

## Session Topic

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- Intra Group Services
- Transfer Pricing Documentation

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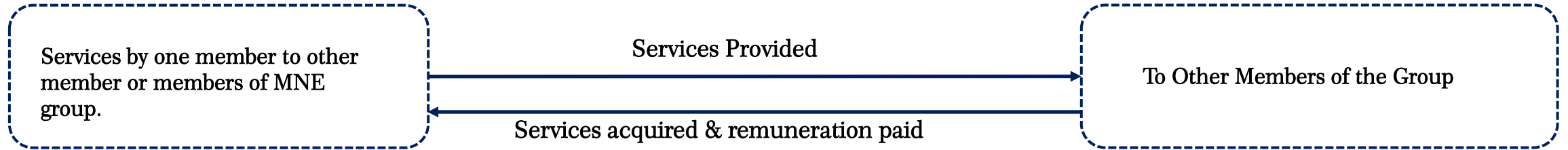
CA. Rishabh Agarwal



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# Intra Group Services

# Intra-Group Services (1/3)



The main issues for transfer pricing purposes are:

1. whether **services have been provided** by one member of an MNE group to other members of that group
2. and, if so, in **establishing arm's length pricing** for those intra-group services

Q. Determining whether chargeable services have been provided or not?

A. Depends on **whether the activity provides a respective group member with economic or commercial value to enhance or maintain its business position.**



**Determining Arm's Length Price**


1. Cost-recharge Types
2. TP Methods
3. Other considerations


# Intra-Group Services (2/3)

Intra-group services refer to the provision of various services within a multinational group of companies, often across different nations and jurisdictions, it involves:



## Most prevalent Intra-Group Services

Strategic and Management Services 


Accounting and Auditing 

IT Support Services 

Engineering Services 

Finance, Legal And Tax Related 

Administrative Support Services 

Laboratory and technical assistance 

HR Support Services 

Procurement & Assembly Support Services 

# Intra-Group Services (3/3)

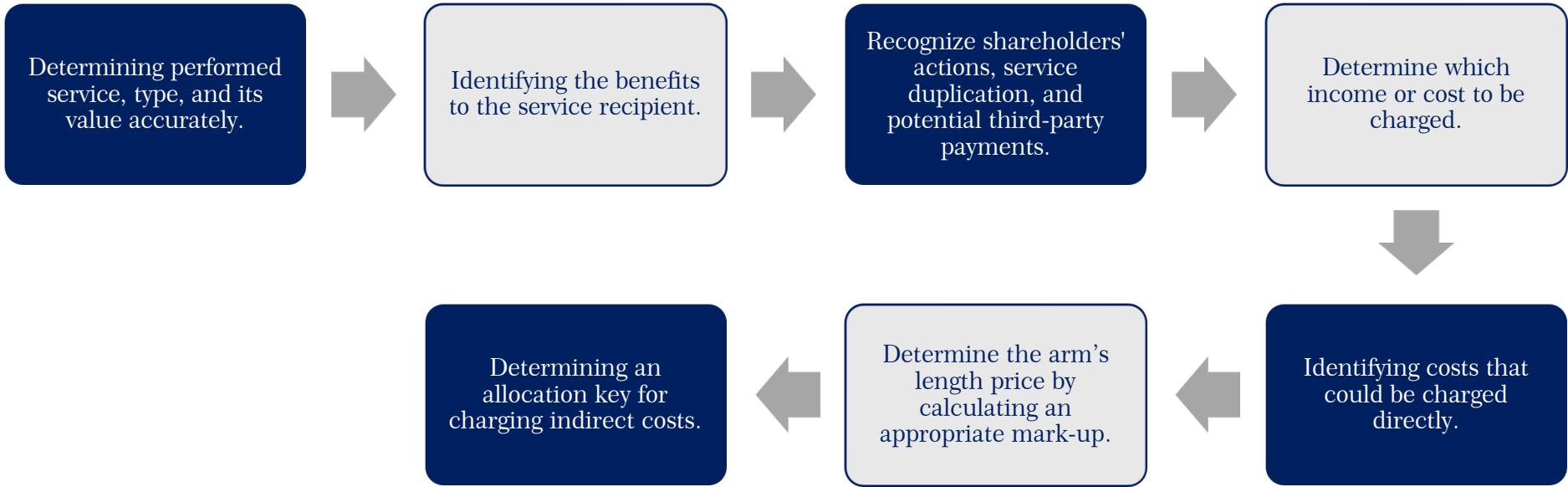
## Excluded from Intra-Group Services

Shareholder Activities 

Duplication 

Incidental Benefits 

## TP Steps to be adopted when dealing with Intra Group services



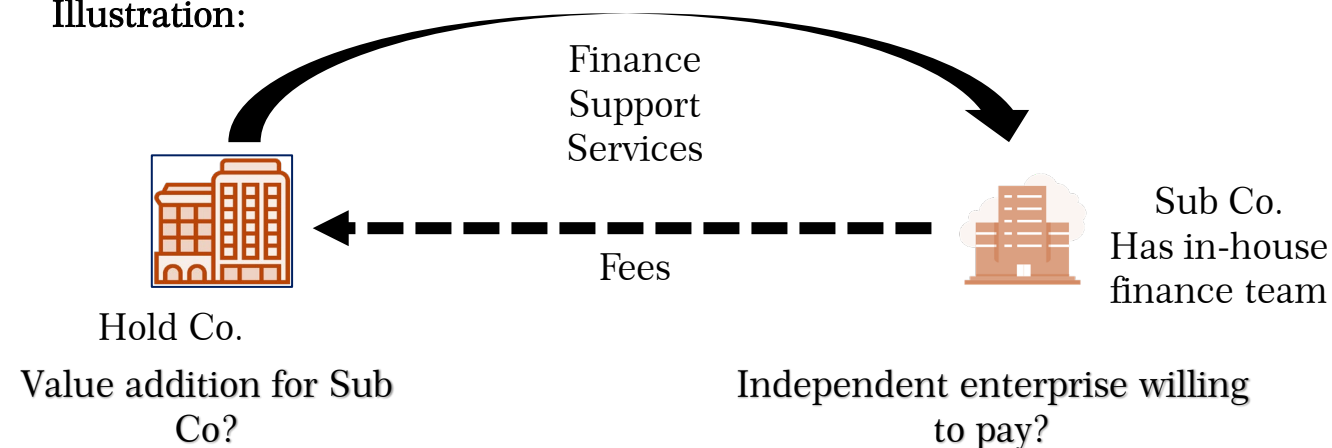
# Benefit Test

Under the **arm's length principle**, the question of whether an intra-group **Service has been rendered** when an activity is performed for one or more Group members by another group member should depend on **whether the activity provides a respective group member with economic or commercial value to enhance or maintain its business position.**

This could be determined by considering whether an **independent enterprise** would be **willing to pay** for such services or **would have performed** the activity **in-house** for itself.

If services **are not** the ones for which the **independent enterprise** would be **willing to pay or perform for itself**, then there might not be any economic and commercial benefits, and hence should **not be considered as an intra-group service** under arm's length principle

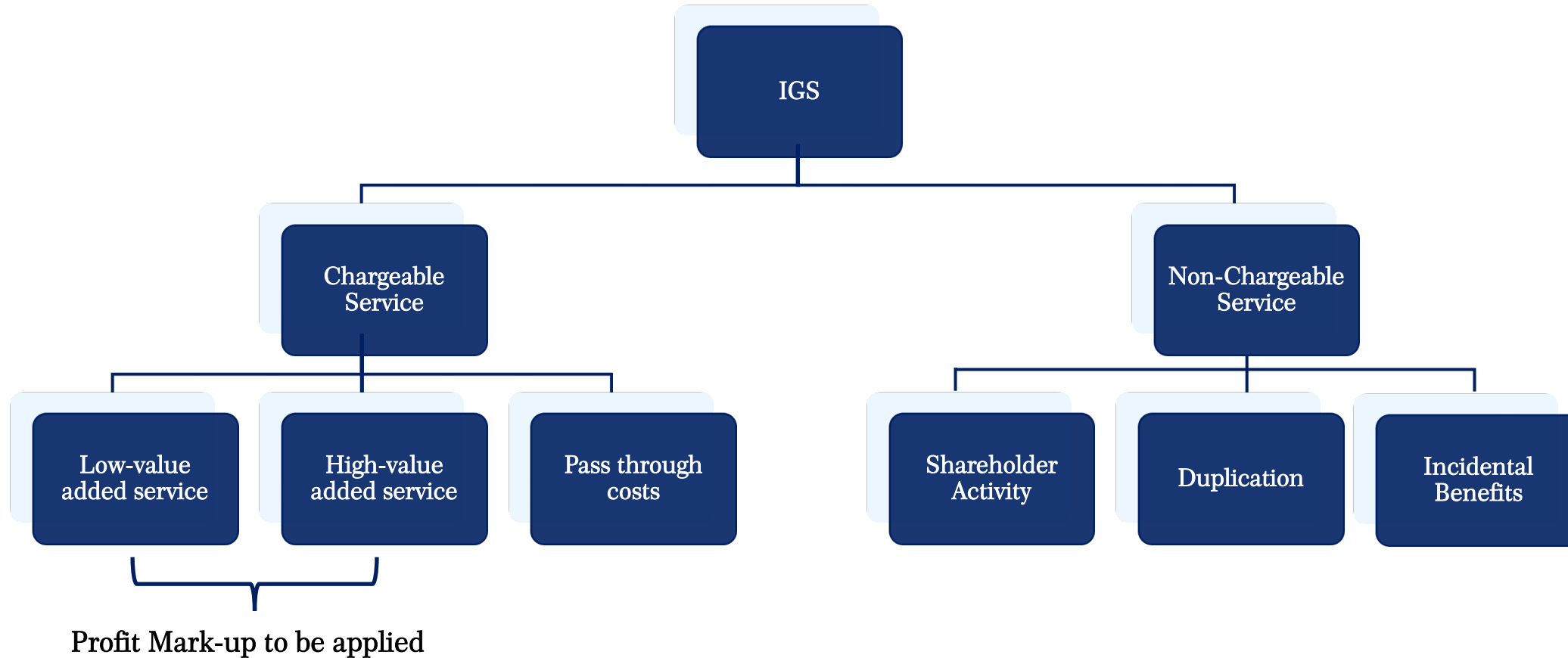
Illustration:



