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EU JOINT TRANSFER PRICING FORUM

EXECUTIVE SUMMARY OF THE DELOITTE STUDY ON COMAPRABLE DATA USE IN THE EU AND EUROPE ONE MARKET

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Contact:
Hartmut Förster, Telephone (32-2) 29.55.511
Morgan Guillou, Telephone (32-2) 29.54.146
E-mail: taxud-joint-transfer-pricing-forum@ec.europa.eu

Deloitte.

Deloitte Belastingconsulenten /
Conseils Fiscaux
Global Business Tax
Berkenlaan 8b
1831 Diegem
Belgium
Tel. + 32 2 600 67 00
Fax + 32 2 600 67 03
www.deloitte.be

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Study on Comparable Data used for transfer pricing in the EU

Executive summary

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1. Introduction

This document is based on the full report prepared by Deloitte Belgium with the support of the Deloitte office located in the other EU 28 countries. Its content may not be interpreted as the position of Deloitte, but rather as a fair representation of the transfer pricing landscape in the EU, to the best of the knowledge of the writers of this report and the interviewees. If the report is believed to be fairly representative, it cannot be construed as exhaustive, though.

Information has been gathered through desktop research, data bases analysis and telephone interviews with other Deloitte offices.

2. Internal CUPs: Milestone 1 – 4

The study confirmed that the Internal Comparable Uncontrolled Price ('ICUP') is a preferred option for all the MS, meaning that it is the first place to look for comparable data. However, by contrast, the ICUP tends to be only occasionally used by taxpayers due to lack of data or material differences in the comparability factors, and at occasions, even later dismissed by the tax administrations for a more stringent application of the same reasons.

Among the comparability criteria, it is believed that ICUPs involving the parties engaging in the considered related transaction would generally offer a better level of comparability than ICUPs situated anywhere else within the considered group (supposedly, better comparability in level of market, product or service traded, market, …).

Further, ICUPs may originate from recently acquired companies that were in the recent past dealing as unrelated parties. However, it is usually so that such ICUPs shelve life may be rather limited, making a systematic application of such ICUPs throughout the group and across time quite tentative.

With regard to the use of ICUPs, here are the preliminary findings, organized by Milestone.

2.1. Milestone #1: Use and availability of ICUP data within EU-28

Scope: For the 28 MS it is verified whether or not the tax authorities accept and apply internal comparables ('ICUPs') for the CUP method.

The ICUP appears to be a preferred method by the majority of the tax authorities. However, the number of available ICUPs cases appears to be very limited. The ICUPs have been used by MS mostly for goods transactions and loans. It appears less common for IP and services transactions. These findings on the use of ICUPs appear to be mostly based on informal internal questioning. Most companies do not seem to use ICUPs databases systematically. If a good ICUP is available, most MS will make use of the adjustments to improve comparability, especially for the contractual terms and characteristics of the goods / services. Typically, the use of an ICUP is only rejected by the tax authorities on the basis of comparability deficiencies. If the adjustments are too complex, MS tend to move to another method rather than making comparability adjustments.

It was reported in the survey that comparability can be achieved by a reasonable number of adjustments like for differences in, e.g.:

- Product quality;

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- Transaction volume;

- Contractual terms;

- Geographic market;

- Embedded intangibles;

- Foreign currency risks.

Applicability of ICUPs

Legend: Not seen · Occasionally seen · Commonly seen

Q1

Applicability of ICUPs heatmap (Q1) for 28 Member States (1. Austria, 2. Belgium, 3. Bulgaria, 4. Croatia, 5. Cyprus, 6. Czech Republic, 7. Denmark, 8. Estonia, 9. Finland, 10. France, 11. Germany, 12. Greece, 13. Hungary, 14. Ireland, 15. Italy, 16. Latvia, 17. Lithuania, 18. Luxembourg, 19. Malta, 20. Netherlands, 21. Poland, 22. Portugal, 23. Romania, 24. Slovakia, 25. Slovenia, 26. Spain, 27. Sweden, 28. UK) across rows: 1. Goods, 2. Services, 3. IP, 4. Loans.

Count summary (#):

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28
Not seen	1	1	1	3	2	2	0	0	1	0	2	0	2	1	0	0	1	2	2	2	1	0	0	1	2	0	0	1
Occasionally seen	2	2	2	1	2	2	3	4	3	3	2	2	1	0	3	1	2	2	2	2	0	2	1	3	1	3	2	3
Commonly seen	1	1	1	0	0	0	1	0	0	1	0	2	1	3	1	3	1	0	0	0	3	2	3	0	1	1	2	0

2.2.   Milestone #2: Legal basis or administrative guidelines

Scope: For each of the 28 MS references / copies have been collected of available documents with the legal basis or administrative guidelines accepting and / or rejecting internal comparables.

The majority of the MS has a legal basis or administrative guidelines for the acceptance of the CUPs in general rather than ICUPs specifically. When there is a legal basis or administrative guidelines available, these usually refer to the OECD guidelines, a translation of the OECD guidelines or they are not very specific.

Legal basis & administrative guidelines

Legend: No · Yes

Q13 & Q15

Legal basis & administrative guidelines heatmap (Q13 & Q15) for 28 Member States (1. Austria, 2. Belgium, 3. Bulgaria, 4. Croatia, 5. Cyprus, 6. Czech Republic, 7. Denmark, 8. Estonia, 9. Finland, 10. France, 11. Germany, 12. Greece, 13. Hungary, 14. Ireland, 15. Italy, 16. Latvia, 17. Lithuania, 18. Luxembourg, 19. Malta, 20. Netherlands, 21. Poland, 22. Portugal, 23. Romania, 24. Slovakia, 25. Slovenia, 26. Spain, 27. Sweden, 28. UK) across rows: 1. Legal basis and 3. Administrative guidelines.

2.3.   Milestone #3: Case law decisions

Scope: For each of the 28 MS, relevant case law decisions have been collected which recognise the use of internal comparables.

A limited number of MS are aware of case law concerning the application of the ICUP. Case law is available in Austria, Belgium, Bulgaria, Finland, Italy, Latvia, Portugal and Spain. In the other MS there is either no case law or a limited number of cases for which no details were available.

2.4.   Milestone #4: Examples & cases of the use of internal comparables

Scope: For each of the 28 MS examples and cases have been provided on the use of ICUPs.

Most MS have generally a preference for the CUPs, including ICUPs. However, often, a good ICUP is not available. Even though ICUPs appears to have been used across transaction types and industries throughout the EU-28, we note higher frequency for (1) products like raw materials or semi-finished products which are standardized and therefore easier to compare and (2) financial transactions. Furthermore, expecting a more prescriptive approach to ICUPs would lead to a higher frequency of their use may be illusory, because the availability of an ICUP is rather facts-dependent rather than regulations-dependent.

3. External CUP: Milestone 5 – 7

With regard to the use of the external comparable uncontrolled price ("ECUP"), here are the preliminary findings, organized by Milestone.

3.1.   Milestone #5: External comparables and CUP method

Scope: For each of the 28 MS, a list of external databases has been provided that can be used for ECUP purposes.

ECUP databases are almost never used for goods transactions with just a few MS making use of databases for services transactions. However, for IP and loans, databases are commonly used, in particular RoyaltyStat, Bloomberg and LoanConnector. We also note that MS with higher TP activity tend to make use of more databases.

Many websites do not specify the availability or not of the independence test. For quite a few databases, especially those related to financial transactions, the data is however deemed as being market data which would mean the independence test is irrelevant.

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The table below provides an overview of the availability of **international databases** and the frequency of usage frequency in the different MS markets to identify ECUP.

ECUP databases

Legend: Not used (white), Occasionally used (light blue), Commonly used (blue)

Q23a + Q24

Database usage frequency counts (Not used / Occasionally used / Commonly used):

ECUP database	Not used	Occasionally used	Commonly used
1. RoyaltyStat	4	3	21
2. ktMine	14	5	9
3. Lexis Nexis	22	5	1
4. RoyaltySource	16	6	6
5. Bloomberg	5	3	20
6. Dealscan	20	1	7
7. LoanConnector	9	4	15
8. Capital IQ	25	0	3
9. ECB	22	3	3
10. Damodaran	20	2	6
11. Euribor.org	26	0	2
12. Lipper	21	5	2
13. Other	24	2	2

Per-country totals (columns 1–28: Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, UK):

#	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28
Not used	5	6	8	12	12	10	9	12	7	6	9	8	8	8	7	9	7	7	13	7	4	8	10	9	11	5	8	3
Occasionally used	6	2	4	1	0	3	3	0	1	0	0	1	1	2	3	0	1	0	0	0	5	2	0	2	1	0	1	0
Commonly used	2	5	1	0	1	0	1	1	5	7	4	4	4	3	3	4	5	6	0	6	4	3	3	2	1	8	4	10

3.2. Milestone #6: Specific firm-level data and intra-firm export prices

Scope: For each of the 28 MS, the use of specific firm-level data and intra-firm export prices by economists as possible external comparables have been investigated.

No MSs have been identified where export prices have been used as a basis for transfer pricing. The reasons were:

- Data is not sufficiently detailed for TP purposes, typically on the goods characteristics, as for customs purposes codes are used for product categories rather than for specific products. Therefore, it appears not possible to clearly identify the goods traded, let alone operate comparability adjustments. For example, when a designer table is being exported, the classification code will identify that it is a table, and that this table is made out of wood. However, the customs declaration does not provide for a more specific description. As such, the custom declaration form will not clarify whether the export price is related to a designer item. Of course, there will be a price difference between a regular table and a designer table. Therefore, it is not possible to drive the price for a particular good based on export prices. Typically, export prices are determined on a case by case basis. As a result, export prices may vary depending on the product, the country of destination, the volume, market evolutions, etc.

- There is no information on the dependence between the transacting parties, whereby intercompany and third party sales are mixed.

- Customs data is not publicly available. Export prices are confidential and they are unknown to the Tax Authorities. There are no databases nor lists available that contain export prices

- Custom prices may be composed of different elements (e.g. cost, overhead cost and profit margin) and / or be situated at different stages of the supply chain.

- There is little interaction between customs and direct tax.

- Keeping track of export prices may create a violation against the principles advocated by the <u>World Trade Organization</u>.

It is also not recommended nor realistic to have databases with export prices, since this would create a significant additional burden on the administration of these prices.

3.3.   Milestone #7: Quality testing of ECUP databases

Scope: For each of the 28 MS, the quality of the external databases which can be used for CUP purposes has been tested.

There are several databases available that are widely used by most MS which are generally large and include market transactions on loans and IP. These databases are regularly updated and are publicly accessible, generally for a subscription fee. Even though most MS use the databases and most tax authorities accept their use, there appears to be room for improvement as some databases do not have the option of performing sufficient screening tests, like the independence test.

4. Internal comparables: Milestone 8 – 9

4.1.   Milestone #8: Availability profit based data

Scope: For the 28 MS it should be verified whether or not the tax authorities accept and apply internal comparables for the Transactional Net Margin Method ("TNMM").

The use of internal comparables under TNMM ('ITNMM') or other profit based methods happens seldomly due to the difficulty of assessing the 'net margin' at transaction level, subjectivity in segmenting accounts, or differences in fact patterns between intragroup and third party functions and risk allocations. However, the ITNMM appears to be helpful, in certain circumstances, to support another method.

Cases considered in which an ITNMM could be used are:

- Production entities selling to dependent and independent entities
- Selling entities buying from dependent and independent entities
- Case of a joint venture (either manufacturer or distributor).

There appears to be no legal bases or case law available to provide additional guidance in any of the MS.

4.2.   Milestone #9: Cases of internal profit based comparables

Scope: For each of the 28 MS, search examples and cases on the use of ITNMM to derive profit margins.

There does not appear to be any case law available where ITNMM were used except for one old case in Poland. If the use of ITNMM can be found in theory as mentioned above, there appears to be very little experience with the use of this approach in practice. Not a single MS has seen a systematic rejection of ITNMM. Only Denmark mentioned a case where ITNMM would have been rejected by the Tax Authorities due to lack of comparability.

5. External comparables and profit-based methods[1]: Milestone 10 – 31

The study suggests overall that the current level of data availability, accessibility, and reliability is generally sufficient and satisfactory in order to conduct comparable studies under the profit-based method (TNMM). That level of general availability allows then selecting, testing and adjusting data on various criteria (e.g. independence test, maturity test, qualitative and quantitative comparability tests).

5.1.   Milestone #10: Overview of the data availability for the whole EU-28 region (2011-2014)

Scope: In this milestone, the search processes and databases reviewed are discussed.

For the overview of data availability, reference can be made to appendix 3. The conclusions of our findings are provided in milestone 13.

5.2.   Milestone #11: Overview of the past availability (2008-2010) of the same data as in milestone #10 for the whole EU-28 region

For the overview of data availability, reference is made to Appendix 3.

5.3.   Milestone #12: Sector overview of the availability of the same data as in milestone #10 for the whole EU-28 region

For the overview of data availability, reference is made to appendix 4.

5.4.   Milestone #13: Indicators / thresholds characterizing the lack or non-availability of data

Scope: An overview is provided of the indicators / thresholds characterising the lack or shortage / sufficient availability of data for each Member State and the whole EU-28 Region.

