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EU JOINT TRANSFER PRICING FORUM

REPORT ON THE USE OF COMPARABLES IN THE EU

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1. Background

1. The EU Joint Transfer Pricing Forum (JTPF), as part of its work programme for 2015-2019 ("Tools for the rules"), addresses the use of comparables in the EU (section 2.2 doc. JTPF/005/2015). Non-Governmental Members and Member States were asked to provide contributions as part of the preparation of the two meetings of 18 February 2016 and 23 June 2016. Those led to issuing two working documents (respectively, (doc. JTPF/009/2016/EN and JTPF/013/2016/EN) and were considered in the preparation of an overview on the current state of play, issues and possible solutions.
A draft discussion paper on "Comparables in the EU" was prepared and discussed at the JTPF meeting in February 2016 (doc. JTPF/001/2016/EN). The present report also reflects the outcome of this discussion.

2. Introduction: context and scope

2. The application of the arm's length principle is generally based on a comparison of the conditions in a controlled transaction with the conditions in transactions between independent parties ('comparability analysis'). The OECD Transfer Pricing Guidelines ('TPG')¹ describe two key aspects of the comparability analysis *(i) to identify the commercial and financial relations between the associated enterprises, the conditions and economically relevant circumstances attaching to these relations in order that the controlled transaction is accurately delineated;* *(ii) the search for comparables,* described as "*compar(ing) the conditions and the economically relevant circumstances of the controlled transaction as accurately delineated with the conditions and the economically relevant circumstances of comparable transactions between independent enterprises*"². These two components are part of the typical process of a comparability analysis³, whereas the delineation is part of step 3 and the comparable search is addressed in steps 4 to 9.
3. Delineating the transaction (see component *(i)* above) and drawing conclusions from the risk analytical framework⁴ is the first step and separate from the search for comparables. The delineation has significant consequences on the result of the comparability analysis. The search for comparables therefore needs to be systematically positioned *vis-à-vis* the delineation of the transaction. It is the delineated transaction, which governs the comparables search and not *vice versa*.
4. This report focusses on the second component described above, i.e. the search for comparables. It contains various recommendations for both taxpayers and tax administrations and aims at increasing in practice the objectivity and transparency of comparable searches in the EU. The purpose here is to make progress towards best practices and to find pragmatic solutions for companies doing business in the EU. While

¹ if not stated otherwise, "TPG" refers to the OECD Transfer Pricing Guidelines in the version which takes into account the final reports on Action 8-10, as published in 2015

² See Par. 1.33 & seq. TPG.

³ See Par. 3.4 TPG.

⁴ See Par. 1.60 TPG.

sections 3 and 4 apply to search for comparable data in general, Sections 5 and 6 are mainly related to the search for data on potential comparable companies ('comparable company search').

3. Comparable search

3.1 General aspects

5. A comparable search should be put in context of the following general aspects. The search for comparable data is part of the comparability analysis. As such, it is inter-linked with the delineation of the transaction and directly based on the facts and circumstances of each individual case.
6. Most Member States have set out legislation and practical guidance on how a comparability analysis should be performed⁵, which broadly reflect the guidance given in Chapter III of the OECD Transfer Pricing Guidelines. This Chapter has not been revised further to the recent Report on BEPS Actions 8-10 Aligning Transfer Pricing Outcomes with Value Creation and is confirmed as setting out the process of “*making comparisons between the controlled transactions and the uncontrolled transactions in order to determine an Arm’s length price for the controlled transaction*”. There is also more and more case law available on the use of comparables in EU Member States and in third countries⁶, which is of growing interest.
7. Finding acceptable comparable data is regarded as a challenge in the practical application of transfer pricing. It is recognised that complete elimination of judgments from the selection of comparable data would not be feasible, but also that much can be done to increase objectivity and ensure transparency in the application of subjective judgements⁷.
8. A balance has to be found between (i) care, thought, analysis and judgment, on the one hand, and, (ii) ensuring consistency and maximizing objectivity, on the other hand. The first (i) attributes need to be exercised when searching for comparables but the second term (ii) is crucial in the context of the EU to ensure a proper implementation of the TPG and best practice and therefore to prevent tax disputes.