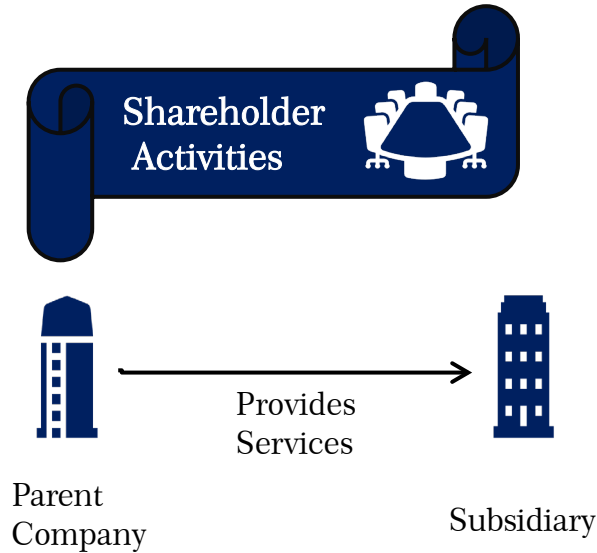
Key considerations for conducting a benefit test

- Receives, or reasonably expects to receive, benefits from such activities.
- Commercial or practical necessity for the activities
- Benefits are identifiable and capable of being valued

# Intra-group service – Chargeability & Non-Chargeability



# Shareholder Services - Non-Chargeable Services

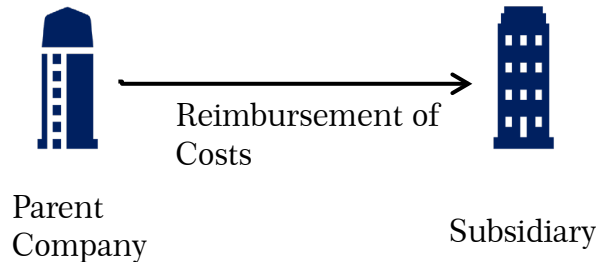


- IGS is performed relating to Group members even though those Group members do not need the activity.
- These refer to the services which a parent company or a regional holding company does solely because of its ownership interest in its capacity as a shareholder.

## Examples of costs associated with shareholder Activities:

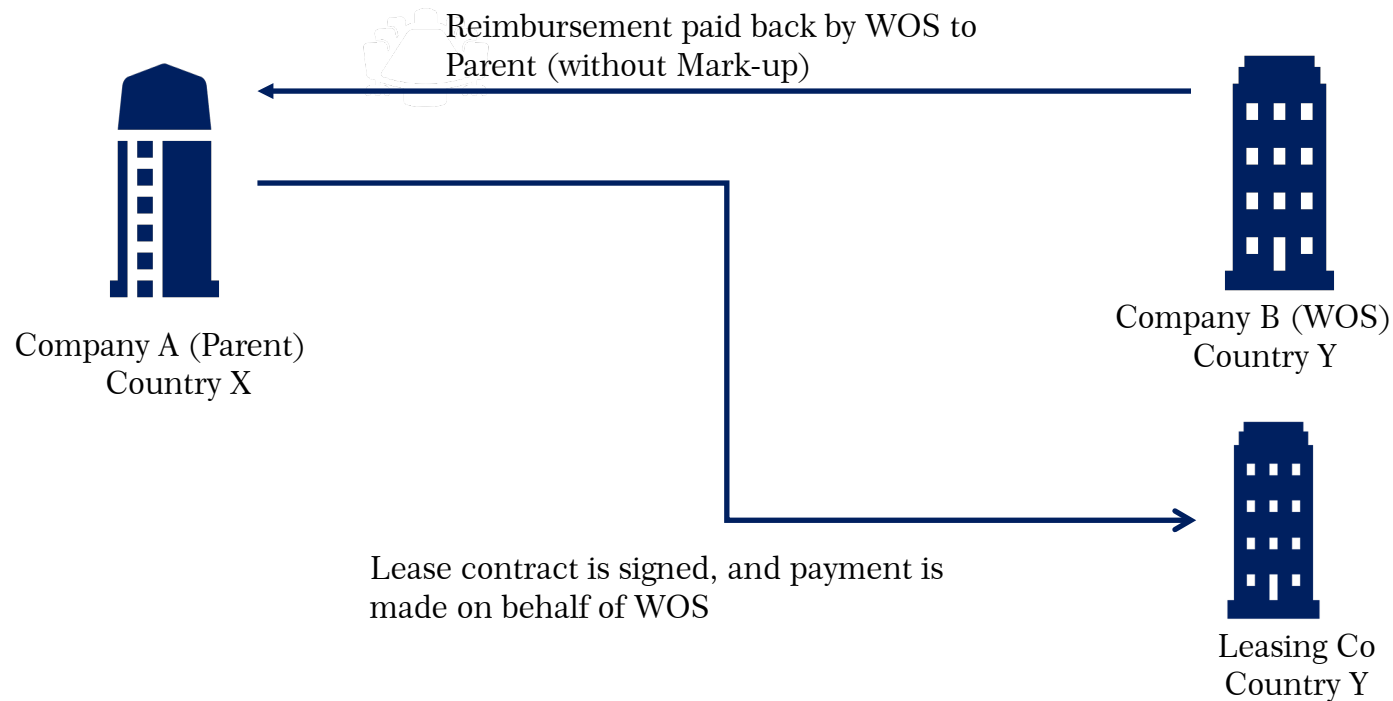
- Costs relating to the juridical structure of the parent company itself
- Costs relating to reporting requirements (including financial reporting and audit) of the parent company, costs relating to the preparation of consolidated financial statements of the MNE.
- Costs of raising funds for the acquisition of its participations and costs relating to the parent company's investor relations
- Costs relating to compliance of the parent company
- Costs which are ancillary to the corporate governance of the MNE as a whole

# Pass Through Costs/ Reimbursements - Non-Chargeable Services (1/2)



- Pass-through costs refer to expenses incurred by a company on behalf of its Related Parties for goods or services procured from various vendors.
- Whether the Group company arranging and paying for such goods or services should add a profit element to the amount paid to the vendors
- Group service provider may pass on the costs from the vendors **without a profit element or mark-up** provided that:
  - Acquired goods or services are **requested by and for the benefit of** the related parties or connected persons;
  - The group service provider is **merely the paying agent (Without value addition)**
  - The cost is **legal or contractual liability** of the related parties.

## Pass Through Costs/ Reimbursements - Non-Chargeable Services (2/2)



- Payment made for benefit of WOS in Country Y ?
- Whether Value addition exists ?
- Whether Legal and contractual obligation liability exists ?
- Whether in a third-party scenario, this kind of payment or service would be provided free of cost ?

# Duplication - Non-Chargeable Services (1/2)

## Duplication



- If a group company is already performing certain functions for itself or for external customers, and another group entity duplicates those same functions for it, the duplicated effort does not add any real value.
- Since it does not provide any new or meaningful benefit to the recipient, such activities should not be regarded as chargeable intra-group services.



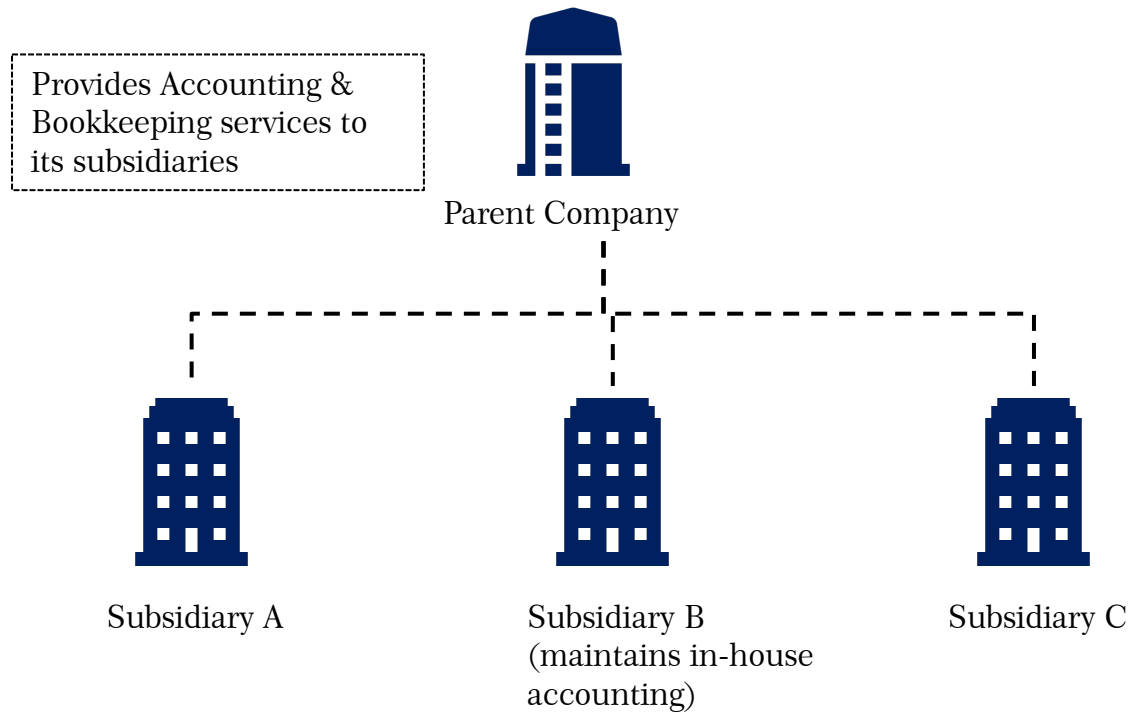
- Exception may be where the duplication of services is only temporary, e.g., where an MNE group is reorganizing to centralize its management functions.
- Another exception would be where the duplication is undertaken to reduce the risk of a wrong business decision (e.g. by getting a second legal opinion on a subject) an exception.



- In general, MNEs aim to avoid duplication of services in order to reduce costs. Furthermore, the mere availability of resources within an entity does not automatically mean that the services provided by another group entity are duplicative.

