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INTRODUCTION

Transfer pricing has been a very important topic on the tax agenda of many multinational enterprises. The topic is of interest not only to taxpayers but also to tax legislators in many countries, and the OECD.

This 6th issue of BDO's Transfer Pricing Newsletter focuses on recent developments in the field of transfer pricing in China, France, Hong Kong, Italy, Japan, Korea and Luxembourg. It follows that paying sufficient attention to transfer pricing is getting more and more important in order to comply with local transfer pricing requirements.

Global Supply Chain Management is a very interesting topic that entails transfer pricing as well as other tax and business related decisions - where best to put assets, functions and risk from a business as well as a tax perspective. Multinational enterprises will often explore options for improving their value chain, which is exactly what Global Supply Chain Management is about. You will find an interesting contribution about Global Supply Chain Management in this issue of BDO's Transfer Pricing Newsletter.

As there is a constant and increasing demand for transfer pricing engagements to be run properly, BDO's Transfer Pricing Centre of Excellence is very pleased that the transfer pricing teams in many countries keep growing. An experienced team of transfer pricing advisors is key to a further development of BDO's global transfer pricing capabilities.

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CHINA
TRANSFER PRICING DEVELOPMENT

Contemporaneous documentation

The Chinese tax authorities started to collect and examine contemporaneous transfer pricing documentation in 2010. The documentation must be prepared to conform to the transfer pricing rules. Many local tax authorities reviewed the documents carefully after receiving them from preparers. They may reject those violating the transfer pricing rules and request the taxpayers to amend the documents in accordance with their instructions.

Foreign investment companies with limited functions and risk must maintain reasonable profits. If they incur net operating losses, they will be subject to transfer pricing adjustments using the median of the arm's-length range of comparable companies, according to the transfer pricing rules.

New transfer pricing areas

In addition to the traditional transfer pricing areas of tangible property and services, the Chinese tax authorities have started to focus on the new transfer pricing areas of equity transfers, intangible asset transactions, and outbound investment. In one of the recent publicly-available cases, a tax bureau in Nanjing reportedly received a capital gains tax (CGT) payment of CNY 23.10 million from a British Virgin Islands company, after making a transfer pricing adjustment on the transfer of a Chinese-resident enterprise's shares by the British Virgin Islands company to its related-party company in Hong Kong. The tax adjustment was made because the transaction lacked a reasonable commercial purpose.

In another case, a U.S. multinational in late 2010 paid CGT of CNY 11 million to the tax authority in Dalian as a result of a transfer pricing adjustment to capital gains the company derived from the transfer of its stake in four Chinese enterprises in an internal reorganisation. The tax authority reportedly used the capital asset pricing method to make the tax adjustment and said it was the first time China had used the income approach to make a transfer pricing tax adjustment on an equity transfer.

Equity transactions are reportedly an important target for tax inspections in 2011. According to a non-public circular (Jibianhan [2011] 10), any equity transaction valued at CNY 500,000 or more will generally be inspected, regardless of whether the transferred company is a public or private entity.

Advance pricing arrangements

In December 2010 the SAT released its first APA annual report on transfer pricing developments in China. The report covers all major APA rules and procedures as well as China's APA data and information from 2005 to 2009. This report was designed to provide guidelines to enterprises interested in entering into APAs with the Chinese tax authorities and to serve as a reference for foreign competent authorities and the general public to better understand China's APA program.

According to the report, China signed 53 APAs from 2005 to 2009, including 41 unilateral and 12 bilateral APAs. 62% of concluded APAs involved related-party transactions of purchases and sales of tangible assets, 19% involved transfers of intangible assets, and a further 19% related to the provision of services.

Due to Chinese tax authorities' frequent use of public data in recent years, the most commonly-used transfer pricing method for APAs is the transactional net margin method, with the most commonly-used profit level indicators being the return on sales and the full-cost markup. The second commonly-used method is the cost-plus method (gross margin). The Chinese tax authorities hope that enterprises will provide sufficient information regarding transactions and prices in an attempt to increase the use of the resale price and profit split methods for future APAs.

The Chinese tax authorities in practice give priority to APA applications made by enterprises in order to make better use of its limited resources more effectively and to enhance efficiency, if the enterprises have provided sufficient and complete information, actively cooperate with tax authorities' examination and evaluation, and proactively submit a reasonable APA proposal, or if the enterprises' transfer pricing policies have been investigated by the tax authorities.

