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Deputy John McGuinness T.D.
Cathaoirleach
Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach
Leinster House
Dublin 2

By email: financecommittee@oireachtas.ie

26 January 2024

Proposals for EU Directives on BEFIT (COM (2023) 532) and Transfer Pricing (COM (2023) 529)

Dear Cathaoirleach

Thank you for the invitation to make a submission to the Joint Committee to outline our views on the European Commission's proposals for Directives on the Business in Europe: Framework for Income Taxation (known as BEFIT) and Transfer Pricing.

We have attached as appendices to this letter, two Position Papers which the Irish Tax Institute prepared in response to the recent public consultations held by the Commission on both Directives. In these papers, we outline in detail the concerns raised by our members in relation to both proposals.

Please contact Anne Gunnell at agunnell@taxinstitute.ie or (01) 6631750 if you require any further information regarding the matters raised in this submission.

Yours sincerely

Martin Lambe
Chief Executive

Member of the Confédération
Fiscale Européenne

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Immediate Past President: Colm Browne.

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Appendix I

European Commission's Consultation on a proposal for a Council Directive on Business in Europe: Framework for Income Taxation (BEFIT)

Position Paper

24 January 2024

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1. About the Irish Tax Institute

The Irish Tax Institute is the leading representative and educational body for Ireland's Chartered Tax Advisers (CTA) and is the country's only professional body exclusively dedicated to tax.

The Chartered Tax Adviser (CTA) qualification is the gold standard in tax and the international mark of excellence in tax advice. We benchmark our education programme against the very best in the world. The continued development of our syllabus, delivery model and assessment methods ensure that our CTAs have the skills and knowledge they need to meet the ever-changing needs of their workplaces.

Our membership of over 5,000 is part of the international CTA network which has more than 30,000 members. It includes the Chartered Institute of Taxation UK, the Tax Institute of Australia, and the Taxation Institute of Hong Kong. The Institute is also a member of the CFE Tax Advisers Europe (CFE), the European umbrella body for tax professionals.

Our members provide tax services and business expertise to thousands of Irish owned and multinational businesses as well as to individuals in Ireland and internationally. Many also hold senior roles in professional service firms, global companies, Government, Revenue, state bodies and in the European Commission.

The Institute is, first and foremost, an educational body but since its foundation in 1967, it has played an active role in the development of tax administration and tax policy in Ireland. We are deeply committed to playing our part in building an efficient and innovative tax system that serves a successful economy and a fair society. We are also committed to the future of the tax profession, our members, and our role in serving the best interests of Ireland's taxpayers in a new international world order.

Irish Tax Institute - Leading through tax education

2. Executive Summary

The Irish Tax Institute welcomes the opportunity to contribute to the European Commission's public consultation on the proposal for a Council Directive on Business in Europe: Framework for Income Taxation (BEFIT).

The proposal is intended to build on the internationally agreed achievements of the OECD/G20 Inclusive Framework *Two-Pillar Solution to Address the Tax Challenges of Digitalisation*[1] (Two-Pillar Solution) and provide a degree of tax certainty and easier tax compliance for larger businesses that have a taxable presence in multiple Member States.

Businesses are currently overburdened at present by the level of effort required to comprehend and comply with the corporate tax reforms agreed as part of the Two-Pillar Solution and within the EU, the implementation of the Pillar Two Minimum Tax Directive.[2] Although the objective of BEFIT is to provide relief from the administrative burden faced by multinational enterprises (MNEs) when complying with their corporate tax liability in multiple Member States, the Institute believes its introduction would add a further layer of complexity and uncertainty.

We firmly believe that the European Commission should defer further consideration of the proposed Directive until the Pillar Two Global Anti-Base Erosion (GloBE) Rules have had sufficient time to operate in practice and any shortcomings or areas of uncertainty in those rules have been identified and addressed.

We do not consider that the proposed BEFIT Directive would benefit businesses or tax authorities across the EU. Our members have raised a number of significant concerns regarding the proposed BEFIT Directive. These concerns, which have been set out in detail in Section 3 of this paper, include the following:

- Under the BEFIT proposal, it is intended that a transition allocation rule would pave the way for a permanent mechanism for the allocation of a common tax base which could be based on formulary apportionment. However, no detail is provided regarding the proposed permanent formulary apportionment method. Consequently, it is not possible to determine the potential fiscal impact of the BEFIT proposal on individual Member States beyond the initial 7-year period when the transition allocation rule applies.

