ICC INTERNATIONAL CHAMBER OF COMMERCE
The world business organization
Commission on TAXATION

Response to Draft OECD BEPS Discussion Draft on the Revised Guidance on Profit Splits

ICC welcomes the opportunity to comment on the BEPS Discussion Draft on the Revised Guidance of Profit Splits. Our comments are set forth below in response to question numbers.

ICC believes that in most cases a transactional profit split method ("TPSM") will not be the most appropriate method and the introduction to this section of the Guidelines should so state.

1.2 The explanation is not clear. Examples will clarify the distinctions. We will be happy to provide suggestions, as appropriate.

Paragraph 4 appears prescriptive in stating that "typically a transactional profit split of anticipated profits will be used in conjunction with a discounted cash flow valuation technique", however limited practical guidance is provided which will create significant uncertainty.
It could also be noted that a "split of actual profits" could be done either via retrospective or forward-looking adjustments.

We suggest an emphasis that a split of combined profit should be based on value drivers/allocation keys that reflect the functions, assets and risks ("FAR"), with appropriate weight for unique and valuable contribution. When a split is so based, a mere change of actual vs. anticipated profit levels should not require any change in methodology.

We also note that paragraph 6 comments on the greater sharing of risks where a transactional split of actual profits is employed because it allows for the sharing of losses. We are uncertain how this statement would apply in the context in which there is a period of losses whether or not anticipated.

2. The concept of integration is logically useful but practically difficult to utilize. In all MNC groups, there is integration at many levels that does not exist between unrelated parties and which does not necessarily impact transfer pricing relationships (such as administration, coordination, movement of personnel, and so on). If this is a concept intended to be a guiding principle, as suggested in paragraph 6, then examples will have to be developed, including updating for the post-BEPS world and CbC data. Examples would also be helpful for paragraphs 8,9,10 to distinguish circumstances in which the parties might consider sharing in the risks of the business of the other.

5. A critical weakness of the transactional profit split ("TPSM") as formulated, with use of actual or anticipated profits, is that the demarcation between the approaches will be fuzzy in practical reality. In addition, the results are likely to vary depending on which approach is used. In practice, tax administrations may develop both methods and make proposed adjustments on the approach that provides the best answer from a base protection standpoint. Prudent MNEs may utilize both methods seeking to ascertain if they provide consistent results on a TPSM basis, as well as with the one-sided TPMs likely used for documentation purposes. Accordingly, it may be appropriate to include a paragraph suggesting that evaluation of both approaches should, if properly developed from a FAR standpoint, should produce convergent results.

It should also be emphasized that the aggregate of the profit split should not exceed the total actual profit due to utilization of a one-sided benchmarking method applied to either of the parties without considering the profit split factors for each party.

It would also be appropriate to evaluate the likelihood that TPSM determinations by tax administrations will be done after-the-fact, when hindsight may suggest that unrelated parties would have assumed risks differently.

In the comments in paragraph 18 about “a lack of comparables” it is important to note that if reliable comparables are scarce but inexact comparables exist, there should be flexibility to adopt the point in the range which closely reflects the arm’s length price point for application of TPSM (e.g., use of an inter-quartile or full range of results as appropriate). Given that TPSM involves subjectivity and frequent lack of reliable comparables, there should be flexibility in applying this method.

6.1 The sharing of risk is a critical factual question for application of the TPSM. In the present draft, it is not defined in a manner to facilitate application to specific situations. For example, when the CbC Report is prepared, it will reflect the functional elements of the related party transactions and how combined profits are allocated. The taxpayer should be applying the most appropriate method, whether that is a one-sided or TPSM based on anticipated or actual profits.

6.2 The draft could be strengthened to provide additional; descriptions and examples as described above. Again, ICC will be pleased to provide assistance in this regard.

7. Experience in handling profit split cases in APA, Competent Authority, and other contexts is that comparables can often be found in the context of public joint ventures. An example could be so framed.

8. No. The distinction of “sequential” and “parallel” seems academic in nature without reference in the practical world in which transfer pricing matters must be resolved.

11. In related party transactional structures, such as “value chains,” all parties typically make valuable contributions and do not share controllable risk. The transfer pricing question is the appropriate TPM. In such situation, the appropriate profit split answer should be as in paragraphs 18-19 of the proposed Guidelines.

12. Synergies should be treated as is passive association.

13. This “value chain” analysis seems duplicative of normal functional analysis. The discussion of value chain analysis should be moved to Chapter I because, if it is somehow different from a normal functional analysis, it still should relate to all transfer pricing methods and not just the TPSM.

14. Our ICC policy has been to limit our responsive comments to BEPS proposals to these 2 pages. We will be pleased to provide an example of value chain analysis.

15, 16, 17, and 18. Once the issues noted above have been resolved, we will be delighted to propose examples or work with a team to develop appropriate illustrations. In the absence of such update, there is too much uncertainty in the principles to be applied to invest the time to suggest examples.

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