Mexico City, January 13, 2015

Via e-mail
transferpricing@oecd.org
Mr. Andrew Hickman
Head of Transfer Pricing unit
Centre for Tax Policy and Administration

Dear Mr. Hickman,

On behalf of IFA Grupo Mexicano, A.C. (Mexican Branch of the International Fiscal Association) kindly find below the comments to the Public Discussion Draft on Action 10 of the BEPS Action Plan – "*Proposed Modifications to Chapter VII of the Transfer Pricing Guidelines Relating to Low Value-Adding Intra-Group Services*" (the "Draft").

1) Comments to paragraph 7.9

> *7.9 Some intra-group services are performed by one member of an MNE group to meet an identified need of one or more specific members of the group. In such case, it is relatively straightforward to determine whether a service has been provided. Ordinarily an independent enterprise in comparable circumstances would have satisfied the identified need either by performing the activity in-house or by having the activity performed by a third party. Thus, in such a case, an intra-group service ordinarily would be found to exist. For example, an intra-group service would normally be found where an associated enterprise repairs equipment used in manufacturing by another member of the MNE group."*

Paragraph 7.9 provides as a general principle that in order to consider that the intra-group service has been rendered, it is necessary to analyze whether an independent third party would have been willing to pay for such service and it is not possible in the abstract to set forth categorically the activities that do or do not constitute the rendering of intra-group services.

In specific, paragraph 7.9 establishes that an intra-group service is rendered when an independent enterprise in a comparable circumstance is willing to perform the service in-house or by having the activity performed by a third party.

In this sense, it is important to mention that in such cases some intra-group services may be difficult to prove its effective render under this basis, due to the fact that some services that are rendered between related parties may be unique and no independent party will be willing to perform them in-house or by having evidence that a third party is performing them.

In relation with the abovementioned, paragraph 1.11 of the OECD Transfer Pricing Guidelines establishes the following:

> *1.11 A practical difficulty in applying the arm's length principle is that associated enterprises may engage in transactions that independent enterprises would not undertake. Such transactions may not necessarily be motivated by tax avoidance but may occur because in transacting business with each other, members of an MNE group face different commercial circumstances than would independent enterprises. Where independent enterprises seldom undertake transactions of the type entered into by associated enterprises, the arm's length principle is difficult to apply because there is little or no direct evidence of what conditions would have been established by independent enterprises. The mere fact that a transaction may not be found between independent parties does not of itself mean that it is not arm's length.*

We suggest to clearly establish in the document that the tax administrations must presume, except if there is proof on the contrary, (i) that the service or activity has effectively been rendered and (ii) that said activity or service that has been paid for, provides economic or commercial value to enhance or maintain its commercial position in a general and broad sense.

In addition to this presumption (principle) in favor of the taxpayer, the administrations must apply this interpretation so that this fundamental principle is not deteriorated. That is, the document must clearly include a wording in favor of the previously indicated principle because if it is not applied as indicated in the Guidelines or tax authorities include specific exceptions, it will be impossible in certain tax jurisdictions to record a deductible expense for intra-group services that were truly rendered if the compensation was establish by using an indirect-charge method or "pro-ratio" due to the nature of the service being provided and the costs and expenses incurred in the rendition of said service.

2) Comments to paragraph 7.14

> *7.14 Similarly, an associated enterprise should not be considered to receive an intra-group service when it obtains incidental benefits attributable solely to its being part of a larger concern, and not to any specific activity being performed. For example, no service would be received where an associated enterprise by reason of its affiliation alone has a credit-rating higher than it would if it were unaffiliated, but an intra-group service would usually exist where the higher credit rating were due to a guarantee by another group member, or where the enterprise benefitted from the group's reputation deriving from global marketing and public relations campaigns. In this respect, passive association should be distinguished from active promotion of the MNE group's attributes that positively enhances the profit-making*

potential of particular members of the group. Each case must be determined according to its own facts and circumstances.

Paragraph 7.14 provides as a general rule that an associated enterprise should not be considered to receive an intra-group service when an incidental benefit attributable solely to its being part of a large concern, and not to any specific activity being performed, is obtained.

It continues by mentioning an example where an intra-group service is rendered when an enterprise is benefitted from the group's reputation deriving from global marketing and public relations campaigns.

In this sense, the incidental benefit that an enterprise might obtain by its solely association with a certain group should not be considered as an intra-group service. Any royalty payments or marketing expenses incurred by the affiliates should be analyzed as separate related party transactions.

As paragraph 7.9 establishes, passive association should be distinguished from active promotion of the MNE group's attributes that positively enhances the profit-making potential of particular members of the group, as well as the fact that each case must be determined according to its own facts and circumstances.

Therefore, we suggest OECD reviewing this example as an incidental benefit or clarifying the context of such case.

