Transfer Pricing Documentation
- In Need Of A Harmonization?

Master's Thesis in Commercial and Tax Law (Transfer Pricing)

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Abstract

In today's global world where internal cross-border transactions are made in a vast amount and thereby affect the economy to a large extent the area of transfer pricing has become more important than ever. Therefore the organization for economic co-operation and development (OECD) have started the base erosion and profit shifting project which aims to prevent the exploiting of gaps and differences of regulations in different states in cross-border transactions. Within this project the documentation requirements are discussed, more specifically a potential harmonization of the requirements. 30 July 2013 a white paper on the subject was published which led to a suggested draft for changes in the Chapter V of the OECD transfer pricing guidelines.

This thesis aims to answer the question of whether or not there is a need for harmonization in the area of transfer pricing documentation and whether or not the purposed discussion draft fulfills the potential need in an appropriate manner. How this affect the Swedish documentation requirements is also asked. The Code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD) is an existing form of harmonizing the documentation requirements which is also analyzed and to some extent compared to the suggested changes in the draft.

The lack of harmonization in such a cross-border dependent area has shown to be problematic and the possible gains for both taxpayers and tax administrations on a global basis suggests that a harmonization is desirable. Some aspects of the draft are still in need of clarification but all in all the draft is desired, the reactions of the industry also support this conclusion. The draft is moving towards a similar harmonization as the EU TPD and since the EU TPD is based on the current OECD transfer pricing guidelines it is inevitable to find clear similarities.
Preamble

This thesis is the final product of five years of studies at the program for Commercial and Tax Law at Jonkoping International Business School (JIBS). We would like to take the opportunity to thank everyone that has made this possible.

First we would like to give thanks to JIBS for an excellent program and fantastic professors. The previous five years have been an amazing journey which would not have been possible without JIBS and all people involved in the Commercial and Tax Law program.

A well deserved special thanks is given to our thesis supervisor Roger Persson Österman at Stockholm University for the great feedback provided and the motivational pushes given. We would like to thank Oscar Good at the Swedish Tax Administration in Gothenburg for providing insight into the organizations operations.

Due to examination rules the thesis content has to be divided between the authors. For this purpose the Chapters 1, 7, 8 and 9 responsibility is on both authors. Puja Karimzadeh is responsible for Chapters 2, 3 and 4. Richard Sandström is responsible for Chapter 5 and 6.
<table>
<thead>
<tr>
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<th>Description</th>
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<tbody>
<tr>
<td>APA</td>
<td>Advance pricing agreements</td>
</tr>
<tr>
<td>BIAC</td>
<td>The Business and Industry Advisory Committee</td>
</tr>
<tr>
<td>BEPS</td>
<td>Base Erosion and Profit Shifting</td>
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<tr>
<td>EU TPD</td>
<td>Code of conduct on transfer pricing documentation for associated enterprises in the European Union</td>
</tr>
<tr>
<td>EY</td>
<td>Ernst &amp; Young</td>
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<tr>
<td>C+</td>
<td>Cost plus method</td>
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<tr>
<td>CUP</td>
<td>Comparable uncontrolled method pricing method</td>
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<tr>
<td>CbC</td>
<td>Country by country</td>
</tr>
<tr>
<td>Draft</td>
<td>Discussion Draft on Transfer Pricing Documentation and CbC Reporting, from OECD</td>
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<tr>
<td>Draft comments</td>
<td>Public comments on the draft, published by the OECD</td>
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<tr>
<td>G8, G20</td>
<td>Discussion forum for the governments of the major respectively eight and twenty economic nations</td>
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<td>ICC</td>
<td>International Chamber of Commerce</td>
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<td>MAP</td>
<td>Mutual agreement procedure</td>
</tr>
<tr>
<td>MNEs</td>
<td>Multinational enterprises</td>
</tr>
<tr>
<td>Mr. Good</td>
<td>Oscar Good, transfer pricing specialist</td>
</tr>
<tr>
<td>MTC</td>
<td>OECD Model tax convention on income and capital</td>
</tr>
<tr>
<td>OECD</td>
<td>The organization for economic co-operation and development</td>
</tr>
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<td>OECD TPG</td>
<td>Transfer pricing guidelines</td>
</tr>
<tr>
<td>p</td>
<td>page</td>
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<td>para</td>
<td>paragraph</td>
</tr>
<tr>
<td>PwC</td>
<td>PriceWaterhouseCoopers</td>
</tr>
</tbody>
</table>
SMEs  Small and medium enterprises
Skatteverket  Swedish tax administration
STA  Swedish tax administration also known as Skatteverket
TTPR  The tax administrations regulation on transfer pricing documentation between associated enterprises
White paper  = White Paper on transfer Pricing Documentation, from OECD
WP6  = Working Party 6
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I Introduction

1.1 Background

Today most countries have adopted transfer pricing rules through national legislation by assistance of the guidelines issued by the organization for economic CO-operation and Development (OECD). Transfer pricing methods are used in the case where associated companies purchase or use goods, services or intangibles from each other. The methods are simply methods to determine the price that would have been set if the transaction would have been with a third party (arm's length principle) instead of an associated enterprise. This is to prevent profit shifting from one country to another and thereby preventing erosion of the tax base. To make sure that the price set is at arm's length the tax administrations in the majority of states can demand certain documentation from the associated enterprises. The companies have to provide documentation in case the price set is questioned by the relevant tax administration.¹

Through globalization the multinational enterprises (MNEs) role in the economy has increased. By viewing today's amount of cross-border activity it is clear that the economy is going towards a more interdependent phase where the governments cannot only focus on their own nationals.² According to the Swedish Statistical Yearbook of Sweden 2006 export of goods out of Sweden in 2004 exceeded 900 billion SEK and imports over 700 billion SEK. The fact that a large part of international trade occurs within international company groups the transfer pricing of those groups greatly impact the tax base of countries.³

The OECD is an international organization created to stimulate economic progress and world trade. It currently has 34 members⁴ and is highly influential in the area of international taxation. The guidelines in chapter V are from 1995⁵ and are in need of an update to keep up with the growing globalizing economy.⁶ Because of this OECD issued a white paper in 2013 regarding a revision, resulting in a draft published January 30 2014 suggesting a

¹ Preface OECD TPG.
² Preface 1-3 OECD TPG.
³ Prop 2005/06:169 p 88.
⁴ http://www.oecd.org/about/membersandpartners/list-oecd-member-countries.htm
complete revision of chapter V.\textsuperscript{7}

As mentioned above, the transfer pricing rules are mostly influenced by guidelines provided by the OECD, PATA and the EU. The guidelines revolving documentation can for example be found in Chapter 5 of "OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations". These solely function as extensive guidelines and therefore the implementation can be quite diverse in different states. Consequently states have different documentation requirements even though the rules are based on the same source. Different applications of the documentations requirements affect the MNE groups since they have transactions in different countries and must obey different rules. The fact that different rules must be observed leads to MNE members establishing a lot of different documentations that in reality has the same content. This is an economic burden for the companies but can also counteract the level of cooperation the member states should have in these cross-border issues.

There is more or less an international consensus that change is needed. Scholars state that there is a need for harmonization,\textsuperscript{8} and the G8 meeting with economic growth on its agenda in 2013 especially urged the OECD to develop the transfer pricing documentation guidelines, showing that it is of a concern for global economic growth.\textsuperscript{9} The suggested change from the OECD starts with a white paper in 2013 and continues with a discussion draft in early 2014. With this the OECD propose a two-tiered system consisting of a master file and local country files, just as the voluntarily EU documentation system EU TPD.

Many questions can be asked in relation to this. Is there really a need for change? Is the OECD moving towards the EU TPD model? Will the new system be successful, and what obstacles lies ahead?

\textbf{1.2 Purpose}

The purpose of this thesis is to evaluate if there is a need for harmonizing the current transfer pricing documentation requirements in accordance with the newly proposed discussion draft on transfer pricing documentation and country by country reporting (discus-

\textsuperscript{7} http://www.oecd.org/ctp/transfer-pricing/discussion-draft-transfer-pricing-documentation.pdf

\textsuperscript{8} the Transfer Pricing Concerns of Developed and Developing Countries, Susan C Borkowski, International Journal of Accounting, Volume 32, Issue 3 p 321-336.

\textsuperscript{9} White paper page 2.
sion draft) and if yes, does the new proposition have any chance of succeeding. The question if the draft proposal shift towards an application more alike the EU TPD than the current OECD model will also be evaluated. The purpose will be sought through three sub-questions:

1) How are the documentation requirements in the OECD TPG and EU TPD formed today?

2) What does the Swedish legislation regarding documentation state and how do the practitioners (Swedish tax administration) actually use the documentation?

3) What changes are suggested in the discussion draft and what would these changes imply for the current application of the documentation; Which specific questions are raised in the discussion draft, how are these addressed and do the changes fulfill what they seek to do?

1.3 Delimitation

The manner in which the purposed changes of chapter V in the OECD transfer pricing guidelines handle intangible properties as well as financial instruments will not be dealt with in this thesis. The reason being that they behave differently to normal assets, why the OECD have given them special considerations in its guidelines. To some extent the transfer of goods and services will however be exemplified for the reader to get an overview of which factors the parties need to consider. The goal is to present how the discussion draft affects the transfer pricing assessment and audit process.

Apart from the Swedish legislation revolving transfer pricing there will be no further review for any other national legislation. Primarily because the Swedish legislation and tax administration are easier for the authors, as Swedes, to communicate with and analyze and because lack of space.

EU TPD will be assessed because of its different system and its ambition to harmonize the documentation requirements by using a two-tier system. Since the comparison between the discussion draft with the EU TPD is not the main question of the thesis a further evaluation of PATA and the ICC becomes otiose.

1.4 Method & Material

When answering the purpose of this thesis the materials that have been used are national legislation, a limited amount of case law, preparatory work, international agreements and
Guidelines (OECD transfer pricing guidelines and EU TPD) and a new OECD proposal. Apart from this an interview has been held with a representative from the Swedish tax administration.

In an area like transfer pricing which is governed by national legislation but mostly based on global guidelines like the OECD transfer pricing guidelines it is of great importance to analyze the purpose of the national legislation. The OECD transfer pricing guidelines are recognized on a global level and in some sense are the leading organ for the transfer pricing industry. That is why this thesis evaluates their discussion draft regarding future changes in the documentation requirements. Another international organization that is given some space is the EU who also have separate rules regarding transfer pricing documentation. They are primarily based on the guidelines presented by the OECD but they promote a two-tier system with a larger master file and specific country-file. This systematic is opted for in the new OECD proposal which makes an comparison with the EU way of interest.

The current documentation requirement is stated in the Swedish law about self declaration and control data (Lag om självdeklarationer och kontrolluppgifter). The law together with its preparatory work is used as a basis to explain the current situation together with its purpose in Sweden. The legislation delegates the responsibility to the government in creating a more detailed explanation on what is to be included in the documentation. The government in their turn have delegated it onward to the Swedish tax administration and thus their regulations are also of importance in this thesis. To answer the purpose of this thesis it is important to analyze the current legislation to be able to see if the discussion draft presented by the OECD means any actual changes in relation to the current system. Moreover it also functions as an reassurance that the Swedish legislation is in line with the OECD transfer pricing guidelines. The case law connected to the documentation requirements are few and fairly irrelevant to answer the purpose of this thesis. It is merely used to show that the Swedish courts are taking the OECD guidelines into consideration when ruling on transfer pricing issues.

The interview with the Swedish tax administration was made with the transfer pricing specialist Oscar Good (Mr. Good) at the office in Gothenburg. As a specialist he holds lecturers and educates businesses and also internally regarding transfer pricing, he also deals a lot with accountants who ask questions regarding transfer pricing. Mr. Good has been working with transfer pricing for the past eleven years. He spent his first three years with Ernst &
Young (EY) and Volvo AB. EY is one of the big four auditing companies and help companies with questions revolving transfer pricing whilst Volvo AB is a big MNE group. He has been working at the Swedish tax administration for the last eight years. The Swedish tax administration are active in keeping an open dialogue with both industry and public. Mr. Good position at the tax administration taken together with his experience provides an reliable source at least based on the knowledge he possesses. By just interviewing one person from the tax administration there is a risk of subjectivity and lack of complete overview. This decision was however made with the limitations of the thesis extent, the information from the interview is not treasured as legislation and not given an analysis on a detailed basis but more used as tool for identifying the current practical structures within transfer pricing in Sweden. Apart from its potential weaknesses the interview gives guidance on what is contemplated when an actual transfer pricing assessment and audit is done. Moreover how it is done and how strict the requirements are followed from the tax administrations.

The white paper and the draft for a new chapter V is the basis for the new suggestion, and therefore an important part of this thesis. The white paper and draft comes directly from the OECD, an organization whose importance in the field is already mentioned. The content of these are presented in a factual manner. When the authors opinion is presented it is clearly stated and is generally under its own heading.

In the draft OECD ask specific questions, wishing for the public to voice its opinion on those matters. Being an important matter, there are too many answers to present them all in this thesis, well over 1000 pages of answers are published by the OECD. To gain valuable information on the potential users of the new chapter V, a few select answers is examined. The select ones are BIAC, Confederation of Swedish Enterprise (Svenskt Näringsliv), the ICC and PwC Global. BIAC was selected as its purpose is to provide advice to policymaking in the OECD. Confederated of Swedish Enterprise was chosen both as a representative of many businesses, large and small, and because of its connection to Sweden as the thesis has a connection to Swedish legislation. The ICC was chosen because its position as the largest business organization in the world. With the business world covered we also wanted a voice of the auditing/consulting firms, since they are highly involved in creating transfer pricing documentation. Our representative from these is PwC Global. We had wished to look at the Swedish tax authority answer, but they left no answers to the draft. Luckily the interview mentioned gives us some insight.
1.5 Disposition

Due to the size of the thesis, analysis are spread out in connection to the relevant topic that is discussed. In the final analysis and discussion the whole these is connected and the purpose is answered.

The thesis begin with Chapter 2 - Transfer Pricing, where the basic concepts of taxation of MNEs are discussed, the arm's length principle is explained together with some commonly used methods of calculating arm's length price.

The thesis continues with Chapter 3 - Creators of Normative Models, where the OECD and EU documentation systems and requirements are examined.

This is followed by Chapter 4 - Swedish legislation, where the Swedish documentation requirements is examined, first in a technical standpoint, and later in a practical standpoint with the help of an interview with the Swedish Tax Authority.

The next is Chapter 5 - The White Paper, where the background and contents of the new suggestion is explained. The OECD conclusions and the new system is presented, as well as our analysis.

After follows Chapter 6 - The Chapter V Discussion Draft, where the significant changes are discussed as well as implementation difficulties and questions asked by the OECD to the public.

The thesis is finished with Chapter 7 - final Analysis and Discussion and Chapter 8 - Conclusion, where a connecting final discussion is made with the full previous thesis as base, and a conclusion is made.

After the thesis is finished Chapter 9 - The Future some thought of what the future might hold is presented.
2 Transfer Pricing

2.1 Introduction

This chapter consists of a short explanation of the basic tax oriented problems that tax administrations and multinational enterprises (MNEs) face when companies are active in different jurisdictions. Thereafter the importance of transfer pricing rules such as the arm's length principle is described. Following this a more detailed description on how the arm's length principle functions to be able to understand the documentation requirements connected to it. In the chapter regarding the arm's length principle a short summery of the principle is presented together with a practical example to illustrate its function. After the summary the comparable uncontrolled method, cost plus method and resale price method which are used to calculate the arm's length price will be evaluated, in order to understand the expressed documentation requirements in chapter 4.3 in a better way.

The information in this chapter functions as a basis and is essential in the evaluation of the current transfer pricing rules and the proposed discussion draft from the OECD, thereby also the purpose of thesis.

2.2 Taxation Of Multinational Enterprises

The MNEs profits in subsidiaries or permanent establishments based abroad are usually taxed where these operate (source-based taxation) but can also be taxed fully and/or to some extent in their home state (residence-based taxation). With these two systems colliding in today's global world comes an increased risk for double taxation. It is more complex to determine the allocation of the MNEs profits today than 30 years ago; the technological advancements (specially communications) and the increased integration of economies makes for a difficult situation for both tax administrations and MNEs. In these circumstances separate national legislations prevents an effective and optimal solution for both parties.\footnote{Preface 1 & 2 OECD TPG.}

MNEs operating in separate tax jurisdictions with different laws and administrative requirements are at larger risk of increasing their administrative burden and consequently having higher compliance costs than a comparable company operating in one tax jurisdiction would have.\footnote{Preface 3 OECD TPG.} The difficulty for tax administrations are found at both practical and
policy level. Policy wise all tax administrations wants to secure their own tax base but this needs to be done in a way where the allocation of profits is in harmony of where the profits arise. The optimal situation is when only one jurisdiction wants to tax the profit but for that to happen the jurisdictions involved need to reconcile the view on where the profit should be taxed. On a practical level the tax administrations might have difficulties gathering the accurate data in the case of cross-border transactions when the relevant information is located abroad. That also hinders the localization and allocation of the taxable profits which produces a dilemma where the different tax jurisdictions need to co-operate to obtain the required amount of information to draw a correct conclusion. A global market with unpredictable tax regimes that could lead to double taxation hinders the movement of goods, services and capital. Therefore double taxation legislation like bi-lateral treaties and more importantly transfer pricing legislation is of great importance.

In an attempt to solve the above mentioned situations where the source-based and residence-based tax systems collide, the OECD member states have chosen to follow the separate entity approach. The separate entity approach means that companies and permanent establishments within the MNE are viewed as separate entities and their profits should primarily be taxed where they arise. Commonly the permanent establishments get taxed in the state they are active (source state) as well as their resident-state but the resident-state exempts or deducts the amount of tax paid in the source-state.

For the separate entity approach to function there must be some regulation revolving transactions between associated enterprises. It is necessary that the transactions are priced in the same manner they would be if the transactions were made with independent parties in a similar situation, i.e. the market price also known as the arm's length principle. By regulating cross-border intra-group transactions the states hinder MNEs from shifting the base of the taxable profits to jurisdictions with lower tax rates. By making the MNEs apply the arm's length principle member states are more confident that the profits are taxed in accurate state and therefore the risk of double taxation decreases.

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12 Preface 4 OECD TPG.
14 Preface 5 OECD TPG.
15 MTC Article 23 A-B.
16 Preface 6 OECD TPG.
To assure the member states that the arm's length principle is applied the member states require MNE's to hand in documentation regarding their intra-group transactions.

2.3 Arm's Length Principle

2.3.1 Meaning

The arm’s length principle, created by the OECD, is the international standard method used for determining the transfer price of a transaction. In article 9 of the OECD Model Tax convention (MTC) the principle is found, it states (where)…

“...conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.”

The arm's length principle aims to regulate the prices of the transactions so that they are set at the same price that would be set between uncontrolled independent entities in a comparable situation. This is accomplished by treating the entities of a MNE as separate entities instead of viewing them as controlled entities of on single company.\textsuperscript{17} The arm's length principle has also been implemented into Swedish law, referred to as “Korrigeringsregeln” and is found in the Swedish income tax act.\textsuperscript{18}

The consequence of applying an incorrect transfer price and thus not applying the arm's length principle is exemplified below:

Company X and Y are associated companies (Company X owns more than 50% of the stocks in Company Y). Company X is based in Ireland and company Y in Sweden. Company X sells water bottles to the price of 1 000 000$ to Company Y. However the arm's length price for the bottles should be 750 000$.

\textsuperscript{17} Chapter 1, para 6 OECD TPG.
\textsuperscript{18} Inkomstskattelagen (1999:1229), Chapter 14, para 19-20.
### Example 1

<table>
<thead>
<tr>
<th></th>
<th>Company X</th>
<th>Company Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Country of origin</td>
<td>Ireland</td>
<td>Sweden</td>
</tr>
<tr>
<td>Income (+)</td>
<td>$ 1 000 000,00</td>
<td></td>
</tr>
<tr>
<td>Costs (-)</td>
<td></td>
<td>$ 1 000 000,00</td>
</tr>
<tr>
<td>Affect on taxation</td>
<td>$1 000 000*12,5%</td>
<td>$1 000 000*22%</td>
</tr>
<tr>
<td>Tax base gain (+)</td>
<td>$ 125 000,00</td>
<td></td>
</tr>
<tr>
<td>Tax base loss (-)</td>
<td></td>
<td>$ 220 000,00</td>
</tr>
</tbody>
</table>

### Example 2

<table>
<thead>
<tr>
<th></th>
<th>With arm’s length price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income (+)</td>
<td>$ 750 000,00</td>
</tr>
<tr>
<td>Cost (-)</td>
<td>$ 750 000,00</td>
</tr>
<tr>
<td>Affect on taxation</td>
<td>$750 000*12,5%</td>
</tr>
<tr>
<td>Tax base gain (+)</td>
<td>$ 93 750,00</td>
</tr>
<tr>
<td>Tax base loss (-)</td>
<td>$ 165 000,00</td>
</tr>
<tr>
<td>Difference in tax base in Example 1 &amp; 2</td>
<td>$ -26 250,00</td>
</tr>
</tbody>
</table>

First off this is a simplified example that does not take into consideration certain tax deductions and other legal affects connected to global trade, its solely functions as an illustration of the importance of the arm’s length principle. The big difference in the examples is the change in the taxable amount in each country. Sweden tax base is decreased by $55 000 when comparing the two examples. By placing the money in Ireland the profits solely get taxed at a rate of 12,5% which lets more money stay within the MNE group than it would if it were to stay in Sweden.

#### 2.3.2 Comparable Uncontrolled Method

The comparable uncontrolled price method (CUP) is a pricing method which compares a controlled transaction of property or service with a comparable uncontrolled transaction. It is of importance that the transactions are very similar for a correct application of this method. The transaction can be compared completely externally, by viewing a transaction between two independent entities or internally by viewing a similar transaction between a company in the MNE group and an external party. Different pricings between an uncontrolled transaction and a fully controlled one may indicate that the price needs to be adjusted to match the market price. In order to use the CUP method there should be practically no differences between the transactions compared, if there are any differences these should be of such art that they would not affect the price of the transaction in the free market or be able to adjust in a way that would remove their effect. This is the most reliable method.

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19 Chapter 2, para 13 OECD TPG.
20 Chapter 2, para 14 OECD TPG.
used to reach the arm's length price but the difficulty in finding a similar enough transactions between uncontrolled entities to compare prices with is a large weakness.  

Examples of CUP transactions: Gasoline, Gold, Lumber etc.

**2.3.3 Cost Plus Method**

When a CUP method cannot be used the OECD recommends the resale price method (RPM) or the cost plus method (C+ method), which seek out the least complex entities. The least complex entity, within a transaction between associated enterprises, is the one that holds the fewest functions, assets and risks. The level of complexity determines the amount of adjustment necessary to compare the transaction with a uncontrolled transaction. The lower level of complexity leads to a higher chance of finding a comparable transaction.

When the manufacturer in a controlled transaction is the least complex entity the C+ method is applied. The main factor viewed is the manufacturers attained costs related to the transaction with the associated enterprise (supply costs). In order to get the arm's length price a cost plus mark-up needs to be added to the supply costs. The cost plus mark-up is based on the relation of the functions, risks and assets taken by the manufacturer and takes into consideration mark-ups for similar transactions with or applied by uncontrolled entities.

**2.3.4 Resale Price Method**

When the least complex entity is the reseller the RPM is the more suitable method. Instead of adding a mark-up the price is reduced by a gross profit mark-up margin. The gross margin is the amount it takes to cover the resellers operating and selling expenses and this in relation the functions, risks and assets taken by the reseller. The arm's length price is the price reduced by the gross margin expenses together with any other related costs.

