

TRANSFER PRICING FORUM

Transfer Pricing for the International Practitioner



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Issue One

To what extent has your tax authority indicated that it would make use of the full list of information that is required by the template in transfer pricing risk assessments? To what extent is it already asking for and making use of this information?

Since the publication of the OECD's Discussion Draft on Transfer Pricing Documentation and Country-by-country reporting ("OECD Discussion Draft") on January 30, 2014, the French tax authorities ("FTA") have not made any comments.

As of January 1, 2010, section L. 13 AA of the French tax procedure code ("FTPC") provides that a specific transfer pricing documentation must be prepared by entities meeting certain thresholds and be provided to the FTA in the course of a tax audit. In 2014, a new transfer pricing documentation requirement was implemented.^{1,2}

The current French requirements are compliant with the OECD Transfer Pricing Guidelines and similar to the structure recommended by the European Union Code of Conduct of 2008. Companies have to prepare two categories of information on their transfer pricing policy (general information on associated companies and specific information on the audited company).

However, the French documentation model is of general nature and the FTA do not provide much guidance in how to prepare it. The FTA specify that the level of details required about each entity will depend on both its place within the group structure (distinguishing between parent and subsidiary level) and its contribution to the group activity, as well on the weight to be assumed by its functions and assets in the determination of transfer pricing policy³ ("FTA Guidelines"). As a result, the documentation requirements proposed by the OECD Discussion Draft is more extensive than the current list of information required under section L. 13 AA of the FTCP and section 223 *quinquies* B of the FTC. However, in practice, even if certain elements of the OECD guidelines are not directly mentioned, these elements should be provided as the FTA usually follow the OECD guidelines. Therefore, we can anticipate that once the final version of the OECD Discussion Draft will be published, the FTA will include all or part of the information that is required by the template.

Issue Two

To what extent have your local tax authority or your local courts shown a willingness or preference to use the Profit Split Method?

French transfer pricing rules do not provide specific input with respect to the choice of the most appropriate transfer pricing method. The FTA recognise the same methods as the OECD and consider that any method applied by a company can be relevant provided that it is justified, consistent with the functions performed and risks assumed. According to the FTA Guidelines, the method chosen must also satisfy the arm's length principle.

The FTA specified that the profit split method can be used when projects or activities within the group are common and interrelated and it is not possible to determine or justify a valuation for each operation. This method could also be implemented when both companies hold valuable intangible assets and where it is therefore difficult to use a traditional method.⁴

However, the FTA Guidelines specifically indicate that the profit split method is a "last resort" method. In the view of the FTA, traditional methods are the most direct and reliable methods to be compliant with the arm's length principle and transactional methods should only be used when no data is available. In practice, the transactional net margin method is used quite often by the FTA.

French transfer pricing case law, which is rare, generally does not adopt a "best method approach". French judges are focused on the justification of the method used by both the FTA and the taxpayer with respect to the arm's length principle and would very rarely ever try to use or refer to an alternative method. Only one court decision can be referred to by looking at the profit split method used by the FTA. In the *Novartis Groupe France SA*⁵ case law, the FTA intended to use a profit split approach. The FTA used assumptions to build consolidated profits for cross-border operations and assessed a tentative arm's length split of those consolidated profits. The court notably criticised the fact that the FTA did not perform a comparable search and the approach was not considered as sufficiently documented to demonstrate a transfer of profits.⁶

To conclude, neither the FTA nor the French courts have shown a willingness to use the profit split method and on the contrary, this method still appears to be a "last resort" method.

Issue Three

To what extent have your tax authority or your local courts been prepared to adopt a global formulary apportionment of profit as opposed to following the arm's length principle set forth in Article 9 of the OECD Model Tax Convention?

FTA and French judges are currently focused on the respect of the arm's length principle in line with the OECD principles. Considering this current practice, we have no example of a global formulary apportionment of profit at this stage.

However, the global formulary apportionment of profit principle was addressed in a recent FTA report where it is stated that this principle is still fairly theoretical and will not resolve the transfer pricing issues. It is also specified that France supports the European Commission's Common Consolidated Corporate Tax Base aiming at implementing a global formulary apportionment of profit approach.⁷

The global formulary apportionment of profits proposed in the European Commission's Common Consolidated Tax Base proposition is currently in a draft stage and we are far from having clear rules in order for the FTA or the judge to use this method.

However, considering the position expressed in the report mentioned previously, the FTA is open to discussion regarding the implementation of a global formulary apportionment of profit approach.

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NOTES

¹ We previously discussed the information requested for French documentation in Bloomberg BNA's *Transfer Pricing International Journal*, Volume 15, Number 1, January 2014.

² Section 223 quinquies B of the French tax code, or "FTC".

³ Administrative guideline BOI-BIC-BASE-80-10-20.

⁴ *Transfer Pricing Guide from small and mid-size enterprises* – Direction Générale des Impôts, November 2006.

⁵ *Novartis Groupe France SA*, Administrative court of Appeal of Paris, June 25, 2008.

⁶ The exact method used by the taxpayer was not indicated in the court decision.

⁷ *French Finance and Budget committee report on Companies' tax optimisation in an international context*, dated July 10, 2013.