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Global Transfer Pricing

Arm's Length Standard

Global views within reach.

April 2016

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IRS files notice of appeal in *Altera* case

The Internal Revenue Service on February 19 filed a notice of appeal in *Altera Corp. v. Commissioner*, 145 T.C. No. 3 (2015), to the Ninth Circuit Court of Appeals (Docket Nos. 006253-12 and 009963-12). The Ninth Circuit will decide whether a regulation that mandates that stock-based compensation (SBC) costs related to the intangible development activity of a qualified cost sharing arrangement (QCSA) must be included in the joint cost pool of the QCSA (the "all costs rule") is consistent with the arm's length standard as enunciated under section 482. This is the second time the Ninth Circuit will consider this issue, and the first time the issue will be considered since the regulations were amended in 2003 to specifically include SBC costs in the all costs rule. The Ninth Circuit invalidated a prior version of the all costs rule that did not specifically mention SBC costs in *Xilinx Inc. v. Commissioner*, 125 T.C. 37 (2005), *aff'd*, 598 F.3d 1191 (9th Cir. 2010).

Factual background

The taxpayer-petitioner in this case, Altera Corporation, develops, manufactures, and sells programmable logic devices (PLDs) and related hardware, software, and predefined design building blocks for use in programming the PLDs. On May 23, 1997, Altera U.S., the parent

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corporation incorporated in Delaware, and Altera International, a subsidiary of Altera U.S. incorporated in the Cayman Islands, entered into a technology license agreement and a technology research and development (R&D) cost sharing agreement that met the requirements of a QCSA under the 2003 cost sharing regulations.

During Altera's 2004-07 tax years, Altera U.S. granted stock options and other SBC costs to some of its employees, including employees who performed R&D activities subject to the QCSA. Those employees' cash compensation was included in the cost pool under the QCSA, but the SBC costs were not. The IRS sent Altera notices of deficiency for those tax years, making allocations of $15,463,565 in 2004, $23,015,453 in 2005, $17,365,388 in 2006, and $15,463,565 in 2007, all pursuant to the all costs rule requiring that such SBC be included in the joint cost pool for the QCSA.

Tax court decision

Altera challenged the adjustments, and contested the validity of all costs rule. Altera argued that, in adopting this rule, the IRS had violated the Administrative Procedure Act (APA). The Tax Court agreed with Altera in a 15-0 decision on July 27, 2015, and concluded that the regulation was invalid because the IRS and Treasury had failed to satisfy the requirements of the APA. Specifically, when the IRS and Treasury issued the final rule, the files they maintained did not contain any expert opinions, empirical data, published or unpublished articles, papers, surveys, or reports supporting a determination that the amounts attributable to SBC costs must be included in the cost pool of the QCSA to achieve an arm's length result consistent with section 482 and the other regulations adopted under the statute. Additionally, when the IRS and Treasury issued the final rule, they were not aware of any written contracts between unrelated parties, whether in a cost sharing arrangement or not, that required one party to pay or reimburse the other for amounts attributable to SBC costs. Moreover, the Tax Court found that the IRS had not sufficiently rebutted taxpayer's assertions that inclusion of such costs was not consistent with the arm's length standard adopted in the section 482 regulations.

Procedural posture on appeal

The IRS is now appealing the unanimous US Tax Court opinion described above. The Tax Court decision caused taxpayers engaged in cost sharing arrangements to reevaluate whether to continue including SBC costs as part of the total costs included not only for purposes of Treas. Reg. §1.482-7, but also Treas. Reg. §1.482-9. Such an evaluation requires analysis of the facts surrounding the cost sharing arrangement on a case-by-case basis.

On appeal, the Ninth Circuit will consider all the legal arguments and it will not be bound by any of the Tax Court's legal determinations in the case.

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UK issues country-by-country reporting regulations

The UK's *Taxes (Base Erosion and Profit Shifting) (Country-by Country Reporting) Regulations 2016 SI 2016 No 237* were laid before parliament on February 26, 2016, and will apply from March 18, 2016. The regulations require certain multinational enterprises (MNEs) to report annually to the UK tax authorities (HMRC) details of revenue, profit, taxes and other measures of economic activity for each tax jurisdiction in which they do business. This information will help HMRC and tax administrations in relevant countries to assess whether MNEs may have engaged in actions intended to erode the tax base or shift profits to low-tax jurisdictions. The information will be automatically shared with other relevant tax jurisdictions in accordance with international agreements governing the exchange of information as set up by the OECD.
URL: http://www.legislation.gov.uk/uksi/2016/237/made

Reports will be required to be filed for accounting periods beginning on or after January 1, 2016. Reporting entities will have 12 months from the end of the relevant accounting period to file a report with HMRC.

The regulations provide details in support of the obligation for MNE groups in the UK to file country-by-country (CbC) reports under legislation introduced in Finance Act 2015. An Explanatory Note and Tax Information and Impact Note were published with the regulations.
URL: http://www.legislation.gov.uk/uksi/2016/237/pdfs/uksiem_20160237_en.pdf

The regulations give effect to the G20/OECD's minimum standard for CbC information to be provided to the tax authorities. The G20/OECD minimum standard was published on October 5, 2015, as part of the final package of recommendations under the base erosion and profit shifting (BEPS) project in the report on action 13: *Transfer Pricing Documentation and Country-by-Country Reporting*. The UK regulations draw on definitions from the model legislation published by the OECD, but with a variation in respect of local filing requirements for UK subgroups in some circumstances.
URL: http://www.oecd.org/ctp/beps-action-13-guidance-implementation-tp-documentation-cbc-reporting.pdf

An MNE group is defined by reference to the OECD definition as a collection of enterprises related through ownership or control that either are required to prepare consolidated financial reporting statements or would be so required if "equity interests in any of the enterprises" were publically traded on a stock exchange. To be an MNE group, the group also must operate internationally, that is, it must have resident entities or permanent establishments in more than one jurisdiction, so that wholly UK groups are excluded.

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MNE groups will be required to submit information as follows:

The UK resident ultimate parent entity (generally the company that prepares the consolidated financial statements for the group) of an MNE group with a consolidated group turnover of EUR 750 million or more in the previous accounting report (reduced proportionately for accounting periods of less than 12 months) will be required to prepare a CbC report (on a global basis).

UK entities of a non-UK-headed MNE group will be required to file a UK CbC report covering all entities within the subgroup of which it is head (the entities in respect of which the UK entity is required to prepare consolidated financial reporting statements, or would be so required if equity interests in any of the enterprises were publically traded on a stock exchange). UK permanent establishments also are subject to this requirement. An exception is available when another member of the MNE group files either a CbC report with HMRC or in another jurisdiction where the report is exchanged with HMRC. Details of the entity that filed the report, the date the report was filed, and the jurisdiction in which the report was filed must be provided to HMRC before the filing deadline.