**2.3.5 Mutual Agreement Procedure And Advanced Pricing Agreement**

Mutual agreement procedure (MAP) is stated in the 25 article of the MTC and is a tool for states to resolve cases where double taxation arises because of different interpretations of

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21 Chapter 2, para 15 OECD TPG.  
22 Chapter 2, para 37 OECD TPG.  
23 Chapter 2, para 39 OECD TPG.  
24 Chapter 2, para 21 OECD TPG.
the MTC. For example when two states have different opinions on what the correct transfer price is.\textsuperscript{25}

Advanced pricing agreements (APA) is an option for MNE groups that want to make sure that their transactions are at arm's length previous to the actual transaction and thus agreeing with one or several tax administrations on the correct market price.\textsuperscript{26} The process is long and very expensive for the MNE groups but in situations with large transactions the companies might benefit from the security and lack of tax risks with having this type of arrangement.\textsuperscript{27}

\textbf{2.4 Summary}

The transfer pricing rules assure that the correct amount of profits are taxed in the right state when it comes to internal cross-border transactions. The right amount of tax is decided by treating/setting a price on the transaction as if it was done with a independent uncontrolled party. To set such a price the arm's length principle is applied and thereby methods such as the CUP, C+ and RPM help in defining these prices. Since this is a cross-border activity which is regulated through national legislation, instruments like the MAP have been created to help the member states in resolving issues of different opinions regarding the pricing. APA is a documentation option that functions as an agreement with relevant states. By obtaining an APA companies are reassured that the pricing on their internal transactions are correct, but this procedure is relatively expensive.

\textsuperscript{25} Article 25 MTC.

\textsuperscript{26} Transfer pricing India - Advanced pricing agreement, http://www.transferpricing-india.com/Advance_price_agreement_APA.htm

\textsuperscript{27} EU joint transfer pricing forum - secretariat discussion paper on alternative dispute avoidance and resolution procedures, Chapter 2 (b-c).
3 Creators Of Normative Models

3.1 Introduction

This chapter aims to answer the present condition of the documentation requirements. Primarily a short presentation of the OECD is made followed by a general explanation of the purpose of TP documentation requirements, thereafter a review of the OECD guidelines and the EU TPD.

To answer the thesis purpose a thorough review of the current transfer pricing documentation system needs to be presented. The documentation requirements as such are regulated through national legislation but there are other organizations such as the OECD and the EU that have recommendations and guidelines on how these rules should be implemented. The Swedish legislation is not bound by these rules but have opted through case law\textsuperscript{28} to follow the OECD TPG, therefore the guidelines have a great impact on the interpretation of the Swedish transfer pricing documentation legislation.

OECDs major impact on the transfer pricing area and future involvement through its discussion draft is of great importance in terms of the purpose of this thesis. To understand the need for changes one needs to analyze the current state. To answer if the proposal goes towards the application of the EU TPD, an fairly thorough presentation of it is necessary.

3.2 The Organization For Economic CO-operation And Development

3.2.1 Background

The Organization for Economic CO-operation and Development was established in 1961\textsuperscript{29}. OECD is an organization that aims to increase global trade on a "multilateral, non-discriminatory basis and to achieve the highest sustainable economic growth in member countries".\textsuperscript{30}

This is done by working closely with business and labor committees as well as creating a forum where governments can work together towards solutions for mutual problems.\textsuperscript{31}

\begin{footnotesize}
\textsuperscript{28} RÅ 1991 ref 107.
\textsuperscript{29} Guide to international transfer pricing: Law, Tax Planning and Compliance Strategies, Author A Michael Heimert Ceteris; et al 2010, PAGE 1.1 purpose of OECD guidelines.
\textsuperscript{30} Preface para 7 OECD TPG.
\end{footnotesize}
The vast amount of cross-border transactions creates a situation where the risk of double taxation is high. Double taxation is harmful for the free movement of establishment, persons, goods, services and capital consequently it is harmful for the growth of the global trade. The OECD model tax convention is the core for many cross-border tax treaties. The tax convention provides states with guidance on how to tax an income that is taxable in both countries by giving them the possibility to use their specially formed template. The states modify certain articles in their bi-lateral tax treaties but overall follow the tax conventions recommendations.

The tax convention does not deal with the issue of MNEs intra-group transactions since the area is complex and the rules are regulated through national legislation. The problem with potential double taxation and tax base shifting led to the creation of the first rapport of the transfer pricing guidelines in 1979. The OECD made a significant revision of the 1979 rapport to the guidelines used today, that were published in 1995.

Both tax administrations and taxpayers use the OECD TPG to find valuable guidance in setting a transfer price.

3.2.2 Chapter V

3.2.2.1 Introduction

Chapter five in the OECD TPG offers guidance to tax authorities on the rules and procedures useful in acquiring sufficient data in order to make a transfer pricing inquiry. The usefulness for taxpayers is demonstrated through an enhanced comprehension of the type of data the tax administrations are requiring from them, in order to be in line with the arm's length principle. Consequently tax payers avoid unnecessary difficulties during audits of the controlled transactions.

In most jurisdictions the burden of proof lays with the tax administration so the tax payer does not have to prove that the transfer price is set at arm's length. However when the

31 [http://www.oecd.org/about/-2014-02-12](http://www.oecd.org/about/-2014-02-12)

32 Prop 2005/06:169 p88.

33 Preface para 7 & 13 OECD TPG.

34 IBID, Prop 2005/06:169 p89.

35 Prop 2005/06:169 p89.

36 Chapter 5, para 1 OECD TPG.
burden is set on the tax administrations, they may reasonably require that adequate data is provided to them by the tax payers. The OECD stress the irrelevance of where the burden of proof lays since neither party should justify unsubstantiated and unverifiable claims about the transfer price by utilizing the burden of proof. 37

According to the OECD the facts and circumstances of transactions between associated enterprises are of great importance when acquiring the required data for a transfer price assessment. This system is somewhat based on individual evaluations. However the guidelines provide some directions on what type of information the associated enterprises should present to the tax administration and how the interested parties can handle cases with individual circumstances. 38

3.2.2.2 Rules And Procedures

Tax payers should make the transfer pricing assessment before setting a fixed price therefore the data realistically available prior to the actual transaction should be taken into consideration. According to the OECD it is reasonable to demand that tax payers have sought if any "comparable data from uncontrolled transactions" are obtainable. It is also feasible to require that tax payers inspect if any changes have been made in relation to transactions made previous years if those conditions form a base in the decision of a transfer price set the present year. 39 It is expected that the tax payers are equally cautious when deciding the price of a controlled transaction as they would be with an uncontrolled transactions of comparable importance and intricacy. To verify that the expected amount of thought has been placed in order to comply with the arm's length principle certain documentations are anticipated. For example; what data was used to support the transfer price, which factors were considered and which method was chosen? As mentioned above this information should be provided to tax administrations when needed but shall not become a contemporary must that forces tax payers to provide information prior to making the transaction nor be a obligatory part of the tax return. 40 The documentation should be provided to the tax authority in a timely manner (decided by national law). The taxpayer may choose to present their documentation in the form of untreated original documents or a preprocessed manuscript in the

37 Chapter 5, para 2 OECD TPG.
38 Chapter 5, para 16 OECD TPG.
39 Chapter 5, para 3 OECD TPG.
40 Chapter 5, para 4 OECD TPG.
form of a book. The information may be gathered in any language they please but a translated version is to be offered to the relevant tax authority if necessary.

The need for certain documentation provided to tax administrations must be put in relation to the emerging costs and increased administrative burden for the tax payers. In the case "disproportionately high costs" are required to obtain data from associated entities based abroad or to find comparable uncontrolled transactions tax payers are released from providing these specific documents. The criteria's to use this exemption are that tax payers either believe that no comparable data exists or that the costs for obtaining the information would be disproportionately high in relation to the transaction in question. The assessment must take the principles within the OECD TPG into consideration. 41 Since documentation is barley produced for tax purposes and other companies making similar uncontrolled transactions are not asked to provide it, documentations should only be prepared and required if the information is necessary to make a reasonable assessment on the transactions compliance with the arm's length principle and the cost put on the tax payer is not disproportionately high. In other words the tax payer should only produce as much documentation that is minimally required to make a reasonable assessment. 42

The tax payers trade secrets, scientific secrets and other confidential information are to be handled with caution. Tax administrations should make certain that this information does not become publicly disclosed. This type of documentation should only be requested when the previous mentioned criteria can be fulfilled. Only exception is when the documentation is needed in a legal proceeding. 43

However the OECD encourages tax payers to present sufficient documentation to support their transfer price since the tax administration will make their own assessment if the documentation is incomplete. In that sense the documentation provides an opportunity for tax payers to persuade the tax administration of their transfer price. Depending on the complexity of the transaction the importance and possibility to affect the transfer price through well based documentation increases. 44

41 Chapter 5, para 6 OECD TPG.
42 Chapter 5, para 7 OECD TPG.
43 Chapter 5, para 13 OECD TPG.
44 Chapter 5, para 14 OECD TPG.
Documentation required at the stage of tax return shall be limited to the information needed for the tax administration to draw an approximate conclusion on which tax payers are of interest for further examination.\footnote{Chapter 5, para 15 OECD TPG.}

\subsection*{3.2.2.3 Guidance On Relevant Information}

Information of relevance to a specific transfer pricing assessment is based on the details and circumstances of that particular transaction. Consequently it is not viable to specify the specific amount and type of information that tax payers should provide to tax administrations in any generalized manner. Nonetheless the OECD TPG aims to provide directions on some general circumstances that all transfer pricing situations have in common. Hence this information is useful in the purpose of complementing the individual assessment of the specific case.\footnote{Chapter 5, para 16 OECD TPG.}

The information in common to all transfer pricing investigations are for example data regarding the tax payer, its associated enterprises, the controlled transaction type and the reasoning about the transfer price.\footnote{Chapter 5, para 16 OECD TPG.} To calculate the arm's length price the information should also include which functions the associated enterprises perform and if there is any possible data from uncontrolled transactions with similar circumstances. The information best suited for an evaluation of the arm's length principle may vary depending on the pricing method that is chosen for the transaction.\footnote{Chapter 5, para 19 OECD TPG.}

Since the purpose of documentation is to show tax authorities that the transfer price of their controlled transaction is in accordance with the arm's length principle the information provided in chapter 2.1-2.2 is of great importance in making the said assessment. Information regarding the controlled transaction can/should include the transaction type (goods, services, intangibles or financial instruments), terms of contract, economic circumstances and any changes made in the arrangement between enterprises with previous dealings.\footnote{Chapter 5, para 17 OECD TPG.}
In certain transfer pricing transactions there is value in referring to information regarding the involved associated enterprises. This might contain:

- A framework of the business,
- An organizational structure,
- "Ownership linkages within the group",
- The entities sales and profits prior to the transaction,
- Amount of transactions between the tax payers and other foreign associated enterprises, for example "the amount of sales from inventory assets, the rendering of services, the rent of tangible assets, the use and transfer of intangible property, the interests on loan."\(^{50}\)

Business strategies and other special circumstances may affect the transfer price quite a bit. Therefore information regarding these areas might be essential for tax payers to prove that their price is complying with the arm's length principle. Providing sufficient documentation could be the most suitable way to persuade the tax administrations that the MNE groups transfer price is correct. The business strategies can for example explain/justify why a tax payer "adds a mark up on manufacturing cost, it might be to deduct related costs from sales prices to end users in the market where the foreign related parties are conducting a wholesale business"\(^{51}\). Whilst special circumstances might be when there are an intentional set-off transactions where both companies draw benefits from each other or part of a management strategy where the tax payer is trying to get established on a new market. An example of set-off is when a entity buys goods from a foreign associated enterprise and receives a lower price because the entity provides some sort of services free of charge in return.\(^{52}\)

The OECD TPG also exemplifies the type of information that could be helpful in identifying the functions performed and risks assumed that ought to be described in the functional analysis. Functions described may include:

"manufacturing, assemblage, management of purchase and materials, marketing, wholesale, stock control, warranty, administration, advertising and marketing activities, carriage and warehousing activities, lending and payment terms, training and personnel."\(^{53}\)

\(^{50}\) Chapter 5, para 18 OECD TPG.

\(^{51}\) Chapter 5, para 19 OECD TPG.

\(^{52}\) Chapter 5, para 20-21 OECD TPG.

\(^{53}\) Chapter 5, para 24 OECD TPG.
The risks assumed can be:

"risks of change in cost, price, or stock, risks relating to success or failure of research and development, financial risks including change in the foreign exchange and interest rates, risks of lending and payment terms, risks for manufacturing liability, business risk related to ownership of assets, or facilities"\(^{54}\)

Regarding information on the financial factors of the taxpayer's foreign associated enterprise the costs of manufacturing, research & development (R&D) "and/or general and administrative expenses" are three factors that could be of use for the tax administration in making their assessment.\(^{55}\)

### 3.2.3 Summary

The OECD is an international organization which aims to enhance global trade. By giving out guidelines and templates for states to use they have become one of the leading actors in the world of taxation, specifically transfer pricing. The documentation requirements established in many countries, for example Sweden, are all based on OECDs TPG, more particularly chapter V. Chapter V gives MNEs the guidance on what they should provide in order to be in line with the arm's length principle and also what tax administrations should bear in mind when they decide to do their transfer pricing assessment as well as audit. The documentation is necessary for MNEs to prove that their transactions are in line with the arm's length principle. In most states the burden of proof lays with the tax administration regarding the correctness of the price set of the transactions, however the MNEs must provide sufficient amount of documentation for the tax administrations to make such an assessment.

Chapter V guides tax administrations on what type of information is of relevance, how to make an assessment of the MNEs transfer pricing situation and also what to demand in case of an audit. Chapter five clearly states that the decisions made in regards to transfer pricing issues, regardless of heritage, should bear in mind the proportionality of the matter. Is the information necessary to make a transfer pricing assessment/audit? Are the benefits for the tax administration deriving from the information justifiable in relation to the burden/cost it puts on the MNEs. Transfer pricing is also stated to be an area of subjectivity that needs it flexibility because of the many complex and diverse situations. The OECD

\(^{54}\) Chapter 5, para 24 OECD TPG.

\(^{55}\) Chapter 5, para 26 OECD TPG.
use the TPG in order to direct the industry in transfer pricing questions as well as exemplifying solutions to potential problems.

### 3.2.4 Analysis

Chapter five of the OECD TPG is full of information concerning what type of data is desirable when making a transfer pricing assessment for both tax payers and tax administrations. It has a broad spectra and leaves room for states to lay their structure as they please. The OECD stresses the fact that the information required can be difficult to obtain since it calls for data on uncontrolled transactions and as if that was not enough the data needs to be comparable. Therefore tax administrations and tax payers should bear in mind that transfer pricing "*is not an exact science*" and requires "*the exercise of judgment*" from both parties.

The OECD fifth chapter in the TPG seemingly functions as a broad guideline where it provides insight in the area of transfer pricing. MNE groups can use it and thereby understand to a certain extent what is expected of them. However they must still be very aware of the countries specific rules when it comes to documentation since the area is governed by national legislation. States legislators and tax administrations on the other hand can use these guidelines when creating the relevant legislation or making the transfer pricing assessments. The TPG instrument covers a lot of ground by exemplifying different areas that are open for interpretation, for example how to balance functions and risks against each other.

Something that permeates the fifth chapter of the OECD TPG is what the authors would call its own proportionality test. Meaning that the rules and provisions regarding documentation in a state should take into consideration whether the information the tax authority might want to attain is putting tax payers in unreasonable burdensome situations. The guidelines even stress that the tax payers should not provide the tax authorities with data that would put too high administrative or costly burden on them. This leads to a somewhat situation based system where complex transactions require more information and therefore the demands on the tax payers increase but on the other hand it is not necessary to create exhaustive documentation when the transaction as such might not generate high profits.

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56 Chapter 1, para 12 OECD TPG.

57 See chapter 3.2.2.
The level of collaboration is put to its extreme when it comes to the burden of proof. The tax authorities have to prove that the price set is not at arm's length and the way to do that is to analyze the documentation provided. The guidelines state that national legislation should regulate a system where companies should provide sufficient data for the tax administration to make the transfer pricing assessment.\textsuperscript{58} Nevertheless it seems hard to balance the sufficient amount of documentation and still withhold the level of proportionality. It puts the tax payers in a position where there transfer pricing might be lacking but it is not worth it for the tax administration to go into a judicial battle since these tend to be long and costly for both parties.

Combining above mentioned factors shows the OECD view on the transfer pricing area. The fact that it is not an exact science puts a lot of burden on both parties and the guidelines are encouraging both involved parties to work together. Countries want businesses to establish within their boundaries and therefore they cannot put an excessive burden on the companies however they do want as much tax base as possible allocated to them. The companies strive towards profits and assurance. If the states demand to much or if the states are unclear with what type of information they need it will not create a good business atmosphere and the companies will look elsewhere for their investments. This calls for an dialogue between the parties where both parties are flexible in reaching the necessary amount of data to attain an correct transfer price. However the authors see a great problem with the burden of proof since it does create a system where tax payers can provide barely insufficient data and the tax authority are in a position where it might not be worth it to pursue the pricing since it might be hard to prove that the price set is wrong with the information provided.

3.3 Code Of Conduct On Transfer Pricing Documentation For Associated Enterprises In The European Union

3.3.1 Background

The European Union (EU) is an economic and political partnership between 28 states within Europe, these states will be referred to as the member states in this chapter. The union started out as an economic union after the second world war to enhance communication and economic interdependence with the purpose to avoid future conflict. Today the

\textsuperscript{58} See chapter 3.2.2.
union is governed by the rule of law which means that the common rules are based on "treaties, voluntarily and democratically agreed by all member countries". The goal is to create one single market within the union called the internal market. The internal market strives towards free movement of goods, services, capital, people etc. In order to have an functioning internal market it is necessary that the 28 member states agree on regulations regarding cross-border activities, especially the taxation of such activities.

In the 2001 company tax study the Commission of the European Union acknowledged the impact that the transfer pricing tax issues have on the internal market. Even though the OECD TPG were accepted and applied by all member states the variety of ways to interpret and implement the OECD TPG frequently created intra-community disputes. These disputes can potentially hinder an effective functioning of the internal market as well as generate unnecessary costs for both national tax administrations and businesses. Four years later the commission concluded that an alternative to the OECD TPG can be a partially centralized and standardized system. A partially centralized system provided by a general documentation file that is provided to all member states (masterfile) and one country-specific file provided to the countries the MNE group has active inter-group transactions. Nevertheless the OECD TPG is still the relevant framework when questions arise about applying the documentation requirement. By having a partially centralized system larger companies within the union will benefit from providing the same information to all the countries in one masterfile.

As a consequence of the above mentioned documents the EU Council together with the representatives of the governments of the member states produced a code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD).

3.3.2 EU TPD
The EU TPD is an international agreement that has the legislative status of a soft law meaning that it is not legally binding for the member states. It does not aim to be imple-
mented in a way that hinders other international solutions that have a wider global scope.\textsuperscript{63} However the EU TPD does function as an optional standardized template provided by the member states for the associated enterprises within the EU when forming documentation of their internal transactions.\textsuperscript{64} Its goal is to provide the tax administrations with enough information to make well-reasoned risk assessments or at least enable them to ask valid and precise questions about the transactions in the case of a tax audit.\textsuperscript{65} As in the OECD TPG the EU TPD emphasizes the importance of proportionality between the need for documentation and the level of burden put on the tax payer. More precisely article 6 states:

"Member States should:

(a) not impose unreasonable compliance costs or administrative burden on enterprises in requesting documentation to be created or obtained;

(b) not request documentation that has no bearing on transactions under review;

(c) ensure that there is no public disclosure of confidential information contained in documentation."

The difference between the two guidelines lies in the way the information is given and the fact that the EU TPD is a more harmonized system. The EU TPD states that the code of conduct is voluntary and it aims to lessen the groups burden of documentation.\textsuperscript{66} By harmonizing the system, multinational enterprises within the union can lower their costs by creating lesser documentation or just providing it in an similar way to the countries involved in the transaction. In applying the EU TPD template both tax authorities and associated enterprises within the union can benefit. The need for legal counseling in each relevant member state becomes almost unnecessary for the MNEs. Also the tax administra-

\textsuperscript{63} Preface, para 14-15 EU TPD.

\textsuperscript{64} p1-2 EU TPD.

\textsuperscript{65} Annex article 1, para2 EU TPD.

\textsuperscript{66} Preface, para 14-15 EU TPD.
tions co-operation should increase because of the transparency that comes with having the same ways and means of obtaining the documentation.  

3.3.3 Technical Assessment - Legal Span And Structure  

3.3.3.1 Introduction  
The EU TPD includes all transactions between associated enterprises residents within the union and transactions where one enterprise is a non-resident and the other party is. Documentation in accordance with the EU TPD is divided into two parts; one masterfile where general information of relevance is provided to all concerned member states and multiple country-specific documentations that are more specific to the involvement of the MNE in that certain country.

The documentation is mainly standardized, however in the case of complex group structures and transactions the documentation may need to be complemented. Where it is possible the information should be sought in already existing documentation within the group nevertheless in the case where this is not possible the enterprises will have to produce new documentation.

3.3.3.2 Masterfile  
The masterfile should show the economic situation of the business and contain the structure of the whole MNE group. It should also present the transfer pricing system that is of relevance and make this information accessible to all relevant member states. Regarding language specifications the EU TPD states that member states involved should accept a "commonly understood" language to the largest extent possible and avoid translations because of the extra cost this will put on the businesses. More specifically it should provide a general description of:

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67 Preface, para 12 EU TPD.  
68 EU joint transfer pricing forum - report on activities of the EU joint transfer pricing forum in the field of documentation requirements. p. 21-22.  
69 Annex article 3 EU TPD.  
70 Annex article 1 EU TPD.  
71 Annex article 2 EU TPD.  
72 Annex article 4.1 EU TPD.  
73 Annex article 23 EU TPD.
• Business, business strategies and if any changes were made with regards to the prior tax year.\textsuperscript{74}

• The groups operational, organizational and legal structure with a graphic representation of the MNE’s organization. In this segment there should also be a list of the MNEs group members and explanation of the parent company's activity in the subsidiaries.\textsuperscript{75}

• An identification of the companies who are dealing in controlled transactions in connection to the enterprises within the EU. The controlled transactions as such should also be described by providing information regarding the: \textsuperscript{76}

"(i) Flows of transactions (tangible and intangible assets, services, financial),

(ii) Invoice flows and

(iii) Amounts of transaction flows"\textsuperscript{77}

• Functions performed and risks assumed. Together with assets used these components help characterize the companies within the group that is why changes made in comparison with the prior tax year also should be described. For example the changes should describe if one enterprise goes from the characterization of a limited risk manufacturer to an assembler.\textsuperscript{78}

• The ownership of intangible property like trademarks, patents, know-how and etc. Also royalties received or paid.\textsuperscript{79}

• "The MNE group's inter-company transfer pricing policy or a description of the group's transfer pricing system that explains the arm's length nature of the company's transfer prices".\textsuperscript{80} For example which transfer pricing method is used in a inter-group transaction when company A (CA) buys goods from company B (CB) and how that would be affected if CA or CB did business with company C instead.

\textsuperscript{74} Annex article 4.2 (a) EU TPD.

\textsuperscript{75} Annex article 4.2 (b) EU TPD.

\textsuperscript{76} Annex article 4.2 (c-d) EU TPD.

\textsuperscript{77} Annex article 4.2 (d) para 2-4 EU TPD.

\textsuperscript{78} Annex article 4.2 (c) EU TPD.

\textsuperscript{79} Annex article 4.2 (f) EU TPD.

\textsuperscript{80} Annex article 4.2 (g) EU TPD.
• A list of the agreements (APA, cost contribution agreements) and rulings regarding transfer pricing affecting the associated enterprises within the EU. 81
• A commitment by all intra-group entity's to provide complementary information when requested and this shall be done in a reasonable time period in consonance with domestic provisions. 82

By making this information fairly specific the companies do not have to make several copies of similar documentation but can have one masterfile to fulfill all the requirements set. Different applications of national requirements might require some alteration or additions in the information needed that a layman might not know or be able to understand which leads to the necessity of acquiring legal assistance and higher costs for the businesses.

