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By e-mail: TransferPricing@oecd.org

Rotterdam, 11 April 2014

Subject: Transfer Pricing Comparability Data and Developing Countries

Dear Mr. Andrus,

By means of this letter, EY would like to make use of the OECD's invitation to provide comments and suggestions with respect to the paper on "Transfer Pricing Comparability Data and Developing Countries" that was published by the OECD on 11 March 2014 ("the Paper").

EY would like to thank the OECD Secretariat and the Task Force on Tax and Development for their efforts to address this difficult topic and for providing directions for possible solutions. We are aware of many technical and practical challenges for taxpayers and tax administrations with respect to the availability and quality of comparability data in developing countries and therefore we appreciate that the OECD is reaching out to the relevant stakeholders to provide input and suggestions that can be used to further develop approaches to address the concerns expressed with respect to this topic.

Our comments and suggestions with respect to the Paper are presented below. If you have any comments or questions, please feel free to contact any of the following:

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Yours Sincerely,
On behalf of EY

Thomas Borstell

Ronald van den Brekel

Executive summary

Our key comments and recommendations with respect to the Paper, as further elaborated on in the Detailed Discussion sections below, are summarized as follows:

1. The arm's length principle should remain the international standard for transfer pricing purposes, even in the absence of (sufficient) local comparability data, to avoid double taxation.
2. Application of the arm's length principle in case of insufficient data should be done within the existing TP Guidelines. Methods should be applied appropriately based on the functional analysis, e.g. inappropriately applying a profit split or using a different tested party should be avoided.
3. Training programs and capacity building programs can be suitable for sharing experiences from developed countries in view of reaching a reasonable solution when dealing with imperfect comparability data.
4. In many cases using a wider regional set is likely to give a more reliable answer than using a single-country set.
5. The use of data from other countries/markets can be a reasonable alternative when dealing with absence of comparables. EY has developed a methodology, through which it can be established whether these countries/markets are sufficiently similar.
6. EY recommends the OECD to take a firmer position towards the use of secret comparables than the position in the Paper. Tax administrations should not be allowed to use secret comparables to adjust the transfer pricing of taxpayers that have taken a reasonable position.

Detailed Discussion

General

The Paper primarily focusses on the challenges faced by developing countries when performing a comparability analysis and in particular when finding and accessing comparability data. EY agrees with the observation in the Paper that developed countries are facing many of these challenges as well. The level of detail of information available in commercial databases for instance is not always sufficient to make a perfect comparability analysis.

Tax administrations, taxpayers and tax advisors in (more) developed countries have gained extensive experience in dealing with these challenges. Based on experience and taking into account the specific merits of the case at hand, taxpayers and tax administrations make efforts to come to a reasonable solution, while at the same time taken into account the inherent limitations. EY therefore strongly agrees with the OECD when it states that sharing experiences may be helpful for developing countries. Training programs and capacity building programs may be most suitable for this purpose. Written guidance to be developed by the OECD would be valuable as support materials and for those parties that cannot participate in training and capacity building programs.

When developing approaches to deal with the challenges with respect to comparability data, we recommend that the OECD take a strong and unambiguous position with respect to the use of the arm's length principle as the international standard for transfer pricing purposes. Certain sections in the Paper could in our view potentially be seen as justifications to deviate from the existing guidance for application of the arm's length principle in the absence of (sufficient) comparability data. In light of the

need to avoid double taxation and the need for certainty for taxpayers, we believe this should be avoided.

Expanding access to databases

It would clearly be very helpful for transfer pricing purposes if developing countries introduced a mandatory requirement for all businesses to file statutory accounts and make these accounts easily publicly available. However, we question how feasible this would be for many countries given the complexities and costs. We also doubt whether transfer pricing reasons alone will be sufficient for countries to take action. If mandatory filings were introduced, we recommend that a threshold be applied (e.g. based on turnover) beneath which companies are not required to file. In our experience, transfer pricing benchmarking studies in developed countries typically use a size filter on the basis that data for smaller companies obtained from the database is generally of limited use for a number of reasons.

The Paper indicates that the use of secret comparables is contentious but a distinction could possibly be drawn in practice between use for risk evaluation purposes and for making a transfer pricing adjustment. The wording in the Paper could be interpreted as only prohibiting the use of secret comparables if information cannot be disclosed to the affected taxpayers. EY recommends the OECD take a firmer position with respect to the use of secret comparables. Even if the data used is disclosed to the taxpayer, the taxpayer would not have access to secret comparables that would potentially support his position. We strongly recommend tax administrations should not be allowed to use secret comparables to adjust the transfer pricing of taxpayers that have taken a reasonable position. In case the OECD will not take such a firm position, we believe taxpayers should at least be offered sufficient protection against the use of secret comparables in case they have made a reasonable effort to comply with the arm's length principle (e.g. by doing an economic analysis based on information that was available to them). Such protection could be the shift of burden of proof to the tax administration and protection against penalties.

