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SUMMARY RECORD OF THE TWENTY-SECOND MEETING OF THE EU JOINT TRANSFER PRICING FORUM

held in Brussels on 5th June 2008

1. ADOPTION OF THE AGENDA (DOC. JTPF/013/REV1/2008/EN/FR/DE)

The revised agenda was adopted. The Chair reminded members that the current mandate was nearing completion and he encouraged continued efforts to secure clear outcomes from the work programme. In particular considerable progress had been made on new recommendations relating to the Arbitration Convention and the JTPF should concentrate on adopting a report on this topic by the end of the mandate.

2. DISCUSSION PAPER ON CENTRALIZED INTRA-GROUP SERVICES (DOC.JTPF/001/2008/EN AND DOC. JTPF/014/REV2/BACK/2007/EN, DOC. JTPF/022/BACK/2007/EN, DOC. JTPF/012/BACK/2008/EN INCLUDING AN EXCEL FILE)

The Chair opened the discussions with a statement that all members agree that the costs of intra-group services rendered have to be deducted; the only question is "where": where they have been provided or enjoyed. All members supported the statement.

The MS` vice chairman explained that this topic was discussed for the first time during the pre-meeting. The document achieved a good balance between MS and Business interests; the documentation chapter was felt to be of high importance and it would be useful to clarify to what extent the EUTPD already covers documentation requirements for services; additional examples of stewardship and shareholders activities to provide further clarity on principles to be applied may be useful , however, the group did not think it was realistic to come with new or

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updated definitions; costing issues were also viewed as important; the risk assessment section of the document including a discussion on the opportunity to have trigger points was considered important. Whilst, at this stage of discussions, a similar prioritization exercise to that presented by Business was difficult for Member States the sub- group tried to identify which topics could usefully be discussed first. Questions 5 & 6 (develop examples on shareholder and stewardship expenses) and 3 (what is a service and what facts should be considered – documentation issues) & 9 (deepen the analysis and provide more guidance of when a mark up is acceptable) introduce some basic principles on what is a standard (basic) or routine service versus non standard (basic), low/high risk, "benchmarkable" services and documentation requirements (hereafter called standard service).

One tax administration explained that they fully support the topic and that their contribution was based on their experience of this issue within MAPs. Often where no clear documentation and justifications are available the auditor does not feel comfortable with costs claimed. In that scenario long discussions frequently take place on the justification of a particular service. Similar discussion may then take place with other Member States in separate MAP proceedings but essentially regarding the same service and available evidence. The JTPF should aim to develop a common approach with standard criteria to facilitate more effective MAP resolution. It was further emphasised that the JTPF was geared towards finding pragmatic solutions to the implementation of OECD guidelines and as issues around services presented practical rather than theoretical issues this was an area well suited to the aims of JTPF.

One tax administration explained that in their opinion this topic is one for OECD and the JTPF is not the right place to discuss it. Others took the opposite view. The Chair noted that the presence of observers from the OECD was a guarantee that our guidance/recommendations would not conflict with the OECD guidelines.

Initial exchanges of views took place wherein it was clarified that everybody agreed the principle that the cost must be deducted for business purposes somewhere. The main issue though was the actual allocation of costs. However this did not prevent MS applying their national rules to prevent some deductions or accept a limited deduction of costs as the JTPF was not in a position to change domestic law.

The Business Vice-Chair expressed appreciation that Member States accept all costs should be deducted somewhere and noted the importance thereof for the debate.

One Business member suggested that internal and external costs should be treated equally. He gave the example of a French consultant working for a German company. The consultant's invoice will include his travel and accommodations costs that will not be limited for tax purposes; on the other hand if we take the same task provided by an internal expert generally the tax administrations will limit the deduction of several costs.

Another Business member remarked that since costs are to be allocated somewhere we may need guidelines regarding such allocation; this would simplify matters.

A wide ranging discussion ensued brought to a conclusion by the Chair reminding the members that the overall aim was to provide the Secretariat with enough material to prepare a first working document. In response to that reminder it was

proposed and agreed to focus the discussions on paragraph 38 and 56 of the document and by concentrating on perceived low risk activity help clarify the principles to be applied more widely.

