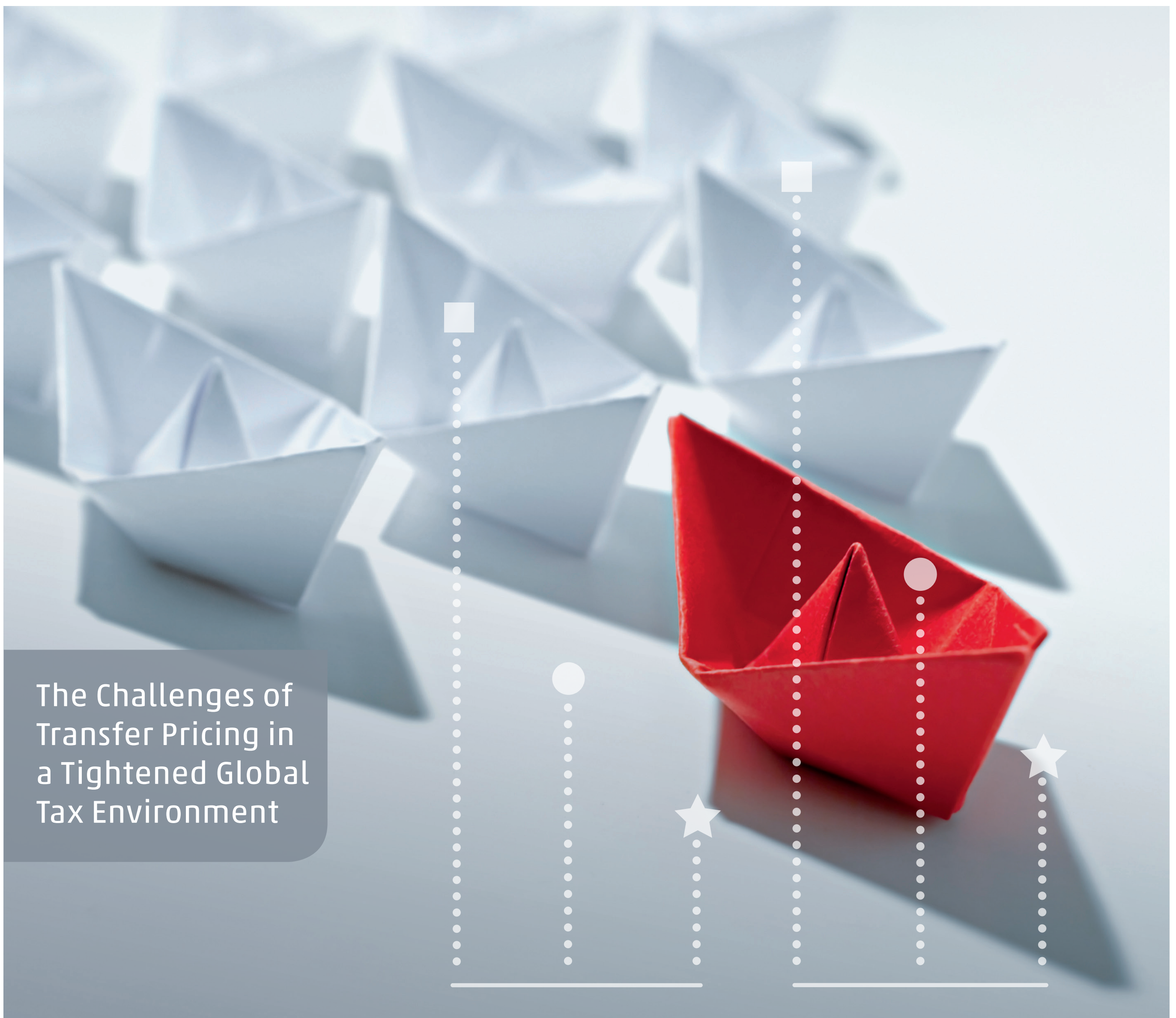
September 2014

wts TAX LEGAL CONSULTING

international wts journal

Client Information

2.2014



The Challenges of Transfer Pricing in a Tightened Global Tax Environment

Table of Contents

3 EDITORIAL

4 AUSTRALIA

5 BELGIUM

6 FRANCE

7 GERMANY

8 HUNGARY

9 INDIA

10 ITALY

11 THE NETHERLANDS

12 NORWAY

13 POLAND

14 RUSSIA

15 UNITED KINGDOM

Imprint

WTS Alliance | P.O. Box 19201
3001 BE Rotterdam | The Netherlands
info@wts.de | www.wts-alliance.com

Contact
Maik Heggmair
+49 89 28646-212
maik.heggmair@wts.de

Editorial Team
Sharon Arasu-Koh, Subhasis Banerjee, Jan Boekel, Nico Demeyere, Tamás Gyányi, Maik Heggmair, Sean Helverson, Raisa Karaseva, Filippo Federico Miotto, Marvin Rust, Maja Seliga-Kret, Dr. Christoph Seseke, Ulf H. Sørdal, Michael Wohlfahrt

Typography, Layout
hartmann brand consulting, Munich

This issue of International WTS Journal is published by WTS Alliance. The information is intended to provide general guidance with respect to the subject matter. This general guidance should not be relied on as a basis for undertaking any transaction or business decision, but rather the advice of a qualified tax consultant should be obtained based on a taxpayer's individual circumstances. Although our articles are carefully reviewed, we accept no responsibility in the event of any inaccuracy or omission. For further information please refer to the authors.

ISSN: 2214-370X

The challenges of transfer pricing in a tightened global tax environment

Dear Reader:

We are pleased to present our 2014 guide "The Challenges of Transfer Pricing in a Tightened Global Tax Environment".