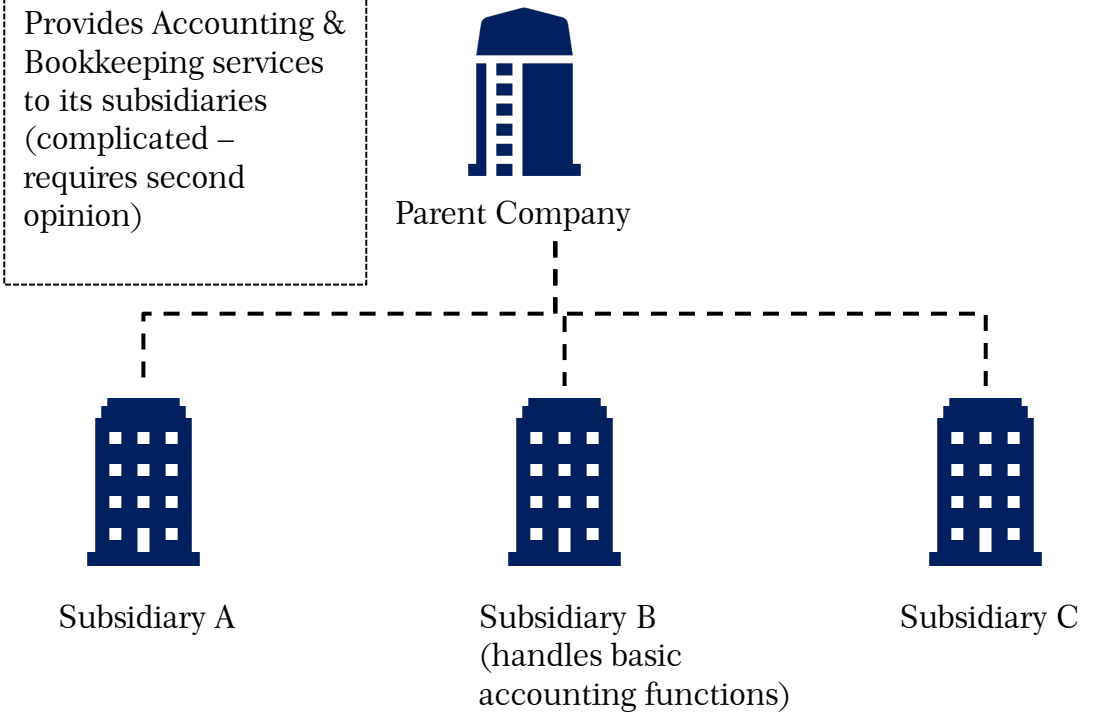
# Duplication - Non-Chargeable Services (2/2)

Illustration for duplication:



Since Subsidiary B handles its own in-house accounting, the service provided by Parent Company **will not be considered a chargeable service as these are considered as duplication services.**

Exception for Duplication



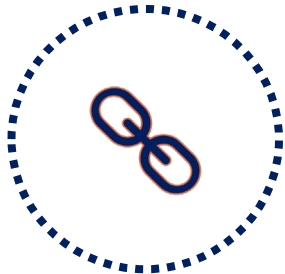
As Subsidiary B handles basic day to day accounting functions in-house, the services provided by the Parent company will not be considered duplicate activities and hence **will be regarded as chargeable services.**

# Incidental Benefits - Non-Chargeable Services

## Incidental Benefits

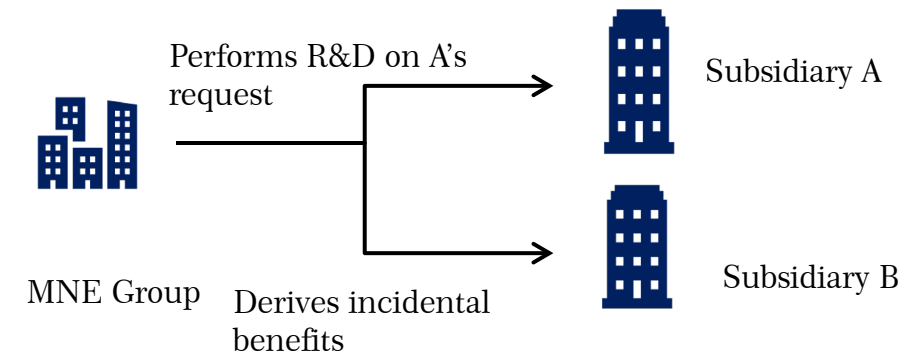


There are some cases where an **intra-group service performed by a group member** such as a shareholder or coordinating center **relates only to some group members** but **incidentally provides benefits to other group members**



The incidental benefits ordinarily **would not cause** these other group members to be **treated as receiving an intra-group service** because the activities producing the benefits would not be ones for which an independent enterprise ordinarily would be willing to pay

For e.g. The MNE group performed certain R&D activities specific to the need of Subsidiary A, however, another Subsidiary B also wanted to evaluate a new line of business based on similar R&D results and got certain incidental benefits out of it. Subsidiary B does not specifically need or requested such services. In such a case, Subsidiary B should not be charged for R&D services.



# Determining the Arms Length Charge for Intra-group services

## Comparability analysis

- ALP Should be determined from **both service provider and the service recipient.**
- The comparability analysis should reflect considerations such as **the value of the service to the recipient and how much an independent third party would be prepared to pay for that service in comparable circumstances.**

## Selection of Most Appropriate TP Method

- CUP
- Cost Plus Method
- TNMM

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## Determination of Cost base

Approach for determining the cost base for centralised services

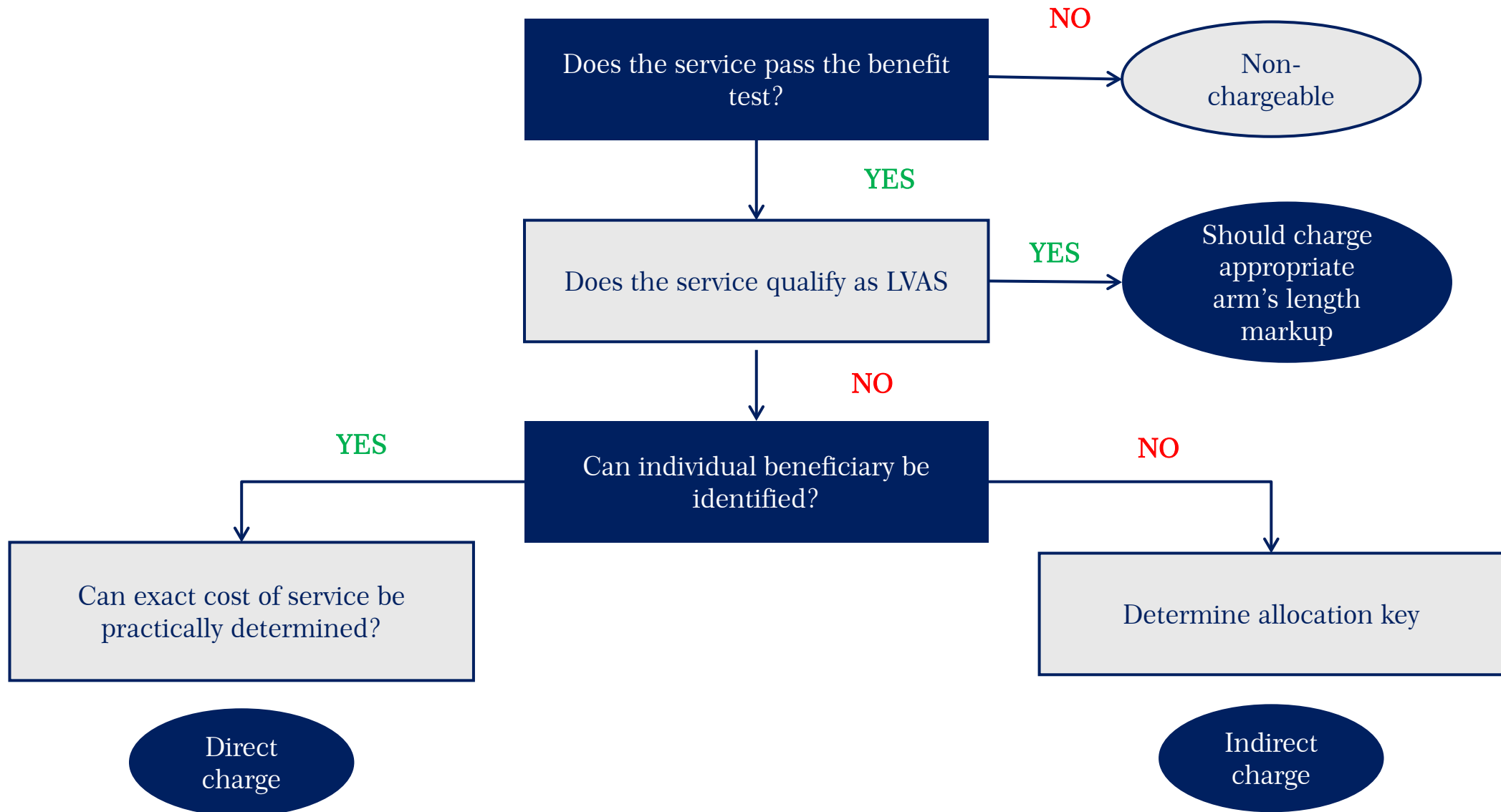
**Step 1 :** To calculate, on an annual basis, a pool of all costs incurred by all members of the Group

**Step 2:** The cost pool should exclude costs that are attributable to an in-house activity

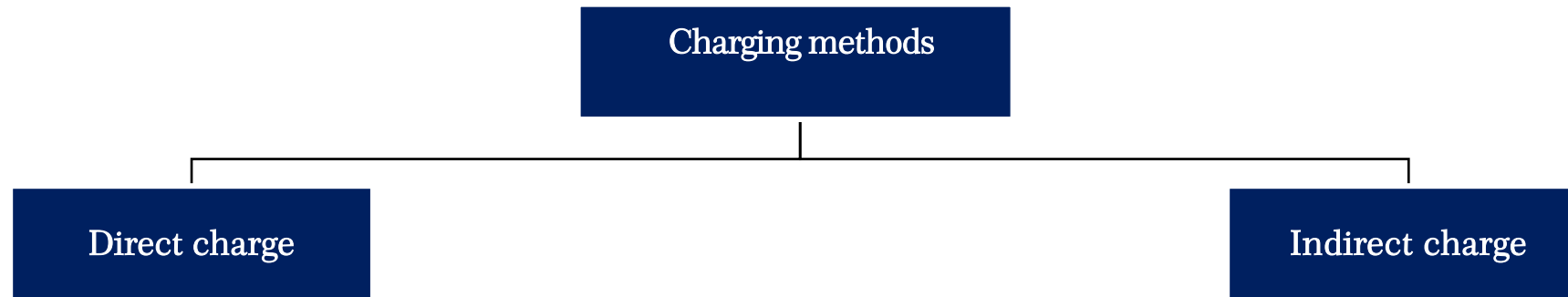
**Step 3:** To identify and remove from the pooled costs any costs that are attributable to services performed by one Group member solely.