Non-UK-headed MNE groups with a UK presence (i.e., a UK tax resident entity or a permanent establishment in the UK) can voluntarily file a CbC report with HMRC when the ultimate parent entity is resident in a country that does not require CbC reporting or does not effectively share information in accordance with international agreements. The filing of a report in the UK would allow HMRC to exchange this information with other relevant tax authorities. The ultimate parent entity must notify HMRC in writing on or before the filing deadline that the entity with the UK presence is authorized to file a CbC report for the MNE group.

Reports should be completed in accordance with the G20/OECD template. The OECD currently is developing a suitable XML schema to allow for electronic tagging of reports for automatic exchange by tax authorities. The G20/OECD template specifies that the following financial data must be included (on an aggregated basis by country):

- Turnover (split between related-party and third-party sales, but excluding dividends received);
- Profit before tax;
- Cash tax paid (including withholding tax paid in other jurisdictions);
- Current year tax accrual;
- Stated capital;
- Accumulated earnings;
- The number of full-time equivalent employees;
- The net book value of tangible assets, excluding cash and cash equivalents; and
- A list of constituent entities by country of residence and an indication of their activities.

A penalty regime will apply when there is a failure to comply or when inaccurate information is submitted. The penalties start at GBP 300 for failure to comply (and increase for persistent failure) and GBP 3,000 for the provision of inaccurate information.

An anti-avoidance measure applies to disregard arrangements when the main purpose, or one of the main purposes, of entering into the arrangements is to avoid a CbC reporting obligation.

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Comments and next steps

A number of changes have been made to the draft regulations published in October 2015 for consultation. The most significant of these is that the final regulations include a requirement for a "local filing" in the UK, which means that subgroups headed by a UK entity may need to prepare and file CbC reports in respect of entities they control. This will be relevant to subgroups in which a non-UK parent does not file a CbC report, and is likely to be of particular concern for first year (2016) filings for groups in which the jurisdiction where the parent company is resident has deferred the introduction of legislation for CbC reporting (such as Germany and the United States). In some cases, it may be necessary to file more than one report when there is more than one UK-headed subgroup. Groups potentially affected by the local filing requirements – especially for their first year – may wish to consider filing their group CbC report voluntarily with the UK tax authorities to allow it to be shared automatically with other tax authorities, some of which also may have local filing requirements. HMRC estimates that 100 UK entities of non-UK-headed MNEs will be required to file locally for their subgroups, and another 100 will be required to complete a CbC report for a short period until other jurisdictions start to require filing. In addition, HMRC estimate that 300 UK-headed MNE groups will be required to file CbC reports.
URL: https://www.gov.uk/government/publications/technical-consultation-country-by-country-reporting

As expected, the UK's requirements apply to large groups with effect for accounting periods beginning on or after January 1, 2016, and follow the agreed G20/OECD common template for reporting by country on an aggregated basis. The threshold for turnover has been set as EUR 750 million, as per the G20/OECD recommendations, but this now will have to be translated into sterling at the average rate for the previous accounting period. This means businesses that are on the verge of the revenue threshold will need to take care with exchange rate volatility; for example, the October 2015 draft regulations included the revenue threshold in sterling at GBP 586 million, but based on average rates for 2015 for a December year-end group, the sterling equivalent is reduced to about GBP 545 million.

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Italy introduces country-by-country reporting requirement

Italy introduced a country-by-country reporting obligation in its 2016 budget law approved on December 28, 2015 (Law no. 208/2015, published in the Italian Official Gazette on December 30, 2015), effective January 1, 2016.

Paragraphs 145 and 146 of Article 1 of the budget law – also known as the Stability Law – impose an obligation on multinational enterprises (MNEs) that exceed certain thresholds to prepare a country-by-country report along the lines set forth in the OECD's final report on Action 13 of the BEPS Action Plan, "*Guidance on Transfer Pricing Documentation and Country-by-Country Reporting*." MNEs subject to this obligation must report to the tax authorities financial information for each country in which the group operates.

The goal of the CbC reporting requirement is to make the global allocation of income among businesses (both legal entities and permanent establishments) belonging to an MNE more transparent, and to make the exchange of information among tax authorities easier, to support them in the evaluation of the appropriateness of intercompany transfer prices.

The CbC report should constitute an additional instrument to support the tax authorities in their risk assessment activities, as indicated by paragraph 145 of Article 1 of the Stability Law, as well as the OECD document "*Guidance on the Implementation of Transfer Pricing Documentation and Country by-Country Reporting*."

The report must be prepared by parent companies of multinational groups with a consolidated turnover of over €750 million (in the tax period before the one referred to in the report), and that are the entities ultimately required to prepare group consolidated financial statements and are not controlled by anything other than individuals. The report must be submitted to the tax authorities in the country of residence, and eventually will be shared with the tax authorities of other countries through exchange of information tools.

It must be highlighted that, pursuant to Art.1, paragraph 146, the reporting obligation, as recommended by the OECD and stated in the regulations of other countries (such as Spain), is extended to subsidiaries resident in Italy for fiscal purposes, part of multinational companies that meet the conditions set forth in the law, if the "ultimate" parent company required to prepare consolidated financial statements is resident in a state that:

- Has not introduced the obligation to file a CbC report;
- Does not have an agreement in force with Italy for the exchange of information related to the CbC reporting; or
- Fails to fulfil its obligation to exchange information relating to the CbC report.

The aforementioned rules refer exclusively to subsidiaries, and it is not clear whether the same apply also to Italian permanent establishments of foreign entities, as, for example, provided by the Spanish CbC reporting regulations.

Instructions regarding the timing and procedures for filing the CbC report with the Italian tax authorities will be provided in an implementing decree to be issued by the Ministry of Economy and Finance within 90 days after the date of entry into force of the Law (January 1, 2016),

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having regard to the relevant OECD guidelines (Action 13 and the document *Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting*).

According to the OECD's recommendations, the first CbC report should cover fiscal years beginning on or after January 1, 2016, and the submission deadline should be either the filing date of the relevant tax return, or within 12 months from the end of the reference year (for companies with calendar year reporting periods, the deadline would be December 31, 2017, for the report relevant to fiscal year 2016).

Content of CbC report

Assuming the standard CbC report is adopted according to OECD Action 13 recommendations, the Italian CbC report would comprise two different sections:

- A first section, containing information on the allocation of the MNE's income and resources by tax jurisdiction, and in particular:
    - Total revenues obtained in a given country, segregated by related and third-party revenues;
    - Total profits (losses) before income tax of all the entities resident for tax purposes in each tax jurisdiction;
    - The group's total current tax expenditures in each country (both in terms of tax accrued and cash taxes paid);
    - Total equity (including the free capital of permanent establishments) of all entities resident for tax purposes in each tax jurisdiction;
    - Total accumulated earnings of all entities resident for tax purposes in each tax jurisdiction as of the end of the year;
    - Number of employees working in the various countries in which the group operates; and
    - Net book value of tangible assets (other than cash and cash equivalents) of all entities resident for tax purposes in each tax jurisdiction.
- A second section, containing information on the individual group entities (both permanent establishment and subsidiaries) operating in the different countries, including:
    - Tax jurisdiction of residence;
    - Tax jurisdiction of the entity at the time of incorporation; and
    - Type of activities carried out by each group entity.

