

Transfer Pricing Alert

Organization for Economic Cooperation and Development (OECD) Release on Transfer Pricing Documentation: The New Global Standard

On September 16, the Organization for Economic Cooperation and Development (OECD) issued the final revisions to Chapter V of the Transfer Pricing Guidelines. These revisions materially reduce the documentation burden on businesses contemplated in the discussion draft on transfer pricing documentation issued on January 30, 2014, and Country-by-Country (CbC) reporting, and clarify many of the issues that had concerned businesses.

However, the full impact of the additional requirements the new Chapter V imposes will not be fully understood until January 2015, when the OECD releases additional guidance on implementation issues, including timing.

It is clear that the new guidance will change the documentation process fundamentally and require most companies to gather and provide to the tax authorities substantially more information on their global operations than they have previously provided. Although implementation dates have not been set, companies should begin to consider the process to compile the information.

The new guidance will provide tax authorities with unprecedented transparency regarding the financial results of a company's global transfer pricing policies.

Three-Tiered Approach to Documentation

With the release of the revised Chapter V, the OECD has adopted a three-tiered approach to documentation that includes:

1. The **Country-by-Country (CbC)** reporting template - which is intended to provide a financial picture of a company's global operations;
2. The **master file** - which is intended to provide a high-level view of a company's business operations, along with important information on a company's global transfer pricing policies on intangibles and financing;
3. The **local file** - which is intended to provide information and support of the intercompany transactions that the local company engages in with related parties.



Country-by-Country (CbC) Template

After wide-ranging consultation regarding the CbC template, the OECD has significantly reduced the amount of information required and provided more flexibility on how businesses could provide the information.

However, the CbC report will still pose a significant challenge to companies trying to comply with the new documentation guidance.

Adoption of the CbC report as part of the OECD's transfer pricing guidelines was one of the key goals of OECD member countries, because it may provide most local tax authorities, for the first time, an organized picture of where a company earns income and pays taxes. The report may highlight gaps and inconsistencies in a company's transfer pricing policies or its implementation of those policies. In addition, the report may highlight potential inconsistencies in the place where revenue is recognized and the place where "value" is created.

Master File

The new master file requirements will require companies to collect and present a considerable amount of information that has not been collected by either headquarters or local companies in the past. Some examples are listed below:

- A chart of the supply chain for the five largest products and service offerings, plus other products or services amounting to more than 5 percent of a group's turnover;
- A list of important intangibles or groups of intangibles and which entities own them;
- The requirement to disclose bilateral advance pricing agreements (APAs) and rulings that was originally included in the master file has been moved to the local file, but disclosure is required only if necessary to understanding local transactions;
- The requirement to disclose Mutual Agreement Procedures was removed, while the requirement to disclose unilateral income allocation rulings and APAs was retained;
- The new master file can be prepared either on an overall company basis or a products group basis. If the master file is prepared on a product group basis, all product groups will have to be submitted to all tax authorities, even if the local subsidiary is part of only one product group.

Local File

The local file will contain much of the same information traditionally included in transfer pricing documentation reports.

The new guidelines state that searches for comparable companies need be completed only every three years if the functional profile of the company has not changed, although the data on the comparable companies must be updated annually.

New governance policies

This increase in global transparency is likely to mean that deviations from a company's transfer pricing policy or the implementation of that policy will become more apparent to tax authorities around the world.

For these reasons, companies that currently do not establish and monitor transfer pricing policies on a global basis may find a need to do so in the near future.

Preparation of documentation

The CbC template and the master file are likely to be prepared by the headquarters company. For companies that do not prepare their transfer pricing documentation on a global basis, the new files will require a substantial change. On the other hand, even if companies do prepare their documentation on a global basis, the new guidance is likely to require companies to compile and explain substantially more information than was traditionally included in documentation reports.

Implementation

The OECD will provide additional guidance on the process for filing and sharing documentation in order to encourage consistent application of the new guidance in January 2015.

The OECD has stated clearly that the CbC template and the master file are intended to be implemented in their standard form by all countries without deviation, to encourage consistency and efficiency of compliance for taxpayers.

Conclusion

The OECD has proposed a new paradigm for transfer pricing documentation that may cause many companies to rethink their current procedures to set, implement, monitor, and document their global transfer pricing policies.

The increase in transparency and the greater need for global consistency may require many companies to increase the resources devoted to transfer pricing issues.

The impact of the changes in Romania

Although Romania is not an OECD member, the Romanian legislation generally follows the Transfer Pricing Guidelines issued by the OECD.

In this context, the present changes to Chapter V of the Transfer Pricing Guidelines are expected to be implemented in Romania as well.

The Romanian legislation already contains provisions similar to the ones included in the Master file and local file approach currently proposed by the OECD. As such, the introduction of the CsC template is expected to create the most significant impact for the multinational group of companies which carry out activities in Romania, in terms of resources involved in the process of collecting and presented the requested information.

Deloitte Transfer Pricing Contacts in Romania



Dan Badin
Tax & Legal Partner-in-Charge
Phone: + 40 21 207 53 92
E-mail: dbadin@deloittece.com



Ciprian Gavrilu
Director
Phone: + 40 21 2075 348
E-mail: cgavrilu@deloittece.com

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