- In line with the principles of subsidiarity and proportionality, it would be important for the European Commission to demonstrate that the aims of the BEFIT Directive cannot be sufficiently addressed by individual Member States and that action at the EU level would provide additional benefits.

[1] OECD/G20 Inclusive Framework on BEPS, Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 8 October 2021.
[2] Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union.

- It is only when the detail of the proposed formulary apportionment method is known that the necessary impact assessment could be prepared by the European Commission with appropriate quantitative and qualitative indicators to allow Member States to fully assess all the implications of a cross-border proposal of this significance.

- The proposed Directive envisages tax authorities in Member States would operate three different tax systems in parallel i.e. their national tax system, the Pillar Two GloBE Rules and the BEFIT regime. This is contrary to the objective of simplifying tax administration and would inevitably increase complexity and administration costs for both tax authorities and taxpayers.

- While the proposed Directive is intended to provide simplification, it is likely to have the opposite outcome and add to the complexity faced by in-scope businesses because the BEFIT rules are not aligned with the Pillar Two GloBE Rules in many key aspects.

- The proposed Directive is intended to simplify compliance with transfer pricing rules. However, it is questionable whether the proposed approach offers any meaningful simplification as:

    - MNEs would remain subject to the arm's length principle on transactions outside of the EU; and
    - the proposed approach for transactions with associated entities outside of the BEFIT group to low-risk activities does not align with the approach proposed under Amount B of Pillar One of the Two-Pillar Solution.

- The interaction of key aspects of the BEFIT Directive and the Pillar Two GloBE Rules needs to be addressed. For example:

    a. The transitional allocation mechanism could result in profits of a BEFIT group member not being taxed in its Member State of residence but being taxed in another Member State. This could result in a GloBE top-up tax liability arising in the Member State of residence, as the effective tax rate (ETR) for the purpose of the Pillar Two GloBE Rules is calculated on a jurisdictional basis, notwithstanding that such profits would be subject to the required minimum level of taxation in the EU.

    b. A GloBE top-up tax liability could be triggered by the cross-border loss relief rules under the BEFIT Directive as such losses could reduce the ETR in an EU Member State for the purposes of the Pillar Two GloBE Rules.

- BEFIT would create a further layer of uncertainty for business operating in the EU making the Single Market a less attractive place to do business.

3. Key issues with the proposed BEFIT Directive

3.1 The fiscal impact of the proposed BEFIT Directive is unknown

Under the BEFIT Directive, the preliminary tax results of each member of a BEFIT group would be aggregated to allow for cross-border loss relief between BEFIT group members. Subsequently, the aggregated tax base would be allocated to group members based on the transition allocation rule set out in Article 45 of the Directive. The transition allocation rule would apply for each fiscal year between 1 July 2028 and 30 June 2035.

Recital 12 of the proposed Directive notes that the transition allocation rule would pave the way for a permanent mechanism which could be based on a formulary apportionment. However, no detail is provided on the proposed permanent formulary apportionment method. Consequently, it is not possible to determine the potential fiscal impact of the BEFIT proposal on individual Member States beyond the initial 7-year period where the transition rule applies. Accordingly, there is no certainty provided to Member States on the potential impact of the proposed Directive.

The previous proposal by the Commission for a Common Consolidated Corporate Tax Base (CCCTB) and indeed, the Call for Evidence for an Impact Assessment on BEFIT[3] proposed that profits could be allocated by reference to a formula that would favour countries where customers are located, and which would under attribute value to ownership of critical intangible assets.

As the proposed BEFIT Directive does not give any indication regarding the permanent formulary apportionment method which would apply following the transitional period, our members have raised concerns that it could mirror previous proposals in this regard. Should that be the case, it would mean that BEFIT would adversely impact smaller countries with service-based open economies, such as Ireland, making them less attractive as destinations for inward investment and thus, erode their tax base.

The Explanatory Memorandum notes that EU policies can build on developments in the field of corporate taxation taking place at international level and refers to the use of formulary apportionment to partially re-allocate taxable profits under Pillar One of the Two-Pillar Solution. The Commission's Call for Evidence for an Impact Assessment also suggests that the formula for allocating profits under Pillar One will be a source of inspiration for the design of BEFIT.