Taxpayers that fail to comply with the CbC reporting requirement (missing or incomplete reporting) will be subject to an administrative penalty between €10,000 and €50,000.

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Canada announces proposed country-by-country reporting requirements

As anticipated by many, Canada's 2016-2017 federal budget, released March 22, proposes new country-by-country (CbC) reporting for large multinational entities (MNEs). While draft legislation is not yet available and will be released for comment "in the coming months," indications in the 2016 budget are that Canada's CbC rules will be consistent with the Organisation for Economic Co-operation and Development (OECD) recommendations in the October 5, 2015, final report *Transfer Pricing Documentation and Country-by-Country Reporting – Action 13* (OECD Guidance).

Canada has generally indicated support for the OECD's action plan on base erosion and profit shifting (BEPS). Countries including Australia, France, Ireland, the Netherlands, the United Kingdom, and the United States all have introduced domestic legislation to adopt CbC reporting for large MNEs. With the release of the 2016 budget, Canada has now also communicated proposed CbC reporting implementation, and has also formally endorsed other BEPS-related changes to international guidance on transfer pricing for MNEs.

While full details will be available only when legislative changes are enacted, at this time the following key transfer pricing themes are known from the 2016-2017 budget.

CbC reporting threshold

The first question taxpayers will consider in respect of CbC reporting is whether they actually will be subject to a requirement to prepare the CbC report (or are likely to be required to do so in the near future) or whether they are exempt from this obligation. The budget has made clear that taxpayers with total annual consolidated group revenues below EUR 750 million do not have a CbC filing obligation. It appears that the reporting threshold is in euros rather than Canadian dollars for consistency with OECD guidance.

While many countries have used the OECD-recommended CbC threshold of EUR 750 million, a number of countries have proposed a local-currency-denominated threshold, such as the CbC reporting threshold of USD 850 million in the proposed US regulations, or the CbC reporting threshold of AUD 1 billion in Australia's legislation. The use of different currencies for CbC reporting thresholds could give rise to inconsistent global CbC filing requirements.

For example, assume that at the current exchange rates, there is harmony between the US and Canadian thresholds for CbC reporting. Therefore, today, if an MNE with a US ultimate parent and a subsidiary in Canada has group annual revenue of EUR 750 million, both the Canadian tax authorities and the US tax authorities would require a CbC report, because the assumption is that EUR 750 million = USD 850 million, and therefore both thresholds are met. However, if the same MNE has group annual revenues in a subsequent year equal to EUR 750 million, but the USD has appreciated considerably as compared to the euro, and EUR 750

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million is now less than USD 850 million, this could give rise to a situation in which the CbC report may not be required in the United States, but would be required in Canada.

It remains to be seen how countries will deal with the issue of changes in foreign exchange rates over time, which could give rise to inconsistent CbC reporting requirements. At this point in time, it appears that MNEs will be required to monitor the rules in subsidiary jurisdictions in addition to the rules in the ultimate parent entity's jurisdiction, or risk running afoul of local CbC requirements.

CbC report data requirements

Consistent with OECD Guidance, although with a relatively low level of detail at this point, the budget notes that the CbC report will include the global allocation by country of key variables for the MNE, including revenue, profit, tax paid, stated capital, accumulated earnings, number of employees and tangible assets, as well as the main activities of each of its subsidiaries. The draft legislative proposals are expected to add clarity as to exactly what is expected to be included in the CbC report, and in what format.

First year of CbC report

The budget notes that the first CbC report will be required in Canada for taxation years after 2015. In other words, taxpayers with a calendar year-end will first have CbC filing requirements pertaining to the year ending December 31, 2016. This is consistent with the OECD guidance and the legislation in many countries globally.

The Canadian CbC filing requirement is likely to be one year earlier than in the United States, as the US proposed regulations are expected to apply to taxable years that begin on or after the date of publication of the US Treasury decision adopting the rules as final regulations. Since the final US regulations will likely be published sometime in 2016, taxpayers in the United States with a calendar year-end would first have a CbC reporting requirement for US purposes with respect to the year ending on December 31, 2017, rather than December 31, 2016.

MNEs are again cautioned to consider the filing requirements of subsidiaries as well as ultimate parent entities, because local rules may vary, and some jurisdictions – including Canada – will likely require CbC reporting for subsidiaries even if the ultimate parent entity is in a jurisdiction that does not require a CbC report.

Deadlines to file CbC report

As noted in the budget, MNEs required to file a CbC report with the Canada Revenue Agency (CRA) will be required to do so within one year of the end of the fiscal year to which the report relates. Therefore, for taxpayers with a calendar year-end, the CRA would expect the CbC report from Canadian CbC filers by December 31, 2017, in respect of the first CbC year-end of December 31, 2016. This is consistent with OECD guidance.

The expectation appears to be that there will be a six-month time lag between the time CRA receives the reports and when it exchanges them with other jurisdictions, as it is noted that the

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first exchanges between jurisdictions of CbC reports are expected to occur by June 2018. This is also consistent with the OECD guidance, which mentions that CbC reports should be exchanged as soon as possible, and no later than 18 months after the last day of the MNE group's fiscal year.

Subsidiary filing requirement

The budget notes that in some circumstances, it is possible that the Canadian CbC requirements may necessitate a CbC report to be filed by a Canadian subsidiary, if the foreign ultimate parent entity does not face the same obligation in its tax jurisdiction, or if there is no mechanism that would allow Canada to obtain the CbC report filed in that jurisdiction. In such instances, the budget suggests that an MNE may avoid the imposition of this filing requirement on multiple subsidiaries in multiple jurisdictions by designating one of its subsidiaries to be a "surrogate" for filing purposes.

Increased compliance burden

The new CbC reports will require significantly increased compliance effort to gather and prepare CbC information. Some data may not be readily available on a global level within MNEs, and many will have to upgrade their existing information systems or introduce new measures to be able to retrieve and gather the required data.

One strategy to better prepare for CbC reporting is to proactively perform a mock CbC report prior to implementation based on historical data. This approach would provide MNEs the opportunity to determine whether existing systems are up to the task of gathering the necessary data before filing deadlines loom.

Increased amount of information provided to tax authorities

The new CbC reports are meant to provide tax authorities around the world with high- level overviews of the global operations of large MNEs to enhance transparency. While the information is intended solely to "assist tax administrations in performing effective risk assessments" and not as a means of calculating transfer pricing adjustments, the questions that tax administrations may ask subsequent to their review of the CbC reports may ultimately lead to adjustments.

