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Via e-mail: TransferPricing@oecd.org

Working Party No. 6 on the Taxation of Multinational Enterprises

Dear Sirs,

we would like to thank you for the opportunity to submit our comments on the OECD Invitation for Public Comments on the scope of the future revision of Chapter IV of the Transfer Pricing Guidelines ("**TPG**") dealing with administrative approaches to avoiding and resolving transfer pricing disputes. In this respect, please find hereinafter some of our observations.

1. **What additional aspects or mechanisms to minimise the risk of transfer pricing disputes should be included as part of the guidance on transfer pricing compliance practices (e.g. co-operative compliance, risk assessment tax examination practices)? While input received in the past on some of these issues in the context of the work of the Forum on Tax administration will be considered, input on business experience with such aspects or mechanisms would be useful, including what have been the advantages and/or challenges?**

Transfer pricing disputes and, more in general, relationships of taxpayers with tax authorities, are a difficult area and are viewed by businesses as a fundamental concern with regard to potential compliance burden and the risk of double taxation in every jurisdiction.

The effectiveness of Chapter IV of the TPG, which provides guidance on the approaches aimed at reducing transfer pricing disputes between taxpayers and tax administrations, is highly dependent on the fast evolution of the behavior of MNEs, on the one hand, and of the attitude of tax authorities (and case law) on the other hand. This is even more true in the light of the BEPS work integrated into the TPG.

In this respect, Maisto e Associati appreciates the OECD's commitment to continue the work on Chapter IV of the TPG and believes that an update or revision of that chapter is still an appreciated initiative.

For this purpose, an important point is paragraph D of Chapter IV of the TPG. In our view, that paragraph should be updated to address not only simultaneous audits but all forms of cooperation between administrations and between administrations and taxpayers, in order to reduce the compliance burden and the risk of double taxation. For example, joint audits (but in the future also the ICAP Programme) begin to be tested. However, there is still no clear framework for the rules that may apply to such types of audits. The lack of sharp rules is one of the problems that may limit the use of this tool, for instance, triggering conflicts between internal procedural rules (e.g. statute of limitations, duration of the audits, validity of documentation acquired outside the borders of the State or with an entity that is not a taxpayer, etc.).

In this respect, it might be also useful to introduce specific rules aimed at facilitating the roll-back or roll-forward (where possible) of the results of the joint/simultaneous audit. With regard to the post-audit phase, in order to ensure legal certainty after a joint/simultaneous audit for the future years, a fast-track bilateral advanced pricing agreement should be recommended. In principle the recommendation should be that the conclusions of the joint audit be considered as applicable also to the future, provided of course that there is no change in the factual circumstances of the case.

Within paragraph D, it would also be useful to have a specific subparagraph regarding cooperative compliance. In fact, in recent years, a number of countries have adopted a co-operative compliance approach.

The form of the approach however can vary significantly: some procedures are based on enhanced relationship with no formalised procedures, whereas some other use formal agreements or rely on specific regulations or legal framework. The taxpayer thus has to deal with regimes that may vary widely from country to country and which are often designed without accurately balancing the needs of the tax authorities with those of the taxpayers. In our opinion, it would be useful to provide general guidance on the principles that should be applied in the context of cooperative compliance regimes adopted by the different countries. In this respect, some of the issues that could be addressed are the following:

a) given the central importance of Tax Control Framework Systems, it would be useful to delineate some principles on how these frameworks can best be assessed (with specific reference to transfer pricing issues) and to establish a standard approach on how to implement that Framework;
b) specific rules governing disclosure and confidentiality should be adopted. Indeed, in our opinion, from a taxpayer perspective, one of the main challenges is the risk connected to the disclosure of confidential information to tax administrations and the possible (mis-)use of such information outside the cooperative compliance program.

In addition to the above, it might be useful if the guidance contained in paragraph D could be extended to the application (or non-application) of penalties where the tax administration ends up disagreeing with the position taken by the taxpayer.

Moving to paragraph B.3. of chapter IV, which relates to the application of penalties, we believe that this paragraph should be further supplemented in order to clarify the requirements for the non-application of penalties. Indeed, the non-application of penalties is often used as a negotiating tool during the discussion between tax administrations and taxpayer, whereas it should be an automatic (and binding) course of action for the tax administration.

A different approach would be contrary to the principles of transparency, good faith, fairness and cooperation on which any penalty-protection regime is based. In addition, the use of penalties as a negotiating tool may constitute a disincentive for taxpayers to pursue a MAP instead of

accepting a settlement option on a transfer pricing claim. In this respect the TPG should make it clear that the existence of a minimum standard of documentation and the formal compliance with the disclosure regulations of a country should put the taxpayer under an automatic protection from penalties (in case of claim), thus eliminating any discretional power of the tax administrations.

2. **Relevant aspects of the minimum standards and best practices contained in the Report on BEPS Action 14 related to transfer pricing have been incorporated into Chapter IV in the 2017 edition of the TPG. Considering this, and based on your experience, is there any additional guidance that would be useful in relation to corresponding and/or secondary adjustments to minimise the risk of double taxation?**

Maisto e Associati commends the OECD for its effort on the corresponding adjustment and secondary adjustment guidance. In the course of the review of the relevant paragraphs of Part IV of the TPG it might be useful that the attention be focused on the following topics.

