

OECD BEPS Project – First Set of Deliverables

Septembre 2014

On-line Tax Strategies

The Organisation for Economic Co-operation and Development (“OECD”) presented in a September 16, 2014 webcast its first set of deliverables following its Action Plan to address Base Erosion and Profit Shifting (“BEPS”). BEPS refers to the reduction in governments’ tax revenues resulting from the erosion of their tax base, particularly through the shifting of profits by multinational corporations to low-tax or no-tax jurisdictions. Two of these BEPS deliverables address transfer pricing, namely, the transfer pricing of intangibles, and transfer pricing documentation together with country by country reporting.

Impact on Taxpayers

The impact of these new guidelines on Canadian taxpayers could be significant given that the Canada Revenue Agency has historically heavily based its interpretation of the transfer pricing laws on the OECD guidelines. Increased scrutiny of transactions involving intangibles will almost certainly be the result of the OECD’s new outlook on the transfer pricing of intangibles. In addition, it appears likely that the documentation and reporting burden will increase as a consequence of the OECD’s new standard involving its three-tiered approach.

Transfer Pricing Documentation and Country by Country Reporting

On the issues of transfer pricing documentation and reporting, a three-tiered approach is presented as the new OECD standard. This standard consists in:

1. a master file;
2. a local file; and
3. a country by country report.

The master file contains a high-level overview of the multinational enterprise’s business, the local file includes detailed information on specific group transactions, and the country by country report requires taxpayers to provide information by jurisdiction (revenues, profit (loss) before income tax, income tax paid¹ and accrued, stated capital and accumulated earnings, number of employees, and tangible assets other than cash and cash equivalents) and by constituent entity (country of organisation/incorporation and main business activity).

According to the OECD, the objective of this approach is to provide tax administrations with useful information to assess transfer pricing risks without imposing unreasonable compliance costs and burdens on businesses. Although the content of the master file and country by country report have been finalised, there remains the issues of how they should be filed with and disseminated to tax administrations. These issues will be addressed in the coming months.

The Transfer Pricing of Intangibles

The OECD’s deliverable pertaining to the transfer pricing of intangibles contains final guidance on location savings, assembled workforce, and group synergies. Final guidance is also provided on the definition of intangibles, identifying transactions involving intangibles, and determining arm’s length conditions for transactions involving intangibles. As well, interim guidance is provided on the allocation of returns derived from intangibles.

With respect to location savings, the new guidance indicates that where location savings exist and are not passed on to customers or suppliers, local market comparables should be used to determine how the location savings should be allocated among the associated entities. Where such local market comparables are

¹ On a cash basis.

not identified, the allocation should be based on a functional analysis.

The new guidance also states that comparability adjustments may be required in instances where a unique assembled workforce provides a benefit that other otherwise comparable enterprises do not have.

Group synergies resulting from, for example, combined purchasing power, economies of scale, combined and integrated computer and communication systems, and increased borrowing capacity may not exist within potentially comparable independent companies. In such cases, the new OECD guidance states that the need for comparability adjustments can also arise. In addition, the OECD clarifies its existing guidance which suggests that an associated enterprise should not be considered to receive an intra-group service or be required to make any payment when it obtains incidental benefits attributable solely to its being part of a larger multinational enterprise group. The new guidance maintains this statement but adds that where the benefit is the result of deliberate concerted group actions, this benefit and its corresponding burden should be shared in proportion to the participants' contribution to the creation of the synergy.

The new guidance defines an intangible as "something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances." Consequently, the OECD points out that an intangible may exist for transfer pricing purposes even if it is not recognised as such for accounting purposes. In addition, legal protection or separate transferability are not necessary conditions for an item to be characterised as an intangible.

The interim guidance on the allocation of intangible returns suggests that although the legal ownership and contractual arrangements are the starting point for a transfer pricing analysis, the parties contributing to the development, enhancement, maintenance, protection, and exploitation of the intangible must be appropriately compensated. Such parties include those actually performing the functions, using the assets, and bearing the risks. However, the OECD suggests the parties controlling these activities should also be compensated.

This final guidance will be included in Chapters I, III and VI of the *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, the OECD publication on which most transfer pricing legislations rely worldwide.

This work represents the first phase mandated by the BEPS Action Plan (Action 8). The second phase (Actions 9 and 10), which will address risk, recharacterisation of transactions, and hard to value intangibles, is to be completed in 2015.

Pascal Saint-Amans, Director, Centre for Tax Policy and Administration at the OECD, concluded the webcast by clarifying that these deliverables, although agreed by consensus, will not be formalized until next year because they might be impacted by the remaining eight deliverables that are due in 2015.

Your Raymond Chabot Grant Thornton advisor can help you determine which measures apply to your business and can help you undertake the necessary steps to use them. Do not hesitate to contact us.

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