In general, the use of local databases versus Amadeus or Orbis is not expected to have a material impact on the search result. There could still be some improvements to the textual description of the activities of the companies. The availability of some financial indicators in the profit and loss data is not consistently available in all MS, especially at the Cost of Goods Sold ('CoGS') / Material Cost ('MC') level. Operating expenses are not uniformly characterized and sufficiently detailed. The absence of separate reporting of R&D and marketing expenses is deplored by quite a few MS (see also Milestone 24). It is also noted that the availability of data has consistently increased since 2010.

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[1] Only Transactional Net Margin Method will be assessed as profit–based method.

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The table below shows for the Amadeus database the availability of data in absolute terms for the turnover, net profit and independence test for the period 2011-2014 (companies with sales over EUR 5 million).

#	Country	Number of companies	Turnover				Net profit				Independence test
			2014	2013	2012	2011	2014	2013	2012	2011	
1	Austria	11 568	7 866	9 741	9 481	9 183	4 431	5 853	5 858	5 651	10 558
2	Belgium	14 491	13 243	13 479	13 165	12 611	13 325	13 826	13 789	13 615	10 302
3	Bulgaria	3 994	3 824	3 844	3 700	3 584	3 789	3 801	3 697	3 524	3 715
4	Croatia	2 407	2 269	2 336	2 324	2 239	2 269	2 336	2 324	2 239	1 776
5	Cyprus	369	35	161	247	296	35	162	247	296	226
6	Czech Republic	12 647	7 293	12 424	12 164	11 338	7 293	9 570	10 148	10 259	9 614
7	Denmark	4 927	4 273	4 224	4 145	3 984	4 741	4 674	4 535	4 348	3 585
8	Estonia	1 904	1 723	1 783	1 771	1 743	1 737	1 796	1 788	1 762	1 782
9	Finland	10 632	9 576	9 652	9 309	7 807	8 063	8 271	8 147	7 844	5 810
10	France	87 382	71 701	75 152	75 994	70 410	58 711	66 205	68 921	68 504	66 314
11	Germany	66 776	21 781	55 301	56 247	53 246	8 210	31 944	32 950	31 847	61 088
12	Greece	4 469	3 944	4 215	4 264	4 152	3 944	4 215	4 264	4 152	3 889
13	Hungary	6 879	6 219	6 465	6 480	6 187	6 219	6 491	6 531	6 269	1 308
14	Ireland	4 756	3 434	3 994	3 908	3 728	3 258	3 770	3 693	3 577	4 300
15	Italy	72 535	63 562	68 292	68 606	67 845	63 562	68 292	68 606	67 851	62 419
16	Latvia	2 052	1 848	1 917	1 880	1 803	1 848	1 917	1 880	1 803	1 845
17	Lithuania	2 491	1 793	2 461	2 352	2 337	1 703	2 059	2 049	2 135	1 925
18	Luxembourg	1 555	872	1 253	1 339	1 305	874	1 254	1 342	1 306	1 340
19	Malta	829	105	400	628	737	105	400	628	737	555
20	The Netherlands	11 231	6 381	8 528	8 411	7 801	7 120	9 641	9 660	8 987	8 047
21	Poland	21 203	14 134	18 768	19 185	18 667	14 134	18 785	19 226	18 739	16 106
22	Portugal	9 426	8 327	8 860	8 891	8 773	8 378	8 928	8 955	8 866	8 475
23	Romania	8 035	7 544	7 623	7 658	7 484	7 544	7 623	7 658	7 484	7 446
24	Slovakia	4 911	4 265	4 509	4 609	4 460	4 265	4 324	4 396	4 292	3 769
25	Slovenia	2 239	1 246	2 144	2 148	2 115	1 244	2 146	2 160	2 123	2 042
26	Spain	40 804	30 550	37 417	38 250	37 871	30 562	37 487	38 379	38 095	33 940
27	Sweden	23 713	21 918	22 392	22 231	21 469	20 972	21 453	21 331	20 597	15 555
28	United Kingdom	71 984	59 053	61 823	59 326	55 074	58 970	61 761	59 375	55 288	35 557

It is observed that:

- All data: some MS release very few data points. At first glance, it would usually be a reflection of the size of the economy (e.g. Malta, Cyprus). The largest economies, expectedly release significantly more data points (France, Germany, Italy, Spain, the UK).

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The table below shows for the Amadeus database the availability of data in relative terms for the turnover, net profit and independence test for the period 2011-2014 (companies with sales over EUR 5 million).

#	Country	Turnover				Net profit				Independence test
		2014	2013	2012	2011	2014	2013	2012	2011	
1	Austria	68%	84%	82%	79%	38%	51%	51%	49%	91%
2	Belgium	91%	93%	91%	87%	92%	95%	95%	94%	71%
3	Bulgaria	96%	96%	93%	90%	95%	95%	93%	88%	93%
4	Croatia	94%	97%	97%	93%	94%	97%	97%	93%	74%
5	Cyprus	9%	44%	67%	80%	9%	44%	67%	80%	61%
6	Czech Republic	58%	98%	96%	90%	58%	76%	80%	81%	76%
7	Denmark	87%	86%	84%	81%	96%	95%	92%	88%	73%
8	Estonia	90%	94%	93%	92%	91%	94%	94%	93%	94%
9	Finland	90%	91%	88%	73%	76%	78%	77%	74%	55%
10	France	82%	86%	87%	81%	67%	76%	79%	78%	76%
11	Germany	33%	83%	84%	80%	12%	48%	49%	48%	91%
12	Greece	88%	94%	95%	93%	88%	94%	95%	93%	87%
13	Hungary	90%	94%	94%	90%	90%	94%	95%	91%	19%
14	Ireland	72%	84%	82%	78%	69%	79%	78%	75%	90%
15	Italy	88%	94%	95%	94%	88%	94%	95%	94%	86%
16	Latvia	90%	93%	92%	88%	90%	93%	92%	88%	90%
17	Lithuania	72%	99%	94%	94%	68%	83%	82%	86%	77%
18	Luxembourg	56%	81%	86%	84%	56%	81%	86%	84%	86%
19	Malta	13%	48%	76%	89%	13%	48%	76%	89%	67%
20	The Netherlands	57%	76%	75%	69%	63%	86%	86%	80%	72%
21	Poland	67%	89%	90%	88%	67%	89%	91%	88%	76%
22	Portugal	88%	94%	94%	93%	89%	95%	95%	94%	90%
23	Romania	94%	95%	95%	93%	94%	95%	95%	93%	93%
24	Slovakia	87%	92%	94%	91%	87%	88%	90%	87%	77%
25	Slovenia	56%	96%	96%	94%	56%	96%	96%	95%	91%
26	Spain	75%	92%	94%	93%	75%	92%	94%	93%	83%
27	Sweden	92%	94%	94%	91%	88%	90%	90%	87%	66%
28	United Kingdom	82%	86%	82%	77%	82%	86%	82%	77%	49%

It is observed that:

- Turnover data: for two countries (Cyprus and Malta), companies reported an average of less than 60% of the data for the turnover for the period in scope. Six countries (Austria, Czech Republic, Germany, Ireland, Luxembourg and the Netherlands) reported on average between 60% and 80% of the data for the turnover. The remaining countries of EU-28 reported an average of more than 80% of the data for the turnover.

- Net profit data: for four countries (Austria, Cyprus, Germany and Malta), companies reported an average of less than 60% of the data for the net profit for the period in scope. Seven countries (Czech Republic, Finland, France, Ireland, Lithuania, Luxembourg, and the Netherlands) reported an average between 60% and 80% of the data for the net profit. The remaining countries of the EU-28 reported an average of more than 80% of the data for the net profit.

- Independence indicator: for four countries (Cyprus, Finland, Hungary and the United Kingdom), companies reported an average of less than 60% of the data for the independence test for the period in scope. Eleven countries (Belgium, Croatia, Czech Republic, Denmark, France, Lithuania, Malta, the Netherlands, Poland, Slovakia and Sweden) reported an average between 60% and 80% of the data for the independence test. The remaining countries of the EU-28 reported an average of more than 80% of the data for the independence test.

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The tables below show in absolute and relative figures a ranking of the countries regarding data availability, based on the average sales and net profit availability for 2011-2013[2] and the independence test availability.

#	Country	Av. of sales & net profit availability 2011-2013, independence test availability
1	France	70 214
2	Italy	67 416
3	United Kingdom	55 458
4	Germany	46 089
5	Spain	37 348
6	Sweden	20 718
7	Poland	18 497
8	Belgium	12 970
9	Czech Republic	10 788
10	Portugal	8 821
11	The Netherlands	8 725
12	Finland	8 120
13	Austria	8 046
14	Romania	7 568
15	Hungary	5 676
16	Slovakia	4 337
17	Denmark	4 214
18	Greece	4 164
19	Ireland	3 853
20	Bulgaria	3 695
21	Croatia	2 225
22	Lithuania	2 188
23	Slovenia	2 125
24	Latvia	1 864
25	Estonia	1 775
26	Luxembourg	1 306
27	Malta	584
28	Cyprus	234

#	Country	Av. of sales & net profit availability 2011-2013, independence test availability
1	Slovenia	95%
2	Romania	94%
3	Portugal	94%
4	Estonia	93%
5	Greece	93%
6	Italy	93%
7	Bulgaria	93%
8	Croatia	92%
9	Spain	92%
10	Latvia	91%
11	Belgium	90%
12	Slovakia	88%
13	Lithuania	88%
14	Sweden	87%
15	Poland	87%
16	Denmark	86%
17	Czech Republic	85%
18	Luxembourg	84%
19	Hungary	83%
20	Ireland	81%
21	France	80%
22	The Netherlands	78%
23	United Kingdom	77%
24	Finland	76%
25	Malta	70%
26	Austria	70%
27	Germany	69%
28	Cyprus	63%

In conclusion, the tables above suggest that:

- There are generally a lot of data points available across EU MS, that should allow for consistent application of the TNMM through EU, by either referring:
    - To local market – for largest MS.
    - Relevant market (see Milestones 25-28) – for all MS.
    - EU market (Milestone 22) – for all MS.
- Depending on market selection, the number of data available should still be sufficient to screen the data with multiple comparability criteria.
- The relative amount of data published goes form average (above 60%) to excellent (above 95%).

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[2] 2014 not included as it is believed not all accounts were published at the time of the analysis.

5.5. Milestone #14: Records for the most recent 5-year period for which data are available

Scope: For the most recent 5-year period (2010 – 2014) for which data are available, the available data for operating profit over rolling periods of three consecutive years (2010 – 2012, 2011 – 2013, 2012 – 2014) is provided

The availability of operating profit (EBIT) has been verified for three different consecutive year periods between 2010 – 2014. The majority of the MS has a similar volume of data available over the considered periods. 2014 data are still lacking for a few countries (not yet released at the time of analysis). For the majority of MS, only a few report little operating profit data.

5.6. Milestone #15: Number of entities in a loss-position for the most recent 5 year-period

Scope: For each year (2010 – 2014) and rolling periods of three consecutive years (2010 – 2012, 2011 – 2013, 2012 – 2014), the number of entities in a loss position is provided.

The profitability of companies in all 28 MS has been verified to identify loss-making companies on an annual basis, and over 3-year periods. Overall, based on relative figures, the portion of loss-making companies seems to be pretty consistent within a MS. Austria and Germany reported a relatively low number of loss-making companies, while Greece was positioned at the other side of the spectrum with the most loss-making companies amongst the EU-28.

The data suggest that (1) after screening on loss-making companies, there should remain a sufficient number of companies to apply other screening tests and (2) that some markets may be defined by the number of loss-making companies they have.

For transfer pricing purposes, though, one can question the combination of the exclusion of loss-making companies and the application of range on the final results. Indeed, the purpose of the range is generally precisely to exclude companies with extreme results (loss or profit). If some comparables have been initially rejected because they were loss-making, and that through the application of a range again the least profitable are rejected, one may argue the results are biased (towards higher values).

5.7. Milestone #16: Number of entities characterized as "start-ups" (years 2011-2014)

Scope: For each year (2011 – 2014), the number of records have been identified which can be characterised as "start-ups".

A 'start-up' entity is defined as an entity in existence for less than three years. There is quite some variety between the different MS. Some MS seem to attract a significant number of start-up companies. Based on relative figures, Ireland would be in a leading position, while the UK has registered the majority of start-up companies based on absolute figures.

The data suggest that (1) after screening on start-up companies, there should remain a sufficient number of companies to apply other screening tests and (2) that some markets may be defined by the number of start-up companies they have.

If the exclusion of start-ups appears to be quite systematic across MS, it is understood to be the reflection of TP being applied in a going concern environment. One may question their elimination, though, if the tested party itself is a start-up.

5.8.   Milestone #17: Number of entities characterized as "SMEs" (years 2011-2014)

Scope: For each year (2011 – 2014), the number of records have been identified which can be characterized as "SMEs".

The majority of companies qualifying as a SME (definition established by European Commission) are based in Italy, Spain, the UK and France. They are also the MS with the largest number of companies.

The majority of MS has around 70% to 80% of their companies qualifying as SME. There are a few MS with far lower number of SMEs: Cyprus, Germany, Ireland, Luxembourg, Malta and Poland.