Transfer pricing continues to be the number one issue for tax directors globally. The highly dynamic and unpredictable global business environment as well as the increasing pressure from international tax authorities to generate tax revenue from all sources, present tax directors of multinational companies with significant challenges in planning and documenting their intercompany transfer pricing policies. Over the last years, almost all countries around the globe have introduced or tightened their national transfer pricing regulations and, at the same time, the OECD[1] as well as the UN[2] are intensively working on new international standards and guidelines. In addition, the national interpretations of the international guidelines by local tax authorities, as well as the specific local transfer pricing regimes are not fully consistent in all countries. Especially the so called "BRIC" countries have significantly different rules and interpretations of the internationally accepted arm's length principle.

Furthermore, at the international level, tax administrations do aggressively focus on transfer pricing issues in tax audits, and the income corrections related to transfer pricing issues realized on a global level are tremendous. Such corrections principally lead to ultimate double taxation risks for the multinational companies, as international arbitration rules are not consistently implemented, and in many countries arbitration procedures are practically not available at all.

Finally, the assumed "profit shifting and tax avoidance" of multinational companies is in the centre of a fierce public discussion, and the OECD has moved its action plan against "Base Erosion and Profit Shifting (BEPS)" to the top of the agenda since early 2013. The OECD "Action Plan on Base Erosion and Profit Shifting", published in July 2013, focuses on significantly tightening the transfer pricing and documentation rules. For example, as the result of action item 13, the OECD "Discussion Draft on Transfer Pricing Documentation and Country-by-Country ("CbC") Reporting" has been issued in early 2014, which will most likely lead to a significant increase of documentation requirements for multinational companies.

Hence, it is obvious that international transfer pricing compliance is among the most complex and potentially expensive issues for multinational companies. Given the complexity of transfer pricing, this Guide can not address all relevant issues associated with the tightened challenges on transfer pricing for multinational companies.

Therefore, this guide provides a summary of certain key issues focusing on

- latest developments in the respective national TP legislation and local legal practice,
- practical experiences from current transfer pricing audits, and
- local views on the current OECD publications especially regarding BEPS and CbC reporting.

We hope that you will find our guide useful, and we thank our authors for their valuable contributions. For more information regarding transfer pricing issues in specific countries or the transfer pricing practice of WTS member firms in general, please feel free to contact us or any of our local country authors.

Maik Heggmair, Head of Transfer Pricing, Partner, WTS Germany

1 OECD "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" from 2010.
2 UN "Practical Manual on Transfer Pricing for Developing Countries" from 2012.

Recent changes in national TP legislation/jurisdiction

Australia's revised transfer pricing rules (applying to income years commencing on or after 1 July 2013) make transfer pricing a self-assessment compliance obligation and provide the Australian Taxation Office (ATO) with powers to reconstruct transactions and alter the financial results of a taxpayer. The focus on arm's length profit rather than the arm's length pricing requires the taxpayer to assess each transaction to determine if a tax advantage has been obtained in Australia because it has been undertaken on non-arm's length conditions. The ATO can reconstruct the transaction and substitute one or more elements with arm's length conditions. It is important for taxpayers to properly document and assess inter-company transactions (i.e. to confirm that 'form' and 'substance' are in agreement).

Taxpayers with gross related party dealings of greater than AU$2m must submit an International Dealings Schedule (IDS) with their Australian tax return. This IDS must disclose the type and value of dealings, and the level of transfer pricing documentation available to support the pricing of dealings (which is now required to mitigate penalties). Public Officers will need to be satisfied that their transfer pricing is arm's length for tax purposes and that they have complying documentation, given they may be held personally liable for providing misleading information. Multinational taxpayers will need to review global transfer pricing studies to ensure compliance with the Australian rules and maintain the study on Australian files. There is some good news: the new rules limit the period during which the Commissioner of Taxation may go back and amend a taxpayer's assessment to 7 years (there was no time limit under the old rules).

Practical experience from actual TP audits

The ATO's decentralized model of managing transfer pricing (where issues are managed by field auditors with insufficient transfer pricing expertise, with some support from specialists) has led to inefficiencies in audits and a blow out in the ATO's timeline for progressing reviews, which is proving to be frustrating and costly to both taxpayers and tax advisers. Instead of engaging in meaningful discussions with the taxpayer, the ATO issues voluminous information requests and undertakes its own analysis and position, in some cases being quick to dismiss the taxpayer's analysis and choice of methodology prior to engaging in dialogue and negotiation with the taxpayer.

Given the new legislation forms the cornerstone to Australia's base erosion and profit shifting strategy (BEPS), it is likely that the ATO will seek to test the new rules soon. Multinational taxpayers and high risk taxpayers, in particular, should review their transfer pricing documentation as soon as possible to ensure compliance prior to lodgment of its tax return and IDS.

Local view on BEPS discussion, especially considering proposed changes to TP documentation and country-by-country reporting

Australia has taken a lead on some of the proposals in the OECD's Action Plan (e.g. tax disclosure requirements for large companies, changes to documentation requirements and a review of debt/equity rules), and the ATO's 2013-14 Compliance Program has a strong focus on BEPS. Whilst the OECD's master file (country-by-country) documentation approach is not required under the new transfer pricing rules, taxpayer's are unable to rely on "reasonably arguable position" penalty protection provisions unless they have adequate and current transfer pricing documentation in place. The documentation rules require that taxpayers review and identify their arm's length profits consistent with 'relevant guidance materials' which include the OECD's Transfer Pricing Guidelines. It is understood that Australia may consider the future policy response to country-by-country reporting once the OECD guidelines have been finalized, but care needs to be taken to balance information needs with the taxpayer's cost of compliance.

