Transfer Pricing in V4 Countries

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PREFACE

In recent years transfer pricing has been one of the major topics of international tax discourse. Again, this was well demonstrated by the outcomes of the OECD BEPS Project, for which transfer pricing became one of the building blocks in combatting base erosion and profit shifting. As a tax topic, transfer pricing remains of great interest for taxpayers, tax administrations, tax practitioners and academia. Due to its complexity, as transfer pricing has specific legal, economic, political, social and other dimensions, ongoing discussions between the key stakeholders appear to be a necessity in furthering development in this area. This has been particularly considered in the methodology of the research project that resulted in this monograph, as the research itself was based on very intensive discussions and cooperation among economists, lawyers, tax advisors and tax officials.

Transfer pricing originated as a set of international tax rules regulating business activities of multinational enterprises. The bilateral nature of transfer pricing is therefore one of its essential characteristics, as the final effects of the arm's length principle always impact taxpayers in at least two different tax jurisdictions. Pure unilateral responses to transfer pricing therefore appear ineffective and unable to deliver satisfactory solutions. It is therefore very desirable that research activities in this area be coordinated among different states in order to identify the key elements for further development. In this respect, this monograph provides unique research outcomes that take into consideration specific characteristics of the integrated region of the V4 countries. The Visegrad group countries represent not only a political level of cooperation but also an important business region which is of particular interest to entrepreneurs. As a result, this research project is a much-appreciated contribution to the development of transfer pricing, providing an interesting comparison of four different tax regimes and proposing interesting *de lege ferenda* solutions.

The first part of the monograph addresses the importance of transfer pricing in the international tax system and offers an in-depth review of the bibliography available on the topic. In addition, the authors identify the main focus areas within the worldwide research on transfer pricing and provide an overview of the most important outcomes delivered on the different aspects of transfer pricing. Subsequently the authors describe the chosen methodology together with specification of general and partial aims of the research. The core part of the monograph is introduced by the OECD background to transfer pricing legal regulations and by the EU transfer pricing standards. The monograph then provides a very systematic analysis of the V4 tax jurisdictions. Based on the applied methodology and common internal structure, this part offers a very complex comparison of the respective legal systems, their historical development, the EU legal context and the current transfer pricing regulations.

Based on the above it can be concluded that the aims of the monograph and objectives of the research project have been fulfilled. The presented research outcomes extend discussions on the issue of transfer pricing and focusing on the current legal status in V4 countries provide for a very valuable comparative study of transfer pricing aspects in the selected geographic region. The significance of the monograph is further increased by identifying existing risks and by proposals for *de lege ferenda* considerations. We believe the monograph will raise interest among tax researchers, tax practitioners, tax officials and taxpayers as it provides very sound theoretical grounds for the presented topic and also a very practical tool for comparison of the key structural parts of different transfer pricing regimes. It can also be expected that the presented outcomes will serve as a unique source of inspiration for further research in this interesting and challenging tax area.

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The project proposal would not have been submitted and this monograph would never have come into existence without first, the stimulus and support provided by prof. Ing. Mária Režňáková, CSc. (at that time, Head of the Department of Finance at the Faculty of Business and Management of the Brno University of Technology, currently, vice-rector at the Brno University of Technology). Support has been continually provided by her successor in the position of Head of the Department of Finance, doc. Ing. Vojtěch Bartoš, Ph.D. As a person responsible for the implementation of the project on the part of the grantee of the project, I would like to express my thanks to them.

All the members of the research team would like to express their gratitude to their institutions for their material and financial support connected with this project – namely to the Faculty of Business and Management of the Brno University of Technology (Czech Republic), Faculty of Economics of the Matej Bel University (Slovakia), Kautz Gyula Faculty of Economics of the Széchenyi István University (Hungary), Faculty of Finance and Insurance of the University of Economics in Katowice (Poland) and the DUMA – Dunamenti Adóklaszter (DUMA). In this respect, we reserve a special thank you to the heads of the Faculty of Business and Management of Brno University of Technology and the Faculty of Economics of Matej Bel University where the workshops connected with the project were realised. The information, knowledge and contacts gained therein have been utilised within this monograph preparation. Thus, our special thanks also go to doc. Ing. et Ing. Stanislavav Škapa, Ph.D. (dean of the Faculty of Business and Management) and to doc. Ing. Peter Krištofík, Ph.D. (dean of the Faculty of Economics).

The authors of the monograph express thanks to the remaining members of the research team – namely to Mrs. Mariann Berényi (DUMA) and prof. Ing. Jaroslav Ďaďo, Ph.D. (Faculty of Economics of Matej Bel University) – for their contribution to the execution of the project and for their suggestions and comments which helped us to increase the quality of the monograph. Thank you for sharing your knowledge and experience with us.

As mentioned above, two workshops were realised in connection with the execution of this project. The members of the research team would like to express their gratitude and thanks to all the participants who attended the workshops and were willing to share their experience, knowledge and opinions or even to discover more about one of the hottest tax issues in the world – transfer pricing. The ideas presented there have been of great value for the monograph. The list of all the participants and the time schedules of the workshops can be found in Annex of this monograph.

We declare our separate thanks for the realised presentations to Mr. Daniel Szmaragowvski (KPMG, the Czech Republic); Mr. Vítězslav Kapoun (General Financial Directorate, the Czech Republic); Mr. Michal Jelínek (V4 Group – Tax, Audit & Legal Advisory Group, the Czech Republic); Mrs. Veronika Solilová and Mrs. Danuše Nerudová (Mendel University in Brno, the Czech Republic), Mrs. Zuzana Svinčáková (Tax Office for Selected Tax Subjects, Slovakia); Mrs. Dana Slivková (Financial Directorate of the Slovak Republic, Slovakia); Mr. Branislav Kováč and Mrs. Frederika Silesky (VGD Slovakia, s. r. o., Slovakia), Mr. Michal Kočiš (Kočiš & Partners, s. r. o., Law Firm, Slovakia) and to Mr. Adam Čiffáry (CLIA Agentúra s. r. o., Slovakia).

