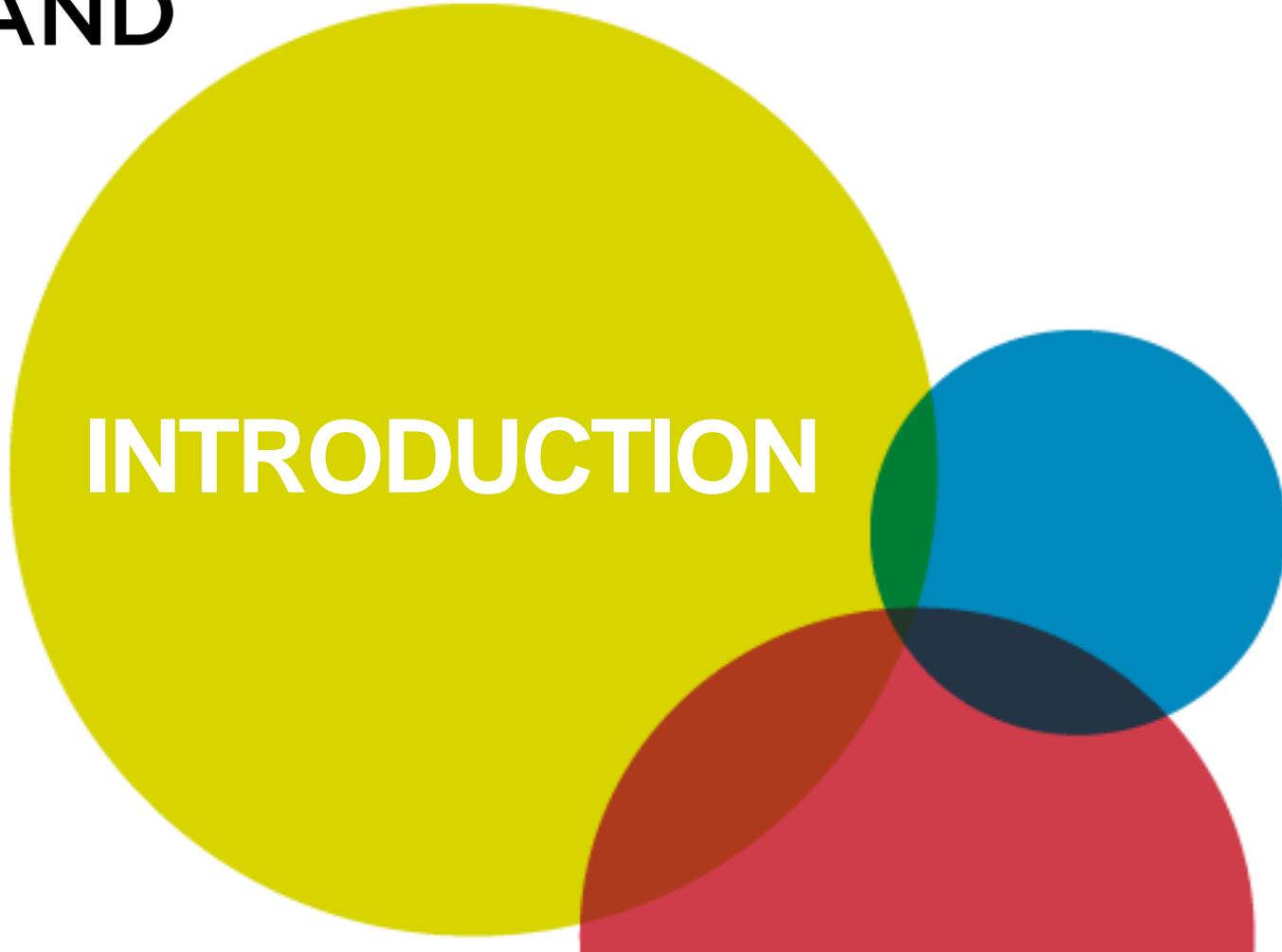


**TP AUDITS –
EXPERIENCES FROM
COUNTRIES**

**Jimmie van der Zwaan
Andreas Medler
Felipe Gonzalez
Renata Blahova
Adriana Craciun**

28 November 2019

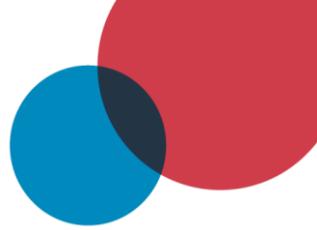
Your global tax partner

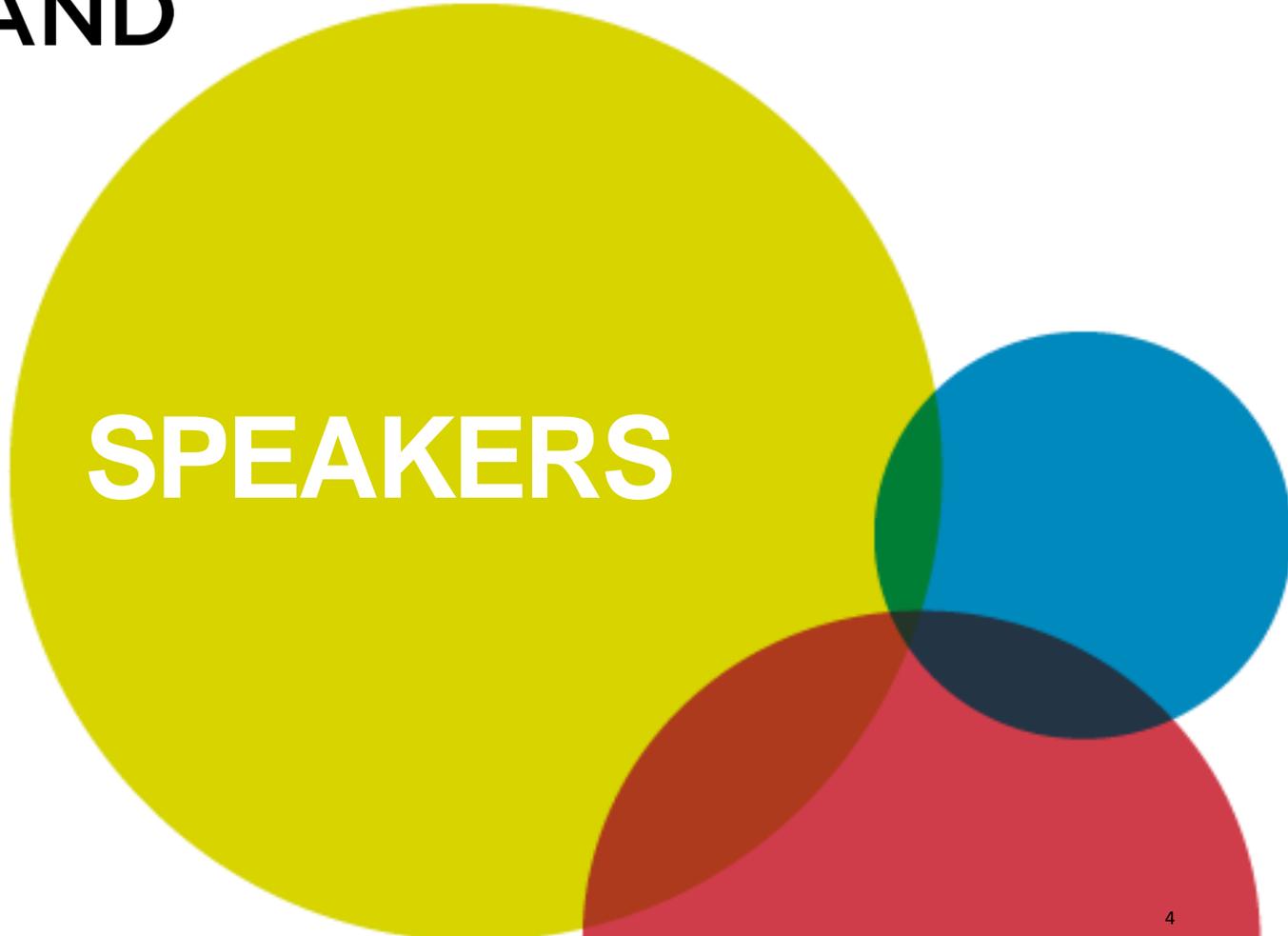


INTRODUCTION

Content

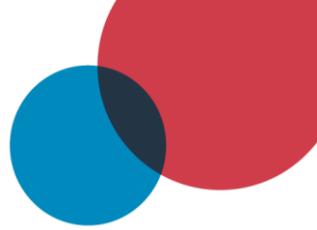
1. Introduction speakers
2. Starbucks & Fiat
3. Spain vs Ikea
4. Largest MAP Case in CEE
5. TP Audits – Romanian experience
6. Speakers bio's





SPEAKERS

Speakers



Renáta Bláhová



Adriana Craciun



Felipe González



Jimmie van der Zwaan

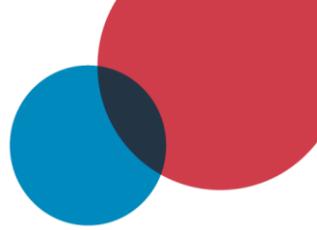


Andreas Medler



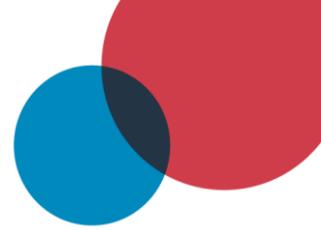
**STARBUCKS
& FIAT**

EU General Court rules on two cases regarding State aid in relation to tax rulings



- ❖ On 24 September 2019, the General Court of the European Union ruled on Starbucks (T-760/15 and T-636/16) and Fiat Chrysler (T-755/15 and T-759/15)
