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# ANALYZING TRANSFER PRICES IMPACT AT EUROPEAN LEVEL ON ROMANIAN COMPANIES

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***Abstract:*** *At present, due to the current project of the Organization for Economic Cooperation and Development, with regard to tax base erosion and profit shifting (OECD BEPS), as well as with regard to the impact of global fiscal reforms in development, in transfer pricing, fiscal authorities are the ones in control in relationship with companies. Within this context, the present study presents and analyses the influences of the transfer pricing current environment at European level in the case of Romanian companies. Realizing a detailed and deep documentation of the existing scientific literature in this field and using a comparative data analysis lead to the conclusion that the diminishing in impact of these influences may be accomplished by the finding of new solutions by multinational companies through which they should manage accordingly the associated risk of transfer pricing and prevent the eventual misunderstandings with regard to fiscal authorities.*

**Keywords: transfer pricing, fiscal planning, companies, fiscal authorities, fiscal reforms**

## 1. Introduction

The difficult period we are going through has demonstrated that the European fiscal policy must support economy in order to make it functional and competitive globally. Within the negative economic context in which we perform our activity, the ongoing fiscal reforms at European level, to which Romania is a contributor, become even more
important for the stimulus of actions against tax evasion. At the same time, through these reforms, it is necessary to support both companies and fiscal administrations.

Taking into consideration the afore said, the present study aims at presenting in section 2, briefly, the main current issues within EU with an impact on transfer pricing. In Part 3we are discussing the means by which the current environment of transfer pricing within EU influences the companies in Romania. In section 4 of this study the aim is to make aware on the importance of fiscal planning in a company, whose objective is not necessarily to diminish tax payment, but rather a price cut in general. We present our conclusions in part 5, deepening the idea according to which companies must adapt, must find new solutions in order to face changes in the law and some eventual controls with regard to transfer pricing. Another conclusion of this research is the increase of transparency through supplementary reports on the activity of companies in a group. For companies, one solution to manage the transfer pricing risk and to successfully face some eventual controls in this field would be the use of fiscal planning.

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**2. A Presentation of Current Issues from EU with an Impact in the Field of Transfer Pricing**

The main current issues from EU with a direct impact in the field of transfer pricing are the ones related to the BEPS Plan implementation - *(Base erosion and profit shifting),* as well as the implementation of C(C)CTB - *The Common (Consolidated) Corporate Tax Base.*

*Country-by-Country Reporting (CbCR),* included in the BEPS project, launched by OECD and assumed at European level through *Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation* [1],includes aggregated fiscal information on income, profit or loss, reported capital, retained earnings, number of employees and tangible assets, other than cash or cash equivalent. These reports may be used by control authorities in order to select tax payers that will make the object of controls in the field of transfer pricing.

The EU companies are affected by *Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market*(ATAD – The Anti-Tax Avoidance Directive) [2]. This directive establishes "with regard to the international taxation" as extremely necessary for tax to be due at the fiscal administration where profit is generated, respectively, the value added tax. The final purpose is establishing some fiscal equities and prevention of practices against "tax base and transfer pricing erosion".

EU Member States are also affected by *Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements*[3], these pursuing to follow the directive as information exchange on a quarterly basis about the financial accounts held by non-residents, with regard to the individual anticipated fiscal solutions with cross-border application, as well as the reporting demands for each country in part. The information exchange will be performed via a secured central register, drawn and monitored by the European Commission. The main objective of this directive is "improving the internal market functioning by discouraging the use of cross-border means of aggressive fiscal planning". There is a need to note the fact that the new regulations will be applied only to cross-border transactions that may represent fiscal planning methods.

European companies will be affected by the *Directive project on digital economy taxation*, approved by the European Commission in March 2018, and as a result, beginning with 2020, a new fee for digital services (DST) is due with a unique rate of 3% from gross income. This directive has not been adopted yet.

*The common corporate tax base (CCTB) and the common consolidated corporate tax base (CCCTB)*, the new taxation algorithm suggested for the tax on profit owed in EU, as well as the means of reserving the tax base among Member states, will have a huge impact on companies.

The initial project of 2016 would include two suggestions to draw a directive, respectively:

- the directive project regarding a common corporate tax base (CCTB) – pursuing *a unique set of norms related to the tax base calculation on the EU territory*;
- the directive project regarding a common consolidated corporate tax base (CCCTB), having the declared objective of *financial result consolidation at group level*.

The European Parliament issued March 15, 2018 two legal resolutions on the two project directives, as a result of the European Commission suggestions, drafting the simultaneous adoption of CCTB and CCCTB having the aim to ensure "the well-functioning of the internal market", as well as the creation of a more "favourable framework for trade and investment", resistant to "mechanisms of avoiding financial liabilities". The amendments are in analysis, the two project directives having not been approved yet.