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And last, but not least, the members of the research team would like to express thanks to their families for their support and tolerance during a period where the team members had less time to spend with them. Thank you!

On behalf of the members of the research team
Karel Brychta

SUPPORTER OF THE PROJECT

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STATEMENT

This monograph presents the results of the scientific cooperation between the Brno University of Technology, Faculty of Business and Management (Czech Republic), DUMA – Dunamenti Adósklaszter (Hungary), Széchenyi István University, Kautz Gyula Faculty of Economics (Hungary), University of Economics in Katowice, College of Finance (Poland) and Matej Bel Univeristy in Banská Bystrica, Faculty of Economics (Slovakia).

The authors of the monograph would like to stress that they take full responsibility for the quality of the texts and that the opinions expressed within them are attributable only to them and not to the institutions in which they are engaged.

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LIST OF ABRREVIATIONS

ALP	Arm´s Length Principle
APA	Advanced Pricing Agreements
Art.	Article
BAPA	Bilateral Advance Pricing Agreement
BEPS	Base Erosion and Profit Shifting
CbCR	Country by Country Report
CCA	Cost Contribution Arrangements
CFC	Controlled Foreign Corporation
CIT	Corporate Income Tax
Coll.	Collection of laws
CP/ C+	Cost Plus Method
CUP	Comparable Uncontrolled Price Method
CZK	Czech crown
DAC	Directive on Administrative Cooperation or its amendment
DTT	Double Tax Treaty
e. g.	exempli gratia (for example, for instance)
EATLP	European Association of Tax Law Professors
EBIT	Earnings Before Interest and Taxes
EC	European Commission
ECJ	European Court of Justice
EEC	European Economic Community
et al.	et alli (and others)
et seq.	et sequentia (and the following)
etc.	et cetera (and other similar things)
EU	European Union
EUR/€	Euro
FDI	Foreign Direct Investments
G20	Group of twenty
GER	Germany
HTVI	Hard-to-Value Intangibles
HUF	Hungarian Forint
i.e.	id est (that is)
IAS	International Accounting Standards
ITPJ	International Transfer Pricing Journal
JTPF	Joint Transfer Pricing Forum
MAP	Mutual Agreement Procedure
MF	Ministry of Finance
MLI	multirateral Instrument
MNCs	multinational companies
MNEs	multinational enterprises
MNFs	multinational firms
No./Nr.	number
OECD	Organization for Economic Cooperation and Development
OEEC	Organization for European Economic Cooperation
p.	page
par.	paragraph
paras	paragraphs
PATA	Pacific Association of Tax Administrators
PIT	Personal Income Tax
PLN	Polish zloty
pp.	pages

PS/PSM	Profit Split Method
R&D	Research and Development
RP/RPM	Resale Price Method
RVHP	Rada vzájemné hospodářské pomoci [Council for Mutual Economic Cooperation]
SMEs	Small and Medium Sized Enterprises
TEU	Treaty on European Union
TFEU	Treaty on Functioning of the European Union
TNMM	Transactional Net Margin Method
TP	Transfer Price/Transfer Pricing
U. K.	United Kingdom
U. S.	United States
V4	Visegrad Group Countries (Czech Republic, Hungary, Poland and Slovakia)
VAT	Value Added Tax

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INTRODUCTION

The problems which had to be addressed within the tax system in the first half of the last century are significantly different to those that must be addressed today. A growing number of complex problems have resulted from many mutually reinforcing factors – in general, one can speak of the effects of social change (Ivorra et al, 2011). The world has become, as accurately noted by Owens (1993), a small place – changes have made the world smaller in terms of space and time (Kubatova, Vancurova and Foltysova, 2008). Russo et al. (2007, p. 1) describes the situation as the following, *"Economic activities have never been as global as they are today. National borders in international trade have faded, the global integration of national economies deepens, the mobility of capital accelerates and growth in international capital flows and trade is massive. This growth has, is and will contribute to boost the mobility of economic activities around the globe and this has created not only opportunities but also problems for the players of the world economy."* On the other hand, it is true that due to war and business conflicts between states there are some protectionism tendencies and measures[1]. However, a removal of business and other barriers between states seems to be a typical feature of the world these days, which is widely supported by the international community (see for example WTO, 2019). The removal of these barriers is not connected with positive results only. That is to say, a release or even absence of the barriers for economic activities realised in the territory of other states and the existence of a different set of rules in particular states are causing (or are capable to cause) a number of related problems connected with taxation of incomes and property including base erosions and profit shifting.

Without rapid change, the tax systems which were established in the second half of the last century are not capable to face the challenges of social realities (for more details see for examples OECD, 2018; OECD, 2019a). This conclusion can be made by a "mere" comparison of the attributes of the previous and current social realities (see Table 1 below).

Table 1: Changes in the attributes of the environment (selected aspects relevant from the view of taxation)

Category	Pre 1990s	Post 1990s
International Business Activities	• restricted and controlled significantly	• liberated • pressure for another liberation • growing volume of provided services (huge problem with the allocation of profits related to them)
Capital	• an easy (or better to say easier) identification of the capital origin • restricted movement of capital • low volumes of capital	• more difficult identification of the capital origin • movement of the capital globally • huge volumes of capital
Travelling costs	• relatively high	• a decrease in the amount of travelling costs (along with a considerable decrease in the time necessary for reaching the destination) • growing level of transport services (negative impact on the environment)
Information	• restricted quantity • restricted availability • high price	• growing quantity of information along with decreasing price (currently, the information overload and their processing are the problems which shall be faced in relation to information) • a positive impact of the information technologies development on the availability and price of the information

1 There are, on the other hand, some countries, branches and situations, for which protectionism is desirable. For some details see e. g. Rozehnalová (2006, pp. 25–26).