At the same time, EY recognises the value of data that is available to tax administrations in developing countries. One possible way of using that source - not being the inequitable use of secret comparables - could be the use of such data by tax administrations to develop safe harbours for certain types of transactions.

More effective use of data sources for comparables

One possible approach described in the Paper is broadening the comparables search to identify comparable transactions in the same sector, but in other geographic markets. EY agrees that this is a possible approach. We recommend the OECD to provide additional clarification and guidance with respect to the comparability of markets.

As expressed in our comments on the Discussion Draft on Transfer Pricing Documentation and CBCR, in our view, unless there are clear economic differences between markets from which regional data are drawn, there is no reason to suppose that a regional comparables set would give less reliable information than a local comparables set. Indeed, in many cases we believe that using a wider regional set is likely to give a more reliable answer than using a single-country set, because with a larger potential pool of comparables, it should be easier to find comparables that are economically closer to the tested transaction, and the impact of random variation will also be diluted.

EY has developed a methodology to establish the comparability of countries/markets. This methodology provides the opportunity to select countries/markets with a similar profile. Through this comparison, the

set of potential comparables can be broadened. For many developing countries, this approach provides a practical and reasonable solution. We are happy to provide you with more details of the methodology.

The Paper raises the possibility of testing the return of the foreign counterparty in a situation where there are no suitable local comparables. In our view, this would only focus on the availability of data, and has the inherent risk that the method applied does not reflect the functional analysis anymore in an appropriate way. E.g., applying a one-sided method to the 'wrong' party would attribute the residual profit (or loss !) to the wrong country. Therefore, this would be moving away from the arm's length principle.

EY strongly recommends that the OECD emphasize that functional analysis plays a vital role with respect to the choice of the most appropriate transfer pricing method and, where needed, the tested party. EY thinks that the emphasis should be on applying the most appropriate method to the circumstances of the case in every case, making all necessary efforts to make adjustments to the available comparables.

Approaches to reduce reliance on direct comparables

EY agrees that alternative approaches may be useful in situations where no comparables exist, or where no reliable adjustments to comparables can be made. However, problems may probably arise if they are not internationally accepted and/or not applied consistently across different jurisdictions. Clear guidance from the OECD would therefore be needed to provide taxpayers and tax administrations with an appropriate framework for performing such analyses. Guidance with respect to the transactional profit split method is already included in the existing OECD TP Guidelines. In accordance with this guidance, the profit split method should be selected in cases where it can be considered the most appropriate method. The absence of adequate or sufficient comparability data on itself will therefore not justify the use of this method.

The value chain analysis as mentioned in the Paper may be helpful in cases where the relative "value added" by functions throughout the value chain can be assessed objectively or against objective criteria. Wherever possible, quantitative data should be used to corroborate the value assigned to different elements of the value chain. Generally speaking it may be more appropriate to use a value chain analysis as a corroborative method in a situation where another transfer pricing method can be applied, rather than a standalone method to test or set prices. We agree that guidance on applying a value chain analysis would be helpful.

It seems that what is referred to as the "sixth method" in some occasions is in fact a crude application of the CUP method. Additional guidance with respect to application of the CUP for certain transactions (e.g. transactions involving commodities) may be helpful but in fact would not be a way to reduce reliance on direct comparables. Furthermore, EY believes that the use of safe harbours may be an effective way to reduce the reliance on direct comparables, specifically when applied on a bilateral or multilateral basis.

Advance pricing agreements and mutual agreement proceedings

EY believes that the use of APAs and MAPs are very useful mechanisms for taxpayers to obtain more comfort with respect to the appropriateness of their transfer pricing policies and to solve transfer pricing disputes. However, APAs and MAPs as such do not solve the problems with respect to the availability and quality of comparability data, EY believes that APAs and MAPs may be beneficial for taxpayers and tax administrations to deal with comparability data issues in practice. We support that work will be done under the BEPS action plan to make dispute resolution mechanisms more effective. However, we notice that a lot of developing countries do not have an APA practice, and the use of MAPs is limited due to the absence of double taxation treaties.