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COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL AND THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE

on the work of the EU Joint Transfer Pricing Forum in the period July 2010 to June 2012 and related proposals 1. Report on Small and Medium Enterprises and Transfer Pricing and 2. Report on Cost Contribution Arrangements on Services not creating Intangible Property (IP)

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1. INTRODUCTION

It is commonly accepted that increased globalization gives rise to practical problems for both multinational enterprises (MNEs) and tax administrations (TA) when pricing, for tax purposes, cross-border transactions between associated enterprises. The approach adopted by European Union (EU) Member States (MS) to correctly evaluate the price of such transactions is that of the arm's length principle (ALP)[1]. The ALP is based on a comparison between the conditions applied by associated enterprises and the conditions that would have applied between independent enterprises.

However, the interpretation and application of the ALP does vary between both tax administrations and tax administrations and business. This can result in uncertainty, increased costs and potential double taxation or even non taxation. These impact negatively on the smooth functioning of the internal market.

To address this, the EU Joint Transfer Pricing Forum (JTPF), an expert group, was set up by the Commission in October 2002[2], to find pragmatic solutions to problems arising from the application of the ALP, in particular within the EU. In 2011, the mandate of the JTPF was renewed and extended until 31 March 2015 by way of a Commission decision[3].

This Communication reports on the work of the JTPF for the period July 2010 to June 2012 and draws conclusions on the future work of the expert group.

2. SUMMARY OF ACTIVITIES OF THE EU JOINT TRANSFER PRICING FORUM

In the period July 2010 to June 2012, the JTPF met six times. Detailed reports were completed on two subjects. One addresses specific considerations on transfer pricing for small and medium enterprises in the EU and the other addresses a particular intra

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1 The arm's length principle is set forth in Article 9 of the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention. OECD has also developed Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

2 Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee: 'Towards an internal market without obstacles — A strategy for providing companies with a consolidated corporate tax base for their EU-wide activities' COM (2001) 582 final, 23.10.2001, p. 21.

3 Decision 2011/C 24/03 of 25 January 2011 (OJ C 24, 26.1.2011, p. 3-4).

group arrangement known as a cost contribution arrangement. Monitoring exercises to gauge the level of implementation of previous JTPF initiatives were also completed. Following its renewed mandate, the Forum agreed in June 2011 updated Rules of Procedure and a new work programme 2011-2015. Discussions commenced in the period, but yet not concluded, cover the following topics from the work program: risk based approaches to transfer pricing, issues related to double taxation resulting from secondary adjustments, and compensating/year-end adjustments. The JTPF will continue addressing these issues, together with monitoring, in the forthcoming meetings.

2.1. JTPF conclusions on small and medium enterprises and transfer pricing

A general feature of transfer pricing is the administrative burden it creates for taxpayers and tax administrations. Small and medium enterprises (SMEs) face particular difficulties as a result of their lack of knowledge, experience of the subject and resource availability. Tax administrations also face challenges when dealing with SMEs as they need to strike a balance between applying their tax policy in an even handed manner taking into account available own resources and cost benefit considerations and avoiding undue administrative burden and unnecessary tax conflicts for SMEs and among tax administrations.

Recognising the central role of SMEs in the EU economy, the JTPF undertook an effort to examine the challenges and present proposals to improve - from a transfer pricing perspective - the environment in which SMEs operate. Although transfer pricing is not an issue for a huge proportion of SMEs, the absolute number of undertakings thus concerned may be quite high.

The report gives various recommendations for a more uniform way to consider the specific requirements for SMEs in the context of transfer pricing. It addresses the different stages of SME's compliance with transfer pricing.

In relation to the definition of SME, the report clarifies that its aim is not to agree on a common definition of SMEs for tax purposes. However, it recommends that MSs build on the criteria already used in Commission Recommendation 2003/361/EC[4] (balance sheet total, turnover, number of employees) when considering how to define an SME.

Regarding compliance with transfer pricing rules, the report contains best practices and recommended guidelines with respect to pre-audit, audit and dispute resolution. It supports the principle of proportionality as a sound approach when considering the needs of SMEs, the requirements of tax administrations and the ability of SMEs to meet these requirements.

For the pre-audit stage the report recommends ensuring an information point accessible for SMEs and raising SMEs' awareness of processes that provide certainty in advance. Further it invites MS to develop simplification measures to reduce SMEs compliance burden. For the audit stage the report recommends considering pragmatic solutions which may be based on other MS experiences and previous JTPF reports. When SMEs are audited, they should receive appropriate treatment. In the area of dispute resolutions the report recommends encouraging fast track dispute resolution

[4] Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises, OJ L 124, 20.5.2003, p. 36.

for non-complex low value SME claims and to exploring and implementing auditor to auditor contact in the framework of Mutual Agreement Procedures (MAP) and the so-called Arbitration Convention (AC)[5].

The report concludes by recognising SMEs' particular needs as regards complying with transfer pricing rules. It concludes that its findings and recommendations rely on the application of proportionality backed by a flexible implementation of that principle. Monitoring the effects of the measures recommended by the report and implemented by MS when dealing with SMEs will be a future action for the JTPF.

2.2. JTPF conclusions on Cost Contribution Arrangements on services not creating Intangible Property (IP)

Cost Contribution Arrangements (CCAs) on services are commonly used as a cost-effective means for MNEs to carry out the group's activities. The business decision to have recourse to a CCA can be justified by various reasons, e.g. reasons of economies of scale, sharing of risks, skills or resources. To avoid duplication of the work currently undertaken by the OECD on transfer pricing aspects of intangibles, the JTPF's work focusses on CCAs on services not creating Intangible Property (IP).

The report first elaborates on the different concepts underlying CCAs and Intra Group Services (IGS). The emphasis of the report is on how most expediently a reviewer can conclude that the ALP has been applied to CCAs on services not creating IP.

For this purpose the report presents the general features for determining whether a CCA is consistent with the ALP. It also provides a list of information items that should meet the requirements of most reviewers when determining whether a CCA can be regarded as arm's length.

Certain aspects are addressed more specifically as e.g. the expected benefit test, allocation keys that may be used for determining each participant's contribution, ways to measure contributions in kind, the treatment of cases where costs referred to are those initially budgeted rather than those actually incurred, as well the possible application of accounting standards generally used throughout the group.

The importance of the report regarding CCAs on services not creating intangible property is increased by the fact that it supplements the existing guidance on low value adding intra group services (JTPF IGS Guidelines) and completes the JTPF's work on intra group services.

The report concludes that compliance with its recommendations, in most cases falling within its scope, will facilitate the evaluation and make it easier for tax administrations to accept that the ALP has effectively been applied. The JTPF will monitor the effect of these guidelines regularly.

2.3. Update on the items of the work programme

During the period covered by this Report, the JTPF has addressed the remaining topics in the previous 2007-2011 work programme, and adopted in June 2011 the

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[5] Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, OJ L 225, 20.8.1990, p. 10.

new 2011-2015 work programme, which forms the basis of the current JTPF work. From July 2010 to June 2011 the JTPF's activity concentrated mainly on SMEs and transfer pricing. The report was adopted by the Forum in March 2011[6].

Carried over from the previous work programme, the first item of the 2011-2015 work programme was the development of a common approach on CCAs. This project, covering CCAs on services not creating IP, was successfully completed in June 2012[7].

