



Bundeszentralamt
für Steuern

Case Study: “Funny Cars” or “Fun (?) with Cars” Possible „*Solution*“

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Case Study: “Fun (?) with Cars”

Preliminary Note:

Since the case has not yet been finally closed, there is no final solution to share.

The considerations of the German Competent Authority are therefore provided below.

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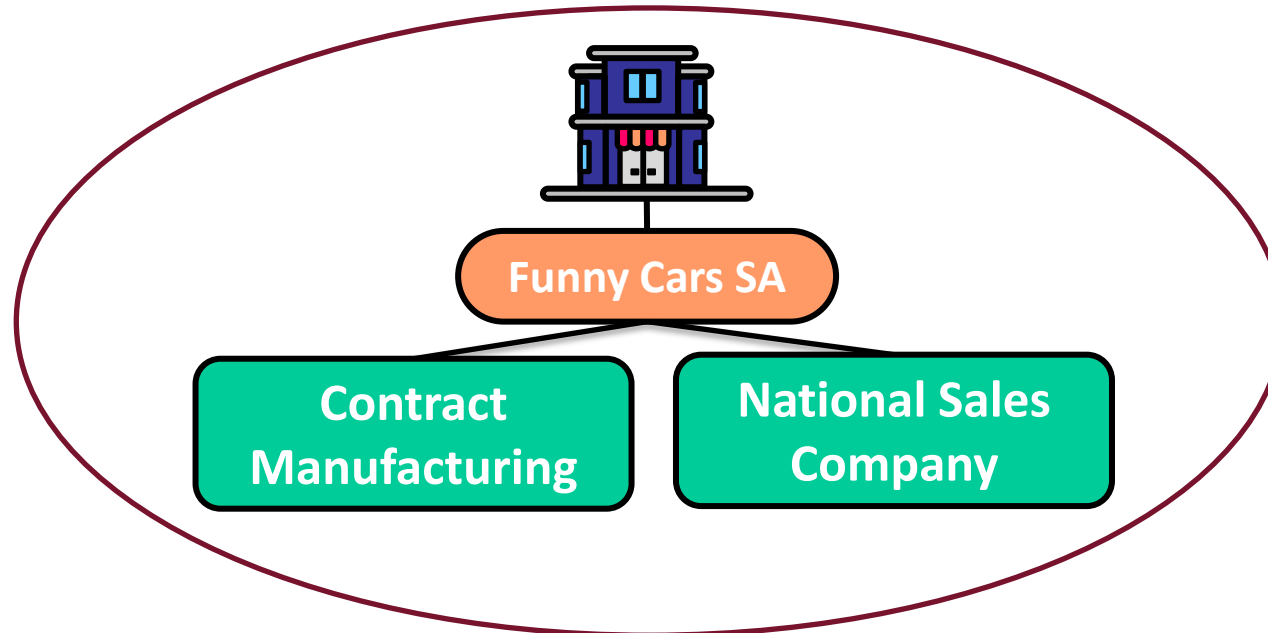
Questions:

1. Is the Tested Party “one” legal entity or different divisions?
2. How to handle Upfront Cost from change of production?
3. Performing a Term Test or a single year test? If Term Test: How long is a “Term”?
4. Which years should a benchmark analysis include?
5. How to deal with Local Tax Audit adjustments during the negotiation/APA period?

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Question 1:

Is the Tested Party “one” legal entity or different divisions?



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Question 1:

Whole of entity or separate approach?

- central element of a transfer pricing analysis should be the individual transaction
- However, it is quite common that several transactions should be tested together.
- Here: “Contract Manufacturing” for Transactions: Provision of production Know-How and Components from AG to SA and export of locally manufactured vehicles to Funny Cars AG) *[OECD TPG Tz. 3.9]*
- purchase of vehicles for sale on the local market differs from contract manufacturing
- No portfolio approach (“razor-blade” oder “printer cartridge” model). This approach should not be used for different business transactions with different economic logic *[OECD TPG Tz. 3.10]*
- No whole of entity approach since the transactions cannot be compared with independent companies *[OECD TPG Tz. 2.84]*
- Also from economic perspective, the different functions are like independent business models
- Both the production plant and the distribution company respectively can act on their own behalf on the market.

