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**EU JOINT TRANSFER PRICING FORUM**

**PROPOSED TOPICS FOR DISCUSSION ON**

**CENTRALISED INTRA-GROUP SERVICES**

**BY THE BUSINESS MEMBERS**

**Document prepared by the Business Members of the JTPF**

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## **POSSIBLE TOPICS TO DISCUSS**

### **INTRODUCTION**

We attach the results of a survey conducted within the PwC EU Transfer Pricing network on local rules and practices related to “centralised intra-group charges”. It is destined to serve as a basis for identification of topics which may be further addressed by the Forum. The attached grid focuses on perceived issues from a mere pragmatic perspective when dealing with cross-border HQ charges and are in no way to be seen as an interpretation of law or administrative guidance.

We list potential issues to be dealt with in more depth based on the process set out below:

- I. Identification of all central costs
- II. Deduction of shareholder/stewardship expenses
- III. Determination of allocations key(s)
- IV. Determination of the mark-up
- V. Supporting documentation
- VI. Other

We suggest to elaborate further on II to VI

#### **I. IDENTIFICATION OF ALL CENTRAL COSTS**

The first step shall be the identification of all central costs that are not incurred in respect of discrete entities.

#### **II. DEDUCTION OF SHAREHOLDER/STEWARDSHIP EXPENSES**

The second step shall be the deduction of the costs that are classed as shareholder/stewardship expenses and therefore not for the benefit of the subsidiaries.

The basis for determining which expenses for intercompany services must be allocated to related parties is the “benefit test.” The benefit test essentially provides that when a member of a group of controlled entities provides services for the benefit of another member or grants the availability to have access to its services as the case may be, the service provider is to receive an arm’s length charge for that service.

Apart from the relevance in the conduct of transfer pricing rules and practices, the concept is in the natural course of events also dealt with under local rules on business relief. Indeed, costs need to be real and inherent to the professional activity of the party that incurred the cost.

An allocation may generally be made if the service was intended to benefit another member, either alone or with other members of the group. Allocations between related entities are to be consistent with the relative benefits intended from the services, hence the term, “benefit test.”

On the contrary, if the probable benefit to the related member is so indirect or remote that unrelated parties would not have charged for the same services, no allocation should occur. Furthermore, an allocation generally should not occur if the service constitutes a stewardship or oversight-type activity undertaken by a parent corporation.

The OECD Guidelines (§7.6) stipulate that services are to be assessed on the basis of whether they provide a “group member with economic value to enhance its commercial position”. A strict assimilation of this test to a “willingness to pay” analysis in an open-market context risks to lack sense for pragmatism.

In the EU countries, there are no specific rules concerning the benefit test but it is felt to be a major issue in practice in Germany, Hungary, Italy, just to name a few.

The OECD Guidelines<sup>1</sup> only offer limited guidance in defining “stewardship activity.” The Guidelines only state that a stewardship activity may be distinguishable as a *broader* term than “shareholder activity,” which covers a range of activities by a shareholder, including the provision of services to other group members. The shareholder activity term is more narrowly defined in the OECD guidelines. The OECD Guidelines (§7.10) provide three examples of activities that constitute shareholder activities:

- Activities relating to the juridical structure of the parent company, such as shareholder meetings, issuing shares of parent company stock, and activities of the supervisory board.

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<sup>1</sup> The 1984 report has not been included in the 1995 Guidelines

- Activities relating to fulfilling reporting requirements of the parent; and
- Raising funds for the acquisition of the parent's participations

The OECD Guidelines also refer to “costs of managerial and control (monitoring) activities related to the management and protection of the investment as such in participations”. Whether these are shareholder activities are determined by facts and circumstances.

The tax authorities in the country of the provider may argue that the central costs (even of making the supplier available) are to be charged to group companies without the need to unbundle these if the recipient will be able to obtain a benefit and thus business relief for the expenses. The benefit is to be interpreted taken into account the upside of vertical integration. For example, strictly spoken, a German subsidiary of a UK PLC does not benefit from the listing on the London Stock Exchange and should consequently not contribute to the cost. However, the listing may be only the vehicle for listing “the group”. The same is true for the expertise and management skills of the main board that risk being barred from on-charging even though the merits to the affiliates cannot be denied.

In this context, the Forum may want to address also developments under local MS' case law and also developments in non-EU jurisdictions (such as e.g. the new US Service Regulations).

In summary, the EU JTPF may facilitate a best practice approach as to clarify what activities constitute stewardship services by e.g. providing conceptual guidance as well as further examples (e.g., treatment of common corporate expenditures such as annual corporate and tax filings, management accounting activities, salaries of corporate officers and directors) based on the input of all MS.