On risk assessment, an important factor of transfer pricing policy which allows both tax administrations and taxpayers to maximize the effective use of their limited resources, presentations made by several members of the Forum (both MS and the Private Sector) will be the basis for future work. The group will analyse best practices in order to decide on the potential scope of EU guidance in this respect.

With respect to the acceptance of compensating/year-end adjustments, there are differing practices within the EU. A questionnaire was launched in 2011 and completed in 2012. This overview already constitutes the accomplishment of a part of the work programme. The JTPF will further analyse whether a common approach on compensating adjustments can be developed within the EU.

In some MS, a transfer pricing adjustment is accompanied by an additional adjustment. These so- called "secondary adjustments" may result in double taxation and were therefore included in the JTPFs work programme. A questionnaire was launched in 2011 and completed in 2012. Although this state of play already constitutes the accomplishment of a part of the work programme, the JTPF is analysing the effects of secondary adjustments in the EU in order to propose solutions to improve the present situation, both in relation to potential double taxation and to some practical aspects of its application.

2.4. Monitoring activity

An ongoing task of the JTPF is to monitor and manage the effective implementation of its achievements. This is done both by producing annual statistical reports and by preparing specific reports. The reports are then examined by the Commission Services and the JTPF to identify where further work by the JTPF could be carried out.

Statistical reports with respect to pending cases under the AC and on Advanced Pricing Agreements (APAs) are prepared and evaluated annually. The format of these statistical reports was improved and will be reviewed again in the future. Further additional guidance for completing the annual APA questionnaire was developed.

As the JTPF has been in place for 10 years, a broader monitoring exercise of its achievements will be carried out. The Codes of Conduct on the effective implementation of the AC and on transfer pricing documentation in the EU, the Guidelines on APAs in the EU as well as the Guidance for low value adding intra group services will be reviewed together. The aim is to evaluate the overall

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6 Appendix I

7 Appendix II

effectiveness of the implementation of JTPF recommendations endorsed by MS, and to consider how improvements might be made.

3. COMMISSION CONCLUSIONS

The Commission continues to regard the JTPF expert group as a valuable resource in addressing transfer pricing issues and providing pragmatic solutions to a variety of such issues.

In particular the Commission notes that the report on Small and Medium Enterprises and Transfer Pricing as well as the report on CCAs on Services not creating IP, address key tasks identified by the Commission when setting up the JTPF, that is to achieve a more uniform application of transfer pricing rules within the European Union.

The Commission fully supports the conclusions and suggestions of the reports in Appendix I: Report on Small and Medium Enterprises and Transfer Pricing and in Appendix II: Report on CCAs on Services not creating Intangible Property (IP).

The Commission invites the Council to endorse the proposed Report on small and medium enterprises and transfer pricing and invites Member States to implement practices that are in line with the approaches and procedural considerations contained in the Report in their national legislation or administrative rules.

The Commission invites the Council to endorse the proposed Report on CCAs on services not creating Intangible Property (IP) and invites Member States to implement quickly the recommendations included in the Report in their national legislation or administrative rules.

The Commission believes that a future periodical monitoring exercise on the implementation of the reports' conclusions and recommendations and its functioning will provide useful feedback to inform any necessary updating exercise.

In this context, the Commission encourages the JTPF to continue its monitoring activity and looks forward to the outcome of the JTPF current work programme items on risk assessment, secondary adjustments and compensating/year-end adjustments.

APPENDIX I
REPORT ON SMALL AND MEDIUM ENTERPRISES AND TRANSFER PRICING

I. Introduction

1. The Joint Transfer Pricing Forum (JTPF), as part of its agreed work programme, considered the impact of transfer pricing on Small and Medium Enterprises (SMEs). The JTPF background discussion papers on this work may be found on the DG Taxation and Customs Union website including contributions from The Federation of European Accountants and Conféderation Fiscale Européenne. This report is the outcome of that work.

II. Background

2. There are around 23 million SMEs in the EU representing 99.8% of all European enterprises. About 5% of those SMEs have associated companies where transfer pricing may be in point.[8] These figures indicate that transfer pricing is not an issue for a huge proportion of SMEs but the absolute number of undertakings thus concerned may be quite high. But, where transfer pricing is in point, SMEs face difficulties as a result of their lack of knowledge, experience of the subject and resource availability. The low figure of international intra-group trading at SME level may also reflect that those same difficulties can impede SMEs from engaging in intra-group cross border trading.

3. Tax administrations also face challenges when dealing with SMEs. Administrations need to strike a balance between applying their tax policy in an even handed manner taking into account available own resources and cost benefit considerations and avoiding undue administrative burden and unnecessary tax conflicts for SMEs and among tax administrations. Within the EU there is neither a common definition of SMEs for general tax purposes or specifically for transfer pricing, nor a common treatment of SMEs.

4. Some tax administrations already have specific SME transfer pricing measures in place. Those measures can be broadly categorised as an overall policy approach or specific administrative actions. An example of a policy approach is that of proportionality. This approach revolves around balancing compliance requirements with the SME resources available to meet that compliance requirement. An example of an administrative action is a more slim line transfer pricing documentation requirement for SMEs than that for non– SMEs.

5. The perspective of Multinational Enterprises (MNEs) is that they and SMEs often complement each other in EU business operations and each has a vested interest in the efficient operation of the other. But non-SMEs also want to maintain an appropriate 'level playing field' and not be disadvantaged as a result of responses by tax administrations to the needs of SMEs.

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8 2009 Annual Report on European SMEs (http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/performance-review/files/supporting-documents/2009/annual-report_en.pdf, page 15).

6. Business recognises that issues like management time and expert tax advisers' costs can cause SMEs to refrain from accessing expert services.

7. The JTPF in its reports on transfer pricing documentation and Advance Pricing Agreements (APA) guidelines acknowledged the need for flexibility when dealing with SMEs and transfer pricing. The documentation report refers to applying "a reasonableness test" and the APA guidelines to "facilitating access" where SMEs are involved.

III. Defining an SME

8. A common definition of an SME for transfer pricing purposes would provide an agreed departure point in facilitating the outcomes and recommendations of this report. A definition of SMEs is set out in Recommendation 2003/361/EC[9] but is not widely applied for direct tax purposes by tax administrations. The JTPF made the following observations on the use of a definition.

9. For small Member States applying a particular SME definition could result in even large domestic companies/groups being classified as SMEs. Therefore, special care must be taken regarding the SME definition applied.

10. A definitional approach can influence SME behaviours. It may be a disincentive for some SMEs to grow their business and thereby cross a defined threshold and potentially incur increased costs, administrative burden and lose access to incentives.

11. Similarly, some Tax administrations feel a too prescriptive EU SME definition would not take sufficient account of the make-up of a particular tax administration's tax base. For example, if, according to a commonly agreed definition, a large proportion of a Member State's tax base were made up of SMEs that may pose different issues than if SMEs make up only a minority of a tax base.

12. The definitions of SMEs currently used by tax administrations, either for direct tax purposes generally or for transfer pricing specifically, often 'borrow' from parts of the definition set out in Recommendation 2003/361/EC. Criteria used within the EU include the following: balance sheet value, turnover, and numbers of employees; individual or cumulative transaction values. These criteria are sometimes compounded by anti-abuse rules. The criteria may or may not be applied on a consolidated basis – i.e. at group level. Where tax administrations have not published a SME definition, either for the purposes of a general definition or specifically for transfer pricing, they are invited to consider using criteria already commonly in use.

