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EU JOINT TRANSFER PRICING FORUM

MULTILATERAL APPROACH TO TRANSFER PRICING

AUDITS WITHIN THE EU

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A MULTILATERAL APPROACH TO TRANSFER PRICING AUDITS WITHIN THE EU.

I.- INTRODUCTION

The 2015-2019 EU JTPF program of work¹ has included multilateral controls in transfer pricing as point 3.3.1. In particular, it stated that “the JTPF will collect guidance already available and invite MS which already undertake joint or simultaneous audits to provide the Forum with their experiences.”(...) ”The outcome may range from a summary of MS experiences up to specific guidance and recommendations tailored to multilateral controls in TP, particularly in the context of Fiscalis 2020”.

In 2007, the EU JTPF Report in the field of dispute avoidance and resolution procedures recognised that

“Double taxation is a real cost to taxpayers and dealing with either double taxation or the threat of double taxation uses considerable taxpayer resources. Tax administrations too recognise that double taxation has considerable disadvantages and dealing with issues of double taxation requires considerable tax administration resources.”²

Although at that time, simultaneous controls were considered as one of the possible procedures which might lessen transfer pricing burdens on taxpayers within the EU, they were not considered the best avenue for improving existing methods for the better elimination of double taxation; as the best option, it was decided to develop a better practice on APAs within the EU.

Six years later, in June 2013, the EU JTPF Report on Transfer Pricing Risk Management stands out the importance of well-founded primary transfer pricing adjustments in order to avoid economic double taxation and it points out the possibilities of simultaneous controls; in particular, it states:

“Managing transfer pricing risk is therefore not only relevant for the State considering the primary adjustment, but also for the other States affected by this primary adjustment. There is a risk that more resources than necessary are invested by States, e.g. because of timing mismatches or different levels of information. The problem is multiplied in multilateral situations, where the adjustments concern more than one State. A coordinated action at an early point in time between the MS involved may help to address these issues. The EU Directive on Administrative Cooperation (2011/16/EU) provides for simultaneous audits or even joint audits may - given the bi- and multilateral nature of transfer pricing - be especially useful in the context of transfer pricing. It may also be helpful if there is a possibility for taxpayers to propose such simultaneous audits in

¹ DOC:JTPF/005/FINAL/2015/EN

² Point 8 of the Report prepared by the EU Joint Transfer Pricing Forum accompanying document to the COMMUNICATION FROM THE COMMISSION TO THE COUNCIL, THE EUROPEAN PARLIAMENT AND THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE on the work of the EU Joint Transfer Pricing Forum in the field of dispute avoidance and resolution procedures and on Guidelines for Advance Pricing Agreements within the EU {COM(2007) 71 final}

*situations where issues are foreseeable. Such a possibility may be regarded as closing the gap between Advance Pricing Agreements (APAs), which generally only apply before the assessment and the MAPs, which are in practice in most cases applied after an assessment, even though simultaneous audits are an instrument for exchange of information and the auditors may not have the authority to negotiate agreements. A common documentation package consistent with the EU TPD is especially useful for simultaneous or joint audits.*³

There are already some experiences in transfer pricing simultaneous controls within the ELI. It is a fact that transfer pricing policy within a MNE is globally driven; therefore, in certain cases, it will be reasonable that several tax administrations conduct a joint examination of such transfer pricing policy. The Report on Transfer Pricing Risk Management already recognised that a multilateral approach in transfer pricing tax audits may be regarded as closing the gap between Advance Pricing Agreements (APAs), and MAPs.

Furthermore, transfer pricing simultaneous controls may contribute to more efficient control activities and certainty to the MNE as well as prevent double taxation and double non taxation situations from occurring. It is acknowledged by the OECD BEPS Action Plan that, *“transfer pricing rules serve to allocate income earned by a multinational enterprise among those countries in which the company does business. In many instances, the existing transfer pricing rules, based on the arm’s length principle, effectively and efficiently allocate the income of multinationals among taxing jurisdictions. In other instances, however, multinationals have been able to use and/or misapply those rules to separate income from the economic activities that produce that income and to shift it into low-tax environments.*⁴

II. - PURPOSE OF THIS CONTRIBUTION

This paper intends to invite the JTPF to work on some best practices for transfer pricing simultaneous controls taking into consideration the actual legal framework within the EU. The aim of these best practices would be to assist taxpayers and tax administrations participating in transfer pricing simultaneous controls and to ensure a transparent and cooperative process where their contributions will grant a more efficient and effective process.

In a simultaneous control, two or more Member States agree to conduct a simultaneous control in their own territory, of one or more persons of common or complementary interest to them, with a view to exchanging the information thus obtained. The facts might be summarised in a final report, which is not binding for the participant tax administrations.

