Transfer Prices. National and European Perspectives

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Abstract. *There is no doubt about the essence of transfer pricing, the Organization for Economic Cooperation and Development presents itself as a Umberto Eco reflecting economic globalization. A brief description is given but it is very broad in key concepts in this area. Through continuous ideas on national and European legal rules to the rules on the issue of concern, it is in the sense of guaranteeing legal tax treatment by referring to affiliated and independent taxpayers. The present paper presents the basic concepts and principles in the field of transfer pricing, which is very necessary for the perception of the phenomenon of internationalization of business, and of all the transfer price.*

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1. Introduction

According to the Organization for Economic Cooperation and Development (OECD) definition, transfer prices are "the prices at which a company transfers tangible goods, intangible assets or provides services to associated companies" (Art.19(5)).

These are more simply defined as the transfer price at which a person (whether natural or legal) (Official Gazette of Romania, no. 1074/18 November 2020.) transfers goods – whether tangible or intangible – and services to a related person. Transactions between affiliated persons are carried out according to the principle of free-market price – the arm's length principle, as it is found in the OECD transfer pricing Guide without being influenced by the relationship between them.

The subject of transfer pricing is a highly complex one. These have emerged in the context of groups of firms with a presence in several States (multinational companies) carrying out economic activities in these States. Transfer pricing developments are closely linked to the development of commercial relations between States and the emergence of the first multinational groups operating in different States. The focus is now on this issue, as transfer prices are seen by transnational companies as tax optimizations and the state wants measures to protect tax revenues and, above all, measures to avoid, in some ways, the need for a more effective system of tax protection outsourcing the tax base of taxpayers to affiliated entities in order to obtain a more favorable tax regime.

The importance and timeliness of the article, which deals with current aspects of the contemporary economy, in the field of transfer pricing, as it is a topical issue but also a subject of conflicting views (Abdallah, W. M., 2004). With the in-depth study of this subject, I have studied that things are not as simple as that, the reality is much more complicated than it seems because the situations encountered in economic relations are so diverse that analysis of transfer prices can become extremely difficult. This study is based on a logical structure as it presents the conceptual framework of

transfer pricing, its history, the legislation underlying transfer pricing, the methods of setting, and the influence of transfer pricing on the tax and economic system in Europe.

We are talking about transfer pricing when referring to transactions between related persons (i.e. transactions between companies within the same group). Transfer pricing rules apply to all transactions between affiliated persons, whether transfers of goods or intellectual property rights, provision of services, or other types of transactions. According to these rules, transactions between related persons must be carried out by following the market value principle (so-called "arm's length principle"). Principle underlying the entire transfer pricing analysis and reflected in Article 9 of the model tax Convention and domestic legislation. The rationale for the transfer pricing market value of intra-group transactions shall be provided by the preparation of specific documentation.

The OECD (Organization for Economic Cooperation and Development) directives have established "arm's length" as the basic principle of transfer pricing theory (Law no. 571/2003). What is the link between the length of the arm and the requirement that transaction prices between affiliates are close to market prices for similar transactions?

The explanation is simple - when two close people (affiliates) meet, have the natural tendency to embrace. The TP theory requires that the same relationships remain between them as between two (independent) strangers, who shake hands when they complete a transaction and thus remain at...an arm apart.

2. Current study of transfer pricing knowledge

National transfer prices are ubiquitous in that they can apply to all goods, services, finance, and intangible assets circulating between members of a group located in different parts of the world. Tax authorities in many countries are modernizing their legislation to ensure that they collect a fair amount of income from companies operating in their justice system. However, draconian tax rules can negatively affect world trade and directly reduce foreign investment.

Transfer prices remain a matter of interest both for related party trading companies and for tax inspectors who have stepped up controls in this area. Many companies already have experience in drawing up a transfer pricing file and even documenting the provision of low value-added services (Choe, Chongwoo, 2020). For this type of transaction, the Organization for Economic Cooperation and Development ("OECD") has recently issued proposals to simplify legislative requirements. Will these proposals also be taken into account in local transfer pricing legislation?

As you already know, transfer prices are the prices established in transactions between a company and its related parties. Affiliation between two legal entities occurs when there is a direct or indirect holding of at least 25% of the shares or if one of the legal entities controls the other. In the case of natural persons, the affiliation exists between the spouses or between the relatives up to and including the 3rd grade.