- ❖ The Commission was unable to demonstrate the existence of an advantage in favor of Starbucks. The Court did however uphold the Commission's decision against Fiat's tax ruling in Luxembourg

Timeline Starbucks



June 11

Formal opening decisions
European Commission

September 24

Judgements EU
General Court in
Starbucks and Fiat case

2014

2015

2018

2019

October 21

Final decisions
European Commission

July 2

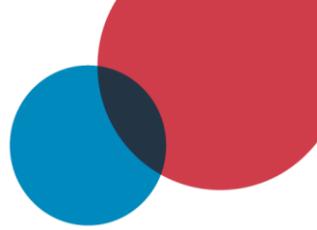
Plea Netherlands before
EU General Court

December 1

Plea Luxembourg
before EU General
Court

Appeals before the EU
Court of Justice?

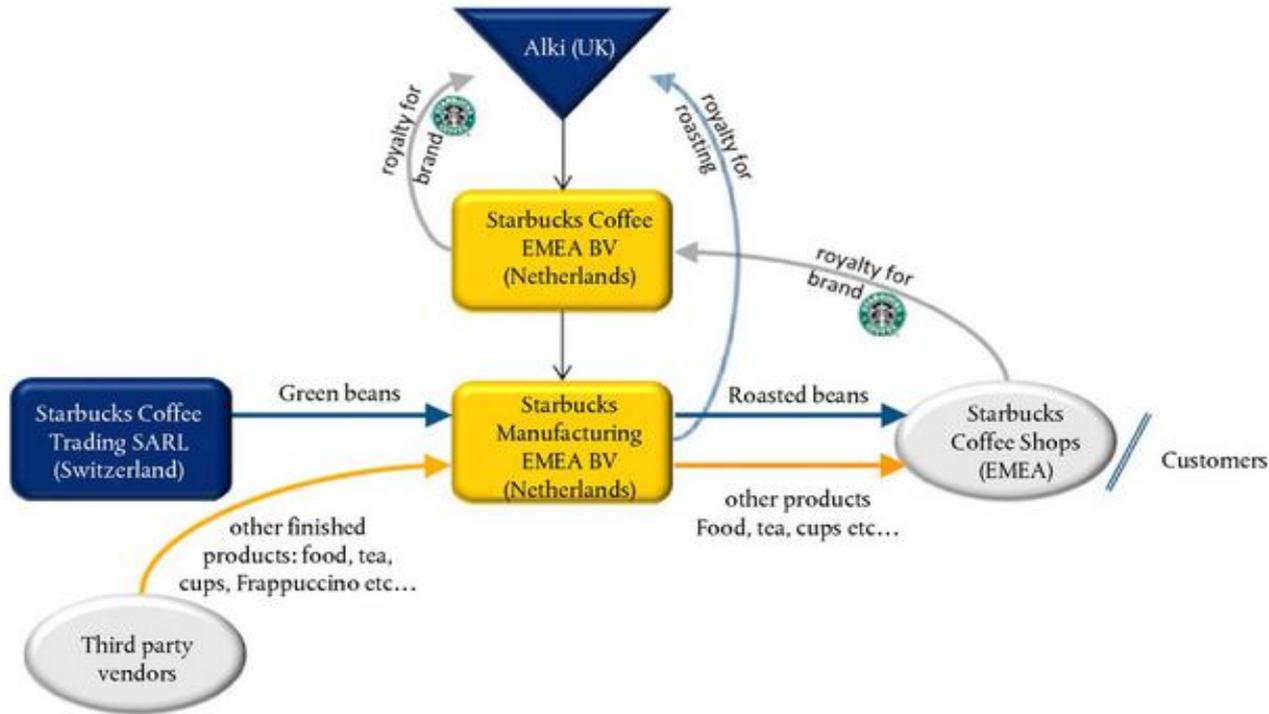
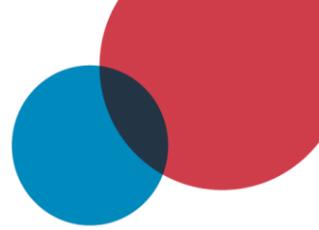
State Aid: art. 107 EU Treaty



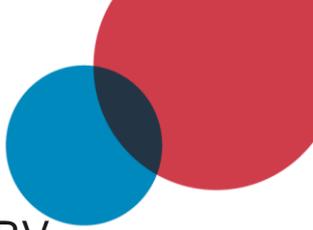
- ❖ **Advantage** granted on a **selective** basis
- ❖ Financed **by the State or through State resources**
- ❖ **Competition** has been or may be **distorted**
- ❖ Likely to **affect trade between Member States**

The General Court confirmed the right of the EC to assess the correct application of the ALP by the Member States based on article 107(1) TFEU, even if the measure assessed is an APA.

