



Organization for Economic Co-operation and Development  
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October 1, 2013

Dear Sirs,

**Comments on the Organization for Economic Cooperation and Development (“OECD”) White Paper on Transfer Pricing Documentation**

Thank you for the opportunity to provide comments on the revised discussion draft entitled White Paper on Transfer Pricing Documentation (the “White Paper”). As a general matter, PwC supports the work being undertaken by the OECD to coordinate and simplify transfer pricing documentation requirements to the extent that it does not encourage increased compliance costs on taxpayers and promote transfer pricing disputes.

Our more detailed comments on each of the five sections of the White Paper are provided below.

***Section 1 - Introduction***

1. The focus of section 1, and much of the White Paper, is to consider the purposes and objectives of transfer pricing documentation rules and to offer suggestions as to how transfer pricing documentation rules might be modified in order to make transfer pricing compliance simpler and more straightforward. It should be noted that several of the suggestions offered throughout the White Paper may make compliance more difficult and costly on an annual basis.
2. A general theme of the White Paper is tax authorities should take a more “holistic approach” to transfer pricing documentation. It is important that taxpayer resource constraints are also clearly recognized in section 1, and to emphasize that documentation is ultimately designed to be beneficial to both taxpayers and tax authorities. The White Paper should recognize and consider both the technical and personnel constraints and limitations of taxpayers in the transfer pricing area when detailing annual transfer pricing responsibilities. Transfer pricing documentation allows taxpayers the ability to be subjected to more targeted-audits rather than general “fishing expeditions” and as such, the preparation of transfer pricing documentation should allow taxpayers to resolve audits relatively quicker and cheaper. On the other hand, transfer pricing documentation offers tax authorities a “starting point” in the risk assessment of a taxpayer and therefore allows the tax authority to better approach further risk assessment measures, as deemed appropriate. To this end, we recommend that White Paper recognize that transfer pricing documentation only offers a preliminary medium for tax authorities to gain information relevant to risk assessment. It is probably not the appropriate medium for tax authorities to request *all* information that *may* be relevant for a proper risk assessment.



3. We view the excessive documentation example noted in the White Paper of the business representative that produced around 10 documentation studies per year in the early 1990's to 2,000 separate reports as the most pressing issue to be alleviated through the efforts beginning with the White Paper. As stated by the White Paper, the project was developed as part of an effort to coordinate and simplify transfer pricing documentation requirements. The White Paper should continue to have as an objective to establish a transfer pricing documentation system that allows taxpayers to prepare documentation, to the extent possible, using available internal resources rather than indirectly requiring the involvement of outside consultants.
4. In addition, we recognize the way in which tax administrations currently interact with taxpayers differs between countries and the differences in level and form of interaction are likely to drive the documentation and risk assessment process. We recommend this is highlighted in the White Paper for both taxpayers and tax administrations to consider. In this respect, the EU Joint Transfer Pricing Forum ("JTPF") has in the past recognized such differences and reviewed distinct programs of EU Member States regarding taxpayer interaction within the framework of its ongoing work on transfer pricing risk management. This was done with a view to explore ways for harmonization and a more uniform basis for efficient and effective approaches to dealing with transfer pricing.

## ***Section II – Overview of existing guidance and initiatives on transfer pricing documentation***

5. We applaud the objective of global consistency provided that the information is useful/applicable at the local level.
6. Paragraph 13 states that documentation does not always yield a complete understanding of the global business. We recommend a comment explaining that for a majority of transactions, an understanding of the global business is often unnecessary from a local country perspective. Production of documentation that covers non-relevant transactions and details will increase compliance costs on taxpayers and increase review and filter costs on tax authorities.
7. Paragraph 14 notes the divergent nature and detail with regards to documentation requirements among countries. We ask that the White Paper consider that while each individual country has its own idiosyncratic requirements meant to address issues it finds most pressing, the diverse and non-consistent nature of global documentation requirements imposes a compliance regime on taxpayers that is highly costly and impractical.
8. Paragraph 15 addresses the differing purposes served by transfer pricing documentation. We recommend that the White Paper clearly distinguish between the risk assessment process and the transfer pricing documentation requirements. We recommend there be more discussion around the level of documentation required and the need to ensure the level of documentation necessary is commensurate with risk. The White Paper should explicitly state its view of the nature of documentation – as a tool for tax authorities in risk assessment or a mechanism for taxpayers to avoid penalties by providing information to tax authorities. Understanding the purpose of documentation will allow taxpayers to better comprehend what is required in particular circumstances.



9. We agree with the conclusion stated in Paragraph 44, that there is room for improvement with regards to the state of affairs of documentation. However, we do not agree that increasing disclosure of non-relevant information is the means to improvement.