Recommendation 1:

- a) Both taxpayers and tax administrations should apply a principle of transparency when they respectively conduct or control a comparable search. This means that taxpayers should justify and document the steps of the searches *vis-à-vis* the tax administration, and,

⁵ An overview of MS TP profile can be found on the JTPF website:

http://ec.europa.eu/taxation_customs/business/company-tax/transfer-pricing-eu-context/joint-transfer-pricing-forum_en

⁶ See for illustration, the case law on the use of internal comparables provided in section 1.3 of the study made by Deloitte Belgium on the use of comparables in the EU, commissioned by the European Commission (2016)

⁷ See Par. 3.46 TPG.

symmetrically, that the tax administration should provide the relevant information for these steps to the taxpayer, when preparing or challenging such searches.

- b) The burden on both taxpayers and administrations as regards comparable searches execution and review should be *proportionate*. Additionally, the emphasis should be placed on *quality, transparency and consistency* of the analysis when conducting a comparable search. Consistency here refers to the application of a coherent approach at each step from the start of the search until its last step (*e.g.* the adjustment phase), but also considering each step in relation with the others and, overall, the comparable search in correlation with the delineation of the transaction. Consistency over time is a good practice: once an approach is taken, it should be consistently applied, unless valid reasons are put forward to change the approach or the facts and circumstances of the underlying transaction have changed. In summary, an 'end-to-end approach' should be taken in which all steps are processed to achieve a relevant, consistent and transparent comparable search, *ie* "from the very beginning to the very end".
- c) Taxpayers and tax administrations should also consider the impact of the delineation of the transaction, including the risk analytical framework, on different steps of the comparable searches during the following steps: the definition of the search terms and scope, the screening and rejection steps and possible adjustments.

3.2 Search strategy proposal

9. Setting a search strategy in line with the arm's length principle by adopting a transparent approach verifiable by a reviewer requires the identification of all the steps needed in order to be able to identify the most reliable comparable information available.
10. As mentioned in paragraph 2 the delineation of the transaction should be conducted prior to the search process. The better the facts and circumstances of the transaction and the functions, assets and risks are defined, the more accurate the search will be.

Example in the context of a comparable company search:

The tested party is characterised as a distributor but it is then established under the Chapter I-D analysis of the TPG that it does not assume the inventory risk. As regards the comparable company search, the question to be addressed in particular is whether a distributor should be searched and then working capital adjustments be done, or, if it would be more appropriate to search comparable company data carrying out marketing operations rather than distribution.

11. Both NGMs and Member States agreed on the necessity of precisely identifying steps and common milestones, as part of the comparable search. Moreover, the following general recommendations, reflecting good practice in the EU, should be made in order to facilitate the transparent step-based analysis just described.

Recommendation 2:

- a) The steps taken in a comparable search described in the subsequent sections, as well as the result of these respective steps and any related judgement, should be made transparent to any relevant reviewer. This applies in particular to the documentation and the justification of the search and screening criteria, the rejection criteria and the adjustments made.
- b) Many sources of information are available within companies and can be used when setting up a comparable search. A broad range of sources, including external data bases, companies' statutory books or internal management and information systems, documentation used internally by marketing, purchasing and pricing departments (to set or negotiate prices) and any other relevant information⁸, can be useful and bring some added value to refine the search for comparables.
- c) Judgment should be used to assess the above-mentioned information sources and possibly complement them at the various steps of the process. Principles of transparency and proportionality should apply.
- d) In principle there are two approaches to arrive at an appropriate set of comparables, non of them having a systematic preference⁹. The choice of the approach is driven by the objective to find the best and most reliable comparables and should be justified. While the deductive approach could be in the majority of cases the preferable approach when selecting comparables from commercial databases, the additive approach happens to be more appropriate in some justified cases.
- e) The comparable search should be appropriately documented and supported, particularly by mentioning the financial data on the comparables used and the respective sources (e.g. database references). This should include sufficiently detailed search and rejection matrices and should consider the information relevant to be provided in cases where tax authorities may not be able to verify the authenticity of the information and/or have access to the data. While performing the search, screenshots may be useful for documenting information that may not be available in the future.
- f) Evidence gathering should be archived and the documents that support the comparable search should be maintained according to the national rules regarding the maintenance of documents.