Contact Person

Sharon Arasu-Koh
sharon.arasu-koh@wtsaustralia.com.au
+613 9939 4488

34 Queen Street
Melbourne VICTORIA 3004
Australia
www.wtsaustralia.com.au

Recent changes in national TP legislation/jurisdiction

During recent years, transfer pricing has become a hot issue on the agenda of the Belgian tax authorities. Where in the past there was only one specialised transfer pricing audit team for the whole country, the Belgian tax authorities have now rolled out skilled transfer pricing audit teams in the major regions. New auditing techniques (including data mining) have also been used to select companies to be audited.

The activities of the specialised local transfer pricing teams make it likely that a Belgian subsidiary of a MNE would be audited, especially if the Belgian subsidiary is in a (structural) loss position, or has important financial flows with related foreign entities. Such special transfer pricing audits may be time consuming, and may require substantial management resources. Moreover, corrections may be communicated to tax authorities, triggering audits in other jurisdictions.

Belgian tax law does not impose formal transfer pricing documentation rules. Each taxpayer is expected to act as a "good businessman", seeking full compliance with the arm's length principle. In order to mitigate risks, it is advisable to be proactive in documenting the arm's length nature of intercompany transactions. In order to have upfront legal certainty on the transfer pricing method to be used, an upfront ruling can be applied for with the central tax authorities.

Management fees paid to foreign related entities are examined in depth during transfer pricing audits. It is of the utmost importance that the Belgian entity can demonstrate that services have actually been rendered, that benefit was derived from these services and that the service fee is arm's length.

Profit allocation to permanent establishments based on AOA

In a recent amendment to the double taxation treaty concluded between Belgium and Switzerland, the existing article 7 on profit allocation to permanent establishments (PEs) has been revamped, as to reflect the Authorised OECD Approach (AOA) for profit allocation to permanent establishments. When discussing rulings or agreements, tax authorities insist on using a method in line with the AOA, including cases where the applicable double taxation treaty has not been amended.

The AOA calculates the profit attributable to a PE as if it were a separate entity. Hence, it is possible that profit has to be attributed to a PE in Belgium while the whole enterprise is suffering losses. This new approach may be relevant if e.g. a German enterprise is realising a construction or installation project in Belgium. It is possible that the supervision of work performed by subcontractors constitutes a PE in Belgium. The cost plus method is often used to attribute profit to this PE. It is then possible that Belgian corporate income tax is due on the PE's profit, even if the project is creating loss on an aggregate basis.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

The Belgian administration is typically an early adopter of new insights developed at the level of the OECD. The tax authorities refer to the amended guidelines on transfer pricing and intangibles (chapter 6) during audits.

No changes to the existing transfer pricing documentation guidelines have been announced. It can be expected that the other BEPS initiatives, including the country-by-country reporting, will be transposed in Belgian law. The current practise note on transfer pricing documentation would have to be replaced. However, requiring a Belgian company to communicate financial information on foreign related entities would require a fundamental change of the Belgian income tax code.

Contact Person

Nico Demeyere
nico.demeyere@tiberghien.com
+32 2 773 40 13

Tour & Taxis
Havenlaan 86C/419
1000 Brussels
Belgium
www.tiberghien.com

The Challenges of Transfer Pricing in France

Recent changes in national TP legislation/jurisdiction

In 2013, France intensified its fight against tax evasion, and has introduced several new requirements within the framework of transfer pricing. A filing obligation and a new disclosure have been enacted in the "Law against tax fraud and economic and financial crime", and in the tax bill for 2014.

Since 2010, large companies (with gross annual turnover or gross assets equal to or exceeding € 400 million, or which hold or are held by, directly or indirectly, a legal entity exceeding the above mentioned thresholds) have to prepare a contemporaneous transfer pricing documentation. This transfer pricing documentation must be available on the first day of the tax audit. Beginning in 2014, according to the new provision, these large companies will be also required to file a "light" transfer pricing documentation with the French Tax Authorities. This light documentation must be filed within six months following the deadline for filing their annual income tax return (f.i. for companies closing on December 31st, 2013, the deadline expires on November 5th, 2014). This light documentation includes extracts from the full transfer pricing documentation and mainly concerns inter-company transactions exceeding € 100,000.

Moreover, large companies also have to disclose in the full documentation the tax rulings obtained by associated companies from foreign tax authorities. Tax rulings in this respect are considered to be individual, and specific decisions issued by foreign tax authorities are binding to those local tax authorities. This new requirement will certainly be very difficult to fulfill by French companies, as this information is not easily available within a group. Furthermore, these decisions are sometimes considered to be confidential information by foreign tax authorities, and companies are not permitted to disclose them.

Practical experiences from actual TP audits

As indicated in the French tax authorities' guidelines, transfer pricing issues are a main part of the tax audit. According to the French tax authorities, the tax inspector must be sure that the income reported in France by the company is consistent with the activity actually performed in France.

Regarding large companies, the first consequence of the tightening of the legislation is fines for incomplete documentation or failure to provide the documentation. Depending on the seriousness of the failure, the tax inspector applies a penalty that could amount to up to five per cent of the income transferred.

Even if the formal transfer pricing documentation only concerns large companies, smaller companies are increasingly challenged on their transfer prices, and are required to justify their transfer pricing policy. Transfer pricing issues are also deeply analyzed in the context of business restructuring.