By preparing a mock CbC report proactively, as suggested above, in addition to identifying whether the required data can be reliably captured, MNEs can also assess the information produced and consider how it may be interpreted by a tax authority. These insights may provide MNEs the opportunity to understand potential or perceived risk areas and determine whether additional information is needed to clarify the CbC data, as well as whether transfer pricing policies themselves may require further clarification and monitoring for adherence to changes to the OECD transfer pricing guidelines.

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Additional CbC questions yet to be answered

Given the limited details provided in the budget, a number of questions remain that will likely be answered when draft legislation is released for comment in the coming months. Such questions include, for example:

- The potential penalty regime in Canada for failure to provide CbC reports to the CRA on time;
- Whether additional exemptions from CbC reporting will be included in Canada, similar to the US exemption related to national security;
- The specific details regarding international exchanges of information (for example, by way of signing the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports or negotiating separate agreements with each of the countries with which Canada expects to exchange CbC data);
- Subsidiary requirements to inform the CRA of the jurisdiction of the ultimate parent entity or "surrogate" entity;
- Specifics in respect of global inconsistencies in CbC reporting requirements; and
- Detailed definitions of important concepts and reporting items.

Other revised transfer pricing guidance

While the arm's length principle is mandated by section 247 of the Income Tax Act, the act itself is silent as to how this principle is to be interpreted and applied. As a result, the CRA, taxpayers, and Canadian courts have used the OECD *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* to interpret and apply section 247. The budget has clarified that the OECD's recent BEPS-related revisions to these guidelines are being applied by the CRA.

The budget asserts that the CRA's current audit and assessing practices already apply the OECD's revisions. The revisions are said to provide an "improved interpretation of the arm's length principle," rather than as a "change in the guidance." It is possible that the intent of this wording is to allow for retroactive application of "improved interpretation" instead of applying the revised guidance only to subsequent taxation years. It is easy to see potential complications as a result of this view.

The budget announcement that the revised guidelines are being applied by CRA could have far-reaching consequences, though additional specific interpretation will be required for clarity. For example, the revised guidelines introduce a three-tiered documentation structure that, in addition to the CbC report, includes master file and local file requirements. The budget does not contain any specific references to a potential adoption of the master file or any significant revisions to the existing documentation requirements currently described in subsection 247(4) of the Act.

Looking ahead

While many questions will be answered only when the draft legislative proposals are released in the coming months, it is clear from the 2016-2017 budget that Canada is committed to the OECD's BEPS project and will continue to work with the international community in the interest

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of global transfer pricing consistency. Despite this direction of global coordination, it will be important for MNEs to be vigilant in identifying local variations in respect of BEPS implementation to ensure proper compliance with CbC requirements.

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US Tax Court rules for IRS on question of aggregation in transfer pricing adjustment

The US Tax Court on February 29 rejected the taxpayer's motion for summary judgment in the case of *Guidant LLC v. Commissioner*, 146 T.C. No. 5 (2016). The case will now be resolved on the full record as developed at trial, which is set to begin on July 25, 2016, in Chicago.

The Tax Court ruled that, as a matter of law:

- The IRS is not required to determine the "true separate taxable income" of each controlled taxpayer in a consolidated group within the meaning of Treas. Reg. §1.482-1(f)(1)(iv); and
- The IRS did not have to make specific adjustments with respect to each controlled transaction at issue in the case, but could instead aggregate the controlled transactions when exercising its authority under §482.

The Tax Court did not rule on whether the IRS was correct in choosing to do an aggregated valuation in the case, but merely whether the IRS was prohibited from doing so as a matter of law. The Tax Court's finding allows the issue of whether aggregation was appropriate in this case to be decided as a factual matter at trial.

This case involves Guidant LLC, a cardiac medical device maker, who is protesting $1 billion in transfer pricing adjustments related to technology licenses and manufacturing arrangements between it and its Puerto Rican and Irish subsidiaries. The initial case was consolidated with: (i) a challenge by related party Boston Scientific Corp., which is challenging an $829.7 million adjustment; and (ii) another set of cases filed by an affiliate named Cardiac Pacemakers Inc. The total income adjustments for all the cases combined to $3.5 billion.

As justification for its position that it was not required to determine the true separate taxable income of each controlled taxpayer, the IRS asserted that it did not have enough information to make reliable member-specific adjustments on the basis of the information available to it. The IRS stated that it was unable to extract the information necessary to ascertain the income reported by each Guidant group member with respect to the products and transactions at

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issue. The IRS also stated that it was unable to determine the separate taxable income of each Guidant group member for the products and transactions at issue.

Although each Guidant group member's available financial statements encompassed all activities the entity performed and all the products it produced and sold, including those not at issue in this case, the Tax Court agreed with the IRS, finding that the taxpayers did not maintain their financial records in a manner that allowed them to readily track income and expenses by place of manufacture, and thus it was not possible to tie the income and expenses in the business unit financial statements to particular product lines. While the available information enabled the IRS to make what it considered a reliable calculation of consolidated taxable income for the Guidant group, the IRS did not believe the available information enabled it to make a sufficiently reliable calculation of member-specific adjustments for each of the Guidant group members.

The Tax Court found that the plain language of the Treasury regulation at issue clearly mandates that both consolidated and separate taxable income be determined, but that the regulation does not specifically require the IRS to determine separate taxable income contemporaneously with making a §482 adjustment. The Tax Court further reasoned that the primary principle underlying the consolidated return regime is a taxing of the true net income of the consolidated group as a whole:

Bearing the principles of the consolidated return regime in mind, we read [Treas. Reg. §] 1.482-1(f)(1)(iv)…to require the [IRS] to determine both [consolidated taxable income] and [separate taxable income] when making a [§] 482 adjustment with respect to income reported on a consolidated return, but also giving the [IRS] a certain latitude to decide when the determination of [separate taxable income] becomes necessary. As we see it, the [IRS]'s main responsibility under the regulation [at issue… is to make sure that the section 482 adjustments serve the purposes of the consolidated return regime discussed above, i.e., reflect the consolidated group's true net income clearly and prevent an avoidance of such tax liability.

Because of this underlying rationale in the regulation, the Tax Court held that the IRS's decision to defer making the true separate taxable income determination until such time when the determination is actually required is not improper as a matter of law. The Tax Court further noted that, if Guidant's interpretation were to prevail, then the IRS might not be able to make a §482 adjustment if a taxpayer consciously withheld or failed to maintain records necessary for separate taxable income adjustments.

In discussing the second issue on aggregation, the Tax Court held that the Treasury regulations allow the IRS to aggregate separate transactions when doing so provides the best means of determining the true taxable income of a controlled taxpayer. Because of this, the IRS's decision to aggregate the transactions involving tangibles, an intangible, and services in this case is a question of fact and should be resolved on the trial record.