3.3.3.3 Country-Specific File

The country-specific file is a compliment to the masterfile that when taken together ensures member states that the tax treatment of the inter-group transaction has been done in a correct manner. 83 This file contains information regarding local conditions and other such information important only to the local tax authorities. The language of the country-specific file should be the language specified by the relevant member state. MNEs can choose to put the country-specific information in the masterfile but must provide the information related to the country-specific file in a language required by the affected member state. 84 In Sweden it would be Swedish, Danish, Norwegian or English. 85 In other words if the MNE group is exclusively active in member states that accept the English language it is sufficient to provide the country-specific information in one language.

When a company resides within the EU and is dealing with controlled transactions within the union or with a party established outside of the union, there must be country-specific files for all the member states involved in the inter-group transaction. This information can also be gathered in one masterfile. 86 The country-specific file can contain all of the relevant

81 Annex article 4.2 (h) EU TPD.
82 Annex article 4.2 (i) EU TPD.
83 Annex article 5.1 EU TPD.
84 Annex article 6 and 9 EU TPD.
85 SKVFS 2007:1 article 13.
86 Annex article 7 EU TPD.
dealings of the MNE within a member state. An MNE can also have more than one country-specific file in each member state and present separate files for each entity active in that specific country or "group of activities in that country." 87

In detail the country-specific file should, in addition to the material provided in the masterfile, contain:

- an in depth explanation of the business and business strategy, with a comparison of the business strategy applied the previous tax year if any relevant changes have been made, 88
- An "description and explanation" on the controlled transactions connected to that specific country, this should consist of

"(i) Flows of transactions (tangible and intangible assets, services, financial),

(ii) Invoice flows and

(iii) Amounts of transaction flows" 89

- "A comparability analysis, i.e:
  (i) characteristics of property and services,
  (ii) functional analysis (functions performed, assets used, risks assumed),
  (iii) contractual terms,
  (iv) economic circumstances, and
  (v) specific business strategies;" 90

- Which transfer pricing method was chosen for the controlled transactions and an explanation on why that specific method was the best alternative, 91

- Description of available internal and/or external comparable transactions of relevance 92

87 Annex article 8 EU TPD.
88 Annex article 5.2 (a) EU TPD.
89 Annex article 5.2 (b) para 2-4 EU TPD.
90 Annex article 5.2 (c) EU TPD.
91 Annex article 5.2 (d) EU TPD.
92 Annex article 5.2 (e) EU TPD.
3.3.4 Summary

The EU is consistently striving towards a more coherent internal market within the union and therefore realized that the diverse national application of the transfer pricing regulations could affect the manner in which companies established their entities. The goal is to have standardized documentation requirements as well as structures within the member states. EU TPD is the documentation form in which the companies within the union can opt to use. It is regulated as a soft law and sets no legal obligation for the member states other than that they should accept this as a form of presenting the documentation. The information provided should still be based on the guidance found in the OECD TPG. With the purpose of having similar documentation requirements and in the same time decrease the burden of the MNEs within the union the EU TPD splits the documentation into two stages. Phase one is a masterfile which has more general information of relevance to all member states and phase two is a country-specific file that is more specific of the dealings within that specific country. As a consequence all tax administrations within the union can turn to the masterfile in the assessment process to see, for example, the structure of the MNE group as well as the type of transactions made. MNE groups can provide the information in one file instead of providing it to each member state that asks.

3.3.5 Analysis

The EU TPD aims to strengthen the internal market by creating a more unanimous application of the interpretation regarding the documentation requirements set out by the OECD. A similar application is supposed to lead to more transparency between tax administrations and lower the compliance costs for the business. The OECD TPG is still used as the framework to resolve uncertainties which makes the type of information the companies need to provide more or less the same. The positive effects is that tax administrations in different member states tend to ask for similar information. A union climate like this should lower the compliance costs when companies establish in a new member states. Compliance costs in this case are the administrative and legal costs provided by abiding to

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93 Annex article 5.2 (f) EU TPD.
different requirements in multiple jurisdictions and the potential tax penalties connected with providing non-sufficient documentation and possible double taxation.\textsuperscript{94}

EU TPDs statute as a soft law creates a problem within the solution. By creating a standardized system that can be applied and interpreted freely by the member states the amount of documentation made by the business does not necessarily need to decrease since the member states still can demand a vast amount of documentation in their country-specific files. It can definitely have positive consequences, such as the masterfile and country-specific file becoming more and more alike with time. A reason would be that the member states might desire the same national requirements union wide in order to ensure an agreeable allocation of profits and thereby make it more predictable for companies to provide the right type of documentation regardless of state of residency. However with the span of company taxation in the EU ranging from 10\% to 35\%\textsuperscript{95} the risk of countries with more preferable taxation regimes applying their demands in accordance with the other member states are fairly slim. So a full "harmonization" is unlikely but as long as the EU TPD has this effect on several member states the businesses compliance costs should decrease. Furthermore if the information required by the EU TPD is sufficient for the tax administrations to make a correct risk assessment and generally no further information is needed the EU TPD would have the affects it strives for. As mentioned in the analysis of the OECD it becomes difficult when it comes to transfer pricing to know exactly what you should ask for since it is not an exact science. Nevertheless the authors believe that it is good that the EU are trying to make the rules more similar but still keep the wiggle room for discussion between the MNEs and relevant member states. It creates a system where it is possible to see if countries are looking for the same information and if followed will be a lot easier to evaluate than the fully separate national legislations.

Using standardized and partially centralized requirements in the union ought to lead towards more transparency between tax administrations.\textsuperscript{96} A higher level of transparency could also have its negative effects, for example sensitive information gathered in the documentation in union might end up in the wrong hands. The more countries involved the higher the chance of sensitive information leaking out. Since there are 28 member states

\textsuperscript{94} EU joint transfer pricing forum, 3.1 (69).

\textsuperscript{95} 10\% in Bulgaria and 35 in Malta. KPMG tax rates online, http://www.kpmg.com/Global/en/services/Tax/tax-tools-and-resources/Pages/tax-rates-online.aspx

\textsuperscript{96} EU joint transfer pricing forum, 3.3 (82,89).
with different historical and cultural backgrounds the level of corruption can vary quite a bit, for instance the commission made a survey where companies answered if they thought corruption had any interference when they lost a contract in a specific country and in Bulgaria and Slovakia the percentage that answered yes were 58% respectively 57% . That is why it is of great importance that companies can choose to not share sensitive information, however to do the risk assessment it can be necessary.

According to the Swedish tax administration the introduction of the EU TPD has not changed the way companies present their documentation in Sweden which indicates that its influence has been quite small. 

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98 See chapter 4.4.3. and 4.6.
4 Swedish Legislation

4.1 Introduction

This chapter will start of by shortly presenting the purpose and evolution of transfer pricing documentation within the Swedish legal system. Thereafter the current regulation will be thoroughly reviewed and function as a base for analyzing chapter 4.4 which revolves an interview with the Swedish tax administration. Finally an analysis of chapter 4 will be presented after the interview has been described.

Since the transfer pricing rules are in their current form governed by national legislation it is logical to analyze the legislated documentation requirements of one state. By understanding how the rules are applied in one state in relation to the OECD TPG and EU TPD the analyzing of the discussion draft becomes better substantiated. The interview with the tax administration also gives a broader picture of the practical application of the documentation requirements, which functions as even better guidance on whether or not the proposal will implicate any differences and if it is desirable.

4.2 Purpose Of Documentation Requirements

As mentioned in chapter 2.1-2.2 the core of transfer pricing is the arm's length principle. A price at arm's length is the price set as if the transaction had occurred between two non-associated enterprises in a comparable situation, in other words the market price. It ensures that transactions between associated enterprises strive towards a market oriented price and prevents tax base evasion and profit shifting. According to the proposition the only reliable way in practice to evaluate if the price set is at arm's length is through an assessment of the documentation. Another reason for having documentation requirements is that the relevant tax administrations involved can reach an agreement on the transfer price, through their underlying tax treaty, and in that way obviate the risk of double taxation. This is however dependent on how well supported the enterprises documentation is.\(^9^9\)

To fulfill the need for a thorough evaluation of transfer pricing the Swedish Riksskatteverket (former tax administration) released a report in 2003 regarding information and documentation requirements in transfer pricing situations. At that time not many nations had opted for a legislated requirement but Riksskatteverket concluded that

\(^9^9\) Prop 2005/06:169 p 101-2.
there is a need for an expressed requirement for controlled transactions.\textsuperscript{100} However it is stated in the report that each transfer pricing situation shall be evaluated separately and that coherent form described by law is not an desired alternative.\textsuperscript{101} Later on this rapport led to a new law which stated that enterprises dealing with controlled transactions should, if asked, be able to present a variety of information. This information ought to be in storage and therefore streamline the process for the tax administration. Companies will have to make most necessary documentations beforehand in order to avoid last minute solutions in the case of audit.\textsuperscript{102} Expressed documentation requirements formulates a more efficient way for the tax administration to get a hold of relevant information, whilst it may be burdensome for entities in the startup phase of controlled transactions. For the entities it does however eliminate the risk for companies to set up documentation for transactions that occurred in an earlier period, which should lead to a clearer transfer pricing mindset and accuracy from the beginning. The more companies deal with transfer pricing the more their level of skill increases which consequently should lead to a decreased risk of double taxation in the case of faulty documentation.\textsuperscript{103}

Another valid argument is that if there is no expressed documentation requirement it will be hard for the Swedish tax authority to claim that their pricing is right when other tax authorities who operate in countries where such an requirement exists disagree.\textsuperscript{104} A clearer way of working creates an easier climate for the tax administrations to defend their pricing, with that said it means that the more precise data equals an easier transfer pricing assessment.

As a consequence of the conclusions drawn in the rapport an expressed documentation requirement was suggested in a law proposition.\textsuperscript{105} This proposition is now the current legislation that was put into force 1 January 2007.\textsuperscript{106} The meaning of the expressed requirements is presented and explained in the coming chapter.

\textsuperscript{100} RSV Rapport 2003:5 p 37.
\textsuperscript{101} IBID.
\textsuperscript{102} IBID and Prop 2005/06:169 p 102.
\textsuperscript{103} IBID.
\textsuperscript{104} Prop 2005/06:169 p 102.
\textsuperscript{105} Prop 2005/06:169 p 29-30.
4.3 Law About Self Declarations And Control Data And Other Regulations Of Relevance

4.3.1 Expressed Documentation Requirements

Sweden is one of the countries that has legislated an expressed requirement for documentation in the case of transactions between associated enterprises where one company is based in another country. The Swedish law self declarations and control data\textsuperscript{107} (LSK) states that a company that has transactions with a non-resident shall set up written documentation regarding the transaction.

The documentation shall consist of:\textsuperscript{106}

- "A description of the company, organization and business operations"
- Information regarding characteristics and scope of the transactions
- A functional analysis
- A description of the chosen pricing method
- A comparability analysis\textsuperscript{109}

However the documentation is only necessary if the companies are to be seen as associated enterprises in accordance with chapter 14 20§ in the Swedish income tax act (Inkomstskattelagen). The government can issue further instructions on the documentation requirements but they can also delegate this onward to another authority.\textsuperscript{110} In Sweden the government has delegated this responsibility to Skatteverket which is Sweden's tax administration.\textsuperscript{111}

In accordance with LSK the Swedish tax administration have created both regulation\textsuperscript{112} and papers\textsuperscript{113} with clear explanations to simplify the application of the documentation rules.

\textsuperscript{107} 19:2a LSK, Lag om självdeklarationer och kontrolluppgifter.
\textsuperscript{108} 19:2b para 1 LSK
\textsuperscript{110} 19:2b para 2 LSK.
\textsuperscript{111} 12:4 FSK (Förordning (2001:1244) om självdeklarationer och kontrolluppgifter).
\textsuperscript{112} The tax administrations regulation on transfer pricing documentation between associated enterprises (2007:1) (TTPR).
The regulations elaborate the information provided in the proposition to LSK with information regarding the approved languages and more detailed practically adjusted explanation of the requirements in 19:2b LSK. The papers are not legally binding nevertheless they function as further and more detailed guidelines with examples of the different pricing methods and when they should be applied, you could call it a handbook.

More specifically the handbook includes information that states that tax administrations regulation also states that documentation should be provided for each fiscal year. The documentation can be demanded by the tax administration earliest the day after the company has to provide their tax declaration for the relevant year. The company shall have a reasonable time to prepare such a request and it might be handed in an electronic form or in paper. Swedish, Danish, Norwegian and English are all accepted languages to provide documentation to the Swedish tax administration. Documentation created should be kept for at least ten years after the end of the calendar year that the fiscal year finished. The regulation also states that documentation provided in accordance with the EU TPD are accepted and that the rules in article 11 to 14 of the regulations are applicable for these cases as well.

Controlled transactions of small proportion are not obliged to provide documentation to the same extent as presented in LSK chapter 19 2b§. To qualify under controlled transactions of small proportion the entities should have transactions of goods below the collected market value of 630 prisbasbelopp and 125 prisbasbelopp for other transaction types. The transfer of intangible property is excluded from this exemption. 2014 one prisbasbelopp equals 44 400 Swedish crones(SEK).

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113 The tax administrations information about transfer pricing documentation between associated enterprises (2007:25).

114 11§ TTPR

115 12§ TTPR.

116 13§ TTPR.

117 14§ TTPR.


119 10§ TTPR.
The information provided in transactions that qualify under transactions of small proportion should be:

- A description of the MNE groups judicial structure and the entities along with MNE groups organizational structure as well as operational business.
- Information about the counter party in the transaction and their business.
- Relevant transactions with information about type, size and value.
- The transfer pricing method used to determine compliance with the arm's length principle.
- A description of possibly used comparable uncontrolled transactions.  

Apart from the expressed documentation requirements the tax procedure law (skatteförfarandelag) also states that companies involved in controlled cross-border transactions should document their transactions. It states that the documentation should be enough for the tax administration to make an transfer pricing assessment that shows if the price is in need of adjustments to be in accordance with the arm's length principle in chapter 14 19§ of the Swedish income tax act.  

The five above mentioned expressed documentation requirements connected to LSK will be presented, in chapter format, in a more detailed matter in order for the readers to get a clearer view on what the documentation in Sweden shall consist of.

### 4.3.2 A Description Of The Company, Organization And Business Operations

With this requirement the companies operational and legal description is desired and required. The purpose of the legal description is to get a clearer picture of the ownership linkage and how the company controls or is controlled by the rest of the business group. The operational part is linked to how the company and its group have organized their business and on what markets the company is active in.

In certain cases the industry in which the company is active within is of interest as well. The description of the industry can give an explanation of which factors and how these factors affect the profitability, trends on the market and the competitive situation. It shall also contain information on the company's position on the market in regards to its compet-

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120 Annex TTPR.

121 39:15-16 Tax procedure law (Skatteförfarandelag).
itors and business strategies. By explaining these factors it will become easier to explain the chosen comparable transactions and to demonstrate differences in the level of competition based on geographical markets, in that way one can explain the different transfer prices in different markets. Furthermore it can state what type of business strategy the company uses and in that way show if the market is a matured market, growing market or decreasing market, all these factors can be relevant in setting a transfer price. This also shows what type of business strategy the company applies.\textsuperscript{122}

If any relevant/essential changes are made within the company or the MNE group they should also be presented here.\textsuperscript{123}

\subsection*{4.3.3 Information Regarding The Characteristics And Scope Of The Transactions}

Intra-group transactions types involves goods, services, intangible property and financial contracts. As mentioned in the delimitation the intangible property and financial contracts aspect will not be discussed in this thesis. This part of the requirements require a documentation of the transaction as such, meaning the information on the type of transaction, contractual terms between the parties and the size of the transactions etc. The documentation shall also strengthen the reasoning behind the chosen arm's length method.\textsuperscript{124} Each transaction between the associated enterprises can be presented either separately or in a collected form.\textsuperscript{125}

Goods: Information to consider include which line of business the goods are sold within and the situation on the market. Moreover if there is any division of the market because of geographical reasons, information about the downstream market, quantity and quality of the products, time period, contractual terms like period of credit, currency, potential service commitments and guaranties. Regarding the information about goods guidance can be found in OECD TPG chapter I.

Services: Intra-group services are often performed by one or several companies within the group. For example one company can be in charge of the human resources or IT services

\begin{itemize}
\item \textsuperscript{122} Prop 2005/06:169 p 103-104
\item \textsuperscript{123} § TTPR.
\item \textsuperscript{124} See 2.2.
\item \textsuperscript{125} § para 1 TTPR.
\end{itemize}
within the group. The documentation should prove that a service has been made, that this service has benefited the group and that the price set is in accordance with the arm's length principle. Intra-group services are often remunerated by direct payment, however indirect methods are not uncommon especially when extensive services are being provided. Indirect methods are usually based on a distribution of the costs followed by a suitable allocation code. Using indirect methods increase the risk of incorrect pricing and that is why it is of great importance that there is documentation that supports the chosen method. In this an description of the services provided, which allocation code is used and why, if a cost + method is used and information regarding potential markup. Furthermore a report if the service receiver had any predictable benefit from the services provided.\textsuperscript{126}

This part shall also include the agreements of relevance in setting the transfer price. Where the enterprise have many agreements (for example many transactions) they may present a collected description where the agreements are split into their main categories and describe their price method. If the company or the group has any agreements regarding the transfer price with authorities these should also be integrated.\textsuperscript{127}

4.3.4 Functional Analysis

The functionality analysis is a crucial part of the transfer pricing documentation. It analyzes what functions, assets and risk each entity bears in relation to each other. Regards are taken to both intangible- and tangible property. Since the functions, assets and risks are viewed in relation to each other it is important to describe which functions affect the profitability of the company the most, which risks are most relevant and held by whom and who owns the assets of importance. The analysis is of great importance for identifying any comparable transaction and also to decide which arm's length method is applicable.\textsuperscript{128} The least complex entity is identified through this analysis.

Example: Apple US vs. Associated enterprise China (AEC)

Apple US: Buys goods from AEC and sells it to interested buyers. Owns all the intangible property such as trademarks and patents and bears the financial risk if the product are not as profitable as expected.

\textsuperscript{126} Prop 2005/06:169 p 104-105. 
\textsuperscript{127} 6§ para 2 TTPR. 
\textsuperscript{128} Prop 2005/06:169 p 105.
AEC: Provides goods to Apple on a contractual basis. Has no rights to the intangible property behind the product. Is very dependent on Apple US for work.

Practically all functions and assets are at Apple US and the risks revolving the sales of the goods are at the hands of Apple since AEC provides the goods based on contract which puts them in a position where they can sell large shipments and not worry about the resale. AEC is therefore the least complex entity and by that the easiest one to replace. This makes it easier to find comparable entities because it does not have to value the patents and such when determining a price at arm's length. The correct pricing method in this case would be the cost plus markup.\textsuperscript{129}

### 4.3.5 Description Of The Chosen Pricing Method

In this part of the documentation the companies describe which transfer pricing method that has been chosen and why. In Sweden it is expected that the choice is based and supported on the criteria's that can be found in the OECD TPG. Amongst these transfer pricing methods are the traditional transactional methods (CUP, C+, RPM)\textsuperscript{130} or the transactional profit methods TNNM and Profit split method. See chapter 2.3 for clarification on CUP, C+ and RPM.

Some states require the companies to justify why they did not chose the methods they deemed not applicable, it is the so called "best method rule". Sweden stated that the increased administrative burden of the companies does not stand in proportion to the benefits it would bestow the tax administration, therefore it is not an expressed requirement but can however be of relevance in exceptional cases.\textsuperscript{131}

### 4.3.6 Comparability Analysis

The arm's length principle proceeds on the basis that transactions between associated enterprises are compared with transactions between uncontrolled parties, a so called comparable uncontrolled transaction (CUP) method. The CUP can be done by comparing the transaction internally, a associated entity's transaction with an uncontrolled party or externally, comparing the transaction with two uncontrolled parties. It is decisive that the circumstances (see functionality analysis) are similar for this method to be used.

\textsuperscript{129} See 2.3.3.

\textsuperscript{130} See 2.3.

\textsuperscript{131} Prop 2005/06:169 p 106.
The comparability analysis should therefore contain a description of the eventual internal or external comparable transactions and how the choice was made. Guidance should be sought in the OECD chapter 1 TPG. Any adjustments made to simplify the comparability should also be described. In the case there are no comparable transactions the companies should describe how their pricing complies with the arm's length principle.\(^{132}\) To determine if the circumstances are comparable the associated enterprises should respond to and describe the expressed documentation requirements set in LSK.

More specifically the comparability analysis should involve the specific characteristics of the goods, service or assets, a functionality analysis, contractual terms, economical circumstances and business strategies. How to balance the criteria's against each other is dependent on the circumstances in each specific case, however the transfer pricing method used definitely affects the influence in which order the criteria are to be valued. For example if the CUP method is applied the product itself is more important than in the case of the RSP method where the functions and risk profile is more valued.\(^{133}\) It is nonetheless important to present information regarding both criteria's regardless of chosen transfer pricing method even if one is more influential than the other.

The proposition also states that the information provided with external comparable transactions is often hard to get. The internal comparisons are more often detailed and therefore also preferred.

Adjustments to improve the comparability between internal transactions and comparable transactions can be made for different reasons and in different ways. When external comparable transactions are used it is common that adjustments are made regarding accounting principles. The common denominator is that adjustments aim to improve the comparability of the transactions and shall only be used when it actually fulfills that purpose. If too many adjustments are necessary the entities should ask themselves if the transactions actually are comparable.\(^{134}\)

\(^{132}\) 9§ third sentence TTPR.

\(^{133}\) See 2.3.2 and 2.3.4.

\(^{134}\) Prop 2005/06:169 p 106-107.
4.4 Interview With The Swedish Tax administration

4.4.1 Introduction And Background

In this chapter the vital parts of an interview held with Oscar Good, an transfer pricing specialist at the Swedish tax administration will be presented and discussed. First off the method of how the tax administration choose which company to audit will be described. Following descriptions on the actual information the tax administration obtain and its use of the expressed documentation requirements. Finally Mr. Good explains his thoughts on the EU TPD, the new proposal and its potential positive effects as well as negative ones.

Mr. Good has been working at the Swedish tax administration for 8 years but have been dealing with the transfer pricing related questions for 11 years in companies such as EY and Volvo AB. He tells us the area is very complex and the tax administration does around 60 revisions a year so the process of finding a company with suspicious transfer prices needs to be thorough.

The Swedish tax administration transfer pricing departments are located in Sweden's three major cities, Stockholm, Gothenburg and Malmö. The average time spent on an audit in Gothenburg was 11 months in 2013. The department nearest the company at hand is often the one who does the audit, however different departments are specialized in different industries and therefore the Stockholm department also do audits in Gothenburg. For example Gothenburg are specialized in transactions connected to transport and pharmaceutical companies.

4.4.2 Identifying Tax Object

We started out by asking how the transfer pricing requirements are used within the tax administration and Mr. Good explained that their way of working is more practically oriented than theoretical. The tax administration start out with trying to identify their tax subject and this is done through a so called "omvärldsanalys" which identifies the biggest risk areas within the area of transfer pricing. These are MNE group restructurings, transfer of intellectual property, financial transactions (primarily internal loans) and large companies.

After they've decided the relevant risk area they want to pursue, the tax administration start seeking information. When it comes to restructurings, information can be found in articles, journals, the company's annual declaration where information is provided through open

135 Swedish, meaning roughly analysis of the surroundings.
claim. In rare cases the tax administration gets anonymous tips. This information is however not always presented in a straight forward manner but with the experience within the tax administration the information is often decodable. The annual report might also contain relevant data like transfer of client register and intangible property but also data regarding restructurings and closing of business branch. The tax administration does not randomly chose a company to audit, there needs to be something they believe is wrong or unclear for an audit to be made. In unclear cases the new routine is to ask for some additional information before auditing.

Industries can differ quite a lot from each other, some have difficulties in setting transfer prices, some make more mistakes and others are more active in "tax planning". So audits are usually done within a industry and with consideration taken to their specific problematic area. To figure out these problematic areas within the industries the Swedish tax administration do yet another “omvärldsanalys” to see if any other countries see structural industry problems. One example is the pharmaceutical industry, which the United States of America (USA) started auditing and Sweden later on followed. In those cases the tax administration looks at how the American tax administration has done their assessments.

