

# *Global transfer pricing documentation strategies*



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### Where are we today?

The new Chapter V of the OECD's Transfer Pricing Guidelines covers three tiers of transfer pricing documentation: (1) the Master File (MF), which provides a detailed representation of the global operations of the multinational enterprise (MNE); (2) the Local File (LF), which contains detailed information on an MNE's intercompany transactions in a particular jurisdiction, and (3) the country-by-country (CbC) report.

Over the last year since the Chapter V final report was published in 2015, many local tax administrations have been taking steps towards introducing, to different extents, new transfer pricing requirements into their domestic legislation. For example, within the last 6 months:

- Canada has issued proposed legislation on CbC reporting.
- Uruguay has submitted a tax bill to Congress, which includes the adoption of the CbC report and the MF approach.
- Austria has introduced mandatory documentation requirements requiring companies to prepare a MF, LF and CbC report.
- Germany has published a draft bill intended to implement the three-tiered documentation approach recommended by the OECD.

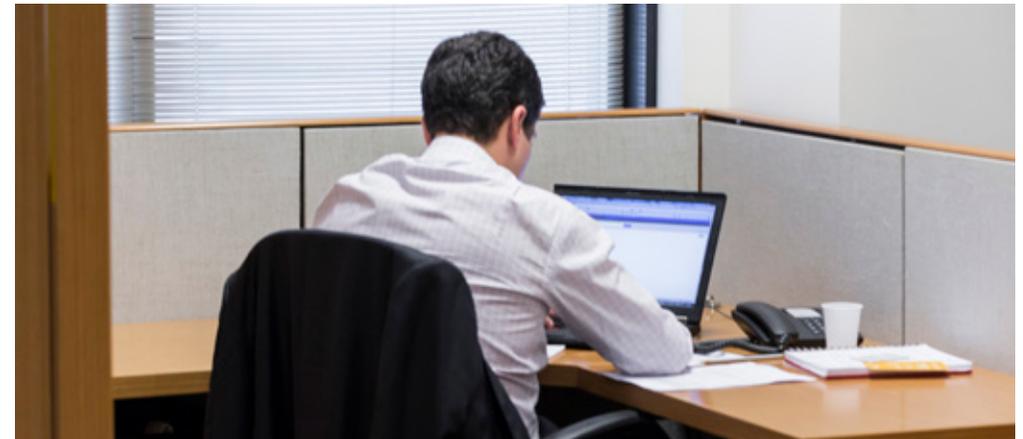
- The US issued final regulations for filing the CbC report for US-parented MNE groups.
- The Australian Taxation Office finalised its design of the LF requirements under the Australian CbC reporting laws.
- Luxembourg has proposed CbC reporting obligations

In addition to the three tiers mentioned above, over the last year, countries that have historically required the filing of local forms detailing various aspects of intercompany transactions (i.e., information returns), have confirmed that such requirements will continue, thereby creating a fourth tier to the transfer pricing documentation burden.

As more and more countries release or update their local documentation requirements, it is clear that while the OECD's aim was to introduce "coherence in the domestic rules that affect cross-border activities", the practical evidence shows that such coherence is not happening. For example, some countries, including the US, only introduced CbC report requirements, while not changing the local documentation requirements, whereas others countries, while introducing the MF/LF concept, did not align their requirements with the OECD Guidelines. Some examples include China where they introduced the MF/LF requirements, but also adding a

special issues file that local taxpayers need to prepare; Japan introduced a group threshold for the MF and contemporaneous preparation of the LF and Australia introduced a form based approach for the LF. These nuances on a country by country basis are challenging MNEs to define a more comprehensive strategy for preparing transfer pricing documentation which meets all the relevant requirements around the world.

MNEs are realising that the approach taken for documentation going forward is likely to change significantly as compared to their historical approach, and the adaptation to this new environment needs to be made quickly to ensure the new compliance requirements in the post Base Erosion and Profit Shifting (BEPS) world are met.



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### **New approach to documentation**

In the past, as a result of the ad hoc development of transfer pricing documentation requirements globally, MNEs have faced a myriad of different regulations, formats, and levels of prescription. The traditional approach adopted by many MNEs in preparing their transfer pricing documentation has typically been designed to ensure compliance with local documentation requirements and penalty protection, where feasible, while minimising the efforts required. This approach typically resulted in MNEs focusing on preparing transfer pricing documentation for higher risk affiliates located in key countries. Some of the most often used criteria included jurisdictions with prescriptive local requirements or aggressive tax authorities, affiliates where the most material transactions took place, or other similar factors.