Because the Tax Court denied Guidant's motion for summary judgement, the case will now proceed to a full trial.

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Belarus refines transfer pricing regulations

Changes to the Belarussian Tax Code introducing more detailed and stricter transfer pricing rules entered into effect January 1, 2016. For the most part, these changes are aimed at harmonizing the Belarussian transfer pricing legislation with the OECD transfer pricing guidelines. However, many of the changes appear to impose more restrictive rules on taxpayers.

Transfer pricing documentation requirements

Effective January 1, 2016, taxpayers are required to prepare and file transfer pricing reports. Before this change, the submission of transfer pricing documentation was not required.

Taxpayers must prepare and file the following transfer pricing reports:

- **Transfer pricing documentation** (for controlled transactions over the BYR 10 billion threshold);
- **Economic justification** of the applied price (for real estate transactions and foreign/domestic transactions over the BYR 1 billion threshold); and
- **Controlled transaction notifications** (taxpayers are required to notify the tax authorities of each transaction by sending electronic invoices).

The deadlines for submission of transfer pricing documentation and economic justification are very tight. For desk tax audits, documentation must be submitted when requested by the tax authorities, but within at least 10 working days from the date of the request. For field tax audits, documentation must be submitted when requested by the tax authorities, but within at least five working days from the date of the request.

Controlled transactions

Effective January 1, 2016, transactions that involve intellectual property (licensing transactions), leases, and loans are subject to regulatory control (previously, only transactions involving goods, works, and services had been subject to control).

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Real estate transactions

The list of real estate transactions subject to the Belarussian transfer pricing regime has been expanded. The transfer pricing rules now apply to the real estate transactions specified below, provided the transaction price differs from the arm's length price by at least 20 percent:

- Sale or purchase of real estate; and
- Sale or purchase of housing bonds.

Both transactions between Belarussian residents and cross-border transactions are subject to control. No threshold is set for such transactions.

Before 2016, only transactions involving the sale of real estate were subject to transfer pricing control. Transfer pricing rules did not apply her to the purchase of real estate nor to the sale/purchase of housing bonds.

Cross-border transactions

In contrast, the list of cross-border transactions subject to the Belarussian transfer pricing regulations has been shortened. The list now includes:

- Transactions with related nonresidents, provided the transaction amount exceeds BYR 1 billion (approx. EUR 49,000 as of January 1, 2016);
- Transactions with nonresidents registered in low-tax jurisdictions, provided the transaction amount exceeds BYR 1 billion. The list of low-tax jurisdictions is published by the President of the Republic of Belarus;
- Transactions with related nonresidents or nonresidents registered in low-tax jurisdictions if independent intermediaries with no substantial functions are involved. The threshold of BYR 1 billion is also applicable to these transactions;
- Transactions involving strategic goods, provided the transaction amount exceeds BYR 10 billion (approx. EUR 490,000 as of January 1, 2016). The list of goods will be published by the Government of the Republic of Belarus;
- Transactions by large taxpayers, provided the transaction amount exceeds BYR 10 billion. The list of large taxpayers is published by the Ministry of Taxes and Duties of the Republic of Belarus.

Before 2016, all cross-border transactions (with both related and unrelated parties) were subject to the transfer pricing regulations if the volume of sale or purchase transactions with a single party exceeded BYR1 billion in the relevant tax period.

Transactions within Belarus

Before 2016, domestic transactions did not fall within the scope of the transfer pricing regime (except for real estate transactions). However, effective January 1, 2016, domestic transactions are regarded as controlled if entered into with a related party, which has the right to corporate income tax exemption inasmuch as the party:

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- Falls under certain categories of taxpayers not subject to corporate income tax;
- Applies specific taxation regimes (for example, the unified tax system); or
- Operates in the territories specified by the legislation (free economic zones, High Technology Park, etc.).

If such transactions involve independent intermediaries with no substantial functions, they are also deemed controlled. The threshold for domestic transactions is BYR 1 billion.

Safe harbor rule

In 2016, a 20 percent variance from the arm's length price range is acceptable. If the variance goes beyond 20 percent, tax liabilities are to be adjusted to the minimum/maximum range values.

This rule was introduced into the Belarussian transfer pricing legislation in 2012, and has not been amended since. However, it is expected to be abolished in the near future.

Expanded rights for tax authorities

The tax authorities have the right to obtain any relevant information required to determine the comparability of commercial and financial conditions from all sources (transaction parties, state authorities, or third parties). This provision is unfavorable for taxpayers, as they do not have access either to the information available to the state authorities or to information from third parties.

Transfer pricing methods

Introduced in Belarus in 2016, the profit split method will be applied in accordance with the OECD transfer pricing guidelines.

The Belarussian transfer pricing rules now comprise five methods, to be applied in strict hierarchical order:

- Comparable uncontrolled price method (CUP);
- Cost plus method;
- Resale price method;
- Comparable profitability method (CPM); and
- Profit split method.

Changes in the determination of related parties

The list of instances in which companies are to be treated as related parties has been extended. Now, if a party has a direct and/or indirect participating interest in other entities, and the participating interest in each of the entities is at least 20 percent, those entities are regarded as related parties. Previously, only members of "vertical ownership chains" with participating interest exceeding 20 percent had been treated as related parties.

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In addition, in 2016, when at least 50 percent of two entities' collective executive bodies or boards of directors are the same individuals, the entities are considered related parties.

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IRS issues international practice units on transfer pricing topics

The Internal Revenue Service released eight new international practice units (IPUs) in February and March:

- Outbound Transfer of Domestic Stock
  URL: https://www.irs.gov/pub/int_practice_units/ISO9411_08_06.pdf
- Pricing of Platform Contribution Transaction (PCT) in Cost Sharing Arrangements (CSA) Acquisition of Subsequent IP
  URL: https://www.irs.gov/pub/int_practice_units/ISO9411_01_02.pdf
- Intercompany Interest Rates Under the Situs Rule of IRC Section 482
  URL: https://www.irs.gov/pub/int_practice_units/ISI9422_08_01.pdf
- Outbound Transfer of Foreign Stock
  URL: https://www.irs.gov/pub/int_practice_units/ISO9411_08_04.pdf
- Change in Participation in a Cost Sharing Arrangement (CSA) – Controlled Transfer of Interest and Capability Variation
  URL: https://www.irs.gov/pub/int_practice_units/ISO9411_01_06.pdf
- Residual Profit Split Method – Outbound
  URL: https://www.irs.gov/pub/int_practice_units/ISOPUOP_1_7_04.pdf
- Outbound Services by US Companies to CFCs
  URL: https://www.irs.gov/pub/int_practice_units/ISO9411_07_02.pdf
- Review of Transfer Pricing Documentation by Outbound Taxpayers
  URL: https://www.irs.gov/pub/int_practice_units/ISOPUOP_1_7_02.pdf

The first of these IPUs discusses the outbound stock exception to the general rule of IRC Section 367(a)(1) relating to outbound transfers of domestic stock, and the second involves a case study where a US parent company acquires a target company and makes some of the target's resources, capabilities, and rights available to a cost sharing agreement. The IPU addresses the best method for determining the arm's length price of the acquisition PCT payments with respect to those resources, capabilities, or rights.

