To	Tax Treaties, Transfer Pricing and Financial Transactions Division, OECD/CTPA	Date	Sep-18
From	KPMG LLP, United States	Ref	KPMG Comments on Discussion Draft on BEPS Actions 8-10, Financial Transactions
cc	Stephen Blough, KPMG LLP, United States		

Executive Summary on Discussion Draft on BEPS Actions 8-10, Financial Transactions

KPMG LLP ("KPMG" or "we") welcomes the opportunity to engage with the Organisation for Economic Co-operation and Development ("OECD") regarding its draft guidance on financial transactions dated July 3, 2018 (the "Discussion Draft" or "guidance"). KPMG has considered input from non-U.S. member firms of KPMG International in developing our comments but submit on our behalf alone.

KPMG commends the OECD for engaging the transfer pricing and tax community in this project at an early stage.

Executive Summary

Our comments will directly address, and where relevant expand on, specific "questions to commentators" included in the Discussion Draft, reflecting the following major themes:

1. The accurate delineation of the actual transaction, as applied to financial transactions, must account for key differences in the nature of intercompany financial transactions and those involving tangible or intangible assets. This includes the fact that the financing function may be separable in tangible or intangible transactions, while it is at the core of a financial transaction. The OECD recognizes the importance of accurate delineation of the transaction, and therefore should take note that issues with such delineation based on misunderstanding of key features of financial transactions will lead to more disputes between taxpayers and tax authorities.

   KPMG recommends against specification of factors to be taken into consideration when delineating a financial transaction. Rather, guidance should allow taxpayers to characterize and defend the nature of their intercompany financial transactions according to their facts and circumstances. KPMG recommends specific edits to paragraph 11 of the guidance, as well as elimination of paragraphs 13-15.

   KPMG believes that an entity's capital structure should be respected unless there is evidence that it is outside the norm of market practices. The OECD should also clarify that any re-characterization of intercompany debt under an accurate delineation of the actual transaction approach is an arm's length issue subject to Article 25 procedures.

2. In most cases, the accurate delineation of a financial transaction should focus on comparing its terms, along with the financial capacities of the parties involved, to observable market benchmarks, largely respecting the contractual allocation of risks and responsibilities among the parties but for cases of clear and egregious distortions of those roles and the resulting pricing of the transactions.

   Where the terms of a related-party transaction depart significantly from market convention, or from the taxpayer's established policies when dealing with third parties, taxpayers may need to include in their transfer pricing documentation some justification for their terms and conditions. However, KPMG recommends against any rules that would automatically impose certain terms on transactions among related parties (e.g., covenants).

3. Consideration of implicit support in a lending or guarantee transaction, and its impact on arm's length pricing, should be based on the particular facts and circumstances of each taxpayer, and not follow from any "rebuttable presumptions" regarding the relationship between the MNE group's credit rating and that of an individual entity. Assertions of implicit support, by either taxpayers or tax authorities, should be based on thorough analysis or market evidence.

   KPMG recommends altering paragraph 67 and deleting paragraphs 68 and 69 of the guidance. We also suggest replacing paragraphs 70-74.

4. KPMG believes that there are many situations where opinions provided by third parties, such as banks or insurance brokers, can be helpful in determining arm's length pricing. Such indicators should not be pre-emptively ruled out. Rather, taxpayers should be allowed to advocate for such opinions on a case by case basis, based on the degree of rigour with which the opinions are established and the extent to which this approach can be shown to be more reliable under the facts and circumstances than alternative methods. Consequently, the OECD should consider revising paragraph 93 of the guidance.
5. Regarding cash pooling, the allocation of group synergy benefits is not typically taken into consideration when benchmarking deposit and lending rates. In most cases, the recommended approach would be excessively costly and data intensive, and should therefore be applied only in exceptional situations.
6. The OECD's draft guidance on captive insurance companies should be significantly revamped to better reflect the nature of risks that they tend to assume, the curbing role of regulators, and practically applicable pricing methodologies. Assessment as to whether or not a captive insurer exercises adequate control of risk should take into consideration unique features of the industry and market, as well as typical functional profiles for a captive.

The BEPS actions have helpfully renewed the focus on financing transactions in particular. The arms-length approach of the transfer pricing guidelines will overlap, and potentially conflict, with domestic rules on related party pricing as well as anti-hybrid and thin capitalisation rules. KPMG believes that the guidance in the Discussion Draft would in some cases increase the potential for disagreement with tax authorities. It is important that the guidelines provide clear rules and approaches to minimise differences and uncertainty. To the extent they arise, the guidelines should allow clear and speedy resolution of disputes.