4. Specific aspects dealing with internal comparables

4.1 Selecting internal comparables

12. Internal comparables are defined as transactions between one party to the controlled transaction and an independent party. The advantages of the use of internal comparables are the easier access and the availability of more detailed information as highlighted in the

⁸ Some Non Governmental Members indicated that other information than external data base can be of particular interest, particularly for SMEs or tested parties evolving in a specific sector or industry with a limited market and few competitors. Depending on the facts and circumstances, data bases searches can be appropriately refined using such complementary information (including in particular import & export data, external lists of prices purchased, market development, raw industry prices, etc.) doc. JTPF/009/2016/EN.

⁹ See Par. 3.40 – 3.46 TPG.

TPG.¹⁰ There may be an asymmetry of information between the taxpayer and the tax administration as regards the availability of potential internal comparables as the taxpayer – naturally – has a more complete overview of the business transaction within the MNE group/the respective MNE Group Member. Taking into account the principles of transparency and proportionality, taxpayers should document sufficiently and without shortcut the approach taken as regards internal comparables in the search for comparables.

4.2 Using internal comparables

13. Generally speaking, internal comparables may be used when applying the Comparable Uncontrolled Price Method (CUP) or for other methods, when determining a margin¹¹. Using internal comparables is a preferred option in all EU Member States¹². By contrast, the internal comparables tend to be widely dismissed by tax administrations, due to lack of data or material differences in the comparability factors. Tax administrations might show a demand of comparability, which is *de facto* higher than for external searches due to the intrinsic nature of such comparables, which allow having access to more information (and therefore more potential reasons to reject them).

Recommendation 3:

- a) Internal comparables are directly available to the taxpayer. Obtaining and processing them can in some circumstances be less costly than searching and adjusting external comparables through commercial databases. Taking into account the guidance provided in the JTPF report on small and medium enterprises and transfer pricing¹³ internal comparables could particularly be explored to achieve proportionality when used for small transactions and SMEs.
- b) Taxpayers having third party transactions with relevance for the comparability analysis of the transaction under review, in particular meeting the comparability factors, should provide sufficient details on the evaluation of internal comparables, *i.e.* documenting which approach is taken, the results obtained and the reasons for accepting/disregarding these potential internal comparables.
- c) The possibility to use internal comparables in combination with or to support other methods should be explored when it is expected to add value to the analysis.
- d) In the context of the same TP method, internal and external comparables should be treated in the same manner as regards the degree of comparability required. There is no systematic preference towards using internal or external comparables and comparability should prevail.

¹⁰ See Par. 3.27 and 3.28 TPG.

¹¹ See Par. 2.22, 2.38, 2.40, and 2.58 TPG.

¹² See also Commission Staff Working Document, “Report on the Activities of the EU Joint Transfer Pricing Forum in the Field of Documentation Requirements”, SEC (2005)543 final, Sec. 2.3.1 (Para. 38) : « Internal comparables where they exist should be preferred to external comparables when applying traditional methods and the TNMM (see Par. 2.15, 2.33 and 3.26 TPG) (note that these references to paragraphs of the TPG relate to the TPG 1995/2010 before they were amended by the Final Report on Actions 8-10).

¹³ Particularly Recommendations 1 and 5 of the JTPF report on small and medium enterprises and transfer pricing, Communication from the Commission 19.09.2012 COM (2012) 516 final.

5. Specific aspects dealing with external comparables

14. There are various sources for external comparables. These comparables may directly reflect a price charged for property or services transferred and therefore often be used for the CUP method (provided the comparability factors are met). Generally, external company data are mainly used for the application of the Resale Minus Method, the Cost Plus Method and in particular the Transactional Net Margin Method. The following section addresses searches for comparable companies except where otherwise mentioned.

5.1 Sources of information in the EU

15. The work conducted at the level of the EU JTPF gives a comprehensive overview of the state of the art regarding the potential sources for external comparable companies and the various stages of an external comparable company search (i.e. selection and screening of the comparable data, use of multiple year data, treatment of the interquartile range and adjustments).