Another IPUs discusses how to determine whether the rate charged on a loan by a foreign parent corporation to a US subsidiary corporation is arm's length pursuant to Treas. Reg. §1.482-1(a)(2). It also addresses the threshold concept of how to determine whether the loan represents bona fide debt. The next IPU focuses on the exception in Treas. Reg. §1.367(a)-3(b) for outbound transfers of foreign stock and the reporting requirements necessary to meet that exception. The next IPU discusses the issues surrounding changes in participation in a CSA under Treas. Reg. §1.482-7.

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Another IPU discusses how to determine if the residual profit split method (RPSM) is the best method, and if so, how to apply the RPSM to a transaction between a US parent company and its controlled foreign corporation (CFC) in which intangible property is employed. The relevant regulations for the RPSM are outlined in Treas. Reg. §1.482-6. The RPSM is also discussed in Treas. Reg. §§1.482-7 (Cost Sharing Arrangements) and -9 (Services), but those sections are not the subject of this unit. While the RPSM is applicable to both inbound and outbound controlled transactions, the IPU published March 7 covers only the outbound scenario.

Another IPU discusses services that US parent companies and their US affiliates provide to their CFCs. It first reviews the threshold issue of whether an activity that benefits the CFC has been performed. It then provides an overview of the seven different transfer pricing methods provided by the Treasury regulations to determine whether an arm's length charge has been applied, with a particular emphasis on the services cost method.

The final IPU provides an introduction to the review of an outbound taxpayer's contemporaneous transfer pricing documentation. Such documentation needs to be in existence at the time the taxpayer files its tax return and also must be provided to the IRS within 30 days of a request in order for the taxpayer to avoid the penalties under I.R.C. §6662(e) and (h). The transfer pricing documentation is used by the IRS as described in the Transfer Pricing Audit Roadmap in the initial risk analysis and development of a preliminary working hypothesis during audit. The IPU highlights that even if a taxpayer supplies all the principal documents specified in the regulations, penalties may still apply if the taxpayer's documentation fails to give "a complete understanding of the taxpayers controlled transactions."

The IRS began the IPU program to provide IRS staff with explanations of general international tax concepts, as well as information about specific types of transactions. IPUs are not official pronouncements of law or directives and cannot be used, cited, or relied upon as such. IPUs provide a general discussion of a concept, process, or transaction and are a means for collaborating and sharing knowledge among IRS employees. IPUs may not contain a comprehensive discussion of all the pertinent issues, law, or the IRS's interpretation of current law surrounding that issue. In addition, IPUs do not limit an IRS examiner's ability to use other approaches when examining issues. Finally, IPUs and any nonprecedential material (such as private letter rulings, determination letters, or Chief Counsel advice) that may be referenced in an IPU may not be used or cited by taxpayers as precedent.

While not authoritative, the IPUs discuss topics that are of interest to the IRS and may be areas of focus by international examiners.

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Irish Revenue Announce Formal APA Program

At the 2016 Global Tax Policy Conference held in Dublin in March 2016, a representative of the Irish Revenue Commissioners indicated that a formal bilateral advance pricing agreement (APA) program would be introduced in Ireland in the near future.

When Ireland's formal transfer pricing regime was introduced into Irish law in 2010, no formal bilateral APA program was in place. However, due to Ireland's network of double taxation treaties, the competent authority of Irish Revenue enters into bilateral APA discussions with other competent authorities on a case-by-case basis when an APA application has been accepted by the other competent authority. Cases are considered when they are deemed complex or likely to result in a mutual agreement procedure (MAP) request under Ireland's treaty network.

Guidelines in relation to Ireland's new bilateral APA program are expected later in 2016, and the program is likely to include APAs that will last three to five years, with a rollback facility. In addition, there will be an annual monitoring requirement in place. No APA filing fees will apply.

Commentary

In light of expected uncertainty on how tax authorities will deal with complex transfer pricing arrangements arising from the OECD base erosion and profit shifting (BEPS) project, taxpayers are increasingly seeking certainty on how such arrangements will be dealt with. The APA process offers taxpayers the opportunity to enter into transfer pricing arrangements with tax authorities, and the imminent introduction of a formal bilateral APA program by the Irish Revenue is a welcome development.

In October 2015, Irish Revenue issued a publication entitled, "The Role of The Competent Authority," which provides an overview of the function of the Irish competent authority and its role in MAP and APA programs in light of the BEPS project. In relation to APA cases, as of the date of publication in October 2015, there were six new requests for bilateral APAs and eight APAs in force. In the current challenging tax environment, the number of cases may be expected to increase in the years ahead, as taxpayers seek certainty regarding their transfer pricing arrangements with related parties.
URL: https://www.irs.gov/pub/int_practice_units/ISOPUOP_1_7_02.pdf

Ireland does not have a unilateral APA program in place, and taxpayers seeking clarification on transfer pricing matters would have to follow the bilateral process within Irish Revenue.

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IRS Releases Annual APA Report

The Internal Revenue Service on March 31, 2016, released Announcement 2016-12, the advance pricing agreement (APA) annual report covering the activities of the Advance Pricing and Mutual Agreement (APMA) Program during calendar year 2015.

The annual report provides a brief summary of recent APA developments in the APMA Program and a statistical snapshot of the program's APA activities during 2015. The 2015 annual report highlighted some efficiencies and an increase in the number of applications in comparison to the prior year.

Statistical highlights of the 2016 APA annual report include:

- **Completed APAs:** During the 2015 calendar year, APMA executed 110 APAs (30 unilateral, 80 bilateral, and no multilateral), compared to 101 APAs in 2014 and 145 APAs in 2013. APA renewals accounted for 66 of the 110 APAs executed, with 18 unilateral and 48 bilateral renewals. As in 2014, renewals represented slightly more than half of all completed APAs.
- **New Cases:** The IRS received 183 APA applications (52 unilateral, 127 bilateral, and 4 multilateral) in 2015, a significant increase from the 108 APA applications received in 2014. While Japan and Canada continue to account for the largest share of bilateral APA requests (39 percent and 17 percent, respectively), APA requests involving other countries have become a significant part of APMA's inventory. Notably, APAs involving Germany and Korea represented 9 percent and 8 percent of APA requests, respectively; the United Kingdom, Australia, and China had 5 percent, 4 percent, and 4 percent shares, respectively.
- **APA Inventory:** The APMA Program had 410 cases in active inventory at the end of 2015: 85 unilateral APAs, 316 bilateral APAs, and 9 multilateral APAs. In comparison, active inventory was smaller at the end of 2014, with 336 cases. The number of pending APA's rose in 2015 dule largely to the record numbers of APA requests received during the fourth quarter.

