Knowledge Hub on Trade and Investment

Commission on Taxation

The International Chamber of Commerce (ICC), as the world business organization speaking with authority on behalf of enterprises from all sectors in every part of the world, welcomes the opportunity to comment on the Platform for Collaboration on Tax draft toolkit designed to help developing countries in the implementation of effective transfer pricing documentation requirements.

ICC appreciates the work of the Platform to collectively produce "toolkits" for developing countries for appropriate implementation of responses to international tax issues under the G20/OECD Base Erosion and Profit Shifting (BEPS) project, as well as additional issues of particular relevance to developing countries that the project does not address. ICC recognizes the efforts of the Platform to develop toolkits to help developing countries implement international tax best practices.

Firstly, we would like to welcome the outcome of the Platform particularly as any additional guidance for developing countries in connection with the transfer pricing documentation framework could be very useful to reach the common goal of standardisation; the more coherent the internal systems are, the lower the costs of compliance for the taxpayer will be as will be the costs of control by tax authorities.

1. **Does this draft toolkit effectively address all the relevant considerations for the design of an effective transfer pricing documentation regulatory system?**

   - In general terms the toolkit covers the main issues that an effective transfer pricing documentation regulatory system requires. A strong message of coherence with the OECD post-BEPS approach to transfer pricing (TP) documentation is critical, as it is a broad model generally accepted by the vast majority of countries, which has already been proved as sufficient and appropriate to report information on related party transactions and their valuation.

   - Three key aspects relating to tax compliance are relevant for any foreign investment in another country:

     - Procedural rights and duties of the taxpayer in such country, including the burden of proof;
     - Tax compliance costs; and
     - Confidentiality.

   - In light of these key considerations, ICC would like to take the opportunity to suggest the following clarifications and alternative representations:

     - **2.1.2) Burden of proof**: ICC appreciates the assessment that it is pivotal to any transfer pricing regime to clearly define the burden of proof. It is undisputed that different jurisdictions follow different definitions of the procedural burden of proof. Still, a clear and reliable definition of the burden of proof is at the heart of any transfer pricing dispute and, therefore, of particular significance for any regulatory system. This being said, the toolkit itself uses language which implies that, as a general rule, the burden of proof was on the taxpayer. For example, in chapter 1.6. *Policy principles* the text reads "*[…] a taypayer on how to* ***demonstrate to*** *the tax administration that its transfer pricing is consistent with the arm's length principle*" (emphasis added). In chapter 3.3.1 *Functions of transfer pricing studies* it reads as first bullet "***evidence*** *that taxpayer has complied with the transfer pricing rules*" (emphasis added). This choice of language implies that at least *de*

facto the burden of proof was on the taxpayer irrespective of the definition applied by the respective jurisdiction. In order to rule out any misunderstanding, the toolkit should (i) define the different duties covered by the report more clearly from the outset (as done in more detail in Part III. of the toolkit) and (ii) refrain from biased language in Part I. and II. of the toolkit. Procedurally, the toolkit should differentiate clearly between the duty to prepare a transfer price documentation, the duty to provide relevant information and (substantiating) documents, the duty to accumulate and keep relevant documents, (if applicable) the duty to file a transfer pricing return and other duties to cooperate (e.g. answering a transfer pricing questionnaire).

The toolkit should make clear that the duty to prepare a transfer pricing documentation report (Master or Local File) may be interpreted to merely require the taxpayer to prepare documentation of facts, including the methodology and reasoning applied by the MNE in determining the transfer prices. In this case, the taxpayer should not be required to prepare, for example, a benchmark study or other means of evidence.

Also, in some jurisdictions (e.g. Germany) the burden of proof is on the tax administration at any time; the burden of proof does not shift to the taxpayer in case of insufficient transfer pricing documentation. Rather, the legal standard of proof is reduced (e.g. a lower degree of probability that the transfer price does not comply with the arm's length standard). This differentiation is particularly important in transfer pricing disputes which rely heavily on the interpretation of the facts and the burden of proof. A more open definition of the burden of proof should lead to a higher degree of legal certainty for the taxpayer and, thus, foster investments in such jurisdiction. This alternative definition of the burden of proof could be added to chapter 3.3.5 *Enforcement*.

- **2.2) Confidentiality**: As regards to the provision of public disclosure of certain tax return data in relation to (large) corporations, it is important to balance the information that can be requested from the taxpayer and the commercial sensitivity of such information (IP, competitors, business strategies). There is a need to reinforce mechanisms to avoid public disclosure of confidential information so that the tax system can be considered as reliable by taxpayers and thus investments are secured.

