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Mr Masatsugu Asakawa
Chair
Committee of Fiscal Affairs
Organisation for Economic Co-operation and Development (OECD)
2, rue Andre Pascal
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By email: TransferPricing@oecd.org.

Dear Sir or Madam

SUBMISSION ON WHITE PAPER ON TRANSFER PRICING DOCUMENTATION

CPA Australia represents the diverse interests of more than 144,000 finance, accounting and business professionals in 127 countries. Our vision is to make CPA Australia the global accountancy designation for strategic business leaders.

Against this background we make this submission in respect of the 'White Paper on Transfer Pricing Documentation' which was issued by the OECD on 30 July 2013.

General comments

CPA Australia welcomes the OECD's White Paper as a first step in developing more streamlined and standardised transfer pricing documentation protocols for multi-national enterprises (MNEs) engaged in related party cross border transactions.

As recognised in the White Paper the regulatory burden imposed on MNEs has increased exponentially in recent years and this growing compliance burden has been a drag on global productivity at a time when MNEs are seeking to recover from the adverse impacts of the global financial crisis.

From the Australian perspective this increased burden has manifested itself in a variety of ways including the requirement to complete a highly detailed and expansive 'International Dealings Schedule' (IDS) at the time of lodging an annual income tax return which must be completed by any resident taxpayer engaged in related party international dealings whose value exceeds A$2 million.

This has been a particularly onerous requirement for resident taxpayers who are small to medium sized enterprises (SMEs) whose related party international arrangements may often be relatively straightforward but who are nonetheless required to complete an IDS form of up to 16 pages which is supplemented by extraordinarily detailed and complex set of instructions on how taxpayers can complete that schedule.

We are of the view that a key tenet underlying the development of any streamlined transfer pricing documentation protocols for MNEs must be that the compliance burden imposed on taxpayers must be commensurate with the materiality of the related party cross border transaction(s) entered into by a MNE.

In raising this issue we recognise that the development of any materiality standard in this context is very challenging given the disparate range of international transactions, industries and jurisdictions in which MNEs trade or invest.

However, given the OECD's stated commitment to facilitate global trade it would be prudent that emphasis is placed in any guidelines which encourage all revenue authorities that a balance needs to be struck between ensuring the arm's length pricing of cross border transactions amongst associated enterprises and the need to ensure that SMEs can continue to grow without being subject to an excessive compliance burden.

We also recognise that the White Paper has also issued in response to the OECD's recently issued Action Plan on Base Erosion and Profit Shifting which required, amongst other things, that rules needed to be developed which will require MNEs to provide all relevant governments with information on their global allocation of income, economic activity and taxes paid using a common template.

Broadly, in response the White Paper has suggested the development of a co-ordinated approach to transfer pricing documentation which is proposed to consist of a masterfile and a local file.

Essentially, the masterfile portion of the documentation provides a detailed analysis of the global business, financial reporting, debt structure and tax situation of a MNE to enable various tax authorities to identify the presence of potential transfer pricing risks, and that this will be supplemented by the local file which would set out how a taxpayer in a particular jurisdiction has complied with the arm's length principle in determining its transfer pricing positions.

We note that MNEs trading in multiple jurisdictions typically already prepare a form of 'masterfile' to alert the tax authorities in those jurisdictions on their global operations which is usually prepared in consultation with an external transfer pricing specialist. This work is completed as a tax compliance savings measure as the same document is provided to multiple revenue authorities. However, its utility is only marginal when the MNE is only in a very simple structure such as may arise where there are only two or three associated enterprises engaged in very straightforward transactions.

As we do not want to unnecessarily increase the compliance costs of such MNEs we believe that the obligation to mandatorily prepare a masterfile should not be imposed on SMEs who have relatively simple ownership structures and operations.

Moreover, we are concerned that the depth of information required to be provided under the proposed masterfile approach may be greater than that currently compiled especially in terms of providing a written functional analysis showing the principal contributions which various affiliates make towards value creation within the group. This requirement would implicitly appear to involve the compilation of significant financial data.

Whilst we recognise that the collation of such data will take time and increase cost it may also provide greater transparency and trust in a period where base erosion and profit shifting is an issue of paramount concern for tax authorities across the world and the constituencies they service.

However, we would be most concerned if such information was used by tax authorities to apply some form of global apportionment of a MNE's profit rather than apply the OECD's long standing arm's length principle in determining the profit that a particular entity should have returned in their country of residence on a cross boarder related party transaction.