When it comes to intra group transactions with low tax states that might work as an incitement for an audit but the Swedish tax administration says their focus is if the companies transfer price assessment is correct or wrong. Wrong assessments are also made in connection with transactions with high tax countries. However transfers to certain states are more likely priced incorrectly than others. For example Brazil is one of the most complicated transfer pricing states and countries like Ireland, Swiss, Malta, Cyprus, Singapore and Hong Kong are often used for tax planning, so this can work as an indicator which would increase the risk of tax audit. Correct tax in the correct state is a slogan used by the tax administration.

There are also cases where companies in Sweden have losses and an ideal tax strategy from the MNE group would be to increase the company's profits in Sweden and pay no taxes on the profits. This would indicate that the pricing is set correctly but there are certain tax administrations who might have an aggressive approach to transfer pricing and demanding a price which according to other countries would not be at arm's length. The mentioned countries in these were Germany, Italy and China. The point being that tax administrations
around the world differ and prices set that are not strictly beneficial out of an tax perspective do not automatically mean a correct pricing.

The money transferred also affects the decision to make an audit. For example the UK does not make an transfer pricing audit if the intra group transactions are under five million SEK and Sweden also has a guideline that is much lower but it is not officially stated. Since a transfer pricing tax audit process takes from four months to three years and within this time period causes double taxation that has to be cleared between the member states it is not proportionate to go after transactions of less value.

As a summary the Swedish tax administration chooses a tax subject by assessing an “omvärldsanalys” to identify certain risk areas connected to the transactions type and specific industries. In finding data regarding transfers of a certain transaction type the tax administration seek information in journals and the company's annual declarations. The Swedish tax administration also admitted that transactions with certain countries are more likely to be incoherent with the Swedish way of applying the arm's length principle. So a transaction with Brazil works as an incentive for the chance of an faulty transfer price but is not something certain. The tax administration stresses the importance of accurate tax paid in the accurate state and also the importance of proportionality between the transaction at hand with the costs and problematic with doing a transfer pricing audit.

### 4.4.3 Risk Assessment/Information Provided

In the annual report the tax administration mainly review the information provided in the footnotes, there is often information on major changes from the previous fiscal year within the company. With that said Mr. Good also stated that the operating profits are analyzed together with the changes in turnover, gross profits and if the company is a loss bearing operation. If the company is a loss bearing operation the tax administration often check what risks the company holds. If it is not bearing any risks it should not have a negative result.

When it comes to intangible properties like patents, knowhow etc the operating margin is not of great relevance instead it is the cash flow within the company to establish the amount of money derived from the property.

Regarding MNE groups compliance with the expressed documentation requirements in LSK it is said that the quality differs in relation to the size of the business. Small business
with few transactions often have individual structures whilst the larger ones who have con-

tultant firms like the big four (KPMG, PWC, EY, Deloitte) have a more expedient struc-

ture. Large companies like Volvo, Skania, Ericsson and H&M follow the OECD guidelines
to at least 95%. This simplifies the communication and understanding of the documenta-
tion since both parties "speak the same language". It is also understandable that small busi-
nesses are not analyzing/applying the OECD guidelines and for the Swedish tax authority
to demand a well-structured OECD evaluation would not be proportionate to administra-
tive burden at hand.

Mr. Good comments the fact that IRS has a goal to solve transfer pricing issues at the av-
erage of 24 months whilst Gothenburg had an average of 11 months last year (2013). He
believes that it is because of the Swedish attitude to the companies and what OECD
would call culture of compliance. The companies want to do right and the tax authority as-
essment is done with that in mind. The companies are not always prioritizing in the same
manner as the OECD and tax administration and when it comes to intangible properties
where there are no clear correct answers the risk of different approaches is high.

It is important to delimit the audit so that it remains comprehensible, efficient and justifi-
able. In big MNE groups there might be as many as 50 transfer pricing questions so Mr.
Good exemplifies three factors that help the delimitation procedure.

- Is the amount of the transaction adequate?
- Is the specific question provable?
- The level of complexity in relation to the other two factors

Point one and three go hand in hand with the proportionality test since it puts the compa-
ny as well as the tax administration in an unfavorable position in which unnecessary re-
sources might be spent. However point two is not based on the proportionality test but is
still the one according to Mr. Good that holds the most leverage. It might seem obvious
that the factor of proving ones claims is crucial nevertheless in such a complicated area
where the tax administration might very well know that something is not right with certain
transactions they cannot pursue it. There are times they pursue un-provable questions in
order to demonstrate the legal situation for both practitioners as well as media. With the
hopes of the process resulting with necessary changes within the system as such.
Since the decision making is fairly complicated and bears a lot of risk the tax administration has a selection group consisting of 6 persons from the three offices that determine which cases are chosen.

Concerning the EU TPD, Mr. Good says there are very few companies that have opted for the EU TPD that are active within Sweden. The EU TPD and OECD are much alike and require pretty much the same amount of information, therefore it is not directly noticeable since companies usually are not separating the documentation into a masterfile and country-specific file. The impacts of the EU TPD have not been evident at least not in Sweden.

### 4.4.4 Audit Process

After deciding that an audit is necessary the tax administration post a audit decision followed by a telephone call a couple of days later where a meeting is set up. There are always at least two representatives from the tax administrations at these meetings. The meeting generally takes place three to five weeks after the call so that the required people can coincide. Sometimes the people who hold the needed information for the transfer pricing audit are positioned abroad so the tax administration are keen on letting them converge for an efficient process. It also gives the tax administration an opportunity to prepare and immerse in the MNE group, which makes the questions and thereby the meeting more expedient. To understand how the company reasoned when setting the price is important, the price as such is the last thing looked upon when making an audit.

In the actual meeting the tax administration uses a form of funnel process where they start out by asking about the MNE group and thereafter work towards the main questions.

A complicated stage of performing the audit is to look at the contract and gather information from it to see if the price is set at arm's length. Contracts with third parties can be around 100 pages but in intra-group relations they can be as short as five pages. It is less detailed and a comparing transaction can be hard to find. Then one has to analyze the actual circumstances to see if they are in accordance with the agreement. Since the actual circumstance is the factor that decides whether the price is set at an arm's length or not, when these two differ the tax administrations make an functionality analysis to see where the money should be allocated.
OECD TPG are used as a guideline and even the proposition to chapter six is taken into consideration even if it is not final yet. It gives the tax administration support for the price they find reasonable.

Sharing of information:

At this time there is not a lot of information being shared between tax administrations and Mr. Good explains it with three points; (1) Mostly the information needed is provided from the companies, (2) In general receiving information from other tax administrations takes a long time, (3) We are lazy in that sense that we do not ask for information that could be valuable. He also states that more information exchange should make it easier to make an assessment and serve the tax administrations very well but it might also lead to larger burden for the MNE groups.

At this point there are only a few calls a year about different cases with other tax administrations. However the tax administrations send each other information on things they find suspicious that does not affect the taxation in their own country on a more regular basis.

The OECD TPG states that a MNE group should use the opportunity, that lays within providing documentation, to affect the tax administrations way of deciding the transfer price. The more complex transaction requires more documentation. In other words, the more information supporting your choice of price the larger the probability for a price to be set in accordance with the MNE groups view. Mr. Good however stated that it tends to be the opposite. Companies who provide a lot of information and do it correctly are definitely in this position but companies who provide a lot of information and get something wrong are in a worse situation than companies with insufficient amount of information provided. The complex transactions are especially affected since the risk of making a wrong assessment on one of the many steps is high. The tax administration has the upper hand of finding these faults and making an correct assessment since it does not have the same efficiency demands as the private industry usually has.

If two states have different views on the market price and there is a risk for double taxation the states need to have a so called MAP to decide which price is the correct market price. Mr. Good explained that the tax administrations meet up and discuss several cases together to negotiate. Obviously each member state wants more tax revenue but also good relations
with the other countries administrations which turns these meetings into negotiations where the tax administration has to lose some to win some. Fortunately the effected company gets respite with the tax, in the country with the lowest tax rate, during this negotiation period.

### 4.4.5 New Proposal

Mr. Good starts out by telling us that there is a group containing him and a few others who are evaluating the changes from 2007 and how these effect small and medium sized enterprises (SMEs). The current rules in TTPR 10§ and the annex gives MNE groups with transactions under a certain amount less documentation requirements. According to Mr. Good these rules are practically the same and not very favorable for small MNE groups. Nevertheless companies in Sweden are fairly well aware of the proportionality aspect in transfer pricing and thus present smaller documentation packages than one could say that the TTPR requires.

Mr. Good stresses that the Swedish tax administration have not yet given out a statement on their thoughts on the OECD draft and are still in the process of evaluating it. Also that the proposal has gotten to the place it is at the moment, very fast. He did say that he does not feel that there are any major changes and that it will affect the companies a lot more.

The Swedish tax administration does not believe in demanding a certain structure on the documentation, rather have an open communication regarding the MNE groups transactions to be certain that the accurate amount of tax is allocated to the correct state. It is however very positive with a documentation structure and creating documentation before the transaction because in those cases the companies have more time to contemplate whether the price is set at arm's length or not. One of the main reasons to have these documentation requirements is for the companies to truly evaluate their own transactions and therefore lessen the chance of setting a price that is inconsistent with the arm's length principle.

The APA is an instrument that is fairly new in Sweden and has a great financial burden on the companies, but the positive side of having the price secured and not having to worry about added tax and other fees can be worth it. Mr. Good sees an interesting area of transfer pricing that if made more efficient and less costly can be used in a larger extent in the future.

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136 See 4.4.3.
4.5 Summary

The Swedish transfer pricing regulations are based on the OECD TPG and it is stated in both preparatory work and case law. Sweden is one of the countries who has instated an expressed documentation requirement through legislation, meaning that it is stated in LSK that companies doing internal cross-border transactions shall have documentation regarding their transactions. The expressed documentation requirements with guidance on what the documentation shall consist of is fairly new and was taken into Swedish legislation 2007. The right to further clarify what information should be provided has been delegated to the government who in their turn delegated it onward to the Swedish tax administration. In theory the requirements are very much alike the requirements recommended by the OECD TPG. A difference is that companies with smaller amount of internal transactions need to provide less documentation, creating a lower burden for smaller entities.

To get an insight in the practical angle of transfer pricing an interview was held with Mr. Good, an employee of the Swedish tax administration who solely works with transfer pricing. The proportionality of the transfer pricing assessment was continuously brought up during the interview as well as the fact that the Swedish tax administration focuses on the right amount of tax in the correct state. Mr. Good also clearly divided the actual assessment process of the tax administrations into:

- Identifying the tax object,
- Making a risk assessment,
- The actual audit process.

When identifying the tax object the tax administrations look in certain risk areas, for example dealings with some specific countries and the pharmaceutical industry. The information is sought through journals, companies annual declaration etc. The risk assessment is done by analyzing the operating profits, with the changes in turnover, gross profits and if the company is a loss bearing operation. The audit process is made by setting up meetings with the MNE group at hand to get insight in their company as well as their way of pricing their internal transactions.

During the interview the area of sharing information between tax administrations in other countries was discussed and explained the lack of it. Some areas are more problematic and since the burden of proof lays on the tax administration they only pursue cases they can
prove which in some way benefits companies who present less documentation against those who present sufficient but have done their evaluation incorrectly.

Mr. Good did not see an increase of the EU TPD structure in the last couple of years and stated that since the tax administration did not have an official statement regarding the discussion draft yet he could only assist with his own opinion. He stated that he believes that the burden of the companies will increase and that for him the important is not if the documentation follows a certain structure but if the companies have contemplated if their price is set in accordance with the arm's length principle. He does also state that a clear structure might lead to companies considering their prices on a more detailed level.

4.6 Analysis

The interview worked as an tool for understanding the practical use of the documentation requirements as well as the level of complexity the parties involved have to deal with. The area feels complex and somewhat unsorted which results in several improvable parts. One thing that is of big interest for this thesis is the expressed level of disparity between countries transfer pricing assessments. The Swedish tax administration viewed the pricing method that Germany, Italy and China apply as aggressive/ assertive which can lead to the wrong transfer price. A valid question to ask is if the MNE groups are aware of these differences and how the tax administrations view each other? Are they aware that having internal group transactions with specific countries leads to a higher risk of being audited? Does it affect what countries you trade with? Not just because of their lower tax rates but for how the country deals with transfer pricing issues.

One tax administrations view of another tax administration might lead to double taxation and the current protective mechanism is the MAP which leads to an respite with the tax but the question at hand is often solved through negotiation between the member states. Since the tax administrations meet to negotiate several cases at once it is also valid to ask if the negotiation expertise gets a huge impact where some cases are given one country and others the other to keep good relations between the states. It would be very problematic for the companies to know if they are applying the right transfer pricing policies if the right amount of tax is not taxed in the correct country but based on bilateral relations between the involved states. The companies and states have a harder time to assess a praxis that should be followed and the assessments are made on a subjective and individual level. Of course this is not a problem in every case neither is it applicable in every case, the tax ad-
ministrations probably make a similar assessment most of the times but it is nevertheless something of noteworthy.

It seems to comprehensible to get a functioning transfer pricing area within one country but a lot more problematic when dealings with other countries is necessary. Cultural and psychological factors which are subjects that are not within the purpose of this thesis can have a great impact on the transfer price, which is problematic but interesting. This makes the current system feel somewhat unpredictable.

The proportionality angle within transfer pricing is clearly shown and debated in every decision that the Swedish tax administration make. The fact that entities within a MNE group can have transactions of goods up to the amount of 27 972 000 million SEK\textsuperscript{137} to qualify for providing less documentation than the full amount saves companies of smaller proportion from great administrative burdens. The thought behind this goes well with the proportionality test that is stressed in the OECD TPG. According to the authors it might however separate companies that sell goods of great value from companies who deal in goods of less value since MNE groups dealing with goods of less value might need to sell great numbers in order to within the range of the full documentation requirements whilst a big company might only need to sell 2 items for them to qualify for that. According to Mr. Good these simplifications are not enough and the burden is almost the same. Which makes the provision counteract its own purpose. Mr. Good believes that these requirements need to be even more simplified and less burdensome.

On the positive side it is also stated that the groups of smaller dimensions often provide less information than required, which shows that even smaller companies are aware of the proportionality principle. It does nevertheless put the current regulation under scrutiny and its purpose is questionable if companies aren't following the TTRP structure. The proportionality angle is also shown through the tax administrations open communication with both companies and the Swedish tax administration, they recognize the complexity, risk of wrongfully applying the rules and have work under the premises that companies follow the culture of compliance.

Creating more strict rules for companies to follow will not consequently lead to less companies doing the assessment on complex transactions correctly. The authors believe that

\textsuperscript{137} See 4.3.1, 44 400*630.
the proportionality process applied today is necessary since the transactions can be very complex or the other way around. Something that could be of use is an increased explanation of what this proportionality test really is. At this moment it is the burden and costs of the companies in relation to the need of the information for the tax administrations. The OECD TPG does give examples but not a clear scheme which would simplify the application of the principle for both parties. A more clear proportionality test like the one provided by EU might be of value. Some factors to take into consideration could be

- The value of the transaction
- The level of complexity of both transaction and MNE group
- The necessity of the information to make an assessment
- The accessibility of the information
- The cost of providing such documentation

The questions can be found in OECD TPG but not in the form of a structured test. The authors believe that the transfer pricing assessment will be less subjective if this test is applied in every case and it will be easier to provide clearer guidance in relation to previous cases. The value is important to value the impact it will have on the tax base within the states and thereby assess the proportionality of the required documentation. How the group is structured and how complex the transaction is makes for a good assessment regarding the risks of the transfer pricing assessment being done wrong and can also help detect other transfer pricing issues that the companies should be made aware of. The three final points should all be viewed together since both administrations as well as MNE groups need to evaluate how they are planning to prove the actual facts of the relevant transaction. A clear assessment of these questions creates a more direct communication between the tax administrations and MNE groups because of the fact that the MNE groups shows that they have clearly thought of the transfer pricing aspect of the transaction.

Also all the tax administrations should use similar grounds for doing an audit, for example the Swedish tax administrations factors that Mr. Good brought up make a lot of sense and should be stated in the guidelines:

- Is the amount of the transaction adequate?
- Is the specific question provable?
- The level of complexity in relation to the other two factors
There are issues with the level of subjectivity within this legal area but the level of complexity of many transactions makes the individual assessment essential for the area of transfer pricing. That is why the authors believe that an potential harmonization must be easy to follow, clear and mainly focus on the tax authority prioritizing the same things so that the companies know clearly what their risk areas are and how they should present their documentation.

The burden of proof is also something that is counteracting the purpose of supplying sufficient amount of documentation. According to the OECD TPG companies who provide a lot of information have a bigger chance of affecting the pricing but the Swedish tax administration also points out that the more a company provides the bigger the risk that they will find something wrong that they can prove. Since the burden of proof lays at the tax administration they need the sufficient amount of documentation to be able to prove the pricing is incorrect. The MNE group is supposed to document sufficient amount of documentation for the tax administrations to make this assessment but what is sufficient amount of information in a highly complex transaction? This question is yet to be answered clearly. The authors find it worrying that providing a lot of information can lead to negative tax consequences and believe that this is something that needs to be solved in a different way. Perhaps by clarifying what insufficient documentation is or open up for a dialog that does not bear the costly burden of APAs for companies with transactions which are intricate.

The delimitation process is something that is interesting. It shows that the area is controlled by the proportionality process as well as an economical process from the tax administration. The tax administration works with resources like so many companies and wasting their or the companies time is not appropriate. It also makes the discussion regarding the burden of proof interesting. Since the burden lays with the tax administration they cannot concentrate on situations that they think are wrong but must focus on what they can prove/know is wrong. The authors believe that having it the other way around could become too much of a burden for the companies and almost put too much power in the hands of the tax administration. The tax administration could in that case make more transfer pricing audits but at a stage when transfer pricing is not something that all tax payers are aware on a detail basis it would become unreasonably burdensome.

For the tax administration the country by country reporting seems to be of big assistance but Mr. Good does say that he believes that the burden on the companies will increase.
There seems to be an openness for a larger extent of information exchange but the tools and routines are not yet in place. The authors believe that an efficient information exchange system would lead to an increased collaboration and easier audits for the tax administrations. By prioritizing in the same way and working in a larger extent together the views on how other countries work become less prejudiced and more based on facts. The dissimilarities might even lead to several tax administration evolving their way of applying the transfer pricing rules and procedures. For example the Swedish tax administration used the skillful American way of auditing the pharmaceutical industry which shows that collaboration between states can benefit tax administrations all over the world. The burden of the companies might increase initially but as the system evolves these costs will be worth the predictability and security within the area. The current system that works with different sets of rules should also lead to higher compliance costs for legal guidance and an expanded collaboration between states should lessen this burden in the long run.
5 The White Paper

5.1 Background

This and the next chapter presents the background and content to the suggested change of the OECD guidelines. First the origin of the suggestion is presented followed by an examination of the two major papers on the subject, those being a white paper published in the summer of 2013 and a discussion draft published early 2014. The contents of each paper is explained and are after that compared to each other as well as the current guidelines. Major questions brought up are also presented.

With increased global economy there is an increased need of international cooperation regarding economic development. As stated by the G20 leaders in 2012, "Despite the challenges we all face domestically, we have agreed that multilateralism is of even greater importance in the current climate, and remains our best asset to solve the global economy's difficulties." Similar concerns were given at the G8 meeting of 2013 where the meeting urged OECD to develop the guidelines for transfer pricing documentation. As stated in the communication to the OECD,

"Comprehensive and relevant information on the financial position of multinational enterprises aids all tax administrations effectively to identify and assess tax risks. The information would be of greatest use to tax authorities, including those of developing countries, if it were presented in a standardized format focusing on high level information on the global allocation of profits and taxes paid. We call on the OECD to develop a common template for country-by-country reporting to tax authorities by major multinational enterprises, taking account of concerns regarding non-cooperative jurisdictions. This will improve the flow of information between multinational enterprises and tax authorities in the countries in which multinationals operate to enhance transparency and improve risk assessment."

On 19 July 2013 OECD published a plan against tax base erosion, "Action Plan on Base Erosion and Profit Shifting", or in short BEPS. The plan contains 15 actions the OECD suggest to develop the area and prevent tax erosion and unwanted profit shifting. Action 13 in the plan is to re-examine transfer pricing documentation to enhance transparency for tax administrations. Following its plan, 30 July 2013 the OECD published a white paper

139 White paper p 2.
140 Chapter 3, BEPS Action Plan.
141 BEPS Action Plan p 23.
regarding transfer pricing documentation.\textsuperscript{142} The white paper surveys the current state of transfer pricing documentation and makes suggestions on how to develop the transfer pricing documentation rules to make compliance simpler, while giving tax authorities information needed to do transfer pricing risk assessments and transfer pricing audits.\textsuperscript{143}

Following the white paper, in a discussion draft published 30 January 2014 the OECD suggested to completely replace chapter V of the OECD transfer pricing guidelines with the revised version in the discussion draft.\textsuperscript{144}

\textbf{5.1.1 Introduction}

In the introduction of the white paper published in July 2013 it is stressed that even if transfer pricing is of global concern, documentation requirements is and will continue to be governed by local law in individual countries. But as transfer pricing is a global concern, transfer pricing enforcement and compliance rules must be designed with that in mind.\textsuperscript{145}

When the current guidelines were created over 15 years ago there was less experience with transfer pricing documentation rules. The position of the OECD is that the guidance given in the current OECD TPG is not sufficient any longer.\textsuperscript{146}

As the OECD states there has been several efforts to create an international standard description of documentation to be used for demonstrating the use of the arm’s length principle. However, none of those initiatives have succeeded, leaving a need for such a standard. The white paper published in 2013 aims to survey the current state of transfer pricing documentation, consider the purpose and objectives of those rules and makes suggestions on how to modify those rules.\textsuperscript{147}

\textsuperscript{142} White paper on transfer pricing documentation.

\textsuperscript{143} White paper p 1.

\textsuperscript{144} Draft p 1.

\textsuperscript{145} White paper para 2.

\textsuperscript{146} White paper para 3.