A joint audit can be understood as a step further where tax authorities will form a joint audit team that executes the agreed audit programme jointly in all involved countries and also reaches a joint binding conclusion. From the time being, there

³Parr 16 of EU JTPF Report on Transfer Pricing Risk Management (DOC: JTPF/007/FINAL/2013/EN, June 2013)

⁴ OECD (2013), *Action Plan on Base Erosion and Profit Shifting*

is no legal framework within the European Union to perform direct taxes joint audits in this sense.

Although there are other international legal instruments which may allow simultaneous controls, such as Tax Treaties or the Multilateral Convention for Mutual Administrative Assistance in Tax Matters, this proposal is limited to some best practices within the EU legal framework, in particular within the Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation.

Therefore, the scope of this proposal is limited to simultaneous controls on transfer pricing within the EU legal framework.

III. - LEGAL FRAMEWORK

Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation should govern transfer pricing simultaneous controls. In particular, Article 12 of the Directive allows conducting simultaneous controls of one or more entities within a MNE, with economic activities in different Member States of common or complementary interest to them, with a view to exchanging the information thus obtained.

In a transfer pricing simultaneous control, Article 11 of the Directive may be also relevant as it allows, under certain requirements, the presence of officials of one Member State:

- a) To be present in the offices where the administrative authorities of the requested Member State carry out their duties;
- b) To be present during administrative enquiries carried out in the territory of the requested Member State.

with a view to exchanging the information.

IV. - GROUNDS FOR SIMULTANEOUS CONTROLS

The aim of a simultaneous control in transfer pricing should be to allocate the appropriate tax base to each Member State, avoid double taxation and double non taxation, as well as to decrease the necessity of MAPs. Joint operating tax authorities may also challenge together MNE transfer pricing policies that appear to shift profits to entities resident in low tax jurisdictions with limited contributions to the value created by the whole group.

A simultaneous control, coordinated in time, resulting in acquiring the same level of knowledge about the case and common understanding of facts and circumstances which have an influence on a MNE transfer pricing policy, may smooth the tax auditors' progress to get a more comprehensive understanding of a MNE's transfer pricing policy and the underlying economic activity carried out by the members of an MNE group before issuing a tax assessment. In particular, it may help them to know where functions are performed, how resources are allocated, who is really assuming the risks, where the assets are located and

what the value contribution from every single company within the group is.

Simultaneous transfer pricing controls can also simplify a tax audit for an MNE. In particular, when information provided by an entity of the group is exchanged among European tax administrations, other entities of the group don't need to provide it again.

A common legal approach to the case is not mandatory; however, in some instances, tax auditors could be able to establish a common understanding of the facts and circumstances of a particular transfer pricing transaction even in cases where they may not agree on how to apply the arm's length principle. Even without such a common approach, the information gathered on the economic activity of the entities can help subsequent reviewers of the case, such as Courts or mutual agreement procedure competent authorities, to solve their case in a more efficient manner. In this context, reviewers, judges or MAP competent authorities, might limit their subsequent intervention to verify the facts and circumstances and apply the arm's length principle according to the relevant legal framework.

Additionally, if facts and circumstances remain the same for the subsequent tax years and the taxpayers apply for a bi/multilateral APA, such a tax auditors' common approach could be a good starting point for an effective negotiation of a bi/multilateral APA, which will grant future certainty to the taxpayers.

V. - AREAS OF INTEREST FOR THE DEFINITION OF BEST PRACTICES

MS legal framework and practices in tax audit are different. Although each participating tax administration in a simultaneous control will carry out the audits in its own territory, a simultaneous control may allow the exchange of information directly between tax auditors.

The main purpose of the simultaneous control would be to share common information of the facts and circumstances of the transactions defined within the scope of the simultaneous control, which may be collected in a final factual report. However participant tax administrations are free to draw their national legal conclusions independently considering also the relevant double tax agreement.

Some best practices might cover the following issues. It is important that some common framework could be agreed among participants in a simultaneous control in order to coordinate the whole process. Particularly important will be to simplify the process of gathering information from the taxpayer and exchanging this information among participating tax administrations and to arrange meetings between tax administrations and taxpayers, within the scope of Article 11 of the Directive 2011/16/EU. Active and cooperative participation of the taxpayer will be extremely valuable to the whole process.

VI. - FINAL REMARKS

At a time where the inventory of mutual agreement procedure cases among Member States increases year after year, simultaneous controls in targeted transfer pricing cases may be a useful approach to avoid double taxation (and decrease the necessity of MAP cases) or to help a more efficient elimination of double taxation through MAP.

Transfer pricing simultaneous controls may be an adequate instrument to solve complex issues on transfer pricing (business restructurings, transfer of IP....) with high amounts of corporate income taxes at stake, particularly if there is an expectation that double taxation is likely to occur without a coordinated approach of tax administrations.

This paper invites the Joint Transfer Pricing Forum to further consider what work could be done in the area of Transfer Pricing simultaneous controls.

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