SMEs appear to be the typical companies that will be used under ETNMM in the EU, as they may offer a closer comparability in size and, hence, functionality, to (individual) group companies. Their generally significant presence across the EU markets is favourable to the application of the ETNMM.

General conclusion for Milestones #15, #16 and #17

Conclusion in terms of **quantity**:

The three controls performed – number of loss-making companies, start-ups and SMEs – confirm the general good availability of data for ETNMM purposes. Indeed, there remains generally a fair amount of companies after elimination of loss-making companies (deemed subject to other specific economic circumstances) and start-ups (deemed not yet presenting going concern profit) and all MS report a large amount of SMEs, which are typically the pool of companies where comparables will be found.

Conclusion in terms of **quality**:

Loss-making companies: assessing the number of loss-making companies in a market can be revealing on the nature of the market. That can then be used for comparability assessment purposes under ETNMM.

Start-ups: likewise, assessing the number of start-up companies in a market can be revealing on the nature of the market. That can then be used for comparability assessment purposes under ETNMM.

SMEs: the generally large amount of SMEs available in the different MS is favourable to the application of the ETNMM, as they often allow closer comparability to the tested party in size and functionalities.

5.9.   Milestone #18: Quality test of the comparable data by the use of a regression method

Scope: Using one 'EU' database, the quality of the following comparable data has been tested for each Member State and for the whole EU-28 Region:

- *Correlation between operating profit and operating assets, in absolute terms;*

- *Correlation between operating profit and sales, in absolute terms.*

A positive correlation is generally expected between operating profit and operating assets: the more operating assets are used, the larger the operating profit is expected to be. The positive correlation appears stronger when all data of the 28 MS is taken as a whole which suggests that the data is generally of good quality.

A similar positive correlation can be identified for the operating profit versus sales data. Again, the higher the level of the sales, the higher the expected profit should be. The positive correlation is strong on an individual MS basis. When comparing MS, we notice that the more data is available in a specific MS, the stronger the positive correlation becomes. Italy reaches almost a perfect positive correlation. The overall

assessment of the 28 MS also indicates a strong positive correlation between the operating profit and sales which suggests the data is generally of good quality.

5.10. Milestone #19: Availability of financial information per sector and per MS (2010 – 2014)

Scope: For each sector and over the last 5 years (2010 – 2014), an analysis of the availability of financial information per MS, for the whole period and per year is provided.

In general, the items in the balance sheet and in the P&L accounts are reported in a consistent way in each of the sectors within the scope. In general, less data is available for 2014 (possibly due to late publishing) and 2010. In addition, less data is available for a consecutive period of 5 years.

5.11. Milestone #20: Tests of sectors on the basis of comparability factors

Scope: For the three given sectors in each MS, an overview is provided analysing the possibility to test these sectors based on the comparability factors mentioned by the OECD TPG.

The contractual terms and business strategies pursued by the parties cannot be assessed because this information is not available in Amadeus. The economic circumstances of the parties can possibly be assessed, but only for certain elements, e.g. geographic area, and on a case-by-case basis. The characteristics of property or services transferred can be assessed based on the data available for the business descriptions. The functional analysis can only be performed for Cyprus, Denmark, Greece, Ireland, Latvia, Lithuania, Malta, Netherlands and the UK since there is lack of data for the operating expenses on total costs and total sales in Amadeus for the rest of the MS.

5.12. Milestone #21: Indicators, tests or thresholds in each MS

Scope: Indicators, tests or thresholds which are used in each Member State in order to assess the acceptability and reliability of comparables in light of the tested transactions, as well as possible adjustments are collected and analysed.

Several MS make use of turnover thresholds during the quantitative screening process. The majority of the MS, thereafter, requires further qualitative screening through a manual process to define the final set of comparables. The qualitative screening process, which may be exposed to more subjectivity, remains the preferred approach by most MS.

Few MS will make adjustments to the comparables. If an adjustment is made, then it will typically be a working capital adjustment. Accounting adjustments may be applied as well in specific circumstances. The most common accounting adjustments consist in adjustments to factor in restructuring or foreign exchange differences. Other adjustments are less commonly applied.

Furthermore, it may be useful to provide additional guidance towards a common search process. There are some differences between search steps applied by different MS, but the ultimate goal of the search step is often comparable between MS. Providing guidance related to a typical search process, especially to screens such as independence, may ease the burden for taxpayers and tax administrations.

We have tested the availability of data using two common independence thresholds, for all companies with sales above EUR 5.0 million and with sales between EUR 2.5 and 5.0 million:

Independence threshold	Number of companies	
	Sales > mEUR 5.0	mEUR 2.5< Sales > mEUR 5.0
No corporate shareholder > 50%	187,248	340,517
No corporate shareholder > 25%	21,706	32,914

It is observed that when looking at the largest companies (sales larger then EUR 5 million), strengthening the independence criteria from a maximum stake by any corporate shareholder of 50% to 25% would decrease the number of potential comparables approximately sevenfold. When looking at the smallest (sales between EUR 2.5 & 5.0 million), the stricter independence would decrease the number of potential comparables approximately tenfold.

This suggests that too stringent thresholds to screen on independence can decrease dramatically the number of potential comparables. A Threshold of 50% – the only objectively determinable – appears then to be preferable.

5.13. Milestone #22: Update the two qualitative contribution studies analysis presented during the JTPF March 2004 meeting

Scope: under this Milestone, two studies about pan-European searches have been updates with more recent and / or extended data.

The update allows maintaining the historic conclusions that (1) pan-European searches produce comparable sets that are generally fairly representative of local profit expectations, that (2) they tend to be more affordable than a series of local searches and that (3), at times, sectoral or industry differences may subsist.

5.13.1. Update of the 2004 study 'Is Europe One Market?'

Overall, the conclusions of the 2004 survey were that (1) the EU was one market for TNMM transfer pricing purposes and that (2) an arm's length range of results based on a pan-European set of comparable companies provides a reliable measure for an arm's length result are confirmed accordingly.

The objective of the present analysis is to reassess the "Europe one-market" hypothesis. This question has been investigated using the chi-square test of homogeneity. The 2004 survey "Is Europe One Market?" has been updated to examine the appropriateness of using pan-European databases rather than local databases. Overall, the updated survey of 2016 seem to conclude again that the EU is generally one market for TNMM transfer pricing purposes, and that an arm's length range of results based on a pan-European set of comparable companies would provide a reliable measure for an arm's length result.

For this update of the 2004 survey, the geographic area has been expanded (EU-28, Iceland, Liechtenstein, Norway and Switzerland). This testing has been performed for each country across a total of twelve profiles:

- Four initial profiles for the specific test (Automotive Manufacturing, Electronics Manufacturing, Chemicals Distribution and Electronics Distribution), from 2004 study;

- Three additional profiles for the specific test (Transport and Logistics, Pharmaceutical Healthcare Manufacturing and Textile Wholesale), only in 2016 study; and

- Five profiles for the broader test (Printing, Machinery Manufacturing, Vehicle Parts Distribution, Food Distribution and Computer Services), from the 2004 study.

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The results of the <u>specific test</u> for the four profiles of the previous study are reported in the table below:

	Automotive Manufacturing	Electronics Manufacturing	Chemical Distribution	Electronics Distribution
Size of Data Set (# Companies)	428	644	642	584
Profit Level Indicator	Return on Assets (ROA) in %		Operating Profit Margin (OPM) in %	
Interquartile Range Europe	2.3 – 9.8	3.1 – 11.5	1.4 – 4.9	1.2 – 5.0
Lower Quartile – **<u>Same as Pan-European</u>** (*Accept null Hypothesis*)	Finland, France, Hungary, Italy, Poland, Slovakia, Spain, Sweden, United Kingdom, Czech Republic, Germany, Portugal	Belgium, Czech Republic, Finland, France, Greece, Hungary, Slovakia, Spain, Sweden, Germany, Italy, Poland, Portugal, United Kingdom	Belgium, Bulgaria, Czech Republic, Greece, Germany, Hungary, Italy, Poland, Portugal, Spain, United Kingdom	Czech Republic, France, Germany, Greece, Hungary, Italy, Netherlands, Norway, Spain, Sweden, United Kingdom
Lower Quartile – **<u>Different to Pan-European</u>** (*Reject null Hypothesis*)	None	None	France	Poland
Upper Quartile – **<u>Same as Pan-European</u>** (*Accept null hypothesis*)	Finland, France, Hungary, Slovakia, Spain, Sweden, United Kingdom, Czech Republic, Germany, Italy, Poland, Portugal	Belgium, Czech Republic, Finland, France, Greece, Portugal, Slovakia, Sweden, Germany, Hungary, Italy, Poland, Spain, United Kingdom	Belgium, Bulgaria, Czech Republic, France, Germany, Hungary, Italy, Poland, Portugal, Spain, United Kingdom	Czech Republic, France, Germany, Greece, Hungary, Italy, Netherlands, Norway, Poland, Spain, Sweden, United Kingdom
Upper Quartile – **<u>Different to Pan-European</u>** (*Reject null hypothesis*)	None	None	Greece	None

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The results of the <u>specific test</u> for the three additional profiles are reported in the table below:

	Transport And Logistics	Pharmaceutical Healthcare Manufacturing	Textile Wholesale
Size of Data Set (# Companies)	3867	199	693
Profit Level Indicator	Return on Assets (ROA) in %		Operating Profit Margin (OPM) in %
Interquartile Range Europe	1.5 – 8.8	3.9 – 11.6	1.5 – 5.8
Lower Quartile – **<u>Same as Pan-European</u>** (*Accept null Hypothesis*)	Austria, Belgium, Czech Republic, Finland, Germany, Hungary, Italy, Lithuania, Netherlands, Norway, Poland, Portugal, Slovakia, Spain, Sweden, Switzerland, United Kingdom	Czech Republic, France, Germany, Greece, Hungary, Italy, Poland, Spain, United Kingdom	Belgium, Germany, Hungary, Norway, Poland, Portugal, Spain, Sweden, United Kingdom
Lower Quartile – **<u>Different to Pan-European</u>** (*Reject null Hypothesis*)	France, Greece, Romania	Belgium	Greece, France, Italy
Upper Quartile – **<u>Same as Pan-European</u>** (*Accept null hypothesis*)	Austria, Belgium, Finland, France, Greece, Hungary, Netherlands, Norway, Portugal, Romania, Slovakia, Sweden, Switzerland, United Kingdom	Belgium, Czech Republic, France, Germany, Greece, Hungary, Italy, Poland, Spain, United Kingdom	Belgium, France, Germany, Greece, Hungary, Italy, Norway, Portugal, Spain, Sweden, United Kingdom
Upper Quartile – **<u>Different to Pan-European</u>** (*Reject null hypothesis*)	Czech Republic, Germany, Italy, Lithuania, Poland, Spain	None	Poland

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The results of the <u>broader test</u> for the five profiles of the previous study are reported in the table below:

	Printing	Machinery Manufacturing	Vehicle Parts Distribution	Food Distribution	Computer Services
Screening criteria	NACE 18	NACE 28	NACE 453	NACE 463	NACE 62, 63
Size of Data Set (# companies)	264	1270	523	4514	991
Profit Level Indicator	ROA in %	ROA in %	OPM in %	OPM in %	NCP in %
Interquartile Range	3.1 – 8.9	3.6 – 9.9	2.1 – 5.8	0.9 – 3.2	2.2 – 7.5
Lower Quartile- **Same as Pan-European** (*Accept null Hypothesis*)	Belgium, Czech Republic, Finland, France, Germany, Greece, Hungary, Italy, Poland, Spain, Sweden, United Kingdom	Czech Republic, Finland, France, Germany, Hungary, Italy, Poland, Spain, Sweden, United Kingdom	Belgium, Czech Republic, Finland, France, Germany, Hungary, Italy, Norway, Poland, Portugal, Romania, Spain, United Kingdom	Belgium, Bulgaria, Finland, Germany, Greece, Hungary, Italy, Netherlands, Norway, Poland, Portugal, Romania, Slovakia, Spain, Sweden	Belgium, Finland, France, Germany, Italy, Norway, Poland, Spain, Sweden, United Kingdom
Lower Quartile – **Different to Pan-European** (*Reject null Hypothesis*)	None	None	None	Czech Republic, France, United Kingdom	Hungary
Upper Quartile- **Same as Pan-European** (*Accept null Hypothesis*)	Belgium, Czech Republic, Finland, France, Greece, Hungary, Italy, Spain, Sweden, United Kingdom	Czech Republic, Finland, France, Germany, Hungary, Italy, Poland, Spain, Sweden	Belgium, Czech Republic, Finland, France, Germany, Hungary, Italy, Norway, Poland, Portugal, Romania, Spain, United Kingdom	Belgium, Bulgaria, Czech Republic, France, Germany, Hungary, Norway, Poland, Portugal, Romania, Slovakia, Sweden, United Kingdom	Belgium, Finland, France, Germany, Hungary, Italy, Norway, Poland, Spain, Sweden, United Kingdom
Upper Quartile – **Different to Pan-European** (*Reject null Hypothesis*)	Germany, Poland	United Kingdom	None	Finland, Greece, Italy, Netherlands, Spain	None

5.13.2. Update of the 2004 study 'Pan-European versus country-specific searches and Pan-European versus country-specific databases: not a clear-cut issue'

The 2004 study concluded, on the basis of financials covering different periods (1997 – 1999, 1997 – 2001, 1998 – 2000) in (1) the acknowledgment of occasional differences in PLIs between countries, sectors, but also – most importantly – in (2) the need to accept pan-European searches given the approximate character of the TNMM and the overall cost of compliance.