Category	Pre 1990s	Post 1990s
Multinational Enterprises	• absence, or better to say limited number of multinational enterprises – the companies operated, as a rule, within one jurisdiction* (in this respect, there were a number of exceptions)	• relatively high number of economically strong multinational enterprises** • very problematic from the point of international taxation (above all, the issue of transfer pricing is involved)
Labour force	• low mobility (however, there were some migration flows)	• high mobility (especially for some categories of employees) • for some occupations, there is no need for a physical presence at the workplace
Administrative cooperation between states in tax issues	• there was a limited one as it was not considered necessary	• essential to secure the fulfilment of relevant duties on the part of the taxpayers (unilateral measures are not sufficient these days) and essential for the fight against tax avoidance and tax evasion

* The states, while observing the protection of their markets, burdened imports with high tariffs, or restricted international trade to protect their producers in other ways. Some companies have responded by setting up a "branch" of their company in the territory of the respective states.

** Some multinational enterprises have been disposing with a huge negotiating power based on their economic strength; some of them have a turnover higher than the amount of GDP reached by some developed countries (see e. g. Ventura, 2019).

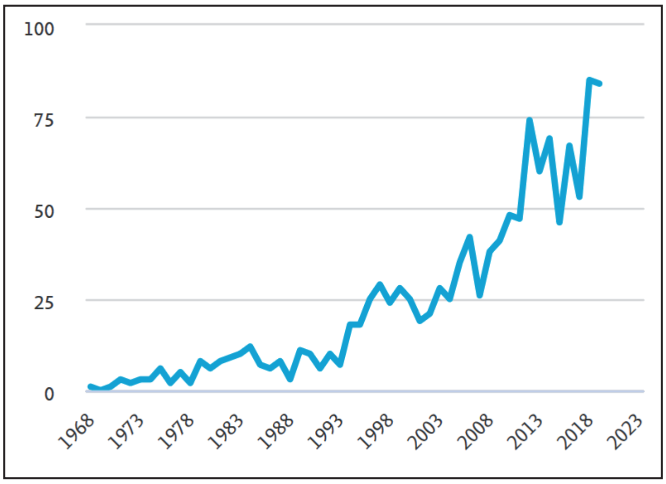
Source: own elaboration based on Tanzi (1996, 2001).

The fact that the current tax systems are not corresponding to social realities has significantly contributed to the problems facing public finances. It has naturally provoked the efforts of not only the states, but also of the international community, to eliminate negative phenomena such as tax avoidance, tax evasions and aggressive tax planning[2] by adopting adequate changes in tax systems in order to reach a fair allocation of tax bases and fair taxation. In this respect, special attention has been granted to transfer pricing, which is understood, as the expert literature suggest, as a profit shifting technique (for relevant aspects see e. g. Tanzi, 2001; Devereux and Keuschnigg, 2008; Elitzur and Mintz, 1996; Chugan, 2007; Auerbach, et al., 2017; Ištok and Kanderová, 2019 and Ištok et al., 2019).

Transfer pricing and the setting of transfer prices in harmony with the arm's length principle have been considered one of the most discussed and problematic tax issues not only in relation to transactions with an international element, but also for purely domestic controlled transactions (see for example Tax Justice Network, 2020; Nerudová and Solilová, 2018). The complexity and growing importance of this topic can be demonstrated by many factors. The growing number of publications dealing with the issue of transfer pricing can be considered as one of them. Transfer pricing represents a complex social phenomenon as proven by the growing number of articles published in world-wide recognized science databases (e. g. see the development of the number of articles published in the Scopus database as presented in Figure 1 below).

2 In the European Union, the estimates of the sum being lost due to tax evasion and avoidance has gone up to € 1 trillion (European Commission, 2019a).

Figure 1: Development of the numbers of articles dealing with transfer pricing in the Scopus database within the period 1968–2019 (key words: Transfer Pricing, Transfer Prices, Transfer Price, Arm's Length Principle)



Source: own elaboration based on Scopus (2020).

The relevance and topicality of transfer pricing can be supported by many other factors; some of them are stated in the list as such:

a) Transfer pricing has been the focus of three action plans of the OECD against BEPS (*Base Erosion and Profit Shifting*), namely action plans 8–10 (OECD, 2019a).
b) There is a special unit established for transfer pricing within the OECD Centre for Tax Policy and Administration, namely OECD Transfer Pricing Unit (OECD, 2019b).
c) There is an established special advisory body for transfer pricing within the European Commission, namely *Joint Transfer Pricing Forum* (European Commission, 2019b).
d) The subject of transfer pricing is very often under investigation by big consulting companies (e. g. Ernst & Young, 2019; KMPG, 2016; Delloite, 2019), which definitely supports the conclusion about the topicality and complexity of the issue.
e) There are specialised research centres dealing with the issue of transfer pricing (e. g. WU Transfer Pricing Center (Vienna University, 2020)).
f) There are specialised conferences and workshops for transfer pricing and related problems.
g) There are specialised departments and professionals for transfer pricing within the financial authorities.

There is another aspect which is worth mentioning in relation to transfer pricing and which pleads in favour of the urgency of transfer pricing and application of the arm's length principle. There is not another globally accepted measure which would play the same role and, at the same time, would be easier for the application and enforcement. In this respect, the European Union has made almost no progress in the adoption of the Common Consolidated Corporate Tax Base, which can be considered as a tool that could replace transfer pricing (for more details to the topic see (European Commission, 2020)).

The aim of the monograph is to extend the discussion on the issue of transfer pricing, focusing on the situation in V4 countries; namely to provide a comparative study of the legal regulation of transfer pricing issues in V4 countries, to identify the existing risks and shortcomings in legal regulation governing transfer pricing in particular V4 countries and to present *de lege ferenda* considerations. The monograph consists of two basic parts: conceptual and empirical. The first part provides the theoretical foundations of transfer pricing, by referring to general ideas behind transfer pricing, transfer pricing as a profit shifting technique, economic and legal perspectives of transfer pricing, as well as other areas connected with transfer pricing such as comparability analysis, transfer pricing documentation, advanced pricing agreements and the issue of safe harbours. The second part of the monograph presents the result of the empirical investigation that was designed to address the following aims:

a) To summarise and present existing rules as included in the OECD and EU standards to provide a background for the description of how particular countries responded to them;
b) To describe the relationships between EU, international and domestic law in particular countries;