Regarding APA (Advance Pricing Agreement) in the future, fees might be charged to the taxpayer. Indeed, this possibility is currently explored by the French tax Administration MEIJEI (Mission d'expertise juridique et économique internationale), which is considering the increase of the costs incurred.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

The "master file" is only the first part of the documentation required by the French tax law. Additional specific information on the French company and its transfer pricing policy are also required.

Regarding the country-by-country reporting, France implemented the article 89 of CRD IV. Under new regulation codified in article L511-45 of the French monetary and financial code, credit institutions, investment firms, financial companies, and mixed financial holding companies have to disclose yearly specific information regarding their sites and activities located in non-cooperative states (name, business activity, turnover and net banking revenue, number of employees, profit or loss before tax, tax on profit due and public subsidies received).

Contact Person

Dr. Christoph Seseke
christoph.seseke@wtsf.fr
+33 1 42 27 05 38

57 Avenue de Villiers
75017 Paris
France
www.wtsf.fr

GERMANY
WTS STEUERBERATUNGS-
GESELLSCHAFT MBH

Recent changes in national TP legislation/jurisdiction

The main topic in the German TP legislation was the introduction of the "Authorized OECD Approach" to German tax law (German Foreign Tax Act), regarding the taxation of permanent establishments ("PEs") for fiscal years beginning January 1, 2013 onwards, followed by a draft decree regarding the execution of this new legislation. The new German legislation is based on the OECD "Report on the Attribution of Profits to PEs" from 2010, and clearly outlines that the "separate legal entity approach" has to be applied for the income allocation to PEs, and that all transactions and dealings between Headquarter and PE have to be executed applying the arm's length principle. Additionally, the new regulations contain a more detailed approach to the profit allocation, as well as additional documentation requirements for the taxpayers, resulting in significant additional tax compliance efforts.

Practical experiences from actual TP audits

Transfer pricing remains the key tax challenge for German multinational companies and German tax authorities. In short, transfer pricing issues are of highest priority in German tax audits. German tax auditors have become more trained and specialised over the last years since the implementation of the legal documentation requirements, and the audit approach on transfer pricing issues is getting more aggressive and demanding.

Especially management services and licence fees are often in the focus of the auditors. On the one hand the documentation requirements regarding the deductibility of management service fees charged to German subsidiaries of foreign groups are very high. On the other hand, the auditors expect that a significant share of the central cost of German headquarters is charged out to the foreign subsidiaries. Furthermore, German tax auditors are increasingly tending to request a license fee to be paid by the foreign subsidiaries of a German group for the use of the so called "umbrella brand". This "umbrella brand" should constitute a compensation for the bundle of different services and intangibles, which German tax auditors assume to be rendered and respectively granted to foreign subsidiaries by the German headquarters (e.g. consisting of global reputation, various know-how and expertise, quality standards, running organisation, etc). Finally, although there is a strict penalty regime on non-compliance with the transfer pricing documentation rules under German law, the actual assessment of penalties during tax audits has been relatively conservative in practice, until now. However, it is expected that the assessment of penalties related to missing or insufficient transfer pricing documentation will increase over the next years.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

Generally, a master file documentation approach as proposed by the OECD is already accepted in Germany. Therefore, it can be expected that the German tax authorities would accept the OECD's proposals, and also adopt the new OECD standards for the German legal documentation requirements. However, the proposed extent of relevant information, especially regarding the so called "country-by-country reporting, is also seen very critically by the German tax administration. It is acknowledged that the disclosure obligations proposed by the OECD could contradict the legally protected tax secrecy, and that significant additional tax compliance efforts have to be expected for the taxpayers, whereas the relevance of the additional information provided could be challenged. There is also discussion of whether the CbC-Reporting proposed by the OECD may be seen as the starting point for the introduction of a formula apportionment of profits, rather than as a transaction based setting of transfer prices in line with the arm's length principle, which has been the common standard of the OECD over the last decades.

Contact Person

Maik Heggmair
maik.heggmair@wts.de
+49 89 28646-212

Thomas-Wimmer-Ring 1–3
80539 Munich
Germany
www.wts.de

Recent changes in national TP legislation/jurisdiction

The Hungarian national TP legislation has changed regularly in recent years; the OECD guidelines and its amendments were always an indicator for the amendments. The modifications in recent years, as well as the latest changes in June 2013 mostly aim to ease the TP documentation burden for Hungarian companies.

According to the latest amendments in the Hungarian TP legislation, if the transactional value does not exceed HUF 50 million (approx. EUR 160,000, excluding VAT) in a given tax year, then no TP documentation needs to be prepared to support the pricing applied between the related parties. Earlier, the above mentioned threshold had to be observed and aggregated from the date when the parties concluded the agreement, resulting in an increased administration in the past.

Practical experiences from actual TP audits

It can be definitely stated that transfer pricing is still a key issue during full-scope tax audits performed by Hungarian companies. Also, there are special tax audits targeting only transfer pricing matters. During the past couple of years, tax auditors have become more trained and qualified; transfer pricing audits have therefore become more thorough and very challenging for companies.

Numerous western European industrial companies have affiliates in Hungary acting as contract manufacturers or toll manufacturers. During tax inspections, the pricing methods applied and the level of profitability were always crucial points. According to the latest law amendments, the allocation keys that are used in intra-group services (e.g. software licence fees are typical whereas the number of IT users is usually applied as an allocation key) should be documented precisely.