\textsuperscript{147} White paper para 4-5.
5.1.2 **Domestic Documentation Regimes**

The white paper divides transfer pricing documentation rules into two groups, first being the rules of individual countries and the second being rules and guidelines developed by international organizations.148

The OECD list and comment on eight different important features of current legislation identified by WP6 in a review in 2011 and 2012.149 Here labeled a-h these features are:

- a) increasing number of countries with transfer pricing documentation rules,
- b) transfer pricing is addressed at a domestic level,
- c) transfer pricing documentation requirements vary widely among countries,
- d) one-sided analysis of the controlled transaction is common,
- e) documentation does not always yield a complete understanding of the business,
- f) significant divergences exist in the nature and detail of country transfer pricing documentation requirements,
- g) purposes served by transfer pricing documentation are not always clear, and
- h) divergent practices regarding timing of documentation closures.150

With increasing number of countries with transfer pricing documentation rules in place it is clear that such rules play a key role in the administration transfer pricing rules and is of growing international importance. Such rules are usually put into place by either legislation or recommending companies to have transfer pricing documentation.151

Transfer pricing documentation is addressed at a domestic level. Even if transfer pricing is of international concern the domestic rules are designed with a domestic tax enforcement in mind. This can lead to discrepancy between the focus of domestic transfer pricing rules and the activities of MNEs. Rules being focused on a national or bilateral situation, while an MNE may have a much more global focus. A result of this one-sided focus from tax en-

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148 White paper para 6-7.
149 White paper para 8.
150 White paper para 9-16.
151 White paper para 9.
forcements is that the taxpayer often is required to comply with several rules, leading to increased burden and cost for the taxpayer.\textsuperscript{152}

Transfer pricing documentation requirements vary widely among countries, specifically it varies in how much detail is put into the requirements. There are countries that have a general requirement to submit documentation, others have a more detailed guidance on how to do this, and some have very specific rules dictating formats. Where there are formats these vary between countries.\textsuperscript{153}

One sided analysis of the controlled transaction is common. Most countries has a one sided approach, focus being on the domestic tax payer and tax treatment. Little or no interest is taken in the financial result of the counterparties.\textsuperscript{154}

Documentation does not always yield a complete understanding of the global business. While legal and organizational structure is most often asked for, it is uncommon to ask for information on global business, transactions between other MNE members, supply chains or APAs and other similar rulings.\textsuperscript{155}

Significant diverges exist in the nature and detail of country transfer pricing documentation requirements. Even if there are certain categories of information in common between countries, the type and detail of the information varies from "high level" to "very exhaustive".\textsuperscript{156}

Purposes served by transfer pricing documentations are not always clear. Most transfer pricing rule-sets does not specify their reasons. While many countries focus on getting general information on tax payers and its transfer pricing position, other countries obtain all information that might be relevant in a transfer pricing audit. There are few rule-sets that explicitly put emphasis on information required for a transfer pricing risk assessment.\textsuperscript{157}

\textsuperscript{152} White paper para 10.
\textsuperscript{153} White paper para 11.
\textsuperscript{154} White paper para 12.
\textsuperscript{155} White paper para 13.
\textsuperscript{156} White paper para 14.
\textsuperscript{157} White paper para 15.
The practices regarding timing of documentation disclosures are divergent. In many countries the tax administrations ask for information available at the time of filing the tax return. Other countries ask for information available at the time of the transfer pricing audit. This difference makes it hard on the tax payer to provide the tax authority the right information at the right time.\footnote{White paper para 16.}

5.1.3 **Documentation Guidance By International Organizations**

As mentioned above the white paper divides documentation rules into domestic rules of individual countries and those guidelines presented by international organizations. Just as the white paper notices problems with domestic legislation, international guidelines are not without problems and are also brought up in the white paper.\footnote{White paper para 17-44.}

Some of the guidelines mentioned in this chapter is mentioned earlier in the thesis. Even if there is some repetition, it can be stressed that this is the opinion of the white paper, and in that indirectly the one of the OECD. As such some information in this chapter is used as basis for the white paper opinion on the current situation and is necessary to include.

The international guidelines were all created for the purpose of easing the difficulties that MNE groups might face in complying with the increasing amount of documentation legislation. The original aim was to provide guidance in order to save tax payers from the potential problems of having to deal with multiple documentation standards.\footnote{White paper para 17.}

The white paper brings up four different international guidelines created for documentation rules. These are the OECD TPG, the EUTPD, the PATA Documentation Package and the International Chamber of Commerce Proposals.

Concerning the documentation guidelines of Chapter V of the OECD TPG it is said that the emphasis is made on reasonableness and cooperation between taxpayer and tax administration.\footnote{White paper para 19.} The current OECD guidelines give no exhaustive list on what specific documents should be produced, but only outlines what could be relevant. Neither is this outline to be seen as minimum requirements.\footnote{White paper para 20.}

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\footnote{White paper para 16.}
\footnote{White paper para 17-44.}
\footnote{White paper para 17.}
\footnote{White paper para 19.}
\footnote{White paper para 20.}
be that the current OECD guidelines give no guidance regarding the link between transfer pricing documentation and the burden of proof. The guidelines also does not differentiate on documents needed to do a transfer pricing risk assessment and full transfer pricing audit.\textsuperscript{163}

The European Union Guidance on Transfer Pricing Documentation aim at standardizing the documents that MNE groups must provide tax authorities while keeping within the OECD guidelines.\textsuperscript{164} The EU TPD is soft law meant to be implemented by the Member States and is optional to use for MNEs. The EU TPD enables the MNEs to use of the same documentation in all of the Member States.\textsuperscript{165} It is composed of two main elements, the master file and the country specific file. Besides the information in these two files tax authorities are able to get more information, but only on specific request or during a transfer pricing audit.\textsuperscript{166}

The key features of the masterfile are common information relevant for all Member States, to provide a blueprint of the MNE and its transfer pricing system while following economic reality, the masterfile is available to all Member States involved and provides information on the MNE such as business strategy, information on controlled transactions and comparisons, information on the MNEs intangibles and information on established CCAs, APAs and other such rulings.\textsuperscript{167}

The key features of the country specific file is some standard documents for each Member State involved. Its available to the specific Member State it handles and contain information relevant to that Member State only such as local bus strategy, local transfer pricing methods, related comparability analysis and how transfer pricing is applied.\textsuperscript{168}

\begin{flushleft}
\textsuperscript{163} White paper para 21. \\
\textsuperscript{164} White paper para 22. \\
\textsuperscript{165} White paper para 23. \\
\textsuperscript{166} White paper para 24. \\
\textsuperscript{167} White paper para 25. \\
\textsuperscript{168} White paper para 26.
\end{flushleft}
Together the two files contain all documentation a Member States tax administration should need and due to the same information is available to all involved tax administration offers a greater transparency.\textsuperscript{169}

Even though the EU TPD contain many advantages, a survey made in 2009 showed little use of the system. Some publications suggest that the flexibility of the implementation in different Member states has created uncertainty. Due to variability of local rules and difference in enforcement the masterfile is less useful than it could be. Furthermore, some tax payers might not like the idea of revealing all their APAs and similar rulings. Also, the EU TPD does not protect MNEs against follow-up question or being asked for more documentation nor against adjustments. It has also been said that due to the wide spread of the information available there is a higher risk of being audited.\textsuperscript{170}

It is speculated that maybe the survey was made to early, just a few years after its release. It can also be noted that some taxpayers make use of the EUTPD without officially opting into it. The future will tell if the EUTPD will be liked outside of the EU, considering it is less detailed and has less requirements compared to some non-EU countries.\textsuperscript{171}

The PATA Documentation Package offers one single voluntarily rule set for MNEs in its four member countries Australia, Canada, Japan and the US.\textsuperscript{172} In this system the MNEs need to make "reasonable efforts" to establish correct prices, maintain documentation and provide documentation upon request by tax authorities. If an MNE fulfill these obligations it is protected by agreement.\textsuperscript{173} The PATA agreement gives an exhaustive list covering 48 specific areas of documentation, but tax authorities are free to request additional information.\textsuperscript{174} The white paper list some concerns from businesses. One such concern being that consensus between the member countries is basically reached by adding everyone's rules on top of each other, making the PATA a heavier rule set than any of the single member countries. There is no notion of relevance so the pressure on MNEs is not really eased. Neither does the agreement protect against transfer pricing adjustments and assessed

\textsuperscript{169} White paper para 27.
\textsuperscript{170} White paper para 28.
\textsuperscript{171} White paper para 29-30.
\textsuperscript{172} White paper para 31-32.
\textsuperscript{173} White paper para 33.
\textsuperscript{174} White paper para 34.
interest. Also, the concept of reasonable efforts is undefined, it is therefore up to each member country to define its meaning, leading to inconsistency.\textsuperscript{175}

In 2003 ICC made a statement on transfer pricing documentation. It is a proposal of a single set of rules for all involved tax administrations. The proposal is based on the information available in bookkeeping and management reports and common documentation rules from national legislations. When fulfilled, the MNEs have no further liability or no further burden of proof. The ICC proposal is not developed into any recognized system.\textsuperscript{176}

\textbf{5.1.4 Discussions With Selected Business Representatives}

Discussions have been made with members of BIAC to identify problems from a business perspective.\textsuperscript{177}

With quantity of transfer pricing requirements having increased by a lot, the detailed and massive constant change in format gives extra work for little to no benefits. Especially the minor differences in formats between countries give lots of extra work for the taxpayers. The result is transfer pricing studies so massive that local tax auditors do not understand them. There are mixed opinions on the drafts proposed two-tier system within BIAC, some think it will result in overhead savings, while others believe the workload will increase. Opinions have been voiced that there is no need to give total corporate overview when there are several lines of businesses within an MNE group. It is also said that a new comparable search every year adds little value. A three to four year period is more reasonable and save taxpayers a lot in term of compliance costs. Another issue mentioned is that many governments will not accept documentation without checking facts or even requiring audits from third parties to validate the facts of the documentation.\textsuperscript{178}

\textbf{5.1.5 Conclusion Regarding The Current Documentation Environment}

The existing documentation requirements vary significantly between countries. The fact that every country has its own specific requirements make it difficult to streamline compliance. The focus on the local situation from tax authorities makes it hard for them to get the

\textsuperscript{175} White paper para 35.
\textsuperscript{176} White paper para 36-38.
\textsuperscript{177} White paper para 39.
\textsuperscript{178} White paper para 40.
bigger picture. With this local perspective there is a risk that focus will land on smaller problems and bigger problems will get passed by.\textsuperscript{179}

International efforts on the area has not been effective. Although some efforts have been promising, lack of flexibility and universal application has made them not being widely accepted. Some other efforts has resulted in compiling demands on top of each other, creating no simplification and are as such not used by taxpayers.\textsuperscript{180}

With growing compliance burden due to more rules, costs are rising for taxpayers in an area only to avoid penalty costs. Ad hoc materiality and risk screens are used largely as a survival tool, due to the burden of the current rules. With these factors in mind, the OECD questions if the current transfer pricing rules really fulfill their intended purpose. It seems there is room for improvement.\textsuperscript{181}

5.1.6 Analysis

There has been many attempts of international standards or guidelines within transfer pricing, arguably the OECD TPG being the most successful to date. Major countries agree that there are issues with the current situation, as do the OECD and businesses around the world.

The white paper divide rules and guidelines into two groups, national legislation and international guidelines, which is somewhat misleading. The aim of national legislations over the world is likely to be close to each other, namely protection of the local tax base. Different international guidelines or systems, however, are made on very different grounds. The EU TPD has a European focus in mind, as is a full set of optional rules. The OECD TPG is likely to have a somewhat neutral mindset but compared to the EU TPD it is not a set of rules but rather recommendations, while PATA is created in a cooperation between the specific countries. The vast amount of different rules and guidelines is likely a problem, as different organizations have different aims.

That an increasing amount of countries have documentation requirements is not in itself a problem, neither is it a problem that international rules and guidelines are developed. With more jurisdictions covered with such rules, the potential for abuse diminishes. Other prob-

\textsuperscript{179} White paper para 41.
\textsuperscript{180} White paper para 42.
\textsuperscript{181} White paper para 43-44.
lems arise however. With more and more rules interacting the more conflicts arise. Especially the fact that an increasing amount of different systems to obey for taxpayers increase the cost of compliance further. The fact that most national legislations have a one sided focus on the domestic level is a clear indication that protection of its tax base comes in first, leaving taxpayers issues at second hand, if even addressed at all.

As it is stated in the white paper, a stated purpose of the rules are not always done. This is not a mechanical issue, to observe and follow a rule, you do not need to know its purpose. However, if there is an aim to create an international standard, a commonly agreed on and stated goal for those rules are needed for both efficient development and to have any hope to reaching any form of consensus. When creating such rules it seems natural to observe what problems previous attempts have had. As already stated, the OECD TPG is arguably the most successful transfer pricing guidelines. Despite its success the national rules taking inspiration from the OECD are quite diverse. This is probably due to the quite open language of the OECD TPG. With the loose language differences should be expected, but it is nonetheless observed as a problem today. The usage of the EUTPD could be claimed to show the same thing. With claims of the EUTPD being used sparsely due to differences in implementation, it gives to show that a voluntarily system with much diversity in rules between jurisdictions will not be used. An overly flexible system or wording will likely not be very successful. A overly burdensome system is likely to not be used either. PATA, being basically all members rules stacked on top of each other is virtually unused due to being too burdensome.

In summary, there is a need for change. The diverse amount of rules creates a burden on the taxpayer. A new system has to find a balance between not being overly flexible as the current OECD guidelines are, and not as burdensome and heavy as for example PATA.

5.2 Purposes Of Transfer Pricing Documentation Requirements

5.2.1 Three Main Purposes

If improvements are to be made there is a need to define the purpose of transfer pricing documentation. By not having common ground the result will be different rules. The OECD present three different reasons in the white paper for requiring transfer pricing documentation. These are:
- "To provide governments with the information necessary to conduct an informed transfer pricing risk assessment at the commencement of a tax audit;
- To assure that taxpayers have given appropriate consideration to transfer pricing requirements in establishing prices and other conditions for related party transactions and in reporting the income derived from such transactions in their tax returns;
- To provide governments with all of the information that they require in order to conduct an appropriately thorough audit of the transfer pricing practices of entities subject to tax in their jurisdiction."

5.2.2 Transfer Pricing Risk Assessment

The ableness to make risk assessments and managing transfer pricing rules are at heart for tax authorities. As said by the OECD in 2012, "effective risk identification and assessment are the key steps which enable tax administrations to select the right cases for transfer pricing audits or inquiries". It is of importance for tax administrations to know when an audit is warranted. As also said by the OECD in 2012, taxpayers notice that “where audits and enquiries are not based on effective risk assessment cases last much longer, and all too often the most significant transfer pricing issues are missed.” To effectively identify risks is the key for fast and low-cost audits. A proper risk assessment require the right information. There are many possible sources of information, transfer pricing documentation being one of them. There are various methods developed in different countries to identify transfer pricing risks that can be used. The white paper lists some of these methods:

- Transfer pricing forms to be filed at annual tax return. In some countries taxpayers need to supplement the tax return by adding information on transfer pricing matters. This generally includes informing on the presence of controlled transactions, what pricing method is used, with whom such transactions are made and if there is documentation to support the pricing. Some countries require much more detailed information already at this stage.

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182 White paper para 45-46.
184 Ibid.
185 White paper para 47-49.
• Transfer pricing questionnaires. These are targeted questionnaires that are sometimes mandatory, but can sometimes be done in the framework of risk assessment after an initial review of the tax return. Sometimes these are a general compliance, other times they are targeted initiatives in certain areas or fields of industry.

• Cooperative approaches with tax authorities. In many countries there are initiatives to create a dialogue between taxpayers and tax authorities. By conversation issues are found faster and easier, transparency is increased and there is less delay. Such systems also give the taxpayer a chance to explain their system and method at an early stage.

• General transfer pricing documentation requirements. Most countries has adopted transfer pricing documentation rules, where taxpayers are obligated to provide evidence that their controlled transactions are satisfying the arm's length principle.\textsuperscript{186}

Vocabulary creates a problem, as the same terms are used in different contexts. The meaning of the word documentation can be very different depending on jurisdiction, creating some confusion. However, no matter the different starting points for different tax authorities, it is clear that they are all in need of an ability and method of to perform an informed risk assessment.\textsuperscript{187}

5.2.3 Taxpayers Assessment Of Its Compliance

When transfer pricing rules were first developed in the US, there were some concerns that taxpayers might report aggressive numbers and only develop a reasoning for those prices they were challenged, an after-the-fact explanation. As it was on the taxpayer to prove the government's position arbitrary, it gave rise to strategies of keeping information as it was advantageous for the taxpayer if they were challenged. By demanding transfer pricing before challenges are issued the taxpayer need to articulate its reasoning beforehand, helping to create a culture of compliance. The creation of a culture of compliance is aided in two ways. Firstly as mentioned taxpayers are forced to demonstrate their reasoning at the time of the transaction, or at least not later than the filing of the tax return. Secondly penalties

\textsuperscript{186} White paper para 49.

\textsuperscript{187} White paper para 50.
are often put into place to reward compliance, as compliance often grants immunity except for pricing adjustments.\textsuperscript{188}

While the creation of a culture of compliance is a good idea, both taxpayers and tax authorities report that it often becomes a process of trying to avoid penalties, leading to minimum compliance. Tax authorities report that studies made by consultants often have a formal cut-and-paste feeling over them, and consultants claim that they often cannot access enough information due to cost considerations. In larger companies it is not uncommon to be asked for comparables supporting certain numbers. Companies claim it is simply too costly and time demanding to comply globally. So while a culture of compliance is in theory a good idea, things such as time constraints and high costs might undermine that objective, leading to a culture of minimal effort.\textsuperscript{189}

\textbf{5.2.4 Provision Of Information Necessary For Audit}

Another purpose of transfer pricing documentation is to provide tax authorities with enough information to conduct a thorough transfer pricing audit. Such audits are fact-intensive and contain different evaluations of comparability of transactions and markets. It is of course vital for tax authorities to have access to adequate information to examine the compliance of transfer pricing rules. As most of this information comes from the taxpayer, governments often claim the taxpayer to be in an advantage in an audit. When a risk assessment indicates that an audit is needed, the tax authorities is in need of a large amount of information as soon as possible from the taxpayer. Often the information is available in the transfer pricing documentation, but not always. Therefore there should always be an option for the tax authority to ask for more information from the taxpayer. Rules regarding this must give the taxpayer enough time to comply, to not impose an unreasonable burden.\textsuperscript{190}

Often it is the case that documents tax authorities need for an audit is in the possession of MNE members outside of the country. Tax authorities need ability to obtain such information. Additionally, when creating rules one must consider the difference of burden of proof in different jurisdictions. Depending on where the burden of proof lies, tax authori-

\textsuperscript{188} White paper para 51-54.
\textsuperscript{189} White paper para 55-56.
\textsuperscript{190} White paper para 57-60.
ties might have different needs in terms of what is needed for risk assessments and audits.\textsuperscript{191}

### 5.2.5 Conclusions Regarding Purposes Of Transfer Pricing Documentation

At least three different valid reasons for having transfer pricing documentation requirements are identified. All of these are important to consider. For tax authorities it is important to have access to information to be able to do a proper risk assessment, and thereby also know when an audit is needed. It is also important that taxpayers need to evaluate their transfer pricing position in a timely manner. Relevant questions are therefore if it's possible to design rules to give enough information to do a proper risk assessment while still providing for an audit if needed. If the initial document is simplified in order to focus on the risk assessment, will taxpayers self assessment improve as compliance burdens are less? These are important factors to consider. Also, when simplifying for the taxpayer care must be taken to not impair tax authorities ability to perform an audit at a later stage.\textsuperscript{192}

Those conclusions combined with the conclusions present in 5.1.5 above leads to the white paper suggestion of a two-tiered documentation approach.\textsuperscript{193}

### 5.2.6 Analysis

The three different reasons for documentation requirements the OECD list are important for several reasons. Reason number one, it gives common ground on why the rules are needed, and thereby also what purpose they serve. This is important because without a common understanding to why rules are made, their effectiveness is severely hampered. A rule without a clear purpose has little chance of achieving something. Also, without a common understanding on why the rules are there, different interpretations of the system and the reasoning of the OECD is inevitable.

The different reasons also appeal to different parties that have an interest in the documentation requirements. The only reason of the three that by nature appeal only to tax authorities are the full audit one. Reason number two, compliance, is basically a reasoning to why a culture of compliance should be, and encourages the idea of incentives to achieve this.

\textsuperscript{191} White paper para 61-62.

\textsuperscript{192} White paper para 63-66.

\textsuperscript{193} White paper para 67.
Reason number one, while focusing on the tax authorities need for an efficient risk assessment, gives a greater opportunity for taxpayers to avoid full audits, since a risk free assessment should normally mean no full audit, and thereby no costs normally associated with those.

In summary, the reasons given are important both to have a common ground on what the rules should achieve, and to motivate all parties to participate in a positive manner.

5.3 The Tiered Approach

5.3.1 A New System

Following the background presented above, the OECD suggests a new format for transfer pricing documentation in the white paper. The focus of this section in the white paper is to describe what tax administrations is in most need of when doing a transfer pricing risk assessment. This is the basis for the suggestion follow in the white paper.

OECD have identified nine features that might indicate the existence of a transfer pricing risk. These were first published in a publication titled "Dealing Effectively with the Challenges of Transfer Pricing", and some, but not all, of these features is listed in the white paper. The ones listed in the white paper are:

- "Significant transactions with, and income allocated to, related parties in low tax jurisdictions;"
- Transfers of intangibles to related parties;
- Business restructurings;
- The existence of specific types of related party payments that have the potential to erode tax base, including payments of interest, insurance premiums and royalties;
- Year on year loss making;
- Poor or non-existent documentation of related party transactions and their results;
- Excessive debt."

Why two was omitted in the white paper is not mentioned, and is hard to draw any conclusions on. The two omitted features can be found in the original document and are:

194 White paper para 68-84.
195 White paper para 68.
196 White paper para 69.
• Poor results; (results not consistent with the industry and/or the functions covered)
• Effective Tax Rate. (a big variation between the group effective tax rate and that of the subject)\textsuperscript{197}

Since these features are identified as the major ones, it seems appropriate to focus documentation requirements on information relating to those. The white paper lists five bullet points of information the OECD deems needed for a quick understanding in the above mentioned seven important features.

• "Identification of material cross border transactions between associated enterprises, including material payments for goods, services, intangibles, and interest flows."
• Identification of recent business restructuring transactions and transfers of intangibles.
• Information regarding the levels of corporate debt and interest expense in relevant countries.
• Information regarding the MNE's global transfer pricing policies and the financial results of applying those transfer pricing policies. It would especially include a description of where the group important intangibles are held. It would also include the identification of the MNE Group's existing APA and ruling agreements related to income allocation with various countries.
• The taxpayer's explanation of how the material transfer pricing arrangements comply with the arm's length principle and local transfer pricing rules.\textsuperscript{198}

It is expressed that just these above features is not enough on their own. A more complete understanding of the larger picture is also needed, and this is normally obtained through the country focused documentation requirements. The reason transfer pricing risks come into existence is most often due to a company seek to move income from a heavily taxed jurisdiction to a less taxed one. This is why a broader view, outside the country border, is needed to fully assess transfer pricing risks.\textsuperscript{199}

Without unnecessary burden companies should be able to report such things as management accounts, income statements, balance sheets and tax returns on an individual country basis. Even if that information by itself is not enough for a detailed transfer pricing analysis, it is helpful in a risk assessment. A MNE with a high portion of its income in a low tax jurisdiction despite most assets being located in a high tax jurisdiction might warrant more

\textsuperscript{197} Dealing Effectively with the Challenges of Transfer Pricing, page 25.

\textsuperscript{198} White paper para 70.

\textsuperscript{199} White paper para 71.
suspicion and thus in need of an audit, compared to an MNE with its income more in line with its asset locations.\textsuperscript{200}

According to the OECD, the two-tier system created in the EU TPD has a great potential to simplify transfer pricing documentation compliance. If all information relevant for all parts of an MNE is put into one file it is easily shared access the MNE. Examples of such information would be overall company descriptions, functional analysis, information on group income, tax rates, debt structure, information on restructurings and ownership of intangibles. Assuming all parts of an MNE has access to such a file it would only need to add information needed in its local jurisdiction, such as local comparables and local financial data.\textsuperscript{201}

Common mechanical issues existing in some countries transfer pricing rules are lifted as a potential problem in the white paper. They are labeled as making transfer pricing documentation preparation more difficult than needed. In short they are listed as:

- Certification of documentation by an outside auditor,
- Mandatory use of consulting firms,
- Use of local or regional comparables,
- Translation and,
- Materiality standards.

To demand certification by an outside auditor is said by the OECD to be a bit excessive at this stage. The somewhat related demand of a mandatory use of consulting firms is met with similar critique, saying that there is no reason documents prepared by internal employees would be less trustworthy, assuming those employees are qualified to do so. The question on what comparables to use is more divided. While businesses suggest that being able to use regional comparables instead of local comparables would simplify the documentation, one must consider how much that undermine the goal of the arm’s length principle in that it might not use the most reliable information. The issue of translation comes from the simple fact that all languages are not understood everywhere, making the translation of documents to a must at some points. The OECD underlines that MNEs should receive sufficient time for translations when such is needed. The last of these points is a tricky one.

\textsuperscript{200} White paper para 72.

