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OECD releases program to develop consensus solution to tax challenges arising from digital economy

The Organisation for Economic Co-operation and Development (OECD), now working as the expanded OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), released on May 31 a program of work1 that, if it reaches fruition and is implemented by member nations, would fundamentally alter the longstanding rules that govern the international taxation of all large multinational entities (MNEs), not just those that might consider themselves "digital companies."

[1] "Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy."

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URL: http://www.oecd.org/tax/beps/programme-of-work-to-develop-a-consensus-solution-to-the-tax-challenges-arising-from-the-digitalisation-of-the-economy.pdf

The program of work calls for "a solution to be delivered in 2020," a time frame the 129-member Inclusive Framework acknowledges is "extremely ambitious," and would require "the outlines of the architecture" to be agreed to by January 2020.

The program of work, like the policy note released on January 29, 2019, and the public consultation document released February 13, 2019, describes a two-pillar approach that could form the basis for consensus. Pillar 1 is focused on revising the rules for allocating income to market jurisdictions and moving beyond the arm's length standard, as well as the related nexus/permanent establishment (PE) rules that would broaden the circumstances in which an MNE's contacts with a country would grant that country income taxing rights. Pillar 2 focuses on establishing a global minimum tax along with a backstop regime that would deny deductions or impose withholding in cases of certain payments to low-tax jurisdictions. (For prior coverage of the policy note, see *Arm's Length Standard*, February 2019)
URL: http://www.oecd.org/tax/beps/policy-note-beps-inclusive-framework-addressing-tax-challenges-digitalisation.pdf
URL: http://www.oecd.org/tax/beps/public-consultation-document-addressing-the-tax-challenges-of-the-digitalisation-of-the-economy.pdf
URL: http://newsletters.usdbriefs.com/2019/Tax/ALS/190211_2.html

Pillar 1: Revised nexus and profit allocation rules

The public consultation document released in February articulated three proposals: a user participation proposal, a marketing intangibles proposal, and a significant economic presence proposal. Using different methods, each proposal allocated more taxing rights to the customer's and/or user's jurisdiction (the market jurisdiction). In addition, all three proposals contemplated the existence of a tax nexus without physical presence, contemplated using the total profits of a business (not just the profits of the group's entities in a jurisdiction), considered the use of simplifying conventions (including those that diverge from the arm's length principle), and would operate alongside the current profit allocation rules.

The program of work released on May 31 explains that it would explore options and issues relating to a modified residual profit split (MRPS) method, a fractional apportionment method, and distribution-based approaches. Specifically, detailed design considerations will look at the use of a residual profit split approach (either on a global or business line/regional basis) alongside existing transfer pricing rules, or the use of formulae or "fractional apportionment" by reference to metrics such as sales, employees, assets, or users. A newly proposed approach considers a base level of return for distribution activities in market countries. For each of these, the program highlights the significance of the technical work that needs to be completed. Key areas will include when a country has the right to tax trading profits and the rules for allocating trading profits to each country. A particular focus is on ensuring enough profit is awarded to the "market" jurisdiction, whether the country of users or sales. The program of work sets forth a goal of settling on one of these approaches by the end of 2019, and the members of the Inclusive Framework have committed to deliver a final report by 2020.

Modified residual profit split (MRPS) method: The MRPS method is similar to the marketing intangibles proposal set forth in the February consultation draft and is widely understood to be the US's counter to narrower proposals that were aimed solely at digital businesses. This MRPS approach would allocate to market jurisdictions a portion of an MNE group's non-routine profit that reflects the value created in those markets that is not recognized under the existing profit allocation rules.

The MRPS method involves four steps:

1. Determining total profit to be split;
2. Removing routine profit, using either current transfer pricing rules or simplified conventions;
3. Determining the portion of the non-routine profit that is within the scope of the new taxing right, using either current transfer pricing rules or simplified conventions; and
4. Allocating such in-scope non-routine profit to the relevant market jurisdictions, using an allocation key such as revenues.

The use of simplified approaches under this proposal would include consideration of possible proxies – such as capitalized expenditures, projections of future income, or fixed percentages of total non-routine income – to determine

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non-routine profit. Furthermore, the MRPS method would coexist with the existing transfer pricing rules for purposes of determining non-market related returns. The Inclusive Framework recognizes that rules for coordinating these two sets of rules would be necessary to provide certainty, minimize disputes, and ensure the avoidance of double taxation.

Fractional apportionment method: The fractional apportionment method would tax MNE groups without making any distinction between routine and non-routine profit. This method would involve three steps:

1. Determining the profit to be divided,
2. Selecting an allocation key, and
3. Applying this formula to allocate a fraction of the profit to the market jurisdiction(s).

Under this method, one possible approach would be to take into account the overall profitability of the relevant group or business line.

In exploring this method, the Inclusive Framework will examine a number of issues, including how to determine the starting point for computing the relevant profits. The options may include looking at the profit of the selling entity as determined by the current transfer pricing rules or by applying a global profit margin to local sales. Under this approach, the Inclusive Framework will also examine what allocation keys to use, including employees, assets, sales, and users.

Distribution-based approaches: In addition to the two methods described above, the Inclusive Framework will also explore other simplified methods. Such an approach might address, in addition to non-routine profit, profit arising from routine activities associated with marketing and distribution.

One possibility would be to specify a baseline profit in the market jurisdiction for marketing, distribution, and user-related activities. Other options might also be considered, such as increasing the baseline profit based on the MNE group's overall profitability. Through this mechanism, some of the MNE group's non-routine profit would be reallocated to market jurisdictions.

In scenarios involving a remote activity, the Inclusive Framework will explore the question whether the amount of profit (including any baseline profit) taxable by that market jurisdiction would be the same as for locally based marketing and distribution activities, or whether that amount should be reduced in some formulaic manner.

In connection with distribution-based approaches, the program of work states that further consideration would need to be given to issues such as whether such an approach would result in a "final allocation" – one that neither taxpayers nor tax authorities would be able to reevaluate under current transfer pricing rules – and whether the baseline profitability would function as a minimum or a maximum profit in the relevant jurisdiction.

Other technical issues: In exploring these three methods, the Inclusive Framework will also examine other technical issues, such as:

- The possibility of determining the profits subject to the new taxing right on a business line and/or regional basis.
- Scope limitations that apply either by reference to the nature of a given business (*e.g.*, through safe harbors) or its size (*e.g.*, thresholds based on revenue or other relevant factors). Although not specifically stated in the program of work, the reference to scope limitations has the potential for certain industries (*e.g.*, financial services, extractive industries in developing countries), and smaller MNEs to seek exemption from the Pillar 1 approach.
- Application of the new allocation rules to both profits and losses.

