

Capital Markets Tax Committee of Asia

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Organisation for Economic Co-operation and Development
OECD 2, rue André Pascal
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France

By email: TransferPricing@oecd.org

Dear Sir/Madam

Comments on the OECD White Paper on Transfer Pricing Documentation

This submission is respectfully made in response to your invitation for comments on the White Paper on Transfer Pricing Documentation (White Paper) issued by the OECD on 30 July 2013.

Capital Markets Tax Committee of Asia (CMTC)

By way of introduction, the Capital Markets Tax Committee (CMTC) of Asia is a financial services industry body consisting of a number of banks, investment banks, securities firms and other diversified financial services institutions operating in Asia who are represented through their regional tax directors.

CMTC's membership comprises ABN Amro, AIA, ANZ Bank, American Express, Bank of America Merrill Lynch, Bank of China International, Barclays Capital, BNP Paribas, Citigroup, CLSA, Credit Agricole CiB, Credit Suisse, Daiwa Securities, SMBC HK Ltd, DBS, Deutsche Bank, Fidelity Investments, Fortis Bank, Goldman Sachs, Hang Seng Bank, HSBC, ING, JP Morgan Chase Bank, Macquarie Bank, Manulife Financial, Morgan Stanley, Nomura, Rabobank, Royal Bank of Canada Capital Markets, Royal Bank of Scotland, Société Générale, Standard Bank Asia, Standard Chartered Bank, Swiss Reinsurance Co and UBS.

The main objects of the CMTC, according to its constitution, are "to provide a forum for discussion by corporate tax managers responsible for the tax affairs of investment banks, securities firms, banks and other diversified financial services institutions of topical taxation issues in Asia affecting their capital and securities markets and similar activities; ... to keep members informed of up to date information on taxation matters affecting capital and securities markets, and to exchange views on the technical analysis thereof; [and] to represent the interests

of its members through acting as the respected voice of investment banks, securities firms, banks and other diversified financial services institutions, and to participate in liaison or advocacy activities on tax matters either directly or indirectly through representation with other groups or societies concerned with or by fiscal matters”.

Submission by CMTC

The CMTC welcomes the OECD’s invitation to launch a global conversation on how transfer pricing documentation rules can be improved, standardised and simplified. We appreciate the opportunity to contribute to this process. For the CMTC members, transfer pricing documentation has become an extremely complex, costly, and time-consuming part of transfer pricing compliance, with an ever increasing documentation and reporting requirements imposed by many tax authorities. We therefore appreciate the OECD’s attempt to simplify and harmonize the current transfer pricing documentation requirements.

We hereby confirm that we have no objections to the posting of our letter on the OECD website.

Interaction of the White Paper and existing local country transfer pricing documentation requirements

Many of the jurisdictions in Asia already have comprehensive transfer pricing documentation requirements embedded in their local transfer pricing regulations. These local regulations require the preparation of specific local country transfer pricing documentation reports, often on an annual basis. While there is a degree of commonality in the documentation information required for each country, differences do exist.

We would therefore recommend that the OECD seek to expand the discussion contained in Annex 1 of the White Paper and seek to focus its recommendations on the key common items already required under local country legislation. This would have to be managed carefully to focus only on the key items required so as to not end up as a simple compilation of all countries’ existing transfer pricing documentation requirements. If implemented successfully it would help to manage the already considerable documentation burden that is currently placed on taxpayers in Asia while also helping to achieve the OECD’s goal of harmonisation with respect to transfer pricing documentation. This would also have the added benefit of managing the risk identified in the White Paper that previous global efforts in harmonising transfer pricing documentation by several international organisations have not been widely recognised.

In this regard we would also urge the OECD to consider its recommendations around safe-harbors and formalising the benefits available to organisations that comply with the documentation structure proposed. As the draft stands, there is no discussion of the potential protection tax payers would stand to benefit from should they meet the documentation requirements outlined.

Purpose of transfer pricing documentation

The CMTC feels that the primary purpose of transfer pricing documentation should be to provide documentary evidence that the transfer pricing policies applied are consistent with the arm’s length principle. However, the discussion contained in paragraph 46 and throughout the White

Paper appears to outline far more wide-reaching purposes for transfer pricing documentation. While we certainly support a motion to increase transparency to facilitate a risk-based approach to transfer pricing audits, setting a standard whereby taxpayers are required to “*provide governments with all of the information that they require in order to conduct an appropriately thorough audit...*” goes beyond our understanding of the scope of transfer pricing documentation and would create an administrative burden that would be very difficult, if not impossible, to manage.

The CMTC submits that a standardised approach to annual documentation requirements should specify only the ‘minimum’ level of transfer pricing documentation in order to explain why a taxpayer’s transfer pricing policies are consistent with the arm’s length principle. The production of more comprehensive ‘audit defense’ documentation should only be produced at the discretion of the taxpayer or the tax authority, and should not be expected to be produced annually as a part of the transfer pricing documentation compliance process.