\textsuperscript{201} White paper para 74-76.
By materiality standards the OECD means that all transactions are not material enough to warrant full documentation. This is something that needs to be addressed in the local country documentation rules where thresholds need to be established. In this matter it is underlined that a lot of different factors need to be considered, such as the size of local economy and the size and impact of the MNE.\(^2\)\(^0\)\(^2\)

In seeking to create simple and efficient compliance, the white paper suggest a two-tier system of documentation. The suggestion is said to take into consideration all of the observations done and presented in the white paper. As previously mentioned, the OECD identifies three main purposes for transfer pricing documentation. Firstly, to provide enough for information to tax authorities for a robust risk assessment. Secondly, to make sure an audit is easily achievable when needed. Thirdly, to create incentive for the tax payers to follow the rules and create documentation in due time.\(^2\)\(^0\)\(^3\)

The two tiers consist of a masterfile and local files. A suggested format is included to the white paper and divide what the two tiers should contain. The masterfile aims to give a clear enough picture of the global business, financial reporting, debt structure and tax situation for tax authorities to be able to make a proper risk assessment. To achieve this the masterfile is divided into five categories;

- information on the MNE group;
- description of the MNE's business or businesses;
- information on the MNE's intangibles;
- information on the MNE's intercompany financial activities;
- information on the MNE's financial and tax positions.\(^2\)\(^0\)\(^4\)

The aim of the local file is for the taxpayer to demonstrate that it has complied with the arm’s length principle in its transfer pricing transactions. Thus, the information in the local file focus on specific transfer pricing analyses and material transactions connected to the local country the specific file aims at. Such information would be financial information re-

\(^{202}\) White paper para 77.

\(^{203}\) White paper para 78-79.

\(^{204}\) White paper para 80.
garding those transactions, comparability analysis and application of transfer pricing meth-

5.3.2 Analysis

As the master file is a tool for risk assessment, it is natural for the creation of an efficient
tool to identify what the indicators of such risks are, so that risks are easily identified. The
OECD identified nine such indicators in a previous work, but only seven of those made it
into the white paper. The two indicators that were cut are; poor results and different effec-
tive tax rate. Poor results in the meaning of results not consistent with the industry in
which the company operates or its functions, and effective tax rate i the meaning of a big
variation of the subjects effective tax rate and that of the MNE group. The white paper
gives no reasons, or even mentions, why they were omitted. Some guesswork could be
done however.

Poor results is a method Mr. Good mentions during his interview as a method used by the
STA as an indicator for transfer pricing risk. The somewhat related indicator year or year
loss making did make it onto the list however, and maybe it was seen as an overstatement
to include both. Another reason might be that to evaluate this indicator, one needs
knowledge on the industry in which the taxpayer operates. The indicators that did make it
onto the list are all fairly easy to evaluate based only on the facts of the MNE group and
the taxpayer in question. In short, a simplification for the tax authorities. Differences in ef-
fective tax rates might arise from a number of different reasons, including the presence of
some of the other indicators. It is also a fact that tax rates are something to be included in
the country-by-country report in the OECD suggestion. With those two facts in place there
seem to be little reason to factor this when designing the master file.

The seven indicators that did make the list all make sense and can be motivated. Transac-
tions to parties in low tax jurisdictions might indicate attempts of lowering the tax of the
MNE. Intangibles are very hard to price because of their uniqueness, so risk of incorrect
pricing increases. In business restructures a lot of assets are moved around, and opinions
on what has happened from a tax perspective might vary. Interest and royalties are transac-
tions that are very easy to create without any tangible ownerships changing, making it easy
to abuse. A company making consistent losses should have a hard time staying in business,
so there might be something wrong there. Poor documentation might indicate a need of

205 White paper para 81.
hiding reality from tax authorities. It is however important to remember that these are only indicators on that something might be wrong, not that there is something wrong. All of these can occur of perfectly valid reasons, but their presence indicate a risk of something being incorrectly priced.

The OECD list information it deem necessary for insight in the seven indicators. The list is mostly self explanatory if compared to the indicators. Internal debt structure is obviously needed to understand for insight in internal interest rates, and information on transactions of intangibles obviously needed for the insight in just that. Even if it can be good to be extra clear sometimes, this feels like overdoing it. Most likely tax authorities around the world know what information is needed to understand the seven indicators.

<table>
<thead>
<tr>
<th>7 indicators</th>
<th>Information needed</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Significant transactions with, and income allocated to, related parties in low tax jurisdictions;</td>
<td>• Identification of material cross border transactions between associated enterprises, including material payments for goods, services, intangibles, and interest flows.</td>
</tr>
<tr>
<td>• Transfers of intangibles to related parties;</td>
<td>• Identification of recent business restructuring transactions and transfers of intangibles.</td>
</tr>
<tr>
<td>• Business restructurings;</td>
<td>• Information regarding the levels of corporate debt and interest expense in relevant countries.</td>
</tr>
<tr>
<td>• The existence of specific types of related party payments that have the potential to erode tax base, including payments of interest, insurance premiums and royalties;</td>
<td>• Information regarding the MNE’s global transfer pricing policies and the financial results of applying those transfer pricing policies. It would especially include a description of where the group important intangibles are held. It would also include the identification of the MNE Group’s existing APA and ruling agreements related to income allocation with various countries.</td>
</tr>
<tr>
<td>• Year on year loss making;</td>
<td>• The taxpayer's explanation of how the material transfer pricing arrangements comply with the arm's length principle and local transfer pricing rules.</td>
</tr>
<tr>
<td>• Poor or non-existent documentation of related party transactions and their results;</td>
<td></td>
</tr>
<tr>
<td>• excessive debt.</td>
<td></td>
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</tbody>
</table>

What the master file should contain is listed in the draft. Similar lists are provided in the other transfer pricing rules presented in this thesis, namely the Swedish legislation and the EU TPD. Comparing the Swedish documentation content list with that of the master file of the proposed draft would be unfair, as the draft divide the documentation into a master file and a country specific file. Comparing with the listing in the EU TPD could however

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206 See 5.3.1.p 67.
207 See 5.3.1 p 68.
be interesting, as the EU TPD also make a division into a master file and country specific files. The amount to be contained seems to be overwhelmingly more in the EU TPD when visually comparing the texts.

<table>
<thead>
<tr>
<th>OECD master file</th>
<th>EU TPD master file</th>
</tr>
</thead>
<tbody>
<tr>
<td>• information on the MNE group;</td>
<td>• Business, business strategies and if any changes were made with regards to the prior tax year.</td>
</tr>
<tr>
<td>• description of the MNE’s business or businesses;</td>
<td>• The groups operational, organizational and legal structure with a graphic representation of the MNE’s organization. In this segment there should also be a list of the MNEs group members and explanation of the parent company’s activity in the subsidiaries.</td>
</tr>
</tbody>
</table>
| • information on the MNE’s intangibles; | • An identification of the companies who are dealing in controlled transactions in connection to the enterprises within the EU. The controlled transactions as such should also be described by providing information regarding the:

"(i) Flows of transactions (tangible and intangible assets, services, financial),

(ii) Invoice flows and

(iii) Amounts of transaction flows" |
| • information on the MNE’s intercompany financial activities; | • Functions performed and risks assumed. Together with assets used these components help characterize the companies within the group that is why changes made in comparison with the prior tax year also should be described. For example the changes should describe if one enterprise goes from the characterization of a limited risk manufacturer to an assembler. |
| • information on the MNE’s financial and tax positions. | • The ownership of intangible property like trademarks, patents, know-how and etc. Also royalties received or paid. |

"The MNE group's inter-company transfer pricing policy or a description of the group's transfer pricing system that explains the arm's length nature of the company's transfer prices". For example which transfer pricing method is used in an inter-group transaction when company A (CA) buys goods from company B (CB) and how that would be affected if CA or CB did business with company C instead.

• A list of the agreements (APA, cost contribution agreements) and rulings regarding transfer pricing affecting the associated enterprises within the EU.

• A commitment by all intra-group entity's to provide complementary information when requested and this shall be done in a reasonable time period in consonance with domestic provisions.

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208 See 5.3.1 p 70.

209 See 3.3.3 p 25.

210 Annex article 4.2 (d) para 2-4 EU TPD.
In reality however, the difference is less. Every bullet point in the EU TPD list is more detailed, leading to the illusion of being vastly different. For example, the draft bullet points of

"information on the MNE group" and "description of the MNE's business or businesses"

are stated in very general terms, and several of the EU TPD points is encompassed. For example it should likely include such things as functions and risks in the MNE group, although the EU TPD is much more clear on this. Likewise, the EU TPD lists a number of internal transactions under one of its larger bullet points, and could reasonably be encompassed in the OECD proposal draft bullet point of

"information on the MNE's intercompany financial activities".

Given enough generosity in interpretation, it should be possible to encompass all of the EU TPD in the listing from OECD. But even if one would encompass all of the EU TPD master file requirements in the OECD requirements it is clear that the EU TPD system offers a clearer system with less room for different interpretations. The more general wording in the OECD version is likely due to the difficulties of reaching consensus between nation in regards to details. The OECD version is likely to influence legislation in a vast number of countries from different region in the world, at least that should be its aim as a creator of guidelines. The EU TPD is regionally smaller, and also exist as an optional alternative next to national legislation. The difference in detail is, however compromising, expected. Still with this in mind, the general terms of the OECD should not be a major problem, as it is clear that it is general global information to be had, and that regional data needed to examine specific arm’s length pricing will be in the country specific files.

The OECD list several items it sees as problematic, making documentation unnecessary difficult.

- Certification of documentation by an outside auditor,
- Mandatory use of consulting firms,
- Use of local or regional comparables,
- Translation and,
- Materiality standards.
The first two are closely related, concerning demands on outside expertise. By nature it is easier to have faith in documentation created by an independent third party, instead of the taxpayer itself. But there are two factors we feel speak against this reasoning. Firstly, auditing firms themselves, while being filled by experts on various related fields, have their own interest to uphold. A firm known to produce documentation more advantageous to the taxpayer than its competitors are likely to find more clients, and vice versa. Since transfer pricing is a complex area with lot of subjectivity and estimations, such possibilities exist. Outrageous claims will not be produced by the firms of course, but neither will any serious taxpayer produce claims that obviously will not stand an audit. Both taxpayers, and any auditing firm they potentially hire, have a self-interest in producing documentation as advantageous as possible for the taxpayer, so the neutrality aspect is a facade. Secondly, hiring auditing firms for such complex and time demanding endeavors are expensive. For smaller companies the cost might be highly non-proportionate to the gain, especially considering the little extra value it gives. It is our belief that it would do good if the OECD condemns such demands.

The use of regional comparables versus local ones is a complex question, and one the reader is badly prepared for from reading this thesis. The OECD takes no definitive stand on the matter, and neither do we. Both the matter of translation and language of documents as well as materiality standards are discussed in the direct questions below\footnote{See 6.3.6 and 6.3.8.}.
6 The Chapter V Discussion Draft

6.1 Introduction

Chapter V of the OECD TPG has been the organizations guide on transfer pricing documentation since it was introduced in 1995. Following the white paper discussed in the previous chapter above, a suggested draft was published on 30 January 2014 for major changes in Chapter V. So major that it is suggested that the entire text is deleted and replaced with the new text.

In this chapter of the thesis the material content of the suggested new Chapter V of the OECD Guidelines are examined and compared to the material content of the white paper, and it is also mentioned if there is a similar idea in the current guidelines. In the draft the public is asked to contribute with comments in general, as well as on specific questions. Those specific questions are presented two times. First in this first in connection with the content where it was asked and later in a specific heading handling these questions. The deadline for comments was set at 23 January 2014. The comments of the public is as such published and available on the OECD webpage. Due to its volume it is not feasible to present all answers. As such only some select answers from the public is presented in this chapter.

Analysis connected to the specific question is not made under specific headings, but instead in connection to each question. This because we find it more efficient reading to have the analysis in direct connection to the question, but a heading for each analysis unnecessary.

6.2 Material Content

6.2.1 Changed purpose and language

The draft is started off with an introduction of its purpose and relation to the current Chapter V. The aim is clearly stated in the first paragraph which states that;

"This chapter provides guidance for tax administrations to take into account in developing rules and/or procedures on documentation to be obtained from taxpayers in connection with a transfer pricing inquiry or risk assessment. It also provides guidance to assist taxpayers in identifying documentation that would be

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212 see 3.2.1.
213 Draft page 1.
most helpful in showing that their transactions satisfy the arm's length principle and hence in resolving transfer pricing issues and facilitating tax examinations.\footnote{Draft para 1.}

Compared to the introduction of the old guidelines, the introductory paragraph is almost identical. Only a single word is omitted where "general guidance" change to "guidance in the first sentence.\footnote{Compare chapter 5, para 1 OECD TPG, Draft para 1.} In the introduction it is observed what the language of the previous chapter V did and did not provide. It is explained that the previous language had an emphasis on;

"...the need for reasonableness in the documentation process from the perspective of both taxpayers and tax administrators, as well as on the desire for a greater level of cooperation between tax administration and taxpayers in addressing documentation issues in order to avoid excessive documentation compliance burdens while at the same time providing for adequate information to apply the arm's length principle reliably."\footnote{Draft para 2.}

It is also explained that the previous language did not;

"...provide for a list of documents to be included in a transfer pricing documentation package nor did it provide clear guidance with respect to the link between the process for documenting transfer pricing, the administration of penalties and the burden of proof."\footnote{Draft para 2.}

Since the aim is still the overall same, the new text still has an emphasis on reasonableness which is demonstrated below. The thing that is really new, as the introduction hints at, is that in the new text there is guidance on specific documents to include in a transfer pricing documentation.

One thing that is not expressed in the current language of Chapter V is a clear statement of the purpose of transfer pricing documentation. While the content is sorted under headlines in the current version, the documentation objective is not specified. The objectives of transfer pricing documentation rules have been discussed in the white paper.\footnote{See 5.2.} The draft
identifies three objectives for transfer pricing documentation rules and is also said to include guidance on development of such rules.\textsuperscript{220}

### 6.2.2 Objectives Of Transfer Pricing Documentation

The objectives for requiring transfer pricing documentation are stated under their own heading and are said to be;

1. "to provide tax administrations with the information necessary to conduct an informed transfer pricing risk assessment;"
2. "to ensure that taxpayers give appropriate consideration to transfer pricing requirements in establishing prices and other conditions for transactions between associated enterprises and in reporting the income derived from such transactions in their tax returns; and"
3. "to provide tax administrations with the information that they require in order to conduct an appropriately thorough audit of the transfer pricing practices of entities subject to tax in their jurisdiction."

These objectives correspond with the objectives set out in the white paper explained above.\textsuperscript{222} The division of number one and three, tax administrations ability to conduct an informed transfer pricing risk assessment compared to information needed for a transfer pricing audit is not present in the current Chapter V. Each of the objectives is sorted under its own heading where the discussion on the topic is held, starting with the topic of risk assessment.

Regarding transfer pricing risk assessment it is stated that effective risk identification and assessment is crucial for an effective screening process to identify the appropriate cases for audits or inquires. Due to the fact that tax administrations has limited resources, it is essential that there exists efficient methods for this purpose. For this purpose tax administrations are in need of sufficient, relevant and reliable information. Transfer pricing documentation remain an essential tool in this area. To find this information there are several tools, one being transfer pricing forms, normally filed in connection to the annual tax return. It is also mentioned in this section that some countries find it advantageous to share risk as-

\textsuperscript{220} Draft para 4.

\textsuperscript{221} Draft para 5.

\textsuperscript{222} Sec 5.2.
essment results with the taxpayers and that this can help improve compliance.\textsuperscript{223} This corresponds to the white paper discussion made above in chapter 5.2.2, while this area is on large not discussed in the current chapter V. A brief mentioning is made that documentation requirements at the time of filing the tax return should be limited to what is necessary to determine which taxpayers need to be further examined. The reasoning is to not impede on cross border trade and investments.\textsuperscript{224}

Question asked in the draft in relation to the risk assessment:

\textit{“Comments are requested as to whether work on BEPS Action 13 should include development of additional standard forms and questionnaires beyond country-by-country reporting template. Comments are also requested regarding the circumstances in which it might be appropriate for tax authorities to share their risk assessment with taxpayers.”}\textsuperscript{225}

The second objective is about the taxpayer's assessment of its compliance with the arm's length principle. It is said that by requiring taxpayers to articulate their reasoning about its transfer pricing position, a culture of compliance is likely to be created. It is stressed that the documentation must be made at the time of the transaction, or at the very least no later than the time of filing the tax return for the fiscal year in question. This to prevent justifications created after the fact. This is method of having documentation to require documentation in a timely manner is one of the two ways the draft suggest compliance to be encouraged. The second way is to have established penalty regimes created intended to reward timely preparation. Penalty provisions is discussed later in the draft and therefore also later in this thesis below. The ideal is that taxpayers will use the opportunity of transfer pricing documentation to motivate its transfer pricing policies. Things as costs and time restraints might undermine this objective, why it is important to keep documentation requirements reasonable to encourage compliance.\textsuperscript{226} This objective is described in the white paper in the same way.\textsuperscript{227} While not described in the same manner in the current chapter V, most of this is mentioned. The idea of limiting requirements to reasonable levels is mentioned in several

\textsuperscript{223} Draft para 7-9.

\textsuperscript{224} Chapter 5, para 15 OECD TPG.

\textsuperscript{225} Draft para 9.

\textsuperscript{226} Draft para 10-12.

\textsuperscript{227} See 5.2.3.
paragraphs\textsuperscript{228}, and that pricing should be set after the circumstances at the time of trade, not in a after the fact matter, is also mentioned.\textsuperscript{229}

The third objective stated in the draft is to provide tax administrations with information they need to properly conduct a transfer pricing audit. It is pointed out that transfer pricing audits are very fact-intense. There are many facts to take into consideration that the tax authority needs access to. It is clear that the tax authority needs access to such material, and if all of it is in the transfer pricing documentation it is of course well. But situations will arise when that is not the case. Sometimes material needed is simply not in the possession of the taxpayer in question, but in the possession of another MNE group member outside of the country. There is therefore a need for tax authorities to be able to obtain such information, either directly or by information sharing.\textsuperscript{230}

Question asked in the draft in relation to transfer pricing audit:

"Comments are specifically requested on the appropriate scope and nature of possible rules relating to the production of information and documents in the possession of associated enterprises outside the jurisdiction requesting the information."\textsuperscript{231}

In the current Chapter V the specific problem with unavailable documents are mentioned. It is stated that taxpayers should not be obligated to produce documents that are not in their control. Even if such documents is in the possession of another MNE member, it can be difficult for the taxpayer to obtain it.\textsuperscript{232}

\textbf{6.2.3 Analysis}

While the change of the statement "general guidance" to "guidance" in the first paragraph might seem insignificant, we believe it signaling a potentially big change. While to current OECD TPG gives guidance, it does so in a very general way, proposing basically no detailed rules or systems. The draft proposes a complex detailed system that is, compared to the current guidelines, not very general at all, but rather a complete system. This becomes even more clear when the draft says the previous language did not provide a list of docu-

\textsuperscript{228} Chapter 5, para 7-11 OECD TPG.
\textsuperscript{229} Chapter 5, para 15 OECD TPG.
\textsuperscript{230} Draft para 13-15.
\textsuperscript{231} Draft para 15.
\textsuperscript{232} Chapter 5, para 10-11 OECD TPG.
ments to include in the documentation at all, while the new does provide a quite extensive one. The feeling of suggestion of the current guidelines is gone, replaced with a draft looking much more like legislation.

As mentioned, the division into risk assessment and full audit documentation could prove to be advantageous for the taxpayer as some costs that would only surface during a full audit might never come to be, if there is no full audit. This divided system should prove advantageous for tax authorities as well. OECD point out that tax authorities has limited resources. With a well-structured risk assessment system in place where more focused information suitable for specifically this, time and resources could be saved. It is also said that sharing risk assessments with the taxpayer in question might be advantageous. We see this as obvious, and there are few reasons to believe that sharing such information would not be an improvement, as it is easier to fix your problems if you are aware of them.

The idea to promote good behavior and compliance among MNEs is in itself a good one, as more compliance means less problems. It might be tempting to MNEs to stall transfer pricing investigations since it's a cost for virtually no gain, it's a mere compliance cost. This cannot be stressed enough, if there was no need to prove your compliance, the amount of companies doing it would be very low. It is somewhat humoristic that the OECD mentions rewarding MNEs in was as not being audited. It might be an incentive, but it is no reward, no more than not hitting your dog for behaving well is rewarding it. No matter the semantics there is however a need of enforcing compliance. Such incentives is probably more effective if they go beyond "not being punished" and instead turn into real advantages such as immunity to fines due to improper pricing. If documentation is done correctly, the only "punishment" possible should be price adjustments in case of incorrect pricing. If that was in the proposed system, a worldwide similar attitude to compliance have a higher chance of developing.

It is obvious that a full audit requires more information than a risk assessment. A risk assessment is only there to identify risks, but a full audit require a detailed analysis from the tax authorities. When doing such analysis there might be a need for documents not easily obtained by the taxpayers themselves, such as documents from other MNE members. The current guidelines advice against taxpayers being obligated to provide material out of the hands of other MNE members. There is no reason why that view should not stand true to-
day. This question is also discussed below\textsuperscript{233}, as it is part of the question to the public in the draft.

**6.2.4 The Two-Tier Approach**

To achieve the objectives described above, the OECD suggest that there should be a standardized transfer pricing documentation. The OECD offers a suggestion on how such a standard should look, describing a two-tier system of a master file for standardized information relevant in relation to all members in a company group, and a local file containing information related to the material transaction of the local taxpayers. It is said that this approach will give tax authorities the ability to make proper risk assessments, means to perform an audit and properly give incentive of compliance.\textsuperscript{234}

The master file is to contain standardized information that is relevant for in relation to all members of an MNE group. The master file is to give a complete picture of the MNE groups global business, financial reporting, debt structure, tax situation, allocation of income, economic activity to aid tax administrations in the risk assessment. It is suggested that the master file should be prepared either for the whole MNE group, or by line of business.\textsuperscript{235}

A question is asked in the draft about the preparation of the master file:

"Comments are requested as to whether preparation of the master file should be undertaken on a line of business or entity wide basis. Consideration should be given to the level of flexibility that can be accommodated in terms of sharing different business line information among relevant countries. Consideration should also be given to how governments could ensure that the master file covers all MNE income and activities if line of business reporting is permitted."

The master file is suggested to be divided into five categories, those being:

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\textsuperscript{233} See 6.3.4.

\textsuperscript{234} Draft para 16-17.

\textsuperscript{235} Draft para 18.

\textsuperscript{236} Ibid.
"a) the MNE group’s organizational structure; b) a description of the MNE’s business or business; c) the MNE’s intangibles; d) the MNE’s intercompany financial activities; and e) the MNE’s financial and tax positions."

The last of these sections is to include country-by-country information, such as global profit allocations, taxes paid and a number of indicators on local economic activity. This is said to be helpful in a risk assessment.

A number of questions is asked in the draft about the country-by-country reporting:

"A number of difficult technical questions arise in designing the country -by-country template on which there were a wide variety of views expressed by countries at the meeting of Working Party n°6 held in November 2013. Specific comments are requested on the following issues, as well as any other issues commentators may identify:

- Should the country-by-country report be a part of the master file or should it be a completely separate document?
- Should the country-by-country report be a part of the master file or should it be a completely separate document?
- Should the country-by-country template be compiled using "bottom-up" reporting from local statutory accounts as in the current draft, or should it require (or permit) a "top-down" allocation of the MNE group’s consolidated income among countries? What are the additional systems requirements and compliance costs, if any, that would need to be taken into account for either the "bottom-up" or "top-down" approach?
- Should the country-by-country template be prepared on an entity by entity basis as in the current draft or should it require separate individual country consolidations reporting one aggregate revenue and income number per country if the "bottom-up" approach is used? Those suggesting top-down reporting usually suggest reporting one aggregate revenue and income number per country. In responding, commenters should understand that it is the tentative view of WP6 that to be useful, top-down reporting would need to reflect revenue and earnings attributable to cross-border transactions between associated enterprises but eliminate revenue and transactions between group entities within the same country. Would a requirement for separate individual country consolidations impose significant additional burdens on taxpayers? What additional guidance would be required regarding

237 Draft para 19.
238 Draft para 20-21.
source and characterization of income and allocation of costs to permit consistent country-by-country reporting under a top-down model?

