

Transfer Pricing

IFA - Landesgruppe Liechtenstein

BEPS and Transfer Pricing

February 2017

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Contents

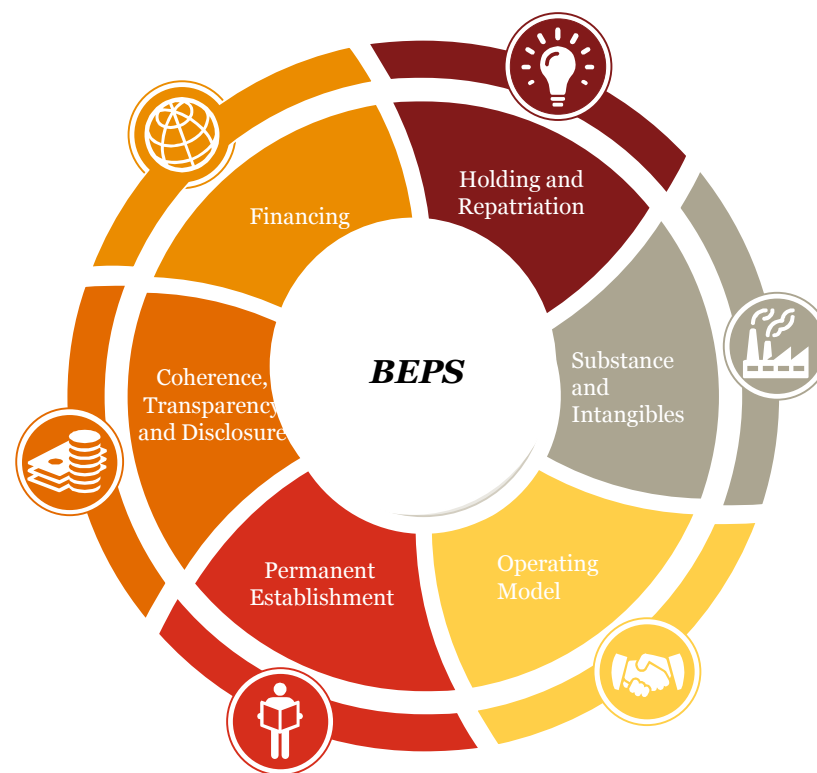
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Introduction

BEPS – Action Plan Overview

No	Action	M*
1	Address the tax challenges of the digital economy	
2	Neutralise the effect of hybrid mismatch arrangements	
3	Strengthen CFC rules	
4	Limit base erosion via interest deductions and other financial payments	
5	Counter harmful tax practices more effectively, taking into account transparency and substance	✓
6	Prevent treaty abuse	✓
7	Prevent the artificial avoidance of PE status	
8	Assure that TP outcomes are in line with value creation Intangibles	
9	Assure that TP outcomes are in line with value creation Risk & Capital	
10	Assure that TP outcomes are in line with value creation Other high-risk Transactions	
11	Establish methodologies to collect and analyse data on BEPS and the actions to address it	
12	Require taxpayers to disclose their aggressive tax planning arrangements	
13	Re-examine transfer pricing documentation	✓
14	Make dispute resolution mechanisms more effective	✓
15	Develop a multilateral instrument	