Starbucks State Aid Case

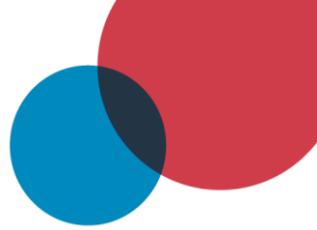


Starbucks tax ruling elements



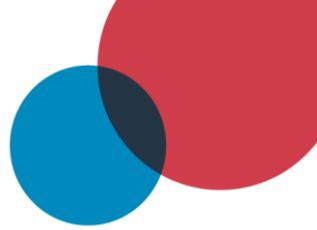
- ❖ The APA regards the determination of the arm's length remuneration for SMBV for its functions performed of roasting and logistics and a royalty payment to Alki LP, for intangibles such as roasting process and know-how.
- ❖ Starbucks and the Netherlands agreed a remuneration for SMBV, of a mark-up of X% on SMBV's relevant costs.
- ❖ The royalty due to Alki LP consist of the “residual profit” after application of the mark-up. SMBV excluded from its cost basis:
 - cost of raw materials such as green coffee beans
 - cost of Starbucks cups, napkins etc.
 - services provided by third party (consignment manufacturing contracts) and the royalty

Judgement General Court Starbucks



- ❖ General Court confirmed the right of the EC to assess the correct application of the ALP by the Member States based on article 107(1) TFEU, even if the measure assessed is an APA
- ❖ The burden of proof is not met by the Commission. The General Court makes clear that is not sufficient for the EC to successfully challenge the transfer pricing methods applied or to allege that they were incorrectly applied, without demonstrating that this has actually resulted in a more favorable tax outcome compared to standalone companies

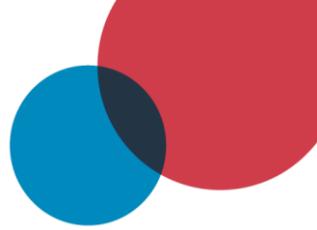
Takeaways Starbucks



- ❖ Prudent market operator vs. **arm's length principle / OECD**
- ❖ EC may test whether the **outcome** of the APA is arm's length based on State Aid. The local legislative framework allows this since it treats integrated companies and standalone companies without distinction
- ❖ It is important that **functions** are rewarded properly: outcome more relevant than journey
- ❖ The arm's length principle is considered a **proper tool**
- ❖ TP is **not an exact science** and the advantage granted must go beyond the **inaccuracies** that are inherent to its application
- ❖ Thus no state aid if remuneration within **range**
- ❖ Application of an OECD TP method does not in itself lead to an advantage. Thus **no best method rule** exists

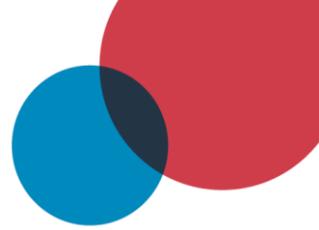
❖ TAXAND

Takeaways Starbucks CNT'D



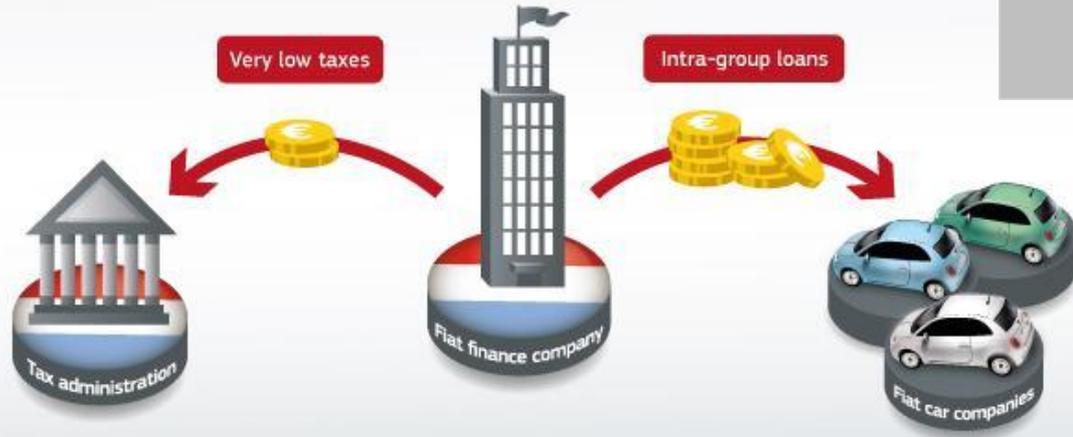
- ❖ EC bears the **burden of proof** and must quantify the **advantage**
- ❖ Tax administration may not use information of a later date (**no hindsight**)
- ❖ What can be concluded regarding the legislative framework and the BEPS updates of the OECD TP Guidelines?
- ❖ One-sided approach not per sé incorrect

Fiat State Aid Case

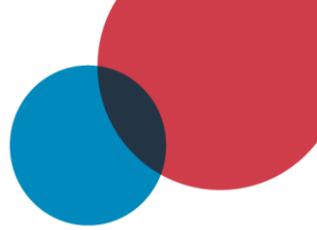


Fiat obtained illegal tax advantage from Luxembourg

**Illegal?
Luxembourg
likely to
appeal**

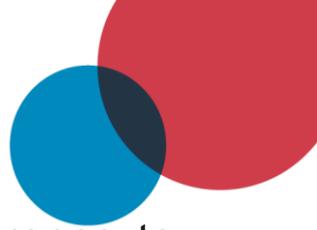


Fiat tax ruling elements



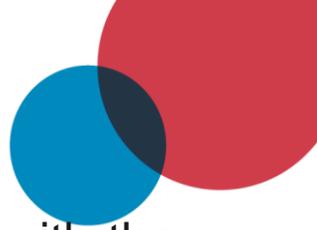
- ❖ **Capital segmented** in three categories
 - Hypothetical regulatory equity conform Basel II framework: 6,05%
 - Equity to offset FFT's holding functions (60% of equity)
 - Equity to perform functions (closing entry): 0,87%
- ❖ **Return on Equity** based on CAPM method with Beta based on sample of 66 companies

Judgement General Court Fiat



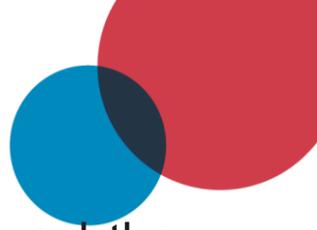
- ❖ The actual existence of an advantage must be demonstrated by reference to 'normal' taxation as defined by the national tax rules.
- ❖ If the national tax rules make no distinction between integrated companies and national companies, the ALP may be used to assess whether the tax ruling reflects the market conditions that apply to transactions of standalone companies.
- ❖ Segmentation of the capital of an integrated company is neither expressly authorized nor prohibited. However, in this case the segmentation of capital was considered erroneous and thus the whole capital of FFT should have been the basis for risk compensation. The APA is thus not a reliable approximation of an arm's length outcome and constitutes State Aid.