c) To provide a list of the legal acts/regulations governing transfer pricing, also showing the areas which are covered in these legal acts/regulations;
d) To give and evaluate the definitions of the key terms and features related to transfer pricing (principally the definition of associated persons/related parties as included in domestic law and as included in Double Tax Treaties in which a particular country has been a contracting party);
e) To identify the platforms of the rules (concepts) as included under Art. 9 of Double Tax Treaties (DTTs) in which a particular country has been a contracting party and to determine which is the prevailing one;
f) To identify and compare the rules for particular areas of transfer pricing law, namely the rules regarding:
   - transfer pricing methods;
   - comparability analysis/compliance analysis obligation;
   - administrative approaches to avoiding and resolving transfer pricing disputes;
   - transfer pricing documentation;
   - special considerations for intangibles, intra-group services and cost contribution arrangements;
   - advanced pricing agreements;
   - penalties connected with breaching transfer pricing rules and
   - additional obligations related to transfer pricing (e.g., those of additional statements and their forms);
g) To identify relevant domestic transfer pricing case law and the conclusions stated therein;
h) To provide a summary of the fundamental oversights in current legal regulations and
i) To present *de lege ferenda* considerations for the material and procedural law in particular countries.

In the conceptual part of the monograph, the authors provide a literature overview for the issue of transfer pricing, a description of the design of empirical investigations and an overview of the basic standards as set by the OECD and EU. These parts of the monograph create a background for the empirical part which deals, among others, with the way the V4 countries adopted these standards. The empirical part of the monograph consists of the chapters dealing with the legal regulation of transfer pricing in particular V4 countries. These chapters also include a basic summary of the case-law related to transfer pricing issues and the identified problems and inadequacies in the legal regulations. The sequence of the countries in the text is as follows: the Czech Republic, Hungary, Poland and Slovakia. This alphabetical order of the countries is also observed also within subsequent chapters and subchapters. In the following chapter a comparison of transfer pricing regulations in the V4 countries is presented. The next chapter comprises the policy implications for transfer pricing legal regulation for V4 countries. The final chapter provides a summary.

The monograph may be useful both for researchers and academicians, as well as tax authorities and taxpayers both within and outside the V4 region.

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CHAPTER 1
THEORETICAL FOUNDATIONS

1.1 TRANSFER PRICING – GENERAL OVERVIEW OF THE PROBLEM

The first scientific and professional articles focused on transfer pricing began to appear at the beginning of the 1950s (Coelho, 2000). Padhi (2019) states that the first concept of transfer pricing (TP) was revealed during the 1940s and the first models were developed during the ´70s and ´80s. The arm's length principle, which was established as a rule against manipulating transfer prices (and ultimately, therefore, manipulating the volume of the tax base), represents the key pillar of transfer pricing rules and the standard that has been used in the international tax field since 1933, namely thanks to Carroll Report. However, the arm's length principle was first mentioned many years before 1933, even during the Double Tax Treaty among US and France. The principle was incorporated into international taxation law through the League of Nations Draft Convention on the Allocation of Profits and Property of International Enterprises in 1933 and by the first OECD Model Convention Draft Tax Treaty (1963) with the same wording as the London Model (1946). At the end of ´60s (in 1968) the US Treasury issued regulations for specific types of intercompany transactions, later known as US TP regulations. This action was the motivation for the OECD to publish a guideline on transfer pricing issues. The first TP report was published in 1979 and was followed by others whose first combined publication in 1995 is known as the OECD Transfer Pricing Guidelines (Solilová and Nerudová, 2018 and 2019; Solilová and Steindl, 2013).

Some of the first authors who studied transfer pricing behaviour were Copithorne (1971) and Horst (1971). There has been a sharp increase in interest in this area in recent years due to the many changes both on a national and international level. As for the literature overview, over 300 scientific and professional papers have been studied to provide a background for the realized research. One can conclude, similar to Brada and Buss (2009) that newer and older literature deals mainly with the following areas:

- general problems of central settings of transfer pricing;
- the use of transfer pricing among associated persons (mainly by multinational enterprises (MNEs) having affiliates located in many jurisdictions with a different tax burden);
- transfer pricing as a profit-shifting technique;
- economic aspects (often focused on the preference of TP systems – centralised or decentralised and the optimisation of TP with respect to taxes and other criteria);
- legal regulation;
- general rules and procedures of the arm's length principle, comparability analysis, transfer pricing methods, transfer pricing documentation, three types of advance pricing agreements; and
- *de lege ferenda* proposals.

While most of the attention is devoted to legal regulation of transfer pricing together with the use of transfer pricing as a profit-shifting technique, only relatively few authors provide also *de lege ferenda* proposals on how to currently improve the functionality of transfer pricing systems in selected jurisdictions and at an international level.

Singh (2016) states that TP is currently one of the most widely debated topics among professionals and tax authorities. Transfer pricing rules regulate the prices charged in intercompany transactions for tax purposes. The main goal is to maintain the arm's length principle (Ylönen and Teivainen, 2017). If the arm´s length principle is not followed, then the price determined by the sale of associated parties is shown using an unreasonable price in the sense that the price may be raised or lowered for tax purposes.

According to Kaur (2013), there are four main reasons why companies use transfer pricing: tax savings, facilitating performance measurements, providing relevant information for trade off decisions and inducing goal congruent decisions. Killaly (2000) states that compliance assurance in relation to transfer pricing has proved to be a multifaceted exercise.

According to Cecchini, Leitch and Strobel (2013), transfer pricing stands at the heart of an MNE management control system. They state that setting transfer pricing policy is indeed a complex problem that includes many factors and has many consequences. Based on this, MNE must make strategic and tactical decisions in order to coordinate their intra-organisational value chain activities. Göx (2000) analyses transfer pricing as a strategic device in a divisionalised organisation facing duopolistic price competition. His paper analysed conditions under which the choice of absorption costing is a dominant strategy. Oyelere and Turner (2000) find transfer pricing as one of the most important issues in the strategic and operational management practices of large business operations. The results of their exploratory survey focus on banks and building societies and reveal that the achievement of overall corporate goals is the highest ranked transfer pricing objective. Dean, Feucht and Smith (2008) focus on the role of internal auditors in using transfer pricing as a tool for corporation taxation strategies. On the other hand, the authors emphasize the importance of following the general rules as in the use of the arm's length principle, choosing correct transfer pricing methods and having the proper transfer documentation worked-out. Shor and Chen (2009) show by using the Cournot model that firms can use transfer prices strategically as a collusive device. They further demonstrate how transfer prices can be used as a collusive mechanism to affect competition and thus welfare beyond one single firm (and partially explain the popularity of decentralisation).

