Organisation for Economic Cooperation and Development
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11 April, 2014

By email: TransferPricing@oecd.org

Dear Sirs and Madams,

Comments on the Discussion Draft on Transfer Pricing Comparability Data and Developing Countries

Thank you for the opportunity to provide comments on the Discussion Draft on Transfer Pricing Comparability and Developing Countries (the "Discussion Draft") dated March 11, 2014. PwC agrees with the OECD in that comparability is at the heart of transfer pricing, and that the application of the arm's length principle often relies on a comparison of the prices charged in controlled transactions with the prices charged in similar transactions between independent enterprises. We also appreciate that tax authorities in developing countries have expressed concerns about the availability and quality of information regarding transactions between unrelated parties for purposes of applying the arm's length principle.

PwC supports the OECD's efforts to make administration of the arm's length principle easier in order to maintain the international consensus. However, we are concerned that some of the suggestions in the Discussion Draft, combined with concepts from the OECD's *Action Plan on Base Erosion and Profit Shifting* ("the BEPS Action Plan") released on July 19, 2013, and *Revised Discussion Draft on Transfer Pricing Aspects of Intangibles* ("the Revised Intangibles Discussion Draft") released on July 30, 2013, may create so many exceptions to the arm's length principle that it ultimately loses some of its vitality.

Further, PwC supports the use of safe harbors to the extent such safe harbors are transparent, based upon publicly-available information, simple to apply, and elective by the taxpayer.

Our specific comments on the OECD's suggested approaches are provided below.

Suggested approach 1: Expanding access to data sources for comparables

1. The Discussion Draft proposes several solutions for expanding access to data sources for comparables. We support the proposals to include more financial data on companies and relevant transactions in developing countries within commercial databases, and we support assisting developing country tax administrations with financing leases on such databases. We believe such measures can significantly expand access to data sources for comparables for tax administrations

in developing countries. However, we observe that there is already a significant amount comparables data concerning developing countries in publicly-filed information and commercial databases. Accordingly, we recommend that there be a means for accessing, extracting, and compiling the currently available information so that it can be used.

2. We do not support the suggestion in paragraph 16 of introducing an obligation to file statutory accounts and making them publicly available. Each country decides for itself regarding the obligation to file statutory accounts and whether to make them publicly available. There are many factors involved in making that decision, but most of those factors will not involve tax considerations. The availability of comparables data will likely be such a small consideration in that decision that it will not be relevant.

3. Additionally, we believe that the suggestion in paragraph 17 for tax administrations to populate an "internal comparables database" for "risk evaluation purposes" raises significant concerns. The OECD Transfer Pricing Guidelines ("Guidelines") make clear that it is fundamentally unfair for a tax administration to apply a transfer pricing method without disclosing such secret information to the taxpayer, in order to allow the taxpayer the opportunity to adequately defend its own position and to safeguard effective judicial control. This concern is equally applicable when secret comparables are used "only" for risk assessment purposes. We are concerned that the inappropriate use of secret comparables is already a significant problem in practice, and do not believe any recommendations for broader use of secret comparables for any purpose is prudent.

Suggested approach 2: More effective use of data sources for comparables

4. PwC supports efforts to ensure that tax authorities possess the appropriate "skill and experience" to use commercial databases. Proper use of databases is instrumental to a tax authority's ability to complete an accurate comparability analysis. However, PwC also expresses concerns based on increasing experience that tax administrations are performing analyses to identify 'identicals' (i.e., companies that are in all aspects identical to the tested party) and thereby reject good comparables. This defeats one of the purposes of a good comparable search where statistical analysis helps to derive an arm's length range.

5. As stated in the OECD's Revised Intangibles Discussion Draft, where comparable entities and transactions in the local market can be identified, then separate comparability adjustments for geographic differences should not be required. However, comparability adjustments for other factors (e.g., capital intensity, payment terms, etc.) may still be appropriate and should be evaluated on a case-by-case basis. Explicit recognition of this guidance should be included within the Discussion Draft.

6. PwC agrees with the suggestion to broaden the search for comparables to uncontrolled transactions in the same industry but in other geographic markets, as discussed paragraph 19. We note that broadening a comparables search within a geographic area is consistent with the current guidance in the Guidelines concerning use of multiple-country and non-domestic comparables.

7. In paragraph 21, the OECD discusses the concept of country risk adjustments and notes the Guidelines provide little guidance on this matter. PwC believes that if country adjustments are going to be contemplated in OECD pronouncements, then guidance must be provided on how these adjustments are to be made. PwC's concern is that if the Guidelines mention country adjustments, but do not explain how to make such adjustments appropriately, there is a risk that tax authorities will make arbitrary adjustments on this matter.