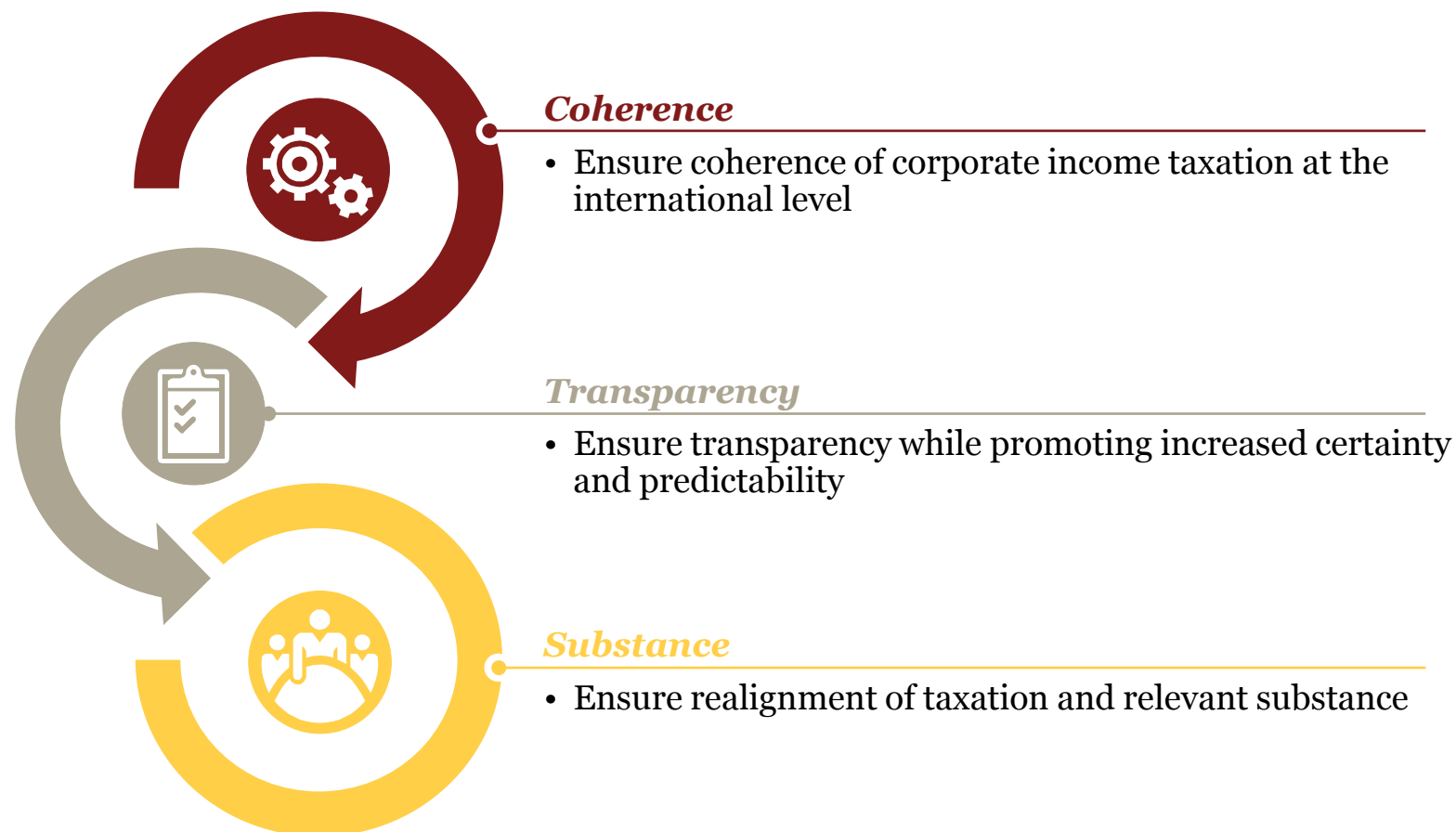
M* = Minimum Standard



Main reports delivered by October 2015

BEPS – Action Plan

Key objectives



TP documentation / CbCR

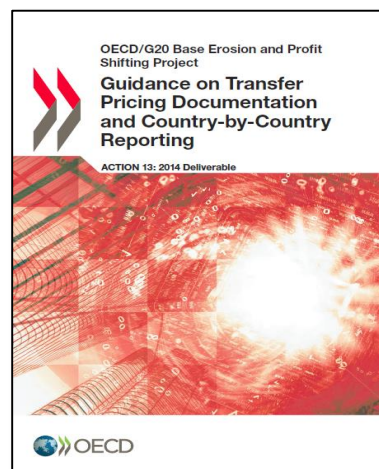
The OECD's objective and its approach

Chapter V Objectives

To ensure that taxpayers give appropriate consideration to transfer pricing requirements in their intragroup dealings

To provide tax administrations with the information necessary to conduct an informed transfer pricing risk assessment

To provide tax administrations with useful information to employ in conducting an appropriately thorough audit



Chapter V Three-Tiered Approach

Master file: high-level overview of an MNE's business

Local file: specific information related to the transactions of the local taxpayer

Country-by-country report: information on global allocation of income and other economic factors

Master File

Content

Org. structure	Description of MNE's business	MNE's intangibles	MNE's financial activities	MNE's financial & tax positions
Chart showing legal & ownership structure & geographic location of operating entities	Important drivers of business profit	Overall strategy: development, oversight & exploitation, including location of R&D facilities & management.	Description of how the MNE is financed, including arrangements with third-party lenders	Annual consolidated financial statement for FY
	Description of supply chain for material products & services	List of IP & entities that own IP	Financial transfer pricing policies	List & description of unilateral APAs & other tax rulings relating to allocation of income
	List & description of service arrangements among MNE members other than R&D, <i>including policies</i>	Agreements related to IP, including CSAs	MNEs central financial function, country of org. & management of entity providing function	
	Main geographic markets for products and services	IP and R&D transfer pricing policies		
	Functional analysis describing contributions to value creations by individual entity	Material transfers of IP among MNE members during FY, including details		
	Business restructurings			