### **III. DETERMINATION OF ALLOCATION KEYS**

A question may be raised on the level of sophistication of allocation keys used. Where sales is often felt easy to manage, the correlation with the efforts spent by the provider may be questioned though it is unclear whether they necessitate a deeply refined approach with a multiple of allocation keys. Many other keys exist such as headcount, assets, number of transactions, invoices processed, regulatory filings handled, number of user IDs just to

name a few. These would cover many service centre type functions in HR, accounting, legal and suchlike departments.

Another issue is the appropriateness of certain allocation mechanisms over time.

#### **IV. DETERMINATION OF THE MARK-UP**

Concerning the mark-up there are no specific rules in any EU countries. As a matter of principle, the “added value” needs to be assessed so as to determine a fair mark-up. In that way (potentially arbitrary) “safe harbours” are rejected. In practice though, some 3-10% appears to be an acceptable margin for typical HQ services; it is however noted that the OECD Guidelines allow for charge at cost. It is relevant to observe in this context that non-OECD countries outside the EU do not necessarily agree with a range of 3-10%. Also note that the OECD draft on profit allocation between head offices and branches might give comfort for charging non core activities at cost whereas this maybe far more difficult between different legal entities.

One of the questions is e.g. whether a different mark-up per function should be the rule or alternatively whether one blended rate based on relative weight of the functions is a practical solution. The EU JTPF may be helpful in providing some guidance based on the Member States’ input.

Another question is whether a comparability study will ever produce a sample of truly comparable companies to these of a corporate centre. As an example, the difference in risk profile can be mentioned. The proceedings of the OECD with respect to comparability are to be followed-up with care.

Finally, some countries tend to put forward (probably as a mere rule of thumb) a lower mark-up on inbound charges versus outbound charges.

#### **V. SUPPORTING DOCUMENTATION**

A timesheet system to substantiate the benefit test may be felt not truly practical. The Forum may want to advise on more pragmatic tools (e.g. percentage of time spent, refined allocation keys,...)

**VI. OTHER**

The Business Members would like the Forum to address also the issue of budgeted vs actual amounts.

A user-friendly methodology would be to charge out periodically based on budgeted numbers and adjust to actual once the final numbers are known through a year-end adjustment.



	Austria	Belgium	Bulgaria	Cyprus	Czech Republic	Denmark	Estonia
1 <b>Specific legislation</b>	No	No	No	No	No	No	No
2 <b>Documentation</b>	Required	Recommended	Recommended	Recommended	Recommended	Required	Special TP documentation required only for certain taxpayers (e.g. companies and PE's not treated as SMEs under EU regulation, publicly listed companies). There are no special stand-alone documentation requirements for headoffice charges.
3 <b>Regulations and case law</b>	Letter rulings from Ministry of Finance. OECD guidelines apply	Some, mainly on benefit test	General provisions on the determination of the market prices of services provided within a group.	None	None	Some, mainly on mark-ups and benefit test	Estonian TP regulation includes general guidelines applicable for inter-company service charges. The regulation is generally in line with OECD Guidelines. No case law in Estonia.
4 <b>Benefit test</b>	No rules / substantiation needed	No strict rules, substantiation needed	No rules, substantiation needed	No rules	No rules, substantiation needed	No rules	The taxpayer is obliged to demonstrate that it benefits from the services received.
5 <b>Annual request</b>	Not required	Not if stated in the agreement	Not required	Not required	Recommended	Not required	Not required
6 <b>Agreement</b>	Required	Recommended	Recommended	Recommended	Recommended	Required	Recommended
7 <b>Allocation keys</b>	No rules	No rules	General rules giving examples of allocation keys that may be applied	No rules	No strict rules / Sales is the most common	No Rules - need to reflect share of benefit	No specific rules. The principles of OECD Guidelines should apply.
8 <b>Mark-up</b>	5-10%	4-10%	Not in legislation. 5-10% acceptable in practice	5-10%	5-10%	No specific rules, in practice from 3-10% depending on function	Arm's length mark up is generally presumed unless it is constructed as a CCA. No defined safe harbours or general practice related to the level of mark-up.
9 <b>Benchmark</b>	Recommended	Highly recommended	Recommended	Recommended	Recommended	Required upon request	Generally required unless this can be constructed as a CCA.
10 <b>Shareholder expenses</b>	OECD 7.10	OECD 7.10	No specific rules	OECD 7.11	OECD 7.10	OECD 7.10	OECD 7.11 and 7.12
11 <b>Acceptability of tax payer data</b>	Audit statement recommended	Audit statement recommended	Audit statement not required, but recommended.	Audit statement is not required	Audit statement recommended	Audit statement recommended	Audit statement is not required.
12 <b>VAT</b>	Applicable / Reverse Charge Method	May apply / Reverse Charge Method / Policy BTO not entirely clear / review recommended	HQ charges/ management services - reverse-charge may apply	May apply / Reverse Charge Method	May apply / Reverse Charge Method	May apply / Reverse Charge Method	Generally taxable supply subject to 0% at the level of service provider and application of reverse charge at the hands of the recipient
13 <b>Other</b>							