Comments on the Court's decision



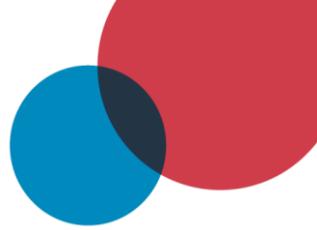
- ❖ Was the methodology applied in the tax ruling clearly inconsistent with the arm's length standard?
- ❖ Is there **only one “right” methodology**?
- ❖ The TP approach shows some resemblance with the excess profit regime in Belgium (a state aid case the Court recently decided in favor of the taxpayer)
- ❖ TP is not an exact science and the **choice of method** may be debatable, but state aid should not be direct consequence of a debatable method

Comments on the Court's decision

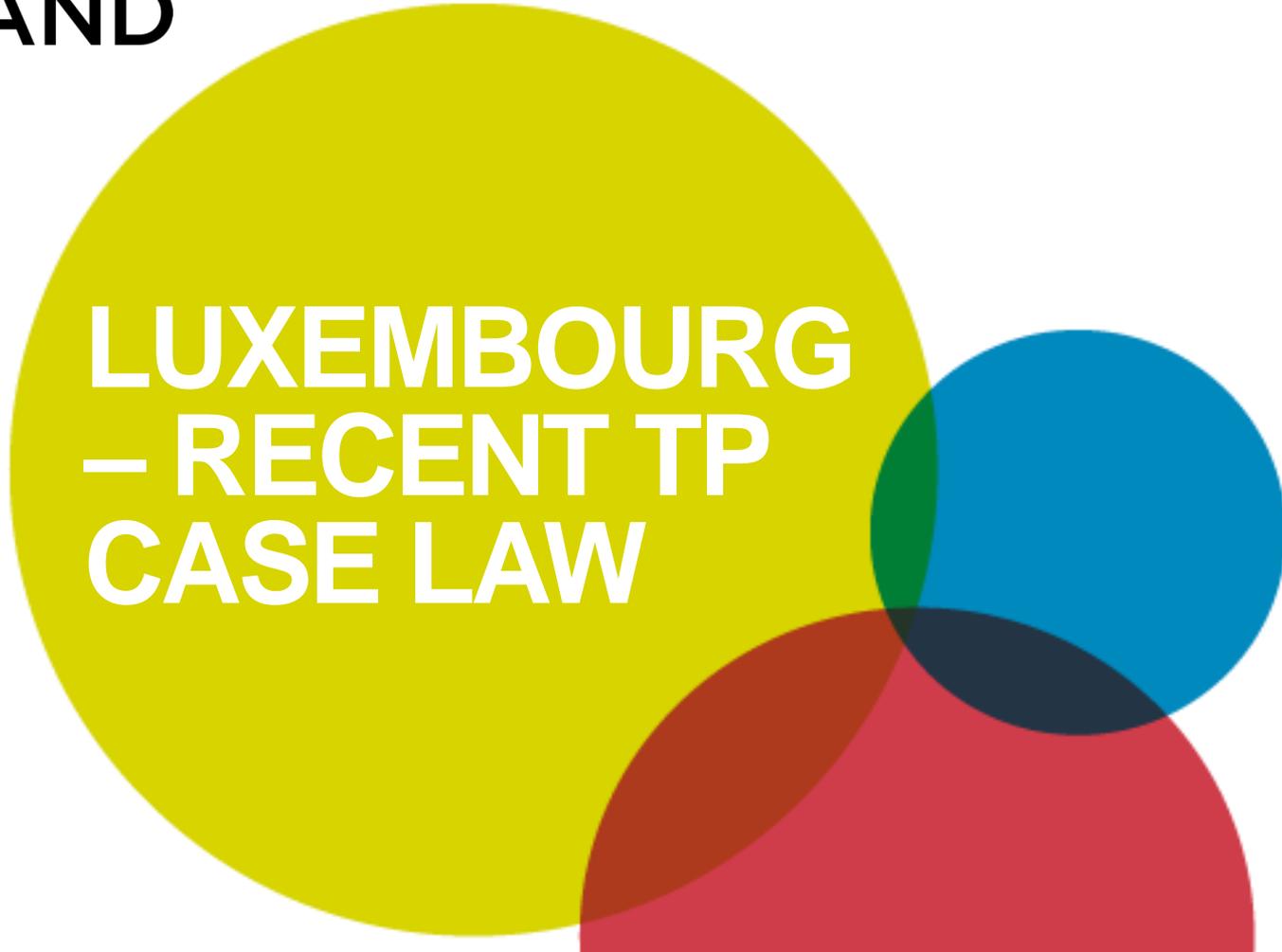


- ❖ The arm's length return on equity considered by the Commission and the Court was based on the **expectations of Deutsche Bank** regarding its own profitability (which, as we know today, did not materialize), deviating from the principle of a **case-by-case analysis**
- ❖ Why should an intra-group finance company with a more limited risk and functional profile realise the **same profitability as a regulated bank**?
- ❖ The same return on equity for different economic activities is debatable

Takeaways Fiat

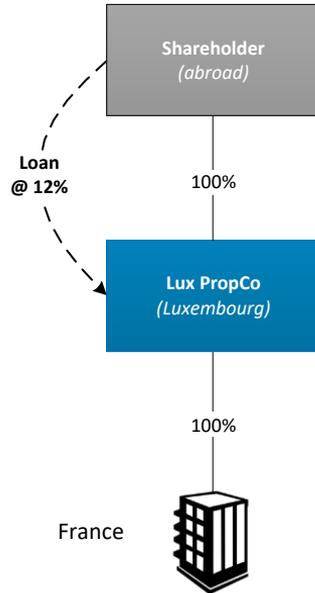
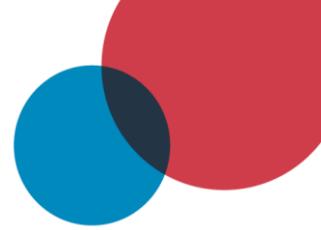


- ❖ Segmentation of capital should be justified by the **functions** performed
- ❖ It should be **demonstrated** why a certain methodology was applied
- ❖ The methodology to determine the equity at risk and return on equity may not be **inconsistent** in itself
- ❖ Taxpayers that still rely on rulings should reconsider their **tax risk management strategies** (rulings vs. comprehensive TP analyses)



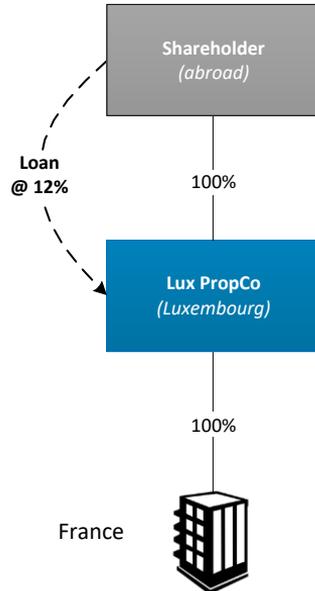
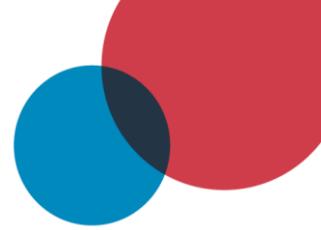
**LUXEMBOURG
– RECENT TP
CASE LAW**

Judgement from 17 July 2019



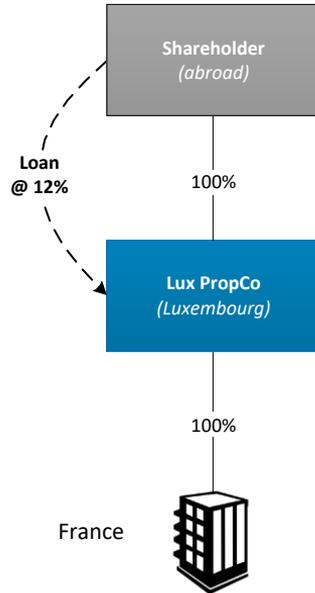
- ❖ A Luxembourg Company investing in foreign real estate had financed the acquisition of a real estate located in France with a loan from its sole direct shareholder bearing interest at 12%. At the time the loan was granted, no TP study had been prepared to determine the arm's length interest rate
- ❖ The Luxembourg Administrative Court considered part of the interest paid on an interest-bearing shareholder loan as a deemed dividend distribution
- ❖ The excess interest is subject to 15% Luxembourg withholding tax