FRANCE

ADMINISTRATIVE GUIDELINES ON TRANSFER PRICING DOCUMENTATION

The French Tax Administration (FTA) recently published the administrative guidelines (the Guidelines) dated December 23, 2010, on transfer pricing documentation (instruction 4 A-10-10).

The Guidelines are the official interpretation of articles L13 AA and L13 AB of the French Tax Procedure Code (FTPC), enforced as from the 1st of January 2010, which require given French entities to provide transfer pricing documentation.

Scope of application

The documentation requirements apply to any legal entity when one of the following conditions is met:

- The entity has a gross annual turnover or gross assets value equal to or exceeding EUR 400 million;
- The entity directly or indirectly owns at least 50% of companies that meet the EUR 400 million criteria;
- More than 50% of the entity's share capital or voting rights are owned, directly or indirectly, by French or foreign entities that meet the EUR 400 million criteria;
- The entity benefits from the worldwide tax consolidation regime in France; or
- The entity is in a consolidated tax group in France where at least one company of the group meets any of the above criteria.

The Guidelines also clarify the FTA's view that permanent establishments are within the scope of the transfer pricing documentation requirements (which was implied in the law, but was not explicitly stated).

Content of the documentation

The documentation requirements are derived from the Guidelines and recommendations elaborated by the European Union joint Forum on transfer pricing. Two levels of information are required: general information concerning the group of companies and specific information concerning the company being subject to a tax investigation.

The general information must allow the FTA to understand the economic, legal, financial and fiscal environment of the group. It comprises:

- A general description of the activity, including: changes occurred during the audited years; group legal and operational structures, identifying the related companies engaged in the intra-group transactions; description of the functions performed and of the risks borne by the related companies to the extent that they have an impact in the audited company;
- Identification of main intangible assets having a link to the (audited) company; and
- A general description of the implemented transfer pricing policy.

The specific information concerns elements allowing the FTA to appreciate the conformity to the arm's length principle at the level of the tax audited entity; in particular, the activity of the entity, the operations and flows realised with the other entities of the group, the distribution agreements and the preliminary transfer pricing agreements as well as the implemented transfer pricing determination method and, if necessary, the relevant elements of comparison.

Furthermore, the Guidelines require that the documentation should be updated. It is accepted that such update should be done every three years.

Timing

As required by article L13 AA, the taxpayer must be able to produce this documentation on first request from the inspector during a tax investigation, and thus on the first day of the audit.

In the event of a failure to produce such documentation, the taxpayer exposes himself to a formal demand from the administration to present sufficient documentation within a 30 day period.

If the FTA deems the documentation report to be incomplete, a 30-day 'grace period' is given to the taxpayer to complete the documentation. However, the Guidelines do not specify whether or not a taxpayer could accumulate both extensions.

Language

While the documentation may be written in a language other than French, the FTA are allowed to request a translation of the documentation report into French. However, the Guidelines are silent regarding the time frame for providing the French translation.

Penalties

In the event of non compliance with the documentary obligations, the company will be penalised by a fine of 5% of the profits considered as transferred abroad, with a EUR 10 000 minimum per Financial Year. At present, only the EUR 10 000 penalty applies.