8. Paragraph 22 of the Discussion Draft notes that if comparables are not available from a local country perspective, it may be "appropriate and possible to evaluate the transaction by testing the return earned by the foreign counterparty." We believe the existing guidance in para. 3.18 of the Guidelines, about choice of tested party, is correct and complete. The suggestion in paragraph 22 to use the foreign counterparty to a transaction as the tested party, in order to mitigate the risk that the domestic entity will only receive a routine return and not share in any residual profits, is inappropriate. When it is appropriate to use a cost plus, resale price, or transactional net margin method, by definition the tested party will "only" earn a routine return, because that is the appropriate result according to the functional analysis. The Discussion Draft seems to suggest a results-oriented approach that unfortunately may encourage inadequate or perfunctory performance of the functional analysis and a choice of transfer pricing method to justify allocation of residual profits to the domestic entity by developing countries (and others).

Suggested approach 3: Approaches to reducing reliance on direct comparables

9. In paragraph 24, the OECD notes that the reduced reliance on direct comparables relates to situations in which no "appropriate" internal or external information exists for purposes of determining and validating the arm's length principle. The Discussion Draft notes that in such situations, other approaches may be appropriate, including use of the profit split method or a "global value chain analysis." We believe the existing guidance in the Guidelines on when the profit split method is the most appropriate method is correct, and that guidance should simply be cross referenced. It is unclear how the "global value chain analysis in the Discussion Draft differs from the functional analysis currently described in the Guidelines. We believe that it should be described more fully, particularly as to how it differs from a traditional functional analysis. Finally, we are concerned that the focus on use of profit splits and a global value chain analysis, along with the suggestion to make the foreign counterparty the tested party in order to allocate residual profit to the local country jurisdiction, will inappropriately encourage countries to focus on ways to secure a share of any "system profit" of a multinational enterprise, instead of focusing on pricing the particular transaction at hand.

10. The discussion of the so-called "sixth method" alternative approach raises concerns regarding consistency with the arm's length principle. PwC supports the use of publicly-quoted commodity prices as a useful starting point to determine arm's length pricing. But the specific circumstances of each transaction must be recognized, and comparability adjustments may need to be made to publicly-quoted commodity prices to account for any differences between the related party transaction at issue. For example, publicly-quoted commodity prices may require comparability adjustments to account for differences in volume, geography, economic circumstances, time for delivery or other contractual terms relevant to a controlled transaction. The Discussion Draft

recognizes that the "sixth method" may be applied in a manner that is inconsistent with the arm's length principle, resulting in either double taxation or double non-taxation. Yet, the OECD contends that it may be appropriate if it is used as an anti-avoidance approach. We do not support broader use of any method that is inconsistent with the arm's length principle, and that will generally result in either double taxation or double non-taxation. We also do not believe that developing countries should be encouraged to apply a different version of the arm's length principle than developed countries.

11. We are concerned by the focus in paragraph 28 on anti-avoidance rules and the denial or limitation of expenses that benefit companies in low or zero tax jurisdictions. Transfer pricing has traditionally been about pricing intercompany transactions, not about the wholesale denial of deductions when they are not considered to be "legitimate." It is unfortunate, for example, that Action 10 of the BEPS Action Plan refers to management fees and head office expenses simply as "base eroding payments." We believe related parties should be entitled to deductions for the same types of expenses that unrelated parties may deduct. It would be prudent to focus on ensuring that the pricing of such deductions is at arm's length, and not on providing for the categorical denial of deductions for such expenses. If transfer pricing rules for related parties do not price transactions in the same manner as would occur between unrelated parties, it is difficult to see what the guiding principle would be.

12. PwC supports the use of safe harbors to the extent that such safe harbors are transparent, based upon publicly-available information, simple to apply, and elective by the taxpayer. From PwC's experience, routine related-party transactions appear most adaptable to standardization and simplification through safe harbors. Further, in order to be truly "safe harbors," their use must be elective solely by the taxpayer. Taxpayer election best protects the arm's length principle and assists in mitigating double taxation.

Suggested approach 4: Advanced pricing agreements and mutual agreement proceedings

13. PwC supports the OECD's view that advance pricing agreements ("APAs") and mutual agreement proceedings ("MAPs") have the potential to function as effective tools for addressing tax controversy. We believe more resources should be devoted to make APAs and MAPs more widely available, which could help to resolve and prevent transfer pricing disputes. Given the potential increase in controversies over the next few years, broader access to appropriate MAPs, including those with the option for the taxpayer to choose mandatory binding arbitration, is essential. Increased resources for controversy resolution will be necessary to prevent double taxation and the consequent harm to cross-border trade and investment.

On behalf of the global network of PwC Member Firms, we submit our response to the Discussion Draft on Transfer Pricing Comparability Data and Developing Countries. For any clarification of this response, please contact the undersigned.

Yours faithfully,

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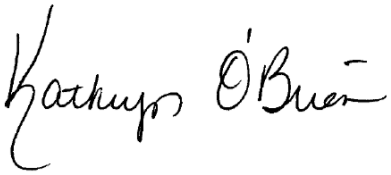

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