### ***Section III – Purposes of transfer pricing documentation requirements***

10. We agree that any improvement to documentation practices around the world should start with a consideration of the purposes for requiring transfer pricing documentation, as stated in Paragraph 45.
11. We agree that taxpayers could use transfer pricing documentation as an opportunity to articulate a well thought out defense of their transfer pricing policies. However, we recommend the White Paper address this point from a small-taxpayer perspective as well. Many small taxpayers do not have detailed transfer pricing policies and only seek to appropriately document their transactions for compliance purposes. A detailed, well thought-out defense file is highly impractical to many small taxpayers which cannot allocate extensive resources to documentation.
12. We are concerned by the comment in paragraph 61 that “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.” The ability to compel production of non-local information may be go beyond the current legal ability granted to many tax authorities under their domestic law, and therefore compliance with Paragraph 61 may not be feasible for many countries at the moment. We also suggest that the ability to compel production of non-local information be limited to information relevant to determining the arm’s length price of transactions within the jurisdiction requesting the non-local information.
13. In general, the imposition of a requirement to disclose financial and other information related to an MNE’s worldwide operations that is not relevant for purposes of assessing whether the taxable income of an affiliated entity within a specific jurisdiction is appropriate (e.g. a contract service provider contractually insulated from risk), can have the effect of hindering, rather than facilitating, an enforcement of the arm’s length principle. There exists a real risk of taxing authorities using such information to impose adjustment that allocate a higher share of a consolidated group’s worldwide income to the entity that operates within the taxing authority’s jurisdiction using a measure of economic activity that is found to be expedient for such an allocation (e.g. employment or sales depending on specific situation) but which fails to take into account other facts and circumstances relevant to a true application of the arm’s length principle (e.g. the risk profile of the local entity, ownership of intangibles etc.). This has the potential to increase disputes between taxpayers and taxing authorities thereby necessitating greater resources and costs on the resolution of such disputes. The threat of double taxation in such an environment would also be greater. Furthermore, a widespread use of such formulary allocations of income, irrespective of whether they are undertaken under the garb of the arm’s length principle (e.g. by applying a profit split but one that is unsupportable given a rigorous analysis of the functions, risks and assets of the relevant group entities), can have wider ramifications on the location, scale and structure of economic activity. In particular, a widespread adoption of such formulary methods can lead to a situation where tax rate differentials between jurisdictions can impact firms’ decisions regarding the scale, location and organization of economic activity to a much greater degree than they do so today along with all the concomitant consequences of such behavior (e.g. potential relocation of jobs, investment, etc.).



#### ***Section IV – A tiered approach to transfer pricing documentation***

14. The two-tier approach is conceptually appealing. Having said this, for some complex organizations, we believe taking this approach may prove to be a step backwards in terms of providing useful documentation to tax authorities.
15. While we applaud efforts to coordinate and simplify transfer pricing documentation requirements, we view a move to the masterfile approach specifically proposed in the White Paper as misguided. The White Paper Masterfile, in comparison to the EUTPD's Masterfile, puts markedly greater emphasis on the MNE's value chain, intangibles, capital structure/debt and financial and tax position. This seems to be a very comprehensive documentation obligation which causes a significant additional burden and increases the duration of audits, as tax auditors might get sidetracked by information not relevant to the business under audit. Furthermore, it is difficult to understand why information should be provided which is not relevant to the case at hand. It would be preferable to allow a limitation of the "big picture" approach to relevant information for the case at hand. This might be a limitation based on geographic regions, business lines, products or other grounds. There should be a clear distinction between "nice to know" information and "relevant" information. This is particularly relevant given the divergence in level of training and experience of public servants charged with transfer pricing audits across countries.
16. It is PwC's observation that we are frequently requested to prepare "localized" documentation based on masterfiles. In many cases, however, the masterfiles simply contain too much unnecessary information, *i.e.* entities or business segments irrelevant to the local operations. The information to be included in the White Paper masterfile appears to be significantly more extensive than what we typically see in a masterfile. Such overload of information could result in providing the tax authorities with too much information to process. For example, is it really necessary for the tax authorities to obtain a full understanding of a company's IP ownership structure and current transfer pricing disputes in other jurisdictions if the local operations engage in limited-risk distribution activities? We recommend the White Paper acknowledge that the appealing aspect of preparing local documentation is the ability to focus on the most relevant information and provide the appropriate amount of content that is necessary to document the arm's length nature of the transactions from a local perspective. We believe the White Paper does not account for the genuine value associated with filtering non-relevant information.
17. We recommend that if a risk assessment is undertaken, the risk assessment should be transparent and, consistent with our comments in respect to the OECD Draft Handbook on Transfer Pricing Risk Assessment provided on September 13, 2013, a taxpayer should be informed of the results from the risk assessment to encourage a principled process and ensure potential issues are addressed and resolved efficiently. We endorse the fact that this risk assessment process is a useful step. However, this assessment should be a two way street.
18. In our opinion, the level of information that can be requested by the tax authority should correspond to the taxpayer's facts and circumstances and should in particular take into account the transfer pricing methods used. As a tool for risk assessment, tax authorities should seek to increase compliance and create an environment of cooperation with taxpayers in line with the OECD's work on risk assessment. We believe this level of



cooperation is not practical if tax authorities request irrelevant information seeking to understand the “big picture” in situations that do not require such understanding. The retrieval of such information is often time-consuming, difficult on both the local entity and foreign entity, and expensive. This point is aggravated to the extent that such information is likely to be misused by tax authorities and spark disagreement between tax authorities and taxpayers.