13. The Forum considers it useful to bring together in one place a description of EU tax administration's SME definitions that are currently in place either for direct tax purposes generally, transfer pricing or both[10].

Recommendations:

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9 OJ L 124, 20.5.2003, p. 36.

10 See DOC: JTPF/001/ANNEX/2011/EN.

R1. If an EU tax administration is considering defining SMEs for direct tax purposes or more specifically for transfer pricing purposes, it is recommended it considers using criteria already used within the EU. Such an approach will also assist in reducing instances of asymmetry of treatment arising from differing SME definitions.

R2. The recommended criteria in current use consist of: balance sheet value, turnover, numbers of employees; individual or cumulative transaction values. It is recommended that all be measured on a consolidated basis, i.e. at group level.

R3. Definitions currently in use by Member States should be brought together in one place and updated regularly[11].

R4. A common EU tax definition of SMEs is recommendable and would provide an agreed starting point in the implementation of the findings and recommendations of this report, but it is not realistic to reach a common agreement in the foreseeable future.

IV. SMEs: compliance and transfer pricing

14. In the EU transfer pricing compliance currently means adherence to the arm's length principle in line with Art 9 of The Organisation for Economic Co-operation and Development (OECD) Model Tax Convention. The arm's length principle applies equally whatever the size of a MNE. However, the degree of difficulty in applying it may be greater for SMEs. The OECD Transfer Pricing Guidelines ("TPG") contain explicit acknowledgement of this difficulty in several places. For instance, paragraph 3.80 contains a specific comment in relation to compliance costs for SMEs. The OECD at paragraph 3.83 of the TPG states that "Small to medium sized enterprises are entering into the area of transfer pricing and the number of cross-border transactions is ever increasing. Although the arm's length principle applies equally to small and medium sized enterprises and transactions, pragmatic solutions may be appropriate in order to make it possible to find a reasonable response to each transfer pricing case.

15. This report considers what best practices and recommended guidelines can be discerned from current compliance activity. A useful structure for that examination is to consider pre-audit, audit and dispute resolution activities. Inevitably these rather broad categories will have some overlap.

16. A recurrent theme in tax administrations is that the approach to SMEs should be proportionate to the requirements of the tax administration and the ability of SMEs to meet those requirements. The JTPF supports the principle of proportionality as a sound approach to meeting the needs of SMEs. The JTPF also noted that an approach based on proportionality aligns itself well with the commentary on Chapter IV and V of the OECD guidelines.

Recommendation:

[11] See DOC: JTPF/001/ANNEX/2011/EN.

R5. An approach based on proportionality is welcomed by the JTPF. It seems particularly appropriate to balance a tax administration's need to even-handedly apply transfer pricing rules with the burden it might create for SMEs when complying with those rules.

Pre-Audit

17. Tax administrations want to receive and taxpayers want to pay the right amount of tax at the right time. Pre-audit activity is possibly the most effective method to enable taxpayers and tax administrations to achieve voluntary compliance – the most cost effective form of compliance. That objective is best facilitated by good communication, the provision and understanding of relevant information, supplemented by easily accessible specialist advice. Getting this interaction right has a direct impact on the level of voluntary compliance and the level of compliance burden.

Tax administration and SME communication

18. There is an increasing international recognition[12] that enhancing the relationship between a tax administration and its corporate taxpayers by means of an ongoing dialogue outside an audit is beneficial to both parties. Exchanges will be less confrontational and promote a wider and better understanding of each other's perspectives. If an audit were launched, each of the parties would start from a more informed position.

19. It is particularly difficult to build up a communication network with SMEs not least because of their limited resources. SME representative groups provide useful insight to matters of concern to their members. What seems harder to establish is a direct line of communication with frontline SMEs. Tax administrations are encouraged to seek opportunities to work with individual SMEs, representative groups and professional advisors to build or strengthen a local communication network with SMEs. For example, a relatively simple action, as already happens in some tax administrations, is to organise technical workshops. A variety of SMEs are invited to attend to discuss and seek solutions to problem areas and identify best practice. Such events can also be used to consult SMEs on transfer pricing policy initiatives a tax administration may wish to introduce.

Access to information

20. The breadth and depth of information provided to assist SMEs to comply with transfer pricing rules varies between tax administrations. It would be beneficial for both business and tax administrations to be able to access that information. Details of where that information can currently be found are contained in DOC: JTPF/001/ANNEX/2011/EN.

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12 The recent work of the OECD Forum on Tax Administration may be cited as an example.

21. The JTPF proposes that the information provided by tax administrations for this report is kept updated. Administrations should consider how best they can establish electronically accessible SME information perhaps either as a dedicated site or as an integrated part of an existing site. The site(s) would detail definitions of SMEs - generally and/or for transfer pricing, as well as any other SME transfer pricing legislation, administrative practice or training material. In addition a contact(s) address for further enquiries can be included. The web pages may also usefully include other non transfer pricing matters relating to SMEs. A list of those web pages will be held on the JTPF website.

Training

22. The possibility of producing some sort of blue print transfer pricing training module for SMEs was debated. To develop this suggestion would require a significant amount of the Forum's resource. Also it was not clear what the additional benefit the JTPF could add over locally produced material[13].

Certainty in advance of a transaction taking place

23. SMEs often seek certainty that before executing a transaction it will comply with the transfer pricing rules but they may not be aware how that might be done.

24. The mechanism generally used in transfer pricing to meet this need is an Advance Pricing Agreement. The process determines an appropriate set of criteria, agreed between the tax administration and the taxpayer, to establish the transfer price of a future transaction. However, APA rules may contain complexity thresholds or fees that make the process inaccessible or at least less accessible to SMEs. As stated at paragraphs 4.158 and 4.163 of the OECD TPG, "the nature of APA proceedings may de facto limit their accessibility to large taxpayers. The restriction of APAs to large taxpayers may raise questions of equality and uniformity, since taxpayers in identical situations should not be treated differently. A flexible allocation of examination resources may alleviate these concerns. Tax administrations also may need to consider the possibility of adopting a streamlined access for small taxpayers. Tax administrations should take care to adapt their levels of inquiry, in evaluating APAs, to the size of the international transactions involved". The JTPF has previously issued some guidelines on how best to approach the subject of accessibility and the guidelines state: Tax administrations should use their experience of the problems faced by SMEs to facilitate access to APAs for SMEs where APAs are useful for dispute avoidance or resolution. This wording is intended to encourage a flexible approach when accepting cases into an APA programme.

25. Some tax administrations offer other options to obtain a measure of certainty of tax treatment. A non-binding opinion may be given. In that case a tax administration specialist will offer a view on a transaction perhaps confirming that transfer pricing is in point and acknowledging that a suggested OECD methodology is appropriate. This approach falls short of agreeing the actual transfer price. There may be a clearance or rulings system that gives a binding view from the tax administration. The clearance or ruling obtained may be obtained ex-ante the relevant tax return.

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[13] See DOC: JTPF/001/ANNEX/2011/EN

26. Measures directed to SMEs and "small transactions" have been identified as some of the most frequently encountered simplification measures.