16. A comparable search of external potential comparable data can be performed reliably only when sufficient information is available on comparable companies. Overall a substantive amount of data is encountered for the EU Member States which is expected to provide in most cases a sufficient and satisfactory basis for conducting a comparable study. The feasibility of the selection (incl. tests such as independence test, rejection of potential comparable start-up companies, choice and application of different PLIs), is most likely in this context and adjustments are expected to be possibly done. Business and Academia members of the JTPF have underlined that the situation has improved over the last two decades and the availability and quality of data at EU level is comparable or even better than in some non-EU countries, in particular major key trade partners.

Recommendation 4:

- a) Inconsistencies in the industry classifications between countries require the application of judgment. Combining the industry codes with other elements (*e.g.* inclusion/exclusion keywords) when defining search strategies of external comparables can be useful. Referring to internal sources of the taxpayer can be relevant (industry codes of the taxpayer and of the competitors, additional information¹⁴).
- b) Specific situations where external CUP comparables are available and can be identified, using an additive approach could be explored: the OECD TPG refer for instance to acquisition operations, where an enterprise “*which used to transact independently with the MNE group is acquired and the acquisition is followed by a restructuring of the now controlled transaction*”¹⁵.
- c) In other circumstances than the ones mentioned in b), CUP comparables at the level of any other related entity within the group to which the tested party belongs could also be

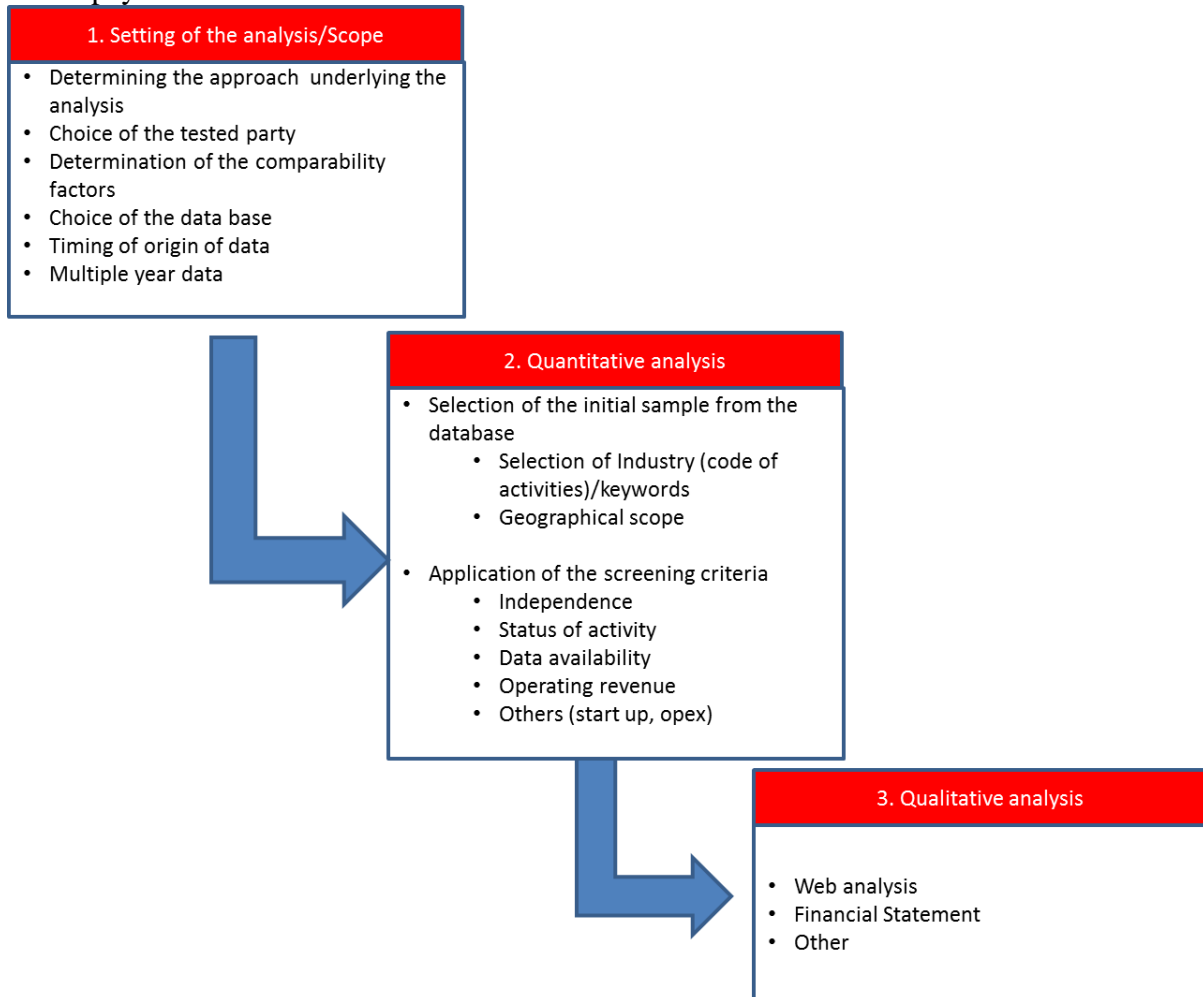
¹⁴ As an example, Non Governmental Members mentioned in their contributions that in some cases (*e.g.* eye glasses wholesalers) for some EU Member States, specific industry codes do not exist whereas in some other cases there are more than one potential industry code (*e.g.* manufacturers of foods). doc. JTPF/009/2016/EN

