Winter Meeting of Geneva Group International Taxation Practice Group (ITPG)
Marbella, Spain
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GGi
INDEPENDENT MEMBER

"Case Study"

Saturday, February 21, 2015

presented by Klaus KÜSPERT
MUNKERT & PARTNER GbR, Nuremberg, Germany

MUNKERT & PARTNER
Steuerberater Wirtschaftsprüfer Rechtsanwälte GbR

Panel members

Panel members:

- Oliver Biernat, DE
- Dr. Sergio Finulli, IT
- Viviane Moro, FR
- Carlos Frühbeck, ES
- Artur Plutowski, PL
- Julie Bryant, UK
- Brian Marita, US

Agenda

1. Current status of T-group

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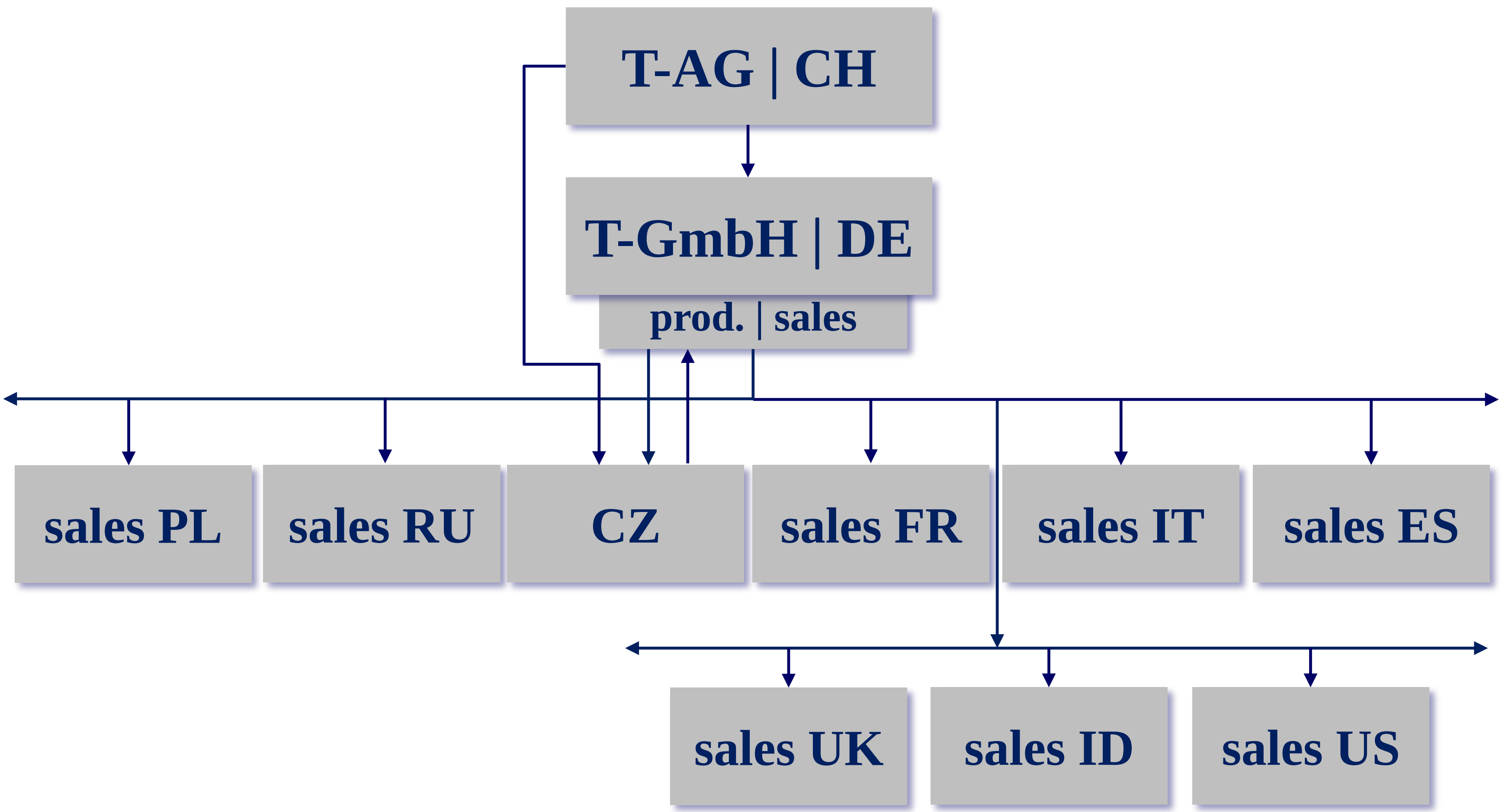

