

## EU Joint Transfer Pricing Forum releases report on application of profit split method within the EU and provides summary of achievements of present mandate

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### Executive summary

In March 2019, the European Union (EU) Joint Transfer Pricing Forum (JTPF) released its [Report on the application of the profit split method \(PSM\) within the EU](#) (the Report).

The published Report is the first part of the JTPF work addressing the relevant challenges in the practical application of the PSM for transfer pricing purposes.

The Report was released shortly before the present mandate of the JTPF expired on 29 March 2019. Against this background, the Secretariat of the JTPF also prepared a summary of the achievements for the present mandate during the period 2015-2019.

### Detailed discussion

#### Background

The JTPF assists and advises the European Commission on transfer pricing tax matters and works within the framework of the Organisation for Economic Co-operation and development (OECD) Transfer Pricing Guidelines (OECD Guidelines). It proposes pragmatic, non-legislative solutions to problems related to the practical implementation of the OECD Guidelines by transfer pricing practitioners and fiscal authorities in the EU. The Report, published in March 2019, represents the JTPF's latest publication.

Clarifying the PSM concept was one of the priorities identified in the OECD's Action Plan against Base Erosion and Profit Shifting (BEPS). Due to the ongoing integration of multinational enterprises and globalization tendencies, the PSM is expected to become increasingly relevant for transfer pricing analyses. Consequently, BEPS Action 10 called for supporting advice with respect to the PSM application. Against this background, the OECD published the [Revised Guidance on the application of the Transactional Profit Split Method](#) in June 2018 that clarifies and significantly expands the OECD Transfer Pricing Guidelines on the application of the transactional PSM. However, uncertainties around the question of the practical application of the PSM remain unresolved.

Thus, the JTPF work program for the period 2015-2019 referred to the PSM as one of the topics on which the JTPF should provide output in order to address the issues in the practical application of the PSM. A particular reference is made to the high degree of subjectivity encountered when stakeholders determine how to share the profit.

The JTPF has undertaken an exercise (including surveys of the JTPF members) to take stock of how the PSM is applied within the EU and to work towards a common approach to addressing the relevant challenges in the practical application of the PSM. A key takeaway from the survey was that the PSM has not been widely applied in practice, and that when it is used, this mostly happens in the context of Advance Pricing Agreements (APAs) procedures. The lack of common methodology has been indicated as a reason for the limited use of the PSM in practice.

At the meeting on 24 October 2018, the JTPF members identified four areas for further work on the PSM:

1. When to use the PSM?
2. How to split the profit?
3. Is there a need for simplification?
4. How to simplify the application of the PSM?

Given the time constraints due to the end of the JTPF's present mandate in March 2019, consensus was reached on a two-stage process. During the first stage, the focus should be on clarifying certain concepts related to the PSM based on practical observations within the EU. During the second stage, potential methods of simplification should be further explored.

## Structure of the Report

The Report addresses the first stage and aims to clarify concepts around the application of the PSM in order to outline the current state of play within the EU, namely:

1. When to use the PSM (i.e., in which circumstances it may be considered the most appropriate transfer pricing method) and
2. How to split the profit based on the concepts described in the revised OECD Guidelines as well as by providing an inventory of recurrent profit splitting factors gathered in the survey of the JTPF members.

The Report complements the OECD Revised Guidance on the application of the Transactional PSM issued in June 2018.

Annex 1 of the Report provides a flow chart tree summarizing "when to apply the PSM," whereas in Annex 2 a flow chart tree is presented on "how to apply the PSM." A non-exhaustive and non-hierarchical list and description of profit splitting factors identified in the survey that formed the basis for the Report are included in Annex 3 as well as a brief analysis of the pros and cons of each splitting factor.

## JTPF's key achievements 2015-2019

The present mandate of the JTPF expired on 29 March 2019. The Secretariat prepared a summary of the output over the period 2015-2019, which includes the following additional key achievements:

- [Report on Improving the Functioning of the Arbitration Convention](#) including a revised Code of Conduct for the effective implementation of the Arbitration Convention
- [Report on the Use of Comparables in the EU](#) establishing best practices and pragmatic solutions by issuing various recommendations for both taxpayers and tax administrations in the EU
- [Report on the Use of Economic Valuation Techniques in Transfer Pricing](#) which aims to build a bridge between general practice of economic valuation and transfer pricing
- [Report on a Coordinated Approach to Transfer Pricing Controls within the EU](#) establishing best practices by issuing various recommendations for both taxpayers and tax administrations, and encourages closer cooperation in the field of TP controls

## Implications

There is a possibility that the PSM may be applied more often as new business models emerge, with an increased need for practical simplification. Although the Report does not contain legally binding guidance, it contains

practical clarifications that may be helpful for multinational enterprises when applying a PSM. The Report sets the stage for the JTPF's further analysis in this regard. The upcoming report exploring simplification approaches might be of high practical relevance. Taxpayers are recommended to further monitor the developments.

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## Endnote

1. See EY Global Tax Alert, [OECD releases final revised guidance on application of transactional profit split method](#), dated 27 June 2018.

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Transfer Pricing Group

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