Judgement from 17 July 2019



- ❖ A TP study was prepared shortly after the tax assessment was released in order to evidence that the interest rate was at arm's length
- ❖ The determined rate was determined based on the comparable uncontrolled price (CUP) method and corresponded to the upper quartile point in the TP study
- ❖ The tax authorities considered that the TP study prepared was only relevant for tax year 2011 as a result of which the taxpayer prepared additional TP studies for subsequent years

Takeaways

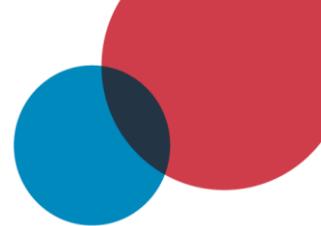


- ❖ TP documentation should be prepared in a timely manner (ideally before implementing a transaction)
- ❖ TP documentation is also relevant where no deduction is sought in Luxembourg (e.g., if foreign real estate is held through a Luxembourg SPV)
- ❖ A deviation from the median value is usually not accepted
- ❖ TP studies need to comply with certain methodological standards



SPAIN vs. IKEA
March 6, 2019

SPAIN vs IKEA March 6, 2019

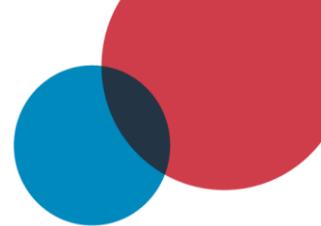


TP key topics

- ❖ Extensive use of the OECD Guidelines by Spanish Court to analyse the case and rule on it
- ❖ Multiple year data analysis
- ❖ Use of measures of central tendency: adjustment to the range rather than to the median

❖ TAXAND

SPAIN vs IKEA March 6, 2019



❖ Multiple year data analysis

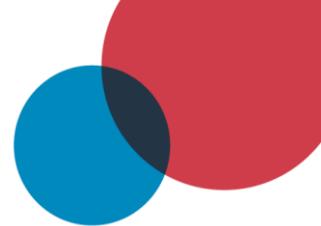
“ 3.75 *In practice, examining multiple year data is often useful in a comparability analysis, but it is not a systematic requirement. (...)*

3.76 *In order to obtain a complete understanding of the facts and circumstances surrounding the controlled transaction, it generally might be useful to examine data from both the year under examination and prior years. (...)* ”

Spanish Court interpretation of Guidelines :

Multiple year data analysis is often useful for comparability analysis but not to assess the taxpayer transfer price which must be assessed on a yearly basis

SPAIN vs IKEA March 6, 2019



❖ Use of measures of central tendency

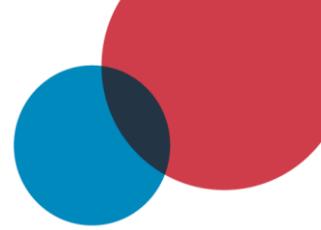
“ OECD Guidelines: *A.7.2 Selecting the most appropriate point in the range*

3.60 If the relevant condition of the controlled transaction (e.g. price or margin) is within the arm's length range, no adjustment should be made. ”

Spanish Court interpretation of Guidelines :

No adjustment if the price/margin applied by the taxpayer is within the range

SPAIN vs IKEA March 6, 2019



❖ Use of measures of central tendency

“ 3.61 *If the relevant condition of the controlled transaction (e.g. price or margin) falls outside the arm's length range asserted by the tax administration (...)*

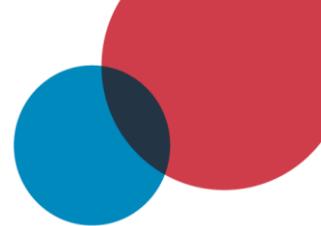
3.62 *In determining this point, where the range comprises results of relatively equal and high reliability, it could be argued that any point in the range satisfies the arm's length principle. Where comparability defects remain as discussed at paragraph 3.57, it may be appropriate to use measures of central tendency to determine this point (for instance the median, the mean or weighted averages, etc., depending on the specific characteristics of the data set), in order to minimise the risk of error due to unknown or unquantifiable remaining comparability defects.* ”

Spanish Court interpretation of Guidelines :

Range comprises results of relatively equal and high reliability, any point in the range shall be acceptable

Only where comparability defects remain in the sample, measures of central tendency shall be applied (median, mean, weighted averages, etc.)

SPAIN vs IKEA March 6, 2019



❖ Use of measures of central tendency

Spanish Court interpretation of Guidelines :

What comparability defects mean?

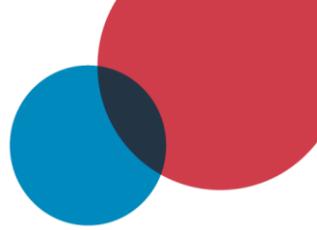
Differences between turnover of comparable entities and taxpayer does not suffice

The use by the Tax Inspection of the taxpayer' Benchmark is an evidence that no comparability defects were identified by Tax Inspection



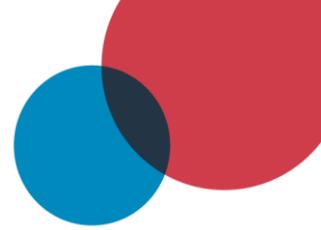
**SPAIN vs SGL
CARBON
HOLDING
April 22, 2019**

SPAIN vs SGL CARBON HOLDING April 22, 2019



- **Facts:** Spanish subsidiary funds the acquisition of intragroup shareholdings with intragroup debt
- **Resolution:** Fraud of Law, the transaction lacks of any business rationale other than tax
- **Taxpayer allegation:** Taxpayer alleged that this intragroup debt helped to redistribute the intragroup financing and that Spanish Companies were less leveraged than the Group (change of criterion: Previous Court Resolution June 28, 2018)
- **Spanish Tax Authority and Court position:** The arm's length nature of the indebtedness is not accepted as business motive

SPAIN vs SGL CARBON HOLDING April 22, 2019



ACCESS TO MAP?

It is denied the access to MAP on the grounds of Spanish legislation on MAPs that determines:

Article 8 Reglamento MAP:

Mutual agreement procedure may be denied, amongst other, in the following cases:

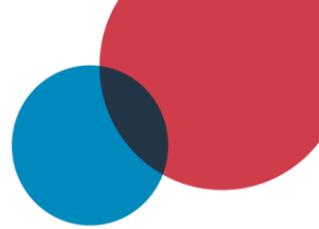
(a) In the absence of an applicable Tax Treaty with a provision on the mutual agreement procedure.

(b) When the request is submitted after the time limit provided for in the Tax Treaty or is submitted by a person not entitled to do so.

(c) When it is not appropriate to initiate a mutual agreement procedure because it is a matter of domestic law and not a Tax Treaty controversy.