**Step 4:** To allocate the remaining pool of costs that is attributable to the services which are provided to multiple members, More than one allocation key can be applied based on the nature of the service (linked to the benefit)

# IGS– Cost Allocation - Decision Tree



# Intra-group service – Charging mechanism



## Directly Allocable Cost:

- Services that can be identified as directly benefiting a particular group company
- Provides greater transparency to the tax authorities

## Indirectly Allocable Cost:

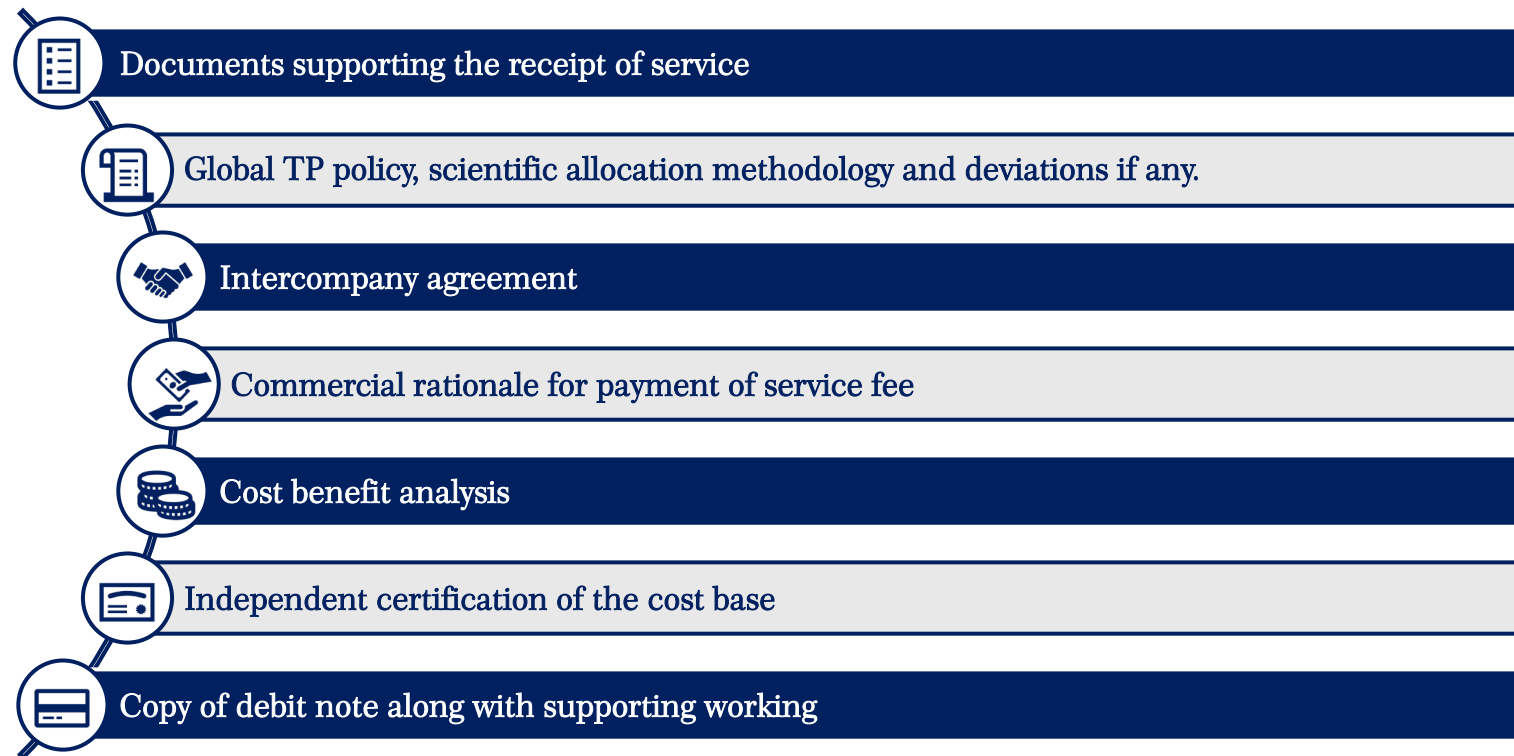
- Used where proportion of the value of services rendered to each entity cannot be exactly quantified except on an approximate or estimated basis.
- Identify all relevant costs, pool them and allocate among all recipients using sensible allocation key/s.
- Allocation keys shall be based on the nature of service
- Allocation of cost should commensurate with the benefit derived by the recipient
- Allocation method chosen must lead to a result that an independent enterprises would have been prepared to accept

## Arms Length Mark-up determined based on the type of service

S. No	Nature of services	Characteristics	Examples	Recommended ALP Mark-up
1	Low value-added services	<ul style="list-style-type: none"> <li>• Supportive in nature</li> <li>• Not a part of core group business</li> <li>• Do not require unique/ valuable intangibles.</li> <li>• Do not lead to creating of unique/ valuable intangibles.</li> <li>• Do not involve or give rise to significant risk</li> </ul>	<ul style="list-style-type: none"> <li>• Accounting &amp; auditing</li> <li>• Processing and management of debtors/ creditors</li> <li>• Human resources</li> <li>• Information technology support services</li> <li>• Internal and external communications</li> <li>• public relations support</li> <li>• Legal, administrative, tax compliance and other clerical services</li> </ul>	<p>5%</p> <p>(As per OECD Transfer Pricing Guidelines)</p>
2	High value-added services (non-routine value-added services)	<p>Involve activities that contribute to a company's overall:</p> <ul style="list-style-type: none"> <li>• value creation,</li> <li>• innovation, and</li> <li>• competitive advantage.</li> </ul> <p>These services often require:</p> <ul style="list-style-type: none"> <li>• specialized skills,</li> <li>• intellectual property, and</li> <li>• strategic decision-making.</li> </ul>	<ul style="list-style-type: none"> <li>• Research and Development (R&amp;D)</li> <li>• Brand Management and Marketing Strategy</li> <li>• Intellectual Property Development and Licensing</li> <li>• Strategic Management and Business Development</li> <li>• Supply Chain Management and Optimization</li> <li>• Financial Advisory and Risk Management</li> <li>• Advanced Technical Support</li> <li>• Market Research and Analysis</li> <li>• Innovation and Product Design</li> </ul>	<p>Based on TP benchmarking analysis</p> <p>(Generally, between 8%-12%-15%-20%-25%)</p>

# Need Benefit Analysis – Documentation for IGS

- Tax authorities /APA are to be satisfied on the need, benefit and evidences
- The documents supporting the need and actual receipt for IGS should be in place, i.e.



## Documentation

- ✓ Prepare and maintain supporting documentation
- ✓ Clear explanation of service
- ✓ Identify the beneficiaries
- ✓ Summary of benefits received
- ✓ Approach adopted to arrive at Costs/ Allocation/ Mark-up

- Involvement of the global tax / TP team in the APA for IGS transaction helps a lot. Close understanding of cost centres, nature of services, etc. during functional interviews helps in devising the collection mechanism for evidences.

# Intra-group service – Practical Challenges

## Identification & Valuation

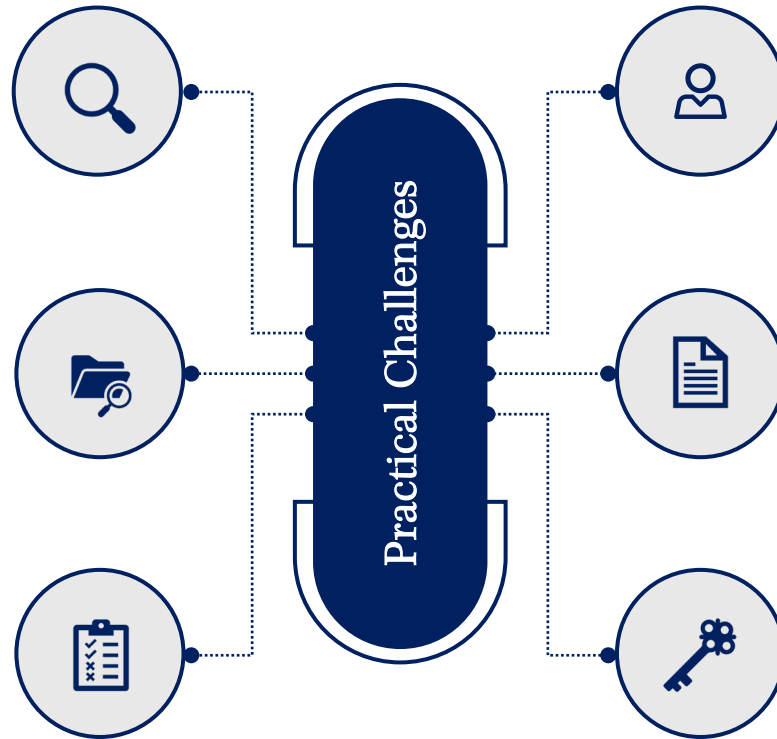
Identifying and valuing intra-group services is challenging due to the difficulty in quantifying benefits and ensuring arm's length pricing.

## Data Availability

Data availability is challenging due to the lack of comparable market data and limited transparency within multinational enterprises.

## Need Benefit Test

Conducting a need benefit test is challenging due to the subjective evaluation of service value and proving its economic benefit to each entity.



## Comparability Issue


Comparability issues in intra-group service arise from differences in service nature and terms, making it difficult to find suitable external benchmarks.

## Documentation Requirements

Documentation challenges arise due to extensive compliance requirements and the need to provide detailed justification for service charges.

## Allocation Keys

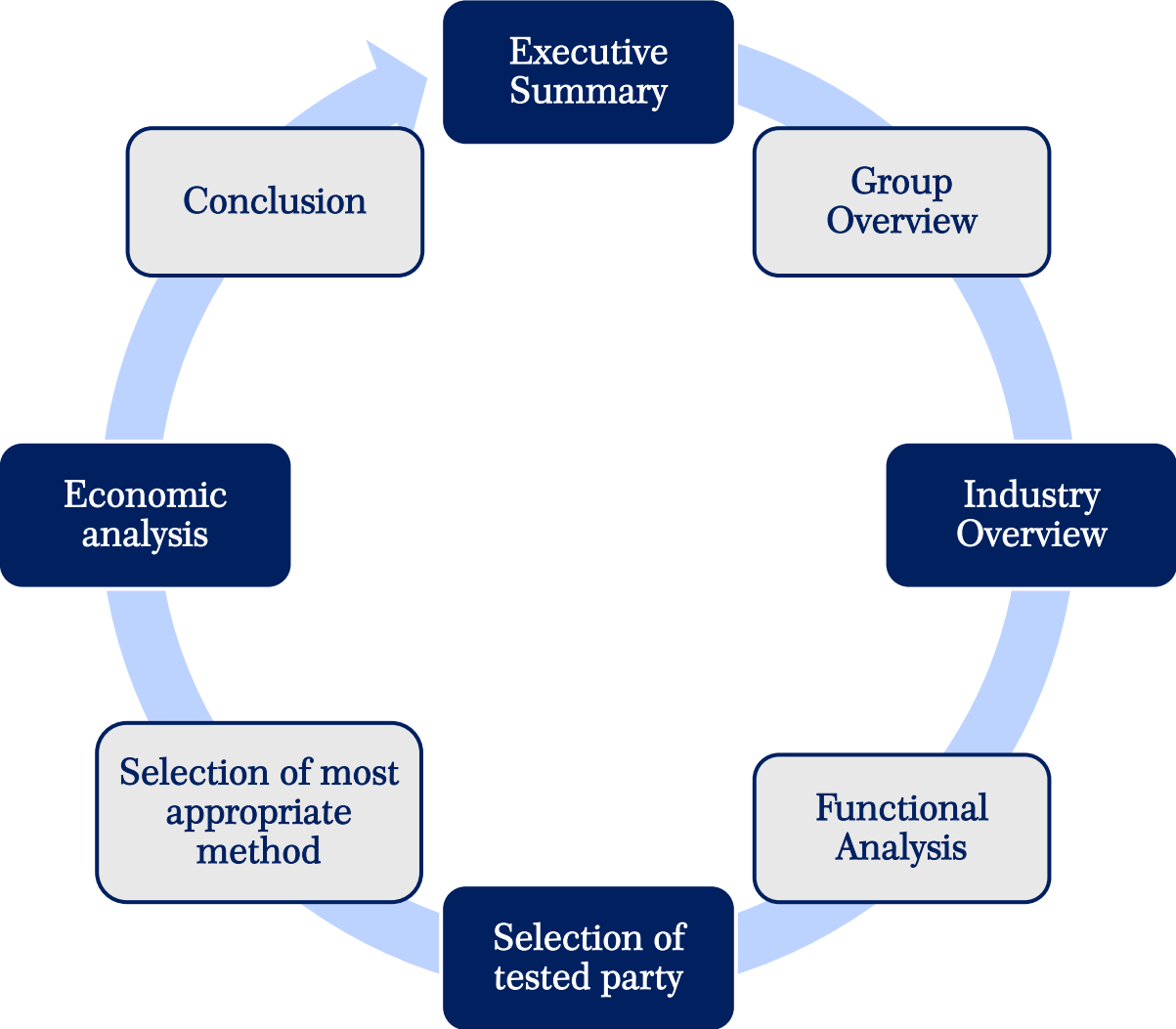
Using allocation keys is challenging due to the difficulty in selecting appropriate bases that fairly reflect the service usage.