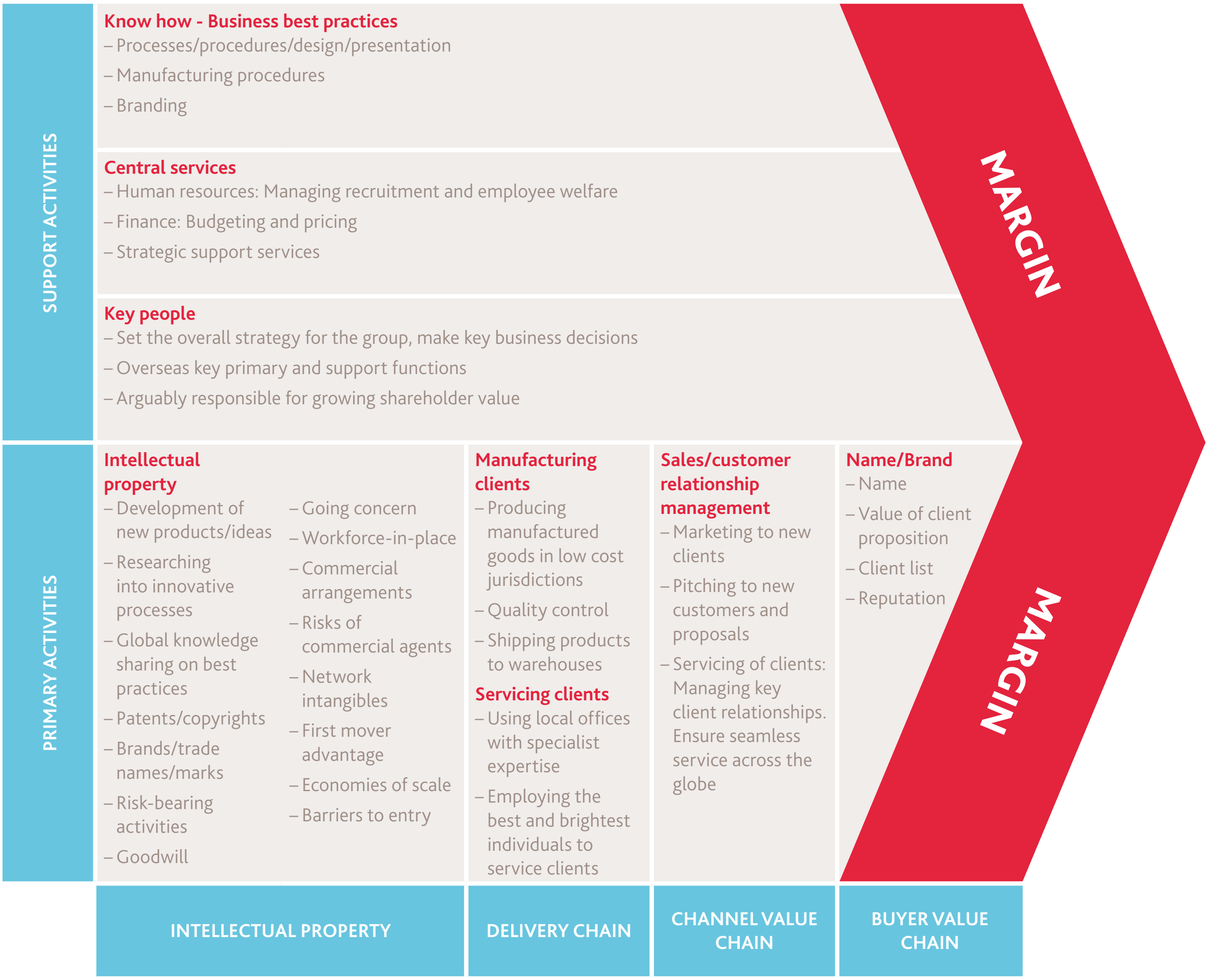
Besides this penalty, the most important risk is the possible increase of the taxable base by the administration on the grounds of incomplete and prejudicial information.

GLOBAL SUPPLY CHAIN MANAGEMENT

Introduction

Transfer pricing management involving corporate supply chains is becoming more complex. In the past, a typical supply chain might have included manufacturing, distribution and a centralised intangible holding company. In order to address the requirements of the current market, the same value chain may now also include purchase companies, centralised financing companies, a research and development (R&D) centre and service centres. Added to this complexity is an increasing awareness of the tax authorities on transfer pricing in order to tax their 'fair-share' of the profit.

A general illustration of some typical business value drivers



Businesses will often explore options for improving their value chain. This will almost certainly be commercially driven, but additional benefits could be available where these changes are structured effectively for tax purposes; Global Supply Chain Management.

Transfer pricing analysis

Using transfer pricing analysis, potentially portable elements of the value chain could be identified. These may include intangible property (IP), shared services or strategic management, but also extend to the assumption of key risks such as ownership of raw materials or finished goods, sales risk from contracting with customers or central procurement. There is then the potential to move the arm's length profit attributable to these activities and risks to low- (or lower-) tax territories, so reducing the overall tax burden of a group. The arm's length nature of these profits is important: the updated and expanded OECD Guidelines have recently reinforced the importance of applying transfer pricing to all relevant parties in the context of business restructurings to examine:

- Whether the transaction would have taken place in the first instance;
- The terms and conditions of transactions more generally;
- The economic reality of transactions - regardless of the contractual arrangements; and
- The control and management of risk as a means of determining where risk is economically borne.