2. Step 1 of restructuring T-group

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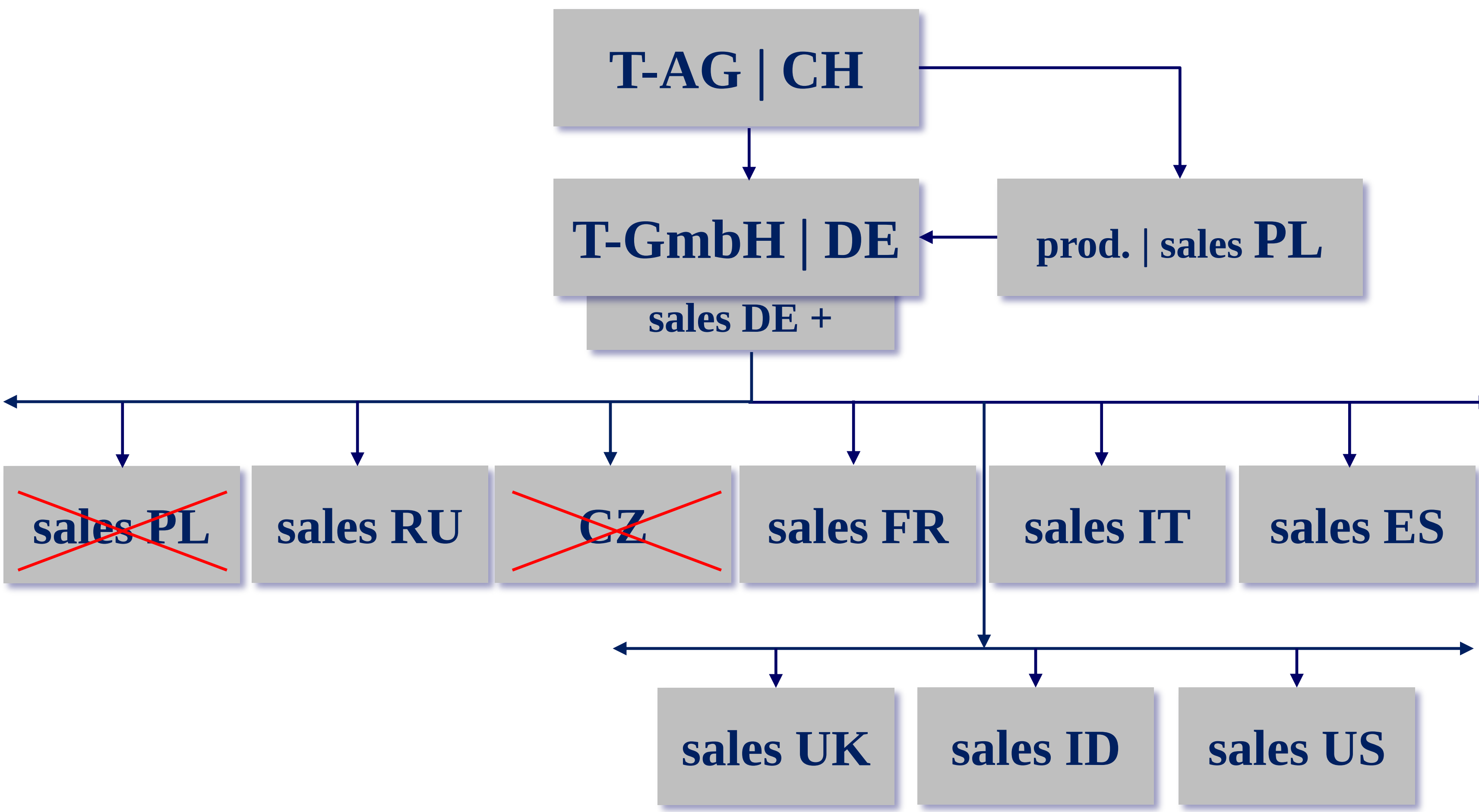
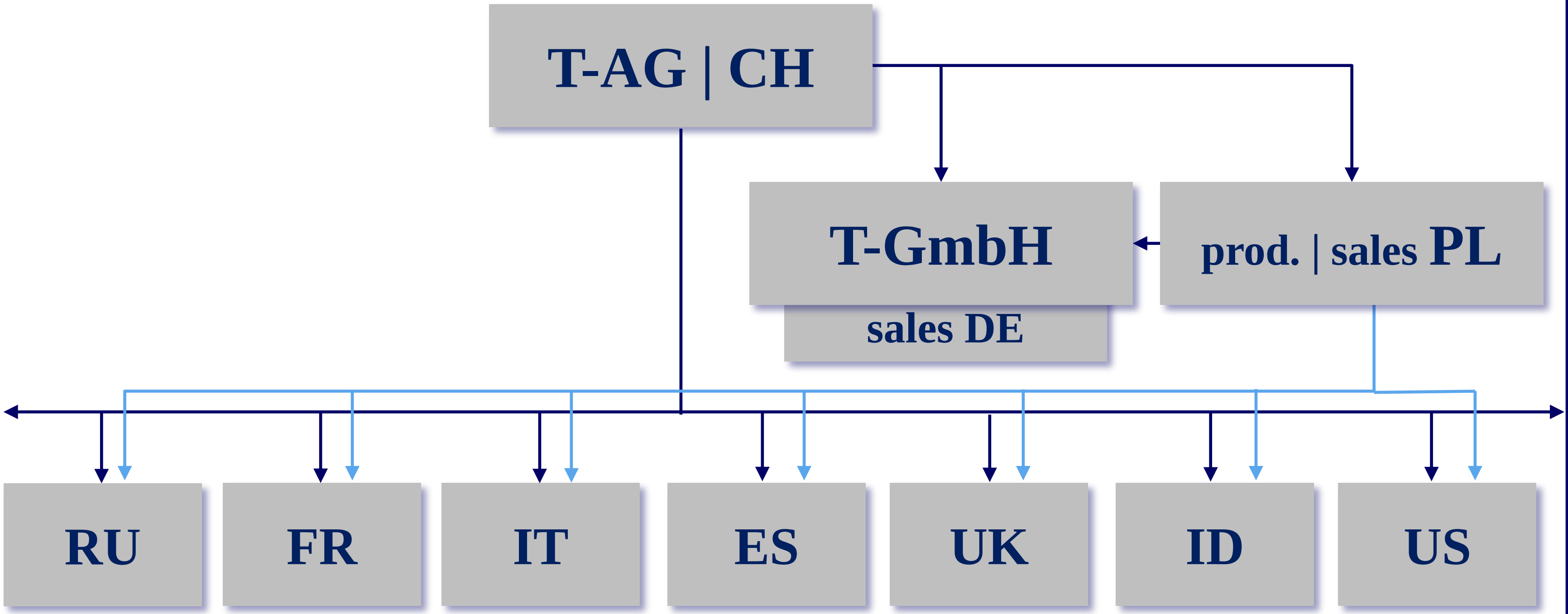


