

Tax Treaties

Transfer Pricing and Financial Transactions Division
OECD/CTPA

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Confidential

Discussion Draft on Transfer Pricing Comparability Data and Developing Countries

General Comments

As stated in the discussion draft, comparability is at the heart of transfer pricing. Any steps to improve the availability and quality of financial data on comparable transactions between unrelated parties for the purposes of applying the arm's length principle to related party transactions is therefore to be welcomed.

In relation to the four possible approaches outlined in the paper for addressing tax authorities' concerns over the lack of comparable data, we would make the following comments.

Expanding access to data sources for comparables

We welcome the development of comparables databases to cover developing countries, either on a regional or a local level. We note that regional databases in particular would provide a cost-effective way for developing countries to access reliable comparable data. However, we strongly believe that both tax payers and tax authorities should have access to any databases so developed. As the OECD notes, the use of secret comparables by tax authorities to make a transfer pricing adjustment, without disclosure of the data to allow the relevant tax payer to defend their position, is inequitable and inconsistent with the drive for transparency. The use of secret comparables by the tax authorities not only lacks transparency but also encourages tax authorities to adopt more aggressive positions, resulting in lengthier and more protracted negotiations. We believe that encouraging tax authorities to use secret comparables in the risk assessment process would not provide any incremental benefit and in practice the distinction between using the data for risk evaluation purposes and for making a transfer pricing adjustment is likely to become blurred and misapplied. In summary, we believe the use of secret comparables should be strongly discouraged for all purposes.

In terms of the sources that could be used to create such databases, we have concerns regarding the increase in compliance costs that would be imposed by developing countries introducing an obligation to prepare and file statutory accounts for this purpose. We agree that the overall costs and benefits of introducing a statutory accounts requirement should be considered on a country by country basis. However, we would anticipate that those countries for which the benefits justify the costs would already have such a requirement in place.

More effective use of data sources for comparables

We support the practical and cost-effective suggestion, which is also consistent with the Transfer Pricing Guidelines, that comparables searches could be broadened to include uncontrolled transactions in the same industry but in other geographical markets. Broadening searches in this way would be of particular benefit to those MNE groups operating via entities

in several different developing countries within a relatively homogenous region and in cases where the local activities are very similar to those operating in other countries in the same region or even a different region. The approach need not be too prescriptive if the comparables are of sufficient quality. Where reliable common comparable sets can be developed to cover such regions, the associated compliance costs per entity could be significantly reduced.

Any guidance that the OECD can provide to developing countries, which would give them comfort over the use of such broader comparable sets would be welcomed.

Section 22 of the paper suggests that, where comparables are not available to evaluate a transaction from a domestic perspective, it may be appropriate to evaluate the transaction by testing the foreign counterparty, including the return earned by the foreign country. We believe that this suggestion is inconsistent with existing guidance and is not a practical or sensible approach for developing countries with limited resources. Encouraging such an approach would potentially result in a large increase in unnecessary information requests that would increase the administrative burden to both the tax payer and the tax authority and increase the time taken to resolve transfer pricing disputes.

Approaches to reducing reliance on direct comparables

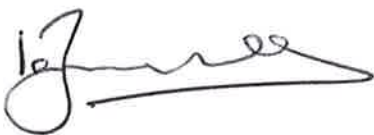
We welcome the suggested use of bilateral or regional safe harbours for low risk transactions. We would expect the use of safe harbour agreements to result in both a significant reduction in the compliance costs associated with transfer pricing and a significant increase in certainty over the transfer pricing positions taken by tax payers.

Advance pricing agreements and mutual agreement proceedings

Whilst the use of APAs and MAP procedures is fully supported in the context of significant transfer pricing dispute resolution, the time and resources required to bring such negotiations to a successful conclusion mean that we would not support the use of these procedures as a regular method of agreeing transfer pricing positions but rather to be accessed in particularly complex cases.

I trust the comments are useful, but if you would like to discuss further please do not hesitate to contact me.

Yours sincerely,



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