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# **Transfer Pricing Documentation (Local File)**

# Local File – Documentation and Drafting

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# Local File – Contents & Checkpoints (1/3)

Contents	Review	Checkpoints
<b>Information of the Local Entity</b>	<ul style="list-style-type: none"> <li>• Description of the management structure, local organization chart, reporting individuals, and their principal office locations;</li> <li>• Executive Summary of the Local File</li> <li>• Detailed description of the business strategy, including involvement in business restructurings or intangibles transfers in the current or past year, with explanations;</li> <li>• Identification of key competitors;</li> </ul>	<ul style="list-style-type: none"> <li>• Reconfirm executive summary with economic analysis and financial results</li> <li>• Properly draft the business overview.</li> <li>• Always extract the Industry overview from the relevant sources. Ensure that the industry overview showcase the current trends in the respective industry.</li> <li>• Provide a brief overview of the global scenario and follow it up with conditions prevailing in the UAE/GCC/Middle East in which taxpayer is operating</li> </ul>
<b>Detailed Information of Controlled Transactions</b>	<ul style="list-style-type: none"> <li>• Description of material-controlled transactions (e.g., procurement, goods purchase, services provision, loans, guarantees, licenses) and their context;</li> <li>• Amount of intra-group payments and receipts for each category of controlled transactions, broken down by tax jurisdiction of the foreign payor or recipient;</li> <li>• Identification of associated enterprises involved in each category of controlled transactions and their relationships;</li> <li>• Copies of all material intercompany agreements concluded by the local entity;</li> <li>• Indication of the most appropriate Transfer Pricing method for each category of transaction and reasons for selecting that method;</li> </ul>	<ul style="list-style-type: none"> <li>• Ensure that full forms of all the abbreviations used are defined</li> <li>• Backup should be maintained for the transactions benchmarked in the local file with invoices, related party ledgers and any other supporting document</li> </ul>

# Local File – Contents & Checkpoints (2/3)

Contents	Review	Checkpoints
<p><b>Functional, Assets &amp; Risks Analysis &amp; Economic Analysis</b></p>	<ul style="list-style-type: none"> <li>• Detailed comparability and functional analysis of the taxpayer and relevant associated enterprises for each documented category of controlled transactions, including changes from prior years;</li> <li>• Indication of the most appropriate Transfer Pricing method for each category of transaction and reasons for selecting that method;</li> <li>• Identification of the selected tested party, if applicable, and reasons for this selection;</li> <li>• Summary of important assumptions made in applying the Transfer Pricing methodology;</li> <li>• Explanation for performing a multi-year analysis, if relevant;</li> <li>• List and description of selected comparable uncontrolled transactions, relevant financial indicators for independent enterprises, comparable search methodology, and information sources;</li> <li>• Reasons for concluding that relevant transactions were priced on an arm's length basis using the selected Transfer Pricing method;</li> </ul>	<ul style="list-style-type: none"> <li>• Read the intercompany agreement before drafting the functions and risks</li> <li>• Use functional questionnaire and conduct functional interviews with relevant management/business teams to draft FAR analysis</li> <li>• Search process backup should be maintained</li> <li>• Ensure that the appropriate TP Method has been selected based on the facts of the case</li> </ul>

# Local File – Contents & Checkpoints (3/3)

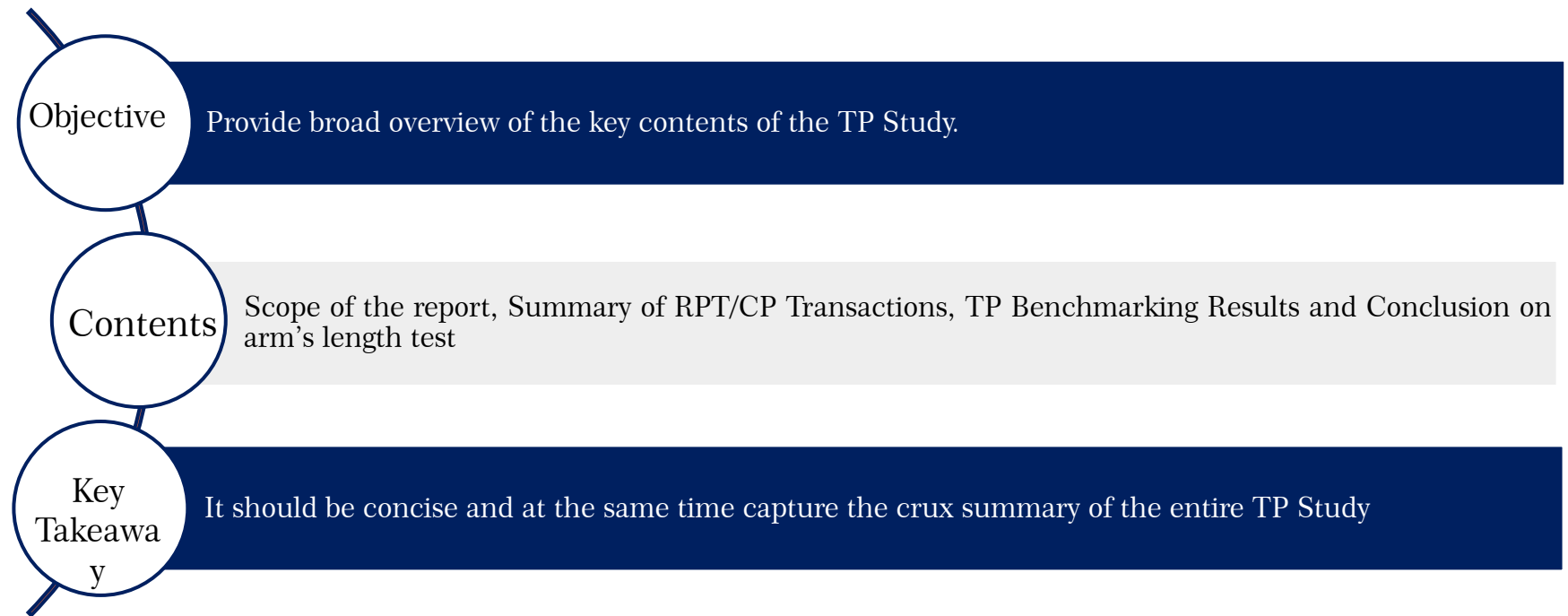
Contents	Review	Checkpoints
Financial Information	<ul style="list-style-type: none"><li>• Summary of financial information used in applying the Transfer Pricing method. Copy of existing unilateral and bilateral/multilateral APAs and other tax rulings related to controlled transactions described above;</li><li>• Information and allocation schedules showing how financial data used in applying the Transfer Pricing method ties to the annual financial statements;</li><li>• Summary schedules of relevant financial data for comparables used in the analysis and data sources;</li></ul>	<ul style="list-style-type: none"><li>• Financial results should tally with signed financials/ segment provided by client</li><li>• Cross check the value of transactions with TP Disclosure Form</li><li>• If company has more than one segment keep back up for the segmental allocation keys</li><li>• Reference any market studies/ reference reports used in analysis</li></ul>

# Local File/ TP Study – Executive Summary

## Executive Summary

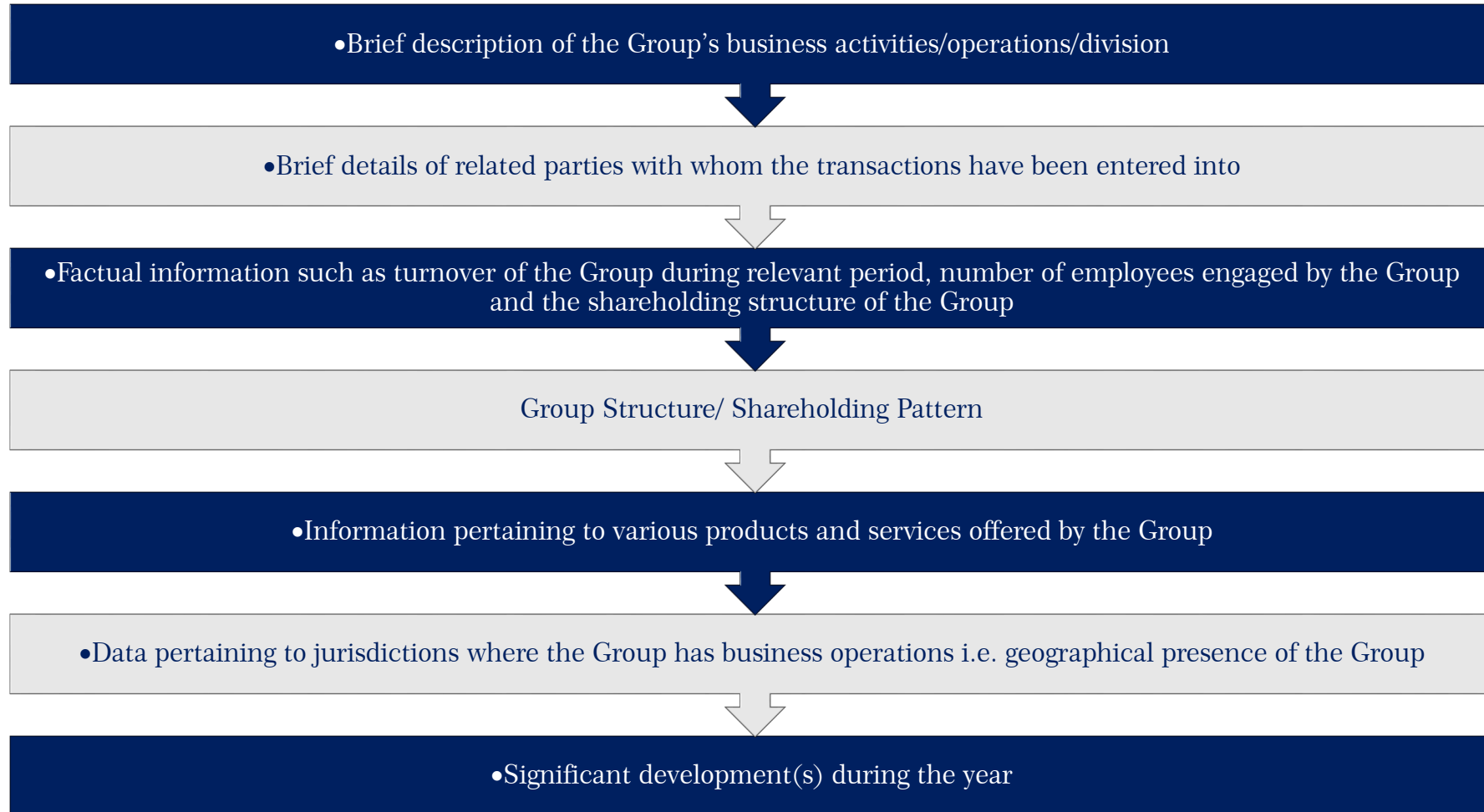
The Executive summary section of the TP report captures high level analysis of the entire TP Study and summarises the results of benchmarking analysis performed to determine arm's length price of the related party transaction(s) undertaken during the relevant period.