As such, transfer pricing analysis creates the framework for economic and tax analysis of a value chain or business restructuring.

Transfer pricing analysis should also be applied where the business change (whether large or small) is already in progress as, by changing the transactions within a group and the characterisation of its entities, a group will need to ensure its transfer pricing policy is up-to-date, effectively implemented and documented.

Tax-risk analysis

Proper Global Supply Chain Management should also include a tax-risk analysis. A business restructuring could result in a tax charge on a transfer of assets/rights, or in other consequences subsequent to a restructuring (permanent establishment risks, CFC exposures, withholding tax as well as Customs or personal taxes).

The tax authorities are well aware of planning structures and are concerned about the potential impact on their tax bases when a group shifts functions and assets offshore. Recently, IP planning has become a point of attention for many tax authorities. The discussions regarding IP can be very complicated. Two simplified examples have been included in order to illustrate the type of discussions which could take place.

Marketing IP

Marketing intangibles can be one of the factors which drive revenue and profits. This could be realised by:

- The use of a legally protected intangible, e.g. a patent or a trademark; and
- Advertising/promotional activities.

Example 1

A US company is the owner of a trademark which has a high value in the US. A related Chinese company has received rights from the US company to use the trademark, and it pays royalties to the US company for the right to use the trademark. The advertising and other similar activities in China are organised and paid by the Chinese company.

The IRS may claim that the rate of the royalty should be high, since the trademark has a high value. China's State Administration of Taxation (SAT) generally disregards the value of a trademark by arguing that it enjoys a limited recognition when first introduced in China. Therefore, the SAT will argue that the advertising activities of the Chinese company are creating the value of the trademark in China. In the view of the SAT, advertising activities of the Chinese company would be considered key-value driver and this should be remunerated through e.g. a lower royalty.

Ownership of an IP

Profits resulting from an IP may be attributed based on the ownership of an IP.

When determining the economical ownership of an IP, the Japanese tax authority examines amongst others which company:

- Conducts development activities; and
- Bears costs.

Other countries may not consider the development activities as an (important) factor when determining the economical ownership of an IP.

Example 2

A high value IP created by a Japanese company is acquired by a related US company. The US company now fully funds the R&D activities of the Japanese company. The service agreement between the Japanese and the US companies clearly states that the Japanese company will continue to undertake the actual R&D. Since the US company has acquired the IP, the Japanese company pays royalties to the US company for the use of the IP. The Japanese company is highly profitable.

The IRS is likely to expect a high royalty rate since the IP has a high value, resulting in high profits at the Japanese company. However, the Japanese tax authority may argue that the rate of the royalty should be lower because it is the Japanese company which conducts the actual development activities, thus retaining (part) of the economical ownership.

Check list

The above examples illustrate the complexity but also the importance of Global Supply Chain Management. In defence of any business restructuring, a group should always have to consider the following questions:

- Would the transaction have occurred at all on an arm's length basis?
- What substance is there to support the restructuring?
- What value should be paid as compensation for the restructuring?
- Is the reward structure after restructuring appropriate, and does this reflect the risks of the different parties?

Do not forget the substance!

As elaborated above, the tax risks involved in Global Supply Chain Management could be significant and complicated. Underpinning all this, however, are the broader commercial considerations and the practicalities of achieving the right level of substance. For example this includes: the location of strategic management and key personnel, the nature of the decision making processes for different functions, and whether the ownership of intangibles is capable of being separated from the business activities to which they relate. The value chain analysis is intrinsically linked with these practical, commercial, economic and tax factors. It is a key strategic area for multinationals.

HONG KONG

DEPARTMENTAL INTERPRETATION AND PRACTICE NOTES

In light of the recent changing taxation landscape in Hong Kong as a result of the increasing number of double taxation agreements (DTAs) entered into by Hong Kong, the Hong Kong Inland Revenue Department (IRD) released two Departmental Interpretation and Practice Notes (DIPN) in 2009, namely DIPN 46 – Transfer Pricing Guidelines – Methodologies and Related Issues, and DIPN 45 – Relief from Double Taxation due to Transfer Pricing or Profit Reallocation Adjustments. Although DIPNs do not have the force of law, these two DIPNS do outline the IRD's current views and practices on (i) how transfer pricing principles will be applied in the territory and (ii) granting relief from double taxation due to a transfer pricing adjustment or profits reallocation under a DTA.