One notable milestone for the APMA Program in 2015 was the execution of the first bilateral APA between the United States and Italy.

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Turkey proposes adoption of country-by-country reporting requirement

The Turkish Revenue Administration on March 16 released a proposed transfer pricing communiqué relating to the adoption of the country-by-country (CbC) reporting requirement under the OECD's base erosion and profit shifting (BEPS) Action 13 recommendations.

The proposed regulations – Draft Transfer Pricing General Communiqué No. 3 – follow the three-tier documentation approach contained in the OECD's "Transfer Pricing Documentation and Country-by-Country Reporting Final Report" issued on October 5, 2015, and would require:

- A **master file** with global information about a multinational enterprise (MNE) group, including specific information on intangibles and financial activities;
- A **local file** with detailed information on all relevant intercompany transactions of the particular group entity in Turkey; and
- A **CbC report** of income, earnings, taxes paid, and certain measures of economic activity.

The goal of the CbC reporting requirement is to make the global allocation of income among legal entities belonging to an MNE more transparent, and to make the exchange of information among tax authorities easier, to support them in the evaluation of the appropriateness of intercompany transfer prices and in their risk assessment activities.

Master file

Turkish corporate income taxpayers that are members of a multinational group with assets and net revenues of TL 250 million (approx. €78 million) or more in the previous year (i.e., 2015), will be required to prepare a master file to be submitted to the Turkish Tax Authority for fiscal years beginning on or after January 1, 2016. The master file must be prepared by the end of the second month following the filing deadline for the corporate income tax return (that is, by the end of June 2017 for taxpayers with calendar year fiscal accounting periods).

The required information in the master file can be grouped into five categories:

- The MNE's organizational structure;
- A description of the MNE's business or businesses;
- The MNE's intangibles;
- The MNE's intercompany financial activities; and
- The MNE's financial and tax positions.

Local file

According to the draft communiqué, corporate taxpayers registered with the Large Taxpayers' Tax Office (LTTO) and corporate taxpayers operating in Turkish free trade zones are required to prepare annual transfer pricing documentation reports regarding both their cross-border and domestic transactions with related parties.

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The obligation to prepare a local annual transfer pricing documentation report has been in place in Turkey since 2007, as per Transfer Pricing General Communiqué No. 1, announced on November 18, 2007. Local documentation must be prepared according to the guidelines stipulated in Appendix 3 of Transfer Pricing General Communiqué No. 1, which has been in effect since November 18, 2007.

The only difference introduced through Draft TP General Communiqué No. 3 regarding the local file obligation is that cross-border related-party transactions of corporate taxpayers operating in Turkish free trade zones are now also included in the scope of local documentation, which are currently outside the scope of local documentation. Corporate taxpayers not registered with the LTTO will continue to prepare annual documentation only for their cross-border transactions with related parties (as under the current rules). These taxpayers are also required to maintain background documents regarding their domestic related-party transactions. The background documents required to be maintained are very detailed and similar to the contents of the transfer pricing documentation detailed in Appendix 3 of Transfer Pricing General Communiqué No. 1.

The local file must be prepared by the time corporate tax returns are filed (by April 25 of the following year for taxpayers that have calendar year fiscal accounting periods).

In addition to the local file requirements, all corporate taxpayers will be required to complete a "Form Relating to Transfer Pricing, Controlled Foreign Companies, and Thin Capitalization, Form No:2," as stipulated in Appendix 2 of the existing Transfer Pricing General Communiqué No. 1, and must submit it to their tax office with their corporate tax returns. The form is intended to collect summary information on the identity of related parties, include an enumeration of related-party transactions, and identify transfer pricing methods utilized to determine intercompany transfer pricing policies.

Corporate taxpayers with assets and net revenues of TL 100 million (approx. €31 million) or more in the previous year (i.e., in 2015 with respect to the reporting obligations for 2016), are required to complete an additional form – Form No:4 – electronically, as stipulated in Appendix 4 of the Draft Transfer Pricing Communiqué, detailing the related-party transactions on an entity basis by providing information on intercompany agreements, previous and current tax inspections, reverse charge VAT, and witholding taxes paid on intercompany transactions. Form No:4 must be prepared by the end of the second month following the filing deadline for the corporate income tax return (by the end of June 2017 for taxpayers with calendar year fiscal accounting period).

Only those related-party transactions wiht values equal to or above the TL 30,000 threshold (approx. €9,000) must be declared in both the above-mentioned forms.

CbC report

The ultimate parent companies of multinational groups are required to file the first CbC reports for their first fiscal year beginning on or after January 1, 2016, and must file it no later than 12 months after the end of the relevant fiscal year. This means that, for MNEs with fiscal years ending on December 31, the first CbC report must be filed by December 31, 2017. For MNEs with special accounting periods, the first CbC report will be required to be filed in 2018, (12

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months after the close of the first fiscal year beginning after January 1, 2016). Accordingly, for corporate taxpayers with special accounting period ending on March 31, the first fiscal year subject to the CbC reporting requirement will be the special accounting period starting on April 1, 2016, and ending on March 31, 2017, and the CbC report will be required to be filed by March 2018.

The CbC reporting requirement applies to MNEs whose 2015 annual consolidated group revenues are TL 2,037,000,000 (approx. €633 million) or more for the first year of CbC reporting (2016). The revenue threshold for reporting periods starting from 2017 will be determined in local currency, the Turkish lira; however, it will always be equivalent to €750 million or more, as recommended in the OECD Action 13 Final Report.

If the ultimate parent company required to prepare the CbC report does not have an agreement in force with Turkey for the exchange of information related to CbC reporting, or has not introduced the obligation to file a CbC report, the reporting rules will apply to the Turkish subsidiaries of the ultimate parent company.

Consistent with the OECD guidance, Draft Transfer Pricing Communiqué No. 3 notes that the CbC report will include the global allocation by country of key variables for the MNE, including revenue, profit, tax paid, stated capital, accumulated earnings, number of employees, and tangible assets, as well as the main activities of each of its subsidiaries in a format presented in Appendix 5 of the communiqué.

All documentation must be prepared in the Turkish language.

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Portugal introduces country-by-country reporting requirement

Portugal's Budget Law for 2016, approved on March 16, introduced a country-by-country (CbC) reporting obligation for multinational enterprises (MNEs) that is intended to provide the Portuguese tax authorities with additional information on the MNE's activities for risk assessment purposes.

This new obligation, included as article 121.º-A of the Corporate Income Tax Code, applies to tax periods beginning on or after January 1, 2016, and is in line with the country-by-country reporting requirements set forth in the OECD's final report on Action 13 of the BEPS Action Plan.