However, the scope of the new Amount A taxing right under Pillar One, which provides for an element of formulary apportionment, will only apply to the very largest of MNEs with global turnover above €20 billion and profitability above a 10% margin. In contrast, the proposed BEFIT Directive would apply to groups with annual revenues of at least €750,000 and therefore, it would encompass a significantly larger number of

[3] Ref. Ares(2022)7086603 - 13/10/2022

businesses. In addition, it must be borne in mind that a number of key issues regarding Pillar One have yet to be resolved. It is therefore premature to suggest that a new system of formulary apportionment of a common consolidated tax base within the EU could be designed based on Pillar One.

3.2 A detailed analysis is essential to demonstrate the need for BEFIT

As set out in our response[4] in January 2023 to the European Commission's public consultation on the BEFIT initiative, we firmly believe it would be important for the European Commission to be able to demonstrate that the aims of BEFIT cannot be sufficiently addressed by individual Member States and that action at the EU level would provide additional benefits.

Article 5(3) of the Treaty on European Union (TEU) provides as follows: "*3. Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level."*

To assist national parliaments in their evaluation of subsidiarity compliance, Article 5 of Protocol (No 2) of the TEU on the application of the principles of subsidiarity and proportionality states: "*Any draft legislative act should contain a detailed statement making it possible to appraise compliance with the principles of subsidiarity and proportionality. This statement should contain some assessment of the proposal's financial impact and, in the case of a directive, of its implications for the rules to be put in place by Member States…"*

While an Impact Assessment Report on the proposed Directive has been published, as the formulary apportionment method which would apply after the initial 7-year period has not yet been determined, the Report does not take this into account in its assessment of the potential impact of the proposed Directive on Member States and businesses.

In our view, there must be clarity at the outset regarding the formulary apportionment method which would apply after the initial 7 years. It is only when the detail of the proposed formulary apportionment method is known that the necessary impact assessment could be prepared by the Commission, which would allow Member States to fully assess all the implications of the BEFIT proposal. For example, we would suggest the analysis to be prepared by the Commission include the following:

- An analysis of the impact of BEFIT on foreign investment in individual Member States, with particular consideration given to small open economies.
- An analysis demonstrating why BEFIT would provide a better solution than current transfer pricing rules.

[4] Position Paper for the European Commission's Public Consultation on Business in Europe: Framework for Income Taxation (BEFIT), 26 January 2023 - https://taxinstitute.ie/wp-content/uploads/2023/01/2023-01-26-ITI-Position-Paper-for-the-European-Commission-Consultation-on-BEFIT-FINAL.pdf

- An analysis of the impact of the proposed Directive on small open economies. The BEFIT Directive must provide for sustainable tax revenues for individual Member States as well as the EU as a whole.

Undertaking such detailed analysis and impact assessment would be in keeping with the Commission's better regulation agenda and its commitment to ensure any proposals to change existing EU laws would provide simplification and reduce unnecessary regulatory costs.

3.3 The proposed BEFIT Directive will not provide simplification

One of the key objectives of BEFIT is to simplify tax rules for businesses in the EU and in doing so, to reduce the compliance costs faced by such businesses when operating cross-border.

Businesses are already burdened by the level of effort required to comprehend and comply with the plethora of recent EU and international tax reforms, including the EU Anti-tax Avoidance Directives (ATAD1[5] and ATAD2[6]) and the multiple iterations of the Directive on Administrative Co-operation[7] (DAC). Alongside these significant legislative changes, businesses are grappling with the level of effort required to understand and comply with the implementation of the Pillar Two GloBE Rules.

The proposed Directive envisages tax authorities operating three different tax systems in parallel. Tax authorities would have to operate their domestic corporate tax system, the Pillar Two GloBE Rules and a new separate regime under BEFIT. In-scope businesses would be required to prepare and file a local tax return and GloBE Information Return in addition to the BEFIT Information Return. Operating three tax systems in parallel would inevitably increase the complexity and costs of administration for both tax authorities and taxpayers and would appear contrary to the stated objective of simplifying tax administration.

While the proposed BEFIT Directive is intended to provide simplification, it is not aligned with the Pillar Two GloBE Rules in many key aspects. This means that it would place a disproportionate compliance burden on businesses as it would increase complexity to an unprecedented level. For example, the definition of a group is not the same and the adjustments required to be made to determine the BEFIT tax base are not aligned with those required under the GloBE Rules.