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Question 2:

How to handle Upfront Cost from change of production?



Pre-Production-Costs: 20 Mio€

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Question 2:

How to handle Upfront Cost from change of production?

- An unrelated third-party manufacturer would also have to bear the costs of a production change if a sufficient profit from the overall business is achieved during the entire delivery period.
- This is common in the automotive industry. In such cases the development costs of the supplier are covered by the part price of the OEM and therefore "subsequently" receive a profit component.

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Question 3:

Performing a Term Test or a single year test? If Term Test: How long is a “Term”?

Single Year

Term Test 20XX - 20XX

Rolling Average

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Question 3:

Performing a Term Test or a single year test? If Term Test: How long is a “Term”?

- important „to identify the commercial or financial relations between the associated enterprises and the conditions and economically relevant circumstances attaching to those relations in order that the controlled transaction is accurately delineated.“
[OECD TPG Tz. 1.33 ff]
- All conditions and economically relevant circumstances must be compared with the relevant circumstances of comparable transactions
- OECD also considers it is necessary to examine data from both the year under review and previous years. [OECD TPG Tz. 3.76 ff]
- A single year approach ignores the cyclical nature of the automotive industry and therefore leads to an unreliable comparison of the margins achieved by the peer companies with those of the tested party.
- The profitability of SA is not constant and can be affected by economic (Covid-19) or product life cycles. [OECD TPG Tz. 1.131]
- Also a comparison of a term test of the benchmark companies with an annual analysis of the tested party contradicts the economic conditions of the individual years, which would not be considered or would only be taken into account inadequately by comparing a single year of the tested party with an average value of several years of the Benchmark-companies. [OECD TPG Tz. 3.75 ff]
- According to the German APA team, the result should be tested using a term test.

Not yet clarified: Rolling Average or (Fixed) Term Test? Rolling Average 3-Years? Term Test -> How Long is a „Term“ ?

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Question 4:

Which years should a benchmark analysis include?

**Benchmark Analysis
Single Year**

**Benchmarking Analysis Term
Test**

**Benchmarking Analysis
Rolling Average**

Ex ante (before requested Years) or Ex post (for requested Years)

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Question 4:

Which years should a benchmark analysis include?

- According to OECD-TPG, a multi-year analysis can also be carried out to improve the quality of the benchmarking. A (weighted) average for the benchmark analysis covering several years is also possible and is in line with international practice. [OECD TPG Tz. 3.75, 3.77, 3.78, 3.79]
- Regarding the years covered by the benchmark analysis, the German CA is of the opinion that years that correspond to the APA period should be used as far as possible, as these years best reflect the economic circumstances.
- This means that for a term test for the years 2018-2020, a benchmark analysis for the years 2018-2020 should be used if possible.

Whether a rolling average or a fixed term test should be used must be answered together with question 3.

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Question 5:

How to deal with local tax adjustments?

Or: Unfriendly Action? - Come on, behave!

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Question 5: How to deal with local tax adjustments?

Or: Unfriendly Action - Come on, behave!

Experience?

Behavior in your Country?

Germany:

1. In Germany, it is absolutely unusual to conduct an audit of transactions covered by an ongoing APA period.
2. Findings only under consideration of single years:
 - looks very much like „cherry picking“
 - intensifies and hardens the ongoing APA-discussions between the CAs
 - Contradicts the economic realities (Life cycle, one-time economic impacts)
 - Ignores extraordinary one-off effects

Note: According to the German law, a single year adjustment is technically also mandatory.

But in practice a German transfer pricing tax audit usually considers a multi-year perspective.

An adjustment often taken place in the last year of audit or in every single year. However, the amount of the adjustment is usually determined by a term test.

Thank you very much for your attention!

Contact

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