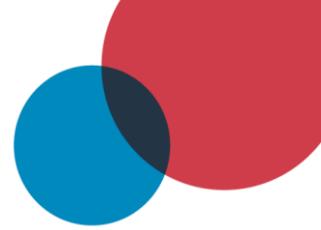
(d) Where it is known that the taxpayer's conduct was intended to avoid taxation in one of the jurisdictions involved. (...)

SPAIN vs SGL CARBON HOLDING April 22, 2019



- **Change of criterion:** Previous Court Resolution March 28, 2017
- **BEPS Action 14** encourages as a **Minimum Standard** the Access to MAP if the adjustment through **domestic GAAR** has resulted in double taxation
- **OECD 2018 Peer Review recommended amendment of Spanish MAP regulation** (in particular Article 8.1 transcribed in previous slide) because it creates risk of denial of access to MAP. Spain claimed in Peer Review that since 2016 it has never denied access on the grounds of domestic GAAR adjustment

SPAIN vs SGL CARBON HOLDING April 22, 2019

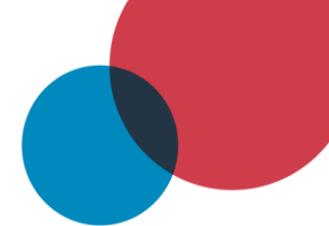


- The **Directive 2017/1852/EU** does not address this issue
- Provided that **MLI** introduces BEPS Action 14 Minimum standard it could be alleged to claim access when entered into force
- Double taxation arise due to **domestic interest barrier rule** and **non-deductibility rule applicable to intragroup financing used for intragroup acquisitions of shareholdings**, should they have access to MAP?



**LARGEST
MAP CASE IN
CEE**

LEGAL AND PROCESS SCHEME



01/12/2012
30/05/2012
05/11/2012
18/08/2014
19/12/2013

15/08/2014

11/06/2015

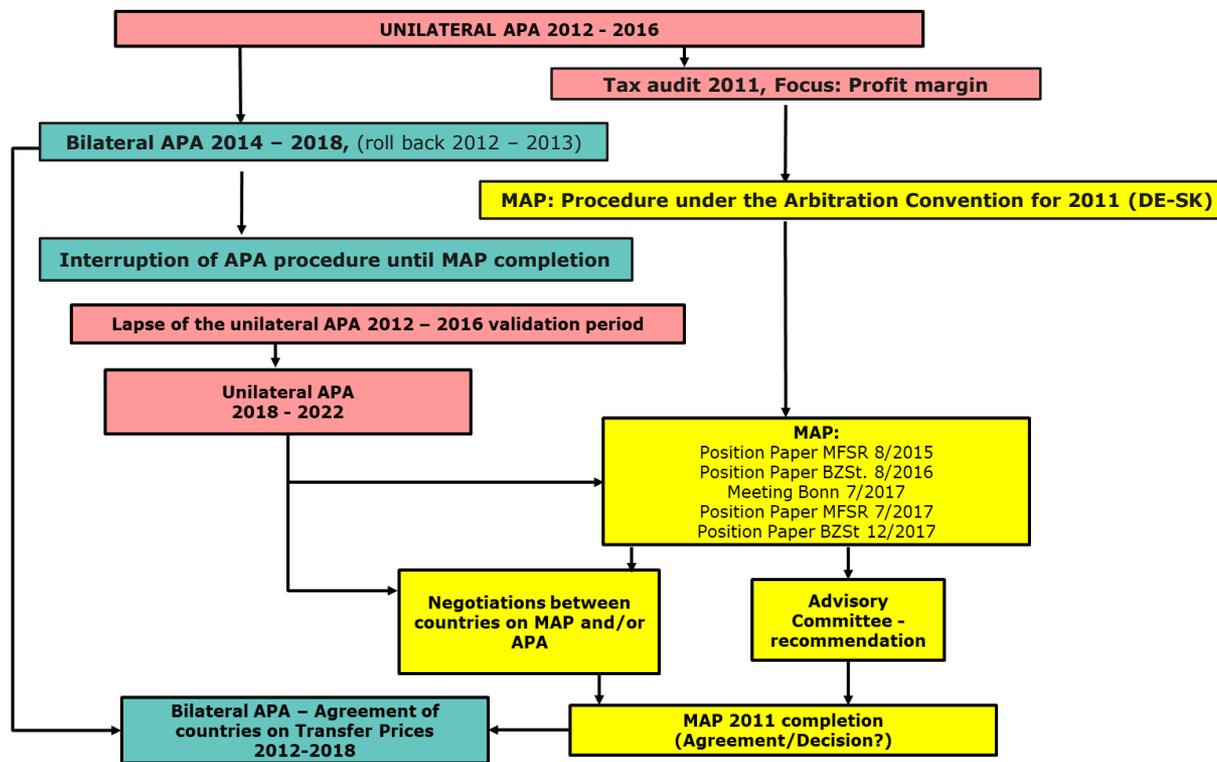
31/12/2016

26/10/2017

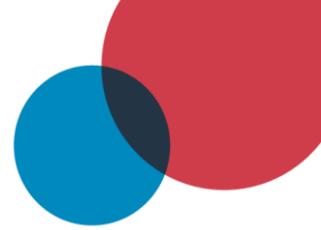
09/01/2018

31/10/2018

2019
2020



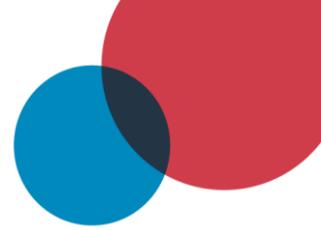
KEY TOPICS IN TAX AUDITS FOCUSED ON TRANSFER PRICES



❖ Transfer pricing

- TNMM or Cost Plus Method
- Cost base (with or without production material)
- Profit margin
- Unrelated parties non existent
- Benchmarking (s. possible approaches, point 3)
- Impact of BEPS (location savings...)

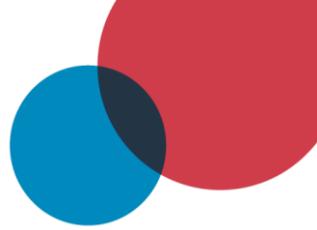
KEY TOPICS IN TAX AUDITS FOCUSED ON TRANSFER PRICES



❖ Fiscal approaches

- Basis: Added value vs. full costs (central procurement)
- Routine production vs. performance, efficiency increase
- Contribution of the local company to the product development process, start-up
- Quality control
- Production know-how, qualified workforce
- Profit margin

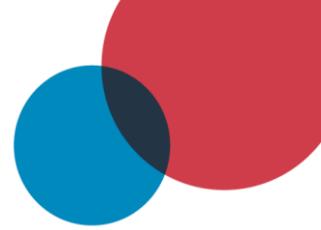
KEY TOPICS IN TAX AUDITS FOCUSED ON TRANSFER PRICES



