

**OECD Transactional Profit Methods
Discussion Draft For Public Comment
Response by the Chartered Institute of Taxation**

1. Introduction

- 1.1. The Chartered Institute of Taxation (CIOT) is pleased to have the opportunity to comment on the Discussion Draft: Transactional Profit Methods.

2. Review of Transactional Profit Methods : Status As Last Resort Methods

- 2.1. We are supportive of the proposal by the Working Party to remove the last resort status of transactional profits methods, subject to our comments below at paragraph 2.2.
- 2.2. The tentative conclusion reached by the Working Party is that an entity "should take account of the respective strengths and weaknesses of each of the OECD recognised methods" (paragraph 5 of the Discussion Draft). This phrase also appears in the draft amendments to the Transfer Pricing Guidelines. We consider that this wording might suggest that an entity may be formally required to consider each option in every case and then demonstrate why other options have been rejected. This would be particularly onerous for the entity concerned and any such inference should be resisted. While the tentative conclusions do later say that this "does not mean that all transfer pricing methods should be analysed or tested in each case" (paragraph 8 Discussion Draft), there is possible confusion and lack of clarity in what is required.
- 2.3. Clarification could be achieved by making the following red italicised additions to the draft amendments to the Transfer Pricing Guidelines set out at paragraph 16:

"1.68 The methods set forth in Chapters II and III establish whether the conditions imposed in the commercial or financial relations between associated enterprises are consistent with the arm's length principle. No one method is suitable in every possible situation and the applicability of any particular

method need not be disproved. The selection of a transfer pricing method always aims at finding the most appropriate method for a particular case. For this purpose, it should take account of the respective strengths and weaknesses of each of the OECD recognised methods; of the appropriateness of the method considered in view of the comparability (including functional) analysis of the controlled transaction under review; of the availability of sufficiently reliable information (in particular on uncontrolled comparables) in order to apply the selected method and / or other methods; of the degree of comparability of controlled and uncontrolled transactions including the reliability of comparability adjustments that may be needed to eliminate differences between them. *The entity must be able to demonstrate why a particular method has been selected, but is not required to demonstrate why other methods were rejected.*

“1.68a The OECD’s recommendation that the selection of a transfer pricing method always should aim at finding the most appropriate method for each particular case does not mean that all the transfer pricing methods should be analysed or tested in each case. *No documentation is required to be kept demonstrating why methods that were not adopted have been rejected.* The selection of the most appropriate method should follow from the application of a process similar to the typical search process that is proposed [*reference to be inserted here*].”

Paragraphs 1.68 and 1.68a are referred to again later in the Guidelines, for example at 2.49, 3.2a and 3.49. It is therefore important that the former paragraphs are unambiguous.

3. The Chartered Institute of Taxation (CIOT) is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT’s primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

The CIOT’s comments and recommendations on tax issues are made solely in order to achieve its primary purpose: it is politically neutral in its work. The CIOT will seek to draw on its members’ experience in private practice, Government, commerce and industry and academia to argue and explain how public policy objectives (to the extent that these are clearly stated or can be discerned) can most effectively be achieved.

The CIOT’s 14,000 members have the practising title of ‘Chartered Tax Adviser’.

The Chartered Institute of Taxation
29 April 2008