Any company carrying out intra-group transactions shall, at the request of the competent tax body, prepare and submit the transfer pricing file. In fact, this documentation shows whether the transactions in question comply with the market value principle or not, and possibly sets out the reasons why this principle is infringed. In jurisdictions with advanced transfer pricing legislation, such as the United States, Canada, Australia, France, tax authorities recommend or even require the preparation of contemporary documentation – documentation prepared annually with the intra-group transaction. Therefore, there is the possibility that also locally, such provisions may appear over time (Holland, 1993).

In addition to the content requirements of the transfer pricing file laid down in order 222/2008, the local transfer pricing legislation refers to the transfer pricing guidelines issued by the Organization for Economic Cooperation and Development ('OECD Guidelines'). Therefore, it is good that any proposal or amendment made by the OECD in the field of transfer pricing should be taken into account by Romanian companies.

A common category of transactions requiring transfer pricing documentation is the provision of low value-added (or underlying) services. Most of the Romanian companies that are part of a group contract/provide such services to companies within the group.

The scope of the support services is very diverse, including support services, human resources, marketing, legal services, accounting, auditing, and administration, etc. the support services are distinguished by the fact that they are not part of the group's main activity, they do not involve the use or creation of single/valuable intangible assets or generate significant commercial risk.

The main problem for these services is that, while they do not add considerable value to the operational work, they entail a high cost of documentation in terms of transfer prices. Therefore, solutions have been proposed to simplify documentation and even certain values for the related market value range.

Such a document shall be issued by the Joint transfer pricing Forum of the European Union (See International Bureau for Fiscal Documentation (IBFD), 2005). It defines the underlying services as "services related to the activity of the beneficiary" and States that the profit margin applied by the providers of these services should be "between 3 and 10%, most often around 5%". In some jurisdictions (e.g. Germany), these values constitute the very range of market value, and the requirements for documenting the provision of low value-added services are limited.

The transfer price is the price charged between companies of the same group located in different countries (Ernst&Young, 2020). In the sale of goods, the price can be undervalued to reduce business profits in a country and to limit tax on profits there. For example: A French-based company selling to its subsidiary in Hong Kong EUR 15.000 a service invoiced in general for EUR 10.000 on the French market decreases its profit by EUR 5.000 in France, where it is taxed by 33,3% and increases by the same amount in Switzerland, Where it is not taxed (0% tax on income earned outside Hong Kong). This operation brings savings of EUR 1.650 to the group, which can become a very significant profit if this operation is carried out several times.

Transfer prices work very well in the other direction too: Jersey's best known example is: There are no growing bananas in Jersey, yet this jurisdiction is the world's largest banana exporter. This is due to the intensive practice of transfer prices by banana sellers. Bananas are sold by a company in Costa Rica (for example) to a company in Jersey. Jersey will then resell these bananas to another company in the same group in France, but at a much higher price, thus allowing most of the profits to be left to Jersey and leaving me only a small margin during the resale in France to French.

How can you justify these price differences from one country to another to the tax authorities?

In the context of a transfer price sale, the French company can justify this tax difference in 2 different ways:

- or showing that the product or service sold is not exactly the same
- or through a consideration obtained from its subsidiary: a counseling service or product promotion on the final market.

The Commission notes that the transfer pricing report does not contain any information that would be available to the tax authorities in the absence of the contested tax ruling.

Companies are concerned not only with sales of goods but also with all intra-group services: the division of certain common costs between several companies in the group (general administration or head office costs), the provision of persons or goods, concession fees for patents or trademarks, financial relations, services provided by a group company to other companies, etc.

3. Taxation of companies

As regards CCTB and CCCTB (Common Corporate (Consolidated) tax base (CC(C)TB),(European Commission, 2005), these are two proposals for EU directives on Harmonization at Member State level of the rules for calculating the taxable base subject to corporate tax (but not the tax rate), as well as introducing rules on tax consolidation in terms of corporate tax and the distribution of income at the level of group entities based on a calculation formula.

The common consolidated corporate tax base of European companies is approaching rapidly. The two projects being the common base (CCTB), i.e. consolidation (CCCTB), have been passed by the European Parliament (EP) with a large majority and several amendments aimed at increasing its revolutionary fiscal character.