With regard to corresponding adjustments we believe that still many uncertainties derive from the application of corresponding adjustments. Such uncertainties could be mitigated by foreseeing that these adjustments should be done within the context of the MAP's umbrella. This would entail that a number of clarifications already applicable to MAPs (such as the recommendations included in the Manual on effective mutual agreement procedures – MEMAP) may become applicable also for corresponding adjustments.
This would help the resolution of many issues related to corresponding adjustments: for example, the case where one country charges interest on a tax deficiency (or insists on collecting tax from the taxpayer prior to resolution of the dispute) and the other country does not pay interest on tax refunded to the taxpayer upon resolution of the dispute and the result is a notable monetary burden.

Another point to be resolved or clarified is about the relationship between corresponding adjustments and transfer pricing challenges grounded on

non-transfer pricing domestic rules. For example, tax administrations can seek the non-recognition or recharacterization of a transaction on the basis of "abuse of law" principles and, for this reason, not enable the taxpayer to obtain a corresponding adjustment in the foreign jurisdiction. Indeed, in such cases, the foreign authority may not grant a corresponding adjustment on the basis that the primary adjustment was not grounded on the transfer pricing rule.

In this respect it might be useful that the recommendations contained in the TPG stimulate (a) tax administrations making the primary adjustments to consider transfer pricing rules as the priority rule for the adjustment, and (b) – in any event – tax administrations of the foreign jurisdictions to accept to apply corresponding adjustments to cases where the primary adjustment is substantially, though not formally (because the applied rule it not a transfer pricing rule), creating a double taxation that is in contrast with Article 9 of the applicable double tax treaty.

With respect to secondary adjustments, we believe that the state of art is still very fragmented as the policy on the application of secondary adjustments varies significantly from country to country or even within the same country. To this end supplementary guidance on this issue would be welcome.

Otherwise, it is left to the discretion of the specific auditor whether or not to make a secondary adjustment. In particular, we believe that para. 4.73 of the TPG, and in particular the statement "*when secondary adjustments are considered necessary",* should be supplemented in order to clarify when the secondary adjustment is considered necessary.

Another point that we believe should be addressed is the application of withholding tax on secondary adjustment qualified as hidden distribution of dividends or hidden contributions. For instance, as already mentioned by the EU Joint Transfer Pricing Forum, most EU Member States where secondary adjustments are applied, treat them as hidden profit distributions/hidden contributions and therefore consider them potentially subject to withholding tax. By contrast, other States might have a different approach and therefore deny creditability of such withholding tax thus triggering a new double taxation.

A last point concerns the possibility to provide guidance on if, and how, to interrupt the effects of secondary adjustments over the years. For example,

we experienced cases of secondary adjustments deeming a loan to exist for the portion of the price exceeding the arms' length. In order to avoid a perpetual figurative loan, a repayment of the deemed loan could be necessary. As the deemed loan is not in the books of the related party and since the latter could not have anymore the control of the relevant funds (for example as a dividend distribution took place), the repayment could be in practice impossible. In this respect, guidance on how to address such situations would be desiderable.

3. **Element 2.7 of Action 14 minimum standards and the best practices related to APAs contained in the Report on BEPS Action 14 have also been incorporated into Chapter IV in the 2017 edition of the TPG. Considering this, is there any additional guidance that could be provided on advance pricing arrangements? Based on your experience, are any features of APAs or specific initiatives related to APAs that could strengthen their role in minimising transfer pricing disputes? What are the advantages of such initiatives and the implementation challenges?**

Regarding the role of bilateral APAs in minimizing transfer pricing disputes, based on our experience, we suggest to provide further clarifications on the relationship between bilateral APAs and tax audits. In particular, more guidance has to be provided on how to handle the mentioned relationship both during the procedure and after the conclusion of the agreement.

With reference to the procedural phase, the purpose is to avoid that a tax audit, challenging the same controlled transactions with respect to the same fiscal year, may lead to different results compared to those agreed upon in the context of the bilateral APA

For instance, in the case of a pending bilateral APA on a certain controlled transaction, it should be recommended that tax administration have to adequately evaluate the opportunity to start a tax audit on the same transaction (on fiscal years potentially covered by the bilateral APA) or, in

cases in which it is necessary to start the mentioned audit, to take into account the conditions that will be agreed upon the APA.

Following the above, a suspension of the bilateral APA in the presence of a tax audit – adopted by some countries – seems, in any case, not to be appropriate. Indeed, a tax audit, if not concluded in such a way that takes into account the bilateral APA results, may lead to a double taxation and, therefore, be in contrast with the nature of the APA itself (reducing double taxation).

Referring to the relationships between bilateral APAs and tax audits after the conclusion of the agreement, it is worth to consider that Annex II to Chapter IV, para. E.2.2, of the TPG states that "*A MAP APA applies only to the parties specified in the agreement and in respect of the specified transactions. The existence of such an agreement would not prevent the participating tax administrations from undertaking audit activity in the future, although any audit of transactions that are covered by the MAP APA would be limited to determining the extent of the taxpayer's compliance with its terms and conditions and whether the circumstances and assumptions necessary for the reliable application of the chosen methodology continue to exist*".

In this respect, more guidance should be provided in relation to the procedure for determining the taxpayer's compliance with the conditions agreed upon the bilateral APA, also taking into account that in most countries the tax officers involved in the APA procedures are not the same of those involved in the tax audit procedures.

As a last remark, we note that the BEPS Action 14 provided for some clarifications on the roll- back of bilateral APAs. However, it is important to further clarify that countries with bilateral APA procedures should provide for the roll- back of APAs also with respect to previous fiscal years not included within the original scope of the APA and within the limits of the statute of limitations, provided that relevant tax and circumstances are the same, so that a real elimination of double taxation can be guaranteed.

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Please feel free to contact us at TP@maisto.it with any questions or comments concerning this letter.

Sincerely yours,

Maisto e Associati