The new Chapter V requires a much more global approach to documentation, which represents a significant change and will require MNEs to reassess how they approach transfer pricing compliance. In PwC's view, the traditional approach to documentation is a thing of the past, and the preparation of transfer pricing documentation will shift from a compliance to a more strategic exercise.

In this new environment of transparency, MNEs need to look at transfer pricing

documentation differently and plan for a more comprehensive and deliberate review in order to determine the approach for compliance and obtain the information required, as well as ensure a smooth transition. It is key for MNEs to consider how the transfer pricing documentation presents their global business to the outside world, as well as which documents exist that impact their transfer pricing policies or practices (such as intercompany agreements, information on their company website, etc.). Furthermore, even if there are currently no requirements to publish any of the tiers of documentation, there is pressure, mostly in Europe, to make certain information (such as the CbC report) available to the public. As such, in planning the future approach to transfer pricing documentation, the nature and sensitivity of the business information to be disclosed needs to be carefully considered.

In terms of preparing the MF/LF, based on the Chapter V guidelines, there appears to be some flexibility in how to provide the mandated information. In this sense, when planning the documentation approach, MNEs could consider different approaches depending on the facts and strategy. For example, for certain businesses a modular approach may be considered appropriate, where the content of the MF is split between a main MF and separate business line MFs with only the relevant business line information, versus having all the different

business lines' information in one MF. Under this approach, only the relevant modules can then be used as part of each local company's documentation set, jointly with a LF that is tailored to the local operations. However, when taking this approach the OECD clarifies that the entire MF consisting of all business lines should be available to each country. Another alternative could be summarising the business information in the MF, limiting the information included in this document, while providing more detailed information in the LFs to meet the local documentation requirements.

Consistency is a critical area of focus. The written words in the MF/LF should provide the background to the data in the CbC report and should be consistent with other relevant documents, such as local information returns. This should be carefully considered throughout the planning process, as any changes in future documentation are likely to be scrutinised by tax authorities.

With this burden in mind, from gathering relevant information to producing the final documentation, it appears as though MNEs are taking a more holistic approach to collecting information and consolidating the process in order to have central visibility and control of the transfer pricing compliance process, although the involvement of the local affiliates is key to ensure that the local operations are accurately represented and the local requirements

are met. Understandably, this approach requires expanding or reassigning transfer pricing resources to meet these new, more onerous documentation requirements, or alternatively looking to outsource some portion of the process, typically from assistance with the MF/LF strategy to preparation of the relevant documents.

Throughout these changes in landscape, we expect that technology will play a larger role for the coordination and preparation of transfer pricing documentation. From centrally gathering the data, to managing the timeline for compliance and documentation process, to issuing final reports, technological tools are likely to have a positive impact in the execution of the documentation strategy and the efforts and resources required to achieve it. With this factor in mind, we have developed various tools to assist our clients with the different elements of the transfer pricing compliance process under the new environment, including project management tools like Tax Engagement Center (TEC) and report writing tools like GCD Reporter.

We believe there is no one-size-fits-all solution when it comes to transfer pricing documentation strategy. There are numerous approaches and it is up to MNEs to take advantage of the flexibility and determine a game plan that fits their business facts, resources, and overall objectives.

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### **Key takeaways**

The last few years have seen a sustained increase in transfer pricing requirements around the world, a trend that is expected to continue based on the OECD's new Chapter V. This constantly changing environment, along with the increased transparency requirements have resulted in a heightened need for MNEs to disclose more information and rethink their transfer pricing documentation approach. In addition, MNEs not only need to closely monitor worldwide developments to ensure compliance with the evolving local obligations, but they need to act now as the rules apply to financial years which end in less than three months' time.

The new rules are currently in place in many countries, so now is time to formulate a plan. MNEs need a global strategy, along with underlying systems and processes to enable them to deliver consistent and robust transfer pricing documentation across all their affiliates in line with statutory deadlines. As the requirements continue to get more onerous it will become even more critical for MNEs to rely on technology to help gather the data, prepare the documentation and project manage the process on an annual basis.

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