27. Several commentators suggest that the use of safe harbours will provide a measure of simplification for SMEs as well as saving on administrative resource and reducing compliance burden.

28. To improve clarity and transparency for both SMEs and tax administrations it is recommended that each tax administration sets out what advance certainty procedures are available on transfer pricing, how to access those procedures and the outcomes that can be expected. Information currently available is contained in the DOC: JTPF/001/ANNEX/2011/EN.

Pre-audit recommendations:

R6. To facilitate voluntary compliance Member States should ensure SMEs have access to up to date information and advice. It is recommended that each Member State establishes an electronically accessible point of information site including details of who to contact for further advice. A list of those sites will be held on the JTPF website and links provided.

R7. Member States and the business community should take opportunities to build constructive relations with individual SMEs and their representative groups.

R8. Member States should seek to increase SME awareness of and ability to access processes that enable SMEs to gain certainty in advance of a transaction taking place or it being reported for tax purposes.

R9. Members States are invited to actively develop simplification measures to reduce administrative and SME compliance burden.

Audit

29. At least one Member State takes the view that a policy of exempting most transactions of its SMEs from its transfer pricing rules is a proportionate response. Clearly that approach has advantages in resource savings and certainty of treatment but it may possibly have some detrimental effects on the tax base of a country implementing it, the significance of which would vary depending on the size of the activities conducted by SMEs in such country. But asymmetries of treatment can arise if associates are not similarly exempted in other Member States

30. Other Member States take a less broad based approach when implementing the principle of proportionality. In both the audit and APA processes specific measures are put in place and include: streamlined documentation requirements; provision of relevant information orally; preparation of a limited transfer pricing study by the Tax Administration; Tax administration provides assistance to the taxpayer in preparing

comparable data; special measures for long term contracts. More details on these current measures are in the DOC: JTPF/001/ANNEX/2011/EN.

31. The JTPF felt that adherence to the principle of proportionality gave an overall framework with enough flexibility for tax administrations to develop their own specific measures. Tax administrations are encouraged to look at measures already introduced by others and seek opportunities to incorporate them into their own rules as appropriate.

32. It is also recommended that approaches available in one process may have similar benefits in another. Examples of this are tax administration assistance in the APA process by preparing comparable data or a limited transfer pricing report for the taxpayer. That type of assistance would be equally useful in the audit process.

33. Similarly, existing JTPF reports can be usefully cross referenced to this subject. For example, in the report on intra-group services, the process of evaluating an arm's length price was discussed. The report acknowledged that cost benefit considerations are particularly appropriate in low tax risk cases. The report proposes that in such cases it is particularly important that a balance is sought between available resource, compliance burden and the potential level of adjustment. The commentary in the report on narratives and an arm's length charge is also relevant. Emphasis is given in the report on working with a minimum rather than maximum amount of information when evaluating a transfer price. It is suggested that the same emphasis could equally apply when evaluating a SMEs' transfer prices.

34. The subject of documentation related penalties was considered. It would be inconsistent for a tax administration to have a streamline approach to documentation requirements pre-audit but then to impose penalties for the absence of additional documentation required only as a result of an audit, if the taxpayer acted in good faith, relying on the streamline approach, and is not able to supply the required documentation.

35. Concerns were raised that experienced tax administration transfer pricing personnel do not often deal with SME transfer pricing issues. This could lead to a disparity of treatment between SMEs and non-SMEs. Some administrations avoid the potential problems of less experienced officials being assigned to SME transfer pricing work by structural means, for example they have dedicated SME centres dealing with a wide variety of cases but by a relatively small group of people. Other administrations have process systems wherein an internal peer group review of audits take place to ensure consistency. Both approaches are recommended for consideration.

Recommendations:

R10. When considering SME audit approaches, Member States are encouraged to consider the simplification measures already introduced by others and where possible introduce similar measures in their own Member States.

R11. Previous JTPF reports contain useful material on pragmatic approaches to transfer pricing issues. Member States are invited to review those previous reports with

a view to drawing on the principles established in those reports that may equally apply in this context.

R12. It would be inappropriate to impose documentation related penalties arising from an audit requirement to provide documentation that was not required pre-audit, if the taxpayer was acting in good faith, relying on the streamline approach, and is not able to supply the required documentation.

R13. Member States should seek to ensure that when SMEs are audited for transfer pricing purposes they receive appropriate treatment. Internal peer group reviews or structural organization of audit resource are put forward as cost effective means of achieving that objective.

Dispute Resolution

36. Once a transfer pricing adjustment has been made it often gives rise to potential double tax. A claim to relief from that double tax is available under a tax treaty, the so-called Arbitration Convention[14] (AC) or both. For SMEs the quantum of relief sought is, generally, at the lower end of the scale but the impact on their business is often at the high end of their scale. Additionally, the timescales involved in resolving claims are often disproportionate to the complexity and the amounts involved in a claim.

37. It is suggested that in dealing with SME claims either from their own auditors or from other MS, tax authorities make greater use of their authority to resolve double taxation unilaterally, either under Article 6(2) of the AC or under the provisions of their double taxation conventions corresponding to Article 9 of OECD Model Tax Convention.

38. If an adjustment involving a non-complex transaction with a relatively low monetary value does need to go through the full Mutual Agreement Procedure (MAP) referred to in the double taxation conventions or the procedure foreseen in Section 3 of the AC, it is suggested there is a role for a fast track approach. The JTPF has not detailed the process of such an approach but notes it is likely to involve CAs agreeing to work to much shorter time scales than might be the case in a large complex adjustment. Also the principles underlying the compliance approach and detailed above could equally apply here. For example, taking a decision on a minimum of information; a flexible approach as to how information is supplied; for example, the provision of relevant information orally rather than in formal written position papers. The fast track approach could also be based for instance, in some countries, on a *de minimis* rule.

39. The need for formal dispute resolution processes may be reduced if the relevant tax administration auditors are in direct communication with each other in the framework of the MAP foreseen in the double taxation conventions or of the procedures set out in the AC to better understand the reasoning behind a particular

[14] Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, OJ L 225, 20.8.1990, p. 10.

adjustment, but this communication must not contravene exchange of information rules. A way to achieve such direct contacts may be provided through meetings at which respective local auditors, acting as competent authorities (CA), discuss certain cases directly and agree upon appropriate solutions, possibly with low involvement of regular CA staff.

Recommendations:

R14. Tax Authorities are requested to make use of their authority to act unilaterally in resolving transfer pricing double tax in SME cases.

R15. Fast track dispute resolution processes are encouraged for the purposes of resolving noncomplex low value SME claims to relief from double tax.

R16. Alternative approaches to dispute resolution including auditor to auditor contact and *de minimis* limit rules should be explored and implemented by tax administrations where appropriate in the framework of the MAP foreseen in the double taxation conventions and of the procedures set out in theAC.

V. CONCLUSIONS

40. The JTPF recognises that SMEs have particular needs in meeting their requirement to comply with transfer pricing rules. The JTPF notes Member States have already implemented some valuable measures in responding to those needs and this report seeks to build on those measures.

41. The findings and recommendations in this report rely on the application of the principle of proportionality backed by a flexible implementation of that principle. The report also suggests how SMEs may be identified so that suggested measures in the report can be effectively targeted.

42. As appropriate the particular needs of SMEs should be taken into account in the future work programme items of the JTPF.