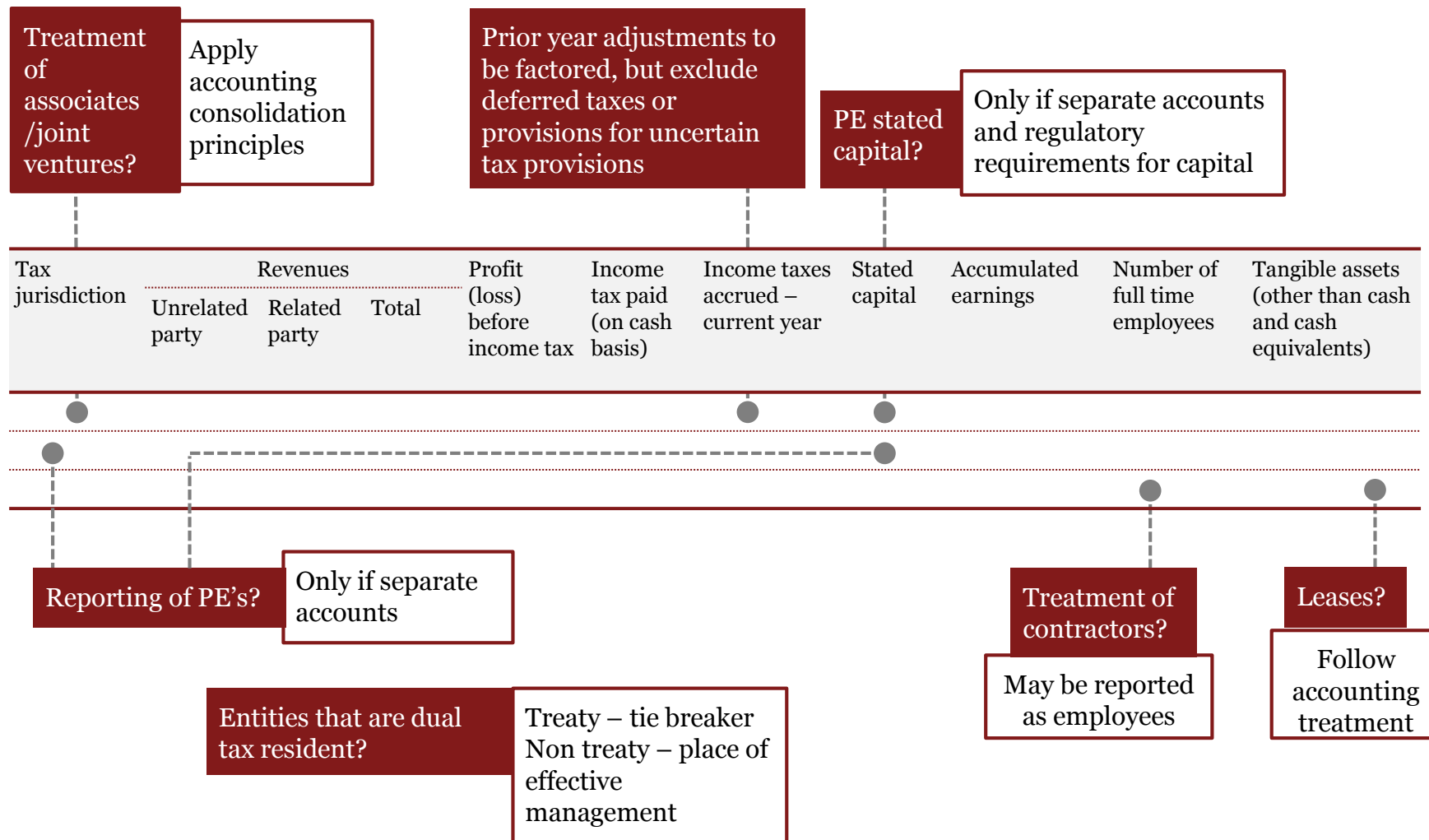
Local File Content

Requires inclusion of the following information:

