

Mirna Screpante

The OECD Transfer Pricing Guidelines and Value Creation

Income Allocation or Anti-Avoidance Tool?

The OECD Transfer Pricing Guidelines and Value Creation

Why this book?

This book critically assesses the updated guidance on intangibles outlined in chapters VI and I of the OECD Guidelines. This evaluation is conducted in the context of the base erosion and profit shifting (BEPS) initiative Actions 8-10 Final Reports. The primary objective is to determine the extent to which the modifications introduced in the 2010 OECD Guidelines (now the 2022 OECD Guidelines) align with the OECD's intentions and effectively test the concept of "taxation where value is created". The overarching goal is to curtail the "artificial" tax planning potential associated with the arm's length principle (ALP), which seeks to ensure that multinational corporations pay taxes in line with the economic activities they undertake.

To achieve this, the book delves into the novel concept of value creation and the emphasis on "taxation where value is created". It seeks to understand the implications and interpretations of these concepts in the context of the ALP.

Additionally, the book aims to anticipate and potentially define any emerging limits on what is considered permissible and impermissible in terms of "new" tax avoidance strategies. The book highlights the need for a reasonableness test in the ALP to address abnormal or unnecessary value-creating features. This involves scrutinizing whether the modifications can effectively deter the shifting of profits from jurisdictions where economic functions are performed to low-tax regions.

In essence, this book contributes to the ongoing discourse on international tax policy and transfer pricing guidelines. It endeavours to shed light on whether the changes introduced by BEPS, as reflected in the updated OECD Guidelines, will indeed serve as a robust mechanism to combat tax avoidance strategies, thereby aligning taxation more closely with value creation in the global economy.

Finally, this book reveals the intricate interplay between the DEMPE concept, Pillar One and the minimum global tax proposed in Pillar Two. Collectively, they establish a comprehensive framework for combating tax avoidance and advancing equity in the realm of taxation.

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The OECD Transfer Pricing Guidelines and Value Creation

Income Allocation or Anti-Avoidance Tool?

Mirna Screpante

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Dr Mirna Solange Screpante, LL.M.

Foreword

It is with great pleasure and pride that I accepted Dr Screpante's invitation to write this foreword for her important contribution to the ongoing international tax conversation. I was privileged to accompany Dr Screpante on her journey as she explored the evolving landscape and the expanding scope of the arm's length standard in transfer pricing. Serving as an informal mentor, I engaged in frequent discussions and debates regarding her thesis in the vibrant and ever-changing realm of transfer pricing. This book is the outgrowth of Dr Screpante's doctoral study at the Vienna University of Economics and Business.

Doctoral study is a little like the sine wave in mathematics and physics: a continuous and at times seemingly endless series of peaks and valleys of changing amplitude, reacting to developments of various kinds that affect the flow of what is being measured. Gradually, the "highs" of study become higher and the "lows" fewer and shallower, until a consistent and clear pathway is observed. Successful doctoral study – achieving a satisfying and informative pathway of understanding, of a sort for which the sine wave is a suitable metaphor – is the product of pushing the boundaries of sophisticated study and overcoming the intellectual and "life" challenges that influence and from time to time inevitably disrupt the serious study of difficult subjects. It is a process that with great effort yields notable outcomes. Dr Screpante's work exemplifies great effort from which has come this notable book.

There is no doubt that Dr Screpante's original research contributed to her own learning and wisdom about her subject. But equally there is also no doubt that her purposeful and determined examination of the arm's length standard (or "principle") and, more generally, the significance and scope of transfer pricing in international taxation enhanced my understanding of this subject and challenged me, as I hope it will for readers of this book, to rethink my own views about this subject. Her insights about the duality of the arm's length standard as a device to measure income and implicitly assign taxing rights among countries, on the one hand, and a tool to discipline unwarranted international tax avoidance undertaken by or simply the result of the activities of multinational enterprises operating in a legal environment that respects legal constructions of various kinds, offer valuable critical commentary on this difficult balance.