On that basis discussions continued on:

1) Defining a Standard Service:

A brief discussion took place on the assessment of what is a standard service .One MS stressed that no general definition could apply and should always be on a case by case basis. It was finally concluded that the aim would be to develop a set of principles applicable in 90% of cases.

One MS suggested that an indicator of a standard service (e.g. accounting services) was that it was not linked to the core business of the company whereas high value adding services probably with high risk would be linked to the core business. The OECD observer said that she could see some logic in this approach.

One Business member made the link between the works of the JTPF to that of the IRS regulations governing "intercompany service transactions" including a cost safe harbour called the Services Cost Method (SCM). One of the requirements for a service to qualify the SCM was that the taxpayer must reasonably conclude in its business judgment that the service does not contribute significantly to key competitive advantages, core capabilities, or fundamental risks of success or failure of the taxpayer's business. The Business member suggested that this principle could be identified as a best practice and applied to standard services.

Another Member State cautioned against accepting that a range of services provided were in fact a series of individual standard services where in fact it may be the case that, cumulatively, a high value service was provided.

The discussion also touched on: defining when a service had been provided; difficulties in applying CUPS; specific shareholder/stewardship issues; when a mark up may not be appropriate and the value of a risk based approach to services provided.

The Chair concluded the discussion by thanking the group for providing thoughts to assist the Secretariat in developing a working document for the forum.

2) Documentation and Evidence

A second important passage of discussion was on which kind of documentation could be requested for these standard services in establishing the provision of a service at an arm's length price. The discussions focused on paragraphs 56 to 58.

One tax administration supported that a requirement to provide the service contract could be replaced by the provision of any document that provided evidence of an agreement or commitment to provide a service. Additionally, his experience showed the worth of timesheets as an evidential base was limited. A better source may be an analysis based on cost accounting evidence. These views were supported by Business members.

A consensus emerged to examine in the working document to what extent the EUTPD already sufficiently dealt with the specific documentation requirements for intra group central services.

The Secretariat would reflect these contributions in the forum's working document

3) Cost Base and Cost Plus

The third topic for discussion was the cost base and cost plus. The Chair explained it may be considered premature to open discussions on this particular topic at this stage. It should be kept in mind , however, these were preliminary discussions and any emerging themes need to be reconsidered in the light of what the group eventually is considers to be a standard service.

From the written contributions it can be concluded that in practice cost plus between 3% and 10% was a common outcome.

One tax administration felt that it should be remembered that the taxpayer should always start by trying to find a CUP. Business members observed that in practice it is never possible to find a right CUP.

If cost plus were found to be appropriate an arm's length assessment of the cost base was even more important as the "plus" that may be applied

Two tax administrations considered that we were developing a kind of safe harbour rule linked to a range and they could not agree with this approach.

The Secretariat explained that any agreement to apply a specific range should respect the following principles to be in line with the OECD Guidelines:

- Taxpayers and tax administrations must have the possibility to argue against the application of the range

- The range should be arm's length established by conducting an appropriate study to evidence the range by comparables

- The agreed range should be updated on a regular basis (e.g every 3 years).

The OECD observer provided the following clarifications on the so called "safe harbour".

It is true that the Guidelines are relatively negative towards safe harbours because the latter may create a risk of double taxation or of less than single taxation, and could deviate from the arm's length principle. However, if safe harbour rules can be designed that do not breach any of those principles; there might be some value in a careful application of pre-defined methods and ranges for some low value adding, limited risk transactions. In trying to simplify the issue of central services by taking a more flexible view of the transfer pricing guidance in this area, the following considerations should be kept in mind:

- Countries may want to apply a risk assessment approach in transfer pricing in order to balance a theoretically sound application of the arm's length principle with the compliance and administrative burden created.

- In applying such an approach to arrive at a possible common safe harbour rule, it would be important to agree on the following: definition of the services covered by the safe harbour rule; how the safe harbour rule will be implemented (e.g. will compliance with the safe harbour rule mean less risk for the taxpayer of being audited on its service transactions; and / or less documentation requirements; and / or no transfer pricing adjustment; etc); what method will apply and how (e.g. definition of the cost and definition of the plus if a cost plus method is used); details of how the approximation of the "arm's length" range used in the safe harbour rule is determined and is to be updated.