New nexus rules: As part of this process, the Inclusive Framework will explore ways to revise the nexus rules to render the new profit allocation rules applicable in a far broader context than the current nexus/PE rules. The new rules will likely involve having a remote taxable presence even without a traditional physical presence and a new set of standards for identifying when a remote taxable presence exists.

The approaches considered to implement new nexus rules include the following:

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- Amendments to the definition of a PE in Article 5 (Permanent Establishment) of the OECD Model Convention, along with potential changes to Article 7 (Business Profits) of the convention.
- Potential changes to Article 9 (Associated Enterprises) of the convention to allow market jurisdictions to exercise taxing rights over the measures of profits allocated to them under the new nexus and profit allocation rules.

Pillar 2: Income inclusion rule and tax on base-eroding payments

Under Pillar 2, the members of the Inclusive Framework have agreed to explore an approach that considers the right of other jurisdictions to apply rules in cases where income is taxed at an effective rate below a minimum rate. The program of work makes no reference to what the minimum rate might be, but suggests that a single, agreed-upon rate would be preferable to either a rate set as a percentage of the rate in the MNE parent's residence country or a band of rates that countries could choose from. As discussed below, the program of work explores an inclusion rule, a switch-over rule, an undertaxed payment rule, and a subject-to-tax rule. These rules are discussed under the global anti-base erosion (GLoBE) proposal and through taxes on base-eroding payments.

Global anti-base erosion (GLoBE) proposal: The GloBE proposal seeks to address the remaining BEPS challenges through the development of two interrelated rules:

- An income inclusion rule that would tax the income of a foreign branch or a controlled entity if that income was subject to tax in the recipient's jurisdiction at an effective rate below a minimum rate; and
- A tax on certain base-eroding payments not subject to tax at or above a minimum rate in the recipient's jurisdiction, which would operate by way of a denial of a deduction or imposition of source-based taxation (including withholding tax), together with any necessary changes to double tax treaties.

These rules would be implemented by way of changes to domestic law and double tax treaties. They would also incorporate a coordination or ordering rule to avoid the risk of economic double taxation.

The income inclusion rule would operate as a minimum tax by requiring a shareholder in a corporation to bring into account a proportionate share of the income of that corporation if that income was not subject to an effective tax rate above a minimum rate. Income taxed below the minimum rate but in connection with a harmful tax regime would nonetheless be taxed in the parent country at full rates. This rule could supplement a jurisdiction's controlled foreign corporation (CFC) rules. The Inclusive Framework would explore, among other options, an inclusion rule that would impose a minimum tax rate and an approach using a fixed percentage of the parent jurisdiction's corporate income tax (CIT) rate or corridor of CIT rates. Various carve-outs might be provided, such as a return on tangible assets.

There is a need to ensure that the income inclusion rule applies to foreign branches as well as foreign subsidiaries. For example, in the case of profits attributable to exempt foreign branches, or that are derived from exempt foreign immovable property, the income inclusion rule could be achieved through a switch-over rule that would turn off the benefit of an exemption for income of a branch in exchange for a foreign tax credit regime.

Tax on base-eroding payments: The second key element of the proposal is a tax on base-eroding payments that complements the income inclusion rule. This element of the proposal would explore:

- An undertaxed payments rule, which would deny a deduction or impose source-based taxation (including withholding tax) for a payment to a related party if that payment was not subject to tax at a minimum rate.
- A subject-to-tax rule in tax treaties, which would grant certain treaty benefits only if the item of income was subject to tax at a minimum rate.

The subject-to-tax rule could complement the undertaxed payment rule by subjecting a payment to withholding or other taxes at their source and denying treaty benefits on certain items of income when the payment is not subject to tax at a minimum rate. This rule contemplates possible modifications to the scope or operations of various treaty benefits, with priority given to interest and royalties.

Other topics covered

The program of work covers a variety of other important topics, including administrative issues and the elimination of double taxation in connection with Pillar 1. It also includes a separate chapter on the need to analyze the proposals'

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"interlinkages with a particular focus on the importance of assessing the revenue, economic and behavioral implications of the proposals in order to inform the Inclusive Framework in its decision making."

Elimination of double taxation: The program of work observes that the work under Pillar 1, depending on the design options ultimately agreed to, "envisage[s] reallocating taxing rights over a proportion of an MNE's *group's* profit (however defined), rather than over the profit from *specific transactions or activities undertaken by specific entities*. It may therefore not be immediately clear which member(s) of an MNE group should be considered to derive the relevant income. This leads to questions about how, in practice, source jurisdictions would exercise the reallocated taking rights, and how residence jurisdictions would provide relief from double taxation of the relevant income." (Emphasis added)

The program of work will consider these questions, including the effectiveness of the existing treaty and domestic law provisions and the need to develop new or enhanced provisions. It notes that consideration would also be given to a multilateral competent authority mutual agreement procedure or similar frameworks that would provide additional guidance. The program of work explains that the current dispute prevention and resolution procedures will be examined in the context of the new nexus and profit allocation rules, and when necessary the Inclusive Framework will make recommendations for changes or enhancements, including arbitration procedures, multilateral competent authority agreements, etc.

Notably, there is no more detail on how double taxation would be eliminated or how such a goal would be measured, nor is there any reference to mandatory binding arbitration as part of a minimum standard to which countries enjoying the benefits of a new approach would be required to adhere.

Administration: With respect to administering the provisions of Pillar 1, the program of work notes the need to identify the taxpayer that bears tax liability in a jurisdiction, and its filing obligations, particularly in cases in which the liability is assigned to an entity that is not a resident of the taxing jurisdiction. It indicates that one option could be to design "simplified registration-based collection mechanisms," along with enhanced exchange of information mechanisms, but considers that "a withholding tax mechanism will also be explored…where it does not lead to double taxation."

The program of work acknowledges that the application of any of the Pillar 1 approaches would likely require a number of data points to be available to tax administrations as well as the MNE group, which "would likely result in the need for new data, documentation and reporting obligations" such that "[t]he work program will develop recommendations for a system to report and disseminate information needed to administer the new taxing right."

Economic analysis and impact assessment: The program of work acknowledges the need to perform "an in-depth consideration of how [the proposals] would be expected to affect the incentives faced by taxpayers and governments, their impact on the levels and distribution of tax revenues and their overall economic effects, including their effects on investment, innovation and growth. The impact assessment will also need to consider how these effects vary across different kinds of MNEs, sectors and economies" and acknowledges that new empirical research will need to be undertaken. The economic analysis is expected to be carried out throughout the entire period of the program of work, with a goal of delivering additional information to members of the Inclusive Framework by the end of 2019, so that they can agree upon an overall "outline of the architecture" by January 2020.