¹⁵ See Par. 9.135 TPG.

considered. This is subject to the review of the five comparability factors and possible adjustments for geographical market conditions or to take into account that the transactions took place at different time periods, which could be considered. Depending on the circumstances, such adjustments may be more feasible and could be justified in more details in such situations.

5.2 Selecting external comparables

17. The following diagram provides an example of current practices observed by both taxpayers and tax administrations:



18. Following the above depicted approach, starting from an appropriate analysis of the controlled transaction, is expected to provide a good basis to reach an outcome aligned with the substance. In detail, the following recommendations should be followed when performing such a search:

Recommendation 5:

Step 1- Setting of the analysis/Scope

- a) To ensure objectivity of the process, the analysis set-up and the approach taken should be documented respectively by the taxpayers when preparing and making the search for comparables and by the tax administration when they challenge it or make a new search.

Step 2- Quantitative analysis

- b) Quantitative criteria¹⁶ should be applied in the search process of external databases in order to process and filter potential comparables (particularly, by using automatic query-based searches to apply these quantitative criteria, e.g. a Boolean query search based on industry codes, potentially involving inclusion keywords and/or exclusion keywords etc. ensure transparency in the process).
- c) Turnover thresholds should be applied based on facts and circumstances of the tested party (and should be justified accordingly as part of each comparable search).
- d) Comparables with consolidated accounts, i.e. those having subsidiaries, should not automatically be excluded at the stage of the quantitative analysis on this sole ground (for the subsequent qualitative analysis see Step 3 below).
- e) As a starting point for the quantitative analysis a general independence test with no shareholder having an ownership percentage (direct, total or calculated total) over 50 %, should be applied¹⁷ (for the subsequent qualitative analysis, see Step 3 below).
- f) Potential comparables with extreme results should be analysed and possibly excluded. In particular, if the functional and risk analysis of the tested transaction concludes to a low risk profile of the tested party, potential comparables being in a recurring loss position or extreme high profit position may be excluded. On the other hand, loss-making companies should overall not be rejected from the sample, based on this sole ground.
- g) Publicly available accounts from listed companies may contain information relevant in the comparability analysis and should not be excluded as a source for comparable information for this sole ground.
- h) The comparison of certain ratios of balance sheets/P&L account items of the tested party ('diagnostic ratios') with those of potential comparables can give valuable input to the comparability analysis, e.g. to test transactions involving services providers¹⁸, contract manufacturers¹⁹ and R&D contracts²⁰. In practice, in some situations where there are a lot of data left in the set of comparables, defining diagnostic ratios by looking at certain ratios of the tested party and checking how the potential comparables match these ratios of the tested party, could help to further refine the set. These ratios should therefore be practiced

¹⁶ See also Par. 3.43 TPG.

¹⁷ Most Member States confirmed that a %-based indicator reflecting a maximum share of interest owned in subsidiaries is practiced, the actual ratio considered in EU28 ranging between 20% and 50%. Applying a common approach in this respect would be particularly useful in case of joint-audits and dispute resolution.

¹⁸ E.g. based on use of indicators such as the Level of inventory, the level of property, plant, equipment (PPE)

¹⁹ E.g. excluding companies with ratios such as R&D/ Sales or Intangible/Balance sheet exceeding a certain percentage.

