

**[full legal name of the head office entity]**

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Local Country file FY 20**[XX]**

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**[Month, year]**

DRAFT

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## **4. OECD Transfer Pricing Guidelines applicable to intra-group services**

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### **4.1 Introduction**

To ensure that the charges made in relation to the intra-group services rendered are in accordance with internationally accepted standards for tax purposes, the [XYZ] group has adopted the arm's length principle for determining service charges. The arm's length principle states that the charges for the intra-group services should be similar to those that would have been made and accepted between independent companies in comparable circumstances.

The approach to set arm's length service charges can be derived from chapter VII of the OECD Guidelines<sup>4</sup>. This section therefore provides a summary of the Guidelines with regard to intra-group services.

### **4.2 Basic principles**

Chapter VII of the OECD Guidelines specifically deals with issues that arise in analysing the provision of intra-group services within a multinational group. The issues recognised by the OECD in analysing intra-group services are briefly summarised in the remainder of this section.

As intra-group service activities vary considerably among groups, each case is dependent upon its own facts and circumstances and arrangements within the group. However, there are two main issues that are addressed in the guidelines. The first issue is determining whether services have, in fact, been provided and have conferred a benefit to the receiving group company. The second issue is determining the appropriate charge for such services in accordance with the arm's length principle.

### **4.3 Transfer pricing methods to determine arm's length prices**

Payments or non-payments made to an associated enterprise for supposed services are not prima facie evidence that such services have been rendered. The OECD Guidelines state that determining whether an intra-group service has been rendered depends on whether the activity in question provides a group member with economic or commercial value to enhance its commercial position. This, in turn, can be determined by considering whether or not the service recipient would have either paid an independent party to perform the services or would have performed the service in-house. If the services would not be paid for in either of these manners, it ordinarily is not considered an intra-group service. The facts and circumstances of each situation will largely determine the result. However, an analytical framework to assess the arm's lengthness of intra-group services is provided in the Guidelines.

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<sup>4</sup> Chapter VII deals with 'Special Considerations for Intra-Group Services'.

expected benefits of the services provided, bearing in mind that some costs will never actually produce the benefits that were reasonably expected when they were incurred.

To determine the amount of the charge for the intra-group services, both the perspective of the service provider and the perspective of the recipient of the service should be considered. In this respect, relevant considerations include the value of the service to the recipient and how much a comparable independent company would be prepared to pay for that service in comparable circumstances, as well as the costs incurred by the service provider.

## **4.6 Functional analysis**

In order to satisfy the arm's length principle, the allocation method must lead to a result that is consistent with what comparable independent enterprises would have been prepared to accept. The OECD Guidelines permit the determination of intra-group services through a specific allocation method and through various non-specific allocation methods. The use of a specific allocation method is encouraged since it entails a rather direct relationship between costs incurred and the services rendered. The non-specific allocation methods are defined as cost allocation and apportionment methods, which necessitate some degree of estimation or approximation as a basis for calculating an arm's length charge.

The OECD Guidelines suggest the use of a functional analysis to establish a relationship between the provided services and the members' activities and performance. Consideration should also be given to the long-term effect of the service and whether the costs will ever actually produce benefits. Taxpayers should be able to demonstrate the reasonableness of their charges. Adequate documentation should be available that can be examined by the tax inspector and whereby the related party involved (either renderer or recipient) is able to demonstrate the reasonableness of the charges.

## **4.7 Low value adding services**

### **4.7.1 Introduction**

On 5 October 2015, the OECD released its final 2015 reports under its Action Plan on Base Erosion and Profit Shifting ("BEPS"). The report on BEPS Actions 8-10, Aligning Transfer Pricing Outcomes with Value Creation (the final report)<sup>5</sup>, inter alia contains revisions to Chapter VII of the OECD Guidelines regarding low value-adding intra-group services.

The main focus of the revision is the new Section D containing additional guidance with respect to an elective, simplified transfer pricing approach for low value-adding intra-group services. The OECD describes the guidance as being intended to achieve a balance between appropriate charges for low value adding services and head office expenses and the need to protect the tax base of payor countries.

Key features of the new guidance include:

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<sup>5</sup> OECD (2015), Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 - 2015 Final Reports, OECD Publishing, Paris.