Next steps

The program of work will be presented for approval by G20 finance ministers during their meeting on June 8-9, 2019 in Fukuoka, Japan. OECD Working Parties will meet throughout the remainder of 2019 to consider the relevant technical issues and a report on the progress of work is expected in December 2019. Consideration will be given to holding further public consultations to gather business feedback as the various proposals are refined.

A recommendation for a unified approach on nexus and profit allocation and the key design elements of the global minimum tax will be submitted to the BEPS Inclusive Framework for agreement at the beginning of 2020. Work will continue to reach agreement on the policy and technical details, with a final report due by the end of 2020.

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Observations

The program of work acknowledges that the timeline to a final report by the end of 2020 is "extremely ambitious." As should be clear from the above description of the work, it involves myriad challenging technical and political issues.

Consider, for example, the program of work's suggestion with respect to Pillar 1 that increasing taxing right to markets would need to be matched by reductions in taxing rights in other jurisdictions to avoid double taxation – all potentially done at the global MNE level, as opposed to the legal entity level.

Consider, too, the suggestion that in order to take into account losses as well as profits under Pillar 1 it may be necessary to have an MNE group develop a "notional cumulative loss account," which, if done on a product line and/or regional basis, would raise a host of difficult issues, including the impact of mergers, acquisitions, dispositions, expense allocation, discontinuation of product lines, etc.

Political issues relate largely to consideration of which countries will be impacted favorably or unfavorably in a global reallocation of taxing rights under Pillar 1. For example, countries that incentivize research and development through their tax laws may not be eager or willing to give up taxing rights when that R&D produces income for the entities in their jurisdictions under current rules.

As another example, developing countries – now an important bloc within the Inclusive Framework – with relatively small markets but large exporting extractive sectors may be unfavorably impacted as a result of such fundamental changes. Notwithstanding these challenges, leaders of the effort at the OECD and in the US Treasury express guarded optimism that these challenges can be met in light of what is widely perceived as the unacceptable alternative of growing uncertainty.

While the document contains ample references to simplicity, administrability, dispute resolution, and avoidance of double taxation, there is little detail on how these objectives might be met. The program of work explains that one of the drivers behind these efforts is the desire to avoid a "proliferation of uncoordinated and unilateral actions" by countries that would result from the failure to reach a global consensus on a new approach. In the event a consensus-based approach cannot be reached by the end of 2020, or if implementation requires additional time, companies may continue to face such uncoordinated, unilateral approaches and may wish to take this into account in their planning. Indeed, the program of work makes no reference to countries' willingness to repeal any such actions already taken, such as so-called digital service taxes, if this effort achieves its goals.

The program of work explains that consideration will be given to the holding of public consultations as necessary to obtain stakeholder feedback as the various proposals are refined, and companies may want to consider how to continue to engage with the process as it unfolds.

The work program is ambitious in scope and timing and has the potential to upend long-standing principles of MNE taxation. Thus, close monitoring of developments is critical, as will be modeling of the potential changes as a final framework begins to come into focus.

— Bob Stack (Washington, DC)
Managing Director
Deloitte Tax LLP
bstack@deloitte.com

Keith Reams (Washington, DC)
Principal
Deloitte Tax LLP
kreams@deloitte.com

David Lenter (Washigton DC)
Managing Director
Deloitte Tax LLP
dlenter@deloitte.com

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UN Committee of Experts issues draft chapter on financial transactions to update transfer pricing manual

The United Nations Committee of Experts on International Cooperation in Tax Matters on April 8 released an update on the progress made by its transfer pricing subcommittee regarding the latest edition of the *United Nations Practical Manual on Transfer Pricing for Developing Countries*.

With the next edition of the manual due to be issued by 2021, the subcommittee is in the process of incorporating new content regarding financial transactions (Chapter B). A draft chapter has now been presented to the committee for the first round of discussions and guidance. This draft chapter is tailored to non-financial multinational enterprises (MNEs) that engage in intercompany financial transactions (the guidance does not apply to banks or other financial institutions).

The committee began work on the manual in 2009, when it established the subcommittee, which includes participants from tax administrations, academia, international organizations, and the private sector. The first edition of the manual was issued in 2013, with the second edition finalized in 2017. The 2017 update improved the manual's accessibility and relevance and included, in response to developing country feedback, new chapters on intragroup services, cost contribution arrangements, and the treatment of intangibles.

The next version of the manual is expected to make further improvements in usability and practical relevance and will include updates and improvements to the existing text as well as new content, such as the chapter on financial transactions. The subcommittee will hold a meeting on July 2-4, 2019, to further build on the draft chapter, including addressing any new issues raised by the committee.

Chapter B – financial transactions

The subcommittee's proposed new Chapter B is segmented into the subsections indicated below. While the draft chapter also discusses cash pooling and captive insurance structures, it does not provide details on the delineation of such transactions or the evaluation of the arm's length results.

Source of capital: The draft chapter provides an overview of an MNE's alternative sources of capital (*i.e.*, internal cash, debt, and equity), and notes that the source of funding may have significant consequences from a tax perspective. While transfer pricing rules do not provide any guidance concerning the optimal capital structure in a specific situation, the capital structure selected by the associated enterprises may strongly affect the enterprise's financial transactions. Specifically, the draft chapter suggests that it may be appropriate to perform a debt capacity analysis to determine whether, from an economic and financial perspective, an associated enterprise would have been able to obtain comparable funding from unrelated parties, based on similar terms and conditions.

One measure of assessing borrowing capacity is to look at the debtor's credit rating, which reflects the credit risk that a creditor would incur in loaning funds to a specific debtor. The non-consensus discussion draft on the transfer pricing aspects of financial transactions, issued by the Organisation for Economic Co-Operation and Development (OECD) in July 2018 incudes similar guidance concerning potential approaches to evaluating the capital structure of an associated enterprise.

Specific issues regarding the debt capacity of an associated enterprise are not discussed in the draft chapter, as a recommendation is made that such issues be reviewed by the committee.

Potential base erosion: The draft chapter indicates that, to the extent a country's tax system permits income tax deductions for interest payments, companies may have an economic incentive to select debt financing over other alternatives. The draft chapter concludes that base erosion by means of excessive interest deductions is a relevant issue.

Several developed countries have introduced measures (such as thin capitalization rules) aimed at reducing the advantages of debt financing. For an in-depth discussion on the specific measures available to counter excessive interest deductions claimed by residents, the draft chapter refers to the *UN Practical Portfolio on Protecting the Tax Base of Developing Countries against Base-eroding Payments: Interest and Other Financing Expenses*. The referenced

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portfolio is aligned with the OECD's 2015 report on Action Item 4 of the base erosion and profit shifting (BEPS) action plan, *Limiting Base Erosion Involving Interest Deductions and Other Financial Payments*.
URL: http://www.oecd.org/tax/limiting-base-erosion-involving-interest-deductions-and-other-financial-payments-action-4-2015-final-report-9789264241176-en.htm

The draft chapter observes that development and implementation of base erosion rules require careful consideration of the possible tax policy consequences.