- Should the country-by-country template require one aggregate number for corporate income tax paid on a cash or due basis per country? Should the country-by-country template require the reporting of withholding tax paid? Would a requirement for reporting withholding tax paid impose significant burdens on taxpayers?

- Should reporting of aggregate cross-border payments between associated enterprises be required? If so at what level of detail? Would a requirement for reporting intra-group payments of royalties, interest and service fees impose a significant additional burdens on taxpayers?

Should the country-by-country template require reporting the nature of the business activities carried out in a jurisdiction? Are there any features of specialist sectors that would need to be accommodated in such an approach? Would a requirement for reporting the nature of the business activities carried out in a jurisdiction impose significant burdens on taxpayers? What other measures of economic activities should be reported?

The local file is to contain information on local transactions to motivate the taxpayers compliance with the arm's length principle. Its focus is on things relevant for the transfer pricing analysis and should contain all relevant information regarding transactions, comparability analysis and motivation of the chosen transfer pricing method.

Since the two-tier system is new to the OECD there is obviously no mentioning of this in the current Chapter V of the OECD TPG. This part of the draft does however more or less mimic the contents of the white paper.

6.2.5 Compliance Issues

A number of compliance issues are listed in the discussion draft. To not overwhelm the reader with information, only those compliance issues that will be discussed in the analysis portion are presented. The compliance issues addressed with specific questions to the public is presented, as this makes it more manageable, and covers questions that, by being asked, should be of importance and in need of input. To not have analysis in two places, these are analyzed in full in chapter 6.3 below.

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239 Draft para 20.
240 Draft para 23.
Materiality is one such compliance issue, as all transactions are not material enough for full documentation. Tax administrations want to see the important information, and taxpayers want to not be overloaded with demands. This is why there should be a materiality threshold. Factors to take into consideration when establishing such a threshold would be the size of the local economy, how important the MNE group in question is in that economy, size and nature of entities in question and the size of the MNE group as a whole. 241

One question is asked in the draft regarding the matter of materiality:

"Comments are requested as to whether any more specific guideline on materiality could be provided and what form such materiality standards could take." 242

The OECD recommends that transfer pricing documentation should be periodically updated to make sure its analysis is still accurate and viable. However, facts related to this often does not change very fast, a yearly update might become an unnecessary burden for the taxpayer. Based on this the OECD suggest in the draft that search for comparables could be limited to once every third year if operation conditions remain unchanged. Financial data is recommended to be updated every year regardless if such changes occur or not. 243

Regarding frequency of updates there is one question in the draft:

"Comments are requested regarding reasonable measures that could be taken to simplify the documentation process. Is the suggestion in paragraph helpful? Does it raise issues regarding consistent application of the most appropriate transfer pricing method?" 244

What language documentation should be made in is a matter of importance, as translations are time consuming and costly. The OECD suggest in the draft that at least the master file should be prepared in English. Local files should probably be prepared in the local language. Sometimes information in the master file would be needed in the local language. In

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241 Draft para 29.
242 Ibid.
243 Draft para 33-34.
244 Draft para 34.
such an event a request for translation of the relevant parts of the master file should be made, to not overburden the taxpayer.\textsuperscript{245}

"Comments are requested regarding the most appropriate approach to translation requirements, considering the need of both taxpayers and governments."\textsuperscript{246}

In the draft the OECD underlines the importance of confidentiality. Tax authorities need to make sure that trade secrets or other confidential information is not publicly disclosed. It is therefore important that tax authorities can assure taxpayers that information in transfer pricing documentation remain confidential, and that necessary steps are made to make sure that is.\textsuperscript{247}

"Comments are requested as to measures that can be taken to safeguard the confidentiality of sensitive information without limiting tax administration access to relevant information."\textsuperscript{248}

### 6.2.6 Implementation

Transfer pricing is and will continue to be a matter of local legislation. An implementation of the proposed system will require changes in local legislation, to have transfer pricing documentation include information that is in the OECD suggested draft in its Annex I-III. For this system to work in a good manner, uniform formats is of importance. The OECD suggest that the master file is to be completed by the parent of an MNE group and from that be shared to affiliates. How this sharing is to be done is not yet clear.\textsuperscript{249}

"Comments are requested regarding the most appropriate mechanism for making the master file and country-by-country reporting template available to relevant tax administrations. Possibilities include:

- The direct local filing of the information by MNE group members subject to tax in the jurisdiction;
- Filing of information in the parent company’s jurisdiction and sharing it under treaty information exchange provisions;"

\textsuperscript{245} Draft para 35.

\textsuperscript{246} Ibid.

\textsuperscript{247} Draft para 41.

\textsuperscript{248} Ibid.

\textsuperscript{249} Draft para 44-45.
6.3 Responses From The Public

6.3.1 The Commentators

A large amount of answers from the public was sent to comment the discussion draft, in total over 1100 pages. From these a select few have been chosen to be presented in this thesis. The answers presented here are those of BIAC, the Confederation of Swedish Enterprise (Svenskt näringsliv), the ICC and PwC Global. These have been chosen to represent a big width. BIAC represent a large amount of big taxpayers. Confederation of Swedish Enterprise represent a big amount of the Swedish enterprises and is chosen due to the thesis connection to Swedish legislation. The ICC is a big international organization in the area of business, and PwC is our chosen representative out of the auditing firms. The opinion of the Swedish Tax authority was not voiced at the time of this writing and has as such not been included. First any general comment from those selected is presented, and after that each question asked in the draft is worked over.

6.3.2 General Comments

BIAC comments that while it believes that the BEPS Action plan is of importance, it is discouraged by the large amount of requirements proposed in the discussion draft. There is a fear that the requirements in the master file and local file will add to what is said to be an already substantial compliance burden. It is of essence that the benefit of any data ask of the taxpayer outweighs the cost of providing it. BIAC believes that the amount of information asked for in the draft is excessive for a risk assessment tool and can therefore be slimmed down. BIAC is also concerned with the matter of confidentiality and underlines the importance of tax authorities keeping sure information is protected.\(^{251}\)

The Confederation of Swedish Enterprise comments that while the EU TPD has a similar approach, it is voluntarily and is filed at a later stage. The fact that the OECD draft suggest filing before an audit and has a substantial amount of information required is seen as an added compliance burden. It is underlined that there is a need for balance between the need of tax administrations and the burden of compliance for the taxpayer. The Confederation of Swedish Enterprise voice the opinion that balance is not present in the current draft

\(^{250}\) Draft para 45.

\(^{251}\) Draft comments volume 1, p 97-98.
and the requirements are too far-reaching and provide too detailed information compared to what is needed for a risk assessment. There is also a major concern that with the master file likely to be circulated a lot, upholding confidentiality will prove to be difficult.\textsuperscript{252}

The international Chamber of Commerce (ICC) comments on that the requirements in the draft goes beyond what is needed for its stated cause and thus does not take into consideration the burden of compliance costs. It is asked that this is looked over.\textsuperscript{253}

PwC Global first comments that the development of this suggestion has had a very high pace and too little time has been given for input from the business perspective. Furthermore PwC is of the opinion that the current draft puts significant additional burden on taxpayers without added benefit. The information required in the master file is too substantial. PwC also brings up the matter of confidentiality in its general comments, stressing the importance of consideration for keeping taxpayers secrets. The master file should only be shared to tax authorities other than the MNE leaders under treaties for information exchange.\textsuperscript{254}

**Analysis**

All investigated comments address that they see a larger compliance burden, and the amount of information asked for is excessive. Especially it is commented that the amount of information to be gathered for the risk assessment is excessive. While no one seems to actively object for a change, there is extensive criticism of the amount of information to be included. One comment also address that the development have been going too fast. All in all, there seem to be negative attitude to the structure of the draft, but not necessarily to the draft as a whole.

We are of the opinion that while it surely has been going fast, a quick development in international co-operations is nice for a change. The amount of detail given in the master file seem to be a big question for many commentators. If the information asked for is relatively easy to produce, we see no issues with lots of information already in the risk assessment stage. More information should hopefully lead to better understanding of the situation, not less. Comments about adding to already exiting compliance burden does not seem to take

\textsuperscript{252} Draft comments volume 1, p 293-295.

\textsuperscript{253} Draft comments volume 2, p 304-305.

\textsuperscript{254} Draft comments volume 3, p 136-138.
into account that these rules, if implemented properly in most countries, should hopefully replace current systems, not add on top of them. Some critique seem unwarranted.

**6.3.3 Risk Assessment Question**

> "Comments are requested as to whether work on BEPS Action 13 should include development of additional standard forms and questionnaires beyond the country-by-country reporting template. Comments are also requested regarding the circumstances in which it might be appropriate for tax authorities to share their risk assessment with taxpayers."  

BIAC comments that while streamlined documentation requirements for low risk business are supported, forms beyond the country-by-country reporting already in place in the two-tier system risks to add even further compliance burden. As such these forms are only appropriate if they can be adopted in a multilateral way. As of now additional forms will only add, not replace, current local requirements. Instead BIAC is of the opinion that the focus right now should stay at the country-by-country report until that is an effective tool. Regarding the sharing of risk assessment BIAC underlines the importance of building trust between taxpayers and tax administrations and welcomes any such move. Sharing risk assessments can help to avoid unnecessary work for either party and helps to develop the transfer pricing structure of the taxpayer.

The Confederation of Swedish Enterprise comments that the proposed system has enough requirements, and even further documents is not something that should be imposed. A more focused format of the master file and local file is however encouraged. On the matter of sharing risk assessment with taxpayers it is commented that doing is so is helpful, as it assist taxpayers in improving its transfer pricing documentation.

The ICC leaves no comment on this.

PwC comments that it supports the idea of harmonized standard forms. It is however of vital importance that these in as large quantity as possible replace forms already in use, as to not add to compliance. On the matter of sharing risk assessment with taxpayers PwC voice

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255 Draft para 9.
257 Draft comments volume 1, p 295-296.
the opinion that it should be done at the earliest stage possible, as it promotes transparency and helps the taxpayer to allocate it transfer pricing resources to where it is needed.\textsuperscript{258}

**Analysis**

Commentators seems to be in agreement that more form are not wanted. To harmonize forms that replace existing ones is however supported. Those that comment on it also mention that sharing of risk assessment should be done, and preferably at an early stage.

We are in agreement with the commentators that a harmonization of forms is desirable, not an addition of them. But as one also hints at it might be advantageous to wait with this until it is clear that the gigantic initiatives that are in motion with the draft itself is evaluated. The contents of the master file is hard to put into formulas and specific wordings. This is an area that is in less need of harmonization, as the content of the documentation is likely to a greater diversity between rules, not what forms they are presented in. As long as the desired content is clear it should be up to the taxpayers to present these facts in any suitable manner. As already explained in the analysis of the white paper above, sharing risk assessment is desirable. With knowledge of where issues are, taxpayers has an increased ability to fix them.

6.3.4 **Audit Question**

"Comments are specifically requested on the appropriate scope and nature of possible rules relating to the production of information and documents in the possession of associated enterprises outside the jurisdiction request ion the information."\textsuperscript{259}

BIAC comments that while it is important for tax administrations to have the information necessary, it must be balanced to be balance towards the burden on the taxpayer. Local taxpayers might not have direct access to information regarding other MNE group members. While taxpayers should make reasonable efforts to provide all relevant information, tax administrations should be using information exchange tools. BIAC expressed the opinion that the master file (and thereby the information in it) should be filed in the country of

\textsuperscript{258} Draft comments volume 3, p 139-140.

\textsuperscript{259} Draft para 15.
the MNE parent, and from there obtained by other tax administration through information exchange treaties.\textsuperscript{260}

The Confederation of Swedish Enterprise comments that while taxpayers should make reasonable efforts to give adequate information, sometimes taxpayers do not have access to certain information. At such times tax authorities should use information exchange treaties to obtain information. It should not be on the burden of the taxpayer to obtain information, if it is at a disproportionate cost.\textsuperscript{261}

The ICC leaves no comment on this.

PwC underlines that the information provided by the taxpayer in the master file and the country-by-country report can be sensitive information. Maintaining confidentiality is therefore a big concern. PwC is of the opinion that this material should be submitted to the tax authority of the MNE group parent. Other tax authorities in need of this information can later access it by information exchange treaties.\textsuperscript{262}

\textbf{Analysis}

The commentators all seem in agreement that it is not for the taxpayer to get information that is in the possession of other MNE members. This is, more or less, the standpoint taken by the current OECD TPG as well. We see no reason to divert from that. There is no reason to assume direct or indirect control of other MNE members. Taxpayers have no means to enforce a transfer of information from other MNE members. How can it be reasonable to ask them too? The answer to us is that it is not reasonable. By developing proper channels between tax authorities for efficient and secure information exchange this can be solved, and is therefore something the OECD should work with. As it stands the OECD has in the past objected to taxpayers needing to collect difficult-to-gain information from other MNE members, and with increasingly improving communications between tax authorities this should prove to be a small issue.

\textsuperscript{260} Draft comments volume 1, p 101-102.

\textsuperscript{261} Draft comments volume 1, p 296.

\textsuperscript{262} Draft comments volume 3, p 140.
6.3.5 Master File Questions

"Comments are requested as to whether preparation of the master file should be undertaken on a line of business or entity wide basis. Consideration should be given to the level of flexibility that can be accommodated in terms of sharing different business line information among relevant countries. Consideration should also be given to how governments could ensure that the master file covers all MNE income and activities if line of business reporting is permitted."

BIAC comments that the concept of the master file assumes a complete knowledge of all transactions in an MNE group. To document and present this information is a huge undertaking and puts a big burden on the taxpayer. BIAC therefore claims that the concept shows a lack of understanding of the compliance burden that would be imposed. There is no general way MNEs is structured, some span over different fields with local as well as global focus. Some MNE groups are simply too large for a group-wide file to be efficient as it will be hard to process. Flexibility is needed and taxpayers should be able to choose to either report on either group-wide or business-line basis.

The Confederation of Swedish Enterprise comments that since MNEs are structured in different ways some flexibility is needed. Some groups might be arranged in business lines while other are not, and some business lines might not be easily separated. There is a need of option between reporting on a line of business or entity wide basis.

The ICC leaves no comment on this.

PwC recommends that taxpayers should be able to chose between preparing the master file on an entity wide or business line basis. Such flexibility is needed, due to different circumstances for every MNE.

Analysis

Most commentators underline that MNE groups are structured differently. And as those comments also says, MNE groups can vary from relatively local endeavors to worldwide co-operations spanning many areas of businesses. Although previous warning about being

263 Draft para 18.
264 Draft comments volume 1, p 103.
265 Draft comments volume 1, p 296.
266 Draft comments volume 3, p 141.
too flexible, this is a place where flexibility is needed. Not only would it be an unreasonable burden on MNE groups spanning over several lines of business to gather it all under one document, it could also prove difficult to work with for tax authorities. We believe it is all parties interest to leave possibilities open for flexibility on this matter.

"A number of difficult technical questions arise in designing the country-by-country template on which there were a wide variety of views expressed by countries at the meeting of Working Party n°6 held in November 2013. Specific comments are requested on the following issues, as well as any other issues commentators may identify."

- "Should the country-by-country report be a part of the master file or should it be a completely separate document?"

BIAC supports the country-by-country report, but as a stand-alone document outside the master file. It is a tool that should be used only for risk assessment. It is a concern that the level of detail promotes a formulary approach, but is happy that the OECD have made several comments on that such a method should not be pursued.

The Confederation of Swedish Enterprise objects to the presence of the country-by-country report in the Chapter V guidelines at all, since it is not a useful tool for a risk assessment in regards to the arm’s length principle. It would be useful in a formulary apportionment, but as OECD has stated that such an approach is not wanted or aimed at, inclusion of the country-by-country report can only encourage a risk assessment based on that principle. As the contents of the master file and the country-by-country report might require different confidentiality approaches, they should be separated.

The ICC underlines that information addressed in the country-by-country report has little or no connection to arm’s length pricing. It is to be used as a risk assessment tool and as such should be separated from the master file.

267 Method of allocating global profits based on a mechanic and predetermined formula, See chapter 1, para 17 OECD TPG.

268 Draft comments volume 1, p 104.

269 Draft comments volume 1, p 297.

270 Draft comments volume 2, p 305.
PwC comments that the master file and country-by-country report should be separated. Doing so increases the possibility to protect the sensitive material of the master file, and assist with filing deadlines. The country-by-country report should however be used in conjunction with the master file in the risk assessment, not on its own.271

Analysis

There is some resistance across the board from the commentators regarding the country-by-country report, some more negative than others. The three main concerns seems to be to make sure it is only used as a risk assessment tool, some security aspects as the report and master file have different needs in confidentiality, and a worry that it promotes a formulary approach.

The security aspect is the only concern we find of real concern. as said there are different needs between protection of the report and the master file. This is a mere mechanical question, and no reason exist to believe OECD will fail at handling. A worry about formulary approach is somewhat unreasonable. As said by BIAC, the OECD have made clear that this is not the case, and that the arm's length principle is still the approach to follow. If nations wanted to change to the formulary approach despite OECD advice, they could have done so under the current system as well. The need of the OECD to underline that the country-by-country report should only be used for risk assessment is small, as it's, as said by commentators, not a useful tool when examining arm's length principle. On the other hand, it won't hurt anyone to be extra clear, so the OECD should consider it, if nothing else to quiet the critics.

- "Should the country-by-country template be compiled using "bottom-up" reporting from local statutory accounts as in the current draft, or should it require (or permit) a "top-down" allocation of the MNE group's consolidated income among countries? What are the additional systems requirements and compliance costs, if any, that would need to be taken into account for either the "bottom-up" or "top-down" approach?"

BIAC comments that MNE groups are structured in many different ways, and a more flexible approach is needed than either bottom-up or top-down approach. The compliance costs are also potentially very high. To create a top-down report there is a need for the col-

271 Draft comments volume 3, p 141.
lection of information from all MNE members in a country, as well as a significant amount of work to process it. The benefit of this does not seem to outweigh its cost. 272

The Confederation of Swedish Enterprise comments as in earlier answer that each MNE group has its own structure, and only one option would mean an unnecessary compliance cost for some taxpayers. As the country-by-country report is to make comparison within an MNE, not with other MNEs, as long as the method is consistent it should be optional to use either the top-down or bottom-up approach. 273

The ICC comments that each MNE is structured differently and thus it is important to have choices in how to present. Some companies prefer a top-down approach, other a bottom-up. What is important is not what method is used, but it is used consistently each year. As it is for comparison within the MNE, not to compare with other MNEs, any reasonable method should suit as a risk assessment tool provided it is applied the same way each year. 274

PwC comments that different taxpayers handle internal information in different ways and that they know of no reason why a tax authority should prefer one above the other. As long as it is done consistently, the taxpayer should be allowed the flexibility of choosing to use either top-down or bottom up. 275

Analysis

The choice of top-down or bottom-up is once again an area where flexibility is needed, due to big differences in MNE group structures. This is also pointed out by the commentators, and it is our assumption that the OECD will have to allow flexibility in these areas to be able to reach any form of consensus.

- "Should the country-by-country template be prepared on an entity by entity basis as in the current draft or should it require separate individual country consolidations reporting one aggregate revenue and income number per country if the "bottom-up" approach is used? Those suggesting top-down reporting usually suggest reporting one aggregate revenue and income number per country. In re-

272 Draft comments volume 1, p 106-107.
273 Draft comments volume 1, p 297.
275 Draft comments volume 3, p 142.
sponding, commenters should understand that it is the tentative view of WP6 that to be useful, top-
down reporting would need to reflect revenue and earnings attributable to cross-border transactions
between associated enterprises but eliminate revenue and transactions between group entities within
the same country. Would a requirement for separate individual country consolidations impose sig-
nificant additional burdens on taxpayers? What additional guidance would be required regarding
source and characterization of income and allocation of costs to permit consistent country-by-country
reporting under a top-down model?"
is of importance especially since some MNEs does not perform country consolidations and that approach would therefore add an additional burden.278

Analysis

The question on consolidation is not a hard one for us. Such consolidation is not normally done, as said by the commentators. That means a large amount of additional work is added on the demanding preparation already present in documentation. Some MNEs has a huge number of entities involved. To be asked to consolidate those is to place an unreasonable burden upon them in our view.

- "Should the country-by-country template require one aggregate number for corporate income tax paid on a cash or due basis per country? Should the country-by-country template require the reporting of withholding tax paid? Would a requirement for reporting withholding tax paid impose significant burdens on taxpayers?"

BIAC comments that while a tax number should be included in the country-by-country report, its members have not reached a common position on what basis this number should be. Flexibility is needed, as long as the method is presented several methods has its upsides and downsides. BIAC comments that reporting withholding tax should not be mandatory.279

The Confederation of Swedish Enterprise comments that as the country-by-country report, documentation of taxes paid is something that would be needed in a formulary apportionment approach, not for the arm’s length principle. If taxes paid are to be included, it should be reported on a taxes reported basis rather than a taxes paid or taxes due, as this is the way income is also reported. Furthermore, if taxes paid is to be reported, all taxes needs to be included for a correct view, including withholding taxes.280

The ICC comments that the number that should be used is taxes paid in cash per country. It comments that "...Apportionment of a group payment across entities based on the pre-tax profit of

278 Draft comments volume 3, p 142.
279 Draft comments volume 1, p 108.
280 Draft comments volume 1, p 298.
each is artificial...", and it is also commented that"...tax charge in the accounts should not be
used as this will include both current and deferred taxes...".281

PwC comments that cash tax paid is normally not important in deciding arm's length pricing,
and that are several factors in tax reporting that must be taken into consideration, such
as book differences, tax attributes and credits. Nonetheless PwC is of the opinion that one
aggregate number for income tax should be reported. Once again PwC recommend that
the taxpayer is allowed the flexibility of choosing of reporting either per entity or per coun-
try. Furthermore, PwC recommend that withholding tax should not be reported, as the col-
lection of information in that case impose an unnecessary burden on taxpayers.282

Analysis

Cash tax paid is as said in the comments not a number useful for arm's lengths principle.
To be useful it therefore has to be useful in the risk assessment. But due to differences in
how tax systems work in different countries and with different company structures even
this might be doubtful. If taxes are to be included we agree with the Confederation of Swe-
dish Enterprise in the statement that it should be taxes reported, as this is how income is
reported. There is a strong connection between income and taxes, and to report them
based on different systems would be strange at best, and at worst lead to incorrect assump-
tions.

**"Should reporting of aggregate cross-border payments between associated enterprises be required? If
so at what level of detail? Would a requirement for reporting intra-group payments of royalties, in-
terest and service fees impose a significant additional burdens on taxpayers?"**

BIAC comments as this information is already to be in the master file and local file and to
further duplicate the data is not helpful. As this information should be included in the local
file there is no need to include it in the master file, especially in consideration of the
amount of confidential data that would be put into the master file.283

The Confederation of Swedish Enterprise comments that information regarding royalties,
interests and service fees are normally not centrally available and that its requirement would

281 Draft comments volume 2, p 308.
282 Draft comments volume 3, p 143.
impose a significant burden on the taxpayer while providing little help for tax authorities. The information in question would be useful for discovering where ownership of intangibles is held, but that information is already available in the master file.\textsuperscript{284}

The ICC comments that the country-by-country report should not include information already included in the master file and local file. Also if the country-by-country report are to include such information there would be a big compliance cost due to the fact that adjustments must be made to different accounting standards. The value tax administrations have of this is as such disproportionate compared to the compliance cost.\textsuperscript{285}

PwC comments that reporting aggregate cross-border payments should not be required, as any individual tax administration will have access to amounts of tax deduction claimed for these expenses on the local tax return.\textsuperscript{286}

**Analysis**

The commentators cover all important arguments here in our opinion. Information already in the master file and local file should not be included, as this only means extra work for no real gain. There is little reason to include reporting for intra-group payments here. Not only would it prove difficult to document all intra-group transactions in an entire MNE since it might be hard to obtain the information. Any relevant intra-group payments are normally already available to local authorities in regular bookkeeping, meaning that for any arm's length principle consideration it is already available.