- The arm's length principle relies on an analysis of the facts and circumstances of each specific case. It therefore follows that taxpayers that do not want to subscribe to a safe harbour rule remain free to demonstrate that a service charge that may be outside of a particular safe harbour range is nevertheless arm's length.

One tax administration fully supported the Business and OECD analysis and considered that tax administrations should concentrate their audit resources on more important topics. The range in paragraph 41 was one they recognised but noted the qualifying language of that paragraph which left the arm's length principle intact.

To further progress this work programme item it was concluded that MS discuss further the topic at a sub-group meeting together with a back to back meeting with a Business members sub group to be held in September. Malta offered to host the event.

3. PRESENTATION AND DISCUSSION OF THE DOCUMENT FROM THE SUB-GROUP ON TRIANGULAR CASES. (DOCUMENT FROM THE SUB-GROUP ON DRAFT RECOMMENDATIONS FOR EU TRIANGULAR CASES AND DOC.JTPF/008/BACK/2008/EN)

Stefaan De Baets who hosted and chaired the sub group meeting held in Brussels on 29th April made an oral presentation of the draft reports on EU and non EU triangular cases.

A business member commented that the Arbitration Convention was an extremely valuable procedure. The forum must be vigilant in ensuring its work did not detract from that value particularly in the area of defining time limits.

The JTPF invited the sub-group to continue the discussions and to present its report on EU triangular cases during the next plenary meeting. To that extend the final sub-group report will be distributed about mid-July and the Chair invited all members to send their comments by the end of September.

4. ISSUES RELATED TO THE ARBITRATION CONVENTION:

4.1 Discussion paper on draft JTPF recommendations related to the interpretation of some provisions of the Arbitration Convention (doc.JTPF/002/REV1/2008/EN).

1. Serious penalties

The recommendation was agreed by the Forum.

The Secretariat reminded MS that the extension of the arbitration convention to Bulgaria and Romania should be adopted in June at the Council. MS were invited to send where appropriate revised unilateral statements. So far only Spain has sent a revised statement to take into consideration a modification of the national law.

2. The setting-up of the advisory commission

The tax administration member withdrew their question. The recommendation was agreed by the Forum.

3. Independent persons of standing

On the competency aspect the Business vice-chair explained that the Business community has some concern in limiting the scope of independency of the parties from companies alone and by consensus it was agreed to also include tax administrations as well. The recommendation was agreed by the Forum.

4. Date of admissibility of cases

The Swedish proposal was agreed by consensus**.** The recommendation was agreed by the Forum

The Chair concluded that the above recommendations included in this document were adopted. He invited the Secretariat for the next meeting to include recommendations on interest charges in the context of Mutual Agreement Procedure and thin capitalization in a revised document-item 2.3 of the above document- next section refers.

4.2. Discussion paper on draft JTPF recommendations related to interest charges in the context of Mutual Agreement Procedure (doc.JTPF/003/2008/EN and doc.JTPF/010/BACK/2008/EN).

The Chair opened the discussions by inviting some MS to clarify whether they could reimburse interest in the context of MAP proceedings. Finland and Greece confirmed that they both charge and reimburse interest. Romania needed to check their current practice. France and Luxembourg do not charge interest.

Portugal explained that they can only reimburse interests for domestic disputes. The Business Vice Chair asked that this point be further clarified as it could constitute a discrimination.

After the February meeting MS were invited to confirm whether their tax systems reimbursed interest incurred on the amount of taxes to be repaid to a taxpayer at the end of a MAP procedure or under the Arbitration Convention. From the table it could be concluded that a large majority of MS reimburse interest relating to the amount of taxes to be reimbursed to a taxpayer at the end of MAP: 18 MS can (including the answer from Romania to be checked); 2 MS (France and Luxembourg) do not charge or reimburse interest during MAP; 2 MS can reimburse interest on a case by case basis (Spain and Czech). 5 MS cannot: Bulgaria, Estonia, Ireland, Lithuania, Portugal.

Ireland made a statement that they couldaccept a recommendation to "not charge or collect interest which would otherwise be due from the date of initiation of the MAP to the date of conclusion of the MAP".