The novel elements brought by the two Directives are:

1. *The common corporate tax base of the companies* – unique regulations within EU to establish the manner of taxation for a group of companies' profit;
2. *Headquarters definition* – from EU and the ones belonging to an EU fiscal resident;
3. *Group definition* – setting the need of fiscal consolidation will be performed on basis of a test that will take into calculus control (more than 50% from the rights to vote) and property (over 75% of the social capital);
4. *The manner of reserving profit* – According to factors, considered of equal importance, respectively: work force, assets, and sales;
5. *European budget* – regarding personal resources – EU revenues for 2021-2027, we speak of CCCTB as a new source for the community budget.

Given the above-mentioned conditions, companies must find new solutions in order to deal with legal amendments and some eventual controls related to transfer pricing.

## 3. The Analysis on the Impact of the Current Transfer Pricing Environment at European Level on Romanian companies

The current transfer pricing environment at European level has direct impact on the way companies in Romania approach the transfer pricing problematics.

Romania has operated the amendments of Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in the Fiscal Procedure Code. Once with the entry in force of the National Agency of Fiscal Administration Order no. 3049/2017 regarding the approving of the template and content of the form: *Country by Country Report*, issued as a result of the General Emergency Ordinance no. 42/2017 for the amendment and completion of the Fiscal Procedure Code with regulations on the report for each country in part, the exchange of information between fiscal authorities has been put into practice in Romania.

*The CbC Reports*, introduced by this Order, make it possible for fiscal authorities to be able to draw an analysis of the fiscal and economic involvement of a multinational group in each jurisdiction in which it develops activity.

In addition to what has been stated previously, the control authorities in Romania will be able to use, beginning with the second part of 2020, another means to select the tax payers involved in schemes of fiscal optimization. The Directive 822/2018 introduces the liability *to report cross-border schemes of fiscal optimization* which present certain characteristics. Within local legislation, Romania implemented this directive, internationally known as the *MDR Directive* (Mandatory Disclosure Regime Directive), completing the mechanism of fiscal reporting and the information exchange already existent at EU level [4].

Companies in Romania must have in view to respect the implications of *Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market*(ATAD), provisioning on the implementation of norms concerning: the limitation of interest deductibility, exit tax, controlled foreign companies, the prevention of non-uniform treatment of hybrid elements, and which have been operated in the Fiscal Code beginning with January 1, 2018.

With regard to *the project Directives on the common corporate tax basis (CCTB) and the common consolidated corporate tax* *basis (CCCTB)*, the position stated in GO no. 45/2017[5] is the following:

➢ It supports "the approach, in stages, of fiscal norms for a common consolidated corporate tax base, suggested by the European Commission, but it is reserved with regard to the second stage, taking into consideration the possible impact on national budgetary incomes, considering that some Member States may be disadvantaged by the suggested CCTB norms".

➢ It does not support "regulations and provisions for the facilitation of cross-border trading and the removing of fiscal impediments…" on the internal market, considering them way too difficult.

➢ It supports "stimulants for activities of research and development and a deduction for growth and investment", which might increase EU competitivity.

Briefly, the implications for the companies in Romania would be the following:

- The existence of two parallel legislations; the common corporate tax base will be applied for groups of companies with income above 750 billion Euro, the rest of companies applying the Fiscal Procedure Code;
- For companies that will apply a common corporate tax basis, a major consequence will be that fiscal facilities or stimulants from the Fiscal Procedure Code will be eliminated;
- From transfer pricing perspective, companies will not draw the transfer pricing file for transactions performed with EU sub-holding companies in the group;
- The introduction of the algorithm of tax base reservation among the EU sub-holding companies will have a great impact on the public budget.

Both the advantages and disadvantages of the CCTB/CCCTB implementation should be analysed in order to obtain the insurance that the EU fiscal harmonization plan does not influence us negatively.

## 4. The Role of Fiscal Planning in a Company

Efficient management has as objective profit maximization, which can be achieved by increasing the turnover, cost, tax and fee reduction while respecting legal provisions. For fiscal liability optimization, companies develop their business in areas with fiscal facilities. This development is a *fiscal planning* result, defined as the *financial and economic activity* planning of the company, with a view to minimum diminishing tax payment.

*Fiscal planning* whose objective is not necessarily the reduction of tax payment, but of costs in general, is an element of economic planning [6].

Fiscal planning is determined by the fiscal legislation which establishes different fiscal regimes, different methods of calculating the tax base, fiscal facilities granted to tax payers. It is dependent on the interest of the State in granting facilities to companies, for the social and economic development of some areas. The objective side of fiscal planning has raised from the need that the tax payers' fiscal pressure is reduced and resources are increased in order to sustain competitivity in the field they activate.

Fiscal planning is based on national legislation regulating legal relations between parties, taxes/fees, respectively international treaties and conventions concluded between States.