43. At regular intervals the effect of SME measures recommended by the JTPF should be monitored.

APPENDIX II
REPORT ON COST CONTRIBUTION ARRANGEMENTS ON SERVICES NOT CREATING INTANGIBLE PROERTY (IP)

I. INTRODUCTION

1. Cost Contribution Arrangements (CCAs) are commonly used as a cost-effective means for multinational enterprises (MNEs) to carry out the group's activities. The business decision to have recourse to a CCA can be justified by various reasons, e.g. reasons of economies of scale, sharing of risks or skills or resources.

2. The topic of CCAs has been of long-term interest to the Joint Transfer Pricing Forum (JTPF). It was carried-over from its previous work programme and under the new mandate the JTPF confirmed its former decision to explore the possible scope and degree to which a common approach to CCAs could be developed within the EU.

3. CCAs are thoroughly discussed in chapter VIII of the OECD Transfer Pricing Guidelines (OECD Guidelines) and the OECD is currently involved in a project on the transfer pricing aspects of intangibles. To avoid duplicating OECD work, JTPF work focuses on services not creating intangibles (IP). This work should be seen as supplementing the existing guidance and completing the JTPF's work on low value adding intra group services (JTPF IGS Guidelines).

4. This report focuses on those issues which are for a reviewer difficult to deal with in practice and proposes how best to address them. The term reviewer covers both the taxpayer and the tax administration. Underpinning this report is the assumption that both MNEs and tax administrations act in good faith and unequivocally endorse the OECD principles. The emphasis of the report, therefore, is on how most expediently a reviewer may conclude that the arm's length principle (ALP) has been applied to CCAs on services not creating IP.

5. Both OECD Guidelines (mainly chapter VIII but also VI and VII in relation to the arm's length principle determination) and JTPF IGS Guidelines are taken into consideration in this document.

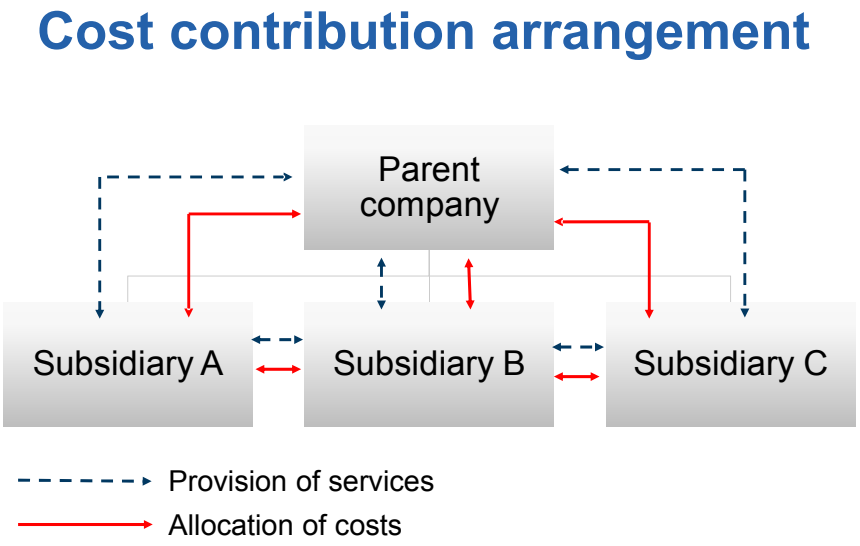
II. TERMINOLOGY

6. Given that there may be a different understanding on whether and how a CCA on services may be distinguished from intra-group services charged directly or by way of creating a cost pool, this chapter seeks to establish a common understanding of the terminology used. It describes the concept of a CCA on services and distinguishes it from intra-group services.

7. A CCA is defined under 8.3 of the OECD Guidelines as *"a framework agreed among business enterprises to share the costs and risks of developing, producing or obtaining assets, services or rights, and to determine the nature and extent of the interests of each* participant *in those assets, services or rights. A CCA is a contractual arrangement rather than necessarily a distinct juridical entity or permanent establishment of all the participants. In a CCA each participant's*

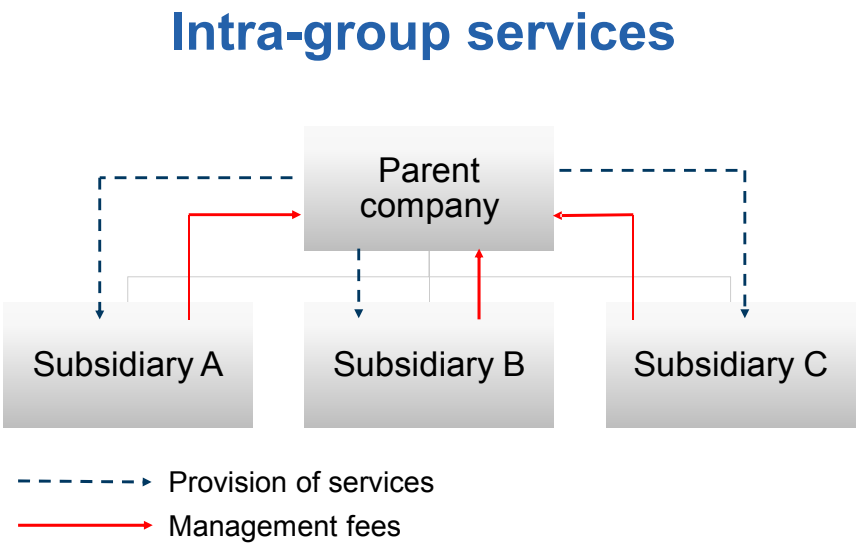
proportionate share of the overall contributions to the arrangement will be consistent with the participant's proportionate share of the overall expected benefits to be received under the arrangement, bearing in mind that transfer pricing is not an exact science."

8. Illustration of a CCA on services:



9. The concept of intra-group services is described in 7.2 of the OECD Guidelines: "*Nearly every MNE group must arrange for a wide scope of services to be available to its members, in particular administrative, technical, financial and commercial services"* and *"The cost of providing such services may be borne initially by the parent, by a specially* designated *group member ("a group service centre") or by another group member"*. Chapter VII of the OECD Guidelines provides guidance for determining whether intra-group services have been rendered, on direct or indirect charging mechanisms and for determining under which circumstances services may be charged at cost or whether and how an arm's length charge including a profit element may be determined.

10. Illustration of Intra-group services:



11. A further variant not explicitly mentioned in the OECD Guidelines but often encountered in practice is arrangements where several members of a multinational group pool the costs of certain services and charge them (directly or indirectly) to members of the group benefiting from those services. Further it is also possible that some members of the multinational group agree on a CCA on services and other members of the group that do not participate in the CCA provide services to the members of the CCA. A participant in a CCA can also engage a separate independent entity to perform all or part of its activities.

12. In practice it is sometimes difficult to differentiate between (shared) intra-group services - including cost pools - and CCAs on services not creating IP. The following table is intended to help reviewers to differentiate between the two concepts.