1. Description of mgmt. structure of the local entity, a local org chart, a description of the individuals to whom local mgmt. reports and the country(ies) in which such individuals maintain their principal offices
2. Detailed description of business(es) and business strategy, including involvement in **business restructurings or IP transfers** in current or immediately prior year
3. Key competitors
4. For each category of controlled transactions:
 - Description of material controlled transactions, including context
 - Amount of payments and receipts for each category of controlled transactions **involving** the local entity
 - Copies of all material intercompany agreements concluded by local entity
5. **Copy** of existing **unilateral and bilateral/multilateral APAs and other tax rulings** to which the local tax jurisdiction is not a party and which are related to the local file controlled transactions
6. Information and allocation schedules applying the TPM

Country-by-country report

Content (Table 1)



Country-by-country report

Content (Table 2 and 3)

Table 2. List of all the Constituent Entities of the MNE group included in each aggregation per tax jurisdiction

Name of the MNE group: Fiscal year concerned:															
Tax Jurisdiction	Constituent Entities Resident in the Tax Jurisdiction	Tax Jurisdiction of Organisation or Incorporation if Different from Tax Jurisdiction of Residence	Main Business Activity(ies)												
			Research and Development	Holding or Managing Intellectual Property	Purchasing or Procurement	Manufacturing or Production	Sales, Marketing or Distribution	Administrative, Management or Support Services	Provision of Services to Unrelated Parties	Internal Group Finance	Regulated Financial Services	Insurance	Holding Shares or Other Equity Instruments	Dormant	Other ¹
	1.														
	2.														
	3.														
	1.														
	2.														
	3.														

1. Please specify the nature of the activity of the Constituent Entity in the “Additional Information” section.

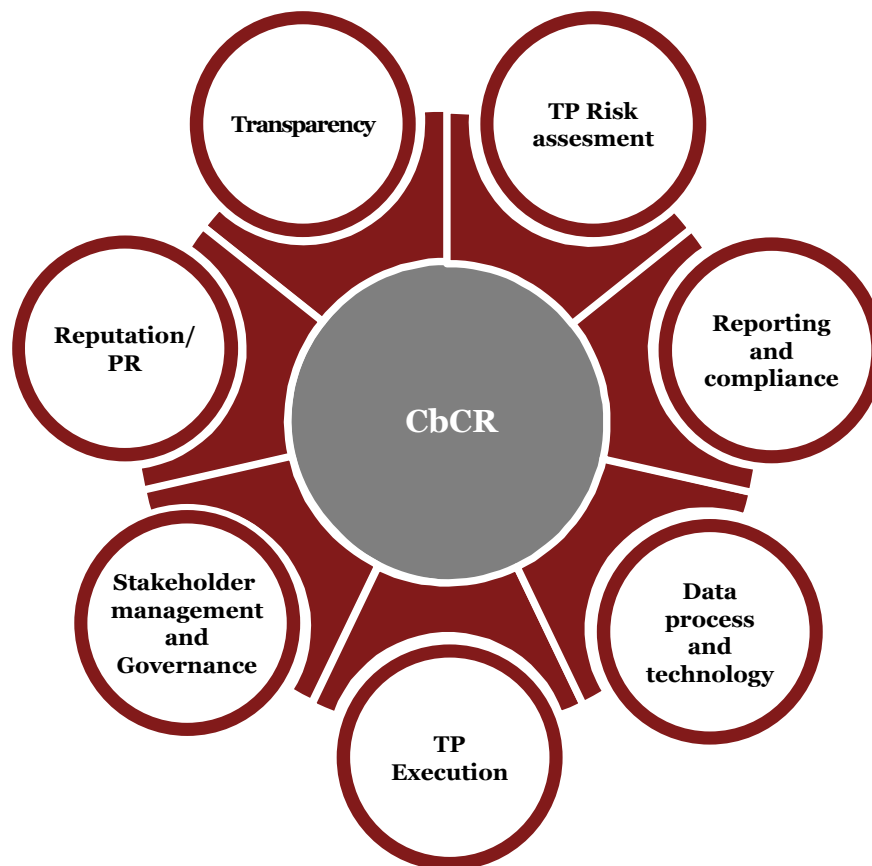
Table 3. Additional Information

Name of the MNE group: Fiscal year concerned:
<i>Please include any further brief information or explanation you consider necessary or that would facilitate the understanding of the compulsory information provided in the Country-by-Country Report.</i>

Country-by-country report

More than a simple compliance burden

- Technical interpretation
- Tax / TP risk and impact assessment
- Transparency and data security
- Links to Master and Local File
- Technology capabilities
- Data extraction and analysis
- Alignment with other transparency initiatives
- Governance and sign off
- Reporting and Compliance



Practical Experience

Consequences and impact for tax departments

General

- High momentum of local jurisdictions expanding transfer pricing compliance requirements
- Increased transparency especially with respect to intangibles, financial activities and tax rulings/APAs

