

Paris, 9 September 2009

Subject: Business Restructuring Project

Dear Jeffrey,

Following the Business Restructuring consultation, we at BIAAC believe it appropriate to provide a short statement of specific concerns.

The OECD (the CTPA and the Working Session) has done a very good job of distilling the emotionally charged perspectives on restructurings into their technical transfer pricing features. This has been a difficult project for the participants, but good progress has been made. In the spirit of aiding momentum, we would like to make a number of comments.

(1) Our first concern is about the **process** of finalizing the work on the basis of consensus views. After the consultation it was clear that there are many provisions on which there is good consensus, but others on which it is absent. The telling references in the text are where the multiple views are explicitly stated (“the majority of countriesSome countries however consider [a different view]” but there are others where the text is dangling in terms of describing considerations but does not reach a cohesive or consensus view. We recommend that the OECD:

Advance the Issues Notes by sharpening the papers as they relate to application of the Transfer Pricing Guidelines and the Arms Length Principle, in accordance with consultation points on which there is good consensus as to the application.

Not include (in several cases remove from the Discussion Draft) thoughts or ideas that do not have the requisite clarity or do not have good consensus

Finalise the Issues Notes and determine if any points therein justify an actual change to the TPG, and if so propose amendment, but otherwise issue the Notes and conclude the project.

The project has come a long way in emphasising a technical grounding of analysis for review of restructurings. This is a major accomplishment. There are significant hazards to doing more at this time.

(2) Two **substantive** areas remain bothersome. The first of these relates to the way that the **Arm’s Length Principle applies to modern group activities** and how to review these. The best and most practical approach is to acknowledge that the way a group chooses to structure itself should be accepted for tax purposes unless it is a sham (i.e., the substance of the actions taken significantly deviates from the legal form). In the vast majority of cases this approach would require both the taxpayer and the tax authority to price or value transactions on the basis of the actual corporate structure and the actual transactions undertaken. Many of the modern group corporate structures and decision-making processes (such as for risk management) simply have no analogue in third party

matters. That fact should not be used to justify engaging in speculation about what unrelated parties might or might not have done under different circumstances.

On a related point, in the representations received, and also during the consultation conference, a good amount of discussion focused on the conceptual and practical difficulties of maintaining that affiliate members of a MNE are, in fact, able to act as independent enterprises against a background of a MNE's group strategy and related decision making. It would seem that consensus has been reached in recognizing that it is problematic to attempt to compare the behavior of members of a MNE with that of independent enterprises. Equally, there is good evidence that progress can be made in determining pricing methodologies that can satisfy the arm's length principle while recognizing the lack of complete, precise comparability between members of a MNE and independent enterprises. However, the concept of control of risk, introduced in Issue Note 1 of the draft, is something new, and has a wider application that would merit further exploration.

(3) The second **substantive** area relates to articulating with clarity the '**exceptional circumstances when re-characterisation of a restructuring by a tax authority** may be allowed. We reiterate that paragraph 1.37 of the Transfer Pricing Guidelines is very narrow, allowing recharacterisation only in sham cases and where there is lack of commercial rationality in the re-structuring. At the consultation and afterwards there has been discussion that some governments do not believe in this constraint, reading paragraph 1.37 to permit disregarding the corporate structure and actual transactions in cases where the tax authorities do not think that a third party would engage in the transaction. This cannot be the test in a group. What is commercially rational at a group level can differ – and most often does – from what would otherwise be commercially rational for group entities were they able to act as independent enterprises. Final versions of Issue Note 4 should clearly express the intention of tax authorities to respect taxpayer business structures and transactions whenever the form and substance of the transactions coincide and the transactions are motivated, at least in part, by bona fide non-tax business purposes.

We think that it needs to be re-emphasised that 1.37 is indeed exceptional, and does not relate to comparables, but to cases of lack of substance and lack of non-tax business motivation. In the context of 1.37, the remedy of non-recognition is intended to be very narrow; indeed one major problem with a broader reading is that the consequences of non-recognition are not stated—a clear sign in tax that this is extraordinary.

We appreciate your consideration of these points, and would welcome further discussion of them.

Cordially,



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