The update of the sectoral PLIs for the period 2010 to 2014 does not, at first sight, allow to deviate from that conclusion in 2016. If a close comparison of both studies can only be tentative given intrinsic differences (periods, screenings) and the absence of broad range statistical testing, we observe nevertheless again that some sectoral differences may exist. If most local tax administrations still do not strictly require to produce local comparables, there are however quite a few, as was revealed in the survey performed otherwise (Milesones 25 – 28), that tend to either require to search first for local comparables or mark a preference for the use of local comparables. These countries are, most notably, Eastern European countries, but also France, Italy, Portugal, Spain and the UK.

Aerospace spare parts industry – Distributor search – Operating Margin

For this sector, the primary NACE code 4614 – Agent involved in the sale of machinery, industrial equipment, ships and aircraft has been used with the combination of inclusion keywords (aero*, air*, space*).

Final Set Results – Pan-European

	2014	2013	2012	2011	2010	WAVG
75th percentile	8.8%	9.8%	4.8%	10.9%	4.6%	4.6%
Median	**2.6%**	**2.0%**	**2.9%**	**2.8%**	**2.1%**	**1.9%**
25th percentile	0.2%	0.3%	0.2%	0.3%	0.2%	0.4%

Final Set Results – UK (Amadeus)

	2014	2013	2012	2011	2010	WAVG
75th percentile	14.8%	10.1%	6.2%	11.5%	6.2%	9.4%
Median	**11.3%**	**9.8%**	**4.1%**	**10.7%**	**4.8%**	**6.4%**
25th percentile	7.8%	6.5%	3.0%	5.9%	4.4%	3.3%

Industrial machines industry – Distributor search – Operating Margin

For this sector, the primary NACE code 466 – Wholesale of other machinery, equipment and supplies has been used.

Final Set Results – Benelux

	2014	2013	2012	2011	2010	WAVG
75th percentile	5.1%	4.4%	4.7%	4.8%	5.0%	4.6%
Median	**3.0%**	**1.9%**	**2.3%**	**2.9%**	**2.7%**	**2.6%**
25th percentile	1.7%	0.2%	0.5%	0.6%	1.4%	0.9%

Final Set Results – North/West Europe[3]

	2014	2013	2012	2011	2010	WAVG
75th percentile	6.0%	5.6%	5.6%	5.9%	5.6%	5.4%
Median	**2.9%**	**2.9%**	**2.7%**	**3.0%**	**2.8%**	**2.8%**
25th percentile	1.1%	0.9%	1.0%	1.2%	1.0%	1.2%

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[3] Belgium, Denmark, Finland, France, Germany, Ireland, Luxembourg, Netherlands, Sweden and United Kingdom.

Final Set Results – Pan-European

	2014	2013	2012	2011	2010	WAVG
75th percentile	6.7%	5.9%	5.9%	6.3%	6.1%	5.8%
Median	**3.4%**	**3.2%**	**3.0%**	**3.3%**	**3.1%**	**3.2%**
25th percentile	1.4%	1.2%	1.1%	1.4%	1.3%	1.3%

Pharmaceutical industry – Distributor search – Operating Margin

For this sector, the primary NACE code 4646 – Wholesale of pharmaceutical goods has been used.

WAVG	UK	France	Germany	Italy	Spain	Sweden	Pan-European
75th percentile	9.8%	6.5%	7.6%	5.3%	4.8%	9.3%	7.7%
Median	**4.4%**	**2.8%**	**4.2%**	**2.5%**	**1.6%**	**4.2%**	**3.3%**
25th percentile	2.0%	1.2%	1.8%	0.3%	0.5%	0.1%	1.0%

5.14. Milestone #23: External comparable and profit-based methods

We refer to our comments in Milestone #6 detailing the use of export prices for transfer pricing purposes.

5.15. Milestone #24: Conclusion and comments for each MS

The highlights of the quality of data and the screening process across the 28 MS are the following:

- CoGS and material cost data are not uniformly available.

- Operating expenses are not uniformly characterized and sufficiently detailed. The absence of systematic separate reporting of R&D and marketing expenses is missed by quite a few MS.

- Independence is not uniformly defined.

- The activities description in 'Business overview' (field, from the database) is not uniformly available.

- Screening on start-up companies is common place, screening on balance sheet items or operating expenses is less common

- Activities description in 'Trade description and under NACE code classification is not always in line with the actual business activities.

- Manual, qualitative screenings are still very much used somewhat to the detriment of quantitative searches that nevertheless are more objective, economically grounded and quicker.

- A certain alignment around the IFRS standard is observed.

- MS generally accept Pan-European searches.

5.16. Milestone #25: Testing the notion of "relevant market" against subgroups of neighbouring countries

Scope: All 28 MS are divided into three groups based on the relevant market, defined by categorising neighbouring countries. In each of these groups, the number of data availability in Amadeus is measured.

Most MS accept the use of pan-EU and foreign data. In addition, a few MS follow a gradual approach where they first prefer local data, and then data from neighbouring countries or close geographic areas, and then pan-EU data. In some limited cases, even global data is accepted. There is no established practice where MS do not consider pan-EU data or only consider local data for specific situations or transactions / sectors. MS generally put their focus on comparability.

The underline relevant market was deemed to be that of geographically close MS, for the following reasons:

- Empirically, it was observed that quite a few MSs considered close geography as an important comparability element for ETNMM purposes.

- Countries which are close to each other are expected to be more likely to have commercial relations, making them more likely to share macro-economic characteristics.

- The products or services exchanged are likely to be more closely comparable.

The following categories have been defined: South EU countries, East EU countries and North-West EU countries.

It can be concluded that:

1. In general terms, we note a trend of data being increasingly available over the years.

2. In absolute terms, North-West EU countries tend to have twice as many data points available as South EU countries and South EU countries tend to have twice as many data points available as Eastern EU.

3. In relative terms, South EU countries tend to have more data available (relatively more companies deliver complete data sets) than East EU countries, East EU countries tend to have more data available than to North-West EU countries. The latter may be caused by smaller companies not releasing financials also being listed in the database.

4. We do not note significant discrepancies, across data sets in the availability of the different data points (turnover operating profit, financial profit, net profit, total liabilities, total assets)

Further, with reference to Milestone 22, it appears that the general number of data points available should be sufficient to apply ETNMM either across the full EU region or across sub-regions within the EU – allowing then supposedly better market comparability – with a fair degree of reliability.

5.17.   Milestone #26: Characterizing a "relevant market"

Scope: All 28 MS are divided into three groups based on the relevant market, defined by categorizing according to the gross domestic product '(GDP') per capita. In each of these groups, the number of data availability in Amadeus is measured.

The relevant market was deemed to be that of MS with similar GDP per capita for the following reasons:

- GDP per capita is a common indicator of the wealth produced by a state, being a reliable indicator of the level of development of their economies.

- There exist listings of GDP per capita by state allowing objective classification and ranking of the MS.

The relevant market, based on GDP per capita led to the following categories:

- Countries with a low GDP per capita (EUR 0 – EUR 20,000)

- Countries with a medium GDP per capita (EUR 20,000 – EUR 40,000)

- Countries with a high GDP per capita (> EUR 40,000).

It can be concluded that:

1. In general terms, we note a trend of data being increasingly available over the years.

2. In absolute terms, Medium GDP EU countries tend to have roughly four times as many data points available as Low GDP EU countries and Low GDP EU countries tend to have twice as many data points available as High GDP EU countries. This measurement suggests, seemingly, that the majority of EU companies is situated in the Medium GDP category and the fewest in the High GDP category.

3. In relative terms, we note no marked difference in the data availability (number companies to deliver complete data sets) across the different data sets, suggesting GDP per capita of a country has little to no impact on the general data publication requirement, and, hence, on availability of data.

4. We do not note significant discrepancies, across data sets in the availability of the different data points (turnover operating profit, financial profit, net profit, total liabilities, total assets)

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Finally, with reference to Milestone 22, it appears again that the general number of data points available throughout the EU, whatever their GDP per capita, should be sufficient to apply ETNMM across the EU with a fair degree of reliability.

Foreign comparables — Yes (blue) — n.a. (white)

Q54	1 Austria	2 Belgium	3 Bulgaria	4 Croatia	5 Cyprus	6 Czech Republic	7 Denmark	8 Estonia	9 Finland	10 France	11 Germany	12 Greece	13 Hungary	14 Ireland	15 Italy	16 Latvia	17 Lithuania	18 Luxembourg	19 Malta	20 Netherlands	21 Poland	22 Portugal	23 Romania	24 Slovakia	25 Slovenia	26 Spain	27 Sweden	28 UK
1. Preference local			■	■			■	■		■		■	■		■						■	■	■	■		■		■
2. Neighb. Countries accepted	■	■	■	■		■	■	■				■	■		■	■	■				■	■	■	■	■	■	■	■
2. EU accepted	■	■	■	■		■	■	■	■	■	■	■	■	■	■	■	■		■	■	■	■	■	■	■	■	■	■
3. Global accepted																		■					■					

5.18. Milestone #27: OECD "relevant market" approach

Scope: All 28 MS are divided into three groups based on the relevant market, as defined by the OECD TP Guidelines. In each of these groups, the amount of data available in Amadeus is measured.

The relevant market was deemed to be that of MS with similar costs of labour for the following reasons:

- The OECD is listing 'Cost of labour' as one of the economic circumstances that may be relevant to determine market comparability in the transfer pricing guidelines (1.55).

- Cost of labour is typically one of the reasons why groups are delocalizing, looking for location savings.

- There exist listings of average cost of labour by state allowing objective classification and ranking of the MS.

Three categories have been defined on that basis the Eurostat classification (http://ec.europa.eu/eurostat/statistics-explained/index.php/Hourly_labour_costs):

- Countries with a Low average hourly rate of EUR 0 – EUR 10

- Countries with Medium average hourly rate of EUR 10 – EUR 30

- Countries with High average hourly rate of more than EUR 30.

It can be concluded that:

1. In general terms, we note a trend of data being increasingly available over the years.

2. In absolute terms, Medium and High average hourly rate EU countries tend to have roughly the same amount of data points available and three times as many as the Low average hourly rate EU countries. This measurement suggests, seemingly, that the majority of companies within the EU is situated in the Medium to High hourly rates categories.

3. In relative terms, we note no marked difference in the data availability (number companies to deliver complete data sets) between the countries situated in Low and Medium average hourly rates categories, and a slightly lower data availability in High average hourly rate countries. The latter may be due to the fact that these countries tend to be in the North-Western region (see conclusion Milestone 25).

4. We do not note significant discrepancies, across data sets in the availability of the different data points (turnover operating profit, financial profit, net profit, total liabilities, total assets)

Finally, with reference to Milestone 22, it appears again that the general number of data points available throughout the EU, whatever their average hourly rates, should be sufficient to apply TNMM across the EU with a fair degree of reliability.

5.19. Milestone #28: Testing the notion of "relevant market" with some competition law aspects

Scope: All 28 MS are divided into three groups based on the relevant market, as defined by Directorate-General ("DG COMP"). In each of these groups, the number of data availability in Amadeus is measured.

A large majority of the MS broadens the categories of companies deemed being sufficiently comparable to companies dealing in similar products or services, if the same products or services cannot be found. MS appear to be more divided regarding the use of comparable companies which have a different position in the value chain. The identification of comparables with a different position in the value chain may indeed raise questions on comparability. Adjustments may be needed to factor in the different position in the value chain. In short, there is a tendency to focus more on functions performed while relaxing the product similarity requirements, rather than moving to a different position in the value chain. Indeed, most MS appear to focus and give more weight to the functional comparability rather than the product comparability.

The relevant market was based on the following two tests:

A. Comparison of distributors of industrial goods in <u>Western Europe</u> and the <u>EU-28 MS</u>.

B. Comparison of <u>car manufacturers</u> with <u>spare parts manufacturers</u> in the EU-28 MS.

On the geographical test (**A**), it can be concluded that:

1. In <u>general terms</u>, we note a trend of data being increasingly available over the years.

2. In <u>absolute terms</u>, within, the EU, approximately a bit less than two third of the industrial goods distributors data points are available in Western Europe countries, suggesting a generally higher number of such companies in that region.

3. In <u>relative terms</u>, we note a slightly lower data availability (number companies to deliver complete data sets) in EU-28 industrial goods distributors compared to Western Europe. This completes the conclusions of Milestone 25 in suggesting that a combination of South-Western and North-Western regions, given their general level of data available, produces a region with high relative availability of data.

