

June 20, 2018

Via E-Mail

TransferPricing@oecd.org

The OECD

To: Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA

Public Comments: Scoping of the future revision of Chapter VII (intra-group services) of the Transfer Pricing Guidelines

Dear Madam/Sir

The business federation SwissHoldings represents the interests of 61 Swiss-based multinational enterprises from the manufacturing and service sectors (excluding the financial sector).

SwissHoldings is pleased to provide comments on the planned revision of Chapter VII of the TP Guidelines (**in the following TPG**).

Our comments to the TPG are hereinafter provided.

1. We welcome and appreciate the OECD's effort to update and provide further practical guidance on Chapter VII of the TPG. We appreciate the update made with regard to the additional guidance and simplification measures for low value adding services.
2. A balance between the level of information requested and the compliance and extensive audit management burden for taxpayers needs to be maintained. We do not have the feeling that this is the case with current TPG and practical experience in tax audits. Hence, further simplification measures need to be considered. Moreover, a consistent (global) application of the revised TP rules needs to be ensured.
3. With regard to services we would like to highlight that it needs to be ensured that all (service) **costs are tax deductible** within a group and double taxation is avoided for taxpayers. In contrast to the assumptions in the general BEPS discussion, unfortunately double taxation, as opposed to non-taxation, is one of the main challenges in practice within the context of intragroup service transactions for MNEs. Hence, further clarification and mitigation measures needs to be considered.
4. Another critical area is the application of **withholding taxes** for intragroup services. Application of WHT often leads to double taxation (not fully recoverable) and a significant administrative burden for taxpayers and tax administrations. We appreciate the acknowledgement of the practical challenges with the new section D.4. (par. 7.65) of the revised TPG. However, the challenges still exist in practice. Therefore, we strongly recommend limiting in general the application of WHT for all type of service transactions. At a minimum, if WHT will apply, it should

be limited to the profit element (mark-up), and this should be applied to all types of services AND actually be implemented in local tax regulations.

5. In practice we face often also challenges in the area of **indirect tax customs**. Hence, we also recommend eliminating indirect tax impact such as non-recoverable VAT and/or import duties on services and/or similar local charges.
6. For the transfer pricing analysis (in particular during tax audits) tax administrations must also analyze and consider the **whole value chain and transfer pricing model** of the group and assess whether the service fee (input transaction) is eventually passed on – in a second step - by the service recipient/beneficiary to other members of the group (e.g., HQ) via other intercompany transactions (output transaction) and not only the services in isolation.

For instance, one group entity (service recipient/beneficiary) might receive “support services” (e.g. finance, accounting, HR or management) from other group members on a regular basis. The main function of this group entity (service recipient/beneficiary), for example, is to perform distribution activities or contract manufacturing services for another group entity and all costs - including the costs related to the “support services” - are indirectly (as a second step) passed on via other transfer prices for other transactions (e.g. contract manufacturing fee or fixed distribution margin) to another group entity. As the received “support services” represent from an economic perspective “pass-through costs” for the service recipient/beneficiary, **as a simplification measure** lower requirements and efforts should be applied to assess and document the arm’s length nature of the received “support services”. A tax deduction should always be ensured.

7. Moreover, we recommend considering **further simplification measures** and options to recharge (routine) shared service costs to one or limited key entities within the value chain (such as the key entrepreneur within the value chain of the group and the entity which receives and is entitled to the residual profit). This option would significantly minimize the compliance burden and tax audit management efforts and risks for centralized groups.
 8. Further practical guidance and examples of the treatment of so called “**pass-through costs**” (or cost plus on local “value added costs”) would be appreciated. The clarifications in paragraph 7.34 and the new par. 7.61 for the treatment of “pass-through costs” is helpful. Further practical examples AND in particular actually acknowledgement/acceptance by tax authorities in practice would be appreciated.
 9. In the current business reality, it is becoming increasingly difficult if not impossible to use the direct charge method for most of the centralized services. Current chapter B.2.2.2 seems to indicate that indirect charging methods are some sort of second-tier solution while in practice they are a worldwide standard. We believe that it should be stated that most MNEs use indirect charge methods for centralized services and that this is a globally accepted approach.
 11. If the benefit test is still required at all in future, at least we strongly believe that the new **simplified benefit test** should be applied for all type of services.
 12. In the current version of the TPG, the benefit test is applicable solely to service transactions. The aim of the benefit test is to assess whether an independent party would be willing to pay for particular services or bear costs to perform particular activities by itself. If so, there is a transaction, if not, there is none and therefore no remuneration is to be paid to the service provider. This analysis, in its core, is not different from the guidance provided in Chapter I of the TPG that addresses the issue of accurate delineation of the actual transactions between related parties which requires an analysis of the economically relevant characteristics of the
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transaction and relevant circumstances in which the transaction takes place. Having accurately delineated provision of particular services as one of the actual transactions in line with the guidance from Chapter I of the TPG, should require no further analyses to reconfirm this fact.