The database used by benchmark studies should also be chosen by keeping an eye on the TP legislation. One of the internationally accepted databases is used by the tax inspectors to set the market based pricing, and thus challenge the prices applied by related parties. To sum up, there are numerous fields that have been in focus in the recent years, and it is expected these areas will remain within the top issues.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

The so-called master file concept was introduced by Hungary in 2010, having the obligation to prepare a country specific part. However, this concept is used in rare cases by taxpayers due to the additional administration requirement. Based on Hungarian regulations, TP documentation has to be prepared by the filing of the corporation tax return for the respective tax year (the final deadline is in five months, calculated from year end). The strict deadline may result in timing difficulties for completing the master file, as other countries may apply more liberal regulations for the preparation deadline. Therefore, companies might face difficulties when completing their master file, especially when information from various group companies needs to be collected and processed for the concept.

With regards to the "country-by-country reporting", the published model template for the reporting seems to be very detailed, and some elements seem to be highly confidential and very sensitive, even within the group. The administration burden on Hungarian companies, in connection with TP matters, is already "very heavy", but the Hungarian tax administration was always keen to introduce rules that increase information exchange among tax administrations, and thus boost tax income and penalties.

Contact Person

Tamás Gyányi
tamas.gyanyi@klient.hu
+36 1 887 3736

Stefánia út 101-103.
1143 Budapest
Hungary
www.klient.hu

Recent changes in national TP legislation/jurisdiction

Indian TP legislation introduced 'Advance Pricing Agreement (APA)' and 'Safe Harbor Rules' to Indian Tax law along with specific clarification on mark up for captive service providers. APA is an arrangement between the tax payer and the tax authority covering future transactions, with an approach of solving the potential transfer pricing disputes in a cooperative manner. To reduce increasing the number of prolonged transfer pricing disputes, the tax authority notified the acceptable mark up in eligible International Transactions, known as Safe Harbour Rules (SHR). The purpose of SHR is to provide long term certainty and greater flexibility to tax payers. In the IT sector, captive services have been the hot bed of controversies. Transfer Pricing Officers (TPO) are treating tax payers who are engaged in contract research and development activities with insignificant risks, as full or significant risk bearing entities, and hence insist on higher mark-ups in the range of 25%- 30%, against a market average of 14%-18% for such development centers. To resolve these disputes the government has come out with a clarification designed to determine the risk status of development centers.

Practical experiences from actual TP audit

Risk adjustments have become more of a routine adjustment in transfer pricing reports filed with the IT department. There are numerous ongoing transfer pricing disputes in India, which could be broadly classified under the following heads:

→ Determination of the margins of the tested party (e.g. pass through cost)
→ Non availability of comparables and comparability issues
→ Risk adjustment
→ Intangibles and financial transactions
→ Valuation of shares (The difference in share valuation is being treated as interest free loan)

The latest controversy is where the tax authorities are treating the share application money, advanced by an Indian Entity to its Associated Enterprises (AE), as an interest free loan.Recently, the Indian tax court has rejected the adjustment of notional interest made by the TPO, by recharacterizing share application money as an interest free loan. Lately, Indian tax authorities have been taking measures to reduce the value of transfer pricing adjustments. The larger measures include the introduction of safe harbor rules, and the conclusion of the first set of the Advance Pricing Agreement (APA) program in a record time frame, in order to give the right signal to the tax payers.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

On an overall basis, the BEPS action plan will surely pave a way for the taxpayer to have clarity of tax positions and TP outcomes, helping reduce litigation and making dispute resolution less painful. Enhanced enforcement of the submission of information during an audit, as proposed in BEPS discussion, is an accepted way of conducting a Transfer Pricing Audit in India. India has a mandatory documentation requirement. In addition, at the time of the audit tax authorities ask for a detailed list of information on top of the TP documentation, which results in a delay in audit process. Several new issues raised in BEPS discussion could only be addressed through a robust and well informed approach to documentation. India, as a member of the G 20 countries, is generally supportive of BEPS documentation initiatives which might help in focusing issue based audits. country-by-country reporting of information on tangibles, sales and employees are the three factors commonly used for allocation of taxing rights under the formula apportionment methodology, and will be a challenge for the tax payers.

Contact Person

Subhasis Banerjee
subhasis.banerjee@wts.co.in
+912261471000

A 902, Marathon Futurex, ,Lower Parel(East)
N.M.Joshi Marg
Mumbai 400013
India
www.wts.co.in

The Challenges of Transfer Pricing in Italy

Recent changes in national TP legislation/jurisdiction

In recent years, the most significant development in the Italian TP legislation was the 2010 introduction of a set of transfer pricing documentation requirements in line with the recommendations and guidelines issued by the EU Commission and the OECD. As far as the Italian taxpayers are concerned, the compliance with this set of requirements is not mandatory, but it grants a penalty protection regime on transfer pricing adjustments deriving from tax audits.

More recently, the following further changes were introduced in the Italian TP legislation:
- applicability of transfer pricing adjustments deriving from tax audits to Regional Production Tax (IRAP) in addition to Corporate Income Tax (IRES) (Law No. 147/2013);
- limitation in the use of profit level indicators based on costs (unless agreed in an advance price agreement (APA) concluded with the Italian Tax Administration) for multinational enterprises operating in the online advertising sector or undertaking related ancillary activities (as unilateral provision to counter-attack web companies) (Law No. 147/2013);
- extension of the validity of an advance price agreement (APA) concluded with the Italian Tax Administration, from three to five tax periods (Law Decree No. 145/2013).

New developments in the Italian TP legislation are expected following the completion of a tax reform process, which the Italian Parliament initiated in 2014. In particular, the Italian Government has been mandated to introduce new provisions in order to strengthen the tax audits on transfer pricing matters.

Practical experiences from actual TP audits

In general, transfer pricing remains a key topic in tax audits. This was also confirmed by the Italian Tax Administration in an official document of 31 July 2013 addressing the key topics on the "prevention and fight against the tax evasion".