### Key Elements of Executive summary



# Local File – Group Overview

This section includes a brief description of the Group's as well as the taxpayer's business operations. The key points to be included in this section are:



# Local File – Industry Overview (1/2)

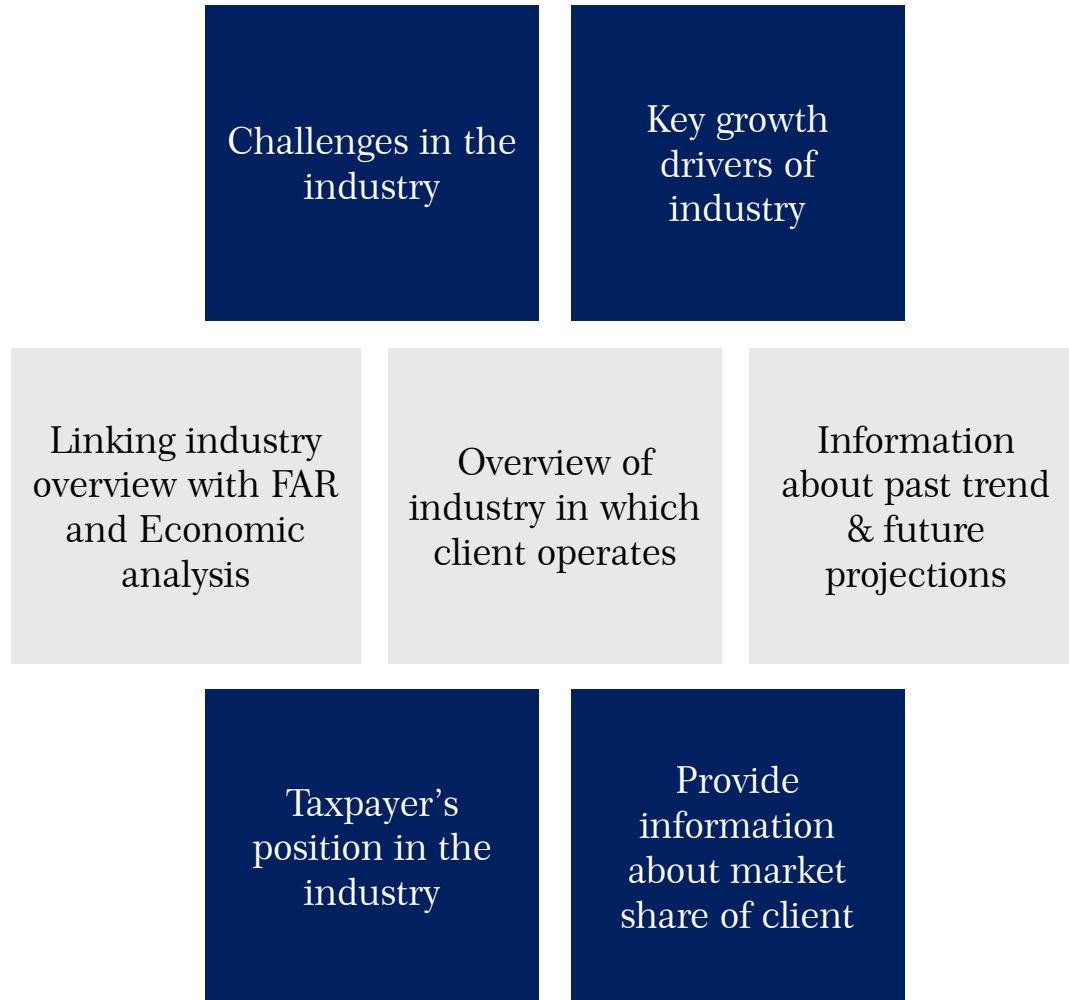
This section provides an understanding of the taxpayer/company's relative positioning in the industry vis-à-vis other players and overall justification of the taxpayer's financial results.

## Contents of Industry Overview

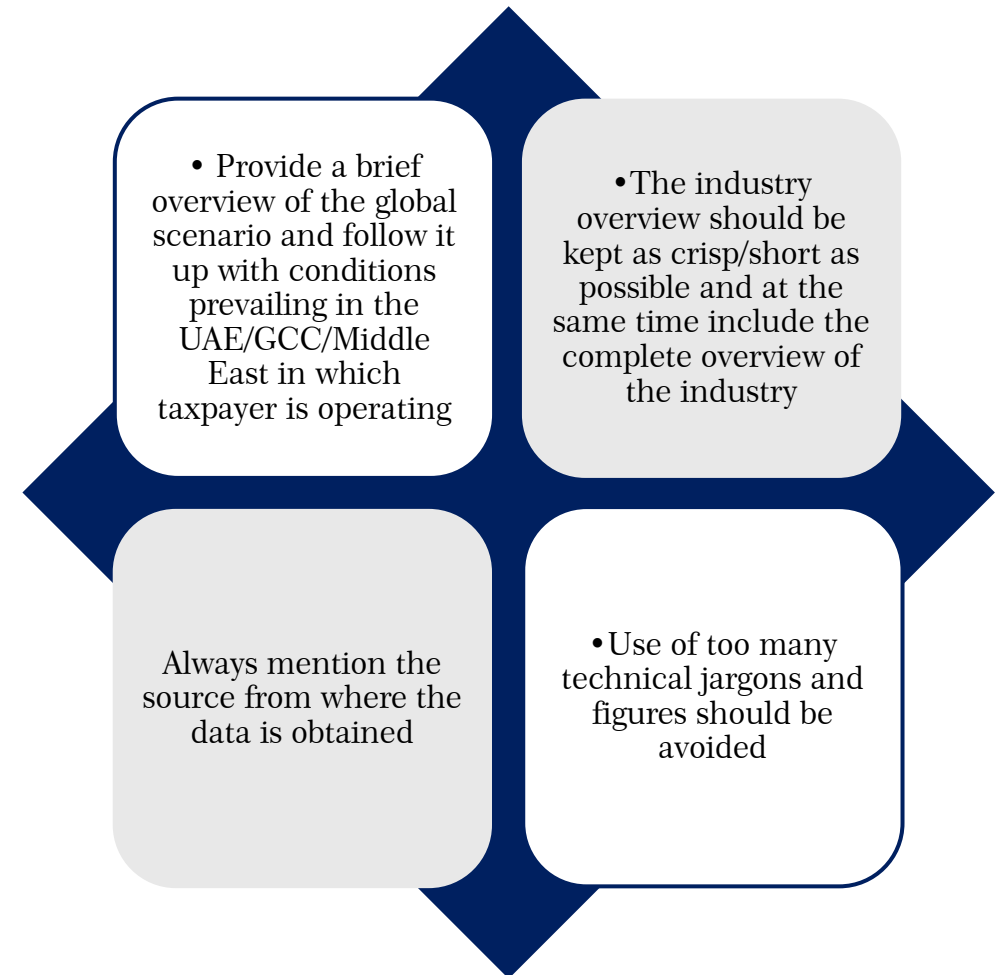


# Local File – Industry Overview (2/2)

## Key Objectives



## Important points to bear in mind



# Local File – FAR Analysis (1/5)



## Need

For transactions between two independent enterprises, the compensation will usually depend on the functions that each enterprise performs (considering assets used and risks assumed). Therefore, in determining whether controlled and uncontrolled transactions or entities are comparable, a functional analysis (“FAR”) is necessary.