Below, we present the legislation influences on fiscal planning.

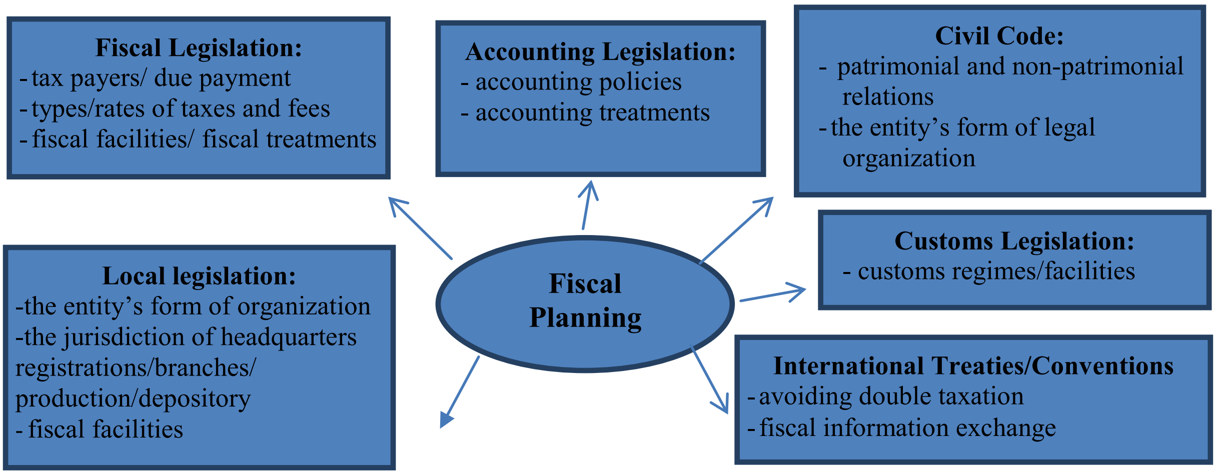


*Figure 1: Legislative framework influencing fiscal planning(Source: elaborated by the authors)*

The stages of fiscal planning depend on the planning objective: fees from actual transactions or the entity's business on the whole. Both the stages and the instruments chosen to be used in fiscal planning are attentively selected by the tax payer, according to the type of activity. In order to succeed in fiscal planning, the following stages need to be proceeded to:

*Table 1: Fiscal planning stages (Source: elaborated by the authors)*

| Stage | Actions specific to the stage |
|---|---|
| **Stages specific to the fiscal strategy of the company** | |
| I | - the idea of business is born, objectives, goals and tasks are formulated, solutions are found to problems regarding the use of fiscal facilities offered by the fiscal legislation |
| II | - most favourable fiscal jurisdictions are chosen, the settlement of holding companies, their branches, production units and depositories |
| III | - the study of the legal framework regarding the matriculation of legal entities, the choice of the legal form of organization of the company |
| **Stages specific to the planning of the current activity of the company** | |
| IV | - according to the fiscal facilities identified in stage I, the company's segments of activity are established, a plan to use the facilities is drawn |
| V | - a system of the company's contractual relations is drawn |
| VI | - the fiscal and financial policy of the company is drafted, an analysis on various fiscal issues that might appear along the activity is performed, eventual losses are prognosed, caused by fines and penalties and are compared with the prognosed financial indicators. |
| VII | - the fiscal evidence of the company is organised, a control is performed on the correctness of calculations and tax payment, procedures of cooperation with control and audit organs are established. |

The fiscal planning instruments most used by companies are [7]:

- *transfer pricing*;
- *fiscal paradises and off-shore zones*

They are judicial entities granting fiscal advantages to companies establishing their head offices or natural persons having the residence on their territory [8].

- *the method of territorial jurisdiction;*
- *the entity's legal form of organization;*
- *the method of accounting and fiscal policies:* accounting transactions with sub-

holding companies lead to the entity's fiscal risk increase, as a result of divergences in accounting principles and fiscal ones [9].Analysing from the perspective of Romanian legislation, we identify three major sources of divergence between the accounting interest and the fiscal one [10], respectively: *tax on profit*, *fixed assets amortization, patrimony evaluation*. Fiscal planning may represent a solution for companies to manage the risk in transfer pricing.

## 5. Conclusions

Given the conditions of global reforms, suggested by EU in the field of taxation on profit, companies must find new solutions in order to face legal amendments.

Transparency will increase through supplementary reports on the activity of the companies in a group, this determining a deeper risk analysis from a fiscal point of view, with regard to the manner of reserving, globally, revenue, profit and taxation.

The use of fiscal planning as an element of economic planning, and not just as an element of cutting on tax payment, may represent a solution for companies to manage the transfer pricing risk and to successfully deal with some eventual controls in this field.

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