4. We do not note significant discrepancies, across data sets in the availability of the <u>different data points</u> (turnover operating profit, financial profit, net profit, total liabilities, total assets)

On the functional test (**B**), it can be concluded that:

1. In <u>general terms</u>, we note a trend of data being increasingly available over the years.

2. In <u>absolute terms</u>, spare parts manufacturers tend to provides more than seven times as many data as car manufacturers, suggesting simply a much higher fragmentation in the former sector, and the scarce availability of data points for, specifically here, car manufacturers. Also, one can expect that car manufacturers would generally by large group ultimately present in the set as consolidated – thus independent – entities, materially lowering their number.

3. In <u>relative terms</u>, we note no marked difference in the data availability (number companies to deliver complete data sets) between the spare parts manufacturers and car manufacturers, suggestive a comparable quality in data availability.

4. We do not note significant discrepancies, across data sets in the availability of the <u>different data points</u> (turnover operating profit, financial profit, net profit, total liabilities, total assets)

5. In case the profitability of a group car manufacturer is to be benchmarked, the small pond of third party car manufacturers may prevent identifying a sufficiently large set of comparables. The number of independent spare parts manufacturers – which is materially higher than the number of independent car manufacturers – allows, however, applying more numerous screening tests, leading to, possibly <u>better comparability</u>, even after having relaxed criteria such as product similarity or positioning in the value chain.

    Point 5 above can be illustrated as follows. There were 441 companies classified as 'car manufacturers' (with sales in excess or EUR 5 mio) in the whole EU-28, before application of the independence test. After the application of the independence test, there were only 198 left. That is only 45% of the original number.

    There were 2,403 companies classified as 'spare parts manufacturers' (with sales in excess or EUR 5 mio) in the whole EU-28, before application of the independence test. After the application of the independence test, there were 1,421 left. That is still 59% of the original number.

    The application of the independence screen materially decreased the number of 'car manufacturers' available for further screening purposes. That was much less the case for 'car manufacturers' industry companion, the 'spare parts manufacturers'. The latter set, or a combination of the latter and former sets, would allow more significant further screening while not relaxing the comparability on the 'industry' criterion.

More generally, with reference to Milestone 22, it appears that the general number of data points available throughout the EU may not always be sufficient for some profiles in some sectors or industries. This may be remedied by, e.g. relaxing comparability criteria allowing then to search (1) other sectors or (2) other levels in the value chain. Needless to say, that this must then be done while keeping sufficient qualitative and quantitative comparability. That, in turn, should be sufficient to apply TNMM across the EU with a fair degree of reliability.

Additionally, the EU market offers certain opportunities in situations characterising lack of comparables: it is admitted by a majority of MS to relax product comparability and conduct searches on similar functions and assets, if no comparable can be identified for same or similar products. Implicitly, MS are actually currently extending the scope of the search to markets presenting similarities (e.g. in terms of structure and / or level of competition). This test is actually similar to what is commonly applied in the competition law area. Hence, the latter field of expertise may deliver helpful support to this TP market practice. It is believed, nevertheless, that given the different objectives and circumstances in which such notion has to be tested in the competition law area (large, one-time transactions) and TP area (repetitive, numerous transactions), a simple transposition of competition law practices onto TP may be impractical… As an example, this could result in considering benchmarking the distributors of industrial goods rather than only distributors of cars at EU-28 level, or distributors of spare parts together with distributors of cars, distributors of laptops / printers and other hardware.22

General conclusion for Milestones #25, #26, #27 and #28

In each of the relevant markets, as defined in the milestones, there appears to be sufficient data for taxpayers and tax administrations to perform ETNMM searches. Accepting that a relevant market is referred to rather than the national market, could be a solution to perform comparables searches for countries lacking of data.

Searching comparables in relevant markets rather than at the full EU-28 territory level (Milestone #22), may also be an alternative to (1) decrease the workload of searching comparables while (2) possibly improving comparability.

Even though Milestone 22 suggests there is no such thing as location savings – the profitability across Europe is generally the same – it nevertheless does not exclude that some discrepancies between MS can exist. Hence, referring to relevant markets defined as, e.g. GDP per capita or labour costs, may allow improving comparability by factoring location savings elements.

5.20.   Milestone #29: List of available complementary databases per MS

There are not many databases available in the MS other than the ones previously mentioned under the other milestones. Alternative databases that were identified are situated in Poland (Tiegel), Romania and Hungary. Other regional databases that were identified are OneSource and Loursof which is used in Latvia.

5.21.   Milestone #30: Quantify the impact of using these alternative databases

The impact of the use of local databases is limited since most MS use Amadeus or Orbis. A driver for using local databases would be to decrease compliance costs.

5.22.   Milestone #31: Analyse impact of implementing adjustments

Most of the adjustments which are made are working capital adjustments. In a few cases accounting and risk related adjustments are performed. No relevant experience was found on applying location saving adjustments, suggesting their general scarcity.

If **locations savings** are believed to exist from an economic perspective – e.g. some countries would propose cheaper labour, better logistics, more favourable geographic location, more educated workforce, more readily available capital – the empirical evidence under Milestone 22 and Milestone 31 suggest they are rather uncommon under ETNMM. It is believed that the reason for this is that under ETNMM, where a (net) profit level is observed, location savings would wash out. Indeed, in an EU market converging towards an equilibrium of returns on capital, prices would adjust and profits would align.

Another category of adjustments that, even though acknowledged to be important, tend to not be performed widely, are **risk adjustments**. It is believed that the reasons for this scarcity are multiple:

- Lack of satisfying <u>definition</u> of 'risk' for TP purposes and 'types of risk adjustments'. On the former a general definition like 'induced volatility in profit' and on the latter a generic list of identified (most relevant) risk adjustments may help.

- The <u>abundance</u> of possible risks associated to any business endeavour making any systematic analysis at the transactional level a very resource-consuming enterprise (e.g. market risk, inventory risk, credit risk, currency risk, quality risk, liability risk, natural disaster risk, …)

- Intrinsic <u>technical difficulty</u> in assessing risks. Risk is generally associated to a certain level of volatility in profit. The latter needs then to be measured on reliable (transactional) data then converted in the impact it may have on prices or profit.

- The <u>implicit impact</u> of any transfer pricing system onto a risk allocation. A transfer pricing policy will indeed 'force' a certain distribution of risk between the parties and will drive their respective profit volatility. In its simplest expression, a group company receiving a guaranteed profit (according to one

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measurement, PLI) is indeed shielded from any variation (on the profit measurement) by the group counterparty that, in turn, will absorb all residual risk impacting that profit measurement.

These elements seem to be the reason why MS widely adopt pragmatic approaches to adjusting for risks, oftentimes in positioning the comparable level of profit within a benchmarked range, in a directionally correct way.

The table below summarizes the replies of the survey on adjustments:

Adjustment types & frequency

Legend: Not performed (white) | Perf. Rarely (light) | Perf. occasion. (cyan) | Perf. frequently (dark blue)

Q61 & Q62

Adjustment type	1 Austria	2 Belgium	3 Bulgaria	4 Croatia	5 Cyprus	6 Czech Republic	7 Denmark	8 Estonia	9 Finland	10 France	11 Germany	12 Greece	13 Hungary	14 Ireland	15 Italy	16 Latvia	17 Lithuania	18 Luxembourg	19 Malta	20 Netherlands	21 Poland	22 Portugal	23 Romania	24 Slovakia	25 Slovenia	26 Spain	27 Sweden	28 UK
1. Capital adj.		occasion.			rarely	rarely	occasion.	rarely		rarely		occasion.	occasion.		occasion.	rarely	rarely		rarely	occasion.	rarely	occasion.	rarely	rarely				occasion.
2. Accounting adj.	rarely	rarely			rarely											occasion.				rarely			rarely	rarely	rarely			occasion.
3. Other		rarely			rarely																	occasion.						

Deloitte.

Europe One Market

Data visualisation

24 May 2016

Data visualisation

Data visualisation

The figures in this section can help provide guidance in understanding the composition of the data for each of the investigated industries.

In the left panel, a series of boxplots is shown for all the countries present in the dataset. The vertical axis corresponds to the financial metric used: depending on industry this can be the ROA, OPM or NCP. The boxplot is a standard way of showing the distribution of data using the median (P50), the lower and upper quantiles (P25 and P75). The median corresponds to the thick black line in the box while the lower and upper quantiles correspond to the edges of the box (this is the inter-quantile range). The dashed lines and whiskers extending beyond the inter-quantile range correspond to 1.5 times the inter-quantile range: any data point beyond this range (displayed as circle) is considered to be an outlier. The dashed blue lines correspond to the pan-european P25 and P75.

In the right panel, a barplot is shown that illustrates the representation of the each country in the dataset. This figure helps to appreciate which countries contribute the most (or, the least) to the pan-european P25 and P75. It also indicates the variation of representativeness of the data across countries: some countries are much more representative in terms of companies than others.

Some first indications of the homogeneity of the European market can be deduced by visual inspection of the boxplots. In several instances one can see that the location of the boxplots does not vary significantly across countries (also note that the axis are zoomed-in). We remark however, that, the chi-square test is based on a different metric than the boxplot and thus it can be misleading to attempt to explain one using the other. In particular, the boxplot is displaying a financial figure (e.g. the ROA) while the chi-square test is based on a simple counting of the number of companies above or below a certain level. It can well be the case that these two coincide and lead to the same conclusion. However, this may not always be the case. Apart from the fact they measure different quantities, they both have some inherent weaknesses: the chi-square test is an approximate method as it depends on the size of the dataset (as it assumes that the sum of squares is a chi-squared-distributed number regardless of the number of terms in the sum) and on the sample data being drawn at random from the population. The boxplot, on the other hand, conceals the information about how many companies contribute to the box.

Summary

Industry	Metric
Automotive manufacturing	ROA
Chemicals distribution	OPM
Electronics distribution	OPM
Electronics manufacturing	ROA
Pharmaceutical and healthcare manufacturing	ROA
Textile wholesale	OPM
Transport and logistics	ROA
Printing	ROA
Machinery Manufacturing	ROA
Vehicle parts distribution	OPM
Food distribution	OPM
Computer services	NCP

Data visualization

- Boxplots are presented showing the distribution of the financial metric within each country.
- Barplots are presented showing the representation of each country (number of companies) in each dataset.

Transport and logistics

Data visualisation
Transport and logistics

20 countries
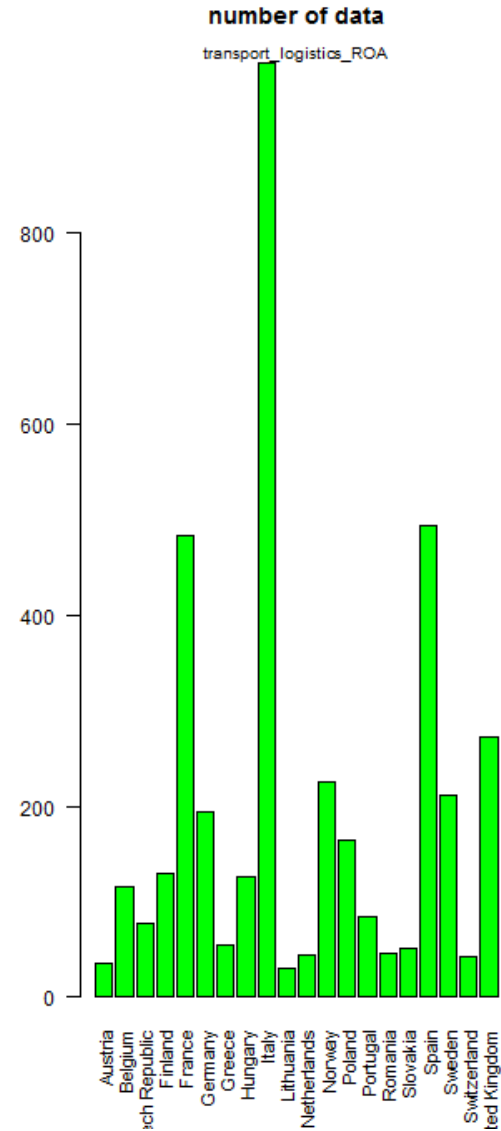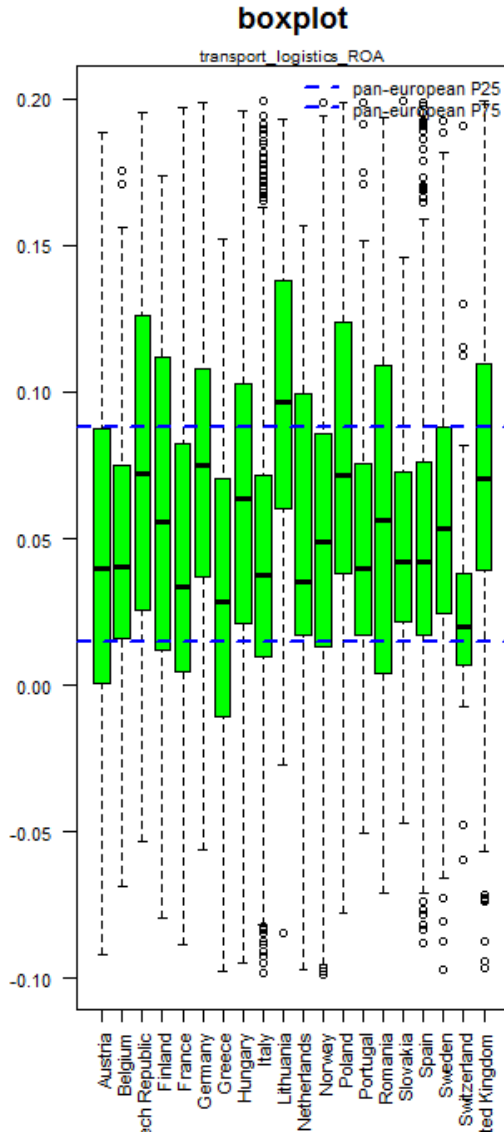
Textile wholesale

