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OECD - Transfer Pricing Comparability Data and Developing Countries

TransferPricing@oecd.org

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Dear Sirs,

We welcome the opportunity to comment on the OECD paper on Transfer Pricing Comparability Data and Developing Countries, published on March 11, 2014, and its efforts to explore approaches that aim for the improvement of comparables access in developing countries.

The present OECD paper reflects the initiative to address the concerns expressed in the G8's request for solutions regarding the quality and availability of information on comparable data for transfer pricing purposes and it suggests four approaches in order to address these concerns expressed by developing countries.

We agree to have our comments posted on the OECD website.

Sincerely yours,

Siemens Aktiengesellschaft

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Enclosure

1) Introduction

We applaud the release of the OECD paper on Transfer Pricing (TP) Comparability Data and Developing Countries, considering that comparability can be considered as being an essential part of TP documentation and serve to define the arm's length nature of the price applied for controlled transactions.

The lack of reliable available information to find comparable transactions and/or local independent functionally comparable companies (which can be used to accurately determine and document the arm's length price of intercompany transactions) is currently a major problem, not only for developing countries but for several developed countries as well (e.g. European countries).

In Europe, there is not enough information available to perform local benchmarks by country. Therefore most of the tax authorities have opted to accepted Pan-European benchmarks. However there are countries like Greece and Italy which have opted to sacrifice functional comparability in favor of geographic and market comparability. This inconsistency in the approach has lead to an increase of the double taxation risk that European companies face operating with these countries since it requires them to evaluate the same transaction using two different types of benchmarks, which in most cases have distinctly different results.

In Latin America, regional comparables are almost not existing forcing companies operating in the region to test the arm's length nature of their intercompany transactions against North American comparables (mainly US and Canada) which operate in a distinctive different economic market reality.

In China, tax authorities have the tendency to give more weight to functional comparability in detriment of geographical comparability. This results in benchmarks which are mostly composed of Japanese companies, even though there seems to be enough reliable information to accomplish pure Chinese benchmarks.

The limited comparable information in these regions in combination with the diverse approaches the different tax authorities around the world have chosen to solve the problem (many of which are not consistent with each other) have not only increased the double taxation risk MNE face but have also increased the administrative burden they have to incur to develop the TP documentation, by demanding two or more different analyses to evaluate the arm's length nature of the same transaction. Having experienced these problems first hand, Siemens welcomes the OECD initiative to find possible solutions that eventually could be accepted and adopted by all countries with TP legislation.

Below we provide our comments regarding the OCDE proposed approaches to solve the current comparability information problem.

2) Comments on the OECD Paper on TP Comparability Data and Developing Countries

a) "Expanding access to data sources for comparables"

For Europe and Asia additional financial information exists that is not included in the data bases. The providers of these data bases should be strongly encouraged to include, in them, all the pertinent financial information available (gross profit/margin, R&D expenses, advertizing expenses, etc.) in order to allow the tax payer to perform more precise working capital and cost capital adjustments.

In the case of regions like Latin America and Africa this request would be very difficult to fulfill since there are not enough independent listed comparable companies or information available. We recommend the OECD to not encourage the introduction of mandatory statutory accounts disclosure in these regions since this would put the local companies in a vulnerable position compared to their non listed competitors from developing countries which would not have to disclose their accounts. These data is considered very sensitive by companies, especially when they relate to trade secrets or reveal financial information to competitors. On top of this confidentiality issue, the disclosure would create an additional administrative burden for companies operating in the region.

Furthermore, we advise against the use of secret comparables unless all the pertinent information from these comparables is disclosed to the tax payers in a timely manner, in order to be able to evaluate and determine the merits for comparability.

b) "More effective use of data sources for comparables"

In our perception the most effective way to deal with the lack of local comparables would be to apply countries risk adjustments to the comparable companies on a case by case basis as the New Zealand example mentioned in the paper. The only problem with this approach is that there are several distinct ways country risk adjustments can be performed and implemented, some of which lead to inconsistent results in comparison to the others. In order for this approach to be effective, tax authorities around the world would have to agree to a common methodology to apply, depending on the country/region that the adjustment is performed. In this sense we recommend the OECD to propose specific country risk adjustments methodologies that could be debated around the world in order to reach consensus.

c) "Approaches to reducing reliance on direct comparables"

The proposals made in this section are well thought but very difficult to implement. The use of safe harbors, the profit split method or the so called "sixth method" are attractive solutions but can be applied only to a very limited number of MNE intercompany transactions. This approach does not solve the main comparability problem affecting most of the MNE intercompany transactions.

Regarding the use of safe harbors, the most obvious advantage is to provide legal certainty, without the necessity of going through the lengthy procedure of a a Advanced Pricing Agreement (APA) or a Mutual Agreement Procedure (MAP). At the same time it is of utmost importance to have a bilateral approach, because unilateral safe harbors generally create double taxation. However, also bilateral safe harbors can lead to double taxation, when they are not based on the arm´s length principle.

As we already mentioned in our comments to the OECD Discussion Draft on TP Documentation and Country by Country Reporting, we advise strongly against replacing the arm's length principle with a formulary apportionment system since this would distort the economic rationale behind the transactions.

d) "Advance pricing agreements and mutual agreement proceedings"

APAs and MAPs can help alleviate the comparability problem for certain transactions but cannot be considered a main solution to solve it because of two reasons: i) the time length for the approval of an APA and/or MAP and ii) different standards around the world for the acceptance of bilateral APAs or MAPs and the conditions for acceptance.

i. The APA and MAP processes take a considerable period of time between application and resolution. During this period, there is no direct assurance or penalty protection for MNEs. These processes provide just a "frame" for discussing the issue, but do not solve the problem regarding quality and availability of the comparables.

ii. Many countries only accept bilateral or even unilateral APAs and/or MAPs with countries with which they have signed tax treaties. In several cases, countries only accept APAs and/or MAPs for specific types of transactions.

Based on these two reasons it can clearly be predicted that the increased use of APAs and/or MAPs will only help to solve the comparability problem at a very small scale.

MAPs without a consecutive mandatory and binding arbitration resolve double taxation issues only in a very limited number of cases. We therefore support the OECD in its endeavor to promulgate the use of arbitration clauses in double tax treaties. It might be helpful to make the introduction of such a clause as a condition for the bilateral exchange of the upcoming information from Country by Country Reporting.

3) Conclusion

This OECD paper is a step in the right direction on dealing with the lack of reliable comparables in developing countries and in many developed ones as well. We consider that the next step should be for the OECD to provide more details on the proposed solutions, especially regarding the preferred methodologies to implement country risk adjustments, in order for them to be debated on a global basis.

We trust that our comments will assist the OECD in its project of increasing the quality and the availability of information on comparable data for TP purposes.

We look forward to the opportunity to continue to provide input on these important issues as the process moves forward. Thank you again for the opportunity to share our ideas and issues with the OECD paper on TP Comparability Data and Developing Countries.

In the meantime, if you have any questions about the submission, please contact:

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