This functional analysis seeks to identify and compare the economically significant activities and responsibilities undertaken, assets used, and risks assumed by the parties to the transactions

## Objective

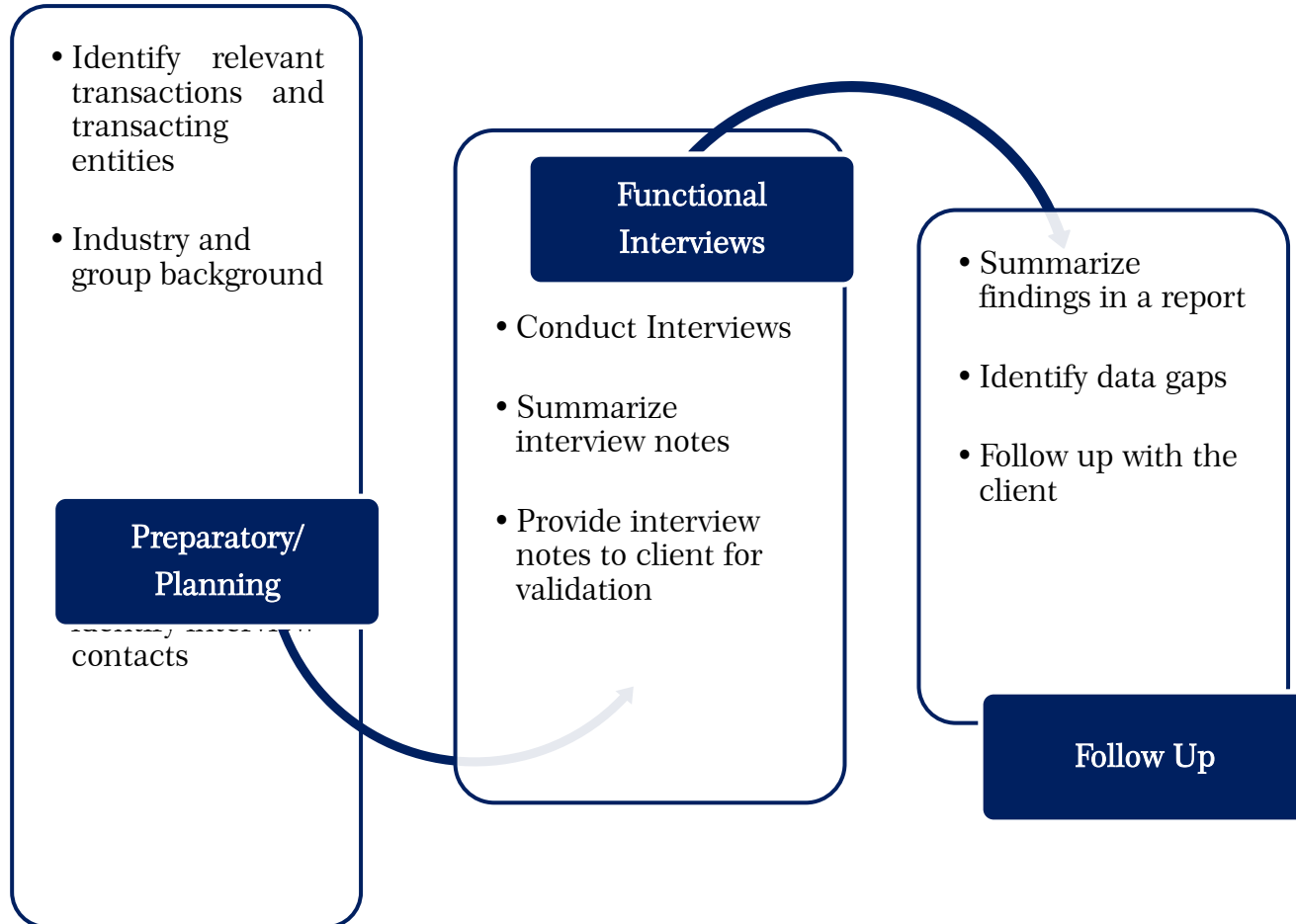
## OECD Guidelines

The guidelines has highlighted the need to have a more granular review of functions, risks, and assets, to support the transfer pricing policy of the taxpayer.

# Local File – FAR Analysis (2/5)



## Steps involved in Functional Analysis



## FAR Documentation

- Complete record of the interviews
- FAR documentation should contain
  - A detailed description of the functional analysis
  - Interview notes kept as back-up
- Review of other documentation as back-up, such as agreements, invoices, process charts, statement of work, etc.
- The functional analysis should direct the reader unambiguously to the correct conclusion about who performs the key functions and bears the related risks.

# Local File – FAR Analysis (3/5)



The various aspects covering functional analysis i.e., functions performed, assets employed and risk assumed are discussed in detail below:

## Functions performed

- Description of functions performed by each transacting party
- Study the entire value chain of the business

Flow charts depicting the value chain, identifying the key value drivers;



Identifying unique intangible assets owned;



Identifying the non-routine value addition



Reference to agreements and pricing mechanism, wherever available.

## Assets Employed

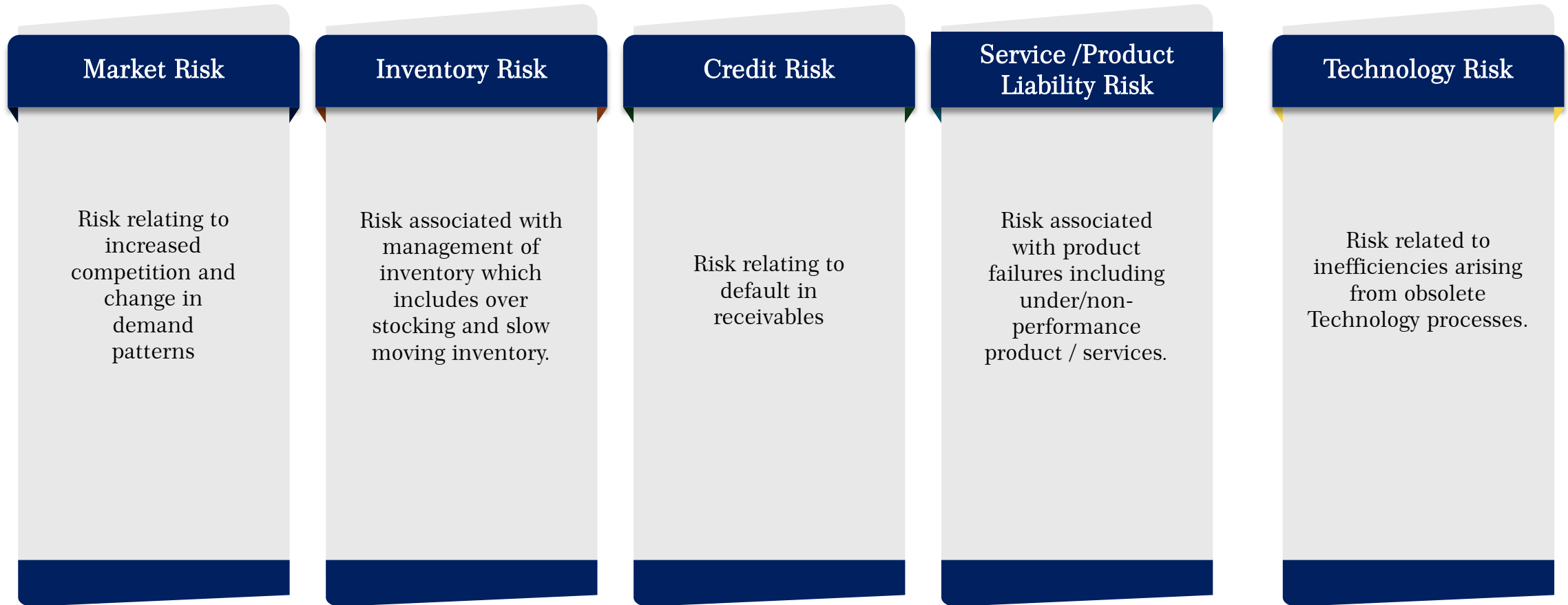
- The analysis of assets employed into tangible assets and intangible assets is of vital importance to determine intensity of functions and selection of most appropriate method.
- The existence of intangible assets in the form of technical knowhow, trademarks, patents, etc. contribute to the supernormal growth in profits of an enterprise.
- However, an entity which owns only tangible assets which are used in normal course of operations such as computers, plant & machinery etc. is expected to earn normal profits.

# Local File – FAR Analysis (4/5)



## Risks performed

The risks assumed by an entity has a direct correlation with the profit margins. Different types of Risk are:



# Local File – FAR Analysis (5/5)



## Risks performed – Contd.

The risks assumed by an entity has a direct correlation with the profit margins. Different types of Risk are:



# Local File – Economic Analysis

Determination of years to be covered

1

Broad-based analysis of the taxpayer's circumstances

2

Understanding the controlled transactions based on functional, assets & risks analysis, in order to choose the tested party

3

Review of existing internal comparables, if any

4

Determination of available sources of information on external comparables where such external comparables are needed taking into account their relative reliability

5

Selection of the most appropriate transfer pricing method and determination of the relevant financial/Profit level indicator

6

Identification of potential comparables using TP databases:  
Based on the relevant factors identified in Step:3

7

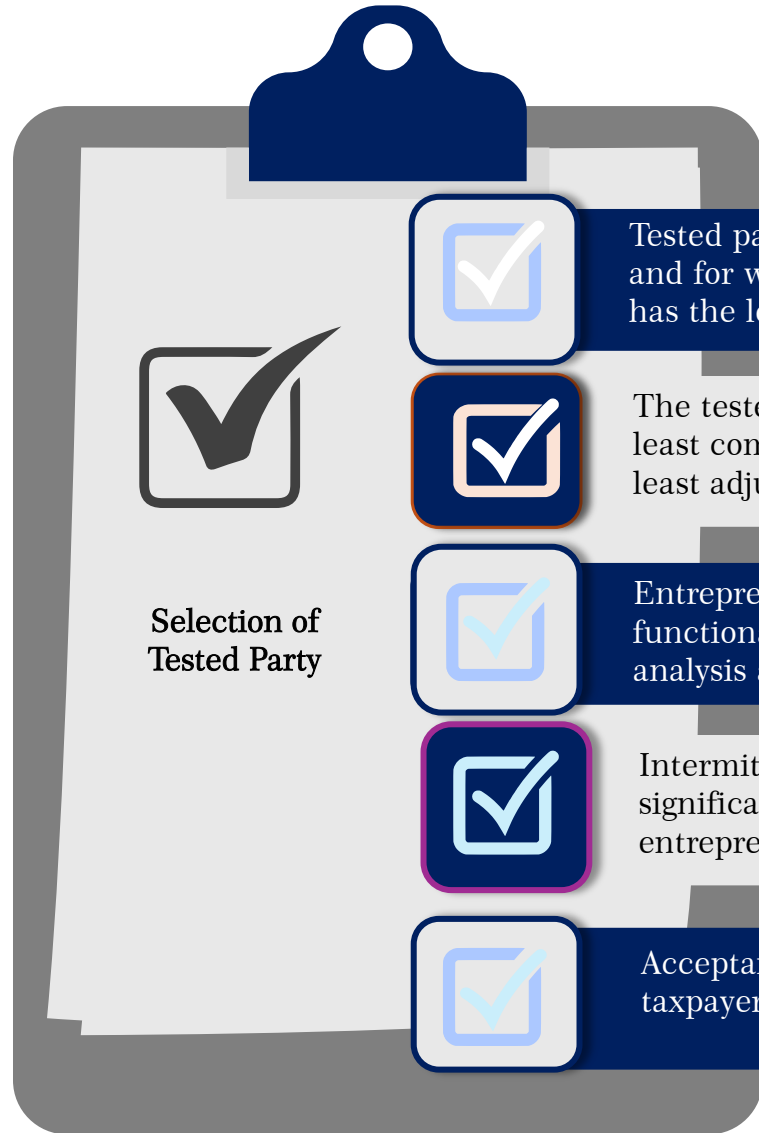
Determination of and making comparability adjustments where appropriate.

8

Interpretation and use of data collected, determination of the arm's length remuneration.

9

# Local File – Selection of Tested Party



Selection of Tested Party



Tested party is one to which a transfer pricing method can be applied in the most reliable manner and for which the most reliable comparables can be found, i.e., it will most often be the one that has the least complex functional analysis.