In addition, the Directive requires that the BEFIT Information Return be filed within four months of the end of the fiscal year whereas the Pillar Two GloBE Rules allow a period of 15 months after the end of the fiscal year (extended to 18 months for the transition year) for the filing of the GloBE Information Return. The rationale for providing such a short timeframe is unclear and in our view, is entirely disproportionate.

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[5] Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[6] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

[7] Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and amending Directives

The BEFIT Directive provides for cross-border loss relief. The Explanatory Memorandum notes that currently cross-border loss relief is rarely possible and this can result in *"over-taxation of the profits of the group and disincentivise businesses from operating across borders in the internal market.*" However, where there is a differential in the corporate tax rates applying in Member States, the compulsory pooling of cross-border losses could mean that relief from corporate tax is given at a lower rate than that which applies in the Member State in which the losses were suffered.

We consider that the additional complexity associated with BEFIT would place EU-headquartered businesses at a disadvantage when compared to non-EU headquartered businesses. In addition, it could act as a deterrent for non-EU businesses wishing to expand their global footprint because non-EU businesses would come within the scope of BEFIT once their EU revenues exceed €50 million. This could discourage such non-EU businesses from establishing in the EU and instead, result in those businesses choosing to sell into the EU from non-EU jurisdictions.

The approach to transfer pricing

For transactions with associated enterprises outside the BEFIT group, the BEFIT Directive aims to facilitate transfer pricing compliance by providing a risk assessment tool. The approach would be based on commonly accepted public benchmarks that would be available for low-risk activities performed by certain eligible distributors and contract manufacturers. The benchmarks are intended to provide taxpayers with increased levels of advance certainty, regarding the arm's length returns that they are expected to achieve in transactions with associated enterprises outside the BEFIT group.

According to the Explanatory Memorandum, this system is intended to simplify compliance with transfer pricing rules. However, our members have highlighted the approach outlined in the proposed Directive is not aligned with what is proposed under Amount B of Pillar One of the Two-Pillar Solution and therefore, they have questioned whether the proposed approach under BEFIT would provide any significant simplification for taxpayers.

In the first seven fiscal years post-implementation, Member States would deem intra-BEFIT group transactions to be priced at arm's length where they fall within a low-risk zone. Recital 12 of the proposed Directive notes that the transition allocation rule would pave the way towards a permanent mechanism and *"that permanent mechanism could be based on a formulary apportionment and would render the need for intra-BEFIT group transactions to be consistent with the arm's length principle redundant*."

However, as BEFIT would not eliminate existing transfer pricing rules for all transactions but only within the EU for those companies within scope, MNEs would remain subject to the current arm's length principle on transactions outside of the EU. Therefore, such companies would be unlikely to realise any meaningful transfer pricing simplification benefit.

3.4 Interaction with the Pillar Two GloBE Rules must be addressed

The interaction of the proposed BEFIT Directive and the Pillar Two GloBE Rules must be addressed. It would appear that the proposed transitional allocation mechanism could result in profits of a BEFIT group member in one Member State being allocated to another BEFIT group member in another Member State. This could result in profits of a BEFIT group member not being taxable in its Member State of residence but being taxable in another Member State. This would result in a GloBE top-up tax liability arising, as the ETR for the purpose of the Pillar Two GloBE Rules would be calculated on a jurisdictional basis, notwithstanding the fact that such profits would be subject to a sufficient level of taxation in the EU.

In addition, the interaction of the cross-border loss relief provisions and the Pillar Two GloBE Rules need to be addressed. As currently drafted, it would seem possible that a GloBE top-up tax liability could be triggered by the cross-border loss relief rules under the BEFIT Directive as such losses could reduce the ETR in an EU Member State for Pillar Two purposes.

3.5 Legal and tax certainty for businesses

We believe the proposed BEFIT Directive would create uncertainty for companies operating in the EU, at a time when businesses are already striving to understand and comply with the substantial tax reforms implemented within the EU over the last five years, not least the Pillar Two GloBE Rules.

The corporate tax systems of Member States are based on detailed legislation, guidance notes and caselaw spanning thousands of pages which both Member States and taxpayers rely on to gain certainty regarding the operation of their tax systems. The introduction of the BEFIT regime, comprising new rules and definitions, would create enormous uncertainty for both businesses and tax authorities. Undoubtedly, it would take years to replicate the existing considerable catalogue of caselaw to support the new BEFIT framework.