  ICC appreciates the confidentiality conditions laid out on page 59 under chapter 3.4.1.1 *Country by Country Reporting and developing countries* of the toolkit. This level of domestic and international safeguards to the business, trade and tax secrets of multinational enterprises should be applied to any transfer pricing measure outlined in the toolkit as well as any other tax measure.

- **2.4) Penalties and compliance incentives**: Table 4 includes penalty conditions for the TP Annual Returns or Schedules, like: "*b) Submission of an incomplete return*" and "*c) Making an incorrect return*". It would be very useful if the toolkit also provided guidance on how to treat cases where a taxpayer incurs in both conditions. We believe it is important to provide guidance on this aspect because most of the developing countries are likely to apply both penalties, which would be an unreasonable solution because the failure to comply is related to the same legal duty.

  It should also be made clear that the level of penalties applied in case the taxpayer fails to provide a Master File (at all or in part) or a country by country (CbC) report should be limited compared to the failure to provide a Local File. The former serve as a basis for a mere high-level risk assessment based on consolidated information and data whereas the latter provides the basis for in-depth investigations of the relevant IC transactions of the local taxpayer and thus, the domestic tax base. The failure to provide sufficient documentation should, therefore, be treated differently, both with respect to the definition of the burden of proof and the applicable penalties.

- As indicated on page 47 of the toolkit, a significant condition to imposing penalties should always be that the taxpayer has failed to take reasonable efforts to gather and prepare the relevant documentation based on the available information. In light of this, the following chapter should be revised.

    - **2.5) Accessing documents held outside the jurisdiction**: Despite other representations in this chapter, it is not uncommon – because of internal procedures, confidentiality policies, or other internal or external restrictions – that multinational enterprises refrain from sharing specific information, like for example: details of a particular costs and expenses structure; the profit earned by foreign group companies in related party transactions; confidential contracts with the customers/clients or suppliers of the related party, etc. So, in this case, the toolkit could suggest that the local tax administration files for an information request with the other country's tax administration (international exchange of information, EOI) due to the taxpayer's (legal or *de facto*) inability to access related party information. Apart from implementing double tax treaty, MCAA or TIEA EOI mechanisms, developing countries may in some cases also request such information based on the general rule of reciprocity in international law.

    - ICC would appreciate it if the Platform for Collaboration on Tax considered amending its wording on page 24 according to which it is unlikely that local management will be denied access to information concering wider (group) operations. In practice, it is, rather, likely that relevant information on group operations are not shared with the management of routine group entities, in particular, in case of doubts on the local confidentiality standards (see above).

    - In light of this, the wording on page 24 should also be changed where it is implied that local management had failed its fiduciary duties if a tax return is filed without safeguarding access to the requested information and documents. In many jurisdictions this statement should be inaccurate as the fiduciary duty of the local management should be to verify whether the declared income and expenses and, therefore, the declared profit is substantiated by proper invoices. The local manager should, however, be unable to verify whether the transfer prices (which in most cases are determined on a global level) comply with the arm's length principle. Also, as outlined above, such management should not have access to all relevant information. Holding such management responsible for such lack of information is clearly unfair.

- Also, requesting transfer pricing returns, documentation reports or questionnaires should never be a self-serving purpose. On page 45 of the toolkit the Platform for Collaboration on Tax outlines that some tax administrations may be unable to prepare yearly or periodic risk assessments. In this case, it should be ensured that appropriate limits are established by the local jurisdiction for the tax administration to make transfer pricing adjustments after a certain deadline. It is important to provide for a system of mutual compliance, both on part of the taxpayer and on part of the local tax administration. At the same time, as indicated on page 77 of the toolkit, the use of transfer pricing questionnaires should be limited to *ad hoc* requests (e.g. during tax audit). To minimise **compliance costs** and foster foreign investments, it should be recommendable to avoid any form of fishing expedition on the part of the local tax administration.

2. In terms of enforcement of transfer pricing documentation, are particular approaches (e.g. penalties or compliance incentives) especially beneficial for limited capacity developing countries?

- Clear rules and measures on investigating the facts of the case are preferable to a legal system where the inability to comply with requests by the tax administration are sanctioned

by penalties and/or result in a shift of the burden of proof.

- When dealing with scarce resources, the legal framework should focus on "simplification and exemption" measures:

    - Little consideration should be given to low-risk transactions, such as those taking place within the same jurisdiction (e.g. approach followed by Canada, Germany) or within the same tax unit/ tax consolidation group (e.g. Spain, US).
    - Reasonable materiality thresholds are key in order to balance the administrative burden of taxpayers and tax authorities. MNEs usually have branches/affiliates in developing countries that are comparatively small, in a start-up phase and/or conduct mere routine functions, so the transfer pricing risks should be limited considering the limited level of value-adding activities and a low amount of IC transactions. Therefore, tax authorities' efforts should be focused on those companies which pose a higher transfer pricing risk.
    - The use of "safe harbours" to low risk transactions is recommendable. This would reduce both the workload of tax administrations and taxpayers, without undermining proper levels of control and tax collection.