Data visualisation
Textile wholesale

12 countries
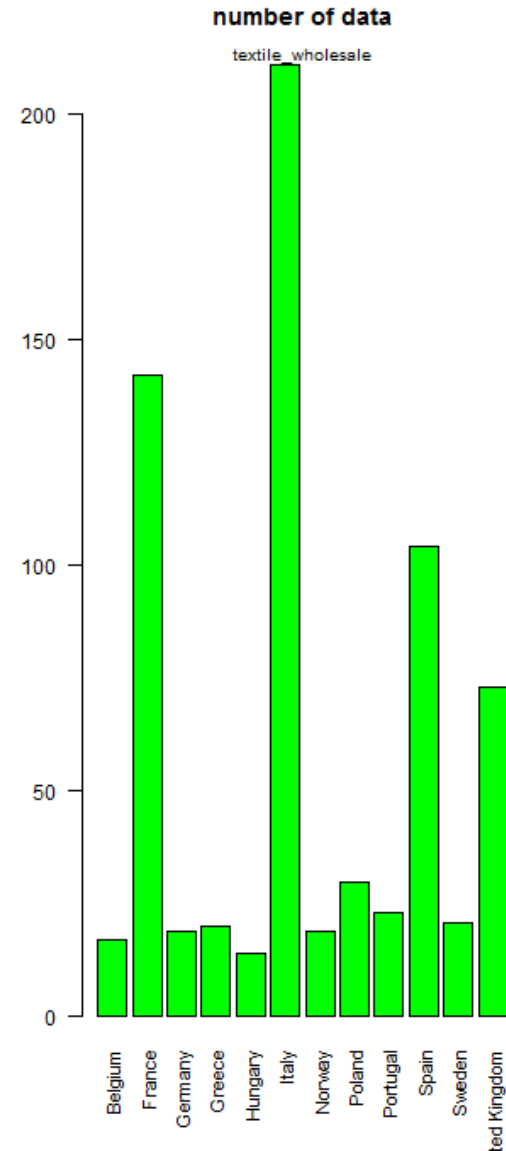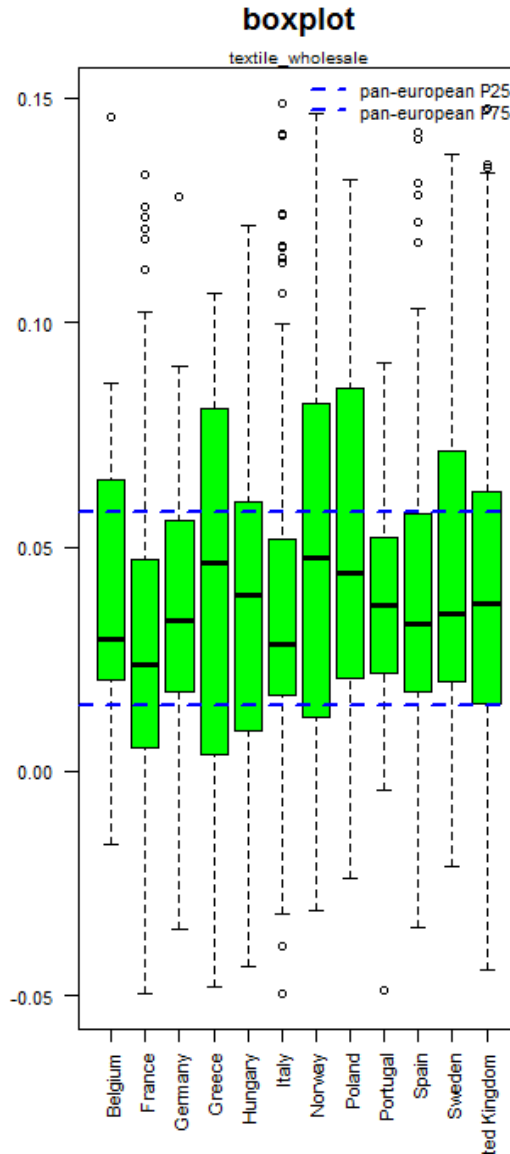
Pharmaceutical and healthcare manufacturing

Data visualisation
Healthcare manufacturing

10 countries
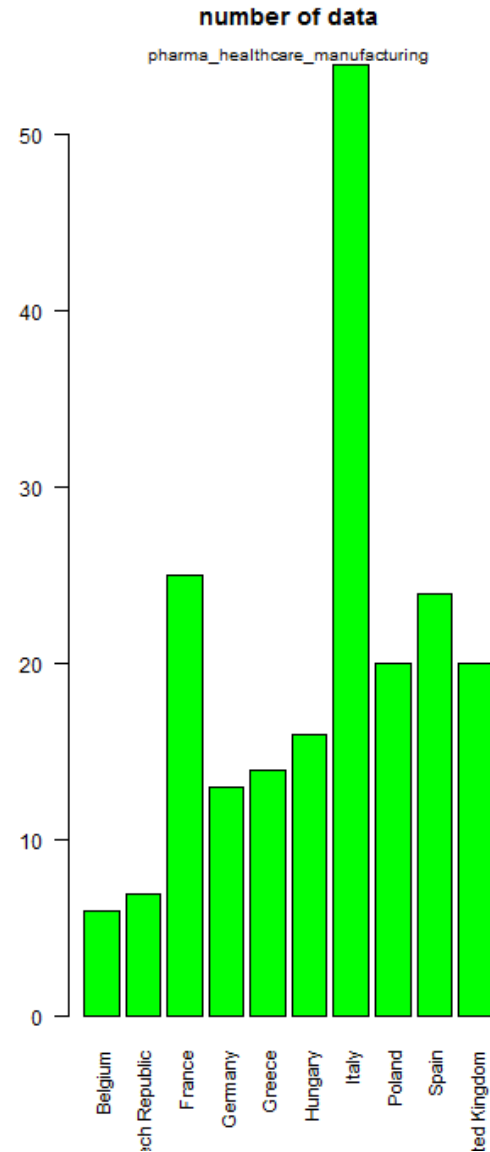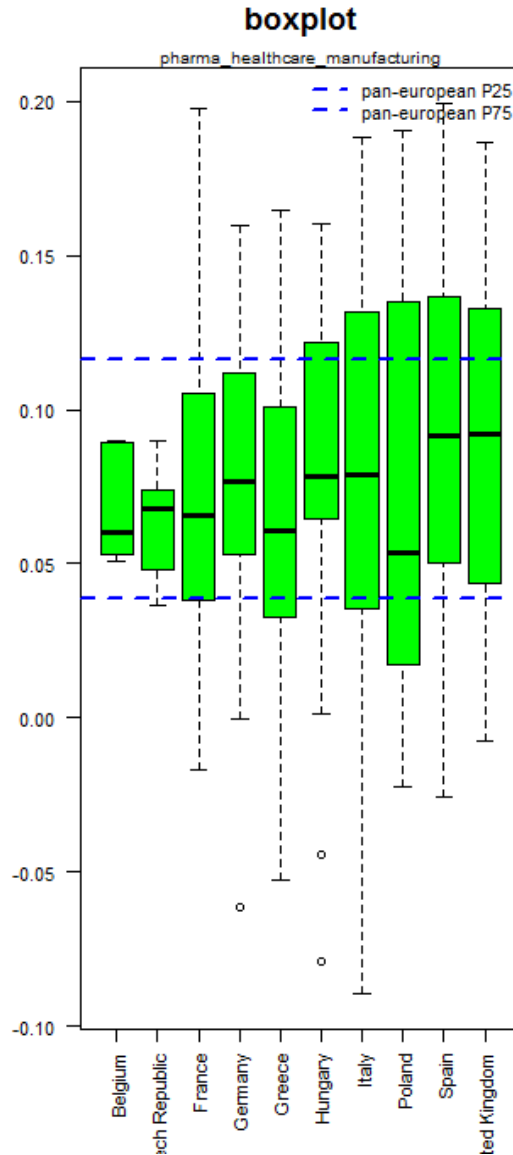
Electronics manufacturing

Data visualisation
Electronics manufacturing

14 countries
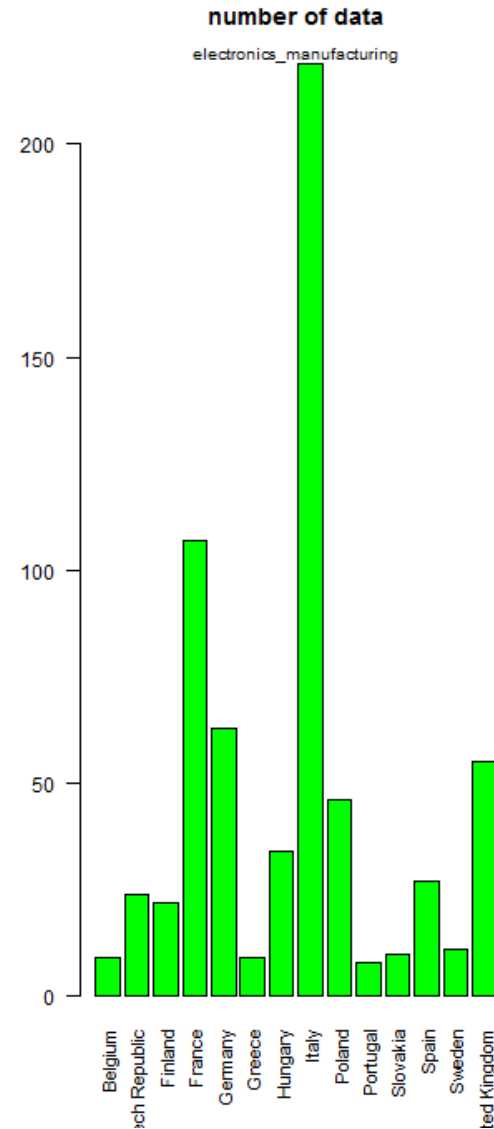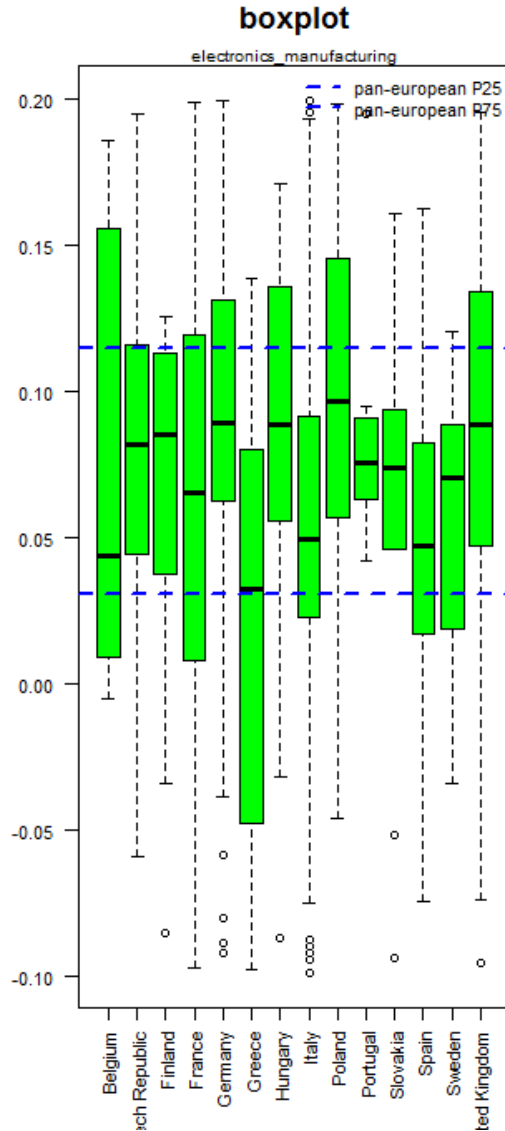
Electronics distribution