Notably, the OECD/G20 Inclusive Framework on BEPS (Inclusive Framework) has already issued hundreds of pages of Commentary and Administrative Guidance on the interpretation of the Pillar Two GloBE Rules and has indicated that it will continue to release further guidance on an ongoing basis. In addition, the Inclusive Framework plan to implement a peer review process and dispute resolution mechanisms to provide a high level of tax certainty to stakeholders in applying the rules.

The Pillar Two GloBE Rules and the Inclusive Framework's guidance on those rules are only now being tested in practice as businesses seek to comply with their obligations. If BEFIT is introduced, businesses operating in the Single Market would also need to consider the interaction of the BEFIT rules with the Pillar Two GloBE Rules.

It must also be considered that many businesses in scope of Pillar Two will be able to avail of safe harbours in the initial years following implementation meaning the proposed timeline for the implementation of BEFIT could coincide with the periods in which some

businesses will be required to prepare detailed GloBE calculations for the first time, leading to further uncertainty for such businesses.

Legal and tax certainty in the international tax framework is of the utmost importance and must be a priority for policymakers. In our view, the proposed BEFIT Directive would create a further layer of uncertainty for businesses that are already struggling to comply with the most significant reform of the international tax framework in decades. We believe that causing further economic uncertainty by adopting the proposed BEFIT Directive could make the Single Market a less attractive place to do business.

European Commission's Consultation on a proposal for a Council Directive on Transfer Pricing

Position Paper

21 December 2023

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1. About the Irish Tax Institute

The Irish Tax Institute is the leading representative and educational body for Ireland's Chartered Tax Advisers (CTA) and is the country's only professional body exclusively dedicated to tax.

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The Institute is, first and foremost, an educational body but since its foundation in 1967, it has played an active role in the development of tax administration and tax policy in Ireland. We are deeply committed to playing our part in building an efficient and innovative tax system that serves a successful economy and a fair society. We are also committed to the future of the tax profession, our members, and our role in serving the best interests of Ireland's taxpayers in a new international world order.

Irish Tax Institute - Leading through tax education

2. Executive Summary

The Irish Tax Institute welcomes the opportunity to contribute to the European Commission's public consultation on the proposal for a Council Directive on Transfer Pricing (the Directive).

The objective of the Directive is to increase tax certainty, reduce compliance costs, mitigate the risk of double taxation by harmonising transfer pricing norms within the EU through the incorporation of the arm's length principle into EU law and provide clarification on the role and status of the OECD Transfer Pricing Guidelines.

The Institute is supportive of the objective of increasing tax certainty and reducing compliance costs for taxpayers in applying transfer pricing rules. However, as currently drafted, we consider that the Directive is likely to result in a divergence between the transfer pricing rules applying to transactions within the Single Market and the rules which apply to transactions with third countries. Consequently, while the Directive may result in less transfer pricing disputes arising between EU Member States, in our view, it will lead to an increase in such disputes with third countries.

Two sets of transfer pricing rules operating in parallel would undoubtedly add further complexity, in particular for multinational enterprises in scope of Pillar Two, as the Global Anti-Base Erosion (GloBE) Rules require intra-group transactions to be priced consistently with the arm's length principle.

Our members, who are tax professionals that provide tax services and business expertise to Irish owned and multinational businesses, have raised a number of concerns regarding the rules set out in the proposed Directive. These concerns, which have been set out in detail in Section 3 of this paper, include the following:

- It is intended that the latest version of the OECD Transfer Pricing Guidelines will be binding when applying the arm's length principle in Member States. In order to provide certainty to taxpayers, it would be important that any newly established principles or concepts developed under the OECD Transfer Pricing Guidelines would apply on a prospective basis only. In addition, the adoption of the latest version of the OECD Transfer Pricing Guidelines should only take place following consultation with Member States.

- Rather than detailing the transfer pricing rules in the Directive, in our view, it would be preferable for the Directive to simply make reference to the rules as set out in the OECD Transfer Pricing Guidelines. This would help to minimise the inconsistencies in interpretation which may arise between the application of transfer pricing rules under the Directive and the OECD Transfer Pricing Guidelines.

- As currently drafted, the definition of 'associated enterprises' in the Directive is broader than what exists at present in certain Member States, including Ireland, and therefore is likely to result in an increase in the number of transactions that will be subject to transfer pricing rules in such countries. The 25% threshold also establishes a different criterion to define a group from those which are contained in the proposed Council Directive on Business in Europe: Framework for Income

Taxation (BEFIT) and the Pillar Two GloBE Rules. In so doing, this adds further complexity and compliance costs for business. In our view, a 50% shareholding requirement would be more appropriate to determine the requisite association for transfer pricing rules.