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MNEs that meet certain criteria must report to the Portuguese tax authorities financial information and other relevant data for each country in which the group operates.

Submission of the report is mandatory and will be performed electronically. The report is due at the end of the 12th month after the term of the tax period to which the data refers to. For example, for tax periods ending on December 31, 2016, the CbC report is due on December 31, 2017.

Similar to the CbC rules introduced in other European countries, such as Spain and Italy, there are two types of entities to which this obligation may apply.

Parent companies of multinational groups

Portuguese resident entities must prepare the CbC report if:

- They are the parent companies ultimately required to prepare consolidated financial statements as defined in the accounting standards;
- Their consolidated turnover exceeds €750 million in the tax period prior to the one the CbC report refers to;
- They directly or indirectly hold or control one or more entities or permanent establishments located outside Portugal; and
- They are not held by one or more entities obligated to submit such report or by foreign companies that submit an equivalent report in a country with which Portugal has an agreement for the automatic exchange of information on this matter.

Subsidiaries of multinational groups

The CbC reporting obligation extends to Portuguese subsidiaries of multinational groups, provided that:

- They are directly or indirectly held or controlled by nonresident entities that are not obligated to file an equivalent declaration or, having such obligation, there is no agreement with the Portuguese tax authorities for the automatic exchange of information related to CbC reporting in force;
- The aforesaid entities, if they were resident in Portugal for tax purposes, would be obligated to file a CbC report; and
- No evidence is provided as to whether any other group entity, resident in Portugal or in a country with which Portugal has signed an agreement for the automatic exchange of information on this matter, has been designated to file such a report.

Despite the aforesaid criteria, any entity (either resident in Portugal or operating through a permanent establishment) that is part of a group that includes an entity obligated to file a CbC report is required to electronically submit to the Portuguese tax authorities the identification of reporting entity and correspondent tax residence. The deadline to file such obligation is the end of the tax period to which the financial information to be included in the CbC report refers to.

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Contents of CbC report

The official form of the CbC report has not been published. However, article 121.º-A of the Corporate Income Tax Code lists the type of data that should be included, which is globally in line with the OECD's final report on Action 13 of the BEPS Action Plan.

Thus, the CbC report should include aggregated data, by country or tax jurisdiction, of all entities that are part of the group (including permanent establishments), on the following items:

- Gross revenues segregated by related and third-party revenues;
- Earnings before corporate income tax and other taxes due on income of a similar or analogue nature to the corporate income tax;
- Corporate income tax and other income taxes of a similar nature due;
- Corporate income tax and other income taxes of a similar nature paid, including withholding taxes;
- Share capital and other equity items, at the end of the tax period;
- Accumulated earnings;
- Number of full time employees at the end of the tax period;
- Net book value of tangible assets (other than cash and cash equivalents);
- List of the entities resident in each country/tax jurisdiction, including permanent establishments, identifying the main business activities carried out by each;
- Other elements considered relevant and, if applicable, an explanation of the data included in the report.

Penalties

Taxpayers that fail to comply with the CbC reporting requirement will be subject to an administrative penalty ranging from €500 to €10,000.

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Romania introduces significant amendments to transfer pricing rules

Romania's National Agency for Fiscal Administration (ANAF) on February 2 published Order No. 442/2016 regarding the values of transactions, the deadline for the preparation, the content and conditions for the request of the transfer pricing file, and the procedure for the adjustment of transfer prices.

The order introduces significant amendments to the Romanian transfer pricing legislation. The main legislative amendment include the introduction of an annual obligation to prepare a transfer pricing file applicable to large taxpayers that engage in intragroup transactions exceeding certain thresholds. The deadline for the preparation of the file is the legal deadline for the submission of the annual corporate income tax return. These provisions apply to intragroup transactions carried out starting with the year 2016.

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Details regarding the most important changes are presented in the following sections.

Preparation and presentation of the transfer pricing file

The provisions regarding the annual obligation for the preparation of the transfer pricing file are applicable to large taxpayers that engage in intragroup transactions with a total annual value higher than the following thresholds:

- €200,000 for interest received/paid for financial services;
- €250,000 for services received/provided; and
- €350,000 for acquisitions/sales of tangible and intangible goods.

These thresholds are computed by adding up the annual total values of the transactions carried out with related parties, excluding VAT.

The deadline for the preparation of the transfer pricing file is the legal deadline for the submission of the annual corporate income tax return, for each fiscal year.

The deadline for the presentation of the transfer pricing file is a maximum of 10 days from the date of a request by the tax authorities, but not earlier than 10 days from the expiration of the preparation deadline.

The transfer pricing file will be presented at the specific request of the tax authorities, either during a fiscal inspection or outside that process.

The aforementioned requirements are applicable for intragroup transactions carried out during 2016.

Preparation of the transfer pricing file based on a specific request

The transfer pricing file will be prepared based on the tax authorities' specific request of either large taxpayers to which the criteria mentioned above are not applicable, or small and medium-sized taxpayers that engage in intragroup transactions with a total annual value higher than the following thresholds:

- €50,000 for interest received/paid for financial services;
- €50,000 for services received/provided; and
- €100,000 for acquisitions/sales of tangible and intangible goods.

These thresholds are computed by adding up the annual total values of the transactions carried out with related parties, excluding VAT.

The deadline for the presentation of the transfer pricing file is 30 to 60 days. The deadline may be extended only once for a maximum period of 30 days.

The transfer pricing file will be presented upon the tax authorities' specific request during a fiscal inspection.

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Documentation rules for other taxpayers

Taxpayers engaged in intragroup transactions for which the materiality thresholds are lower than those described above have the obligation to document their compliance with the arm's length principle during a fiscal inspection, according to general rules provided by the financial accounting and fiscal legislation in force.

Contents of the transfer pricing file

The order makes some amendments regarding the content of the transfer pricing file. In addition to the requirements of the legislation applicable prior to the issuance of this order, the transfer pricing file must include, among others, information regarding:

- The value of payments for each transaction performed with each related party;
- A description of the transfer pricing policy related to intragroup financing, including the presentation of financing agreements concluded with both related parties and independent lenders; and
- A description of intragroup services, including cost allocation keys, with an emphasis on services that significantly contribute to value creation.

Transfer pricing adjustment and estimation procedures

The tax authorities may adjust the transfer prices of transactions that are not carried out in accordance with the arm's length principle. The adjustment of transfer prices will be performed when the taxpayer fails to submit the transfer pricing file or when an incomplete transfer pricing file is submitted. The transfer prices will be adjusted using the median of the market range.

Applicability of the Order

The legislative provisions introduced by the order will apply to administrative procedures initiated after January 1, 2016.

The obligation to prepare a transfer pricing file by large taxpayers engaging in intragroup transactions that exceed the thresholds provided will apply to transactions carried out starting in 2016.

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