Data visualisation
Electronics distribution

12 countries
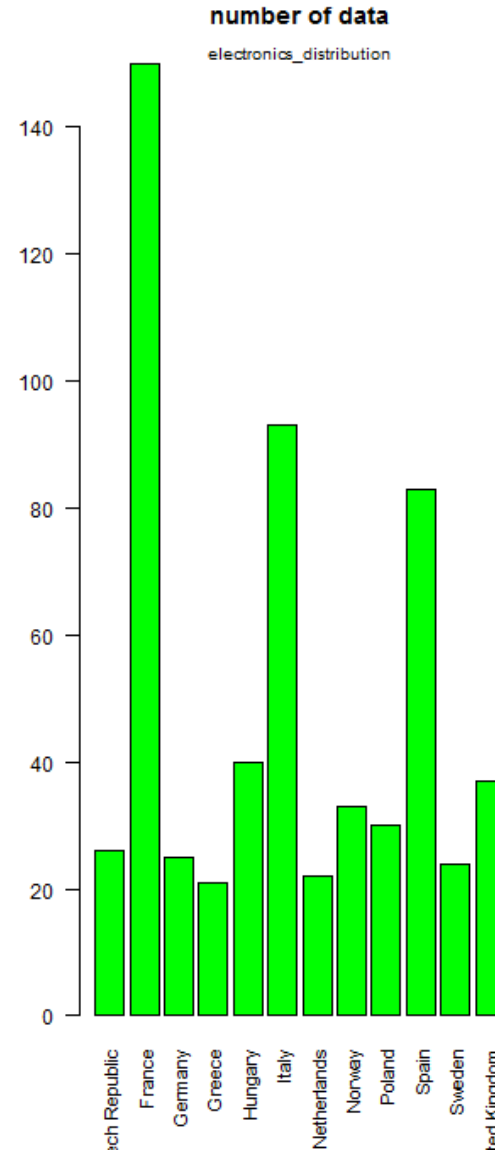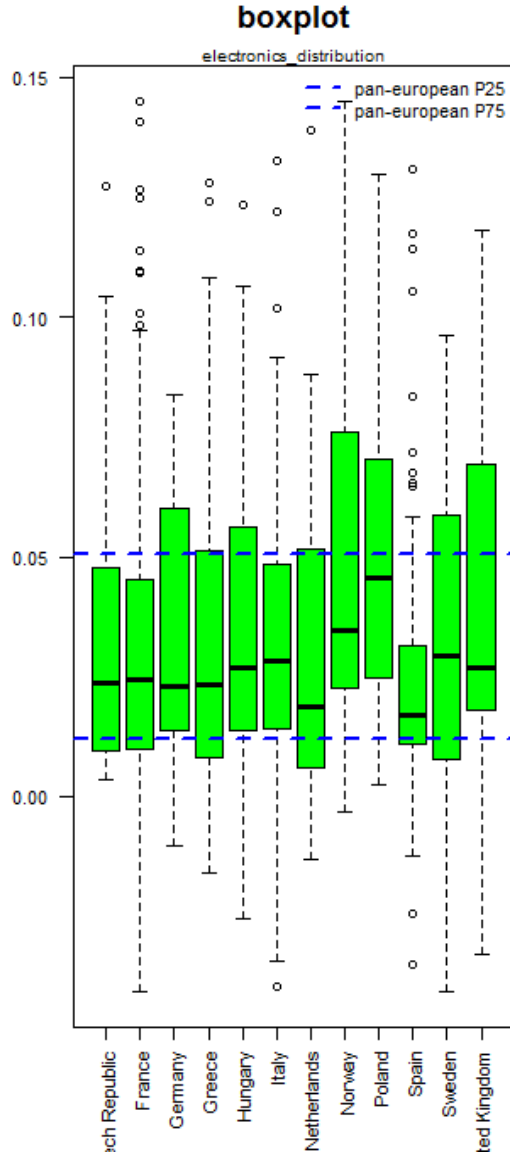
Chemicals distribution

Data visualisation
Chemicals distribution

12 countries
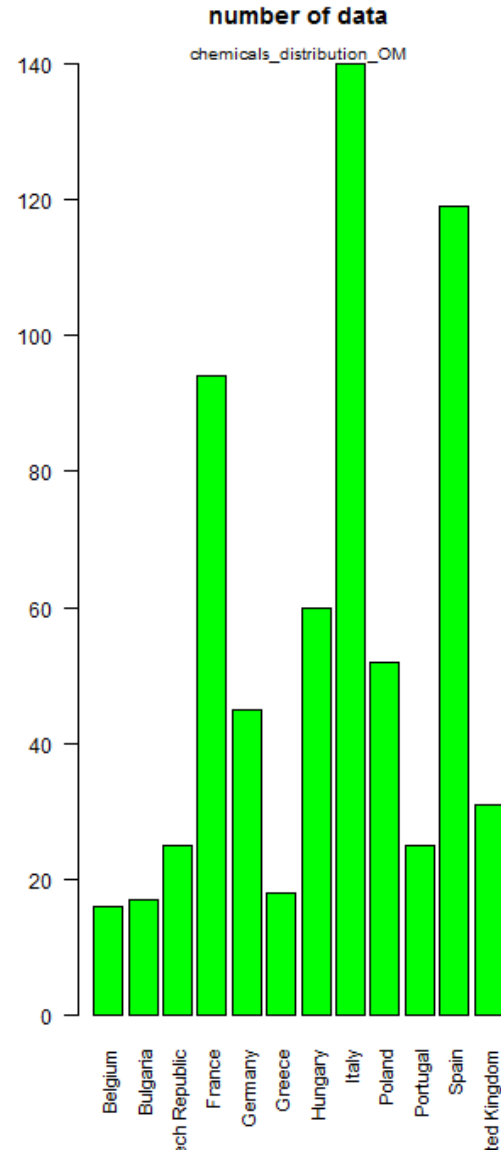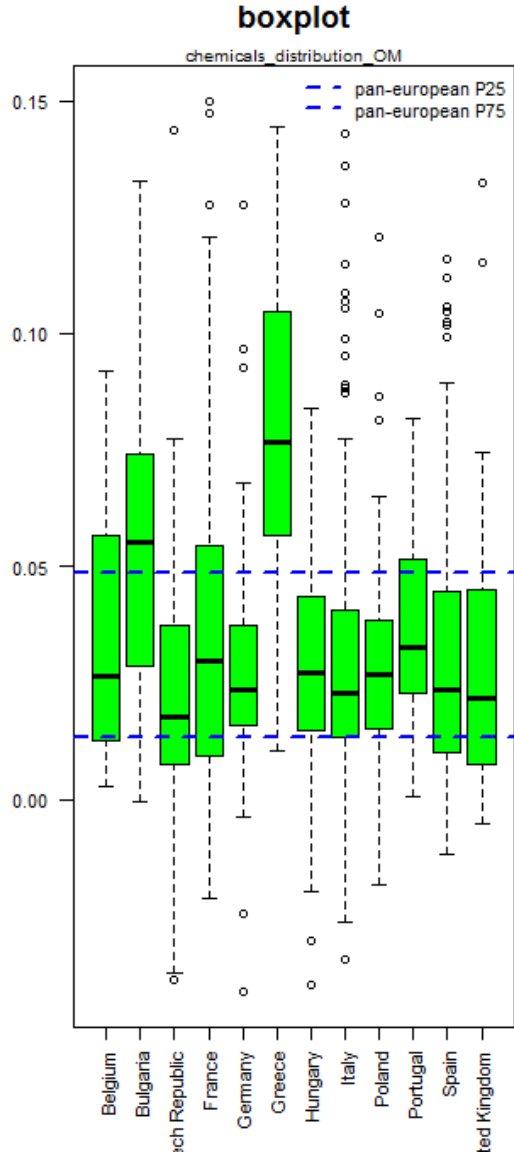
Automotive manufacturing

Data visualisation
Automotive manufacturing

12 countries
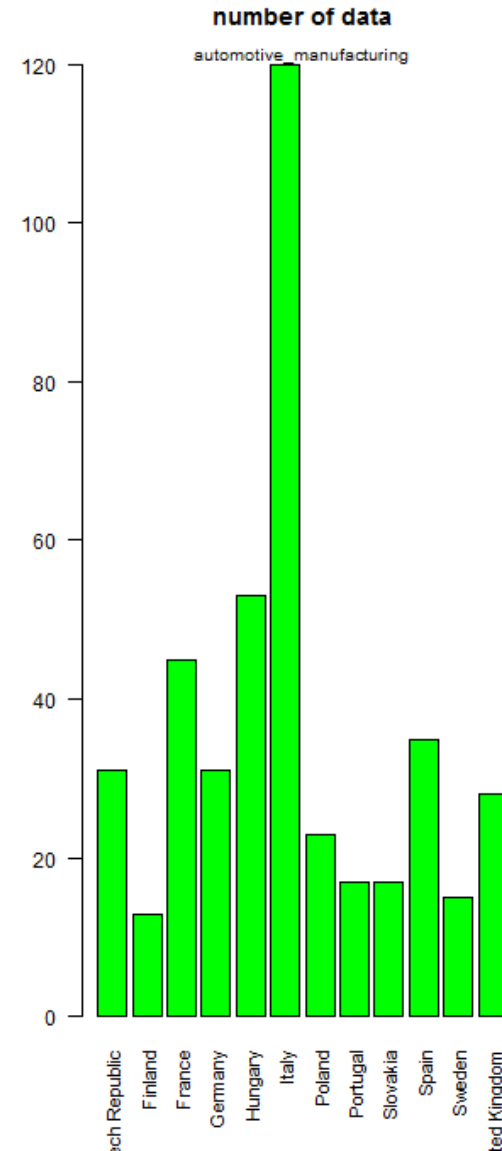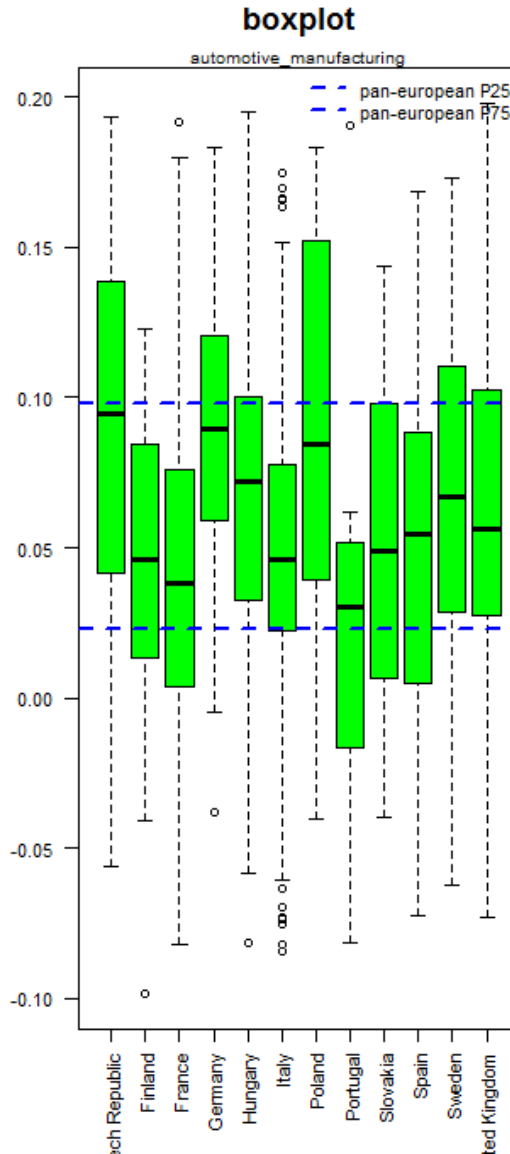
Vehicle parts distribution

Data visualisation
Vehicle parts distribution

13 countries
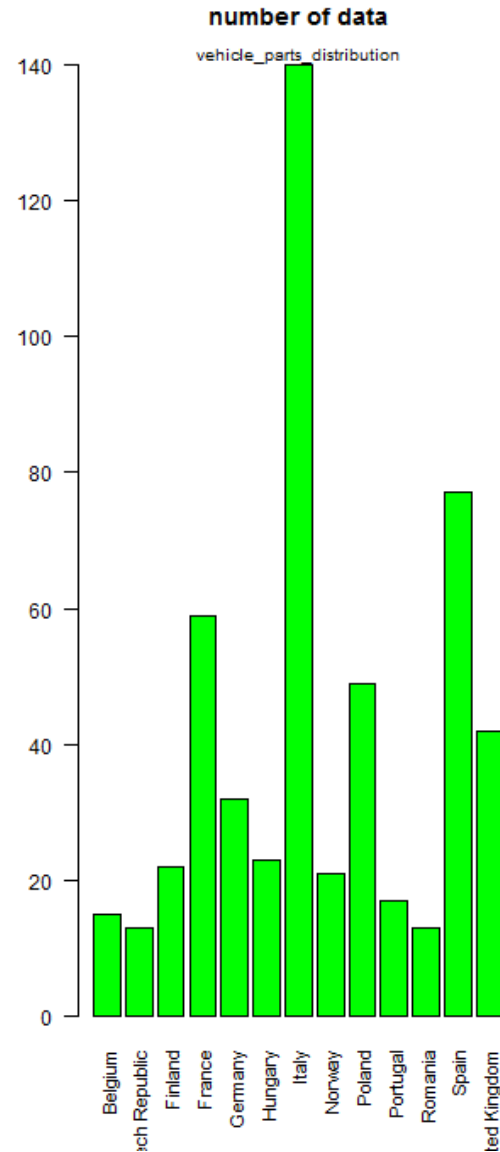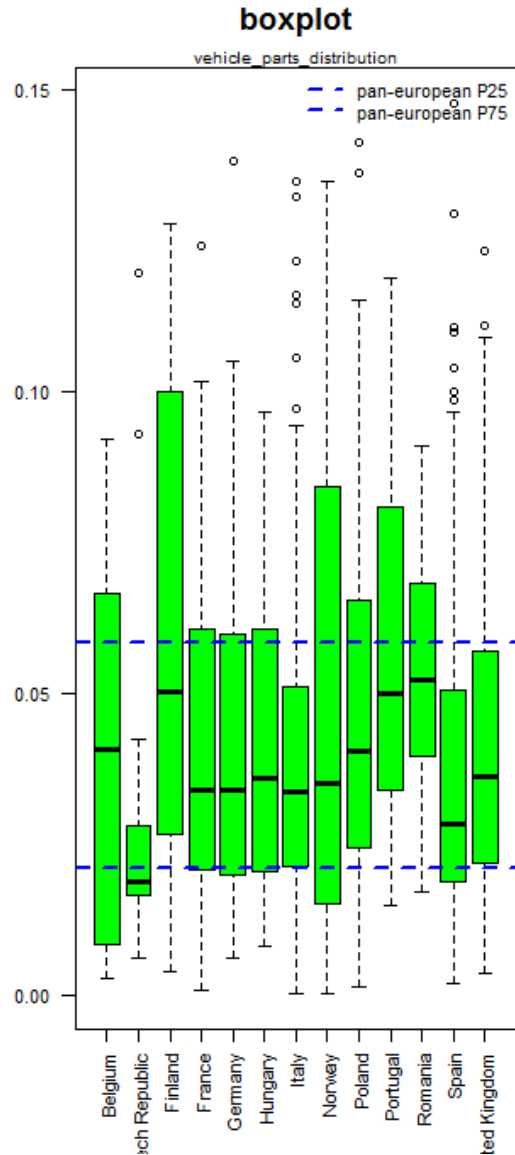
Computer services