²⁰ E.g. excluding companies with a ratio PPE & Equipment/Sales or total Balance sheet or whose ratio Inventory/sales exceed a certain percentage.

and taken into account when properly applied. The terms and conditions under which they are applied should be documented. In the circumstances described in paragraph 3.57 of the TPG, statistical tools may further help to enhance the reliability of the analysis.

Step 3- Qualitative analysis

- i) A complementary manual and qualitative analysis should be performed after the quantitative review using all information sources. Potential comparables for which no public information (e.g. financial statements, company reports or website) is available should generally be excluded.
- j) The qualitative analysis relies on judgement which needs to be properly documented. It can lead to the exclusion and/or confirmation of some potential comparables.
- k) A detailed independence test should be applied in the qualitative analysis taking into account factors like actual control or the ownership structure in the year to which the relevant data relates. Potential comparables for which relevant information cannot be obtained should be excluded.
- l) Comparables with consolidated accounts remaining in the set of potential comparables which is subject to the qualitative analysis should only be accepted if it can be demonstrated that the comparability criteria are met.

5.3 Processing and interpreting external comparables

19. Beside issues dealing with comparability adjustments (see section 6), contributions from the JTPF Member States and from Business and Academia Members laid the emphasis on (i) the use and interpretation of the range through statistical tools and (ii) the treatment of multiple year data, as areas for which converging guidance would be useful. The contributions also confirmed that the interquartile range is a statistical tool which is commonly used in the EU for narrowing a range.

Recommendation 6:

As regards practice related to the **use of ranges**:

- a) Defining a minimum or maximum number of comparables to be included in a range should not be required. The possibility to accept one or two comparables only should not generally be excluded (e.g. when applying the CUP method or if the comparability factors are fully met). However, it may be the case that, while every effort has been made to exclude points that have a lesser degree of comparability, what is arrived at is a range of figures for which it is considered given the process used for selecting comparables and limitations in information available on comparables, that some comparability defects remain that cannot be identified/or quantified and therefore not adjusted²¹. This can happen particularly in cases where potential comparables are derived from a database search. In such cases, if the set of data contains a sizable number of potential comparables, it is common practice in the EU to narrow the range.
- b) The full range should generally not be excluded where the range comprises results of equal and high reliability as regards all the comparability factors. On the other hand, if

²¹ Paragraph 3.57 TPG

such a range of figures is considered too broad, using statistical methods to ensure the reliability of the selected benchmark is a common practice.

- c) In cases where taxpayer and tax administrations agree that statistical tools like the interquartile range have correctly been used to enhance the reliability of a range, every point situated in the narrowed range should be considered as being arm's length and no adjustment should be made if the relevant conditions of the controlled transaction are within that range.
- d) If the relevant conditions of the transaction fall outside the range asserted, an adjustment should be made to a point within the arm's length range. A thorough analysis of all relevant facts and circumstances should be performed by both the tax authorities and the taxpayer in order to decide which specific value within the range should be selected for the purpose of the assessment. If no reasons for another point in the range can be justified by the taxpayer or the tax administration, the median of the range should be considered as a reference point.

As regards practice related to the **use of multiple year data**:

- e) In most cases multiple year data may be used to better understand the controlled transaction and provide useful information on the comparables. In this respect the effect of business and product/intangible life cycles or anomalies in third party information would need to be considered to determine the applicable period or even warrant consideration of a multiple year data. The approach taken for applying multiple year data should be used consistently. A consistent approach taken for applying multiple year data should be used and recognised by both taxpayers and tax authorities. Changes to the approach taken and the underlying reasons should be explained. Complete and accurate data should be available for the whole period.
- f) The use of averages may also improve the reliability of a range²².
- g) As regards the data considered in a multiple year analysis, comparables should not be excluded for the simple reason that they report losses in a limited number of years covered by the analysis.
- h) The time period covered by a multiple year analysis will finally depend on the facts and circumstances of the case and often includes a time period of 3-5 years but should at a minimum cover 3 years.
- i) In a multiple year analysis, information²³ which is available at the time of transaction should be used and the principles of transparency, proportionality and consistency respected. An aspect to be considered when setting the price at the time of the transaction²⁴ is the delay of availability of information on third party transactions.