Germany law generally requires that interest is either charged or reimbursed so they could not introduce a "no charge" process but they are open to deal with the issue as part of the MAP procedure on a case by case basis

The Chair invited the Secretariat to prepare a recommendation taking into consideration the three reported situations concerning reimbursement of interest.

4.3. Updated table on thin capitalization questionnaire (doc. JTPF/018/REV2/2007/EN) and Secretariat's discussion paper on thin capitalization (doc. JTPF/005/2008/EN) and the Italian and Dutch Contributions (doc. JTPF/009/BACK/REV1/2008/EN).

The Chair tried to sum up the table:

R*educes the rate of interest paid on an inter-company loan (Q1)*, 25 yes 2 without answers (Romania and Slovenia); *reduces the amount of a loan on which interest is paid because of the limited borrowing capacity of the debtor (Q2*), 9 yes; 4 yes on a case by case; 7 no specific rules; 3 without answers 4 NO: Latvia, NL, Poland, Portugal; *reduces the amount of a loan on which interest is paid because the debt would not have existed for reasons unrelated to borrowing capacity. (Q3),*8 yes; 5 Yes on a case by case; 6 no specific rules; 4 without answers,4 NO: Latvia; NL, Poland, Portugal; *reduces the amount of a loan on which interest is paid because the debt exceeds a thin cap ratio (Q4),*6 yes, 6 yes on a case by case, 6 no specific rules, 3 without answers, 6 NO: Finland, Latvia, NL, Lithuania, Poland, Portugal; *Finally, please say whether your view would differ if the actions above had been taken by another tax administration and you were being asked to give a corresponding adjustment. (Q5),* 6 yes (The other answers introduce further considerations).The Chair concluded that from these answers we can consider that a large majority of MS do consider the thin cap issues are covered by the AC.

The tax administrations' vice Chair provided a summary of the conclusions from the pre-meeting: at the OECD level it has never been possible to conclude this topic (no agreed definition, no agreement whether thin cap rules are covered or not by the arm's length principle) and therefore MS considered the only possible outcome is the updated table.

Several Business members fully disagreed with that statement and provided the following legal arguments:

The question whether something is governed by the Arbitration Convention is decided in Art. 1 together with Art. 4 of the Convention. Art. 1 reads that the Convention shall apply to profits which are included in the profits of two enterprises contrary to the principles of Art. 4. Art. 4 states with respect to those principles that the Convention is applicable if conditions are imposed which differ from those of independent enterprises. This is usually known as the arm's length test. Therefore, the question of the right capitalization of a company is an issue governed by the Arbitration Convention if this issue is a question of the arm's length test. There are several arguments to support the view that this is indeed a question of arm's length behavior.

Almost all governments and existing transfer pricing rules consider the question of the right amount of interest (e.g. is 5 % or 6 % the right rate?) as a question of the arm's length test. Clearly on capital markets there is a correlation between the ratio

of capital and debt of a company and the arm's length interest rate (high debt ratio = high interest rate). Therefore, the question of the right interest and the right debt equity ratios are both issues of the arm's length principle and cannot be reasonably distinguished. They are different sides of the same coin.

This aspect is also recognized by some country legislators who accept their specific capitalization rules will not apply if a taxpayer can show that the financing is obtainable from third parties under similar conditions.

Also, the ECJ in the Test Claimants case has found that capitalization rules which requalify interest into dividend payments are only allowable under the freedoms if the amount of interest exceeds that amount which the parties would have agreed upon if no special relationship between them had existed. In other words, the re-characterization rule is only permissible insofar as it requalifies interest which exceeds the interest under the arm's length test. This seems to be in line with the arguments put forward by the member states which have filed briefs in the Test Claimants case. They have argued that there was no violation of the freedom of establishment because the re-characterization rules at issue were part of the relationship between the states covered by Art. 9 of the OECD Model Convention. Hence, it can be concluded that those member states also consider the question of appropriate capitalization as a question of the arm's length test.

In addition, No. 3 of the Commentary to Art. 9 of the Model Convention and the example in No. 1.37 of the OECD Transfer Pricing Guidelines state that thin capitalization rules only do not violate the principles of Art. 9 if they result into profits which would have accrued in an arm's length situation.