Master File / Local File

- Consistent TP documentation approach for the entire Group
- Centralisation and standardisation of documentation approach

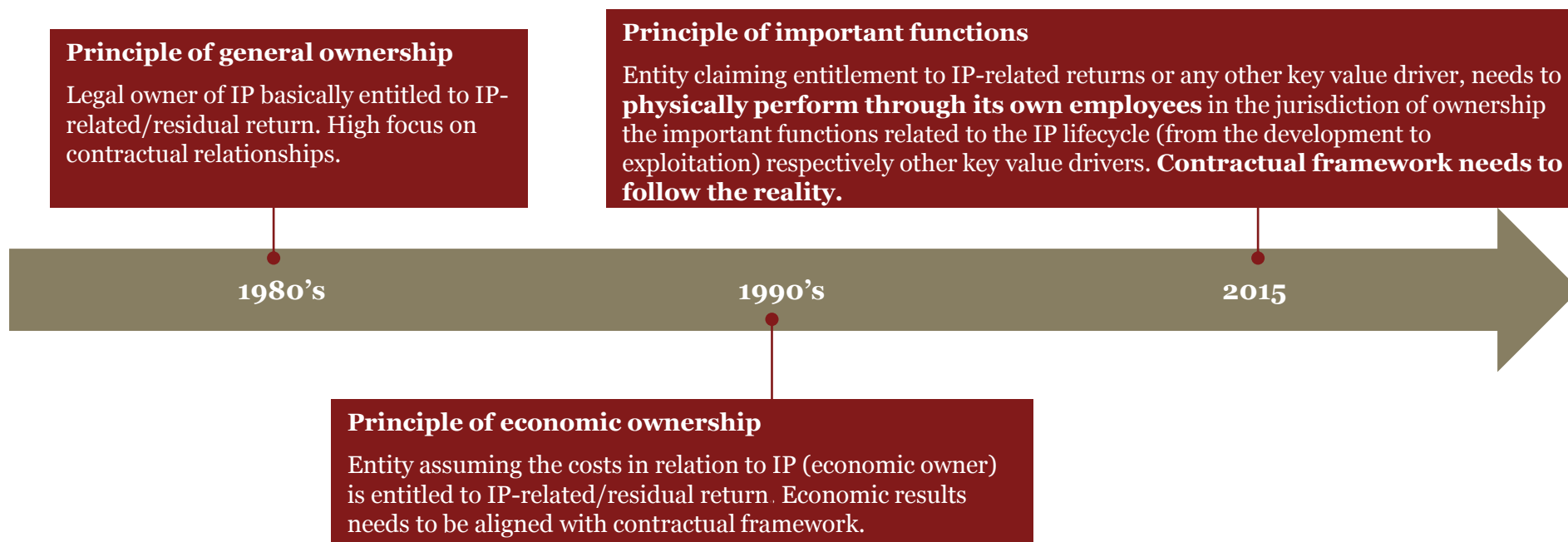
CbC Reporting

- Unclear definitions / Room for interpretation
- Required alignment of taxation with substance