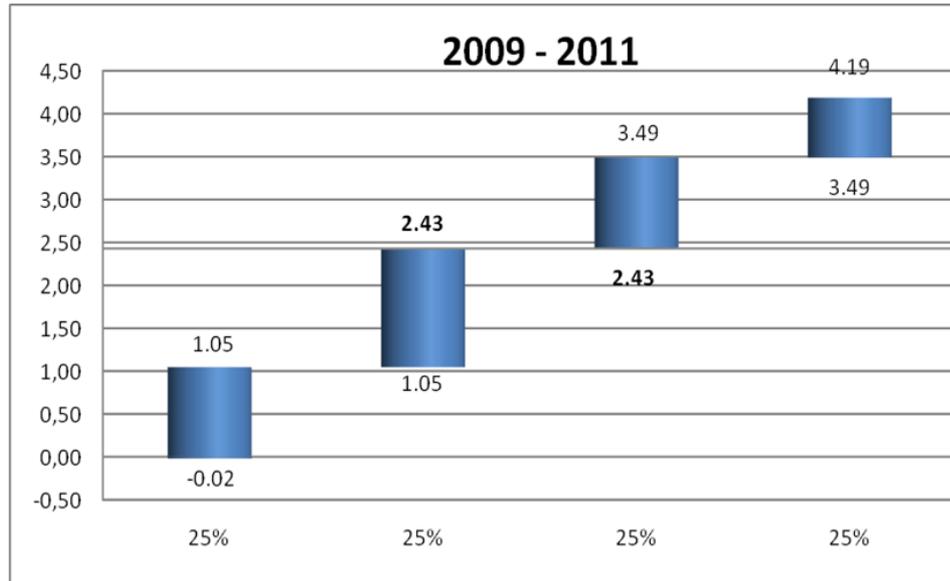
❖ Impact on local tax law

- More detailed regulation of both unilateral and bilateral procedures
- Roll-back in the case of bilateral APA (consent of countries)
- Zero or reduced procedure-related sanctions
- New regulation of the Finance Ministry on the procedure

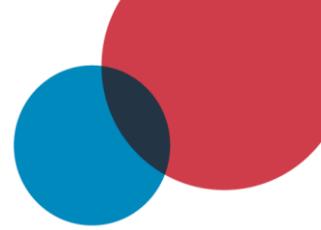
BENCHMARKING ISSUES AND ALTERNATIVES



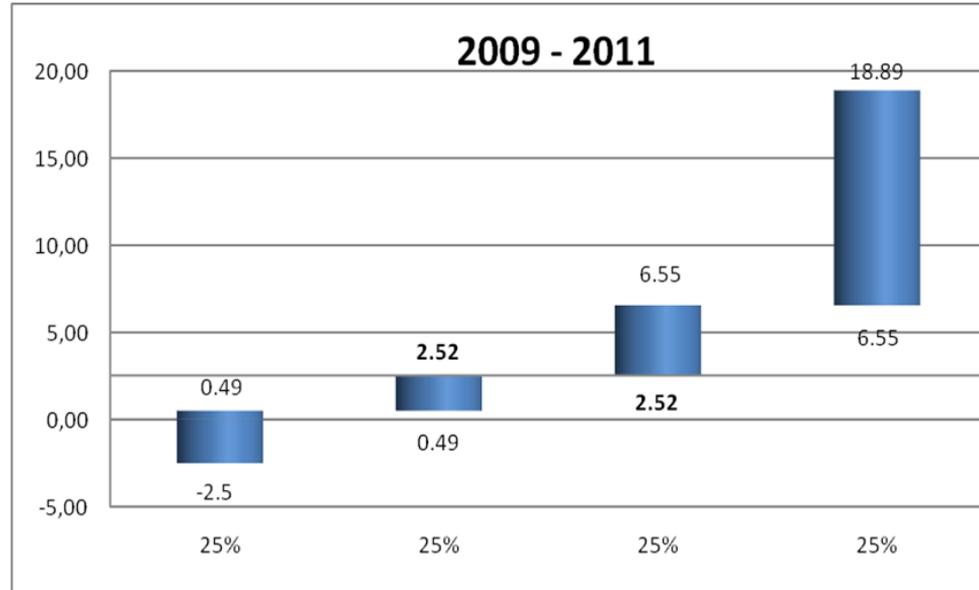
Benchmark study 1: Total of 7 (out of 10) entities comparable in terms of **size** (turnover over EUR 1 billion), **character of activities (industry codes)**, **region** (V4 – CZ, SK, PL, HU), even though parts of multinational enterprises.



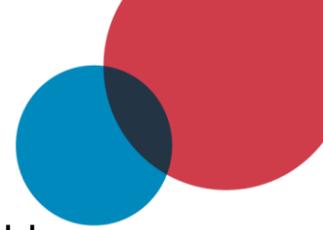
BENCHMARKING ISSUES AND ALTERNATIVES



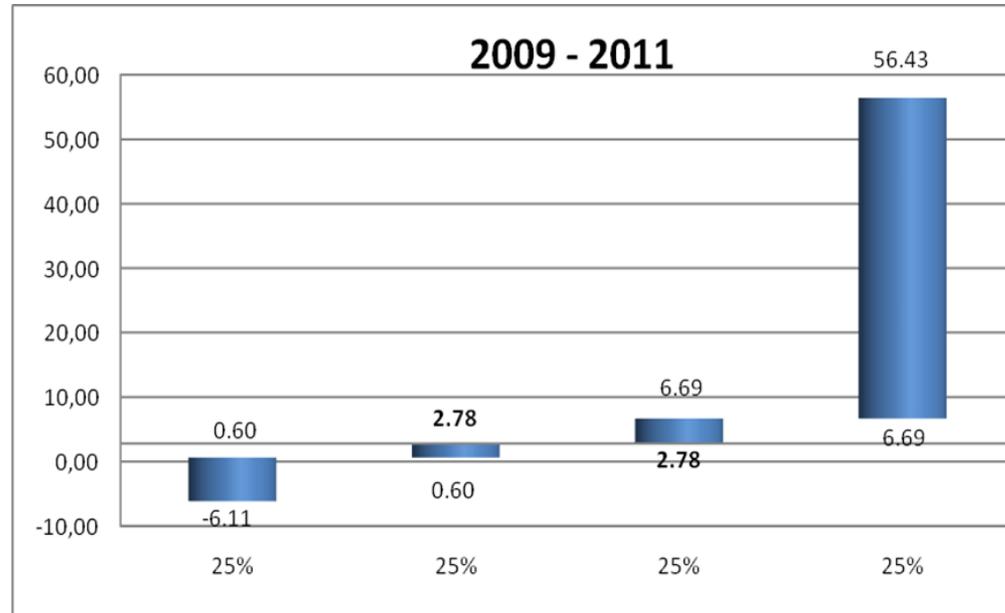
Benchmark study 2: Total of 6 (out of 17) entities comparable in terms of size (**turnover over EUR 100 million**), character of activities (broader scope of industry), wider region – Europe, but **independent and partly independent entities** (up to 50% participation).



BENCHMARKING ISSUES AND ALTERNATIVES



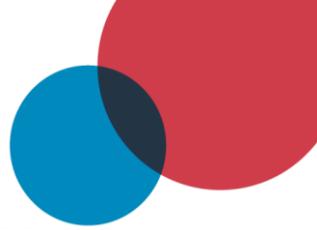
Benchmark study 3: Total of 26 (out of 64) independent entities less comparable in terms of size and character of activities (**broader scope of industry**), **wider region** – EU28.