Taking all the above together they believe it is clear that the question of the right capital of a company is a question of applying the arm's length principle and therefore should be covered by the Arbitration Convention.

These arguments were not accepted by all MS.

Finally all MS tax administrations' members were invited by the Chair to answer whether they consider that the arbitration convention can be applied to thin cap issues. (modification requested by Italy, the Netherlands and UK).

The answers were the following:

Member State	**Preliminary Answer**
Austria	YES if based on the application of the arm's length principle
Belgium	In principle YES
Bulgaria	**?**
Cyprus	YES if based on the application of the arm's length principle
Czech Republic	Yes if related to interest rate
Denmark	YES
Estonia	YES

Finland	YES in principle
France	YES if based on the application of the arm's length principle
Germany	YES if based on the application of the arm's length principle
Greece	To be checked
Hungary	NO because they have thin cap rules
Italy	NO
Ireland	In principle YES but Ireland has no thin capitalisation legislation
Latvia	In principle YES if based on the application of the arm's length principle
Lithuania	In principle YES
Luxembourg	
Malta	YES if based on the application of the arm's length principle
Netherlands	NO
Poland	They have no thin cap rules but Yes only if related to interests
Portugal	NO
Romania	?
Slovak Republic	Yes if based on the application of the arm´s legth principle
Slovenia	YES in principle but limited to the interests
Spain	YES because based on article 4 of the AC
Sweden	In principle YES but there is no common thin cap definition
United Kingdom	YES

Some tax administrations suggested basing the proposal to the Forum not on "thin cap" but on the wording of article 1 and 4 of the Arbitration Convention.

The Chair invited the Secretariat to prepare a draft recommendation along these lines for further discussions.

4.4. List of independent persons of standing eligible to become a member of the advisory commission (doc.JTPF/010/BACK/REV10/2005/EN): lists from new Member States and availability of CVs.

The Chair reminded that CVs are still missing for Belgium, France, Luxembourg, Portugal and UK.

Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Romania and Slovenia are in the process to select the members**.**

4.5 Table on the application of Art. 7(3) of the AC (interaction between MAP and judicial appeals) (doc. JTPF/024/REV2/BACK/2007/EN).

The Chair explained that the table will be used during the Fiscalis seminar on MAPs and the Forum would reexamine the issue in November and could prepare some conclusions/recommendations for the JTPF.

4.6 Reports from the Member States on the implementation of the Code of Conduct for the effective implementation of the Arbitration Convention. (doc.JTPF/014/BACK/2008/EN and doc.JTPF/015/BACK/2008/EN)

The Chair invited the members to have a look on the Secretariat's document summarizing the most relevant suggestions and he invited the Secretariat to include some considerations in the document including recommendations on the AC.

4.7 State of play of the implementation of the Code of Conduct related to the Arbitration Convention (doc.JTPF/006/BACK/REV5/2006 February 2008)

It was provided for information only.

4.8 2008 table on the number of pending cases under the AC (doc.JTPF/016/BACK/2008/EN)

Two answers are still missing: Luxembourg and Poland.

5. DRAFT 2007 APA TABLE ON THE AVAILABILITY OF AN APA PROCEDURE (DOC. JTPF/006/REV3/2007/EN)

Missing information from: Finland, Luxembourg and Portugal.

It was agreed that the Secretariat will send the same questionnaire for 2007.

6. ANY OTHER BUSINESS:

6.1 2008 meetings are scheduled on **27/11/08 and on 28/11 morning.**

In 2009 the first meeting should take place at the end of February.

6.2 Documents adopted under written procedure: (summary record)

6.3 Monitoring of the work programme

The Chair summarized the future work by reminding:

- The issue of centralized intra-group services will be discussed by the sub-group in September and the Secretariat will issue a working document in October. We should try to come to some first recommendations for the February meeting.

- On triangular cases the sub group has received a mandate to present its report on EU triangular cases during the next meeting.

- It will not be possible to examine more topics than AC and intra-group services under this mandate. The next meeting should firstly focus on the recommendations for the AC with the aim to adopt final recommendations.

- The Secretariat is asked to provide provisional meeting dates for 2009.

6.4 EUTPD:

The Secretariat will issue a questionnaire to assess the implementation of the EUTPD by tax administrations and by MNEs.