In the Commission's draft Directive, the calculation formula provided for allocation by three factors, taken in equal proportions, 1/3 – work (factor divided equally between wages and number of employees), (tangible) assets, and sales by destination. Subsequently, in the light of research into a practical way of taxing the digital economy, the EP's ECON Committee also proposed the introduction of a fourth factor, also equal to the three other factors – the data factor, expressing the collection and use of personal data by online platforms and service users. It should be noted that, according to the amendments, a factor can be eliminated if it does not fit into the business model while maintaining the principle of equal shares for the relevant factors.

The initial study establishes that the system will only be mandatory for European companies belonging to groups whose annual consolidated revenues exceed EUR 750 million. The European Parliament wants to 'zero this threshold within seven years'.

The notion of permanent establishment becomes crucial in the distribution of financial results. This famous wording "CCCTB will ensure that taxes are paid where profits are generated" (Gresik, Thomas A, 2020) the European Parliament added, "and where companies have a permanent establishment".

Among the advantages and objectives pursued by the introduction of the CCTB and the CCCTB are:

-significant reduction of administrative costs and obstacles for EU cross-border companies;

-giving the possibility at company level to compensate the profits made in one EU Member State with the losses made in another;

-assuring a stable and transparent system at EU level;

-assuring an increased legal certainty at the level of companies;

-reducing fiscal obstacles (such as double taxation) or fighting the practices of avoiding taxation, stimulating investments in research and development etc.

All these initiatives in international and European taxation can have a significant impact both at the level of companies (which can be put in a position to rethink their operational and financing model) and at the level of the countries that will implement the tax measures.

Thus, it is certain that the countries concerned will have to prevent the impact of these measures from attracting investment and developing the business environment, in a global economy in which multinational companies are adopting more and more rapidly to legislative changes. It remains to be seen to what extent (and at what speed)

Romania's fiscal legislation will adapt to what the global fiscal landscape offers, to benefit from opportunities and attract more foreign investment (which will generate more than necessary positive impacts at the macroeconomic level).

Let's also add that the Euro-parliamentarians wanted to send a clear message that the new fiscal environment is intended to restore group transactions on new bases. An EP amendment added that "transfer pricing means the prices at which transfers of tangible goods or intangible assets are completed or services are provided in relation to related parties".

Beyond the technical aspects, the CCCTB means a new European tax policy. In this regard, we also wanted to draw attention through our new Article transfer pricing services, which was also taken over by the press (Official Gazette of Romania, 2020). A new signal that we now need more than ever to define a place in Europe. Otherwise, the evolution of our economy will be one with ascent and descent.

It is starting to be more and more likely that in a year we will somehow come to throw something away, looking at how we changed (overnight) the framework of direct taxation. So, in March, there was an earthquake. Predictable, but the earthquake was also approved by the European Parliament (Pricewaterhouse Coopers, 2020) (EP) with a large majority of the historic CC(C)TB project. The European Council is therefore still taking a step and the CC(C)TB is now present.

After the questions asked: But what do you mean by these statistics? This is a legitimate question, since for three years since Brussels has put this old subject back on the European public agenda, Bucharest, caught up with the explanation of the small-big fiscal "revolutions". he found no time for any minimum information of his own public opinion on what to come.

Because those initials come from the English version of the "common (consolidated) corporate tax base". We are talking about a system that is binding at the moment only for European companies, which are part of groups with total revenues of more than EUR 750 million, but as will be pointed out, this threshold will be reduced in seven years and thus the system's generalization.

Since the summer of 2015, since the European Commission started its new wave of shock, it has been trying to draw attention to the next perspective – after limiting state aid, small national economies will now no longer be able to come to investors even with the argument that we are more attractive, because, for example, we have accelerated depreciation." It will be a common basis across Europe and so there will be one set of rules on how to calculate profit and how to tax. I then came, for the first time, with a profit allocation exercise, building on the CCCTB algorithm model proposed by the European Commission, which confirms what we could see: that subsidiary where only cheap labor is located, where there are no large sales and where value-added is low, that subsidiary is unable to make claims for a substantial part of the profits of the group.