Such a global apportionment approach may also be potentially subject to disputation between revenue authorities concerning their respective cuts of total global profit and may be susceptible to abuse particularly by inexperienced or ill-equipped auditors of competing revenue authorities.

It is for this reason that we believe that the most fundamental element of the transfer pricing documentation must be the local file which sets out the arm's length nature of a particular entity's related party cross border transactions.

This must remain the cornerstone of any transfer pricing documentation as the arm's length principle ensures that a resident of a particular jurisdiction will be assessed on a profit which reflects the functions provided, assets used and risked assumed by that particular taxpayer.

Moreover, the application of the arm's length principle ensures that reference is made to comparable uncontrolled transactions in a particular jurisdiction to verify the arm's length nature of transactions entered into by a taxpayer factoring in the use of external comparable data and the domestic trading environment in which the particular member of the MNE operates.

Specific comments

We also make the following specific comments in respect of the White Paper:

- Any review of the efficacy of transfer pricing documentation must be accompanied by a recognition that the technical competence of revenue authority auditors across jurisdictions must also typically increase to ensure that a more sophisticated approach to assessing transfer pricing risks is adopted. We understand that the Australian Taxation Office is currently ramping up its own internal transfer pricing expertise to reflect the need to further increase its depth of understanding of transfer pricing issues.

- The provision of a big picture analysis of a group's global operations in a masterfile may sometimes distract auditors from focussing on whether the particular transactions that an entity has entered into in their 'home' jurisdiction are arm's length or not.

  For example, a subsidiary of a routine global distribution business which may account for, say, less than 2% of the global MNE business, and which has no interest in any intangibles, has no reason to be concerned or interested in the manufacturing, financing and management of the intellectual property of the global group which is fully controlled offshore . In these circumstances the determination of all these issues is made offshore by the parent company which will be subject to the transfer pricing rules and documentation requirements of their resident jurisdiction. In these circumstances the tax authority in the resident country of the subsidiary distributor should be concerned solely with the prices paid or the profitability of the distributor compared to independent distributors in that market.

- Care should therefore be taken that unsophisticated auditors do not apply the masterfile to mistakenly focus on issues outside their jurisdiction rather than determine whether the resident taxpayer's assessable income has been understated because of non-arm's length positions.

  The comment is made in relation to the provision of information necessary to start, conduct and complete an audit that …'It may often be the case that the required documents will be in the possession of members of the MNE group other than the local affiliate under examination. Often the necessary documents will be located outside the country whose tax administration is conducting the audit. It is therefore essential that the tax administration's power to compel production of information during the course of an audit extend beyond the country's borders.'

  We suggest that this observation be revisited as it appears to be advocating extra-territorial authority for taxation officials. Currently the powers of a tax authority of a jurisdiction are limited, and must be limited, to that jurisdiction. Accordingly, the MNE cannot be compelled to produce such information. Certainly the MNE can be encouraged through veto of evidence laws which exist in some countries, but the power to compel a non-resident to provide documentation from beyond their borders is not possible.

The essential issue with documents held outside the jurisdiction is that any information in those documents cannot be used in evidence by the taxpayer if the MNE has refused access to the documents during the audit. It should be noted that the tax authority also has the right to make assumptions based on best available information if refused access to particular documentation.

- We believe that documentation requirements concerning the transfer of intangibles or business restructures should not unduly focus on the form of such transactions, but their substance and the value of any intellectual property or business functions that have been transferred. In many cases such transfers take place because MNEs are required to continually commercially innovate in order to be internationally competitive rather than be primarily undertaken for tax reasons.

- The comment is made in the section concerning the mechanics of preparing transfer pricing documentation that some countries require an outside auditor to certify the transfer pricing documentation prepared by a taxpayer. We concur with the view that such a requirement may be excessive and may be limited (if required) to entities operating in emerging countries whose governance standards are continuing to evolve.

  Similarly we do not agree that consulting firms be mandatorily required to complete transfer pricing documentation as this would be counterproductive to the stated goal of containing unnecessary compliance costs. Furthermore, in our experience the most optimal mix of resources in compiling such data is a mixture of external transfer pricing specialists who have the technical and econometric expertise to provide advice to in house finance and operational staff who will be able to source the various internal source data to verify the transfer pricing positions adopted.

If you have any questions regarding the above, please contact Mark Morris, Senior Tax Counsel, on (03)9606 9860 or via email at mark.morris@cpaaustralia.com.au.

Yours faithfully

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