In regard to transfer pricing matters, the Italian Tax Administration and the Italian tax police have become more and more experienced over the last years. This experience significantly increased after the introduction of transfer pricing documentation requirements.

In particular, tax audits have been focused on the following matters:
- loss-making activities;
- selection of comparables for the application of the resale price, cost plus and transactional net margin methods;
- attribution of profits to permanent establishments;
- deductibility of management service fees and interest expenses paid to foreign associated entities.

Considering the above matters, the compliance with the set of transfer pricing documentation requirements strengthens the position of the Italian taxpayer vis-à-vis the Italian Tax Administration and Italian Tax Police.

Also, there has been an increasing number of advance price agreements (APA) concluded with the Italian Tax Administration.

Finally, it is worth mentioning a quite recent arguable position of the Italian Supreme Court, according to which transfer pricing rules may also apply to transactions between Italian associated entities leveraging the abuse of law doctrine.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

The set of transfer pricing documentation requirements introduced in the Italian TP legislation already foresees a Master file and a Country file document. However, it does not foresee the statutory financial statements and other financial information relevant for the country-by-country reporting proposed by the OECD. In this respect, no official positions have been taken by the Italian Tax Administration, although the matter is highly discussed among scholars and professionals.

Contact Person

Filippo Federico Miotto
filippo.miotto@taxworks.it
+39 011 433 83 51

Corso Francia 32
10143 Torino
Italy
www.taxworks.it

Recent changes in national TP legislation/jurisdiction

In 2013, a new transfer pricing decree was introduced by the Dutch tax authorities, replacing previous decrees. This has been one of the main topics regarding transfer pricing in the Netherlands. The decree includes adjustments regarding legislation, jurisprudence and the 2010 version of the OECD Transfer Pricing guidelines. Of interest is the non-limitative list of shareholder costs, and practical examples of mixed costs (which include both costs of shareholder activities and services). Furthermore, the substance over form view of the Dutch tax authorities on the transfer of (in)tangible assets is described, as well as the transfer pricing treatment of subsidies. New is the text describing the obligation to take into account guarantee fees in certain cases where group companies provide security for a loan by a group company. Other subjects covered are captives, the arm's length character of a loan and central procurement.

Practical experiences from actual TP audits

Transfer prices are in many tax audits under review. Companies that have concluded an advance pricing agreement experience hardly any discussions with the authorities on the transfer prices applied. Companies that have a (construction) permanent establishment in the Netherlands that do not have an APA are more often scrutinized. The same applies for companies that are loss making, pay large amounts for intercompany services, or that try to report costs or profits under a different tax regime than where they originally belong.

Given the complexity of transfer pricing, in the parliamentary history it has been stated that penalties will only be imposed if the use of incorrect transfer prices was deliberate. In January 2014 a penalty of EUR 125.000 was imposed in a transfer pricing court case, where the transfer prices regarding a captive insurance company in Switzerland were incorrectly set, given the actual substance of that Swiss captive. An appeal has been filed against this decision.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

The BEPS discussion is followed critically by the Netherlands. On the one hand each company should pay its fair share of taxes, where the Dutch tax authorities in principle apply the substance over form principle. On the other hand, companies should not be faced with excessive administrative and compliance burdens. It is felt that the Dutch business climate must remain attractive for internationally operating companies, so change arising from the BEPS action plan should not be applied individually by the Netherlands, but simultaneously with the other (European) countries.

In the 2013 transfer pricing decree, the Dutch State Secretary of Finance states that the OECD transfer pricing guidelines provide an internationally accepted explanation of the arm's length principle, and therefore regards those guidelines as a clarification of the Dutch legislation on transfer pricing. The Dutch rules do not prescribe how the transfer pricing documentation should be drafted. It may be drafted in line with those OECD guidelines, and needs to meet the proportionality principle to ensure that sufficient information is recorded, but that the administrative burden for tax payers is also limited where possible. This proportionality principle also applies in case the EU master file concept is applied. It is expected that documentation drafted in line with changed OECD documentation obligations will be accepted by the Dutch tax authorities, taking into account the proportionality principle.

Contact Person

Jan Boekel
jan.boekel@wtsnl.com
+31 10 217 9172

P.O. Box 19201
3001 BE ROTTERDAM
Conradstraat 18
3013 AP ROTTERDAM
The Netherlands
www.wtsnl.com

The Challenges of Transfer Pricing in Norway

Recent changes in national TP legislation/jurisdiction

The main topic in the Norwegian TP legislation was the introduction of the Documentation requirements back in 2008. The Norwegian Tax Authorities have recently supported the recommended actions from OECD in regard to BEPS, and will follow up with concrete proposals in the near future.

The thin capitalization regulation has been changed recently, and the introduction of a complete new set of detailed regulations is effective from 1.1.2014. The main idea is to restrict deduction of interests above the threshold of 25% of EBITDA. This is also effective for companies within Norway, and would create many additional compliance and tax planning efforts in the near future. It is expected that this will reduce the use of Norway HoldCo's as a hub for acquisitions in Norway. The use of low tax jurisdictions will probably be reduced or challenged even more due to the new restrictions.

Practical experiences from actual TP audits

Transfer pricing remains the key tax challenge for Norwegian multinational companies and Norwegian tax authorities. In short, transfer pricing issues are of the highest priority in tax audits. The tax auditors and professionals have become more trained and specialised over the last years since the implementation of the legal documentation requirements, and the audit approach on the transfer pricing issue is getting more aggressive and demanding. In particular, this is relevant in the special tax regimes for both Oil & Gas and Shipping.