	Finland	France	Germany	Greece	Hungary	Ireland	Italy
1 <b>Specific legislation</b>	No	No but ruling possible for Headquarters, Logistic centers and R&D centers	No	No, but GMoF regulation*	No	No	No
2 <b>Documentation</b>	Recommended	Highly recommended	Required	Required	Required	Recommended	Required (according to recent case law)
3 <b>Regulations and case law</b>	General provisions on anti-avoidance and hidden profit distribution	Few tax court decisions on benefit and value, ruling possible	Some case law	Some case law	None	No specific legislation	Some
4 <b>Benefit test</b>	No rules / Major dispute	No rules / Major dispute	Major issue in practice. Cost-benefit analysis is essential.	No rules, but important	Specific Rules / Major dispute	No specific rules, but important	Major issue / Document cost-benefit analysis
5 <b>Annual request</b>	Not required	Recommended	Not required	Not required	Not required	Not required	Recommended
6 <b>Agreement</b>	Highly recommended	Highly Recommended	Required	Recommended	Recommended	Recommended	Required
7 <b>Allocation keys</b>	No rules	No rules / sales accepted but could be challenged if other allocation keys more appropriate	No specific rules, OECD applies	No rules	No specific rules, sales and # of persons accepted	No specific rules	No fixed rules, sales acceptable or other adequate criteria
8 <b>Mark-up</b>	5 – 10%	usually 5%- 10% - higher mark-up are sometimes applied for high added-value services	Pool: nil / Other: 3 - 10%	No specific rules	No specific rules	No specific rules	No specific rules. Mark up should not be applied to non core business activities
9 <b>Benchmark</b>	Recommended	Unusual	Unusual	Recommended	Required	Not required	Recommended
10 <b>Shareholder expenses</b>	OECD 7.10	OECD 7.10	OECD 7.10 / 11	OECD 7.10	Required to be eliminated	No specific rules	OECD 7.10
11 <b>Acceptability of tax payer data</b>	Audit statement not required	Audit statement recommended	Tax auditor will often require access to underlying data. Auditor statement is not sufficient	Supporting documentation/ Beneficiaries certified auditors certificate required	Audit statement strongly recommended	Supporting documentation required at time of Revenue audit // Self assessment regime	Audit statement recommended
12 <b>VAT</b>	May apply / Reverse Charge Method / Policy not entirely clear	May apply / Reverse Charge Method	May apply / Reverse Charge Method	May apply/ Reverse charge rule	Applicable / Reverse Charge Method	May apply / Reverse Charge Method	May apply / Reverse Charge Method. / Policy not completely clear
13 <b>Other</b>		Withholding tax issue when fees are deemed excessive		Very sensitive issue during a tax audit	High focus of HTA		VAT is not applicable to services between the Italian branch and its headquarter since out of the scope of Italian VAT.