Alternative financial instruments: Subject to its capital requirements, an MNE may consider several different financial instruments, such as:

- Debt instruments (*e.g.*, money market instruments, bonds, loans);
- Equity instruments (*e.g.*, common stock); and
- Financial derivatives (*e.g.*, options, futures, forwards).

From a transfer pricing perspective, common financial transactions include cash pooling, loans, financial guarantees, hybrid financing, and derivatives. The draft chapter is limited to the analysis of intercompany loans and financial guarantees, because they are the most commonly seen financial transactions, as a practical matter. However, some of the guidance concerning these transactions might also be relevant for other financial transactions. The OECD discussion draft, in contrast, provides specific guidance on cash pooling and captive insurance structures.

Treasury functions: The specific functions performed by an MNE's treasury department will depend on the degree of centralization and complexity of its operations. Per the draft chapter, an MNE's treasury department generally operates according to one of the following paradigms (or a combination thereof):

- Cost center: Operates as a service provider, assisting associated enterprises by performing routine services (*i.e.*, ensuring efficient use of cash and reducing financial volatility);
- Value-added center: Operates as a cost-savings center, focusing on consolidation of transactions and achieving net savings; or
- Profit center: Operates as a profit center, deliberately taking market positions and actively managing operational exposures.

The OECD discussion draft similarly acknowledges that the arm's length compensation due to the treasury function will differ, depending on how much autonomy the function has and the specific activities that it performs. In contrast to the draft chapter, the OECD discussion draft states that when the accurate delineation of the transaction indicates that the funding entity lacks the capability, or fails to perform the decision-making functions associated with controlling the risk of investing in a particular financial asset, the funding entity will be entitled to no more than a risk-free return as an arm's length return for the funding activity undertaken.

Creditworthiness analysis: The draft chapter states that, in order to accurately delineate the financial transaction and to identify uncontrolled transactions to evaluate the arm's length result from the transaction, the borrower's creditworthiness must be considered. This process, which relies on both quantitative and qualitative factors, should also consider the following:

- Financial transaction adjustment: While in most situations creditworthiness is evaluated as of the time the financial transaction is entered into, the draft texts state that it may also be useful to compare historical versus forecasted results, for purposes of evaluating creditworthiness.
- Passive association: Per the draft chapter, the decision whether to evaluate an associated enterprise's creditworthiness on a stand-alone basis or to consider its status within the MNE group (also known as "implicit support") is highly dependent on the entity's level of strategic importance within the MNE group. Reference is made to guidance issued by Standard & Poor's (S&P) *Group Rating Methodology*, published on November 19, 2013. While it does not specifically cite the S&P report, the OECD discussion draft reaches a similar conclusion, suggesting that a facts-and-circumstances approach is appropriate, which takes into account the entity's relative importance to the group.

The evaluation of creditworthiness may also need to consider market risk if the associated enterprise operates in a particularly risky country (*i.e.*, the risk deriving from a country's political or business environment).

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The draft chapter acknowledges that the evaluation of creditworthiness of an associated enterprise can present an analytical challenge. Relying on the MNE group's credit rating may be appropriate, absent evidence that using that rating would produce inaccurate results. When appropriate, this approach may increase certainty and reduce administrative burdens on taxpayers and tax authorities.

Once the creditworthiness of the associated enterprise is determined, the draft chapter suggests that adjustments may be necessary to take into account issue-specific risks associated with the financial transactions (*e.g.*, security, structural and contractual subordination). Apart from credit risk, the most common risks relevant in an intercompany loan include:

- Interest rate risk
- Reinvestment risk
- Call/prepayment risk
- Inflation (or purchasing power) risk
- Liquidity risk
- Foreign exchange risk
- Volatility risk
- Political/legal risk
- Event risk
- Sector risk
- Country risk

Pricing financial transactions – Loans: The draft chapter states that the first step in determining an arm's length interest rate is to analyze the economically relevant characteristics (or comparability factors) of the loan, such as:

- Contractual terms
- Functional analysis
- Characteristics of financial products or services
- Economic circumstances
- Business strategies

Once the financial transaction has been accurately delineated, the next step of the analysis is to select and apply the most appropriate transfer pricing method:

- The comparable uncontrolled price (CUP) method;
- The profit split method (the draft texts acknowledge that this method is not likely to apply to intercompany loans); or
- Safe harbor rules, if applicable in the specific jurisdiction.

The OECD discussion draft also identified transfer pricing approaches to determine arm's length interest rates, including the CUP method, a cost of funds approach, and reliance on bank opinions. The OECD draft goes on to state that bank opinions generally would not be regarded as evidence of arm's length pricing, because they may not pertain to an actual loan transaction between independent enterprises.

Pricing financial transactions – Financial Guarantees: As it did with loan transactions, the draft chapter states that the pricing of financial guarantees should take into account all economically relevant characteristics (or comparability factors) associated with the transaction. Per the draft chapter, an intercompany financial guarantee has commercial value if:

- The associated enterprise's obligations are transferred to the guarantor;
- An independent party would be willing to pay for a similar guarantee; or
- The guarantee allows the associated enterprise to obtain a lower interest rate for a loan than would be possible absent the guarantee.

Conversely, the draft chapter suggests that an intercompany financial guarantee will not have commercial value if:

- The associated enterprise is perceived as having improved creditworthiness solely on account of its group affiliation (*i.e.*, passive association);

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- The associated enterprise has no or extremely limited debt capacity or creditworthiness and therefore would not be able to access the capital markets, absent the financial guarantee; or
- The creditor requested the financial guarantee only to prevent the parent company from diverting funds from the financed company, *i.e.*, moral hazard issues.

Once the terms of the financial guarantee transaction have been accurately delineated, the next step of the analysis involves selecting and applying the most appropriate transfer pricing method:

- The CUP method;
- Other method (yield approach): Estimates the maximum potential interest rate savings achieved by the associated enterprise because of the explicit guarantee. This approach – alternatively referred to as the "interest savings" approach – is accepted by several tax authorities; or
- Other method (cost approach): Considers the value of the expected loss that the guarantor would incur by providing the guarantee. The calculation can be achieved by relying on several alternatives (*i.e.*, credit default swap, contingent put option, cost of capital, financial guarantee insurance).

The OECD discussion draft described broadly similar approaches to evaluate the arm's length charge for financial guarantees, including the CUP method (although similar guarantees between unrelated parties may be difficult to find), the yield approach, the cost approach, and the capital support method.