The main points to be noted regarding DIPN 45 and 46 are as follows:

– They follow the OECD Guidelines for transfer pricing, based on the arm's length principle to determine the appropriate price for transactions entered into by associated enterprises;

– They do not specifically set a threshold (e.g. ownership percentage) to define an associated enterprise from a Hong Kong transfer pricing perspective;

– They apply to both domestic and international related party transactions;

– They do not provide 'safe harbours' that would assist in determining generally acceptable mark-up fees for routine services transactions;

– The most appropriate transfer pricing method should be selected for a particular case. Where both the transaction-based method and the profit-based method can be applied in an equally reliable manner, the transactions-based method is preferred;

– Taxpayers are free to apply a method not described in the OECD Guidelines to establish arm's length transfer prices, provided that the arm's length principle is followed and the choice of a non-OECD recognised method is justified;

– The sourcing principle will be used primarily to determine whether profit is taxable in Hong Kong. Once it is concluded that profits of an enterprise are sourced in Hong Kong, the IRD will not accept an adjustment of profits using transfer pricing principles unless a primary adjustment has been made under the Associated Enterprises Articles under the relevant DTA;

– Transfer pricing documentation is not mandatory but is encouraged;

– Relief from double taxation due to transfer pricing adjustments should be sought under the relevant provision of the Inland Revenue Ordinance within the 6-year statutory time limit and/or under the Mutual Agreement Procedure Articles of the relevant DTA, rather than claiming a current year deduction for a retrospective adjustment;

– The IRD can make transfer pricing adjustments within Hong Kong's 6-year statutory time limit by reallocating profits or adjusting deductions by substituting an arm's length consideration;

– The IRD takes the view that they can also impose a penalty for transfer pricing adjustments, at a maximum amount of three times the tax undercharged;

– Certain basic information (e.g. transaction amounts, jurisdictions of related parties, nature of transactions and relationship) are required to be disclosed in the annual Profits Tax Return.

ITALY

LEGISLATION ON TRANSFER PRICING DOCUMENTATION

The Italian Government has enacted an amendment to the Law Decree 471/1997, with effect from 31 July 2010, under which no administrative penalties are due in the event of a transfer pricing adjustment, provided the tax payer is able to supply the Tax Administration with documentation certifying that inter-company transactions are carried out in compliance with the arm's length principle.

On 29 September 2010, the Italian Revenue Agency issued Note 2010/137654 implementing the legislation on transfer pricing documentation.

The Note provides detailed instructions on the documentation to be prepared by different types of taxpayer, the content of the documentation, and filing procedures.

The Note makes reference to the OECD Transfer Pricing Guidelines and is broadly consistent with the recommendations of the EU Code of Conduct on transfer pricing documentation for associated enterprises, including the reference to a *Masterfile* and a *Country file* (*country specific documentation*) concepts.

Classification of taxpayers

According to the provisions of the Note, Italian resident taxpayers are classified as follows:

- *Holding company*: an Italian resident company that is not controlled by another company and controls (also by means of a sub-holding) one or more non-resident companies;
- *Sub-holding company*: an Italian resident company that is controlled by another company residing anywhere and controls, in turn, one or more non-resident companies;
- *Controlled company*: an Italian resident company that is controlled by one or more non-resident companies.

Italian permanent establishments of non-resident companies are classified as a (sub) holding or controlled company in accordance with the status of the non-resident companies to which they belong.

Documentation requirements

The documentation requirements depend on the classification of the company:

- *Holding and sub-holding companies*: transfer pricing documentation should consist of both a Masterfile and a *Country file*;
- *Controlled company*: the documentation should consist of a *Country file*.

A *Masterfile* generally contains the following information on the group:

- A general description of the group;
- The group structure;
- Business strategies pursued by the Group (including potential changes to the overall business strategies compared to the previous tax year);
- Transaction flows;
- Intra-group transactions;
- Functions performed, (intangible) assets used and risks assumed;
- The group transfer pricing policy, explaining the reasons according to which such policies are deemed to be compliant with the arm's length principle;
- Relationships with the tax administrations of the Member States of the European Union regarding Advance Pricing Arrangements (APAs) and transfer pricing rulings.