In paragraph 65, the OECD pose the following questions:

“Would it be possible, for example, to focus initial compliance efforts on the information necessary for risk assessment, while preserving the ability of the tax administration to get the information it needs when it conducts an audit? Moreover, if initial document demands were to be simplified and focused on risk assessment, what would the consequences be for the meaningful self-assessment that documentation was originally intended to encourage?”

The CMTC submits that it is possible for taxpayers to provide a ‘minimum’ level of transfer pricing documentation that will allow a tax administration to conduct a meaningful initial risk assessment. This would not prevent the tax administration to get the information it needs when it conducts an audit, the nature of which will be dependent on the risk that has been identified and the relevant facts and circumstances. In this way, focused and detailed analysis can be targeted towards business operations and transactions that are significant and considered higher risk profile, as required.

Role of two-tiered transfer pricing documentation

We agree with the two-tiered approach to transfer pricing documentation as outlined in the White Paper and the desire to create a standardised documentation structure. However, we submit that the OECD should promote a more ‘principles-based’ approach to the items required to be maintained in each of the Master File and the Local File. In this way, the OECD would need to accept that a strict, standardised approach to transfer pricing documentation cannot be applied to all taxpayers, in all businesses and all industries. Given the variety of global businesses, operating models and geographic footprints, the CMTC submits that the adoption of a strict, standardised approach for transfer pricing documentation could create a number of risks including:

- ***Inadvertently failing to provide useful information to assist tax administrations in performing a risk assessment analysis.*** As specified in paragraph 69, the OECD Forum on Tax Administration previously identified nine features that may indicate the presence of significant transfer pricing risk. Some of these features are less relevant in the financial services context, as compared to other industries. For example, when considering

financial services organisations, the focus on intangibles is less likely to be a relevant factor when compared with other industry sectors where the presence and use of intangible assets plays a larger and more significant role. Another example of a feature that is less relevant relates to excessive debt, given the extensive regulation of capital and debt structures throughout the industry.

- ***Creating a threshold for Local File documentation that could well end up being greater than many existing local country transfer pricing documentation requirements.*** This will serve to increase the documentation requirements in some countries. Furthermore, tax administrations who may have historically adopted reasonably minimalist approaches to transfer pricing documentation may potentially react by increasing their compliance requirements for fear of being perceived as being inconsistent with OECD requirements.
- ***Creating a template that is difficult for different industry groups to comply with resulting in inconsistent information and compliance risk.*** For example, the White Paper proposes taxpayers could provide, without undue burden, individual country data based on either management accounts, consolidating income statements and balance sheets, and/or tax returns demonstrating how global income is allocated and how that allocation compares to the location of assets and employment (paragraph 72). This might be possible for industries with transfer pricing policies applying at a whole-of-entity level, whose global supply chain is less complex, but for participants in the financial services industry, such information could be very difficult to provide, resulting in estimates and assumptions being made which would undermine the purpose of the process.

The typical global supply chain for financial services industry participants involves multiple transfer pricing policies applied across multiple product lines and lines of business. At any one time, each entity within a financial services group might be impacted by dozens or more transfer pricing policies applying to the business that are conducted locally in-country. Asking taxpayers in the financial services industry to complete a standardised template, that is arguably designed to detect risks that are less relevant to our industry (per paragraph 69) represents an excessive compliance burden.

An additional complexity for organisations operating in the financial services industry is that often our businesses are conducted utilising permanent establishments (PEs) or branches. In this regard, we seek to comply with the transfer pricing guidance regarding PEs which is embedded in the tax law for individual countries, and follow the guidance of the OECD that is set out in the ‘*2010 Report on the Attribution of Profits to Permanent Establishments*’, 22 July 2010. As set out in paragraph 16 of the Report:

“Because of the special relationship between risks and financial assets in those specific sectors, the authorised OECD approach uses the “key entrepreneurial risk-taking function” (“KERT function”) terminology in describing the functions relevant to the attribution of both risks and assets, but that terminology is not used for other sectors. Outside the financial enterprise sector, risks may be less intimately linked with assets, so that there may be less overlap between the significant people functions relevant to the assumption of risk and those relevant to the economic ownership of the assets.”

The analysis in the transfer pricing documentation regarding the application of the KERT concept, which is specific to the financial services industry, will be difficult to summarise in a meaningful way in a template. The CMTC submits that to present the information in a meaningful manner will lead to an “undue burden” and would go beyond our understanding of the purpose of transfer pricing documentation.

Accordingly, we would ask the OECD to consider including discussion points to clarify that not all the items noted in the White Paper will be necessary in all circumstances or to include guidance on the types of information that should be included as opposed to specific documentation items as currently suggested.