Other considerations: The draft chapter states that, while the primary compensation for an intercompany loan generally consists of the interest payment, other elements might be present that are compensated separately. For example, treasury services rendered on behalf of an associated enterprise will require arm's length remuneration. To determine the arm's length remuneration for services rendered, it is necessary to perform an accurate delineation of the actual transaction (including a functional analysis). Per the draft chapter, treasury entities operating as service centers are typically remunerated by applying the CUP method, the cost-plus method, or the transactional net margin method (TNMM). Treasury entities operating as profit centers are typically remunerated based on a percentage of the financial transaction.

Conclusion & key takeaways

The draft chapter provides relatively high-level preliminary guidance on the transfer pricing analysis of common types of financial transactions, including treasury functions, intercompany loans, and financial guarantees.

The draft chapter provides guidance on methods for determining the arm's length compensation for financial transactions. It also indicates that it is necessary to perform an accurate delineation of the financial transaction to determine whether the transaction was characterized correctly or should be recharacterized for tax purposes. Similar to the OECD discussion draft, the draft chapter summarized herein indicates it is necessary to perform an examination of the contractual terms of the transaction, the functions performed, the characteristics of the financial products or services, the economic circumstances of the parties and the market, and the business strategies pursued by the parties.

—

Jack Kontopoulos (New York)
Manager
Deloitte Tax LLP
jakontopoulos@deloitte.com

Boris Nemirov (New York)
Principal
Deloitte Tax LLP
bnemirov@deloitte.com

Robert Plunkett (New York)
Principal
Deloitte Tax LLP
rplunkett@deloitte.com

Ariel Krinshpun (New York)
Principal
Deloitte Tax LLP
akrinshpun@deloitte.com

Bill Yohana (New York)
Managing Director
Deloitte Tax LLP
byohana@deloitte.com

Jon Gemus (New York)
Senior Manager
Deloitte Tax LLP
jgemus@deloitte.com

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India's issues proposals on attribution of profits to PEs for public consultation

India's Central Board of Direct Taxes (CBDT) on April 18 issued a draft report on the attribution of profits to permanent establishments (PEs) of nonresident enterprises in India. The report proposed changes to India's rules in this area and invited public comments to be submitted electronically by May 18.

The report's theme seems to revolve around the ideology reflected in this passage cited in the report:

> *"The oranges upon the trees in California are not acquired wealth until they are picked, and not even at that stage until they are packed, and not even at that stage until they are transported to the place where demand exists and until they are put where the consumer can use them."* – League of Nations Document E.F.S.73.F.19 Economic and Fiscal Commission, Report on Double Taxation, 1923.

Background

When a jurisdiction taxes profits to the extent of its contribution, while avoiding double taxation, the "virtuous" cycle of taxation can operate in the globalized economy. The rules for the attribution of profit are a fundamental feature of the international tax system. Over time, there have been significant developments and controversies around the attribution of profits to PEs, and more fundamentally, the transfer pricing (TP) aspects of that attribution.

TP and profit attribution are intricately linked with the issue of taxing the profits of foreign enterprises. Profit is a function of the quantum of sales, price, and cost of goods. Cost works on the supply side, while price and quantum of sales depend on the interaction of demand and supply. Hence, both the demand and supply sides play an important role in generating an enterprise's profits.

Until 2010, the OECD and UN model tax treaties treated profit attribution under Article 7 (business profits) and allowed sales to be taken into account, both in the direct accounting method as well as in the indirect apportionment method. However, the revised Article 7 in the 2010 update of the OECD model tax treaty (which was based on the OECD's 2008 report on the attribution of profits) approximated profit attribution with transfer pricing and omitted the option of apportionment, thereby ostensibly undermining sales and contributions made by market jurisdictions toward the profits of an enterprise. Article 7 was modified to the extent of taking away the formulary apportionment option and inserting the condition that profits should be attributed using a functions, assets, and risks (FAR) analysis considering the arm's length principles under transfer pricing regulations.

Before 2010, Article 7 had remained largely unchanged since the introduction of the OECD model tax treaty in 1963, and a large number of treaties retain the earlier version of this article in the OECD or UN model tax treaty versions, both of which allow formulary apportionment, and do not impose a FAR-based approach. Hence, generally, three standard versions of Article 7 exist today – the pre-2010 and the 2010 versions of Article 7 in the OECD model tax treaty and the Article 7 version of the UN model tax treaty.

The UN model treaty provides relatively greater taxation rights to the source country in the form of force of attraction rules and restrictions on deduction of certain expenses. Apart from these differences, this article in the two model treaties was somewhat similar until the OECD 2008 report, and sought to tax only those profits of the PE that it would be expected to make if it were considered an independent and separate entity. This would normally be achieved by maintaining separate accounts for the permanent establishment (separate accounting or direct method). However, in the absence of separate accounts, both conventions provided in paragraph 4 for attribution of profits by way of apportionment as may be customary in the pertinent state (fractional apportionment or indirect method).
URL: http://www.oecd.org/tax/transfer-pricing/41031455.pdf

India has strongly dissented from the FAR-based approach, considering the lack of economic justification and the potential adverse consequences to India, a net importer of capital and technology, with a large talent pool and a high consumption capacity. Given its strong disapproval, this approach was neither accepted in Indian tax treaties nor adopted in its domestic law.

Indian tax treaties, domestic law (Rule 10 of the Indian Income Tax Rules), and several court decisions (such as *eFunds Corporation v ADIT* [(2010) 42 SOT 165 (Del)] and *Convergys Customer Management Group Inc v ADIT*

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[2013-TII-88-ITAT-DEL-INTL]) have affirmed and upheld the apportionment method as permissible. However, an objective method was not prescribed in the existing scheme. Therefore, wide discretion was accorded to the assessing officers and thereby different methodologies seem to have been adopted in different cases, leading to litigation due to uncertainty.

Recognizing the significance of issues regarding the attribution of profits to a PE, as well as the need to bring greater clarity and predictability in the applicable tax regime, the CBDT recently issued its report on the attribution of profits to PEs, inviting stakeholders to comment.

The proposal

The report is an exhaustive draft that provides insights into the economic basis for the allocation of taxing rights in respect of business profits by looking at how economies contribute to business profits of multinational enterprises. It also documents various international practices for profit attribution.

The report recommends the use of the fractional apportionment method for profit attribution, which is a method permissible under paragraph 4 of Article 7 of tax treaties and Rule 10 of the India Income Tax Rules. The fractional apportionment method differs from formulary apportionment (which is followed by the US states and has been proposed by the EU) in that it does not necessitate consolidation of profits of the enterprise from different tax jurisdictions, and can be determined by considering only those profits that have been derived by the enterprise in India, and thereafter apportioning them on the basis of certain factors.