3. Step 2 of restructuring T-group



➡ Statements of panel members

4. Documentation

A) Documentation of facts

- description of group structure
- business concept, product policy, market situation
- details of intercompany relations
- immaterial goods used
- extraordinary items
- analysis of risks and functions for individual group members
- added value and value chain

4. Documentation

B) Arm´s length documentation

- Use of methods
  - comparable unrelated price method (CUP)
  - resale price method
  - cost-plus
  - transaction net margin method (TNMM)
  - profit split
  - residual profit split between strategic partners
- Pricing tests
  - dates analysis
  - use of comparable
  - Proof of appropriateness

➡ discussion of panel ❶

5. Intercompany relations in current status

A) T-GmbH uses sub in CZ as workbench Materials, machinery etc. belong to T-GmbH. CZ uses own premises. Services of CZ to T-GmbH are rendered at cost-plus with a profit mark-up of 10 %. Is this appropriate?

B) T-AG has engineering and consulting capacity. It charges CZ with daily rates of 1.500 € per person for special services regarding the production line of T-GmbH handled by CZ. Is this appropriate?

5. Intercompany relations in current status

C) T-GmbH delivers its goods to all subs acting as sales force.

With the exception of FR the sales subs have the function of independent, but licensed (franchise) dealers. Product risks are borne by T-GmbH, all other risks by the subs.

In case of France, sub bears all risks as it has an alternative product line licensed by a third party.

5. Intercompany relations in current status

a) Functions and risks of distributors determine intercompany pricing:
- the more risks are borne by distributor the lower the margin payable to parent
- adjustable net margins as basis appropriate?
- resale price method acceptable?
- TNMM? Benchmark of tested party?

b) Examples to C) in case of FR:

		alternative
resale price	100 €	100 €
gross margin	50 €	70 €
net	50 €	30 €
cost	30 €	20 €
net/net	20 €	10 €

5. Intercompany relations in current status

Examples to C), if distributor is agent:

▸ gross margin	50 €	70 €
▸ cost plus 10 %	33 €	22 €
▸ net margin	17 €	48 €

c) What happens to tax adjustments made in DE on margins to subs in jurisdiction of subs? Corresponding adjustments available?