13. From our perspective the focus should be to prove that that the **activities exist** (costs incurred) and the cost base of the service provider is appropriate. A statement of the certified accountant (e.g., the statutory auditor) that the costs have been properly recorded in the books of the service provider should constitute a sufficient proof for the tax authorities who should not request any further accounting records from the foreign service provider. With regard to appropriate cost base we mean that costs for so called - shareholder activities - should be excluded from the cost base of a recharge. Shareholder costs needs to be borne by that parent company of the group. Again, key is to ensure that all (service) **costs are tax deductible** within a group. I.e. OECD should consider replacing the benefit-test with a “cost base test”.
14. In our global competitive environment, **multinationals cannot afford to perform non-value adding activities** (and/or duplicative activities); or probably the more correct economic term an “inefficient operating model/value chain”. Insofar, given the competitive environment there is no need to continue to perform a benefit-test for service transactions, i.e., except the costs for shareholder activities, all other service costs are performed for the benefit of one or several group members. Hence, again the focus of the analysis must be the right cost base, allocation keys and the mark-up to be applied on the right cost base (excluding pass-through cost, if relevant).
15. We appreciate the efforts to clarify the definition of shareholder activities. However, we would welcome a clarification that there exist only 2 categories:
 - *Shareholder activities*, where the cost should be borne by the parent company as the ultimate beneficiary); and
 - *Services*, where the costs should be borne by the respective recipients/ beneficiaries of the services within the group (or to HQ if the simplified method is selected, see comments above).

We also recommend avoiding reference to the old 1979 Report in paragraph 7.10 and the 1984 Report in paragraph 7.9. These references could give the impression that these old Reports are still applicable legal sources to interpret the arm’s length principle and/or “stewardship activities” is still a category taxpayers need to consider.

16. The examples mentioned in paragraph 7.9 are helpful to clarify the distinction. However, the examples need to be clear to avoid disputes in the future.
 17. It would be helpful to provide guidance on characteristics and pricing of high-value services including a number of examples categorizing certain types of services as high or not high value. In practice, services can either attract relatively moderate remuneration if based on costs and, in some cases, incomparably higher remuneration if based on results. There is no clear guidance as regards factors which determines how particular service transactions should be assessed from a transfer pricing perspective, which can lead to disputes around the extent to which particular services are considered as high-value and what should be the basis for remuneration in return for the service.
 18. TPG should acknowledge that depending on the service type and the functions and risks assumed by the involved entities cost based service charges may be based either on budgeted costs or on actual costs.
 19. In case it is concluded that a service fee based on actual costs is an arm’s length consideration for the services provided, it should be acknowledged that in the business reality of a large MNE
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it can be difficult to calculate such service fee in real-time. This may be specifically the case when one central entity is pooling costs of services performed by several sub-suppliers in order to provide a comprehensive service to its related service recipients. In such cases, the complete and accurate information about related costs can be only available after all the accounting records are booked, usually several weeks after year end. In such cases, MNEs usually agree that during the financial year the service fee is established based on budgeted or forecasted costs while after the year end, the full and accurate service fee is calculated. The difference between the amounts invoiced during the year and the service fee due based on actual costs is then either invoiced as a separate true-up/true-down invoice at the beginning of the next year or included in the service charge for the next period. TPG should acknowledge this practical challenge and the options to resolve it. The reconciliation of the difference between preliminary charges and the final service fee should be part of the documentation maintained by the service provider.

20. Similarly to the comment above, the allocation key used to calculate the service fee (e.g. revenues) may not always be available at the time the service invoices are issued. In such cases, MNEs may choose to use budgeted or historical values of the respective allocation key for preliminary invoices made during the year. Actual values of the allocation key should be then reflected in the computation of the final actual service fee as described above.

We kindly ask you to take our comments and proposals into due consideration.

Yours sincerely

SwissHoldings

Federation of Industrial and Service Groups in Switzerland



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CEO



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cc - SwissHoldings Board

- Nicole Primmer, Senior Policy Manager, BIAC
 - William Morris, Chair of the BIAC Tax Committee
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