In essence, the formulary apportionment method allocates profits from intra-firm transactions on the basis of a formula that reflects contributions made by each sub-unit (group member) to the overall profit of the corporation (MNE group).

The report suggests a "three-factor" method to attribute profits, as discussed below.

Three-factor approach

The report proposes a formula-driven methodology for profit attribution in India that gives weight to three factors:

- Sales;
- Manpower (employees and wages); and
- Assets.

In a way, this three-factor approach takes into account both demand and supply-side factors that contribute to the profits of the enterprise. The possible reasons for including these three factors in the formula may be:

- The sales factor could capture high consumption in India;
- The manpower factor (*i.e.*, the product of the number of employees and their wages) could capture the large, cost-effective talent pool available in India; and
- The asset factor could balance the formula, as most Indian operations follow contractual business models that have a weak assets base.

The report suggests assigning equal weight to all the factors and highlights that international practices (as embodied by the European Union's common consolidated corporate tax base proposal) and tax literature support the assignment of equal weight to each of the factors.

The committee recommended adopting the following formula to determine the profits derived from India:

> *Profits attributable to operations in India = Profits derived from India x [India Sales/3xGlobal sales+ (Indian employees/6xGlobal employees) + (Indian wages/6xGlobal wages) + (Indian assets/3xGlobal assets)]*

Further, the report suggested the inclusion of a fourth factor (users) in the formula in the case of digital businesses, in light of the "significant economic presence" concept legislated by India for digital businesses.

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Separately, the committee endorsed assigning a relatively lower weight of 10 percent to users in low and medium user intensity models, and 20 percent in high user intensity models at this stage, with the corresponding reduction in the weight of employees and assets, except that sales are assigned 30 percent weight in apportionment in both fact patterns.

Calculating profits derived from Indian operations

In the absence of separate accounts of Indian operations for calculating profits derived therefrom, the report recommended determining such profit by applying the global profit margin on the revenue generated from customers in India.

Profits derived from India = Revenue derived from India x global operational profit margin

The global operational profit margin is the earnings before interest, taxes, depreciation and amortization (EBITDA) margin.

Further, a floor rate of 2 percent of the gross revenue or turnover derived from India operations is deemed as “profits derived from India,” in cases in which an enterprise has global losses or a global operational profit margin of less than 2 percent and has operations in India.

Step-by-step mechanism to implement proposed model

The committee’s recommendation would be implemented by following these steps:

1. Determining the profits derived from the Indian operations of the enterprise;
2. Apportioning the profits from Indian operations of the enterprise on the basis of the three/four factors mentioned above, depending on the business model; and
3. Deducting profits from Indian operations of the enterprise that may have already been taxed in India.

Illustration on how profit attribution would work under the proposed approach

Particulars	**Sales**	**Employees**	**Wages**	**Assets**
Indian	1,000,000	300	50,000	40,000
Global	10,000,000	1,000	400,000	2,000,000
Proportion	10%	30%	13%	2%
Weight as per the proposed approach	1/3	1/6	1/6	1/3
Total percentage attribution under the proposed three-factor approach				**11%**
Total percentage attribution as per judicial precedents				**26% to 50%**

Comments

An analysis of pertinent case laws indicates that the courts have upheld the application of the apportionment method, which is permissible under Indian tax treaties and Indian rules. However, the courts have not insisted on a universal and consistent approach for the apportionment of profits.

In most court decisions, ad hoc percentages ranging from 26 percent to 50 percent of the profits derived from Indian sales are attributed to activities undertaken by the enterprise through a PE in India. If profits were to be attributed using the proposed three-factor approach, the enterprises that have a lower proportion of these factors would as a result be attributed lower profits than under the courts’ decisions.

Therefore, from an Indian perspective, the enterprises in India that contribute heavily through their supply side (manpower and assets) and demand side (sales) activities in India would likely see a higher share of their profits attributed to their operations in India, and consequently would pay higher taxes.

In the case of digital enterprises that undertake activities through a digital platform, the attribution of profits using the method recommended by the committee would almost always result in a higher attribution of profits to the Indian

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entity than in the case of non-digital companies because of the addition of the fourth factor in profit attribution (10 percent or 20 percent of weight based on user intensity – these ratios are constant).

While the committee deliberated on the significance of digitalization and the role of users in value creation and profit of an enterprise, the report does not define the term "users" and the threshold of users for including them in the formula. Rather, it discusses only the various kinds of users (active and passive, depending on the level of participation) and assigns two weights depending on the level of intensity.

Disengaging from the FAR-based apportionment and yet hanging on to it

The report explores the option of attributing profits on the basis of supply-side factors by resorting to FAR, along with demand-side factors represented by sales. This has application in the case of a PE that comes into existence through the presence of an Indian subsidiary, which is separately taxed in India on its own income. An example of this situation would be a dependent agent PE or a service PE that comes into existence on the basis of stewardship provided by the employees of the foreign enterprise while on secondment to the Indian entity. When such a PE maintains separate accounts from which taxable profits can be determined, that would suffice. However, when the PE does not maintain separate accounts, the report recommends the following approach:

- To the extent that the Indian subsidiary is remunerated for its contributions on an arm's length basis, the profits of that Indian subsidiary may be considered to represent the profits derived from the contribution of supply-side factors in India.
- To the extent that those profits are already taxed in India (in the hands of the Indian subsidiary) they need not be included again in the PE's profits. Thus, in such a case, where the activities of an Indian subsidiary contributing to the business of the foreign enterprise lead to the creation of a PE in India, the profits need to be attributed to the PE only in respect of demand-side factors, or sales, because the supply-side factors have already been taken into account in the taxable income of the Indian entity.
- To the extent there are no sales in India (or if Indian sales are less than INR 1 million ($14,000)), and only the supply-side activities are carried out by the Indian subsidiary, which has been remunerated for such activities on an arm's length basis, using a FAR analysis, no additional profits may be subject to tax. Although this concept has been upheld by the Indian courts, this explicit recommendation should come as a welcome relief to development centers that are Indian branches of overseas entities and hence PEs in their own right.

Observations

Upon cursory review, the report's suggested approach appears to factor in both demand- and supply-side factors by assigning weights to the factors that contribute to the business profits of the enterprise, and thereby gives rise to a valid justification of taxation of the profits to which their economies have contributed. The profits derived by the enterprise from its operations in India are defined objectively using a simple formula. Accordingly, the subjectivity of the existing scheme and the resulting litigation are intended to be mitigated once the recommendations find their way into legislation. At its core, the committee has only sought to improve on the existing Rule 10, rather than exorcising a rule that has outlived its utility.