➡ discussion of panel ❷

6. Step 1 of restructuring and intercompany pricing

A) Shares of PL are shifted to T-AG, CH
Production of T-GmbH is shifted from DE/CZ to PL

- machinery is partly relocated in PL
- part of machinery is still owned by DE
- closing cost in DE amount to 1,0 Mio. €
- intangibles and brand name are owned by DE
- PL sells all products to DE as main distributor

6. Step 1 of restructuring and intercompany pricing

B)

a) Is transfer of production considered as a deemed asset deal? If yes, which assets are involved and how are they valued?

b) DE approach considers the transaction to PL as overall transfer of the product function of DE at market value (so called transfer package); approach is basically in line with OECD model

c) If no significant intangibles are transferred, does valuation include market value of assets but no goodwill?

6. Step 1 of restructuring and intercompany pricing

C)

		alternative
appraisal in DE for value of production function = minimum pricing	10 Mio. €	14 Mio. €
appraisal in PL for value of production function = maximum pricing	12 Mio. €	12 Mio. €
➡ range of pricing	2 Mio. €	2 Mio. €
➡ intercompany price DE	11 Mio. € ?	14 Mio. € ?

➡ which profit is allocated to production and sales?

6. Step 1 of restructuring and intercompany pricing

D) Would PL accept a tax base of 11 Mio. € or 14 Mio. €? If yes, how would this tax base allocated and depreciated? Which is the normal depreciation of goodwill for tax purposes?

E) Example C) above:

		alternative
➡ German tax (corporate) 30 % on deemed price	3,3 Mio. €	4,6 Mio. €

6. Step 1 of restructuring and intercompany pricing

- marginal tax rate difference (assumed) DE/PL = 10 %
- DE has pre-tax profit of 2,5 Mio. €
  after-tax profit 1,75 Mio. €

- PL has pre-tax profit 2,5 Mio. €
  after-tax profit 2,0 Mio. €
  tax saving 0,5 Mio. €

- Up-front payment in DE 3,3 Mio. € - 4,6 Mio. €
- full-tax saving after year 8 - 10?
- effect of corresponding depreciation base?
- discussion of panel ❸

7. Step 2 of restructuring and intercompany pricing

A) Shares of foreign subs are shifted to T-AG/CH
Sales function of DE is cut down to distribution in DE

➡ German approach assumes that the downgrading of sales functions may constitute a “sale” of a regular customer base

➡ If foreign subs may give notice to DE on a regular basis and customer base is not owned by DE, a shifting of function does not take place?

7. Step 2 of restructuring and intercompany pricing

B)

➡ German approach to a sale of stock within a group means either taxation of a hidden profit distribution or an adjustment of prices

7. Step 2 of restructuring and intercompany pricing

C)

Ebit of subs	2 Mio. €
Earnings after tax	1,6 Mio. €
Multiple 5	8 Mio. €
DE tax on transaction	2,4 Mio. €

Amortization of adjustment to stock value is not available

➡ discussion of panel ❹

8. Conclusion

- **Germany applies the OECD approach on most intercompany transactions**
- **Germany is fixed on documentation rules and burden of prove regulations**
- **tax payer may use any of the available intercompany pricing methods to comparable transactions, if testable**
- **Germany has excessive rules on the deemed shifting of functions as part of avoiding base erosion**
- **problems in valuations of the same assets and objectives in different jurisdictions are inevitable**

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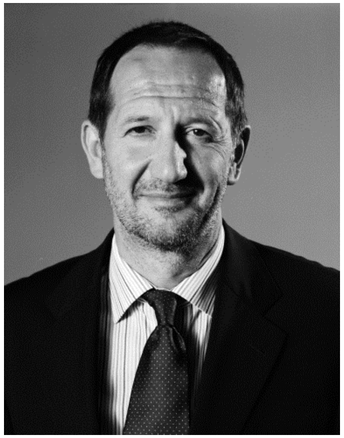
8. Conclusion

- corresponding adjustments are difficult
- a lift of the tax base in foreign countries after a deemed transaction is not realistic
- a shifting of transactions should be underlined by appraisals and a real process to create tax base as far as possible
- the tax rates in the EC may vary from time to time in that tax savings from shifting companies or functions are uncertain
- Tax savings have to be located at on a long run

➡ **Final statements of panel members**

- Final remarks

Contact



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