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Via e-mail: TransferPricing@oecd.org

Working Party No. 6 on the Taxation of Multinational Enterprises

Comments on the scoping of the future revision of Chapter VII (intra-group services) of the Transfer Pricing Guidelines

Dear Sirs,

we would like to thank you for the opportunity to submit our comments on the OECD Invitation for Public Comments "*Scoping of the future revision of Chapter VII (intra-group services) of the Transfer Pricing Guidelines*" released on 9 May 2018 (the "**Invitation**"). In this respect, please find hereinafter some of our observations.

1. General remarks

First of all, we respectfully confirm that, based on our experience, all the challenges listed in the Invitation surrounding the practical application of the guidance contained in Chapter VII of the OECD Guidelines[1] are in fact currently faced by several multinational enterprises ("**MNEs**") and frequently give rise to disputes between taxpayers and tax administrations. This is due not only to the absence of a detailed guidance in Chapter VII but also to the lack of consistency among domestic transfer pricing rules and audit practices in many countries, in combination with the increasing

[1] OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (Paris: OECD Publishing, 2017).

complexity of global business models of MNEs. The intention of Working Party No. 6 to revise Chapter VII by aligning it to the most recent developments brought by the BEPS project and by providing further guidance on its practical application is consequently highly welcomed. Indeed, without a broad alignment of the approaches to be adopted by both taxpayers and tax administrations with reference to the main practical issues concerning intra-group services, MNEs will continue facing uncertainties and experiencing disputes which may result in double taxation.

Such alignment could also be fostered by the OECD with a specific recommendation aimed at stimulating the domestic implementation by tax administrations of the recently introduced guidelines on "low value-adding services", which already represent a significant step towards the elimination of some of the above mentioned issues.

2. Observations on specific topics

Among the list of practical challenges provided by the Invitation, we highlight here below those which, in our opinion, would particularly need detailed guidelines.

2.1 First, we note that one of the most relevant issues faced by both taxpayers and tax administrations when intra-group service transactions are audited concerns the demonstration that the latter have actually been rendered and that they have enhanced or maintained the business position of the service recipient (so-called "benefits test"). Based on our experience, some tax authorities do not challenge the deductibility of intra-group service fees on the basis of transfer pricing rules, but by applying general internal law principles or provisions concerning the existence of the intra-group services and the existence of a corporate benefit.

For example, the Italian tax authorities ("**ITA**") usually require taxpayers to demonstrate that the services *(i)* have actually been rendered, *(ii)* provide benefits to the service recipient and *(iii)* are useful to the service recipient, both in the sense that they do not duplicate activities carried out by the service recipient and in the sense that there is a reasonable "proportionality" between the benefits received and the compensation paid. Where the ITA considers that the proof given by the taxpayer in this respect is not sufficient, it typically raises a challenge grounded on the

principle that the costs incurred by the service recipient are not inherent to its activity and, therefore, are not deductible (*i.e.* no transfer pricing adjustment is performed). Since the proof sought by the ITA is substantially the same as the benefits test required under the OECD Guidelines (which are often recalled by tax auditors), it is our opinion that more detailed guidance should be provided in Chapter VII in this respect. In particular, the Guidelines should establish that these types of assessment should fall within the scope of application of Article 9 of the OECD Model Tax Convention.[2] This statement, although not directly relevant for the deductibility of the costs (which could in any case qualify as non-deductible in either case), would have a crucial impact in those jurisdictions (such as Italy) where transfer pricing adjustments benefit from a penalty protection regime.

Moreover, it would have the effect to make it possible for the taxpayer to access to mutual agreement procedures under the relevant double tax treaties or (where applicable) the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises dated 23 July 1990, No. 90/436/CEE (the "Arbitration Convention").