CCAs on services not creating IP	Intra-group services
Agreement to share costs, risks and benefits where all participants contribute in cash or in kind.	Intra-group services are limited to the provision or acquisition of a service by members of the MNE Group. The risk of not successfully and efficiently providing the service is generally borne by the service provider.
If participants join or leave a CCA, shares should be adjusted/rebalanced in accordance	Terminating the service agreement or extending it to other participants has

with the ALP.	generally no implication on other service recipients.
Written agreements are highly recommended for reasons of having the CCA accepted or recognised by tax administrations. They are even compulsory in some MS. A written agreement and/or appropriate documentation is important for the reviewer when examining the implementation/performance of the CCA.	In practice, formal contracts are not always available. The agreement often is limited to the direct relationship between the provider and the recipient of the service. It should be feasible to demonstrate that from the perspective of the provider the service has been rendered and from the perspective of the recipient the service provides economic or commercial value to enhance his commercial position (section VII.1 IGS Guidelines)
As all participants are contributing to a common activity and share costs and the contributions reflect the expected benefits, contributions are usually valued at costs.	The profit element charged by the provider of the service is usually a key element as the provider will not share profits with the recipients.
The allocation of the costs is based on the expected benefits for each participant from the CCA.	The allocation key is based on the extent each company has requested/received or is entitled to the service.

III. SCOPE

13. While the JTPF IGS Guidelines focus on issues encountered in relation to services of an administrative nature ancillary to the business of the recipient, this document addresses specific considerations in cases where all kinds of intra-group services without IP impact are embedded into a CCA.

14. An exhaustive definition of the services which may be the subject of a CCA is neither possible nor desirable. Services that are within the scope of this document might include the following activities: IT, logistics, purchasing, real estate, finance, tax, human resources services, accounting, payroll and billing. This list of services is only illustrative and does not automatically imply that a service is covered by or excluded from the scope of this document.

IV. GENERAL FEATURES: IS THE CCA CONSISTENT WITH THE ARM'S LENGTH PRINCIPLE

15. As a general principle, a CCA is consistent with the ALP if the contributions agreed upon correspond to what independent enterprises would have agreed to contribute under comparable circumstances given the benefits they reasonably expect to derive from the arrangement and which includes the sharing of costs and risks to satisfy a common need. The relevant question for a reviewer under Article 9 of the OECD Model Tax Convention is whether a CCA is implemented/ performed in accordance with the ALP.

16. The OECD Guidelines (9.163) state that MNEs are free to organise their business operations as they see fit. A tax administration may perform where appropriate

transfer pricing adjustments in accordance with Article 9 of the OECD Model Tax Convention. This means that a MNE should take into account the respective implications (e.g. on bearing risks) of each of the reasonably available alternatives when deciding whether services performed intra-group will be charged directly or indirectly, by way of IGS (including cost pools), or whether a CCA is considered as being more appropriate. The choice should not be a simple labelling exercise (see also paragraph 43 below). The relevant facts should be documented. This should not lead the reviewer to challenge the business choice or the reasons behind the choice or to request from the taxpayer an analysis of what was the best choice.

A CCA on services not creating IP that is consistent with the ALP will have the following features:

i) The arrangement should make business sense.

ii) The economic substance should be consistent with the terms of the CCA.

iii) The terms of a CCA should be generally agreed prior to the beginning of the activity.

iv) The terms of a CCA should be at arm's length taking into account the circumstances known or reasonably foreseeable at the time of entry into the arrangement.

v) Each participant should have a reasonable expectation of benefit.

vi) The participant's share of the costs should be consistent with its share of the expected benefits.

vii) Reasonably expected benefits can be assessed in terms of efficiency or effectiveness in quantitative or qualitative terms.

viii) Contributions by a participant can be in cash or in kind and therefore active participation is not a requirement. The level of influence on decision-making will vary depending on the type of CCA, the expertise of the participants and the amount of costs being allocated to the respective participants.

ix) When a service subject to a CCA is also provided to or received from non-participants in the CCA it has to be valued at arm's length.

x) If participants join or leave the CCA, shares should be adjusted/re-balanced in accordance with the ALP.

17. The actual outcome may differ from the projected outcome, e.g. the contribution provided by a participant is excessive or the benefit derived from its participation in the CCA is inadequate. When such a difference occurs, the reviewer should analyse the reasons for this difference before concluding whether a participant’s proportionate contribution has been correctly or incorrectly determined, or whether the participant’s proportionate expected benefits have been correctly or incorrectly assessed.

18. A further question for the reviewer is whether the difference is so material that it requires an adjustment or the difference is considered as small enough to avoid any adjustment, given that the OECD Guidelines provide that tax administrations should refrain from making minor or marginal adjustments. The reviewer should also bear in

mind that any modification will impact the other participants, which is also a factor in favour of avoiding small adjustments.

19. In some cases the facts and circumstances may also indicate that the reality of the arrangement differs from the terms purportedly agreed by the participants (8.29 OECD Guidelines). A reviewer's decision should always be based on the facts and circumstances relating to the specific arrangement for an adequate period but the reviewer should generally refrain from making an adjustment based on a single year. A reviewer should also take into consideration that the ALP does not require per se that projections of benefits match the actual benefits and even a material difference between actual and projected benefits does not automatically mean that the projection was not at arm's length. Care should be taken to avoid the use of hindsight.

20. Considering the previous paragraph, the application of the ALP might require an adjustment of the participant's contribution through a balancing payment when the situation arose for example from an incorrect evaluation of the expected benefits. In some other cases part or all of the provisions of the CCA will be disregarded e.g. when the facts and circumstances differ from the terms agreed in the CCA (8.26 to 8.30 of the OECD Guidelines).

21. Balancing payments will be treated as an additional cost for the payer and as a reimbursement of costs for the recipients.

V. CORROBORATIVE INFORMATION: NARRATIVE RELATED TO A CCA ON SERVICES NOT CREATING IP

22. In the light of the facts and circumstances of a case, the level of experience and knowledge of the particular MNE concerned, a reviewer may take different approaches in requesting what is considered sufficient corroborative information to confirm that a CCA on services complies with the ALP. In making an informed decision, access to appropriate, good quality information is crucial.

23. In preparing or reviewing a CCA, a reviewer will need to understand and achieve confidence on several key issues. The main question is: "does it achieve an arm's length outcome"? In most circumstances this question may be answered by the provision of a narrative that includes the information requested at paragraphs 24 and 25 below[15].

24. The key element is of course the agreement itself. There should be a clear expectation of mutual benefit for all parties to a CCA. An independent party would not enter into a CCA-type arrangement without a reasonable expectation of benefit (see VI.1 below). Secondly, the agreement should ensure that the allocation of the contributions reflects each participant’s expected benefits (see VI.2 below).

25. As each CCA will be different, the exact content and extent of the narrative may vary but the following list of items should meet the requirements of most reviewers. If relevant, additional documentation can always be provided.