Melnyk (2017) provides an overview of transfer pricing risks, their classification, types and possible sources of their occurrence. The adoption of a transfer pricing strategy is associated with three basic principles – following the company's goal, staying within the law and complying with the concept of corporate social responsibility. Multinational corporations are under increasing pressure to adhere to regulation on transfer pricing. Because of this, tax risk management plays a considerable role in transfer pricing strategy and decision making for firms today (Rossing, Cools and Rohde, 2017). Bãndoi, Dãnciulescu and Tomitã (2008) formulate four main reasons why companies should be very careful when considering their risk management strategies. The first one is the approach of financial administrations when their vigilance increases and yet more and more documents are required. The second reason is that the views of tax authorities in various countries differ increasingly. Although most of these authorities adhere to the principles of the OECD, the interpretations of these principles vary greatly. The third reason is related to the novelty of the subject in the legislation of some nations, which can cause uncertainty, but at the same time affect the trust of contributors in the manner in which the competent authority tries to resolve the problem of double taxation. The last reason mainly regards the case of multinational companies, which are often under higher pressure and a large dose of suspicion. They typically are under more rigorous controls and a more detailed assessment of the rules related to certain tax with positions that aren't extremely clearly defined. Companies are therefore forced to invest more time and effort to deal with problems in terms of the risk related to the emergence of a disconnect between taxpayer and tax authorities.

Bulana (2015) focuses on tax risks caused by methodological differences between customs valuations and transfer pricing of controlled transactions.

McGee (2010) highlights that most papers focused on transfer pricing deal either with the technical aspects of the topic or with strategy. The ethical aspects of transfer pricing are almost totally absent from the business literature and is scantly covered in the ethics literature. The study of Pendse (2012) finds that the non-tax outlook for transfer pricing is very strong and, in some cases, so compelling that it affects transfer pricing strategy. This study further finds various issues other than tax liability management which the multinational companies (MNC) must attend with while deciding their related party pricing strategy. Solilová and Nerudová (2013) created their general model with focus on transfer pricing, under which the MNEs could decide the best business model within the frame of tax planning, but which would also enable the quantifying of the impacts on the state budget resulting from that tax planning strategy. According to Li and Ferreira (2007), transfer pricing decisions and methods are not bound exclusively to MNCs, but the MNCs may encounter more difficulties in transfer pricing than their domestic counterparts. They further highlight the importance of transfer pricing as a key strategic dimension to understanding intra-firm flows and their associated costs. Buus and Brada (2010a) summarised the newer and older literature on transfer pricing, dividing into 5 main categories: the general problems of central setting of the transfer price; preference of the system of transfer pricing (centralised or decentralised); impact of information asymmetry and managers' compensation; optimization of transfer pricing with respect to taxes and other criteria and regulation of transfer pricing.

Martin and Sayrak (2003) define transfer pricing as the imposition of the price if a segment of the company provides goods or services to other segments from the same enterprise. Bernard, Jensen and Schott (2006) in addition to goods and services points also to the implied prices of intangible assets between the companies with a special relationship. A particular transaction is a transfer of resources, services or liabilities between associated parties regardless of the price charged (Di Carlo, 2014).

Behrens, Peralta and Picard (2008) studied the choice of structure and location of firms under the alternative transfer pricing rules for different taxation and transport cost levels. They find that firms that operate as exporters use an arm´s length relationship with an independent foreign firm generating double marginalization.

Transfer pricing is still more and more present in scientific research (mainly, but not only as a profit-shifting technique) linked with corporate governance (e.g. Sekhar, 2013 or Ohnuma and Sakurada, 2017) and corporate social responsibility (e.g. Hasan et al., 2019). Bateman (2007) presents an ethical decision-making model for transfer pricing application. Mei and Li (2015) investigate transfer pricing-based money laundering in barter trades and provide an overview of the methods against trade-based money laundering.

As suggested by the results of carried out research, there are many references to transfer pricing as a technique related to profit-shifting. That is not surprising, even the OECD deals with transfer pricing in its three actions aimed against base erosion and profit shifting to establish rules which should avoid, or better to say eliminate, this phenomenom.

1.2 TRANSFER PRICING AS PROFIT SHIFTING TECHNIQUE

Transfer pricing is one strategy used by companies to erode their corporate tax base in high tax countries (Devereux and Keuschnigg, 2008). Hanlon and Heitzman (2010) state that there are four main areas of research and literature regarding tax research: a) corporate tax avoidance; b) the informational role of income tax expense reported for financial accounting; c) corporate decision-making including investment, capital structure and organizational form; and d) taxes and asset pricing. Among the remaining two profit-shifting channels they include debt (interest expenses as tax deductible expenses) and the location of intangible assets. The same classification of aggressive tax planning channels is provided also by the European Commission (2019b). This classification is focused on the economic substance of aggressive tax planning structures as identified in the Ramboll and Corit (2015) and ZEW (2016) studies. The aggressive tax channels are divided into the following three groups:

a) aggressive tax planning via interest payments,
b) aggressive tax planning via royalty payments, and
c) aggressive tax planning via strategic transfer pricing.

Nugroho, Wicaksono and Utami (2018) state that tax motivation is one of the reasons companies partake in transfer pricing by making the transaction to an associated company. Gordon and MacKie-Mason (1994) focus on income shifting, both on national (between personal and corporate tax bases) and international level (transfer pricing). According to Chan, Lo and Mo (2015), tax officials find transfer pricing the most common form of tax avoidance by multinational companies.