IP and DEMPE

OECD Developments on operational substance requirements

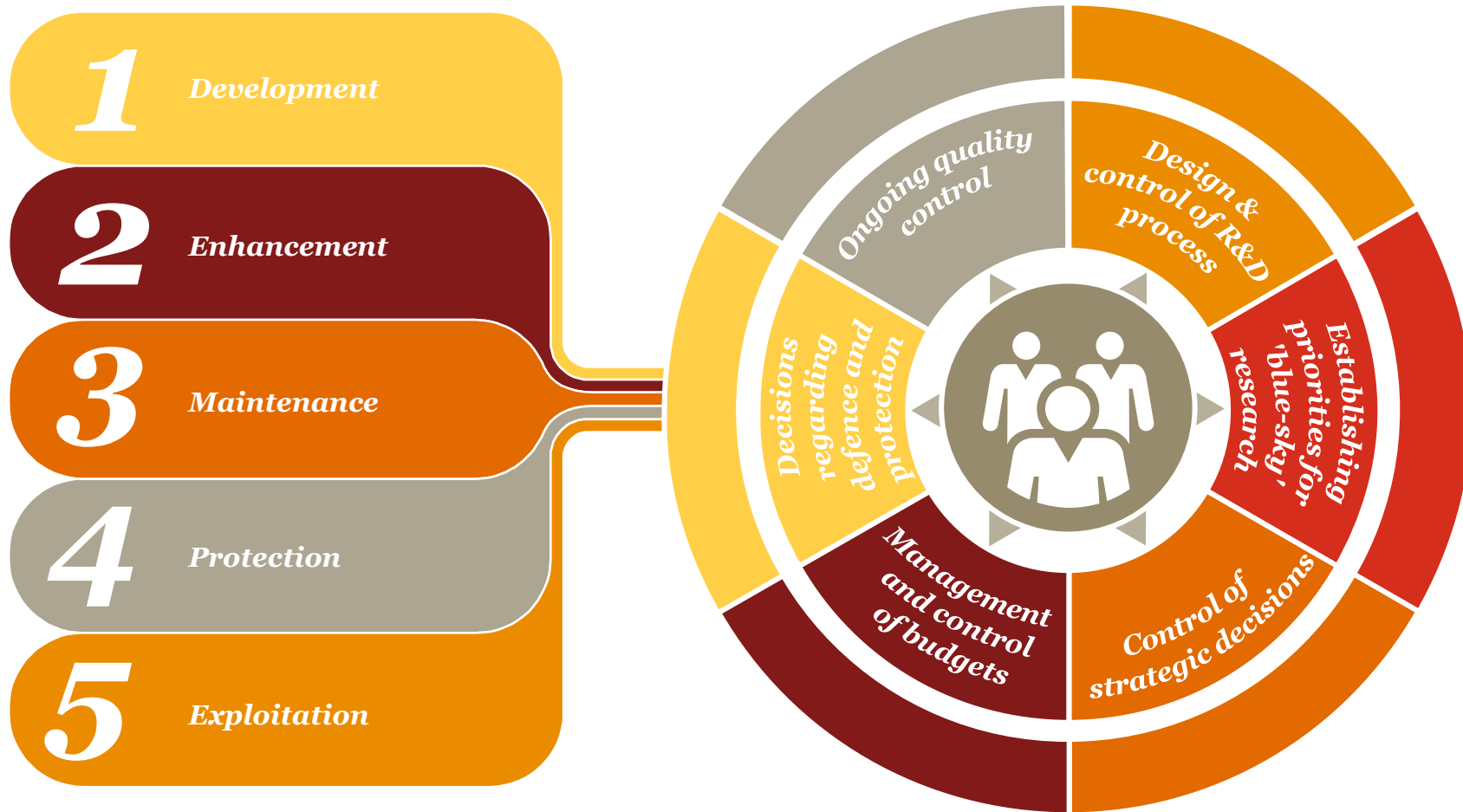
In the last decades, the international (OECD & best practice) principles for allocating residual (excess) profits to an entity have dramatically changed. The following graph illustrates the different principles that were applied in the past and that have been now completely revised based on OECD's BEPS project (majority of reports finalised in October 2015).



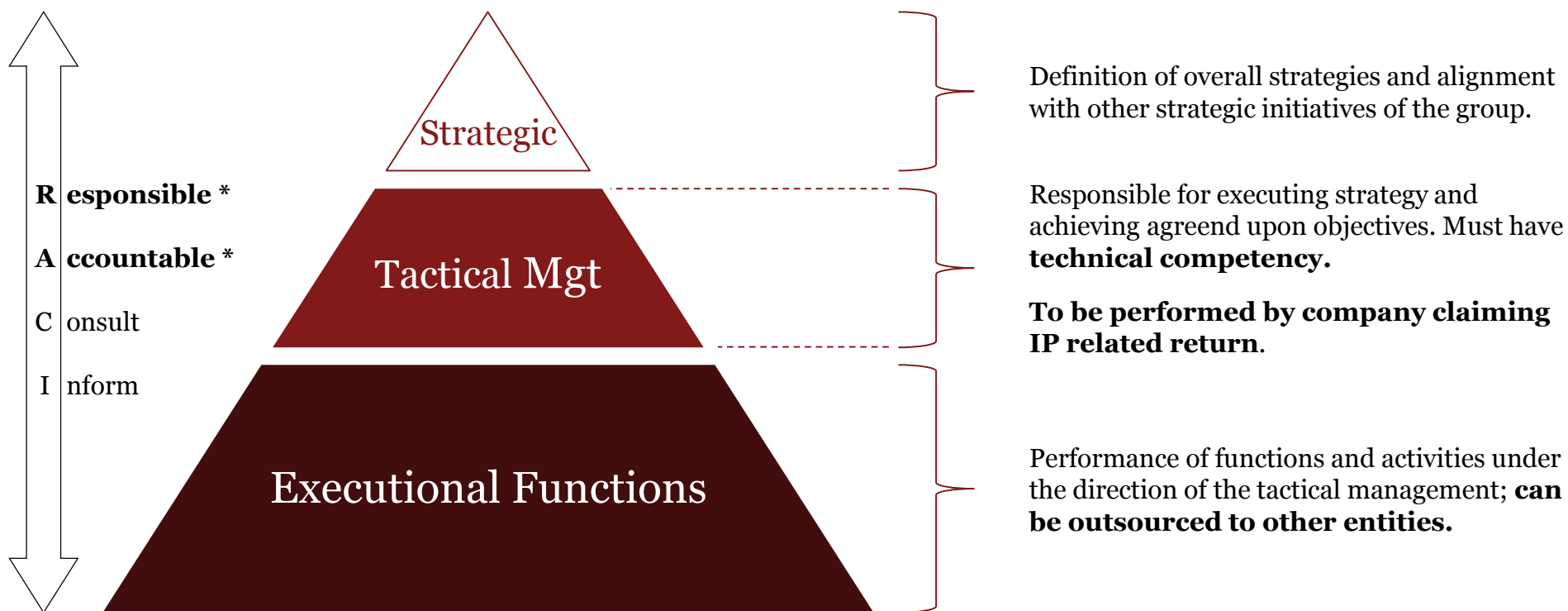
→ The important functions need to be aligned for the whole IP-lifecycle (**D**evelopment, **E**nhancement, **M**aintenance, **P**rotection and **E**xploitation).

