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Grant Thornton discussion draft response

Transfer pricing documentation and country by country reporting

Grant Thornton International Ltd, with input from certain of its member firms and their clients, welcomes the opportunity to comment on the discussion draft issued on 30 January 2014 regarding transfer pricing documentation and country-by-country (CbC) reporting.

Response to discussion draft on Transfer pricing documentation and country by country reporting

We applaud the OECD's continuing efforts to provide guidance to tax administrations regarding documentation requirements that might, over time, be adopted by all OECD countries, thereby providing both tax authorities and taxpayers, with a clear and consistent framework for showing that their transactions satisfy the arm's length principle.

We appreciate the spirit of openness which the sharing of this early draft demonstrates. We would however refer to our comments of 30 September 2013 at the scoping stage, several of which have not been addressed, or not fully addressed, by the discussion draft.

Developing guidance around the risk assessment process, for both tax administrations and taxpayers, is a challenging yet important endeavour. As will be seen in the following discussion, we believe that transfer pricing compliance by all MNEs will be significantly enhanced by having a well-developed risk assessment process in place. This process could include tax authorities providing consistent guidance regarding the factors that could create an enhanced risk of audit. Given that country-by-country reporting is intended to be part of the risk assessment process, we have specific suggestions regarding the form that such reporting should take.

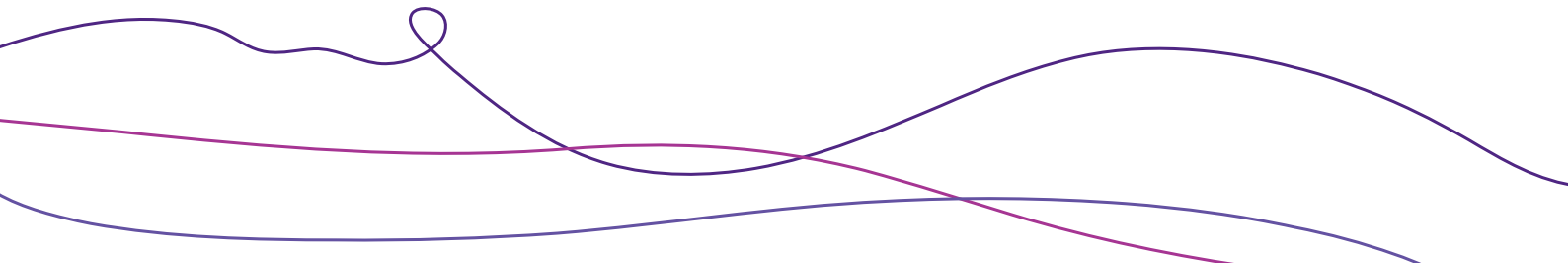
Likewise, establishing a standard approach to transfer pricing documentation is a laudable goal but also a significant challenge. As you noted, there exists tremendous variety in the transfer pricing laws and practices of tax authorities both in terms of tax return disclosure and documentation requirements. Getting to a consistent practice will in many cases require a country to take either administrative or legislative action to adopt rules that might differ significantly from that country's current practice.

Finally, the discussion draft requests comments regarding materiality standards, and whether any more specific guidance could be provided. Our recommendations regarding materiality focus on reasonableness, and on developing a flexible approach to materiality, rather than a rigid numbers-based approach. We believe that, just as transfer pricing itself is an inherently factual exercise, where no two companies are exactly alike, so too the determination of which transactions are material to a particular company cannot always be measured in absolute values or percentages of the total business activity. It is important, therefore, that whatever guidance is issued provide flexibility and consider materiality from the perspective of the group.

Therefore, our comments and recommendations can be summarized as follows:

- regarding risk assessment, establish a flexible format for taxpayers to include specific information about their material intercompany transactions at the time the tax return is filed;
- regarding documentation, not to specify the master file/ local file structure unless and until countries agree not to impose additional local rules for documentation;
- regarding materiality, establish standards that will both reduce the extent of required documentation and exempt certain taxpayers from specific reporting requirements regarding documentation;
- respect taxpayers' confidentiality.

A discussion of each item is presented below, and a summary of the responses of some of our clients to the questions posed by the OECD in the discussion draft is attached as an appendix.



Treat risk assessment separately from documentation

The discussion draft seems to conflate documentation and risk assessment, for example on page 2, Para. V.B.5 identifies as an objective for requiring transfer pricing documentation.

> To provide tax administrations with the information necessary to conduct an informed transfer pricing risk assessment.

Whilst we agree that both tax administrations and taxpayers need to conduct a transfer pricing risk assessment, we believe that it is important not to mix up the process of documenting specific transactions with the process of analysing the taxpayer's overall risk of a transfer pricing audit or adjustment. The objective of a risk assessment transfer pricing regime should be to provide information to tax authorities contemporaneously (i.e. along with parent company tax returns) and to allow taxpayers to demonstrate mindful compliance. Risk ratings for taxpayers could then be established based on the initial information, and future documentation requirements could be scaled to risk ratings.