For such reasons, we would suggest to refine the description of the benefits test and to clarify that it falls within the (wider) functional analysis that taxpayers should conduct in order to establish the relationship between the relevant services and the group's value chain.[3] Moreover, it would be useful that the OECD Guidelines reiterated within Chapter VII the need to accurately delineate the transaction (and thus to properly identify the transaction as a service) in order to avoid conflict of characterizations by different tax administrations.

The same holds true for cases where the corporate services are provided (or functions executed) on a multi-jurisdictional basis due to the matricial organization of the MNE. Also in these cases, indeed, it would seem appropriate to provide a coherent guidance on how to prove that such

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[2] OECD, *Model Tax Convention on Income and on Capital, Condensed Version 2017* (OECD Publishing, 2017).

[3] Paragraph 7.32 of the OECD Guidelines currently states that "*[i]t may be necessary to perform a functional analysis of the various members of the group to establish the relationship between the relevant services and the members' activities and performance*".

multi-jurisdictional services/activities meet the "benefits test" and may be explained and justified from a transfer pricing perspective.

2.2 We also note that the proof that the intra-group services have been actually rendered and benefitted the receiving entity requires a careful analysis of the facts and circumstances of the case, which is generally characterized by a certain margin of discretionality. This is the case, in particular, with reference to those services which are provided for by the parent company on a centralized basis (the "centralized services"). Tax authorities often challenge the deductibility of the costs for such intercompany services arguing that the latter have not been actually rendered or that they have not enhanced the business position of the service recipient based on the fact that the taxpayer did not prove that the benefit test has been met. Considering the complexity of today's MNEs' business models, we would suggest to strengthen the guidance provided by Chapter VII by clarifying the level of detail that must be documented by the receiving entity and by introducing some concrete examples of what type of evidence would be sufficient. Indeed, our experience shows that there may be cases where it is almost impossible to document that a service described in a contract has effectively been rendered. For example, it happens very often that within MNEs services are rendered on a day-by-day basis simply through conference calls or instant messaging systems and not with written opinions as could happen with external advisors.

Another issue that comes into play is the identification of the portion of the costs incurred by the parent company for the purpose of providing the intra-group services. For example, it often happens that the top management of the MNE regularly dedicates time to the definition of strategic aspects of group activities that benefit also the subsidiaries. In those circumstances – as it is extremely difficult to have the top management preparing timesheets – costs are often charged indirectly by identifying a specific percentage of the total cost of the people involved that may approximate the percentage of the time spent by the top management in order to define the strategic aspects of group activities.

In our opinion, Chapter VII should provide further guidance and identify specific audit procedures – perhaps including interviews to the personnel involved in the country of the service supplier – based on which taxpayers would be able to prove the benefits derived from the services received and

the costs incurred for rendering them at the level of the service provider (possibly by considering certain safe-harbors when services are low-value adding and there is evidence of no duplication of the same services or costs).

2.3 As a last remark, we highlight that another area of concern usually relates to the identification of appropriate allocation keys for charging intra-group services. Indeed, the tax authorities of most countries frequently argue that the allocation keys selected by the taxpayer do not lead to arm's length results and often require the production of time-sheets showing the time spent in the provision of the services which may not always be available to the receiving entity. While we acknowledge that allocation keys have to be selected on the basis of the facts and circumstances of the case, we believe that more specific guidance could be provided in Chapter VII on this issue, for instance through a number of detailed examples and specific safe-harbor rules aimed at identifying recommended allocation keys which, if adopted by the taxpayer under specific circumstances, should not be challenged by the tax administrations. This would help reducing the uncertainties and the disputes currently faced by MNEs in the context of intra-group service transactions.

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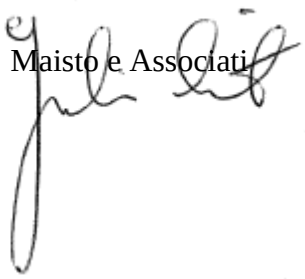
Please feel free to contact us at TP@maisto.it with any questions or comments concerning this letter.

Sincerely yours,



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