²² See Par. 3.79 TPG.

²³ The term 'information' in this recommendation is not limited to information on comparable transactions but also covers information on economic and market changes that may have occurred between the year the comparable data refers to and the time of the transaction.

6. Specific aspects of comparability adjustments

6.1 Observation in practice:

20. In the contributions from Business and Academia and Member States on comparability adjustments, the following comparability adjustments are often mentioned:

- a) Working capital adjustments (related to account payables, account receivables and inventories in particular). The Annex to Chapter III TPG contains an example of such a working capital adjustment.
- b) Accounting adjustments. Most of the accounting adjustments deal with foreign exchange difference adjustments or local/international standards of financial reporting and/or treatment for income tax purposes.
- c) Market adjustments related to volume of sales, terms and conditions of sales and payments, credit terms.
- d) Other types of adjustments, *e.g.* balance sheet adjustments and asset intensity adjustments.
- e) Risk related adjustments, particularly linked to the how the potential comparables include the same level of risks and management of risks²⁵.

Within the EU the adjustments mentioned in b) – e) above are rarely observed in practice. There is an interest at the JTPF to further explore such adjustments as regards their exact definition, reasonableness, and if considered reasonable, their functioning and the aspects to be considered for their application and reliability.

6.2 General aspects to be considered for comparability adjustments

21. Following the TPG²⁶, comparability adjustments should be considered if (and only if) they are expected to increase the reliability of the result. Whether comparability adjustments should be performed (and if so what adjustments should be performed) is a matter of judgment that should be evaluated in light of costs and compliance burden. A further aspect to consider is the quality of data subject to the adjustment. While a high degree of detailed information can be expected for the controlled transaction, the information on uncontrolled transaction, especially on external comparables may be limited and consequently limiting the possibility for accurate adjustments.

Recommendation 7:

Adjusting potential external and internal comparables should be considered only at the last stage of the overall analysis of comparable company data before the summary of results, be consistent with the former steps²⁷ and should meet the following criteria:

²⁵ See par. 1.73 TPG, regarding risks such as strategic risks or marketplace risks, infrastructure or operational risks, financial risks, transactional risks, hazard risks.

²⁶ See Par. 3.50, TPG.

²⁷ Following thus an « end-to-end approach », see Recommendation 1 b) above

- a) Should not be applied to unsuitable comparables, *i.e.* the comparable data obtained should be the result of a proper selection, screening and filtering of potential comparables. It is generally not possible to adjust for large differences in balances sheets, assets and risks as those differences would rather suggest a different function asset and risk profile of the tested party.
- b) Should be kept as clear as possible and applied only if comparability is improved. The general principles of quality, transparency, consistency and proportionality²⁸ apply.
- c) If comparability adjustments are considered appropriate under the facts and circumstances of the case, it should be explained which conditions have a definite and reasonably ascertainable effect on the price (profit), how they affect the price and how the comparable(s) was (were) subsequently adjusted. In case some conditions are not evaluated as materially affecting the comparison²⁹, it should be explained how the conclusions were arrived at.
- d) Should generally be applied at the level of the benchmarked sample. It should, however not generally be excluded for the tested party. A limited number of corrections should be applied, also to avoid in practice correcting twice the same issue through different adjustments or accounting twice a difference, *i.e.* when setting the screening criteria and when considering the adjustments³⁰.
- e) Comparability adjustments leading to a significant change of results should indicate a review of the preceding steps of the comparability analysis,
- f) Should be reasonably accurate³¹ and fit with the overall approach, as initially set up with reference to the properly delineated transaction ("end-to-end approach").
- g) Should be properly documented.

7. State of play and way forward on pan-European comparables

22. The following provisions of paragraph 3.35 of the TPG which refer to the use of foreign and non domestic data for comparable searches are relevant: *"Taxpayers do not always perform searches for comparables on a country-by-country basis, e.g. in cases where there are insufficient data available at the domestic level and/or in order to reduce compliance costs where several entities of an MNE group have comparable functional analyses. Non-domestic comparables should not be automatically rejected just because they are not domestic. A determination of whether non-domestic comparables are reliable has to be made on a case-by-case basis and by reference to the extent to which they satisfy*

²⁸ See recommendation 1 b) above

²⁹ See in this respect TPG 1.40: "Where there are differences between the situations being compared that could materially affect the comparison, comparability adjustments must be made, where possible, to improve the reliability of the "comparison".