The objective of transfer pricing documentation, on the other hand, is to demonstrate, with regard to one or more material intercompany transactions, that the results of the transactions are consistent with the arm's length standard. Therefore, we suggest that the OECD may be better served by separating the discussion regarding risk assessment from that regarding transfer pricing documentation, and consider a framework where risk assessment and documentation are different exercises done in different stages.

We would suggest that the first stage of review, i.e. risk assessment, be comprised of a review of tax returns, either CbC reporting or transfer pricing disclosures filed with tax returns, and/or information in the public domain.

We would also like to see some recognition by tax administration that unless current local rules are reduced, new requirements will inevitably be an extra burden. The OECD can help here by strong recommendations, for example that if and when CbC is adopted, local rules for tax return disclosures should be removed.

Allow flexibility and reduce reliance on the master file/local file structure for documentation

Similarly, unless the master file/local file structure is going to be adopted by all countries as constituting adequate documentation by consensus, the master file/country file approach is only likely to add to the burden.

In our experience, where the compliance burden exceeds the anticipated benefit, e.g., in the avoidance of fines or penalties, the level of mindful compliance is significantly reduced, and taxpayers who become frustrated in attempting to comply with rules that do not fit their circumstances are more likely to become non-compliant.

The information requested in the CbC, the master file and the local files is far too prescriptive in our view and too onerous. It would be preferable to start with a very limited list of requirements than to start with a huge 'wish list' as in the discussion draft annexes, and then hope to pare this down in future.

Allow taxpayers to prudently scale the level of documentation and be exempted from a documentation requirement where the intercompany activity is not material

We would like to expand on the idea of the 'principles of effective documentation' and focus on materiality. This consideration resonates particularly clearly with our clients. We appreciate the OECD's acknowledgement that…

'not every intercompany transfer requires the same level of documentation' and 'that not all transactions are sufficiently material to require full documentation'.

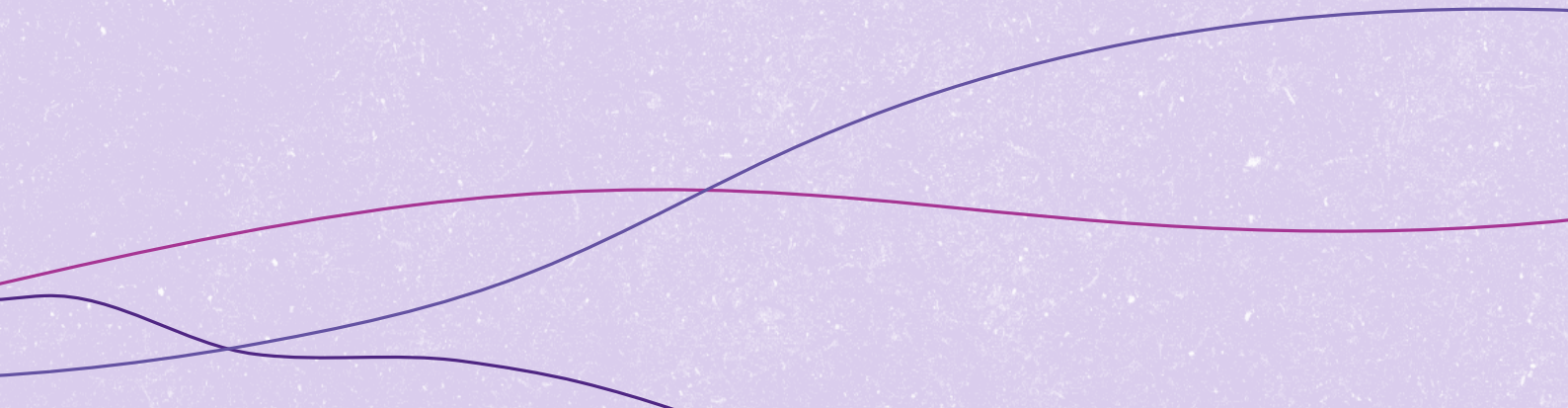
And we believe materiality should be considered both from the perspective of the size of the transaction (relative to the size of the taxpayer) as well as the size of the taxpayer (relative to other taxpayers).

We applaud the OECD's efforts with respect to exploring the suitability of safe harbours, and we support their application to certain transactions, and to SMEs in general.

Respect confidentiality

As can be seen from the views of our clients (attached) they regard confidentiality as paramount as it can severely affect their commercial operations if information on their business fell into the hands of their competitors. Taxpayers confidentiality must be respected, and information shared with, and between, tax authorities only under treaty or exchange of information provisions.

We very much appreciate the OECD's efforts with respect to the discussion draft and look forward to further material. We trust you found these comments helpful, and we welcome the posting of these comments on the OECD website if you deem appropriate.



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