19. Sections 71 and 72: We believe that these paragraphs may not have been properly considered and should be deleted. These paragraphs introduce so-called “country-by-country” reporting requirements, through the concept of obtaining more “big picture” information regarding an MNE’s global allocation of income as a risk assessment tool. We believe this kind of information is not at all useful as a risk assessment tool and has the potential to lead to a transfer pricing system based on formulary apportionment, rather than the arm’s length standard.
20. As an initial matter, we question the assertion that business could provide this sort of information “without undue burden,” we believe it will likely be significantly burdensome. More importantly, the information being requested will have no relevance as a risk assessment tool, at least not if the assessment is whether transfer pricing conforms to the arm’s length standard. Indeed, paragraph 72 gives an example of how such information would be utilized; namely, by comparing whether a taxpayer’s income in each country is proportionate to its employees or assets in each country. In other words, the information will be used to determine whether a taxpayer’s global allocation of income conforms to the allocation which would have occurred had the taxpayer allocated its income based on a formula. That is completely inconsistent with determining transfer pricing under the arm’s length standard, and therefore renders that type of information completely irrelevant as a risk assessment tool. It also creates significant incentives for tax authorities to make transfer pricing adjustments based on formulas, with the likelihood that the formula chosen will vary from country to country, and from case to case, based upon whatever formula results in the most profit being allocated to the local jurisdiction. For example, in a country with a large consumer market and significant sales, there would be pressure to align income and taxes paid proportionally with sales. On the other hand, in a country without a big customer base but where many employees were located who did the manufacturing for the MNE, there would be pressure to align income and taxes paid proportionately with the number of employees or payroll expense in that jurisdiction. Consequently, country-by-country reporting will likely result in irreconcilable claims to the same income in different jurisdictions and increasing cases of double taxation.
21. Section 77 does not bring sufficient clarification to the question of regional versus local comparables. The White Paper states that “the use of regional comparables in situations where appropriate local comparables are available will not, in some situations, comport with the obligation to rely on the most reliable comparable information. The desire to simplify compliance processes should not go so far as to undermine compliance with the requirement to use the most reliable available information. In our experience appropriate local comparables will often be available. The main reason why regional studies are preferred is to reduce compliance costs. It is obvious that local comparables are better but in many cases it is not possible to perform local comparables studies for all jurisdictions. We recommend the White Paper consider the availability of local data and additional costs on taxpayers required to update regional studies with local benchmarking studies. The EU JTPF has made a substantial contribution in this respect by promoting the acceptance of pan-European benchmarking searches under its 2006 Code of Conduct on transfer pricing documentation for associated enterprises in the EU (“EU TPD”). Paragraph 25 of the EU



TPD states that both domestic and non-domestic comparables should be evaluated with respect to the specific facts and circumstances of a case, and that comparables found in pan-European databases should not be rejected automatically.

22. There is an underlying assumption that all documentation will initially be prepared in English. This assumption leads to unnecessary inefficiencies. We ask that the White Paper recognize that in practice, not all documentation is initially prepared in English. Many tax authorities do not prefer documentation prepared in English as it implies preparation outside the local country. On the other hand, where local tax authorities are happy to use English for the local package, the White Paper as drafted can be taken to imply that the local file should still be translated.
23. The White Paper also comments on translating documentation into local language and states that tax authorities should request translation at the beginning of an audit. We ask that the White Paper recognize that translation takes time, especially when translating technical content. For instance, in Korea, taxpayers receive about 10 days advance notification of selection for audit and audits will start and finish within 6 to 8 weeks.
24. Paragraph 77 regarding materiality standards is vague and does not offer much in the way of practical help. The idea that materiality should be considered in the context of the size and nature of the local economy and the role and importance of the taxpayer in the local economy, is a different approach to determining materiality, one that is removed from the objective of producing transfer pricing documentation. The issue as to what is and is not material is fairly problematic in situations where the implication is that all transactions will be covered. Such a standard may lead taxpayers to excessively document immaterial transactions for the sake of prudence. A certain level of flexibility should be provided which would allow an MNE to adapt its transfer pricing documentation to its size. For example, a small MNE with a limited number of cross border intercompany transactions should be able to simplify its transfer pricing documentation with more limited information relating to the group.

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On behalf of the global network of PwC Member Firms, with the contribution of my colleagues Richard Collier, David Ernack, Kathryn O'Brien, and Aamer Rafiq, we respectfully submit our response to the White Paper on Transfer Pricing Documentation. For any clarification of this response, please contact the undersigned or any of the contacts below.

Yours faithfully,

A handwritten signature in black ink that reads "Adam M. Katz".

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