- In this regard, seeking for standardised approaches should also be seen as an appropriate tool for developing countries with limited capacity. The more standardised the practice is the easier it will be to follow-up and comply, which will revert in benefits for both tax authorities and taxpayers. To this end, full alignment with the outcome of BEPS Action 13 would be advisable, in particular regarding the content of the Local File and Master File.

3. Are there other transfer pricing documentation requirements not covered in this toolkit that should be considered?

- Some developing countries include in their domestic tax law regime a duty related to the provision of additional documents and information. This set of documents may differ from the regular supporting documents to be kept by all taxpayers, like contracts and invoices (e.g. the referred additional supporting documents may include valuation reports prepared either by a third party service provider or by the company itself or third party invoices and other external or internal means of evidence, which could be difficult to access for the local taxpayer).

  In this case, legal limitations should be introduced on the local tax administration's right to request and to evaluate information and/or documents which the tax administration deems relevant to the case. In cases where the local taxpayer shows (with reasonable effort) its inability to provide requested information/documents it should be more reasonable for the tax administration to request an exchange of information with the other country or (if applicable) to request the information directly from another company.

- As for transfer pricing returns, as they are usually requested together with the standard transfer pricing documentation report (i.e. Master File & Local File), the information to be included should not be redundant. Duplications of the transfer pricing documentation report should be avoided. This should reduce tax compliance costs while providing local tax administrations with access to necessary information for conducting risk assessments and verifying the appropriateness of set transfer prices. In fact, the quantitative information which is usually reported in a transfer pricing return is similar to that included in the Local File.

- The same approach should be taken in connection with transfer pricing questionnaires and any other additional documentation requirement. The preparation of proper transfer pricing documentation is a burdensome task for taxpayers. Therefore, the request for documentation beyond BEPS Action 13 should be carefully justified, in terms of risk assessment, in order to avoid duplicities and inefficiencies.

4. What additional considerations and/or tools can be included in this toolkit to assist developing countries to implement effective transfer pricing documentation?

- As a general rule, countries should balance the level of exigence in terms of transfer pricing documentation with their capacity to control compliance.

- It could be very helpful if the toolkit included more detailed suggestions and examples on the kind of documentation or level of supporting documents that a local tax administration could request from the taxpayer. As indicated above, there are cases where the local tax authorities request documents to which the local taxpayer has no access as they are in the exclusive possession of an affiliated entity. In these cases, it would be reasonable that the tax administration asks for support from the company which possesses the document, uses the exchange of information mechanism (in case of a foreign entity) or issues a direct request note (in case of a local entity).

- With regards to the CbC report, consistent implementation among countries, following the BEPS Action 13 standards, are essential to avoid asymmetries of information and appropriate use of the information. This means that protocols to allow for automatic exchange of CbC reports need to be fully in place before imposing any respective duties on the taxpayer. Also, taxpayers should not be required to file its CbC report in more than one jurisdiction.

- In addition, guarantees of confidentiality among the countries that intend to require the filing of the CbC report should be reviewed by an independent body like the OECD before the introduction of the filing requirements in those jurisdictions. The work of the Global Forum on Transparency is very much appreciated in this respect. The conclusion from the second phase of the peer review of the minimum standard on BEPS Action 13 was that 41 jurisdictions have received a general recommendation to either put in place or finalise their domestic legal or administrative framework, and 17 jurisdictions received one or more recommendations to make improvements to specific areas of their framework. Taking these conclusions into account, jurisdictions in which its domestic legal or administrative framework is not finalised or is incomplete at the time they received the CbC reports should not have access or the right to use the information contained in the CbC report and /or the faculty of imposing any related penalty.

- As CbC reports contain very sensitive information, sufficient safeguards and tax certainty on their appropriate use should be provided to taxpayers before requiring the filing/exchange of CbC reports. Accordingly, getting access to the CbC report could be seen as an incentive for countries to join the OECD Inclusive Framework.

- Finally, as a suggestion, the Toolkit could be completed with reference to the information that the tax authorities could request from taxpayers in the process of an Advance Pricing Agreement (APA) or a Mutual Agreement Procedure (MAP), as it is not unusual that tax administrations in developing countries do not have broad expertise in these fields and may tend to request information which is irrelevant and to an extent which is ineffecient.

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