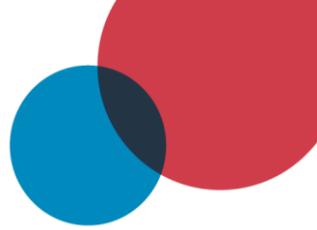
**TP AUDITS –
ROMANIAN
EXPERIENCE**

Romania – Audit and Litigation



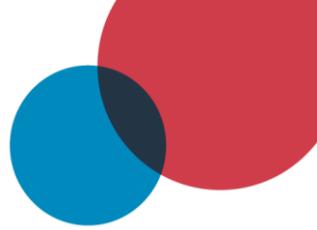
- ❖ Increased scrutiny of tax authorities with respect to transfer pricing issues
- ❖ Special audit operations initiated by the tax authorities targeting specific categories (e.g. operation “Iceberg”) of taxpayers and/or specific industries aimed at identifying TP risks
- ❖ Significant transfer pricing assessments made (e.g. decrease of tax loss, additional corporate income tax and late payment penalties, additional withholding tax)

Romania – Audit and Litigation - Issues



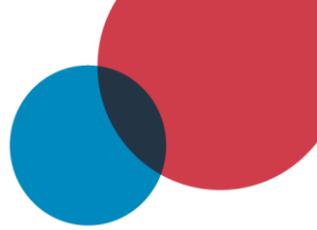
- ❖ Management & Consultancy fees
 - ❖ Highly scrutinized and denied for deduction in most of the cases
 - ❖ Initially dismissed on the grounds of lack of supporting documentation proving the actual rendering of the service
 - ❖ Currently dismissed on grounds such as: lack of benefit for the beneficiary, lack of need for the service, duplication

Romania – Audit and Litigation - Issues



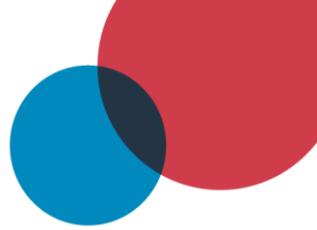
- ❖ TP methods
 - ❖ Preference for the TNMM method and tendency of tax inspectors to disregard other methods applied by the taxpayer
 - ❖ Lack of analysis of the tax authorities of special circumstances such as: start-up period, reorganization, etc.

Romania – Audit and Litigation - Issues



- ❖ Benchmarks
 - ❖ Mandatory requirement for performance of local benchmarks as a first step of the analysis
 - ❖ Independence criterion highly scrutinized
 - ❖ Year by year analysis
 - ❖ Adjustment to the median value of the range if financial indicator falls outside the inter quartile range
 - ❖ In practice, benchmark still required for low value added services

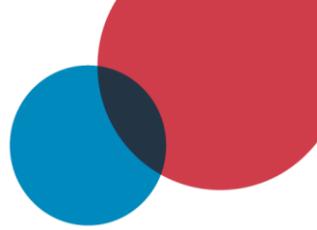
Romania – Audit and Litigation - Issues



❖ Others

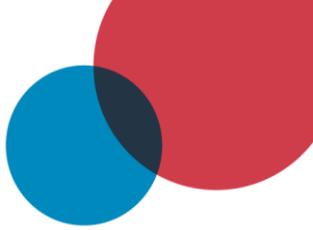
- ❖ Reclassification of transaction under substance over form principle
- ❖ Attention focused to other intra-group transactions (financial transactions, IP licensing, PEs) which were not that scrutinized in the past
- ❖ Different approaches taken by audit teams with respect to similar issues
- ❖ Initiation of criminal investigations

Romania – Audit and Litigation - Issues



- ❖ Litigation
 - ❖ Administrative proceedings in TP area not very successful
 - ❖ Most of the TP cases are taken further to Court
 - ❖ Court litigation
 - ❖ Lack of specialized courts as regards taxation matters
 - ❖ No consistency of court decisions for similar matters

Takeaways



Plan

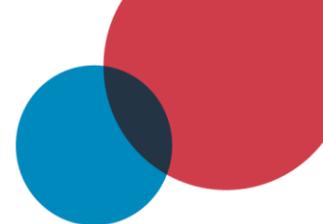
Prepare

Assess risks

Consider APAs

Document

BIO / CONTACT



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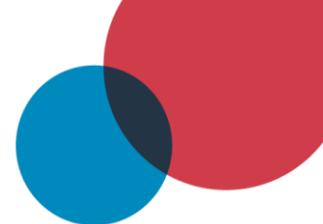
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Renáta Bláhová is founding partner of BMB Partners in Slovakia. She has 20 years of experience in tax and accounting law, specializing mainly in Slovak and international tax law, direct taxes, transfer pricing, transactional services and M&A.

Renata is president of the Slovak branch of the International Fiscal Association, a member of the Methodical Commission for Direct Taxes at the Slovak Ministry of Finance and chair of the working group Law and Taxes at the Slovak-German Chamber of Commerce and Industry.

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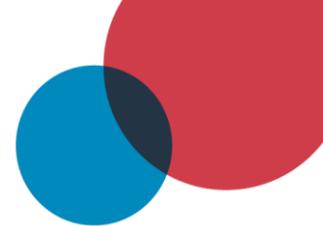
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Adriana is a certified tax consultant with over 15 years of professional experience as tax advisor with Taxhouse and KPMG Romania. She is specialised in domestic and international direct taxation, focusing on transfer pricing and international taxation.

Adriana's experience includes drafting of transfer pricing files, assistance during tax audits, tax reviews and on-going advice to multinationals acting in various industries such as retail, FMCG, banking, energy, and services. She also acted as trainer and speaker at various conferences and seminars.

Adriana holds a Bachelor's degree in Business Economics from the Academy of Economic Studies in Bucharest and she is a member of the Romanian Tax Advisors Chambers and also a judicial tax expert.

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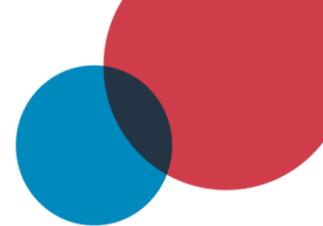
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Jimmie van der Zwaan is a partner of Taxand Netherlands. He specializes in international corporate tax and transfer pricing. He frequently works on complex business restructuring and APA negotiations. As the global leader of the Taxand Energy service line, Jimmie's clients include many corporations from the Energy industry sector.

His Transfer Pricing Team is ranked as Top Tier by World Transfer Pricing (International Tax Review). Jimmie is a member of the Dutch Association of Tax Advisers.

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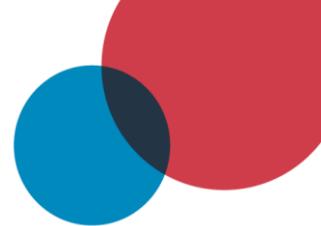
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Felipe is a partner of Garrigues since 2009.

He is a specialist in Transfer Pricing and Tax Law, having a vast experience in the advice of multinational companies and international investors with interests in Spain, being the reference tax advisor of several large multinational groups with regard to all their dealings in Spain.

He has represented many multinational groups in TP and tax audit processes, as well as in legal procedures in front of the Spanish Courts. Felipe has advised on the implementation of the global TP policy of Spanish multinational and represented numerous clients in MAP and APA procedures.

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A tax professional since 2010, Andreas has experience in Luxembourg transfer pricing and international tax advisory for a wide range of institutional investors and financial institutions. Andreas provides advice on the tax and transfer pricing structuring of alternative investments through Luxembourg (private equity, real estate, sovereign wealth funds) as well as multinational groups. He advises clients on all direct tax matters (deal structuring, corporate reorganisations, mergers and acquisitions as well as exit planning) as well as on transfer pricing aspects in relation to the pricing of financial instruments and intra-group services. Andreas is a chartered accountant in Luxembourg (“expert-comptable”) and a certified German tax adviser (“Steuerberater”).



ABOUT TAXAND

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