→ **Very high focus on having all the important DEMPE functions** in relation to a specific IP or any other key value driver **in the entity that is claiming the respective return.**

IP Ownership - the DEMPE concept

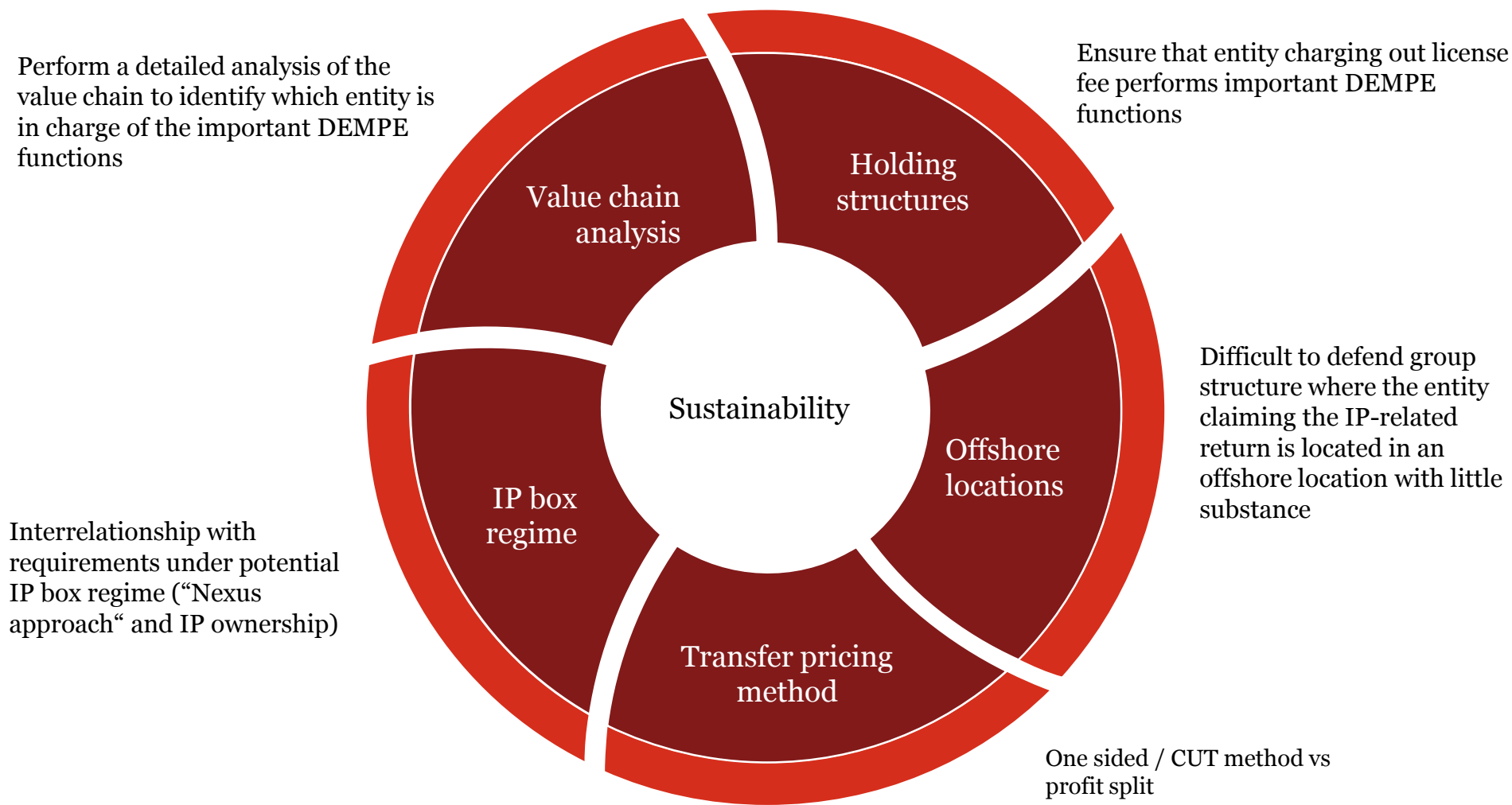


Identification of important DEMPE functions



* DEMPE relevant functions

Practical considerations



The OECD Nexus approach

- Expenditures and benefits must directly be linked = nexus approach
- Expenditures as a proxy for substantial economic activities
- The goal of the nexus approach is to grant benefits only to income that arises from IP where the actual R&D activity was undertaken by the qualifying taxpayer itself
- Qualifying tax payer must own the IP box qualifying IP (= perform important DEMPE functions)

$$\frac{\text{Qualifying expenditures incurred to develop IP asset}}{\text{Overall expenditures incurred to develop IP asset}} \times \text{Overall income from IP asset} = \text{Income receiving IP box tax benefits}$$

Permanent establishment

BEPS Action item 7

Overview

Mandate – Prevent the Artificial Avoidance of PE Status

Develop changes to the definition of PE to prevent the artificial avoidance of PE status in relation to BEPS, including through the use of commissionaire arrangements and the specific activity exemptions. Work on these issues also includes related profit attribution issues.

Widening

**Dependent Agent
scope**

Tightening

**Specific Activity
Exemptions**

Eliminating

**Fragmentation
of activities/splitting
of contracts**

Modifications to paragraphs 4, 5, and 6 of Article 5 and its Commentaries.

BEPS Action item 7

Revision of Art. 5 (5) OECD-MC

Old version OECD-MC 2014	Proposed version
<p>5. Notwithstanding the provisions of paragraphs 1 and 2, where a person — other than an agent of an independent status to whom paragraph 6 applies — is acting on behalf of an enterprise and has, and habitually exercises, in a Contracting State an authority to conclude contracts in the name of the enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph.</p>	<p>5. Notwithstanding the provisions of paragraphs 1 and 2 but subject to the provisions of paragraph 6, where a person is acting in a Contracting State on behalf of an enterprise and in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are a) in the name of the enterprise, or b) for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or c) for the provision of services by that enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph.</p>

BEPS Action item 7

Revision of Art. 5 (5) OECD-MC (Practical implications)

		Client identification	Product promotion	Price Negotiations	Drafting agreements	Signing contracts	
old	Principal	-	-	-	-	✓	→ PE
	Related Party	✓	✓	✓	✓	-	
new	Principal	-	-	✓	✓	✓	→ PE
	Related Party	✓	✓	-	-	-	
new	Principal	-	-	(✓)	(✓)	✓	→ PE ?
	Related Party	✓	✓	(✓)	(✓)	-	

BEPS Action item 7

Revision of Art. 5 (6) OECD-MC

Old version OECD-MC 2014	Proposed version
<p>6. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.</p>	<p>6. a) Paragraph 5 shall not apply where the person acting in a Contracting State on behalf of an enterprise of the other Contracting State carries on business in the first-mentioned State as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent within the meaning of this paragraph with respect to any such enterprise.</p> <p>b) For the purposes of this Article, a person is closely related to an enterprise if, based on all the relevant facts and circumstances, one has control of the other or both are under the control of the same persons or enterprises. In any case, a person shall be considered to be closely related to an enterprise if one possesses directly or indirectly more than 50 per cent of the beneficial interest in the other (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) or if another person possesses directly or indirectly more than 50 per cent of the beneficial interest (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) in the person and the enterprise.</p>

Conclusion

Conclusion

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- OECD BEPS objectives on coherence, transparency and substance
 - Data analytics and tax audits
 - Consistency and sustainability



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