A *Country file* includes amongst other details the following information on each resident company involved in inter-company transactions:

- An overall description of the company;
- A description of each business sector in which the company operates;
- The company's organisational chart;
- General business strategies pursued by the company and potential changes compared to previous tax years (if any);
- Controlled transactions (sale of tangible or intangible goods, provision of services, and financial services transactions);
- Intra-group transactions/Cost Contribution Arrangements (CCAs) of which the company is part;
- A Country file may include the following annexes:
  - A flow chart describing inter-company transactions flows; and
  - A copy of all inter-company agreements/ CCAs.

Communication of the availability of transfer pricing documentation

Companies wishing to benefit from the penalty protection provided by the new legislation have to communicate the existence of transfer pricing documentation (drafted in accordance with the provisions described above) when filing the annual income tax return.

For financial years ending before 31 May 2010, the communication had to be filed by 28 December 2010. However, communications sent after the above deadline can still grant penalty protection if filed before any assessment activities have been started by the Italian tax authorities.

Furthermore, in order to benefit from penalty protection, the taxpayer must deliver the documentation to the tax authorities within 10 days of the receipt of a formal request.

The documentation has to be provided both in hard copy and electronically.

JAPAN

THE RECENT TAX REFORM IN JAPAN

On 16 December 2010, Japan's Tax Commission of the Cabinet Office released its tax reform proposals for 2011, including a section on transfer pricing.

At present (April 2011), the 2011 tax reform proposals have been suspended due to 'the Great East Japan Earthquake' and are expected to be resolved in June 2011. Additionally, it is expected that the revisions to transfer pricing regulations will be made without any modification.

OECD Transfer Pricing Guidelines

In order to harmonise transfer pricing regulations in Japan with the recent amendments to the OECD Transfer Pricing Guidelines, the following proposals have been made:

- A change of the Transfer Pricing Method (TPM) election rule to the 'Best Method Rule' from the 'Statutory Prioritised Method Rule';
- The addition of a Comparable Profit Split Method and a Residential Profit Sprit Method to other specified methods;
- Permission to use ranges in testing the transfer prices or profitability of foreign related party transactions of the tax payer.

Documentation requirements

The 2011 proposals do not impose administrative requirements in relation to the documentation in the transfer pricing regulations, except for a filing requirement of an information return (Form 17-4) which shows e.g. the types and amounts of related party transactions, TPM, and profit and loss statements of a foreign related party.

It should be noted that the 2010 tax reform enacted in April 2010 provided clarification of the 'necessary documents' by stipulating two types of documents:

- The contents of foreign related party transaction;
- Documents pertaining to the arm's length prices determined by the taxpayer.

A transfer pricing study report on the prevailing transfer pricing practice around the world would cover almost all of the above necessary documents. However, a profit and loss statement of each related party transaction segmented out of the entire profit and loss statement is specified as a necessary document.

The use of secret comparables by the tax authority

In Japan, tax inspectors have been granted a right of inquiry under which they can visit third parties engaged in similar transactions to obtain comparable data. This data is not disclosed to the taxpayer undergoing a tax audit (hence the 'secret comparables' term). The application of these secret comparables had been at the sole discretion of the tax inspector in charge. Serious disputes have therefore arisen between taxpayers and tax inspectors regarding the application of the secret comparables.