Management services, licences and financial payments are especially often in focus. In particular the use of Permanent Establishments is under scrutiny, due to a lot of media attention and discussions about misuse of the concept from inbound multinationals. The Oil & Gas industry and related service industry are the main targets and subjects for control and focus.

An example is Allseas Marine Contractors S.A, which was not heard in their allocation of profit to a PE in Norway, in a 2011 supreme court resolution. The contract gross value was allocated to Norway, as the supreme court assessed that the main functions to achieve the contract were in Norway, and not in Switzerland. The Swiss ParentCo was merely supporting the contract by sub functions and got a fee for this.

Furthermore, Norwegian tax auditors are increasingly tending to request a benchmark with concrete country specific data. The use of hidden comparables has been widely used by tax authorities, and has recently been tried by court without a clear statement or guidance of how to use this information.

It is expected that the use of comparables, scrutiny of foreign Intellectual Property (IPR) ownership and rate level of licences will increase in future audits, and that the use of penalties related to missing or insufficient transfer pricing documentation will increase during the coming years.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

Generally, a master file documentation approach as proposed by the OECD is already accepted in Norway. Therefore, it can be expected that the Norwegian tax authorities would accept the OECD's proposals and adopt the new OECD standards for the Norwegian legal documentation requirements. However, the proposed extent of relevant information, especially regarding the so called country-by-country reporting, is also seen as very critical by the Norwegian tax administration.

Norway will most likely adopt the recommended view from the OECD, and will await the final reports before any actions will lead to concrete changes in the legislation. Some minor changes in the Controlled Foreign Corporation (CFC) legislation, and not at least a change of direction in the interpretation of cross border relevant issues has already been the outcome of the BEPS discussions. This is expected to escalate.

Contact Person

Ulf H. Sørdal
ulf.sordal@steenstrup.no
+4755301017-
+4741916717

Torgallmenning 3B
5811 Bergen
Norway
www.steenstrup.no

POLAND
DORADZTWO PODATKOWE
WTS&SAJA SP. Z O.O.

Recent changes in national TP legislation/jurisdiction

The main topic in the Polish TP legislation is the amendment to the Transfer Pricing Decrees, effective since July 2013. The amendment aligns the Polish legislation with (i) the 2010 update of the OECD Transfer Pricing Guidelines, specifically the business restructurings and (ii) conclusions of the EU Joint Transfer Pricing forum on the low value-adding services.

The above amendments imposed a new documentation regime on tax payers, regarding the intercompany services (low-value adding services) involving cost allocation.

With respect to the business restructuring, new provisions entitled the tax authorities to examine the business circumstances behind the restructuring, as well as other options available for the involved related parties. With respect to the "consideration for restructuring", strong adherence to the OECD Guidelines is observed: the transferor should receive the arm's length consideration for the assets, intangibles or other values carrying the profit potential.

The above regulations apply to all tax audits commenced after 18 July 2013. In practice, all tax years that have not been yet proven (from 2008 onwards) could be audited for the business restructurings.

Practical experiences from actual TP audits

For a number of years transfer pricing has been pointed out by the Polish Ministry of Finance (MoF) as the key audit issue for the tax controls. In April 2014, the MoF appointed a specialized team responsible for transfer pricing audits. The main task of this team is to increase the effectiveness of the transfer pricing audits by developing relevant tools and procedures. The team is led by the head of the APA practice which undoubtedly results in sharing the relevant expertise.

Over the recent years, increasing awareness and expertise of the tax authorities regarding transfer pricing has been observed. The request to submit the TP documentation became a routine element of each tax audit involving MNE subsidiaries. The tax authorities conduct a more critical review of the TP documentation content, and if they spot any deficiencies, they attempt to challenge the TP documentation for the accuracy/ reliability, which could lead to 50% tax assessment. However, the burden of proof lies on the tax authorities.

The key focus is on the management services. Particularly, the tax authorities require taxpayers to provide credible evidence that services were actually rendered. Otherwise they tend to disallow service charges as tax deductible costs. The other area of exposure is a lack of the periodical transfer price adjustments under deteriorating market conditions. Following the recent changes in the TP Decrees, business restructurings are expected to become the top priority for the audits.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

The international discussion on BEPS is reflected by the several legislative initiatives aimed in abusing tax driven optimization structures. Currently, the Polish parliament is working on i.e. the taxation of controlled foreign companies (CFCs) (being a completely new concept under the tax law), restricting the thin capitalization rules, and introducing to Polish legislation specific anti-avoidance provisions. These changes will probably come into force within the next two years.

With respect to transfer pricing documentation, the OECD proposal on Master File and country-by-country reporting has not yet triggered any wider public debate. However, from observing the overall evolution of the TP legislation in Poland, further implementation of the OECD concepts are highly probable.

Contact Person

Maja Seliga-Kret
maja.seliga@wtssaja.pl
+48 22 697 66 82
+ 48 61 643 45 50

Towarowa 35
61-896 Poznan
Poland
www.wtssaja.pl

The Challenges of Transfer Pricing in Russia

Recent changes in national TP legislation/jurisdiction

The new Russian TP legislation entered into force in 2012. Since that time TP rules have not significantly changed. However, some transition period rules established for 2012-2013 ceased to have effect beginning in 2014, and general provisions became applicable. In particular, the following rules related to MNEs came into force on January 1, 2014:

- TP documentation should now be prepared irrespective of the amount of revenue received by a taxpayer in controlled transactions. In 2013 the documentation should have been prepared only in case the total revenue received in controlled transactions between the same parties exceeded RUR 80 mln. (around EUR 1.7 mln.) per year; in 2012 this limit was RUR 100 mln. (around EUR 2.1 mln.). The same rule entered into force with respect to the obligation of the taxpayers to notify the tax authorities about their controlled transactions.
- Similarly, starting January 1, 2014 the tax authorities may audit the prices in controlled transactions irrespective of the amount of revenues received by taxpayers in these transactions.
- Starting from the tax period 2014, penalties will be applicable for non-payment (or insufficient payment) of taxes resulting from the application of transfer prices in controlled transactions. The penalty amount is 20% for the tax periods 2014-2016 and 40% - starting from the tax period 2017. However, no penalties will be applied in case the TP documentation is provided to the tax authorities. For the tax periods 2012-2013 no penalties can be applied.