3) Comments to paragraph 7.16

7.16 In considering whether a charge for the provision of services would be made between independent enterprises, it would also be relevant to consider the form that an arm's length consideration would take had the transaction occurred between independent enterprises dealing at arm's length. For example, in respect of financial services such as loans, foreign exchange and hedging, all of the remuneration may be built into the spread and it would not be appropriate to expect a further service fee to be charged if such were the case. Similarly, in some buying or procurement services a commission element may be incorporated in the price of the product or services procured, and a separate service fee may not be appropriate.

Paragraph 7.16 provides that it would be relevant to consider the form that remuneration is established between independent parties in order to assure the arm's length nature of the remuneration that associated parties should establish for the provision of services

It continues by mentioning an example where the building of the remuneration in the provision of financial services and buying or procurement

services should be based on the form that remunerations established between independent parties is built.

In this sense, independent parties may engage in transactions that establish different ways of remunerations from the transactions carried out between associated parties. Such cases may respond to different economic circumstances that might drive the entities to follow certain way of remuneration or another.

Specifically for purchases or procurement services, related parties may determine the consideration as incorporated in the price of the products or as a service commission, as applicable. Therefore, we suggest adjusting the example, or clarify that the remuneration that associated enterprises might establish for the provision of services must be determined according to its own facts and circumstances.

4) Comments to paragraph 7.31

7.31 In trying to determine the arm's length price in relation to intra-group services, the matter should be considered both from the perspective of the service provider and from the perspective of the recipient of the service. In this respect, relevant considerations include the value of the service to the recipient and how much a comparable independent enterprise would be prepared to pay for that service in comparable circumstances, as well as the costs to the service provider.

Paragraph 7.31 provides that the analysis of the arm's length compensation must consider the perspective of the service provider and the perspective of the recipient of the service, as well as some other relevant considerations that include the value of the service to the recipient and the costs of the service provider.

In transactions between independent parties it is not possible to have information from both, the service provider and the recipient so this kind of information should not be mandatory for testing related party transactions. Also, in general it is very difficult for affiliates to obtain information from the related service provider.

Thus, recommendation to access service provider information could probably be limited to past-through costs only where CUP methodology is used to prove compliance with arm's length principle.

Of course, affiliates should be encouraged to make their best efforts to request and obtain the information but the effective obtaining of all foreign information the tax authorities may request to the taxpayer should not be a requirement for the deduction of the service.

It is important to consider that more often than not service providers might consider for their billing process cost pools comprised of (i) actual figures corresponding to expenses incurred from X to Y months and (ii) estimated figures for the last months of the year. Authorities need to consider that true-ups might be done in future periods and be flexible when reviewing the information used by the service provider for its billing process. In other words, it is important to encourage tax administrations to consider estimated figures as valid when reasonable or proven close to actual or final ones.

Therefore, we suggest that in order to calculate an arm's length consideration for the services provision between associated entities, applicable transfer pricing methods should be considered, and any specific information to be requested by the tax authorities related to a foreign based related party should be requested through the applicable procedures for exchange of information between competent authorities.

Additionally it is our opinion that alternative approaches could be explored in terms of (i) agreed consideration between related parties (i.e agree on a fixed fee as third parties may in some cases do, rather than entering into the complexity of allocating costs and determining the most appropriate allocation key which could likely be subject to several interpretations on appropriateness) and; thus, (ii) documenting compliance with arm's length principle potentially considering the service recipient's perspective as tested party by testing its results, with the overall results of similar enterprises in comparable conditions.

5) Comments to Section D. Low value-adding intra-group services

We do believe the information included in the Action 10 of the BEPS Action Plan –"*Proposed Modifications to Chapter VII of the Transfer Pricing Guidelines Relating to Low Value-Adding Intra-Group Services*" regarding low value –adding intra-group services is focused to try to simplify the administrative burden and analysis of some kind of related party services, although at this stage the guidelines are complicated for its application since all the information mentioned therein is not fully available or at hand for affiliates of the MNE's.

Regarding the simplified determination of arm's length charges for low value-adding intra-group services section, such section sets out the elements of a simplified charge mechanism for low value-adding intra-group services. Such simplified method has to be applied on a consistent, group wide basis in all countries in which the company operates.

In this sense, the requirements that the document establish in order to follow the simplified method are excessive and unduly onerous, which transform the methodology into a complicated one rather than to simplify it.

Also, the documentation does not provide a plenty identification of the services considered as low value-adding intra-group services for which the mark-up within the 2% to 5% range should be applied. This is, it could be worth including a “white” list and a “black” list of services that could be used or not for the 2% to 5% safe harbour of net cost plus mark-up.

This simplification should qualify to the kind of service engaged by the related parties. Allocation of costs or cost sharing agreements should be analyzed separately under general guidelines also included in Chapter VII.

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The participation of IFA Grupo Mexicano, A.C. is made on its own behalf exclusively as an IFA Branch, and in no case in name or on behalf of Central IFA or IFA as a whole.

We hope you find these comments interesting and useful. We remain yours for any questions or comments you may have.

Sincerely,

IFA Grupo Mexicano A.C.