# 5. Functional analysis

## 5.1 Introduction

This section provides a detailed description of the various services provided by [HQ]'s departments to the operating companies. It describes the nature of the services rendered, the cost structure related to these services and the benefits of these activities to the various operating companies. The functional analysis will be the basis for the charges related to the services made by the departments of [HQ].

Each support department of [HQ] reports its costs in one or more cost centres.

For the descriptions of the activities we relied on the information supplied by [HQ] and on information obtained during interviews with key staff members at the company.

## 5.2 [HQ]

In order to obtain an indication of the relative size of each of the activities of [HQ] and its respective departments, please find below a table indicating the number of employees per department that is subject to review.

*Table 4: FTEs per department*

Department	#of FTEs
[Executive board]	[X] FTEs
[Human resources]	[X] FTEs
[Legal]	[X] FTEs
[Finance]	[X] FTEs
[Tax]	[X] FTEs
[Sales and marketing]	[X] FTEs
[Information technologies]	[X] FTEs
[Procurement]	[X] FTEs

### 5.2.1 Executive board

#### 5.2.1.1 Activities

The executive board of the [XYZ] group is responsible for the development of the short-term and long-term vision and strategy with respect to the returns and value of the [XYZ] group. In addition, it is managing, stimulating and providing guidance to the group companies in many

### 5.2.8.2 *Benefits*

The main benefits that the operating companies derive from the activities of the procurement department are:

- Generating cash savings for the entire group by way of bundling procurement volumes, a good understanding of the suppliers and the relevant markets;
- Ensuring that the procured goods are delivered in alignment with the required specifications and in time;
- Establishing consistent quality of the procured goods; and
- Sharing of available knowledge and best practices with the various operating companies.
- [Please add other benefits or adjust this list]

### 5.2.8.3 *Cost structure*

The costs for this department are reported in [a] [several] separate cost centre[s]. The costs incurred by the procurement department mainly consist of salaries, fringe benefits, social security charges and overhead and travel costs.

## 5.3 **Entity characterization**

Based on the functional analysis as described above, it can be concluded that [HQ] as the [XYZ] group's head office provides and coordinates a wide range of useful and beneficial services in above-mentioned functional areas to the operating companies. In this intercompany transaction [HQ] should be considered as the service provider. The operating entities have a continuous need for qualified and experienced assistance and could be considered as the service recipients.

basis of the turnover realized by a particular operating company compared to the total turnover of the [XYZ] group of companies. The costs incurred by the departments Human Resources are allocated on the basis of the number of employees of the relevant operating company compared to [XYZ] group’s total number of employees. [HQ]’s management considers said allocation keys to provide a fair reflection of the benefits received by the various country offices and local entities.

*[Please note that the above serves as an example. Allocation keys should be determined in alignment with the expected benefits the relevant activities confer to the operating companies. Therefore, other allocations keys, like assets or number of licences, may also be used]*

**6.5 Actual charge out**

The charges for the directly allocable services and costs (as determined in Step 3: above) will be made on a monthly basis and be based on the actual costs borne.

The charges for the indirectly allocable services (as determined in Step 5: above) will be made on a semi-annual basis and -provisionally- be based on the expected costs for the year.

Following year-end, all actual costs associated with the indirectly allocable costs will be gathered and analysed. In addition, the average value/number of the applied allocation keys will be determined for the past year. This is done by adding the value/number of the respective keys at the beginning and end of the year and dividing them by two.

To the extent the actual indirectly allocable costs for an operating company for the full year deviates from the costs that were charged in the two provisional invoices over the year, a true up is made in a final invoice for the past year. [HQ] strives to issue this final invoice within 6 months following the end of the year.

Please find a detailed overview of the actual charges made to the operating companies for FY [20XX] in *Appendix VII*. The table below summarizes this overview:

*Table 6: Allocation of head office services costs*

(in [Currency])	Step 1	Step 2	Step 3	Step 4	Step 5		
Department	Total costs	Reallocation of costs	Direct costs	Shareholder costs	Indirect costs	Mark-up of [%]	Charged to operating companies
Executive Board							
Human Resources							
Legal							