	Latvia	Lithuania	Luxembourg	Malta	Netherlands	Poland	Portugal	
1	<b>Specific legislation</b>	No	No	No	No	Limited*	Art. 12° and 13° of the Administrative Decree 1446-C/2001 of 21 December 2001	
2	<b>Documentation</b>	Recommended	Required	Recommended	Recommended	Required	Required	
3	<b>Regulations and case law</b>	None	None	None	None	Extensive regulations on shareholder costs. Limited case law, mainly on mark ups	OECD applies. Many cases. Internal plan of control issued by The Ministry of Finance	Specific regulations. No court decisions yet. OECD guidelines apply
4	<b>Benefit test</b>	Not required, but recommended	Yes - no benefit if arises purely by virtue of being part of a group.	No specific rules.	No rules	No specific rules	Yes** / Major issue	Required
5	<b>Annual request</b>	Not required	Not required	Not required.	Not required, but recommended	Not Required	Not required	Required
6	<b>Agreement</b>	Recommended	Recommended	Recommended	Recommended	Recommended	Required	Required
7	<b>Allocation keys</b>	No specific rules	Must correspond to benefit received. Legislative example - turnover and headcount.	Best to follow OECD.	No rules	No rules, sales accepted	No rules; OECD applies	Specific rules
8	<b>Mark-up</b>	No specific rules	No specific rules	No specific rules / 5-10%	No rules	Policy unclear // Possibly different mark up per function	5-15% in practice	Required, 5-10% should be acceptable
9	<b>Benchmark</b>	Recommended	Recommended	Unusual	Recommended	Not often performed	Not required though recommended	Recommended
10	<b>Shareholder expenses</b>	Not required, but recommended	OECD 7.12	No specific rules. OECD 7 is influential.	No rules, but in general OECD Model principles are typically followed.	By regulation of August 2004 a non-limitative list of shareholder activities is provided.	OECD 7.10	OECD 7.10
11	<b>Acceptability of tax payer data</b>	Supporting documentation strongly recommended	Audit statement strongly recommended	Audit statement not required but recommended	No history on this due to absence of sophisticated transfer pricing rules. Tax payer data is useful, but some supporting documentation is recommended.	Audit statement recommended	Audit statement recommended	Audit statement recommended
12	<b>VAT</b>	Applicable / Reverse Charge Method	Depends on components of service/reverse charge neutrality	May apply / Reverse charge likely.	EU VAT rules apply	May apply // Reverse charge method	EU VAT rules apply	Applicable / Reverse Charge Mechanism
13	<b>Other</b>	Agreement and other supporting documentation recommended. 10% withholding tax may apply	Must avoid semblance of duplication of local functions		N/A	DTA has performed extensive research into HO functions. Approach is to identify whether HO performs "core functions" for the value chain. If so, cost plus approach is not appropriate. Marketing may serve as an example. When HO is involved in marketing, their view may be that HO should not charge out expenses but rather receive a royalty because one can argue that HO is involved as entrepreneur / decision taker in the development of brands, etc.	Documentation/ evidence proving that HQ services, for which the local subsidiary is charged, were in fact rendered. (e.g. periodical reports, analysis, e-mail correspondence, notes from conference calls, statements of employees etc.) * There is one specific paragraph in TP Decree of 10 October 1997 applicable to intangibles and "immaterial services" ** According to Paragraph 13.2 of TP Decree of 10 October 1997: " Where reasonably anticipated benefits (profit) of an entity concluding such a transaction are obviously smaller than expenditures incurred in the transaction, such expenditures, pursuant to Article 15, Section 1 and Article 22, Section 1 of the laws mentioned in Paragraph 1 Section 1, respectively, cannot be treated as revenue earning costs. In such case, the provisions of Paragraph 3, Section 3 apply."	

	Romania	Slovakia	Slovenia	Spain	Sweden	UK
1	<b>Specific legislation</b>	No	No	No	Yes, art. 16.5 corporate tax law	No
2	<b>Documentation</b>	Required	Required in case of tax inspection	Required	Required	Required
3	<b>Regulations and case law</b>	None	No case law, OECD rules apply	General provisions on anti-avoidance and hidden profit distribution	No case law	Follow OECD. Some case law mainly on mark-up of external consultancy costs, allocation keys, and negligence to charge out central costs.
4	<b>Benefit test</b>	No rules	No rules	No rules, substantiation needed	Yes/ no detailed rules	Recommended
5	<b>Annual request</b>	Not required	Not required	Recommended	Not required	Not required
6	<b>Agreement</b>	Recommended	Required	Required	Recommended	Recommended
7	<b>Allocation keys</b>	No rules	No rules, however allocation key should be in place in case of tax inspection	No strict rules / Sales turnover and number of employees are the most common	general criteria of rationality	No rules
8	<b>Mark-up</b>	5-10%	No specific policy	No clear guidance (lack of practice)	No rules/possible different mark up per service/ In practical 5-10%	5-10%
9	<b>Benchmark</b>	Recommended	Recommended	Required for every transaction	Recommended	Required
10	<b>Shareholder expenses</b>	OECD 7.14	OECD 7.15	OECD 7.10	OECD 7.10	OECD 7.10
11	<b>Acceptability of tax payer data</b>	Audit statement not required but recommended	Audit statement recommended	Supporting documentation is required / External audit statement is recommended	Supporting documentation will be required but there is no detailed rules	Supporting documentation is recommended
12	<b>VAT</b>	May apply / Reverse Charge Method	May apply / Reverse Charge Method	Reverse charge mechanism may be applied / Use & Enjoyment Rule for non-EU countries	May apply / Reverse Charge Method	May apply / Reverse Charge Method
13	<b>Other</b>			Withholding tax 15 % applicable in case of hidden profit distribution		