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[15] This is achieved in a similar way in Section VI Narrative, paragraphs 21 to 25 of JTPF IGS Guidelines.

i) General information about the CCA

a) Explaining the CCA within the overall context of the MNE's business in order to understand the rationale for entering into the CCA: the MNE's overarching transfer pricing policy, the type of services that are subject to the CCA, participants' mutual economic interest, required knowledge and skills, what contributions and risks are shared, etc.

b) List of participants and the allocation of responsibilities and tasks associated with the CCA activity between participants and other enterprises.

c) The budget for the CCA and its expected duration.

ii) Expected benefit from the CCA

d) Expected benefit to be derived by each participant and the way it was assessed and reflected in the allocation method (including methodology and any projections used).

iii) Contribution to the CCA

e) The form and value of each participant's contributions and a detailed description of how the value of initial and ongoing contributions is determined.

f) A description of the accounting standard used and how it is applied consistently to all participants in determining expenditures and the value of contributions. A description of direct and indirect costs included in the contribution pool, settlement dates, payment methods and any budgeted versus actual adjustments.

g) Information about the existence of government subsidies or tax incentives linked to the participants' contributions and their impact.

iv) Monitoring/Adjusting the CCA

h) Information about balancing payments, i.e. under which conditions they arise, how they are calculated and when they are due.

i) A description of the Group standard as it relates to its audit approach and as applied to CCAs. For example, safeguards in place to ensure the consistent application of an allocation key for a particular service; ensuring costs/services are not duplicated.

j) How the CCA conditions are monitored and updated.

k) An understanding of how new participants are integrated into the CCA and how a participation is terminated. Provision of the method to be applied when shares in the CCA need to be adjusted/rebalanced.

v) Relationship to other entities

l) A list of other members of the Group or independent enterprises who benefit from services included in the CCA. Description of the fees to be charged and allocation key(s) for the allocation between the participants.

26. The above information may be made available and provided in different ways such as a dedicated written narrative or it may also be the case that the written agreement already provides most information. The important point is that the reviewer gets an understanding of how the CCA works in practice.

VI. SPECIFIC ASPECTS

27. This chapter addresses some specific issues for which the reviewers might need additional guidance.

VI.1. The 'expected benefit' test

28. The 'expected benefit' test is an essential element in the setting-up, appropriate monitoring and review of a CCA. It will be the basis for assessing the arm's length nature of participants' contributions to the CCA and will justify the allocation key.

29. Based on the ALP, a participant's contribution must be consistent with the expected benefits it will derive from its participation in the CCA. Benefit in this context means an increase in economic or commercial value such as savings in expenses or an increase in income or profits. An appropriate demonstration that profits or income can be maintained or losses/greater losses can be avoided may also be considered as an expected benefit. It should be noted that what distinguishes IGS from CCAs as regards the benefit test is that for CCAs a reviewer should check - in addition to verifying whether the services covered were actually provided (IGS requirement) - whether contributions are in accordance with the expected benefits that participants might derive from the CCA.

30. It is important that the reviewer is satisfied that from a participant's perspective the contribution is in accordance with expected benefits in terms of e.g. economies of scale or sharing of risks and skills, and that the participant would have paid for the service or else performed the service itself. The key used for allocating costs should reflect the benefit expected by the participant and how the participant takes advantage of the outcome of the CCA in a way consistent with the arrangement.

31. The degree of certainty a reviewer requires to accept that the provision of a service under a CCA meets the arm's length standard will vary from case to case on a risk assessment basis. While in most cases the expected benefit for the respective participant can easily be derived from the appropriate demonstration of the overall benefit of the CCA and the appropriateness of the allocation key chosen, cases where the expected benefit for the individual is less clear require a stronger focus from the viewpoint of an individual participant. Additionally and depending on the facts and circumstances, the expected benefit may also be evaluated directly i.e. by an estimation of the additional income to be generated or costs to be saved, or indirectly i.e. by using indirect indicators of the expected benefit such as turnover, number of employees, gross profits, etc.

VI.2. Contributions of each participant

32. Each participant's contribution must be consistent with what independent parties would have contributed in comparable circumstances. Valuation of the shares in the expected benefits is one of the key elements in CCAs. This will form the basis for the calculation of the contributions.

33. Often allocation keys are used to determine what each participant will have to contribute, although the allocation method might be based on estimated costs that will be saved by each participant in the arrangement. The guidance on selection, justification, application, documentation and potential allocation keys given in paragraphs 48 – 55 of the JTPF IGS Guidelines applies equally in the context of CCAs on services not creating IP.

34. The value of each participant's contribution must be consistent with the value that independent parties would have agreed to in comparable situations. No specific result can be provided for determining participants' contributions in all situations, but rather the question must be resolved on a case by case basis consistent with the general operation of the ALP. With respect to CCAs in general, countries have experience both with the use of costs and with the use of market prices for the purposes of measuring value of the contributions to arm's length CCAs (8.15 OECD Guidelines). However, for the type of CCAs covered by this document, it is assumed that there is often a small difference between pricing at costs and at market value and it is therefore recommended for practical reasons to generally value the contributions at costs.

35. As contributions are based on expected benefits this generally implies that they are initially based on budgeted costs. In service CCAs there may be little material difference between budgeted and actual costs and therefore it may be practical to use the actual costs as the measure of the contribution of each participant. However, where adjustment of the contribution from estimated to actual costs is necessary this would generally be done retrospectively, i.e. by adjusting the historical budgeted costs. Unless national law prohibits it, it may be appropriate for practical reasons to make the adjustment prospectively. This means taking the eventual adjustment into account in the following year if it can be considered as not having a major impact. The question of whether any adjustment of the contributions from cost (at either budgeted or actual) to market price[16] is required to value the contribution is considered in paragraph 34.

36. In order to address the issue of adjustments to contributions, the OECD Guidelines recommend preparing an annual account of expenditure incurred in conducting the CCA activity, which would include a detailed description of how the value of the contributions is determined and how accounting principles are applied consistently to all participants in determining expenditures and the value of the contributions. It can be assumed that also third parties, when contributing jointly to a certain project, will agree on a common standard on how to determine their contributions. For practical reasons it is therefore recommended that MNEs should be allowed to use the accounting standards that are generally used throughout the group. A tax

[16] 8.15 OECD TPG refers to valuing contributions at market price.

administration is however entitled to require adjustments, especially in cases where permanent major differences with the domestic accounting standards can be expected over the duration of the CCA.

37. Contributions should include all relevant costs for the acquisition, maintenance or for securing the benefits derived from the arrangement. A reviewer will need to understand which costs have been considered relevant (and can, therefore, be allocated). Sometimes this will be self-evident from the type of services covered by the CCA. Sometimes, in more complex situations, the arrangement should clearly explain what costs are excluded or how potential duplication of costs has been avoided.

38. A related issue is the treatment of tax incentives and government subsidies which is addressed in 8.17 of the OECD Guidelines. The key question is whether costs passed to the CCA should only include costs effectively spent from which tax incentives and government subsidies have been deducted. "*Whether and if so to what extent these savings should be taken into account in measuring the value of a participant's contribution depends upon whether independent enterprises would have done so in comparable circumstances*".

VI.3. Anticipated versus actual benefit

39. As CCAs are arrangements based on expected benefits, independent parties might in consideration of the often long duration of the CCA include a clause in the contract allowing regular assessment of whether expected benefits are in line with actual benefits and whether contributions should not be changed in the future.

40. Addressing those two concerns opens the issues of whether contributions can be adapted to the actual situation and whether this is to be considered as arm’s length or as the improper use of hindsight.

41. The CCA must be examined by reference to the assumptions of future benefits based on the economic and commercial circumstances prevailing or reasonably foreseeable at the time the arrangement is entered into. Therefore if a reviewer considers the benefit projections as reasonable, future events affecting the initial projections should not lead to retrospective adjustment of the contributions.

42. As unexpected or unforeseeable events or circumstances may affect the initial benefit assumptions, a reviewer should consider whether independent parties would have provided for an adjustment or renegotiation of the agreement in such cases.