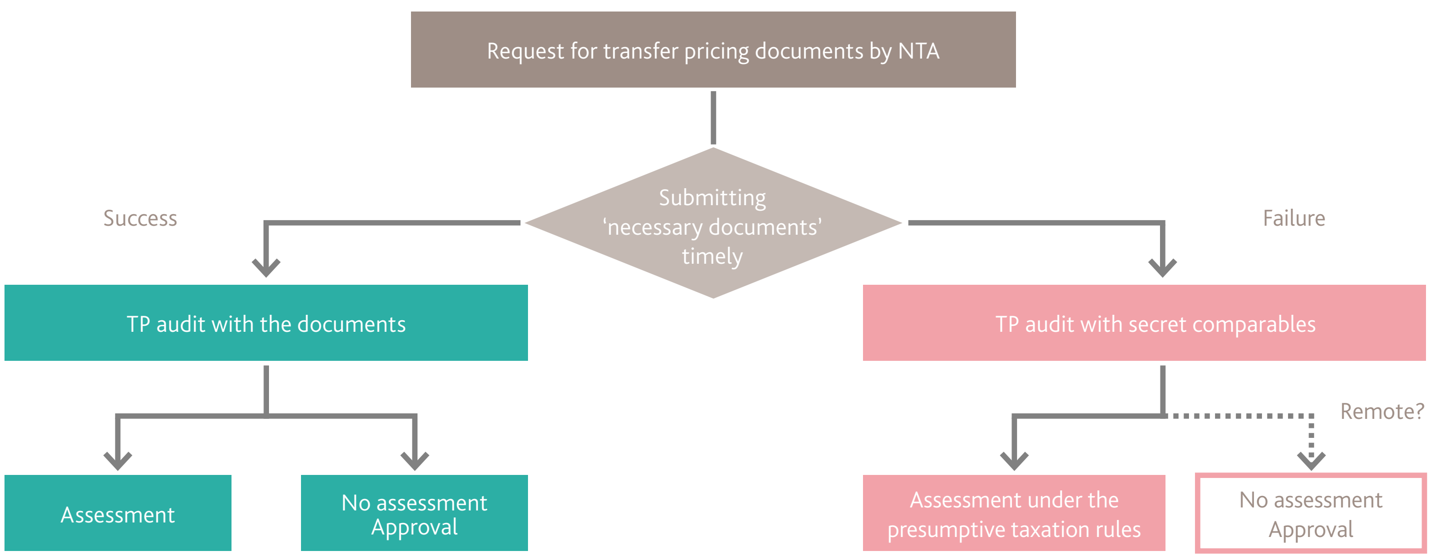
Under the 2011 proposal, the risk of the NTA applying secret comparables exists mainly where the taxpayer fails to submit the necessary documents on time, following the notification of a request by the tax inspector.

Proposed sanctions for failing the documentation requirements

If the taxpayer fails to provide documentation to tax inspectors within 30 days of a request, the so-called 'presumptive taxation' rule may be applied. This rule allows the NTA to presume 'certain prices' to be at arm's length, based on e.g. secret comparables. In this context, the application of the presumptive taxation rule constitutes a type of penalty.

The NTA does not impose penalties for failing to meet the documentation requirements (even for failure to file the information return).

The following flowchart illustrates the possible outcomes following a request by the NTA:



KOREA

CHANGES IN KOREAN TRANSFER PRICING RULES

South Korea's National Tax Service (NTS) has recently published a number of amendments to the existing transfer pricing policies. The changes include:

- The selection of the most appropriate transfer pricing methods;
- The selection of Profit Level Indicators (PLI);
- Substantially higher fines.

Most appropriate method

Prior to the amendments, the taxpayer had to apply the traditional transactional methods (Comparable Uncontrolled Price method, Resale Price method and Cost plus method) first. If the taxpayer could not apply the traditional methods, it could apply the transactional profit methods (Profit Split Method or Transactional Net Margin Method (TNMM)).

Under the new rule, prioritisation has been abolished. The taxpayer can apply the most appropriate method out of the five mentioned above. Other (reasonable) methods can also be applied if the taxpayer can demonstrate that the traditional and transactional methods are not the most appropriate methods.

It should be noted that each method has its own characteristics, strengths and weaknesses. Each method requires a different level of comparability with respect to the following five comparability factors mentioned in the OECD Transfer Pricing Guidelines:

1. The characteristics of the property or services transferred;
2. The functions performed taking into account the assets used and risks assumed;
3. The contractual terms;
4. The economic circumstances of the parties; and
5. The business strategies pursued by the parties.

The published amendments by the NTS clarify how these comparability factors should be dealt with.

Profit Level Indicators

When applying the TNMM, it is important to select a reliable PLI to examine the net profit margin between the taxpayer being tested and comparable companies.

The new rule states that the following PLI's can be applied:

- Net profit margin (operating profit/turnover);
- Net cost plus margin (operating profit/total expenses);
- Return on operating assets (operating profit/assets);
- Berry ratio (gross profit/operating expenses);
- Other appropriate PLI.

Under the OECD Transfer Pricing Guidelines, other possible PLIs should only be used where reliable comparable information is available to support the application. This should also be the case in South Korea.

Penalty protection

The Korean tax authority can request taxpayers to submit transfer pricing documentation. The taxpayer should provide the authority with the information within sixty days of the request.

Prior to the amendments, the maximum penalty for not complying with the documentation submission requirement was KRW 30 000 000. The amendment states that this amount, which was determined in 1995, was too low. Under the new rule, a failure to provide the authorities with the necessary documentation within sixty days may result in a fine of up to KRW 100 000 000.

