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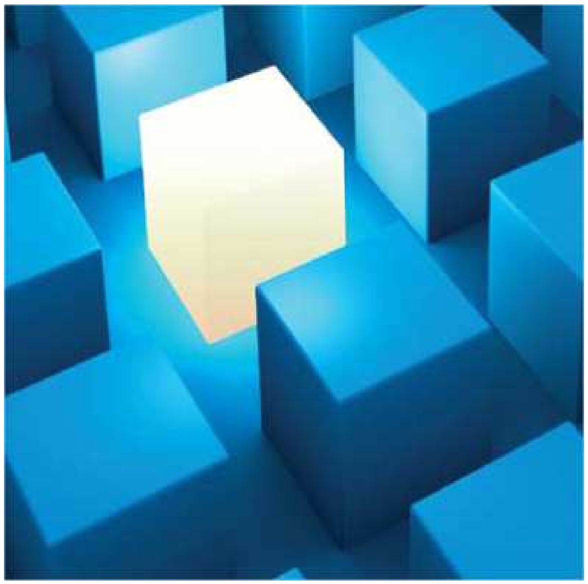

OECD – Public Consultation on Transfer Pricing Matters – *Value Chain Analysis and Profit Split in the context of BEPS*

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Fifteen Years of One-Sided Transfer Pricing

Relational Arm's Length Transfer Pricing

- Historically, the analysis of compliance with the arm's-length principle is *transaction*-based. Over time, *entity-based outcome* comparisons with industry benchmarks have been introduced as the primary testing method for arm's length character. The arm's-length principle itself, however, refers to commercial and financial relations between entities within a group

- *Relational Arm's Length Transfer Pricing* defines arm's length transfer prices that are consistent with both tax and business objectives. The focus is shifted from testing stand-alone entities (the "tested parties") to **mapping the relative position of group entities involved in the process of jointly creating value**

- Key features of this approach are as follows:
  1. Determine **industry value drivers**
  2. Undertake detailed factual analysis of the company and its business model, including a **value chain analysis**
  3. Identify transactions, legal and operational structure and define the **responsibility profiles** of the group entities concerned

Value Chain Analysis and Roles and Responsibilities

- **Value Chain Analysis**: understand, in addition to an analysis of functions, how value is created in the Enterprise
  - Identify the key value drivers as part of a company's value chain which influence the most the **Critical Success Factors** of the Enterprise within its industry
  - Identify the key value drivers in the value chain which can be held accountable for the Enterprise's **major risks** within its industry and its chosen business model
- **Responsibility Centers**: define roles of the entities in the joint value creation and responsibilities in respect of the different value drivers and related risks

Link between Value Chain Analysis and Profit Splits

- **Value Chain Analysis** is a tool for a qualitative assessment of steps in a company's value creation and can serve as a framework for identifying bargaining positions of entities involved therein
  - It helps the selection and application of the most appropriate transfer pricing methods for the case at hand, including the Profit Split Method when appropriate
- When the **Profit Split Method** is applicable, it should find its origin and justification in the Value Chain Analysis
  - Application of the Profit Split Method should rely on solid economic analyses (analysis of external long-term relationships, investment-based models, game theory, compensation-based models, surveys, etc.)

Conclusion

What should the BEPS project consider in connection with global value chains and profit split approaches?

- Broaden the transaction and entity-outcome-based implementation focus towards a relationship-based interpretation of the arm's length principle
- To that end, revise Chapters I – III of the Guidelines so as to cover the definition of value, define and describe the concept of value creation, and introduce the perspective of value chain analysis
- Assess the relative bargaining positions of parties (whether or not related) vis-à-vis their long-term, cooperative relationship and their respective contributions to joint value creation
- Recognize the limits of one-sided-only TP analyses; profit split can serve both as a primary price-setting method and as a complement to other methods, testing the case-specific relevance of outcomes

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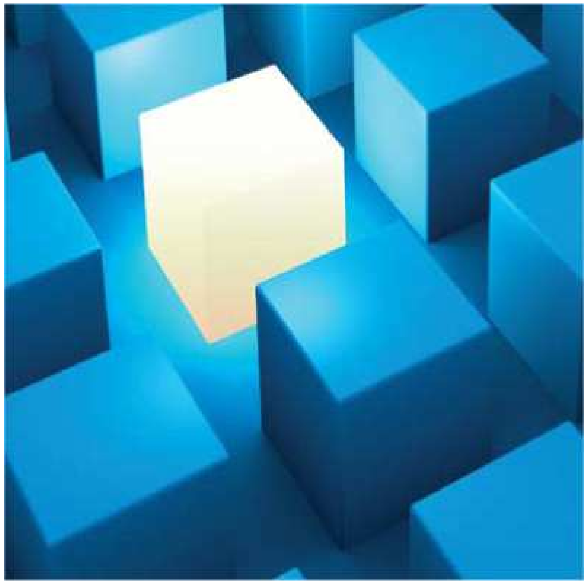

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