VI.4. Participation in a CCA

43. The key feature of a CCA is that the contributions of the participants are in accordance with the expected benefits of the respective participants from the participation in the CCA. An enterprise taking its expected benefit solely or mainly from the performance of the CCA activity itself would not be considered as being a member of the CCA but rather as a service provider (company) that would add a profit element in its calculation, i.e. should be considered as a company providing services at arm's length.

VI.5. Joining/Leaving a CCA

44. The general issue of entities joining or leaving a CCA is in practice often a very difficult topic even if mergers and restructuring are part of the day-to-day business of MNEs. How to assess the value of work in progress and/or the specific skills acquired from past activities are questions often leading to difficulties for any reviewer.

45. However, as the present scope is limited to CCAs on services not creating IP, the examination of buy-in / buy-out issues should be very limited (or non-existent). Answering the following questions should help reviewers: what additional costs will be paid by participants when an entity leaves or exceptionally when it joins? Is the arrangement still sustainable after the departure of this company? Should those new elements (different cost structure, or expertise, or skills, or risks, etc.) be compensated in money or do they only lead to a revision of the expected benefits that will lead to the adoption of new allocation keys or does the new participant bring specific knowledge?

46. Clearly, if the outcomes of prior activities developed under the CCA have no value, no compensation should take place. However, entry or departure of a company will generally lead to an adjustment of the proportionate shares (allocation keys).

VI.6. Documentation

47. Reviewers should be aware that CCAs are already governed by the Code of Conduct on EU Transfer Pricing Documentation (EU TPD) wherein it is stated that MNEs should include in the masterfile a list of CCAs as far as group members in the EU are affected.

48. The OECD Guidelines (5.4) refer to prudent business management principles that would govern the process of considering if transfer pricing is appropriate for tax purposes and the extent of any required level of supporting transfer pricing documentation.

49. This theme is echoed in point 2.3.1 of the EU TPD which says: "The "prudent business management principle", based on economic principles, implies that the sort of evidence that would be appropriate in relation to a transaction of large value might be very different from the sort of evidence that would be appropriate in relation to a transaction where the overall value is significantly smaller".

50. Applying this principle to CCAs would lead participants to prepare or to obtain materials about the nature of services covered and the terms of the arrangement as well as its consistency with the ALP (including projections used to establish the expected benefits and budgeted versus actual expenditures).

51. It should be noted that information from one source (e.g. a written agreement) may cover information already covered by another source (e.g. a narrative). The extensive use of computerized systems also provides the opportunity to see summary level detail which may then remove the need for more extensive primary documentation.

52. CCA agreements supplemented where necessary by information listed in the narrative relating to CCAs are considered by the JTPF as relevant information as regards EU TPD requirements.

VI.7. Post review considerations

53. CCAs will often involve more than two entities and are often set up between many or even all the members of a MNE. Adjustments may therefore not only affect one entity but impact on all the other participants. The avoidance of double taxation may in those cases of dispute require cost and resource intensive procedures. It is therefore recommended that, on the one hand, tax administrations refrain from challenging the participation or contribution allocated to their taxpayer for minor adjustments and on the other hand, taxpayers should make efforts to follow these guidelines when setting up and documenting their CCAs on services not creating IP.

54. In case of dispute the mutual agreement procedure may involve more than two Competent Authorities. Therefore it will be useful to apply the multilateral approaches recommended in the Code of Conduct on the Arbitration Convention for triangular cases.

VII. CONCLUSIONS

55. Compliance with the recommendations in this report, in most cases falling within its scope, will facilitate the evaluation and make it easier for tax administrations to accept that the ALP has effectively been applied..

56. It is recommended that for future reference and at the end of this process the narrative becomes a file note in conjunction with some arrangements for regular updates.

57. The JTPF will monitor the effect of these guidelines regularly.

ANNEX: Summary of the current state of play as regards Member States' CCA legislation, administrative guidance and best practices

This section aims to summarise the current state of play as regards CCA legislation or administrative guidance within EU MS.

The section below is drafted on the basis of contributions provided by EU tax administrations to reflect the situation prevailing on 1 July 2011.

Question 1: Do you have specific legislation relating to CCAs? If not, is it under consideration and when might it be introduced?

Few MS have specific legislation on CCAs.

Estonia, Spain, the Netherlands, Portugal and Slovenia apply specific legal provisions concerning CCAs for obtaining assets, rights or services, whereas Poland's legislation refers to CCAs only in the context of intangibles. Germany has specific provisions only as regards CCA documentation. Other MS use the OECD Transfer Pricing Guidelines or their own general TP guidelines to evaluate CCAs.

Introducing new specific provisions on CCAs is only under examination in Greece.

Question 2. Has your administration issued internal audit guidelines providing guidance on CCAs and if yes, which key points do they address (e.g. how to recognise an arrangement, how to audit the arrangement, how to facilitate exchange of information with other countries, etc.)?

Few MS have issued internal guidelines on auditing CCAs.

Italy, Lithuania, Slovenia and the United Kingdom have guidelines on transfer pricing which also cover the audit of CCAs. In particular, the UK guidelines stress the importance of identifying a clear expectation of mutual, overall benefit to distinguish a CCA from a more normal situation with straightforward transfer of goods or services.

In Hungary, a government decree on documentation requirements regarding transfer pricing agreements in general is applied.

Latvia has internal general guidelines regarding CCAs, which are based on the OECD guidelines.

Portugal is in the process of approving a Transfer Pricing Audit Manual that also includes internal audit guidelines in areas such as CCAs.

Question 3. Has your administration published domestic administrative guidance on CCAs (Guidelines, Regulations, Circular Letters, etc.) explaining the procedure to be followed by the taxpayer when preparing a CCA, with particular reference to the structure and documentation requirements (where existing, could you provide details of the electronic link to the documents)?

Few MS have issued domestic administrative guidance on CCAs.

In Denmark, CCAs are addressed in the Danish Transfer Pricing Documentation Guidelines.

Estonia has issued guidelines containing a short overview of the OECD TP guidelines and examples.

In Hungary, a government decree on documentation requirements regarding transfer pricing agreements in general is applied.

Germany has issued administrative guidance which is binding for the tax administration, but not for the courts.

The Italian audit guidelines are public, addressed to tax inspectors but also followed by taxpayers.

Portuguese regulations envisage including relevant information on a CCA in the TP file.

Question 4. What is the most common type of CCA used by enterprises in your MS?

CCAs dealt with by MS Tax Administrations most often relate to services, development of intellectual property, research and development and acquisition of assets.

Questions 5-7. What particular practical problems have you encountered in dealing with CCAs and how have you addressed those problems? What are your particular concerns as regards CCAs on services? Based on your experience, how frequent are disputes linked to CCAs?

The most common practical problems encountered in the context of CCAs relate to the availability/timely provision by taxpayers of sufficient information/TP documentation, the suitability of allocation keys, the calculation of entry and exit fees, valuation of buy-in/buy-out payments, distribution of costs, identification of comparables, applicability of profit margins, as well as the actual identification of a CCA.

Specific concerns for TAs in this context include the criteria for identification of a CCA, measuring the value of participants' contributions to a CCA and evaluating the associated benefits (expected and actual) and risks for the purpose of allocating costs, the applicability of mark-ups, as well as access to relevant documentation.