Dr Screpante’s analysis is particularly stimulating because she was required to confront and understand her subject beyond the seemingly obvious – but in fact elusive – notions of the “accurate delineation” of transactions that are “commercially rational” in the service of “value creation” somewhere by somebody. The task was made more difficult because the accepted parameters of international tax jurisdiction, of which transfer pricing’s quest for the “source” of income when interested transaction parties are parts of an economic unity, have been in a state of flux most recently because of the OECD base erosion and profit shifting (BEPS) Project and its emanations, Pillars One and Two. The OECD’s critical evaluation of the adequacy and utility of accepted parameters of international income measurement and distribution lie at the heart of transfer pricing, served by the discipline of the arm’s length standard.

Yet, we do not live in a world of universal tax or legal systems; this reality cannot be avoided. So, how do we mobilize the arm’s length standard as a signpost for agreeing on acceptable international income allocation, and with it, an agreeable assignment of taxing rights among countries in the spirit of the OECD and UN Models? Fundamentally, it is this that Dr Screpante’s research explores, using a thorough understanding and chronicle of the income measurement versus anti-avoidance duality of the arm’s length standard as her platform. Indeed, understanding the objectives served by and the coherent principled application of the arm’s length standard requires a textured understanding of that standard well beyond a simple exposition of the two extremities of the duality. Dr Screpante’s careful work reflects this.

More than that, however, and indeed, before advances in the expression of Pillar One in particular, Dr Screpante broached what in transfer pricing has for years been a somewhat “untouchable” subject, that is, the use of objective formulas to translate manifestations of economic activity into credible income assignments for countries touched by the business operations of multinational enterprises. Dr Screpante uses the OECD’s development, enhancement, maintenance, protection and exploitation formulation to align the economic and jurisdictional attachment of income from “intangibles” as a point of reference not only to understand what the arm’s length standard seeks, and has always sought, to accomplish, by an example of how the opacity of that standard could be enhanced by the kind of disciplined objective connotations she recommends.

This book offers transfer pricing neophytes the opportunity to plunge safely into the “deep end” of transfer pricing, providing a window on the

international tax conversation that is continuing. It also offers experienced thinkers about and practitioners of transfer pricing a critical foil for testing and enhancing their understanding of transfer pricing's objectives, in themselves and as irrepressible influences on the recalibration of international taxation which seemingly is the ambition of BEPS Project and the Pillars One and Two.

Dr Screpante's analysis engages as it challenges the standard assumptions and the shibboleths of transfer pricing. In so doing, it makes us better thinkers about this important subject. And, as a supporter of Dr Screpante's research from its beginning to completion, I know that this book is the product of a lively mind, careful intellectual effort and a purposeful commitment to and passion for her subject – features that make the insights offered in this book even more important to consider.

Scott Wilkie
Toronto, Canada
September 2023

List of Abbreviations

ALP	Arm's length principle
AOA	Authorised OECD Approach
ATO	Australian Taxation Office
BEPS	Base erosion and profit shifting
CRA	Canadian Revenue Agency
DEMPE	Development, enhancement, maintenance, protection and exploitation
ECJ	Court of Justice of the European Union
ETR	Effective tax rate
EU	European Union
G20	Group of 20
G8	Group of 8
GAAR	General anti-avoidance rule
GVC	Global value chain
GVCA	Global value chain analysis
ICC	International Chamber of Commerce
ICTA	Italian Corporate Tax Act
IP	Intellectual property
ITA	Income Tax Act
ITAA	Income Tax Assessment Act

List of Abbreviations

LGT	<i>Ley General Tributaria</i>
LIS	<i>Ley de Impuesto a las Sociedades</i>
LOB	Limitation on benefits
MNE	Multinational entity
OECD Model	OECD Model Tax Convention on Income and on Capital
OECD Guidelines	OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations
PE	Permanent establishment
PSM	Profit split method
PPT	Principal purpose test
SAAR	Special anti-avoidance rule
UN	United Nations
UN Model	United Nations Model Double Taxation Convention between Developed and Developing Countries
US Reg.	United States Regulations
VCA	Value chain analysis



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