- "Should the country-by-country template require reporting the nature of the business activities carried out in a jurisdiction? Are there any features of specialist sectors that would need to be accommodated in such an approach? Would a requirement for reporting the nature of the business activities carried out in a jurisdiction impose significant burdens on taxpayers? What other measures of economic activities should be reported?"\textsuperscript{287}

\textsuperscript{284} Draft comments volume 1, p 298-299.
\textsuperscript{285} Draft comments volume 2, p 308.
\textsuperscript{286} Draft comments volume 3, p 143.
\textsuperscript{287} Draft para 20.
BIAC comments that while activity indicators might be useful, each line of data could relate to a number of activities, making it potentially misleading. A limited amount of indicators is said to be preferable. For that to be effective there is a need for a universal standard, or the different classifications will probably led to confusion. Certain industries behave differently and is such in need of special consideration. BIAC exemplifies with the commodity industry that swings widely and can therefore incur loss making periods.\(^{(288)}\)

The Confederation of Swedish Enterprise leaves no comment on this.

The ICC leaves no comment on this.

PwC comments that the use of business activity code are generally appropriate for the country-by-country template. These should, as mentioned about the country-by-country report, be used in conjunction with the master file for best result a to get a proper context.\(^{(289)}\)

**Analysis**

Commentators has either not commented this or are in agreement that it is desirable. Business activity code already exist as said by one comment, and if the country-by-country report can be more informative with little to no extra burden on the taxpayer we see no reason to object, especially when the commentators, as associated with the taxpayer community, see no reason.

### 6.3.6 Materiality Question

"Comments are requested as to whether any more specific guideline on materiality could be provided and what form such materiality standards could take.\(^{(290)}\)

BIAC comments that a specific guideline on materiality is vital to avoid unnecessary burden on taxpayers and put focus on the high-risk transactions. Examples suggested by BIAC includes the excluding of small members or countries, a transaction amount limit by either

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\(^{(288)}\) Draft comments volume 1, p 109-110.
\(^{(289)}\) Draft comments volume 3, p 143-144.
\(^{(290)}\) Draft para 29.
a fixed amount or an amount relative to the size of the MNE and excluding low-risk transactions putting focus on core business transactions.\(^{291}\)

The Confederation of Swedish Enterprise comments that materiality thresholds would be useful for both the master file and local files. It would simplify for both taxpayers and tax administrations as it would concentrate the data reported to the most relevant one. There is however no suggestions in the Confederations answers on what form such standards could take.\(^{292}\)

The ICC comments that the country-by-country report need to take materiality into consideration. There is however no suggestions in the answer from the ICC on what forms such standards could take.\(^{293}\)

PwC comments that materiality should be discussed in context of other initiatives on the area, such as the "EU Reporting under the Capital Requirements Directive IV". The presence of materiality thresholds are of importance, since without them excessive burden is placed on the taxpayers.\(^{294}\)

**Analysis**

Materiality standards is in our opinion helpful, as this focus the efforts on what is deemed to be most important. Without such standards for what transactions and companies to investigate there is a risk that important ones to look at drowned is less important ones. As mentioned in the interview above\(^{295}\) both Britain and Sweden use a monetary amount as a material limit. While this is an excellent method, it is hard to conjure a number that would fit all nations. BIAC suggest that an amount relative to the MNEs size could be feasible. Perhaps a combination of these with a relative number depending on MNE size with compared to local industry with a roof and floor to avoid extremely low or high numbers would work out. It is also important to state that the tax administrations audit processes are long and costly which makes it reasonable for MNE groups with few and low amount transactions to generally be exempted from audits.

\(^{291}\) Draft comments volume 1, p 110.

\(^{292}\) Draft comments volume 1, p 300.

\(^{293}\) Draft comments volume 2, p 309.

\(^{294}\) Draft comments volume 3, p 144.

\(^{295}\) See 4.4.2 p 41.
6.3.7 Update Frequency Question

Comments are requested regarding reasonable measures that could be taken to simplify the documentation process. Is the suggestion in paragraph 34 useful? Does it raise issues regarding consistent application of the most appropriate transfer pricing method?²⁹⁶

BIAC comments that while it is welcomed to have a clear guidance on frequency on updates, the need for searching comparables every year is limited and should be every three years as well. Comments are also made that the guidance on regional vs. local benchmarks is needed. Access to variable databases might be limited, increasing compliance costs. Furthermore BIAC express that this should be a good opportunity to discuss the timing of analysis, now stretching from the time of transaction to the time of the tax return.²⁹⁷

The Confederation of Swedish Enterprise leaves no comment on this.

The ICC comments that a yearly comparable analysis is of limited benefit. A three year gap should be suitable for all transactions.²⁹⁸

PwC comments that while the paragraph is helpful, it is not enough. There is a need of uniformity between the requirement of local files under OECD and the requirements of each jurisdiction. As such PwC is of the opinion that each jurisdiction should modify its local transfer pricing requirements to conform with the OECD guidelines before implementing the system of the discussion draft. It is also the view of PwC that regional comparables needs to be accepted in place of local comparables when the latter is sometimes too costly and burdensome to obtain. There are seldom any relevant difference between them and it would ease the compliance burden of the taxpayer.²⁹⁹

Analysis

Commentators in general find the advice of paragraph 34 useful. Most comment that an even more liberal view is needed, as updating comparables every year is of limited need anyway. We are also of the opinion that unless any major change in the MNE structure occur, the need for checking comparables every year is limited. Markets do not change that fast

²⁹⁶ Draft para 34.
²⁹⁷ Draft comments volume 1, p 111-112.
²⁹⁸ Draft comments volume 2, p 309.
²⁹⁹ Draft comments volume 3, p 144.
and a substantial cost saving would be made for taxpayers by having such work only every third year, at a very low cost in risk. As OECD already suggest this unless any change has been made, extending that suggestion is not a big step.

6.3.8 Language Question

"Comments are requested regarding the most appropriate approach to translation requirements, considering the need of both taxpayers and governments." 300

BIAC comments that permitting one common language for the master file would ease compliance. Preparation in the local language of the MNE leader should however be permitted. Furthermore BIAC comments that there should be no requirement to have the master file in languages other than English. The level of standardization of the master file should be enough for local tax administrations to understand it. 301

The Confederation of Swedish Enterprise comments that it is reasonable to expect that tax authorities specializing in cross-border taxes should be able to understand documentation in English. As such taxpayers should be allowed to submit the masterfile, as well as the country-by-country template and local files in English. If there is a need for translation into a local language it is of importance that the taxpayer is given enough time for this. A recommendation of minimum time from the OECD would be helpful. 302

The ICC leaves no comment on this.

PwC comments that it support the idea of the master file and country-by-country report to be in the English language. PwC furthermore underlines the need of giving taxpayers a reasonable amount of time to make translations when such is needed and requested by tax authorities. 303

Analysis

Commentators seems to be in agreement on that the master file and country-by-country report should be possible to file in English. One commentator even suggest local files should be possible to file in English. Transfer pricing is a very international area and most

300 Draft para 35.
301 Draft comments volume 1, p 112.
302 Draft comments volume 1, p 300.
303 Draft comments volume 3, p 145.
academic work on the area is written in English. The OECD guidelines are written in English. It is reasonable to assume that most cross-border communication are in English as it is a commonly understood language among educated people around the world. Add to this the fact that the purpose of the master file is to be a document for all involved taxpayers, it's unreasonable to demand it to be translated to potentially dozen of languages. Such demands would severely undermine the purpose of the new system and place unreasonable costs on the taxpayers. Hence, the master file should be in English if desired. Local files are mostly a local concern, and demanding them to be in English serve far less purpose than demanding the master file to be.

6.3.9 Confidentiality Question

"Comments are requested as to measures that can be taken to safeguard the confidentiality of sensitive information without limiting tax administration access to relevant information."

BIAC comments that while it welcomes the draft statement that trade secrets and similar should not be publicly disclosed, that should hold true for all information given to tax administrations. Confidentiality rules need to be imposed by either a treaty or domestic law to ensure this. As the master file and country-by-country report contains such a high amount of sensitive information its confidentiality needs to be safeguarded. BIAC suggest several such safeguards, the three major ones being:

- Disclosure of master file and country-by-country report only to the tax administration of the MNE parent. Other tax administrations are to gain access by information exchange treaties. This limits the pressure to give out these documents to minor partners.
- Country-by-country data should only be used for risk assessment, never for audits. As such those data would not be a part of a despite and such exposure in public records is limited.
- A need for specific channels where taxpayers and tax administrations can safely exchange information.

The Confederation of Swedish Enterprise agree on the importance of confidentiality, but believe it might be difficult to ensure. It is pointed out that with the master file available to

304 Draft para 41.
305 Draft comments volume 1, p 113.
a large number of tax authorities it is not possible to make sure that there are satisfying protection in all countries. To minimize the risk the proposed draft should only include data that are useful for a risk assessment. In addition to this, the master file and country-by-country report should only be submitted to the tax administration of the MNE groups parent.306

The ICC comments that more consideration needs to be taken in regards of the confidentiality of information provided. Some safeguards are suggested:

- Anti-infringement procedures in case of real damage due to disclosure of information by tax administrations.
- A need of secure channels between taxpayers and tax administrations to exchange information.
- A need of limiting sharing of information between tax administrations to those that have that particular entity in its jurisdiction.
- Reviewing the information at the premises of the taxpayer, rather than receiving and filing the information.307

PwC comments that information exchange treaties should be the method of which to transfer master files and country-by-country reports. It is recommended by PwC that information sharing between tax authorities is tracked, and that the MNE parent is informed whenever information is exchanged. There is also a need of sanctions in the case of misuse or inappropriate sharing.308

Analysis

The question of security is one that has been lifted in other answers as well, showing that this is a real concern by involved parties. As said, with the master file and country-by-country report potentially exposed to many tax authorities, confidentiality risks increases. It is suggested that if the filing is done at one place, to be distributed from there via information exchange channels such as treaties, risks are lower. The OECD point out that trade secrets must be kept unexposed, and BIAC express the opinion that this should hold true

306 Draft comments volume 1, p 301.
308 Draft comments volume 3, p 145.
for all material turned in to tax administrations. The obvious place for filing would be the tax authority of the country of the ultimate parent of the MNE group.

This raise the matter of proper channels to communicate such information and level of security. For such a system to work an efficient information exchange system is needed between most tax authorities, and for the security measures to mean anything the level of confidentiality needs to have the same minimum levels in all involved countries. If confidentiality does not hold up in all involved places, either exchange will not happen, or the information exchange endangers the confidentiality of taxpayers. To ensure functionality, it is our opinion that the OECD need to engage itself in these questions for the suggested draft to have the desired effect.

### 6.3.10 Implementation Question

> "Comments are requested regarding the most appropriate mechanism for making the master file and country-by-country reporting template available to relevant tax administrations. Possibilities include:

- The direct local filing of the information by MNE group members subject to tax in the jurisdiction;
- Filing of information in the parent company's jurisdiction and sharing it under treaty information exchange provisions;
- Some combination of the above." ³⁰⁹

BIAC comments that for the system to be effective the country-by-country report and rules surrounding transfer pricing documentation needs to uniform. The more complex rules and requirements for taxpayers and tax administrations, the likelihood of direct acceptance without local modifications is lower. As such, BIAC suggest that a step-by-step approach might be a good idea, and also gives time to fix problems in each system along the way. ³¹⁰

The Confederation of Swedish Enterprise comments that as previously stated, the master file and the country-by-country report should be filed only to the tax administration of the MNE group parent. If a tax administration other than the one holding the master file is in

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³⁰⁹ Draft para 45.
³¹⁰ Draft comments volume 1, p 114.
need of it, information exchange treaties should be used. Local taxpayers that normally do not have access to the master file should not be held accountable for not providing it.\textsuperscript{311}

The ICC leaves no comment on this.

PwC comments that as mentioned in earlier questions, PwC is of the opinion that information sharing treaties is the appropriate way of transmitting the information to the relevant authorities.\textsuperscript{312}

\textbf{Analysis}

All commentators seem in agreement of that a system where the master file and country-by-country report is filed at the MNEs parent company and distributed by exchange treaties or similar. As indicated by our previous comment on the confidentiality question we agree in this, since it would be needed for a proper confidentiality approach.

\section*{6.4 Chapter Summary}

In summary, commentators are positive to the idea of change. There are however major concerns of that the burden on the taxpayer will increase, a direction echoing badly with perceived intent of the OECD. The concern is somewhat warranted, as there is plenty of room for additional demands in local requirements, making the new suggestion potentially more burdensome than the current situation.

The other major concern is matter of confidentiality. The fact that a lot of information need to be exchanged is a concern, as there are no arranged system for this. Such an exchange system is something the OECD needs to lay a foundation for.

\textsuperscript{311} Draft comments volume 1, p 301.

\textsuperscript{312} Draft comments volume 3, p 145.
7 Final Analysis and Discussion

In this chapter the aim is to bind all analysis together in a short but effective final analysis and discussion, reminding the reader of what has been said earlier and what it should mean in relation to the actual questions asked in this thesis.

Before the final analysis and discussion it is therefore wise to revisit the questions asked in the purpose of chapter 1. One main question was asked, and it was said that three sub questions was to be answered to come to a conclusion. The main question was:

The purpose of this thesis is to evaluate if there is a need for harmonizing the current transfer pricing documentation requirements in accordance with the newly proposed discussion draft on transfer pricing documentation and country by country reporting (discussion draft) and if yes, does the new proposition have any chance of succeeding.

The tree sub-questions were:

1) How are the documentation requirements in the OECD TPG and EU TPD formed today?

2) What does the Swedish legislation regarding documentation state and how do the practitioners (Swedish tax administration) actually use the documentation?

3) What changes are suggested in the discussion draft and what would these changes imply for the current application of the documentation; Which specific questions are raised in the discussion draft, how are these addressed and do the changes fulfill what they seek to do?

It is observed that the documentation requirements of the OECD TPG are general and broad in nature. Transfer pricing is not an exact science and as such any guidelines meant to give general advice to a large number of countries is more or less forced into the broad construction of the OECD TPG. In a strict sense the OECD TPG are not documentation rules, because they are not applicable as a full rule-set on its own. In reality the guidelines are not detailed enough, but requires input from national legislation to be functional. It is important to remember that the OECD TPG are guidelines for national legislation, not rules by themselves. One thing that must be noticed when reading the OECD TPG is its heavy focus on proportionality. Basically every paragraph weigh the burden on the taxpayer towards the need of the tax administrations. It is clear that the OECD focus heavily on that

313 See 1.2.
any documentation rules must not only cover the technical needs of the tax administrations, but must also take the burden put on the taxpayers into consideration.\textsuperscript{314}

While the EU TPD are in some way similar to the OECD TPG due to its status as soft law, it is still clear that there are major differences. While both have a quite open environment, leaving nations to affect the actual use, the EU TPD has a much more legislative nature. The system of a master file and a country specific file should in theory lead to a more harmonized system with less compliance costs for the taxpayers, but given the flexibility of implementation, this is not a reality. The fact that the EU TPD has been fairly unsuccessful is clear, and this is likely due to the fact that it is not harmonized in reality, giving doubt to the taxpayers. The EU TPD system itself is very structured, and giving a more strict implementation it could possibly be very successful. The level of detail is high, the only hindrance for success in the authors eyes is the diversity in implementation.\textsuperscript{315}

The Swedish documentation requirements are put into national legislation, but the OECD TPG have an impact on its application. The documentation requirements looks strict on surface and by looking on only the legislation one can get the idea that all companies in Sweden are required to do well structured, thoroughly analyzed documentation. The reality is different as was shown in our interview with Mr. Good. In reality the demands on structure from the tax administration is lower on small companies. As said in the interview, there must be a proportionality. The burden of compiling a proper documentation is too big for smaller companies. Instead of a very formal approach, the tax administration have a very open communication with the taxpayers.\textsuperscript{316}

The changes suggested in the draft are massive. This is exceptionally clear due to the entire text being replaced. It is not a minor change in language, but a complete replacement of the current text. The new text is much more detailed, similar in many ways to the EU TPD with a master file and a country specific file. While the current guidelines are broad and general, the draft has a legislative look to it, proving a documentation system and rules.\textsuperscript{317}

\textsuperscript{314} See 3.2.4.
\textsuperscript{315} See 3.3.5 and 5.1.3.
\textsuperscript{316} See 4.3 and 4.4.
\textsuperscript{317} See 3.2.2 and 6.2.
We observe that most questions lifted specifically in the draft are quite technical. Most concern from commentators is however not technical matters, but a potential increased burden and questions on confidentiality. A question on burden is indirectly a question on proportionality. This indicate a more profound fear of a system not harmonizing at all.

The major areas identified within this thesis have been the importance of proportionality in the area of transfer pricing for both taxpayers as well as the tax administrations. In this specific context the proportionality can be both the tax administrations benefits put in relation to the burden it puts on the taxpayers but also the proportionality on a more detailed level that is take into consideration in every decision that is made. The Swedish tax administration uses the proportionality test in almost each choice they make, from the assessment phase to the actual audit. Taxpayers in Sweden are also, according to Mr. Good, using it when they create their documentation. Many smaller MNEs or big ones who have few internal cross-border activities are not fulfilling the form and information requirements that could be expected by them out of the wording of the current regulation on the area. This because the high costs involved in establishing a correct documentation. This is however accepted by the tax administration since it goes hand in hand with the proportionality with-in the area. It is simply said not reasonable. It is also one of the main concerns the industry\textsuperscript{318} has expressed, permeating all their answers, that the proposal lay too much burden on the taxpayer and that more flexibility is needed.

The authors believe that there does lay some potential excessive burden put on the taxpayer, especially at the starting phase since the two-tiered system is used by many MNEs but also the risk of national rules adding the new regulations atop of the old ones. Therefore it is of grave importance that the OECD structure the harmonized regulations in such a way that they replace the old system, thereby assuring MNE groups the same amount of burden in all the member states but also assuring that the harmonization process is eased by having countries apply the same rules.

By getting countries to apply the same rules another point of relevance is touched upon, the information exchange. One of the great unused benefits that an harmonized system could bring is the increase of information exchange, something that can benefit tax administrations together with taxpayers. The tax administration in that sense that they could get information that they would have the ask the MNE group about which could be a longer

\textsuperscript{318} BIAC, The Confederation of Swedish Enterprise, PwC Global and ICC.
process than necessary but also the fact that an increased communication could mean a development of their own way of making transfer pricing assessments. Regarding taxpayers they can benefit by having tax administrations in the countries they are active in ask for similar documentation and thereby decrease their compliance costs. It might also lead to a reduction in the risk of being audited if tax authorities have better communication and your MNE group has already been audited by another trustworthy country. Of course there is a risk in an increased documentation exchange which might lead to sensitive information getting into the "wrong hands". The authors are in agreement with the industry\textsuperscript{319} that this area needs to be well regulated and that the information should be provided by the MNE groups parent company. The potential benefits of harmonizing the requirements outweigh the potential downsides since the changes will most likely reduce the compliance costs and create a guidelines that are easier to follow according to the authors.

The affect the proposal would have on the Swedish system is that the two-tier approach would be put in place but also the now lacking information exchange would increase which is a great benefit according to the authors. According to Mr. Good the actual changes will be few for the tax administrations\textsuperscript{320} since they will still make a similar assessment and for him the certain structure is not as important as getting the necessary information. We believe that the necessary information will probably be provided to a larger extent if there is some form of structure that gives the taxpayers a better insight on what they need to provide.

According to the tax administrations together with the industry the draft has been formed rather quickly but neither party has stated that this has affected the drafts quality.\textsuperscript{321} This indicates that the said changes are sought since both parties would probably be very negative if they thought otherwise. One thing that the draft needs to elaborate on is how the information exchange is supposed to be regulated if the system is to be used to its optimal potential. By that said the authors mean that for companies and countries to be comfortable in the new system matters like confidentiality needs to be well regulated.

One of the purposes of this thesis was to examine whether the OECD proposal is going towards a system alike EU TPD. The similarities are many since the EU TPD documenta-

\textsuperscript{319} See 6.3.8 and 6.3.9.

\textsuperscript{320} See 4.4.5.

\textsuperscript{321} See 4.4.5 and 6.3.2.
tion requirements as such are based on the OECD TPG but also the fact that the proposal has a similar purpose and way of achieving it. The two-tier approach is something that is applied within the EU TPD and the purpose of harmonizing the documentation requirements and structures to benefit taxpayers and tax administrations are also brought up in the discussion draft.\textsuperscript{322} Since the EU TPD use the same basis as the OECD TPG it is hard to say that the OECD new proposal is going towards the EU TPD, it is however clear that the structure of the EU TPD must have had some impact on the proposal. It is also important to take into consideration that the EU TPD has not had a great impact on the current documentation climate since most companies stick to the way they have always done it or the way other companies do it. The authors believe that the OECD is a better organ to influence the direction that transfer pricing should go than the EU. The effects will be bigger and it is not until these effects start to show that one knows if a harmonization benefits the whole area of transfer pricing or if the burden becomes too large for the taxpayers.

The authors suggest that a clearer tool for using the "proportionality test" in transfer pricing assessments should be stated in the new proposal. The authors suggest that tax administrations should take these facts into consideration when they make the decision to make an audit:\textsuperscript{323}

- The value of the transaction
- The level of complexity of both transaction and MNE group
- The necessity of the information to make an assessment
- The accessibility of the information
- The cost of providing such documentation

But also the points that the Swedish tax administration work by:\textsuperscript{324}

- Is the amount of the transaction adequate?
- Is the specific question provable?
- The level of complexity in relation to the other two factors

\textsuperscript{322} See 3.3.2, 3.3.3 and 5.2.

\textsuperscript{323} Also mentioned in 4.6.

\textsuperscript{324} Also mentioned in 4.6.
By providing more clear directions for tax administrations companies can easier identify what they should work towards when they are deciding the transfer price but also creating the documentation. Critics might claim that it will help the MNEs who want to transfer their profits to another state by having them know what the tax administration is searching for but the authors find this argument irrelevant because these suggestion will only work as something to have in mind when making the assessments and if companies are working towards shifting their profit base this information will not help them.
8 Conclusion

Transfer pricing is a cross-border activity that has rules which are applied differently in separate states. The current non-harmonized system that is based on recommendations from the OECD has proven to create a diverse climate for MNE groups which consequently has led to high compliance costs in order to provide the correct type of information to the different states demands. It also leads to a climate where tax administrations are safe in their own rules and interpretations of the guidelines provided by the OECD which impairs the communication between tax administration from different countries. Communication and a harmonized tool for making transfer pricing assessments creates a similarity in application of the documentation requirements which reduces companies compliance costs but should also function as a catalyst for evolving the area of transfer pricing audits since tax administrations can learn from each other.

The OECD presented discussion draft is a suggestion that has been formulated fairly quickly, which both tax administrations and taxpayers have reacted to. The main question of this thesis is whether or not there is a need for the harmonizing changes brought upon by the discussion draft and if the draft has the tools to succeed. By reviewing the current system, with comments on the draft from four independent parties from the industry\textsuperscript{325} and interviewing a representative from the Swedish tax administration the conclusion is that a harmonization would benefit the transfer pricing situation for both parties. A harmonization is desired and should function more in accordance with the purpose of the documentation requirements but is not essentially needed. If the suggestion has a good chance of succeeding is another question, as for an effective system a large consensus is required. There is a risk that to reach such a consensus the draft must be hollowed out towards a more general wording, like the current OECD TPG.

\textsuperscript{325}BIAC, The Confederation of Swedish Enterprise, PwC Global and ICC.
9 The Future

If you as a reader found the contents of this thesis interesting, there are plenty of opportunity in the close future. The area covered in this thesis is currently "under construction" and the following years will be interesting since many changes might come. Subjects of interest could be:

- How is the transfer of information between tax authorities regulated and is it safe enough for the MNEs to provide their confidential information?
- If the said changes are put in place; is the burdens put on the taxpayers proportionate to the benefits provided to the tax administrations.
- How many changes will the draft go through before accepted? And will the final product be anything like the current draft? A close to worldwide consensus on a document of rules is basically unheard of.

We, the authors, will closely follow the development with interest!
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