European Parliament seeks faster adoption of harmonised transfer pricing rules 3/15/24


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On 22 February 2024 the European Parliament Committee on Economic and Monetary Affairs (ECON) published a draft report that includes proposals for a transfer pricing (TP) directive drafted by the European Commission. The ECON draft report generally supports the Commission's proposal to align the TP requirements across the EU, yet it recommends a number of crucial amendments. This article explores the ECON amendments that could affect Latvian TP requirements, too.

An overview

The TP directive mainly aims to:

- Enhance tax certainty
- Reduce costs incurred in preparing TP files
- Minimise the risk of double taxation

The member states enjoy wide latitude in interpreting and applying recommendations made by the OECD TP guidelines, which create tax obstacles and risks for businesses. The TP directive has another key objective:

- Align the TP requirements by including the definition of an arm's length range in EU law and describing the role of the OECD TP guidelines.

While ECON generally agrees with the draft TP directive, it proposes to make specific amendments to the TP directive, which could affect the requirements for preparing TP files.

A dynamic reference to the OECD TP guidelines

The ECON draft report proposes to simplify the TP directive and align it more closely with the latest TP guidelines, instead of referring to the version of 2022, as prescribed by the TP directive. In particular, the draft report proposes to:

- Remove clauses relating to the definition of related parties
- Delete the descriptions of TP methods and the selection criteria on the grounds that those are not sufficiently precise and justified

ECON has said the unilateral methods (e.g. Resale Price, Cost Plus, and Transactional Net Margin) are not considered reliable where each party makes a unique and valuable contribution to the transaction or if the parties carry out very integrated activities. The Profit Split method would be best suited for this case because independent parties would possibly price the transaction in proportion to their contributions.

ECON also recommends deleting the definition of an arm's length range, which provides for a comparatively strict approach to determining this range from the bottom quartile to the top quartile.

To ensure the TP directive is able to stay compliant and change with the times, ECON recommends making a dynamic reference so the definitions (e.g. of unrelated parties, of an arm's length range, and of TP methods) are applied across the EU according to the latest version of the OECD TP guidelines.

The effective date of the TP directive

The ECON draft report recommends the TP directive should take effect from 1 January 2025. The member states are to pass it into their national laws by 31 December 2024, a year earlier than what the Commission proposed.

A sunset clause

The ECON draft report includes a sunset clause that provides for phasing out the TP directive by 1 January 2035 for multinational enterprise (MNE) groups covered by BEFIT[1] and by 1 January 2040 for the rest of MNE groups operating in the EU, except for transactions with related parties in third countries. In this regard the draft report states that the long-term distribution of profits and payment of taxes between jurisdictions should be made by introducing calculation-based group consolidations and profit distributions to apportion profits between countries fairly and recognise the reality of MNE operations.

The ECON draft report has been put to a vote representing the European Parliament's opinion on the TP directive (a plenary session scheduled for 10 April 2024). It's important to note, however, that the European Parliament's opinion does not bind the EU Council, i.e. the 27 member states will have to agree on the TP directive's final version.

[1] Council Directive on Business in Europe: Framework for Income Taxation