The amount of the fine is substantial, and taxpayers should consider ensuring that proper transfer pricing documentation is in place.

LUXEMBOURG

CIRCULARS ON INTRA-GROUP FINANCING ACTIVITIES

On 28 January and 8 April 2011, the Luxembourg tax authorities clarified the domestic Transfer Pricing (TP) rules in two Circulars concerning companies involved in intra-group financing activities.

These Circulars give greater legal certainty for Luxembourg taxpayers, and detail the conditions for an 'arm's length' (i.e. market) margin which was until then determined based on quite broad provisions of the domestic law.

General considerations

These Circulars refer to the OECD Transfer Pricing Guidelines, and consider that an intra-group service has been rendered if, in comparable circumstances, an independent enterprise would have been willing to pay another independent enterprise for such an activity, or if it would have performed such an activity itself. The Circulars also specify the conditions to be met in order to obtain a binding advance transfer pricing agreement (APA) from the Luxembourg tax authorities.

Entities within the scope of the Circulars

The Circulars apply to entities which conduct activity consisting of the granting of loans or cash advances to affiliated companies, refinancing funds and financial instruments such as public offerings, private loans, cash advances or bank loans (excluding holding activities).

Conditions for obtaining an APA from the tax authorities

An APA which is binding on the tax authorities will be provided on the gross margin to be realised on the intra-group financing activity only if:

- The majority of the members of the board, directors, or managers, who have the authority to bind the group financing company, are either Luxembourg residents, or non-residents who carry on a professional activity in Luxembourg. Where a corporate entity is a member of the board of directors/ managers, its registered office and central administration must be located in Luxembourg;
- Members of the board of directors referred to above have professional knowledge to fulfill their duties and the authority to bind the company;
- Key decisions concerning the company's management are taken in Luxembourg;
- The group company has sufficiently skilled staff;
- The group financing company has at least a bank account in its own name at a financial institution established in Luxembourg;
- The company's equity is at least equal to 1% of the nominal value of the loan(s) granted to affiliated companies, or EUR 2 million.

Content of the request

All requests for an APA should include at least the following information:

1. Specific information on the requestor and on the entities which are party to the transaction;
2. A detailed description of the transaction;
3. Any other country or countries affected by the transaction;
4. A presentation of the group's legal structure, including information concerning the beneficial owner of the requestor's entity;
5. The tax years covered by the request;
6. A TP study in line with OECD Transfer Pricing Guidelines;
7. A general description of the market environment;
8. A review of any pertinent ancillary tax issues raised by the proposed methodology;
9. A confirmation by the taxpayer that the information reported in the APA is comprehensive and truthful.

Validity period

Decisions given from 28 January 2011 by the relevant tax office will be binding on the tax authorities for a maximum period of 5 tax years, which may be renewed for another maximum period of 5 tax years. APAs obtained before 28 January 2011 should remain valid until 1 January 2012.

Conclusion

The impact of these Circulars must be analysed on a case by case basis. Neither the APA nor the TP study are mandatory. However, in the absence of such documentation, the Luxembourg tax authorities may challenge the amount earned by the taxpayer. In case an APA cannot be requested, a TP study in line with the OECD Guidelines should be sufficient to sustain that the applied margin is at arm's length.

From 1 January 2012, the tax authorities will no longer be bound to APAs obtained before 28 January 2011. In this context, taxpayers who want to benefit from a new APA concerning their intra-group financing transactions will need to file a new APA in line with the above listed requirements. Practice will fine tune these new rules to reach a top level of compliance with internationally accepted TP standards.

Caveat

Other countries - the Netherlands is a very good example - have similar rules for intra group financing structures, including the possibility of agreeing an APA with the tax authorities.


Web
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SAP Data
Analyst/Designer, SR.
517 Technology Employment
Technician III
Programmer
Systems Analyst
Analyst/Programmer
Sr. Project
Engineer
Sr.Electro/Optical
Engineer

CURRENCY COMPARISON TABLE

The table below shows comparative exchange rates against the euro and the US dollar for the currencies mentioned in this issue, as at 24 May 2011.

Currency unit	Value in euros (EUR)	Value in US dollars (USD)
Euro (EUR)	1.0000	1.4054
Chinese yuan renminbi (CNY)	0.1093	0.1536
South-Korean won (KRW)	0.0007	0.0009
US dollar (USD)	0.7115	1.0000

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