The alarm signals were not meant to try to stop the European train - not even influential countries at the European level can do this, but to trigger debate analyzes, questions, perhaps even answers, if we can negotiate something more, let us do it, if not, then let's get ready from now on with a treatment to strengthen Romanian companies after this shock. And as it is clear that this treatment can no longer be based on taxes, deductions, facilities, the issue where the difference can be made is at the administrative level, I see only the chance of a fantastic improvement in procedures, administrative and fiscal rules.

21st century how the tax was said based on data collected by the Smart digital platform. In any case, more elegant than the brutal French proposal (which Romania had also been involved in) to tax turnover, a tax which, as in the case of VAT, would have made direct use of the final customer's pocket.

In theory, the Commission has presented two draft directives – the common base (CCTB) with a deadline of 1 January 2019 (Official Gazette of Romania, no. 147/18 February 2019.), followed by consolidation (CCCTB) – until 1 January 2021. In practical terms, as has been seen in THE EP, the two projects are practically dealt with together.

In the subsidiarity opinion issued last February by the lower House of the Dutch Parliament, the members of the ruling VVD admit that "there will be no going back, resulting in the same problems as the current inflexible VAT system, in which the introduction of desired changes (at the national level) it is almost impossible or very long.

The proposal may work for large countries with manufacturing industries, but it is certainly not good for small countries with an open economy such as the Netherlands".

The Irish are also among the major losers of the new rules: "The CCCTB has the potential to lose significant case law and expertise in tax administration, and the introduction of a completely new tax system has the potential to complicate a tax environment considered transparent and accessible in Ireland".(ART. 227)

In the short term, however, a single EU-wide tax of 3% would appear to be imposed on gross revenues from major Internet platforms, based on where users are located under a project from the European Commission seen by Bloomberg at the end of the week.

The details are not clear, it is only said that they will apply to groups that have global revenues of more than EUR 750 million and chargeable digital service revenues of more than EUR 50 million in the EU. However, the temporary version (until the CCCTB comes into force) will be presented on Wednesday 21 March, as announced during the debates in Strasbourg, Commissioner Moscovici.

Initially, the calculation formula (CCCTB algorithm) provided for allocation by three factors, taken in equal proportions, 1/3 – work (a factor divided equally between wages and number of employees), (tangible) assets, and sales by destination.

Subsequently, against the background of discussions on a practical way of taxing the digital economy, the EP's ECON Committee also proposed the introduction of a fourth factor, also equal to the other three – the data factor, expressing the collection and use of personal data by online platforms and service users. It should be noted that, according to the amendments, a factor can be eliminated if it does not fit into the business model while maintaining the principle of equal shares for the relevant factors.

4. Conclusions

Transfer prices are the link between tax regulations in different national and European markets and a group using tax zones can pay high transfer prices to its subsidiary, in a normal tax country, by increasing its profits at the tax point and reducing them in normal tax countries.

According to the law, no specific formal documentation on transfer pricing is required. However, in practice, authorities can request documentation on a case-by-case basis. Also, taxpayers are required to complete an annual statement of payments to foreign natural and legal persons, except for amounts related to the import of goods and international transport.

Transfer pricing legislation in its current form is quite complete, so we no longer expect any significant changes.

Ideally, the legislator could provide some clarifications/clarifications on the (non-) obligation of affiliated persons resident in Romania to document transactions between them.

The definition of a minimum threshold for the volume of intra-group transactions between related persons for which the transfer pricing file does not need to be drawn up would also be a positive initiative from the tax authorities. Moreover, to assist taxpayers, the authorities could issue a practical transfer pricing guide.

We can say that in the current context of the nationalization of business, transfer prices are aroused by the tax authorities, which are the main area investigated by them in the context of tax controls.

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Art. 19 (5) of the Fiscal Code states: “Transactions between affiliates are carried out according to the principle of the free market price, according to which transactions between affiliates are carried out under established or imposed conditions that must not differ from commercial or financial relations established between enterprises independent. When establishing the profits of the affiliated persons, the principles regarding the transfer prices are taken into account. "
2 Art. 79 (2) of the Fiscal Procedure Code mentions: “In order to establish transfer prices, taxpayers who carry out transactions with affiliated persons have the obligation that, at the request of the competent fiscal body, to prepare and submit, within the deadlines established by it. , transfer pricing file. The content of the transfer pricing file will be approved by order of the president of the National Agency for Fiscal Administration.
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