- The Directive provides that a permanent establishment (PE) shall be considered an associated enterprise of the enterprise of which it is a part of. Given the legal and economic differences between a PE and legally independent enterprises we consider it essential that the Directive does not seek to equate a PE with an associated enterprise.

3. Observations on the detailed rules of the Directive

We have set out below some further observations on the detailed rules set out in the Directive as currently drafted.

3.1 Article 3 - Definitions

OECD Transfer Pricing Guidelines

The Directive defines the OECD Transfer Pricing Guidelines as those endorsed by the OECD Council pursuant to the OECD Council Recommendation of the Council on the Determination of Transfer Pricing between Associated Enterprises [C(95)126/Final], and as amended in January, 20 2022 and included in Annex I, any further amendments to these OECD Transfer Pricing Guidelines that the Union approved in the context of the OECD Committee on Fiscal Affairs via the adoption of a Union position under Article 218(9) of the Treaty on the Functioning of the European Union (TFEU).

The Explanatory Memorandum clarifies that to ensure a common application of the arm's length principle, the latest version of the OECD Transfer Pricing Guidelines will be binding when applying the arm's length principle in the Member States. It also states that as the OECD Transfer Pricing Guidelines will be amended from time to time that these new guidelines should be the new binding reference framework.

Adopting a dynamic approach to the definition of the OECD Transfer Pricing Guidelines enables mere clarifications of the rules to be applied immediately. However, in order to provide certainty to taxpayers, it would be critical that any newly established principles or concepts developed under the OECD Transfer Pricing Guidelines would apply on a prospective basis only. In addition, the adoption of the latest version of the OECD Transfer Pricing Guidelines should not occur automatically without first consulting and obtaining input from Member States.

3.2 Chapter II - Transfer Pricing Rules

Article 14.1 provides that Member States shall include in their national rules transposing the transfer pricing rules laid down in Chapter II of the Directive,

provisions which ensure that those transfer pricing rules are applied in a manner consistent with the OECD Transfer Pricing Guidelines.

Chapter II of the Directive includes articles on transfer pricing methods (Article 9), comparability analysis (Article 11) and determination of the arm's length range (Article 12). However, many of these areas are already addressed in detail in the OECD Transfer Pricing Guidelines which will be included as an annex to the Directive. Consequently, the proposed approach gives rise to the possibility of a different interpretation of the transfer pricing rules applying to transactions intra-EU to that which would apply for transactions with third countries.

For example, Article 12 of the Directive adopts a different approach to the determination of the arm's length range than the OECD Transfer Pricing Guidelines where the application of a transfer pricing methodology produces a range of values. The Directive prescribes that Member States may only make adjustments if the results fall outside the (interquartile) arm's length range, unless it can be demonstrated that an alternative position within the range is justified by the facts and circumstances of the specific case.

If an adjustment is made, it should be made to the median, unless it can be shown that a different position in the range is justified by the facts and circumstances of the specific case. This proposed different approach to determine the arm's length range under the Directive will impact the pricing of existing intra-EU transactions.

As it is intended that the rules set out in the Directive should be applied in a manner 'consistent with' the OECD Transfer Pricing Guidelines, albeit 'consistent with' is not defined, we consider rather than detailing the transfer pricing rules in the Directive, it would be preferable for the Directive to simply make reference to the rules as set out in the OECD Transfer Pricing Guidelines. This would help to ensure inconsistencies in interpretation do not arise between the application of the rules under the Directive and the OECD Transfer Pricing Guidelines.

If policymakers determine that it is preferable to elaborate further on the rules in the Directive, then care must be taken to ensure that the terminology and principles used in the Directive are harmonised with the OECD Transfer Pricing Guidelines. Accordingly, such newly established principles or concepts should only be considered to form part of a Member State's reference framework after their adoption and of no effect retrospectively.

Article 14 – Application of the Arm's Length Principle

Article 14(2) of the Directive provides as follows: "*The Council may lay down further rules, consistent with the OECD Transfer Pricing Guidelines, on how the arm's length principle and the other provisions laid down in Chapter II of this Directive are to be applied in specific transactions to ensure more tax certainty and mitigate the risk of double taxation."*

We consider the provisions of Article 14(2) create the potential for competing and divergent transfer pricing rules applying to transactions within the Single Market with

the rules that apply to transactions with third countries. Such a divergence could lead to increased uncertainty and increased disputes.

