BEPS
ACTION PLAN

ACTIONS 8, 9, 10 AND 13 AND TRANSFER PRICING IN BRAZIL

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PRESENTATION PLAN

- **BEPS AND BRAZIL**
- **BEPS ACTION PLAN AND ACTIONS N. 8, 9, 10 AND 13**
- **ASPECTS OF BRAZILIAN TRANSFER PRICING METHODOLOGY**
- **TRANSFER PRICING IN BRAZIL AND BEPS ACTIONS N. 8, 9, 10 AND 13**
- **FINAL REMARKS**

BEPS AND BRAZIL

- "Action Plan on Base Erosion and Profit Shifting", issued in July 2013, formally endorsed by the G20. OECD. – Brazil is not OECD member, but a G20 member.
- Brazil joined the BEPS Project, and as a G20 member, it also coordinates the BEPS initiative.
- Brazil is also approaching to OECD, it has joined important fora of the OECD, especially those related to taxation. On June 3, 2015, Brazil signed a Cooperation Agreement with OECD.
- OECD countries are engaged in attracting developing countries.
- BEPS is a very serious problem for developing countries when they rely on foreign MNEs for tax revenue.

BEPS ACTION PLAN AND ACTIONS N. 8, 9, 10 (*Assure that transfer pricing outcomes are in line with value creation*) AND 13 - ACTIONS RELATED TO TRANSFER PRINCING

8 – Intangibles

9 - Risks and capital

10 - Other high-risk transactions

13 - Re-examine transfer pricing documentation

8 – Intangibles

Action Plan 8 shall be developed to prevent BEPS caused by moving intangible among the members of the economic group. To reach this goal, the following issues are considered:

a) a broader definition of intangibles;

b) allocation of profits associated with intangibles in accordance with value creation;

c) special rules for transfer of hard-to-value intangibles; and

d) updating the approach to cost contribution arrangements

The proposal replaces the former Chapter VI of the OECD TP Guidieiness by a new language followed by an annex with examples (the chapter was changed from 10 pages to more than 100 pages). The new Chapter VI of the OECD TP Guidelines is more comprehensive and clear and tends to be more useful for tax administrations facing the intangibles challenge.

9 - Risks and capital

Regarding risks and capital, the OECD Action Plan on Base Erosion and Profit Shifting states that it is necessary to avoid the shifting risks among, or allocating excessive capital to, group members.

Relation with interest deductions, and other financial payments, also to the work on hybrids and CFC rules.

10 - Other high-risk transaction

This Action is related to unusual transactions between third parties, i.e., operations that would not happen between unrelated parties.

Adoption of special measures and specific transfer pricing rules aiming to:

a) clarify the circumstances in which transactions can be recharacterised;

b) clarify the application of transfer pricing methods, in particular profit splits, in the context of global value chains; and

c) provide protection against common types of base eroding payments, such as management fees and head office expenses.

<u>Discussion draft regarding cross-border commodity transactions</u>

<u>Discussion draft on of low value-adding intra-group services</u>

13 - Re-examine transfer pricing documentation

It will require that "MNE's provide all relevant governments with needed information on their global allocation of the income, economic activity and taxes paid among countries according to a common template."

a) **addresses the issue of country-by-country reporting, which was not considered in the previous version of Chapter V of the OECD Transfer Pricing Guidelines;**

b) **expresses concerns on compliance;**

c) **revised the standards for transfer pricing documentation and replaced the Chapter V of the OECD Transfer Pricing Guidelines with a more detailed orientation and 3 annexes.**

- **Three levels of documentation: CbCR, master file (high-level global information regarding their global business operations and transfer pricing policies) and local file (shows relevant related party transactions).**

The CbCR:

requires multinational enterprises (MNEs) to report annually and for each tax jurisdiction in which they do business the amount of revenue, profit before income tax and income tax paid and accrued. It also requires MNEs to report their total employment, capital, retained earnings and tangible assets in each tax jurisdiction. Finally, it requires MNEs to identify each entity within the group doing business in a particular tax jurisdiction and to provide an indication of the business activities each entity engages in.

METHODS ADOPTED BY BRAZILIAN TP REGULATIONS

There are two set of methods for goods, services an rights (in general):

For import transactions:

Comparable Uncontrolled Price Method (PIC)/(PCI) **(CUP)**
Resale Price Method (**20% gross profit margin or other specific margins for specific economic sectors**) (PRL) **(RPM)**
Cost Plus Method (20% mark up margin) (CPL) **(Cost Plus)**

For export transactions.