Transfer pricing systems in multidivisional firms focus on the maximisation of divisional income, leading the divisions to achieve their goals through sub-optimisation. Clempner and Poznyak (2018) consider that the implementation of transfer pricing models for global profit maximisation represents a fundamental opportunity that must be seriously considered by large-scale multidivisional firms. According to many authors (e.g. Elitzur and Mintz, 1996; Chugan, 2007 and Auerbach, et al., 2017), transfer pricing belongs to one of the three most significant profit-shifting channels under existing tax systems together with the use of debt and location of intangible assets. Gnerre (2015) provides a new diagnosis (anti-avoidance) approach in the corporate policies of transfer pricing. Melnychenko, Pugachevska and Kasianok (2017) consider transfer pricing as a significant profit shifting channel, primarily in connection with low tax jurisdictions. Their paper focuses on the tax inspection of prices in controlled operations and on the current situation in Ukraine. The obtained results of an analysis performed by Clausing (2000) on U.S. data indicate a clear relationship between taxes and intra-firm trade flows. Her additional evidence indicates that trade between the U. S. affiliates in different foreign countries is also likely influenced by tax considerations. The paper of Kaur and Kaur (2015) examines the various strategies used by companies to manipulate taxes through transfer pricing. These authors also provide the study, which examines the various court cases related to transfer pricing. Transfer pricing is attractive because it is largely invisible to the public and is difficult and expensive for regulatory authorities to detect. Tran, Groson and Seldon (2016) state that theory predicts that for a wholly owned subsidiary, transfer prices should be responsive to the tax-tariff differential. The results of Brada and Buus (2009) suggest that the tax base of a whole MNE depends on the ownership structure of companies contained within the MNE, which could be described quite simply in a simply matrix form.

The findings of Blouin, Robinson and Seidman (2017) suggest that MNEs might decrease their aggregate tax burdens by increasing coordination within the firm or that governments might increase their aggregate revenues by improving coordination of their enforcement across tax authorities and further document, in a specific setting, how coordination influences MNEs´ reporting behaviour.

There are many investigations which combine the behaviour of (not only) MNEs in misusing transfer pricing as profit-shifting techniques. E.g. Choi, Furusawa and Ishikawa (2018) focus on cost plus and comparable uncontrolled price methods as two alternative implementations of the arm's length principle that mitigate against the problem of internal price manipulation. They further develop a novel theory of vertical foreclosure as an equilibrium outcome of strategic transfer pricing. Finally, they state that imposing the arm´s length principle without high-quality monitoring in place can be counterproductive. Swenson (2000) states that TP represents one potential avenue for income shifting, but her evidence from trade transaction prices suggests that the manipulation of product transfer prices is not generally responsible for large movements in reported income.

As we already stated, the use of transfer pricing as a profit-shifting tool is the subject of research that occurs very often between academics and professionals. The following Table 2 contains a list of selected investigations within this context.

Table 2: List of selected research papers with focus on transfer pricing as profit-shifting technique

Year	Author(s)	Title of the paper
1997	Limberg, Robinson, Christians	International transfer pricing strategies for minimizing global income taxes
1999	Koenigsberg	Multinational firm decision making in the presence of enforceable TP regulations
1999	Mansori and Weichenrieder	Tax Competition and Transfer Pricing Disputes
2003	Eden	The internationalization benefits of transfer price manipulation
2004	Shangina and Vieira	Transfer Pricing and Tax Havens for Attracting FDI
2004	Choe and Hyde	Keeping Two Sets of Books: The Relationship between Tax & Incentive TP
2008	Wang and Wang	Brand proliferation and inter-brand competition: The strategic role of TP
2010	Sikka and Willmott	The dark side of TP: Its role in tax avoidance and wealth retentiveness
2010	Buus and Brada	Searching for Potential Tax-Evasive TP in Multinational Enterprises: A Mathematical Approach
2011	Jarallah and Kamazaki	A review of empirical studies on transfer pricing manipulation
2013	Shunko, Debo and Gavirneni	Transfer Pricing and Sourcing Strategies for Multinational Firms
2014	Vargas-Hernández	Income Distribution in Multinational Firms through Transfer Pricing
2015	Rathke	TP manipulation, tax penalty cost and the impact of foreign profit taxation
2015	Vicard	Profit Shifting Through TP: Evidence from French Firm Level Trade Data
2016	Cristea and Nguyen	TP by multinational firms: New evidence from foreign firm ownership
2016	Christian and Zdanowicz	State corporate tax implications of abnormal transfer-pricing by U.S. com.
2017	Talab, Flayyih and Yassir	TP and its effect on financial reporting: A theoretical analysis of global tax in multinational companies
2018	Agana, Mohammed, Zamore	International TP and Income Shifting in Developing Countries: Evidence from Ghana
2018	Beebeejaun	The Efficiency of TP Rules as a Corrective Mechanism of Income Tax Avoidance
2018	Davies et al.	Knocking on Tax Haven's Door: Multinational Firms and Transfer Pricing
2018	Richardson, Taylor and Alhadi	Income Shifting Arrangements, Audit Specialization and Uncertain Tax Benefits: An Empirical Analysis of U.S. Multinational Firms

Year	Author(s)	Title of the paper
2018	Taylor, Richardson, Al-Hadi	Uncertain tax benefits, international tax risk, and audit specialization: Evidence from US multinational firms
2019	Rathke	Fuzzy Profit Shifting: A Model for Optimal Tax-induced Transfer Pricing with Fuzzy Arm's Length Parameter

Source: own elaboration.

Koethenbuerger, Mardan and Stimmelmayr (2018) analyse contrasts that exist in literature where transfer pricing incentives are insulated from investment incentives and transfer pricing induces inefficiently low taxes. Ma (2017) finds that cross-country differences in corporate tax rates and product intangibility play an important role in affecting firms' internalization decision.