Article 14(2) delegates authority to the Council to create new transfer pricing rules in respect of certain types of transactions provided they are consistent with the OECD Transfer Pricing Guidelines. Article 14(3) provides that these rules shall be taken by means of Council implementing acts based on a proposal from the Commission. The commentary on the grounds for the proposal notes that the Commission aims to draft Implementing Acts for the majority of transactions listed in Article 14 in the first five years of application of the Directive.

As tax is a national competence and sovereignty in tax matters is a fundamental principle of EU law, it would be an imperative for the Directive to address the need for unanimity among Member States to adopt any Implementing Acts in this regard.

3.3 Article 5 - Associated Enterprises

The Explanatory Memorandum to the Directive notes that differences can exist across Member States in the definition of 'associated enterprises' and in particular on the concept of 'control', which is normally the pre-condition to apply transfer pricing. It notes that certain Member States apply a 25% shareholding requirement while others apply a threshold of 50% when it comes to determining whether the control criterion is met.

Article 5 of the Directive proposes a threshold of 25% to determine whether enterprises are associated. It also proposes that an associated enterprise may include a person who participates in the management of another person and can exercise "significant influence" over the other person. However, no definition of significant influence is provided in the Directive.

As currently drafted, the definition of 'associated enterprises' is broader than what exists at present in certain Member States, including Ireland, and therefore is likely to result in an increase in the number of transactions that will be subject to transfer pricing rules in such countries.

The 25% threshold also establishes a different criterion to define a group from those which are contained in the BEFIT proposal and the Pillar Two GloBE Rules and in so doing adds further complexity and compliance costs for business. We believe a 50% shareholding requirement would be more appropriate to determine the requisite association for transfer pricing rules under the Directive.

Permanent Establishment (PE)

Article 5(7) of the Directive provides that a PE shall be considered an associated enterprise of the enterprise of which it is a part of. In light of the legal and economic differences between a PE and legally independent enterprises, we consider it essential that the Directive does not seek to equate a PE with an associated enterprise.

By requiring a PE to be considered an associated enterprise of the enterprise of which it is a part of, it would appear to impose the transfer pricing rules set out in Chapter II of the Directive applying to transactions between associated enterprises to similarly apply to transactions with a PE.

At the same time, Article 14(2) of the Directive provides that further rules may be laid down in a number of areas consistent with the OECD Transfer Pricing Guidelines, on how the arm's length principle and other provisions laid down in Chapter II of the Directive should be applied to specific transactions, to ensure more tax certainty and mitigate the risk of double taxation.

One of the specific transactions listed in Article 14(2) includes dealings between a head office and its permanent establishments. Notably, Article 7(2) of the OECD Model Tax Convention (MTC) contains the Authorised OECD Approach (AOA) to determine the profits attributable to a PE. Guidance on the application of the AOA is set out in the OECD's 2010 Report on the Attribution of Profits to Permanent Establishments. We believe the AOA approach should continue to apply to determine the attribution of profits to PEs and this should be reflected in any proposed Directive on Transfer Pricing at EU level.

3.4 Article 6 - Corresponding Adjustments

Article 6 of the Directive proposes to limit access to the mutual agreement procedure (MAP) for intra-EU adjustments in certain circumstances. Our members have raised concerns that this approach could potentially result in extreme positions being adopted by individual Member States within the EU, with no ability to manage these adjustments through the MAP process. This could also lead to knock-on consequences for multinational groups in-scope of the Pillar Two GloBE Rules.

In our view, a preferable approach would be to create a streamlined procedure for intra-EU negotiations which would include arbitration, to expedite the MAP process while ensuring that Member States continue to have the right to negotiate and or defend their positions.

3.5 Article 13 - Transfer Pricing Documentation

The potential harmonisation of transfer pricing documentation requirements is a welcome feature of the proposed Directive. A possible approach could be to use the existing Local and Master Files templates as included in Annex I – II to Chapter V of the OECD Transfer Pricing Guidelines as a common template across Member States. Consideration could also be given to harmonising the criteria for when the Local File and Master File documentation requirements apply, as well as simplified documentation requirements for SMEs in scope of transfer pricing that would not fall under the Local File and Master File documentation requirements.