Items to be included in transfer pricing documentation

The CMTC further submits that there are particular elements of the proposed Masterfile that are inappropriate or unnecessary for transfer pricing documentation purposes:

- If the idea is that the Masterfile is to be provided to all tax administrations, we do not believe that it is appropriate to include a “*list and brief description of the MNE group’s applicable unilateral or bilateral/multilateral APAs*”. APAs will be agreed based on the very specific facts and circumstances of the related party arrangements in the APA’s scope. Moreover, the outcome from APAs might result from a process of negotiation between a taxpayer and one or more tax administrations, rather than representing a strict application of the arm’s length principle. Summarising the outcome of an APA (whether it be unilateral, bilateral or multilateral) and providing this to all tax administrations whether they are involved in the APA or not, is unnecessary and runs the risk of oversimplifying the APA outcome. Tax administrations not directly involved in the APA cannot understand the outcome of the APA without knowing all the specific facts and circumstances.
- Similarly, the CMTC submits that providing a “*list and brief description of other relevant tax rulings related to the allocation of income to particular jurisdictions*” in a Masterfile is not appropriate to the determination of whether transfer pricing policies are consistent with the arm’s length principle. Tax rulings will be based upon the specific application of the domestic tax law applying to the relevant income, and do not necessarily take account of the application of the arm’s length principle. How domestic income tax allocation rules interact with the transfer pricing rules will be a matter for the specific jurisdiction. Should tax administrations wish to exchange information regarding tax rulings relevant to a taxpayer, they should do so through other information exchange mechanisms and not through transfer pricing documentation.
- Furthermore in relation to the proposed content of the Masterfile as set out in Table 1, it is our submission that it is not appropriate for all tax administrations to have access to a “*list and brief description of transfer pricing matters pending under treaty MAP processes or resolved in MAP during the last two years*”. MAP processes resolved under treaties are conducted between the relevant competent authorities, often with little or only informal involvement by the taxpayer. Whilst the outcome of a MAP process will be known to the taxpayer involved, the details behind the decision-making process may not necessarily be transparent. MAP processes can be resolved by competent authorities as a

matter of negotiation between the two competent authorities, with little regard to the precise application of the arm's length principle to the transfer pricing arrangements. This would have limited practical use to any tax authority beyond the two authorities already involved in the MAP process. The issue of disclosure of MAPs is further complicated given the potential overlap of transfer pricing documentation with accounting provisioning and disclosures of uncertain tax positions. It is our submission that including such detail regarding the MAP process to authorities other than the competent authorities is not the right approach, and could lead to further unnecessary complexity in meeting transfer pricing compliance and documentation requirements of individual local countries.

Additional items for consideration

In addition to the points above, the CMTA asks the OECD to include guidance on the timing of transfer pricing documentation in the updated guidelines. Many transfer pricing documentation requirements in Asia are considered contemporaneous requirements which result in a need to prepare an annual transfer pricing documentation report for the business or legal entity in question. To help manage the compliance burden created by transfer pricing documentation, we would recommend including discussion of the timeframes over which documentation is likely to be valid. We accept that, once again, it is impossible to provide definitive guidance on the specific situations of taxpayers across different industries and geographies. However, indicative guidance on the key triggers or business change that would warrant updating or preparing new documentation would help taxpayers to manage their ongoing transfer pricing documentation compliance process and costs.

The OECD's Base Erosion and Profit Shifting Action Plan identifies management fees and head office expenses as being common types of base eroding payments (Action 10). While we would challenge that assertion, we would welcome guidance from the OECD on what would constitute a reasonable level of documentation for such charges so that tax authorities can be guided as to when deductions for such charges ought to be sustained. The issue of the deductibility of management fees and head office expenses is one of the most significant audit issues facing financial services organisations in Asia. Coupled with interest from banking regulators, we see this as a critical area where guidance would be most relevant.

We also recommend that the OECD expands the discussion in the White Paper on the role and purpose of transfer pricing forms. In practice, a number of countries in the Asia region require the completion of detailed related party transaction forms providing significant information on a company's related party transactions. We would urge the OECD to expand the discussion on these forms and given their increasing prevalence, to consider the role of transfer pricing documentation, its purpose and the value it provides to tax administrations given the mandatory forms taxpayers are also required to prepare.

Finally, paragraph 83 of the White Paper introduces the concept of materiality into transfer pricing documentation. Similar to our comments above, we would urge the OECD to further develop this area of the White Paper alongside the discussion about a risk-based approach. In our experience, within a financial services organisation there are a huge number of intercompany transactions. Many of these are routine, low risk transactions that do not ordinarily warrant significant investment of time or cost to analyse. Therefore, expansion of the discussion around

where and when materiality thresholds may be appropriate would, in our opinion, significantly increase the operational efficiency of the preparation of transfer pricing documentation.

We believe that this consultation is a critical step in the process of moving towards developing standardised and simplified transfer pricing guidance with the aim to enhance transparency and lessen the current compliance burden. We are eager to see the OECD's developments in the space and thank you once again for the opportunity to submit our response on this important topic.

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If you would like to discuss anything contained in this submission further, we would appreciate the opportunity to do so, especially where it is likely to lead to improved, standardised and simplified transfer pricing documentation.

I can be contacted on +852 2252 6083 or jesse.kavanagh@nomura.com if there are matters you wish to discuss.

Yours sincerely

A handwritten signature in black ink, appearing to read 'J. Kavanagh', with a long, sweeping horizontal stroke extending to the right.

Jesse Kavanagh
Chairman
Capital Markets Tax Committee of Asia