³⁰ For illustration, examples of loan databases are sometimes mentioned to observe that several of the possible comparability factors in a loan agreement can be strongly correlated and that to make additive adjustments for each of them could be to double or treble count what was essentially the same adjustment

³¹ For illustration, in the framework of applying the CUP method see par. 2.15 and 2.16 TPG.

the five comparability factors. Whether or not one regional search for comparables can be reliably used for several subsidiaries of an MNE group operating in a given region of the world depends on the particular circumstances in which each of those subsidiaries operates”.

23. The TPG also refers in this respect to paragraphs 1.112 and 1.113 (ex-paragraphs 1.57-1.58) regarding market differences and multi-country analyses. On this basis, the use of non-domestic data may be appropriate in the case of a MNE performing similar transactions in several countries where the economic circumstances in these countries are in effect reasonably homogenous. Consequently, in situations where conditions set forth by the above-mentioned paragraph 3.35 of the TPG are met, a case-by-case approach prevails in the EU and using non-domestic data will depend on (i) the extent to which the comparability factor matters (taking into account the transfer pricing method used) and (ii) whether the search is based on a market which can be considered being reasonably homogenous.
24. The EU Code of Conduct on Transfer Pricing Documentation (“EU Transfer Pricing Documentation” (EU TPD)) adopted by the European Council on 27 June 2006³² states also the following as regards comparable searches using pan-European databases:
- Member States should evaluate domestic or non-domestic comparables with respect to the specific facts and circumstances of the case. For example, comparables found in pan-European databases should not be rejected automatically. The use of non-domestic comparables by itself should not subject the taxpayer to penalties for non-compliance.*
25. In some Member States, establishing the lack of local independent comparable data is a pre-requisite for using pan-European databases. In these situations, the notion of "local independent comparables" refers to country-specific data but can also include "regional" data. As an illustration the Visegrad region, the Baltic Countries, and the Scandinavian countries are mentioned as examples of practices where regions were considered as appropriate sources for regional comparables.³³

Draft Recommendation 8:

- a) In practice, conducting a pan-EU comparable search in accordance with the OECD TPG requires to refer to the relevant geographic market³⁴, which generally includes the territory in which the MNE operate as long as it is homogeneous. Therefore, when using foreign or pan-European data, taxpayers should document the reasons underlying the choice of the region on which his comparable search is based including the extent to which he considers that the economic circumstances matter for the comparable search.
- b) When there is a lack of local independent comparable, some practices may be further considered to define a relevant geographic market: as an example, a majority of Member

³² Code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD) (2006/C 176/01) [http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:42006X0728\(01\)&from=EN](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:42006X0728(01)&from=EN)

³³ See doc. JTPF/016/2016/EN page 13

³⁴ See TPG Par. 1.112 and 1.113.

States conduct data searches on similar functions and assets if no comparable can be identified when screening on product comparability³⁵. Some criteria which can characterize market specificities, e.g. similarities in labour cost structures or GDP per capita, could also be useful to define a relevant geographic market on a case-by-case basis.

8. Assessing the reliability of the comparability analysis

26. The review on the use of comparables in the EU showed a broad variety of potential sources for obtaining information on comparable transactions in the EU with a high level of detailed information. However, whether the use of comparables in the EU will finally result in a reliable outcome for a case under review will depend on the facts and circumstances of the case. The analysis further confirmed that a comparability analysis requires judgement by the reviewer at various stages of the process. The differences in underlying data and the need for judgement may create a degree of subjectivity of a comparability analysis.
27. Some sources mention that a better understanding of the value creation, i.e. of the wider generation of value by the MNE group to which the tested party belongs, may contribute to increase the reliability of a comparability analysis³⁶ either by supporting the factual and functional analysis, or as a tool for assessing the reliability of the comparability analysis.

³⁵ In the survey conducted by the JTPF 18 MSs have mentioned that they consider a research based on function rather than products as acceptable in the absence of acceptable comparables.see document JTPF/013/2016/EN, question 4

³⁶ See par. 1.36 TPG