However, the following points merit consideration in adoption of the suggested approach:

1. Most treaties mandate the attribution of income to a PE on the basis that the PE is a "single, distinct and separate" enterprise (Article 7(2)). However, the treaty further states that nothing in paragraph 7(2) will preclude attribution to a PE based on a country's customary approach (Article 7(4)) and the result of such apportionment is in conformity with the principle of Article 7. In India, whether this customary approach is the apportionment-based Rule 10 or whether it is the arm's length principle (after the introduction of transfer pricing provisions in the Income Tax Act in 2001 (along with CBDT Circular No. 14 of 2001 and Circular No. 5 of 2004) is a matter of debate that requires careful consideration.
2. The fractional apportionment method will not produce an allocation of profits that would be the same as that under separate accounting and arm's length pricing. Such a method tends to disregard market conditions as well as particular circumstances of the individual enterprises, and ignores management's own allocation of resources, thus producing an allocation of profits that may bear no sound correlation to economic facts. Inherently, it runs the risk of allocating profits to an entity that in reality is making losses based on what third parties would realistically do in similar circumstances.

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3. The enterprise's global operational profit margin may not always be commensurate with the functions and risks attributable to the PE and would therefore lead to an imbalanced attribution of profits.
4. The report does not provide any reasoning or impact analysis for assigning equal weight to all the factors.
5. Given that manpower is one of the factors in the proposed apportionment formula, the scope of the definition reasonably would extend to include contract workforce as well, but the report does not address this issue.
6. The report's approach completely ignores intangible property, which is often the crown jewel of some enterprises, especially in the technology and pharmaceutical sectors. Accordingly, intangible property will not have any impact on profit attribution. This might be because fair value for self-generated intangibles is not being recognized. Because ownership of intangible property is not a significant factor in India, such an exclusion may be seen as deliberate.
7. The proposed formula cannot adequately address the movement of exchange rates.
8. The multiplicity of taxes in the digital context, particularly owing to withholding on royalty payments, the equalization levy and significant economic presence (SEP) can lead to multiple taxation with no credits available because the bases are different under each levy (gross in case of withholding tax and the equalization levy, net in the case of SEP).
9. The transition to the suggested approach would present enormous political and administrative complexity and require a level of international consensus that is unrealistic in the field of international taxation. Further, apportionment does not provide a complete solution to the allocation of profits of an MNE group unless it is applied to the whole enterprise. That in turn would render this a unilateral measure, prone to causing double taxation, and the likely disagreements destined to eventual resolution under the mutual agreement procedure (MAP) of tax treaties.

As an alternative, the proposed formula-based method could be, at most, applied selectively and used alongside a FAR-based approach based on the arm's length principle. The proposed formula would be resorted to only when the traditional transfer pricing methods are unsatisfactory.

Another possible solution would be to allocate taxing rights to routine profits to countries in which functions and activities take place, and allocate the right to tax the residual profit to the market or destination country where sales to third parties take place. This approach would use transfer pricing methods to achieve an arm's length outcome and then reap the benefit of the unitary approach when they do not (*i.e.*, for allocation of residual profit). This would be similar to the proposal regarding marketing intangibles the OECD has put forward in the context of the digital economy, and is intended to move from a FAR to a FARM approach that would add a market component to the FAR analysis. Thus, the market state would also obtain the right to tax part of the profit linked to sales in the other state that represents a more inclusive nexus orientation.

Stakeholders' perspective

Many stakeholders consider the report a welcome attempt by the CBDT towards providing a uniform approach to profit attribution to remove ambiguity and uncertainty. Moreover, the CBDT's consultative approach of inviting comments from various stakeholders is appreciated.

Several stakeholders submitted comments on the report to the CBDT. Based on our discussions with stakeholders, the following are additional points that need to be considered:

1. The fractional apportionment approach recommended by the CBDT seems to keep India's position strongly in contention, especially in global fora (for example, the program of work issued by the OECD to develop a consensus solution for the digital economy released on May 31, 2019, refers to it), but the approach requires much more deliberation and broader discussion;
2. The calculation of profits attributable to a PE, whereby only those employees and assets of the AE involved in the Indian operations are to be considered, should be clarified;
3. A formula-based approach would need to consider the possible outcomes for different business models prevalent in the industry, and it would need to be sensitive to all relevant factors;
4. Amendments should allow for deduction of interest and depreciation/amortization in computing a "global operational profit margin" and should further specify that only the profits of the legal entity that carries on the specific business are to be considered, not those of the wider group or ultimate parent; and
5. The existing treaty framework and separate entity/arm's length approach as advocated in the treaties should not be subject to the new rules until consensus is achieved.

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Way forward

Profit attribution has always been a problematic issue, and it has been litigated in several fora. The CBDT's publication of the report for public consultation is a welcome move, and it allows the government to test the waters as to the public's receptiveness. It remains to be seen what changes the CBDT makes to its recommendation after comments from the various stakeholders are reviewed, now that the consultation period has ended. However, we would suggest that the formulary methodology be once and for all abandoned in favor of a realistically available alternative methodology to align transfer pricing and profit attribution principles.

— Suchint Majmudar (Bengaluru)
Partner
Deloitte India
suchintm@deloitte.com

Mudigonda Vishweshwar (Bengaluru)
Partner
Deloitte India
mvishweshwar@deloitte.com

Argentina amends transfer pricing regime

Argentina's tax authorities on May 27 published a general resolution that introduces changes to the transfer pricing rules regulated by Law No. 27,430, Decree No. 1,170, and General Resolution No. 1,122.

The principal modifications introduced by RG 4496/2019 are described below.

Transactions with third parties

Form 867 must be filed if the taxpayer entered into import/export transactions of goods (non – commodities) with third parties within the calendar year. The new resolution has modified the thresholds for filing this form; if the taxpayer's import/export transactions with third parties total less than ARS 10 million, there is no need to submit the form.

Threshold on transfer pricing obligations

Argentinian taxpayers whose transactions with foreign related parties and with third parties located in non-cooperative jurisdictions or tax havens invoiced in the fiscal year individually exceed the amount of ARS 300,000 or on an aggregate basis a total of ARS 3,000,000, must submit the following information annually:

- Form F. 743, which includes information regarding transactions with foreign related parties and/or with third parties located in tax havens or non-cooperative jurisdictions.
- Form F. 4501, which includes a transfer pricing report and a certification by an independent public accountant.
- The financial statements corresponding to the two immediate fiscal periods before the fiscal period that is reported.

Deadlines

The new general resolution harmonizes the due dates for filing various transfer pricing forms. More specifically, forms F. 741, F. 743, F. 867, and F. 4.501, as well as the taxpayer's financial statements, must be submitted by the eighth month immediately following the close of the fiscal year, with the exact date depending on the last digit of the taxpayer's ID number.

Elimination of Form 969

The general resolution eliminates the obligation to file Form 969, which required information regarding transactions with foreign related parties and/or with third parties located in tax havens and non-cooperative jurisdictions. Much of this information is now provided as part of form F.743.