Gupta (2018) suggest that that the OECD's recent transfer pricing guideline amendments and BEPS action plans (8-10) are considered as the benchmark and will prevent companies reducing their tax burden by using artificial transactions between associated parties that would not normally occur between independent parties. The aim of the analysis is also to determine how MNCs follow commercial principles to adjust tax liability through intangible asset grouping structures and risk allocation techniques. The results of the Indriaswari and Aprilia (2017) study show that tax and tunnelling incentives have significant influence on transfer pricing, while bonus mechanism does not have a significant influence on transfer pricing. According to Dumiter and Boiță (2017), the efforts in recent decades to change the legislative framework in order to eliminate double taxation in cross-border transactions have led also to double taxation. The BEPS project introduced by coordinated action of member states is considered more effective than unilateral action. The authors are of the opinion that the whole transfer pricing framework at both national and international levels requires considerable improvements. Sari and Hunar (2015) analyse how Starbucks Corporation uses transfer pricing to minimise their tax bill and provide a brief analysis of BEPS action plans.

Tax optimization means lowering the costs of the company and thus, in an economic sense, it represents a way for increasing the value of the company. Thus, transfer pricing mobilises the interest also from the perspective of the economics.

1.3 ECONOMIC OUTLOOK AT TRANSFER PRICING

There is a rich amount of literature on economic models and mathematical models regarding transfer pricing issues (e.g. Alles and Datar, 1998; Vidal and Goetschalckx, 2001; Chang, Cheng and Trotman 2008; Diewert, Alterman and Eden, 2011; Leng and Parlar, 2012; Liu, Zhang and Tang, 2015 or Grundel et al., 2018). Buus and Brada (2007) focus on the problem of transfer pricing mathematical modelling methodology. Buus and Brada (2008) further state that older and more recent literature on transfer pricing are not unified on whether the optimal transfer price should be equal to the marginal cost of the supplying company and set by a centralised decision maker (headquarters of multi-business company) or whether it should be set by negotiations or even set on the level of market price. Falvey and Fried (1986) examine the interaction between national ownership requirements and transfer pricing.

Arnold, Elsinger and Rankin (2016) investigate how a headquarters involvement affects the efficiency of decentralised transfer price negotiations. They find that efficiency is increasingly reduced when a headquarters involvement is strong rather than weak. Baldenius (2000) finds that negotiated transfer prices generally achieve higher expected contribution margins, as this method tends to be more efficient in aggregating private information into a single transfer price. Clempner (2018) suggests an approach for solving the transfer pricing problem, where negotiation between divisions is carried out with consideration to the manipulation game theory model for a multidivisional firm.

Li and Balachandran (2000) state that under a separate management and ownership assumption, transfer pricing is at minimum a three-person problem involving one principal and two agents. Van der Meer-Koistra (1994) examines the functioning of transfer pricing systems in the organisational context.

The study of Chang and Ryu (2013) focuses on determining the key factors that affect a firm's optimal transfer pricing policy (the vertical structure, production technology, the demand characteristics and the competition mode). Chong et al. (2018) examine two control mechanisms - leadership tone (informal control) and performance evaluation schemes (formal control) that companies can use to manage transfer pricing negotiations. Chwolka, Martini and Simons (2010) analyse the potential of one-step transfer prices based on either variable or full costs for coordinating decentralised production and quality-improving investment decisions.

Lutz (2012) presents a theoretical derivation of how multinational enterprise and equity risk premium can be calculated simultaneously under generated conditions and an application example e.g. in the automobile industry. Chan, Landry and Jalbert (2004) examine the effects of exchange rates on international transfer pricing decision. The authors often focus their investigations on interacting supply chain distortions (e.g. Arya and Mittendorf, 2006) and on transfer pricing supply chain in manufacturing sector (e.g. Seppälä, Kenney and Ali-Yrkkö, 2014). Komoriya, Furusawa and Mukunoki (2007) tackle an investigation on the effects of firm heterogeneity on transfer prices.

Dziwok (2016) presents the role of funds transfer pricing in the liquidity management process of a commercial bank and their application to estimate the costs and benefits of liquidity.

Dai (2010) formulates three motives of multinational corporations to use transfer price strategies: evading tax, dodging risk and adjusting the flow of internal funds to gain competitive advantages. Niu et al. (2018) consider a chain-to-chain competition model and they formulate multinational firms' trade-off between global tax-planning gains (via transfer pricing) and channel decentralisation loss.

The book of Eden (2019) covers the topic of TP in relation to divisionalisation, government regulations, bargaining models, market distortions and product characteristics as well as touching on the important subjects of empirical estimates of transfer price manipulation and transfer mispricing estimates. Padhi (2019) provides an overview of various theoretical models that have been developed to address the transfer pricing complexities and the empirical studies that have been made to understand the transfer pricing practices in MNEs in the last six decades.

Models and their changes are naturally connected with the development of the legal regulations of transfer pricing and related areas. The changes in legal regulation cannot be surprising since the law has to address changes in social reality.

1.4 LEGAL REGULATIONS OF TRANSFER PRICING

Dumiter and Boiță (2017) provide the historical overview on TP legal regulation adoption in many countries. They state that the US government introduced specific legislation on TP at the end of the 1960s, but TP was not a hot topic for the IRS until the 1980s. As the adoption of TP regulation is a gradual process, they worked out a list in selected jurisdictions and based on the period of adoption, they further created categorisation of jurisdictions.

As for the current TP legal regulation updates and news in different countries and areas, the International Transfer Pricing Journal (ITPJ) can be considered as a very useful source. This journal publishes papers from this field on a regular basis. The IBFD Publishing House, which is regularly updated, can be considered another important source of transfer pricing legal framework.

Many authors describe the legal regulations of transfer pricing in selected jurisdictions and very often with a focus on a specific sector. The table 3 contains the collection of selected investigations in this context.