The tested party should be the one for which reliable and accurate data is available., should be the least complex among the parties to the transaction and should be the one, whose data requires least adjustments in order to make it comparable.



Entrepreneurs are generally not considered as “tested party” on account of their complex functional and risk profiles which results in vulnerable profits margins making comparability analysis a difficult proposition



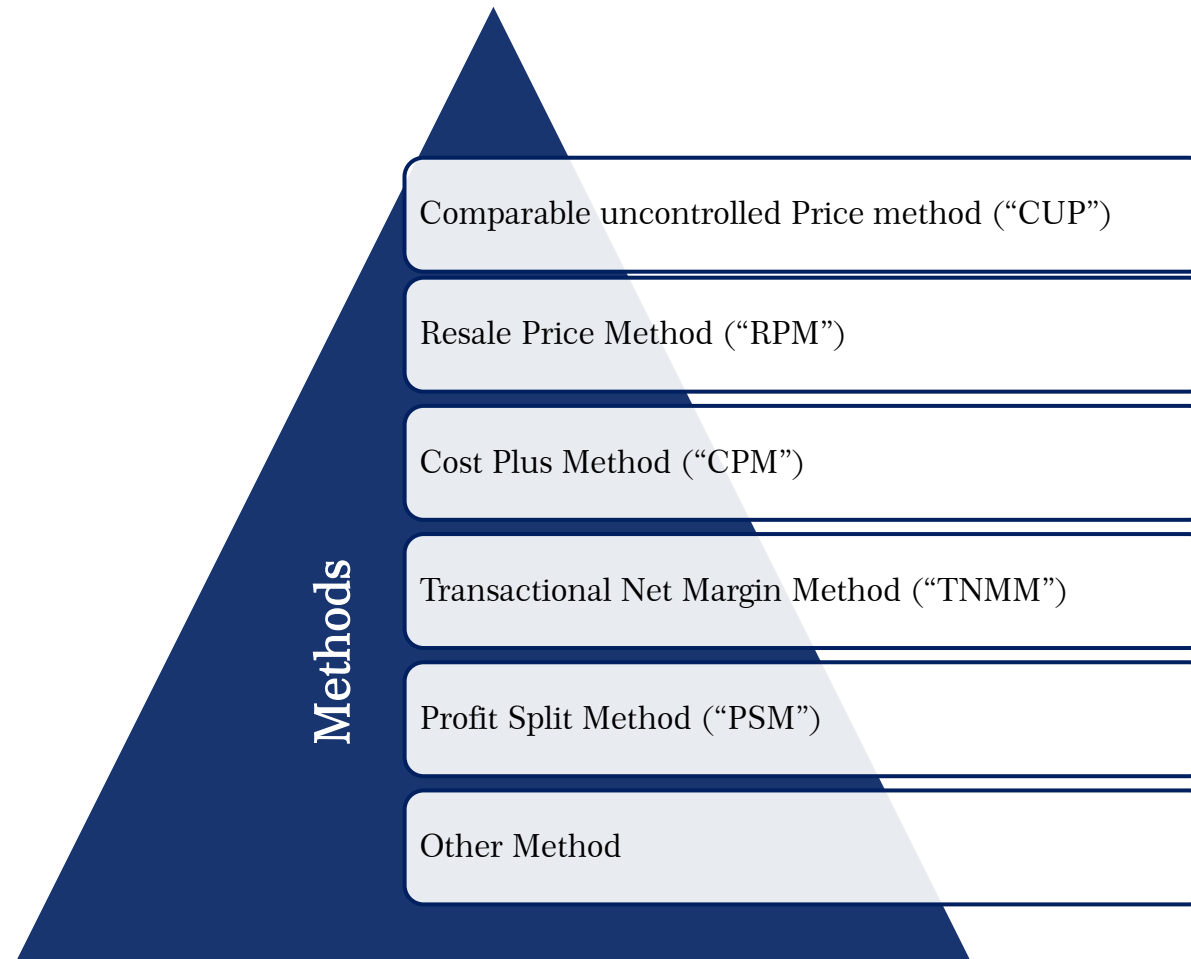
Intermittently, entrepreneurs which carries out significant entrepreneurial activities and bears significant risks associated with such activities can be chosen as tested party on the basis of entrepreneur bearing normal business risks.



Acceptance of foreign entity as a tested party is not a matter of convenience and the onus is on taxpayer to substantiate its choice of tested party with robust documentation.

# Local File – Selection of Most Appropriate Method (1/2)

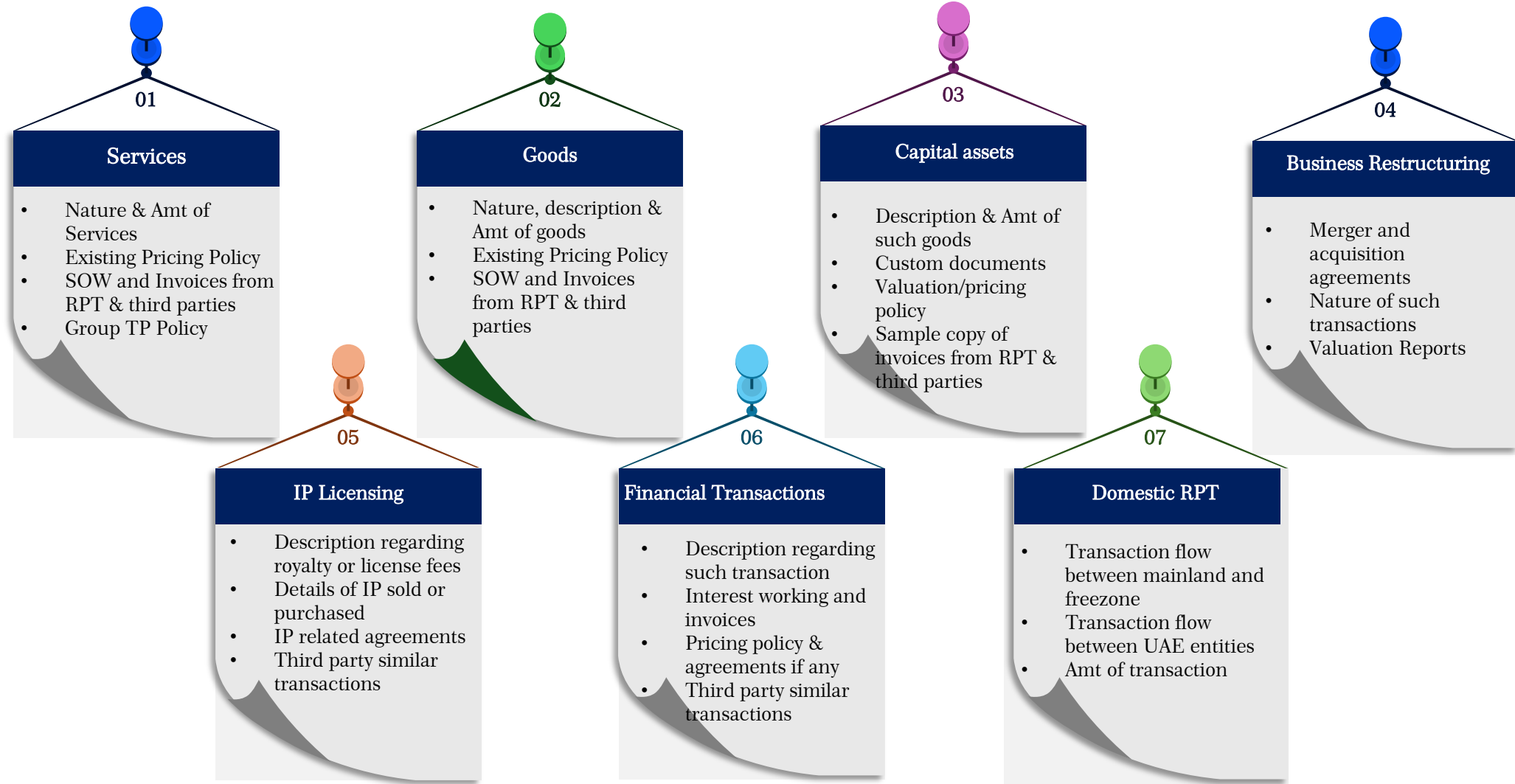
In order to benchmark the international/intra group transactions, a taxpayer has to choose/select the most appropriate method out of the six methods prescribed by the UAE TP regulations which are as follows:



# Local File – Selection of Most Appropriate Method (2/2)



# Local File - Supporting Documentation / Checklist



# Transfer Pricing Domain (1/2)



## TP Benchmarking & Policy Setting

- Local, Regional And Global Transfer Pricing Benchmarking Analyses
- Drafting/Review Of Inter-company Agreements
- Group TP Policy Document Preparation
- TP Benchmarking Reports Review & Recommendations
- Transactional TP Policy Setting



## Global TP Compliance

- Disclosure Form
- Local File
- Master File
- Country-by-country Report
- Group Level Transfer Pricing Compliances Management
- Comfort Letters/Memos For Statutory Auditors
- Fin 48 Assistance



## Tax Controversy Management

- Representations In Case Of TP Audit/Scrutiny
- Filing Of TP Submissions And Supporting TP Workings & Back-up Documentation In Response To Notices, Information Requests
- Strategy Based On Facts, Law And Judicial Precedents
- Cost Benefit Analysis For Litigation Vs Dispute Resolution
- TP Adjustments & Provisioning Review

# Transfer Pricing Domain (2/2)



## TP Structuring & Advisory Service

- Transactional Level and Group Level Structuring Advisory
- Value Chain Analysis
- Operational Transfer Pricing
- Drawing Segmental P&L for Transfer Pricing Purposes
- Complex Intra-group Transactions Review & TP Policy Setting
- TP /Economic/Secondary/ Corresponding Adjustments Computation



## TP Technology

- Monitor Due Date and Track Progress
- Data Gathering & Aggregation
- Design & Execute Legal Framework
- Analyze Inter Company Transaction Values
- Establish arm's length Price
- Prepare Country specific documentation
- Monitor TP Policy



## Dispute Resolution

- Transfer Pricing Health Check-Up to avoid/ mitigate risks
- Transfer Pricing Due Diligence
- TP Risk Assessment
- Advance Pricing Agreements Assistance
- Mutual Agreement Procedures
- Safe Harbour Applications



## BEPS & International Taxation

- BEPS Impact Analysis
- OECD Pillar 1 & 2 – Readiness, Implementation & Impact
- CbCR Risk Assessment
- IP Structuring /DEMPE analysis in view of Action 8
- PE Evaluation & Profit Attribution
- Thin Cap Evaluation
- POEM Risk Assessment & Recommendations



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*Thank You*

For any queries feel free to contact:

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