The modifications introduced by RG 4496/2019 became effective as of the day of publication – May 27, 2019 – and will be applicable to obligations regarding fiscal years beginning on or after January 1, 2018, inclusive.

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contact Deloitte Touche Tohmatsu Limited.

— Horacio Dinice (Buenos Aires)
Partner
Deloitte Argentina
hdinice@deloitte.com

Silvana Blanco (Buenos Aires)
Partner
Deloitte Argentina
siblanco@deloitte.com

IRS introduces campaign aimed at captive service providers

The IRS's Large Business and International division (LB&I) announced on April 16 a new transfer pricing-related campaign that will focus on ensuring that US multinationals pay their captive service providers no more than arm's length prices.
URL: https://www.irs.gov/businesses/corporations/irs-announces-the-identification-and-selection-of-three-large-business-and-international-compliance-campaigns

The new campaign, the Captive Service Provider Campaign, will focus on the transfer pricing of controlled transactions involving a foreign captive subsidiary that performs services exclusively for its US parent or for other members of the controlled group. The notice stated that if the prices of such controlled services exceed arm's length prices, the result could be inappropriate shifting of income and erosion of the US tax base. Although the notice did not identify a specific industry or fact pattern, the subsidiaries that would be subject to this campaign presumably perform medium- or high-value functions.

The total number of LB&I campaigns has risen to 53. Since the initial roll-out of 13 campaigns in January 2017, LB&I has considered this program the primary way to promote strategic, efficient, and issue-focused application of examination resources. (For prior coverage, see Global TP Alert 17-002).
URL: https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-global-transfer-pricing-alert-17-002-15-february-2017.pdf

Currently, only two of the 53 campaigns focus on transfer pricing issues – the Captive Service Provider Campaign and the Inbound Distributor Campaign introduced in January 2017.

— John Breen (Washington, DC)
Managing Director
Deloitte Tax LLP
jobreen@deloitte.com

Kerwin Chung (Washington, DC)
Principal
Deloitte Tax LLP
kechung@deloitte.com

Belgium amends CbC report notification requirement

Belgium's law of 2 May 2019 regarding various tax provisions was published in the Belgian Official Journal on 15 May 2019. The new law introduces a change in transfer pricing reporting obligations that reduces the compliance burden for Belgian entities required to file a country-by-country (CbC) report notification form (Form 275 CBC NOT). The law adds a new section to the Belgian Income Tax Code's (ITC) article 321/3, which deals with the CbC report's notification requirement.

Background

According to ITC article 321/3 §1 and §2, each Belgian entity of a qualifying multinational entity (MNE) group is obligated to file a CbC report notification form (275 CBC NOT) with the Belgian tax authorities on an annual basis, indicating whether the Belgian entity is the group's ultimate parent entity (UPE) or a surrogate parent entity (SPE). If it is neither the UPE nor an SPE, the Belgian entity must identify the group entity that will file the CbC report.

The 275 CBC NOT form must be filed on or before the last day of the group's reporting period.

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Change introduced

The new section in article 321/3 ITC (§3) states that the filing of form 275 CBC NOT is required only if the information provided deviates from what was filed for the previous reporting period (that is, in case there is a change in ultimate parent entity).

This change to the law, which entails a reduction in taxpayers' compliance burden, will be applicable for reporting periods ending on or after 31 December 2019.

— Jurgen Meersman (Gent)
Senior Manager
Deloitte Belgium
jmeersman@deloitte.com

Ann Gaublomme (Brussels)
Director
Deloitte Belgium
agaublomme@deloitte.com

André Schaffers (Brussels)
Partner
Deloitte Belgium
aschaffers@deloitte.com

Canada's 2019 budget introduces transfer pricing measures

Canada's 2019 federal budget, released March 19, proposes two new measures concerning the relationship between the transfer pricing rules in the Income Tax Act (ITA) and other provisions of the ITA. The budget also provides commentary on the ongoing base erosion and profit shifting (BEPS) project.

A summary of the transfer pricing-related measures contained in the budget is provided below.

Transfer pricing measures

The two budget measures related to transfer pricing include the order of application of the transfer pricing rules and the definition of transaction for extended reassessment period.

Order of application of the transfer pricing rules: The government proposes amending the ITA to clarify that the transfer pricing rules in Part XVI.1 (s. 247) should have priority of application over other provisions in the ITA. The budget notes that this change may have various implications and provides an example on the calculation of transfer pricing penalties imposed under Part XVI.1 of the ITA.

The budget notes that the current exceptions to the application of transfer pricing rules that pertain to Canadian resident corporations that have amounts owing from controlled foreign affiliates, or guarantees of amounts owed by controlled foreign affiliates, will continue to apply.

The order of application measure will apply to taxation periods that begin on or after March 19, 2019.

Definition of transaction for extended reassessment period: The government also proposes to amend the ITA to ensure that the term "transaction" has the same meaning in both the transfer pricing rules and the applicable reassessment rules.

As background, an extended three-year reassessment period applies to reassessments made as a consequence of a transaction involving a taxpayer and a nonresident with whom the taxpayer does not deal at arm's length. The budget notes that this reassessment extension is intended to apply in the transfer pricing context, but that the expanded definition of "transaction" used in the transfer pricing rules does not apply for purposes of the extended reassessment period. As such, the change in definition of transaction for reassessment purposes is intended to better align the transfer pricing rules and the extended three-year reassessment period.

The change to the definition of "transaction" for purposes of the extended reassessment period will apply to taxation periods of taxpayers for which the normal reassessment period ends on or after March 19, 2019.

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Update on the BEPS project

The budget reiterates that the Canadian government continues to cooperate and actively participate in the Organisation for Economic Co-operation and Development (OECD) project known as the BEPS initiative.

Multilateral instrument: The budget notes that the Canadian government is taking the necessary steps to enact the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) into Canadian law and to ratify the MLI as needed to bring the tool into force.

Country-by-country reporting: In addition, the budget notes that Canada is currently participating in an OECD review of the information being collected in the country-by-country reports to ensure that they provide tax administrations with information that facilitates accurate assessment for transfer pricing and other BEPS risks. This review is scheduled to be completed in 2020.

For further details, see the Ministry of Finance's budget website.
URL: https://www.budget.gc.ca/2019/home-accueil-en.html

— Tony Anderson (Burlington)
Partner
Deloitte Canada
toanderson@deloitte.ca

Hernan Allik (Montreal)
Partner
Deloitte Canada
hallik@deloitte.ca

Christine Ramsay (Toronto)
Partner
Deloitte Canada
chramsay@deloitte.ca

Rob Stewart (Vancouver)
Partner
Deloitte Canada
rostewart@deloitte.ca

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