Practical experiences from actual TP audits

The tax authorities still tend to challenge an expense as tax deductible, and not just the prices used in transactions between the associated parties. In practice it is much easier and less time consuming to argue that a certain expense is non-deductible than to prove that the price used in a transaction differs from the market level. A recent case of British American Tobacco which was heard in the Moscow Federal Arbitration Court in February 2014 is a good illustration to the above point. In this case expenses on consulting services were allocated to the group's Russian subsidiaries. And although one of the main issues was the level of prices applied in intra-group transactions, the tax authorities did not actually audit the prices, but rather proved that the services in question were not really rendered to the subsidiaries, and that the transactions in question were pretended.

However, it is anticipated that in the future the tax authorities will more frequently use the possibilities of special TP audits, and will more and more actively use legal procedures for control of prices.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

Russia is not an OECD member, therefore discussion on the draft revised guidance on transfer pricing documentation and country-by-country reporting is not applicable in Russia. It also should be noted that in Russia there are no special rules on documentation for MNAs. The Russian Federation Tax Code stipulates that the TP documentation should contain information about a taxpayer as a separate legal entity. The tax authorities additionally recommend that the TP documentation should also contain information about the group to which a taxpayer belongs, in particular a group structure (ownership chart, functions and places of tax residence), list of group's main assets, and general description of the group's market place. In this respect the information, which is proposed by OECD for inclusion in a Master file, is much more detailed than required in Russia. The Russian tax authorities also developed the detailed recommendations on the information about a taxpayer and controlled transactions, which should be included in TP documentation. This information is quite close to the information which should be included in the Local file as proposed by OECD.

Contact Person

Raisa Karaseva
raisa.karaseva@nb-notabene.ru
+7 925 507-14-68

Zarayskaya str., 21
Moscow 109428
Russia
www.nb-notabene.ru

Recent changes in national TP legislation/jurisdiction

The 2014 Budget did not introduce any specific changes to the UK's Transfer Pricing regime. However, the tax policies and practices of multi-national enterprises (MNE) carrying on business in or with the UK is a 'hot' topic with widespread media attention and government debate. In particular, the Chancellor committed to quickly bringing into effect the proposals on international tax changes being formed by the OECD. As part of the Budget Statement, the UK government published a paper that outlines the UK's priorities for the BEPS project, discussed in more detail below.

One specific announcement made was the extension of an anti-avoidance measure to tackle schemes involving the transfer of corporate profits. This was originally introduced in the Autumn Statement 2013 in respect of mechanisms involving financial derivatives. Due to new schemes being designed to work round the new measure, it was extended to also cover arrangements involving mechanisms other than derivatives. The measure will only apply where there is a tax advantage motive. However the wide scope of the rule means that many MNEs may have to carefully review their intercompany arrangements as a result.

Practical experiences from actual TP audits

The UK Government has committed a significant amount of additional funding to HMRC (the UK tax authorities) to provide the resources so that it can 'delve deeper' into the tax arrangements of multinational businesses. This has seen the creation of a single large business directorate to deal with the tax affairs of the largest 2000 businesses operating in the UK, and increased staff resourcing within particular areas including Transfer Pricing. Consequently, this will inevitably lead to increased scrutiny of multinationals intercompany arrangements and transfer pricing. HMRC have reported that investigations into transfer pricing arrangements produce the highest return on resources committed.

Local view on BEPS discussion, especially considering proposed changes on TP documentation and country-by-country reporting

As part of the 2014 Budget, the UK Government set out its priorities in relation to BEPS. This is within the simple overall approach that they will do everything they can to help companies compete in the world but expect them all to pay the tax they owe. Notably:

- The UK tax authorities are in favour of country by country reporting. With the UK Presidency of the G8 in 2013, the UK authorities led the way in initiating the push for adoption of the country-by-country reporting template. Their current view is that the information should be high level, and broadly based on information that would already be prepared for local tax authorities in each jurisdiction, to enable risk assessment without creating a significant additional compliance burden for business;
- The UK is committed to extending the model for enhanced exchange of tax information between tax authorities; and
- The UK is committed to working with other tax authorities to identify risks posed by cross-border operations in the digital economy. The taxation of the digital economy is a key priority for the UK government. UK consumers are the highest 'digital' purchasers in the EU with the result that the UK will be the most impacted country economically by developments in this area.

Contact Person

Marvin Rust
marvin.rust@fticonsulting.com
+44 203 727 1450

200 Aldersgate
Aldersgate Street
London, EC1A 4HD
UK
www.fticonsulting.co.uk

wts TAX LEGAL CONSULTING

Visit us at IFA Mumbai

October 12 – 17, 2014

→ WTS at IFA Mumbai 2014
NCPA Marg, Nariman Point
Mumbai, Maharashtra 400021, India

→ Join the WTS Panel Discussion at IFA 2014
Monday, October 13, 2014
From 14.30 to 16.00 p.m.
Experimental Theatre, NCPA

Contact at WTS | Heidi Jackelsberger | heidi.jackelsberger@wts.de