Data visualisation
Computer services

11 countries
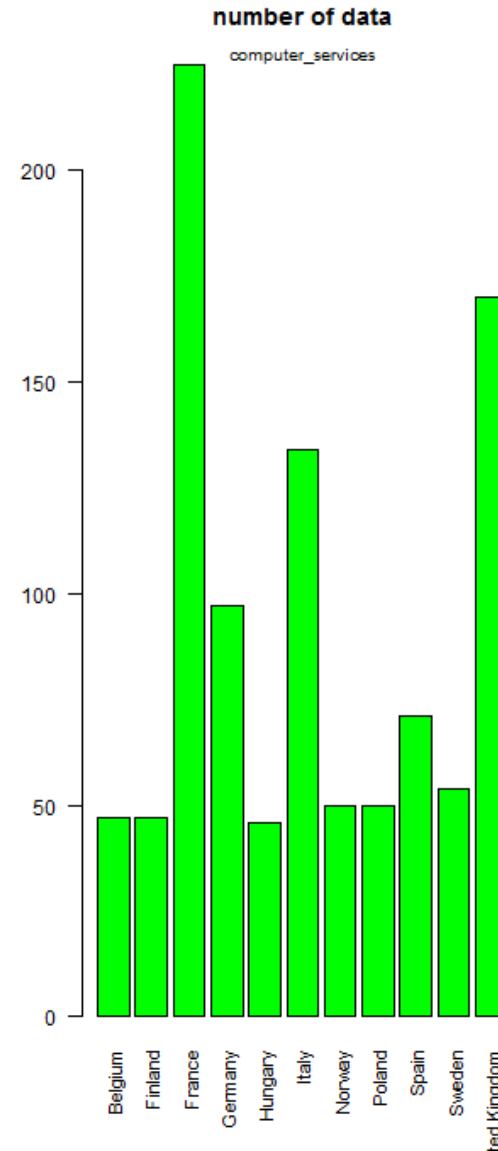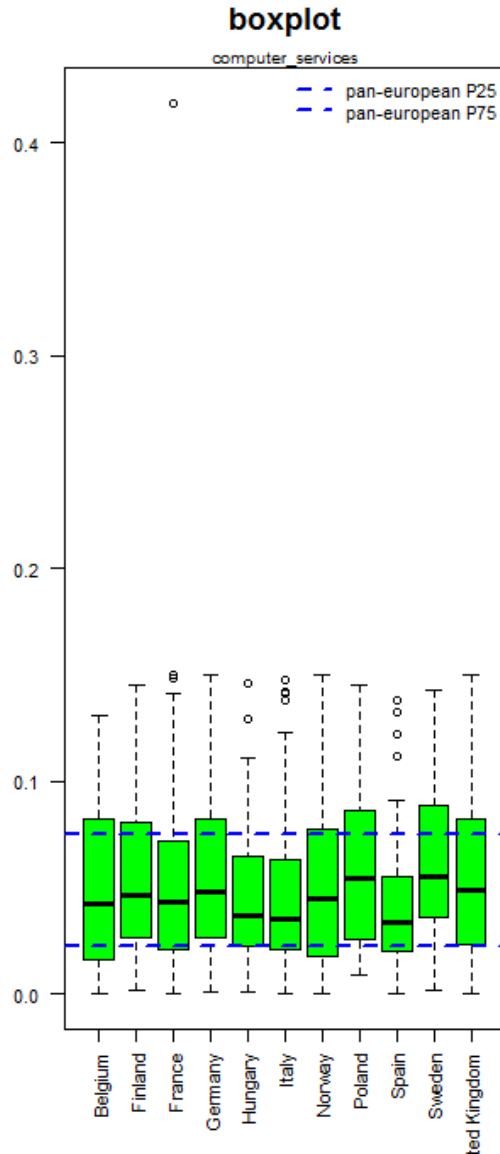
Food distribution

Data visualisation
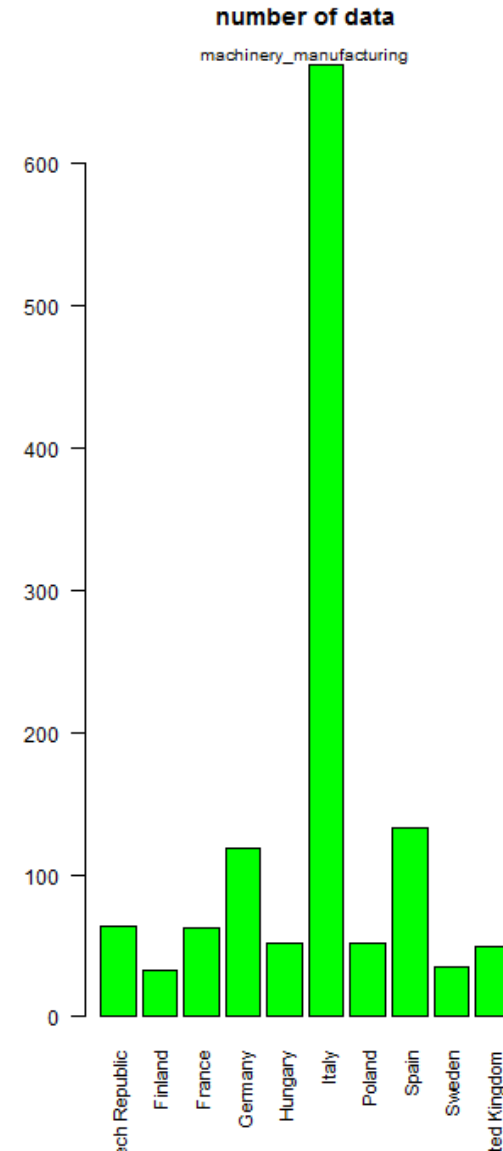## Food distribution

18 countries
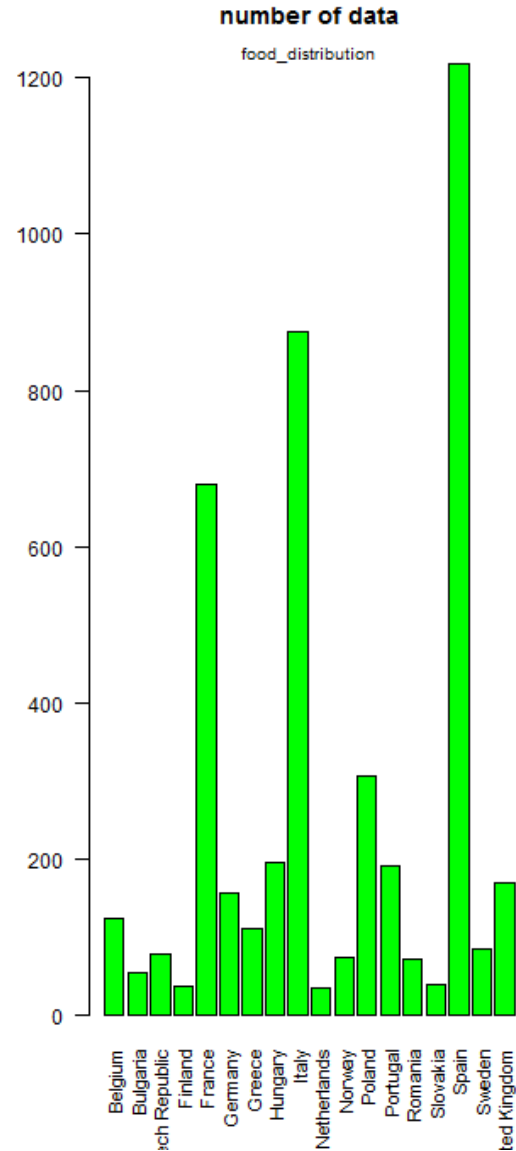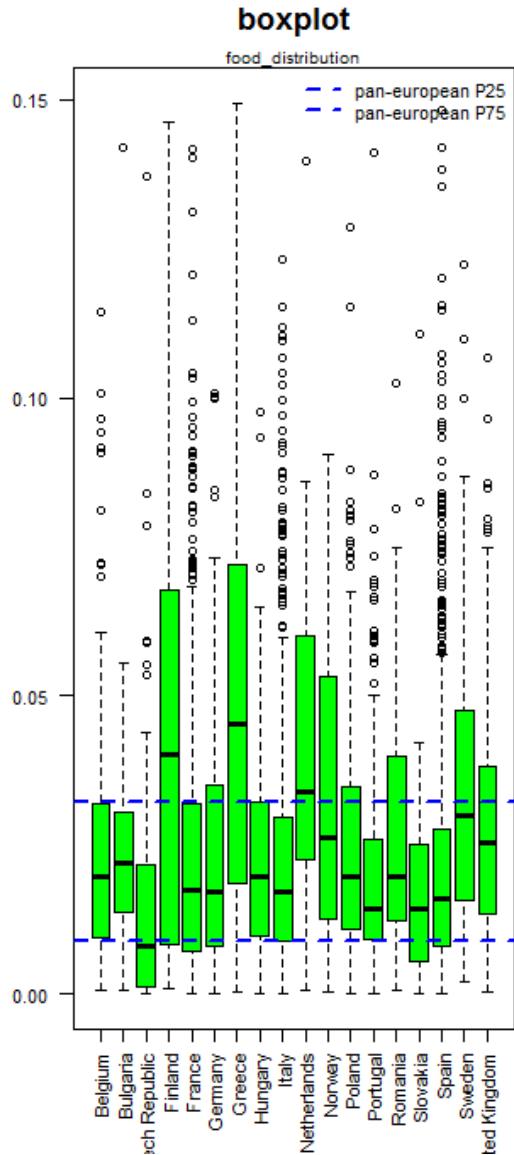
Machinery manufacturing

Data visualisation
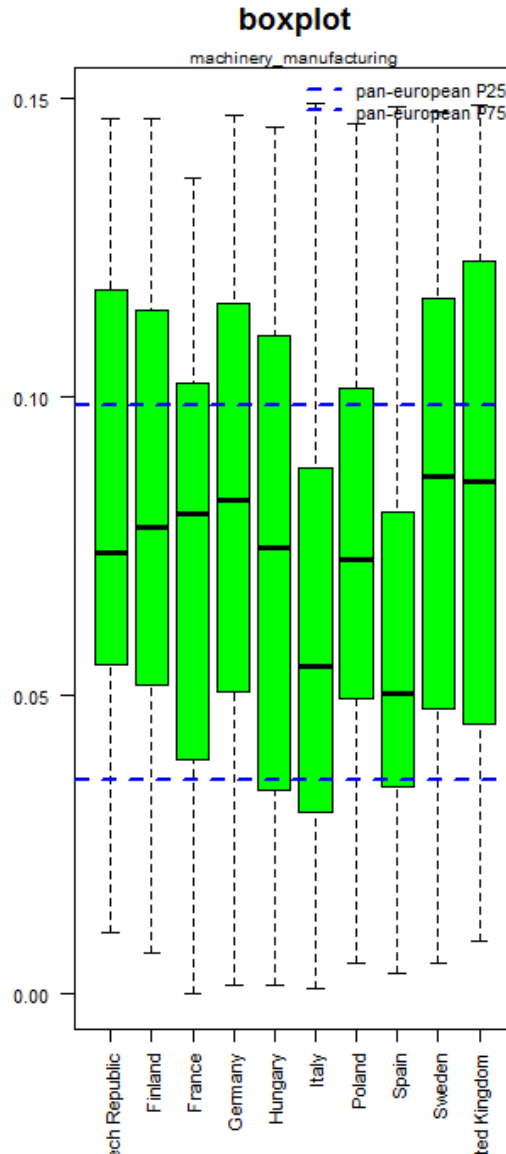## Machinery manufacturing

10 countries

Printing industry

Data visualisation
Printing industry

12 countries