## Pricing Knowledge Network

Focusing on the impact of major intercompany pricing issues

May 20, 2011

A Transfer Pricing Publication PKN Alert EU - ECOFIN adopts European Commission's transfer pricing proposals on low value adding intra-group services and welcomes its report on non-EU triangular cases

During the ECOFIN meeting held in Brussels on 17 May 2011, the EU Economic and Financial Affairs Council has endorsed the Guidelines drafted by the EU Joint Transfer Pricing Forum ('JTPF') on low value adding intra group services ('Guidelines'). The Council considers that the implementation of these Guidelines should contribute to reducing tax disputes within the EU and should improve the functioning of the internal market.

Next to endorsing the Guidelines, the Council also recognized the importance of identifying potential approaches to resolve non-EU triangular cases and welcomed the report on non-EU triangular cases.



## Guidelines on low value adding intra-group services

The welcomed endorsement of the Guidelines on the transfer pricing aspects of low value adding intra group services is the result of the work of the JTPF that started in 2007 and which resulted in the publication of a report in February 2010. The scope of this report was focused on creating a transfer pricing framework around those services that are of an administrative nature, auxiliary to the business of the recipient. The key goal of the Guidelines is to achieve an appropriate level of confidence between MNEs and European tax authorities which should ultimately result in:

- A more efficient allocation by the tax authorities of their available resources without restricting their right to conduct an audit;
- Limiting the compliance burden MNEs are faced with when demonstrating compliance with the arm's length principle for such services; and
- Reduce the potential levels of transfer pricing adjustments which should ultimately reduce the incidence of double taxation in relation to such services.

The solution put forth by the Guidelines to reach this goal is that of a "narrative". This "narrative" should be drafted in such a way that it gives sufficient confidence to tax authorities that (i) services have actually been rendered, (ii) these services provide economic or commercial value to the recipient and (iii) the recipient would have paid for the service or else performed the service itself. Also here, the Guidelines stress that a balance should be maintained between the level of information that is required, the low risk nature of the services and the compliance burden.

As for the most appropriate transfer pricing method, the Guidelines recognize that a cost based method is the most commonly observed method. As it concerns low value added services, only a modest mark-up to an appropriate cost base should be applied. The Guidelines indicate that typically agreed profit elements tend to fall in a range between 3-10%, often around 5%. However facts and / or circumstances may support a different mark-up. Also, attention is to be paid to determining the cost base in itself.

These endorsed Guidelines represent a step forward in the establishment of a single market and should allow to better facilitate the evaluation of the arm's length nature of low value adding intra group services within an EU context. It nevertheless remains to be seen how tax authorities and taxpayers in the EU will deal with these Guidelines. The JTPF has identified the monitoring of the effects of the implementation of these Guidelines as one of its important future actions.

## Non-EU triangular cases

The JTPF's report on non-EU triangular cases was also endorsed by the Council. A triangular case has been defined by the JTPF as a case where two states in a Mutual Agreement Procedure cannot fully resolve any double taxation arising in a transfer pricing case when applying the arm's length principle. The reason for this being that an associated company situated in a third State (and recognized by both Competent Authorities) had a significant influence in contributing to a non arm's length result in a chain of relevant transactions or commercial / financial relations and being

recognized as such by the taxpayer suffering the double taxation and requesting the MAP. In a non-EU triangular case, the associated enterprise identified as being the source of non-arm's length results is situated outside the EU. In its report, the JTPF made a number of non prescriptive suggestions for the resolution of disputes arising in such non-EU triangular case such as:

- The improvement and extension of the tax treaty network;
- The inclusion of article 25(5) by EU Member States when renewing or renegotiating their double tax treaties which allows for the possibility to submit MAP cases to arbitration;
- Possibility to roll-back APAs to tax years covered by a MAP procedure; and
- Inclusion of the possibility to solve transfer pricing cases under a tri-lateral approach in double taxation treaties concluded by EU Member States.

## For more information, please do not hesitate to contact:

Isabel Verlinden +32 2 710 44 22 isabel.verlinden@pwc.be

Eric Bonneaud +33 (0)1 56 57 41 33 eric.bonneaud@fr.landwellglobal.com

Ionut Simion +40 21 202 8702 ionut.simion@ro.pwc.com

Hugo Vollebregt +31 88 792 7661 hugo.vollebregt@nl.pwc.com

Jonas Van de Gucht +32 9 268 8336 jonas.van.de.gucht@pwc.be

This document is for general information purposes only, and should not be used as a substitute for consultation with professional advisors.

© 2011 PricewaterhouseCoopers LLP. All rights reserved. In this document, "PwC" refers to PricewaterhouseCoopers LLP, a Delaware limited liability partnership, which is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.