Comparable Uncontrolled Price Method (PVEx)/(PECEX) **(CUP)**
Wholesale Price in the Country of Destination Less Profit Method (15% gross profit margin) (PVA) **(RPM)**
Retail Price in the Country of Destination Less Profit Method (30% gross profit margin) (PVV) **(RPM)**
Cost Plus Method (15% mark up margin) (CAP) **(Cost Plus)**

METHODS ADOPTED BY BRAZILIAN TP REGULATIONS

<u>Other features:</u>

- **Transactional methods (Profit Split and TNMM) are not allowed by law;**
- **PCI and PECEX are specific methods for commodities, based on the market price (6th method);**
- **Specific methodology for loans based on market rate (similar to 6th method);**
- **Safe harbors;**
- **Intangibles, in general, in import operations, are not subject to transfer pricing adjustments (subject to limited deductions);**
- **Strict treatment for transactions with non cooperative and low tax jurisdictions**

METHODS ADOPTED BY BRAZILIAN TP REGULATIONS V. OECD GUIDELINES

BRAZIL	OECD
PIC /PCI– PVEx/PECEX	***Comparable Uncontrolled Price (CUP)***
PRL – PVA/PVV	***Resale Price Method (RPM)***
CPL – CAP	***Cost Plus Method***
N/A	***Transactional Net Margin Method (TNMM)***
N/A	***Profit Split Method***

TRANSFER PRICING IN BRAZIL AND BEPS ACTIONS N. 8, 9, 10 AND 13

Action 8 - Intangibles

The BEPS approach does not substantially affect Brazilian methodology because intangibles, in general, in import operations, are not subject to transfer pricing adjustments. The Brazilian methodology, where transactional methods are not allowed, makes the issue of intangibles more practical and predictable, by limiting the deductibility based on a percentage of the revenue (gross receipt) derived from the use of the intangible.

TRANSFER PRICING IN BRAZIL AND BEPS ACTIONS N. 8, 9, 10 AND 13

Action 9 - Risks and capital

Brazilian legislation regarding to aspects related to Action 8 are covered by TP rules for interest and also by the legislation to prevent the harmful tax effects from thin capitalization and CFC rules (Action 3 of the BEPS Action Plan). It is interesting to note that the Actions of the BEPS Action Plan are not independent, i.e., sometimes there is more than one approach to the same tax problem.

TRANSFER PRICING IN BRAZIL AND BEPS ACTIONS N. 8, 9, 10 AND 13

Action 10 - Other high-risk transactions

***Clarify the circumstances in which transactions can be recharacterised*.**

Brazilian legislation does not have too much room for recharacterisation. However, there are regulations that prevent the abuse of certain arrangements allowing to tax a transaction as it had been recharacterized. It is the case of the interposed person, where an international transaction is conducted as it was a transaction between non-related parties. It is worth mentioning that this aspect is closely related to the Action 12 (Require taxpayers to disclose their aggressive tax planning Arrangements) - in this regard, Brazilian Government recently issued the Provisional Measure n. 685/2015.

TRANSFER PRICING IN BRAZIL AND BEPS ACTIONS N. 8, 9, 10 AND 13

Action 10 - Other high-risk transactions

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***Clarify the application of transfer pricing methods, in particular profit splits, in the context of global value chains*.**

Currently it is not a relevant aspect because Brazilian TP legislation does not adopt transactional methods.

***Provide protection against common types of base eroding payments, such as management fees and head office expenses*.**

Depending on the circumstance the deduction is limited, and, in general, the benefit test always apply. Transactions with non-cooperative/low-tax jurisdiction are subject to additional restrictions to allow tax deduction.

It also relates to cross-border commodity transactions, which is covered by the Brazilian adoption of the specific method for commodities based on the market price (PCI and PECEX).

TRANSFER PRICING IN BRAZIL AND BEPS ACTIONS N. 8, 9, 10 AND 13

Action 13 - Re-examine transfer pricing documentation

MNEs operating in Brazil (as a resident company) have to disclose their profits for tax purposes by country, including profits of all their foreign subsidiaries and investments abroad and show detailed information on imports an exports (in line with the CbCR, but not so detailed as it requires). In Brazil the tax returns are filled electronically (tax accounting is also electronic), and documentation (invoices, contracts, etc.) are presented to tax administration only when the taxpayer is asked to do so (under tax auditing procedure), or when the taxpayer asks for modification of the pre-determined margins.

The question is whether the full adoption of the Action 13 is really necessary in Brazil, considering the simplicity of Brazilian TP approach, and the fact that transactional methods are not adopted in Brazil, and that the current source of information is, in the majority of the situations, sufficient to apply Brazilian TP approach.

FINAL REMARKS

BEPS Actions 8, 9, and 10 may not affect too much Brazilian TP legislation unless Brazil changes the law by adopting transactional methods.

- **Under Brazilian tax law the issue of intangibles is more practical and predictable, by limiting the deductibility, which is based on a percentage of the revenue (gross receipt) derived from the use of the intangible. The same with interest payments, which particular method is similar to the sixth method approach (is assumed that the interest rate for some money markets is a proxy for the arm´s length interest rate). The commodities transactions are also subject to specific methodology which is in reference to a quoted price – in line to the BEPS current approach.**

- **Strict treatment of transactions with residents of non-cooperative/low-tax jurisdictions also avoids strategies aiming to erode tax base and shift profits.**

FINAL REMARKS

- As for the Action 13, we will have to wait for future developments of the approach adopted by the BEPS/G20, in order to see the effectiveness of the new approach.

- In any case, a multilateral agreement on information exchange is important, and Brazil has signed the Multilateral Convention on Administrative Assistance in Tax Matters (03/11/2011).

We also have to keep in mind that each country has its particularities and, therefore, there is no one-size-fits-all set of tax measures that will solve transfer pricing complex issues across the globe. Differences in tax legislation, tax structure, tax administration capability, <u>accounting systems</u>, the level of expertise, development level, etc., which vary from country to country are also barriers for such proposals.

Thank you!

Obrigado!