Table 3: Overview of selected research papers with focus on TP legal regulation

Year	Author(s)	Jurisdiction(s)	Sector(s) or field(s)
1997	Borkowski	Japan and USA	General overview
1997	Limberg, Robinson and Christians	Brazil	General overview and OECD guidelines
2002	Barry	Ireland	TP and R&D
2008	Zsíros	Hungary	General overview
2008	Abu-Serdaneh, Al-Okdeh and Gauher	Jordan	General overview (manufacturing firms)

Year	Author(s)	Jurisdiction(s)	Sector(s) or field(s)
2010	Solilová and Lobotková	Czech Republic	General overview
2010	Solilová	EU countries	General overview
2010	Boulogne	Netherlands and USA	Intangibles
2011	Loncar, Golemac and Vidak	Croatia	Banking industry
2011	Abdellatif	Egypt	TP methods, documentation and APA
2011	Krever and Zhang	Australia	General overview and OECD Guidelines
2011	Gill	India	General overview
2011	Devonshire-Ellis, Scott and Woollard	China	General overview
2014	Lee et al.	South Korea	Related-party transactions, financial statement comparability
2015	Bulana	Ukraine	TP methods and TP control
2015	Kočiš	Slovakia	General overview and OECD Guidelines
2015	Smith	Nigeria	General overview, business restructuring
2016	Harmse and van der Zwan	South Africa	Dividend, equity contribution and debt
2016	Djurica, Jovanovic and Maric	Serbia	TP methods and application
2016	Singh	India	International taxation and FDI (TP area)
2016	Garcia	Colombia	Arm´s length principle and intangibles
2017	Kurfi, Udin and Kasuwa	Nigeria	General overview
2017	Grondona and Knobel	Argentina	General overview, coordination with foreign tax authority and regulatory changes relating to the G20/OECD BEPS
2017	Perčević and Hladika	Croatia	TP methods
2017	Neacșu and Feleaga	Romania	General overview and adjustments
2017	Nakonieczny	Poland	General overview and TP methods
2017	Greggi	Italy	General overview and BEPS
2017	Lincoln	USA	General overview and BEPS (OECD)
2018	Vawda, Parsons and Mabutha	South Africa	ALP, TP documentation and BEPS
2018a	Beebeejaun	Mauritius	General overview and APA
2018	Oosterhoff	Netherlands	New Transfer Pricing Decree
2019	Brychta and Sulik-Gorecka	Czech Republic, Poland	APAs

Source: own elaboration.

Most of the authors provide an overview of transfer pricing rules in domestic legislation. In addition, they also include a comparison with other selected countries and with the OECD guidelines and suggest *de lege ferenda* proposals either for selected home jurisdictions based on the underlying tax system and domestic legislation (e. g. Aditya, 2015; Kurfi, Udin, Kasuwa, 2017 or Brychta and Sulik-Górecka, 2019) or for the selected group of countries, e. g. the EU (Solilova, 2010) or OECD (Büttner and Thiemann, 2017). Susanti and Firmansyah (2018) recommend the Indonesia Financial Services Authority issue a policy or fixed rate to a standard related party for a company with a certain majority shareholder. Other recommended policies focus on protecting the rights of minority shareholders and to improve corporate governance for companies in Indonesia by maintaining common indices such as the OECD index.

Chan (2005) worked out the comparison of transfer pricing regulation between the USA, Australia, Canada, China and Japan regarding the sale or transfer of tangible goods or property. Rathke and Rezende (2016) analyse several TP systems in order to identify similarities among countries and create groups of countries based on uniformity of TP characteristics. They divide the selected countries into six subgroups and they further found three major groups of companies displaying substantial differences. Ignat and Feleagă (2017) analyse the transfer pricing regulations of all European countries and build a transfer pricing strictness index, based on which they define four categories of countries. They find that in most EU countries, TP rules are not so strict and on the other side not so flexible. Matei and Pîrvu (2011) provide an overview among EU countries comparing the national legislative to OECD principles, arm's length principle, TP documentation requirements and rates of corporate income tax.

Lohse, Riedel and Spengel (2012) analyse the development of different aspects of transfer pricing regulation among 44 countries between 2001-2009. Their study underlines the increasing awareness and importance of transfer pricing regulation. They further find:

- there is only little variation between countries regarding TP methods, the only differences exist in the priority of methods;
- documentation requirements were introduced to a greater extent during this time period;
- only twelve countries enforce penalties regarding special transfer pricing rules, especially with respect to documentation;
- the possibility to enter into advance pricing agreements is increasing with only nine countries not allowing for such agreements; and
- the regulations have become stricter over time and it seems in general, that the rules in Europe are less strict compared with countries outside of Europe.

Harmse and van der Zwan (2016) and Vawda, Parsons and Mabutha (2018) provide alternatives for the treatment of transfer pricing adjustments in South Africa based on conceptual analysis mainly in the area of the arm's length principle application, preparation of TP documentation and following the rules as stated by BEPS project actions (8-10) and OECD guidelines. Perčević and Hladika (2017) suggest recommendations that could improve the control of transfer pricing in Croatia. Burke (2010) demonstrates problems inherent in the assumptions of transfer pricing regulation and further highlights the difficulties in determining the arm´s length principle price and the cost of information sharing and tax adjustments among diverse tax administrations. He is of the opinion that it is essential to reconsider the underlying first principles of transfer pricing rules with a view towards their revision, if not possible elimination. Van der Meer-Kooistra (2004) presents a model for determining the amount of qualitative adjustments to be made to the prices or profit margins of insufficiently comparable transactions. Solilová (2011) analyses revised OECD Guidelines (1995 vs 2010) in terms of comparability and the use of profit-based methods and the impact of the revised text on the application of transfer pricing analysis and transfer pricing methods. She focuses also on the significant changes of newly approved guidelines with the aim to evaluate how the Czech Republic began applying the principles set out in the revised text of these OECD Guidelines.

Hsu, Xiao and Xu (2019) find that the regulatory restriction on transfer pricing may bring benefit rather than burden to the global firm. The paper of Budd and Tyrrall (2002) presents an overtly theological critique of governmental regulation of international transfer pricing activities of multi-national enterprises. Grecu et al. (2010) state that fiscal authorities throughout the world attack more frequently transfer price setting methodologies and they impose even more severe sanctions to companies that they find do not follow regulations. Heriford et al. (2013) describe the development of the US Cost Sharing Rules (arm's length royalty paid for intangibles) since 1995 and highlight that companies must be aware of the following questions and issues in case one company is located in the US:

- what are transferred intangibles?
- characterization of transaction,
- life of the pre-existing intangible property, and
- contribution of the offshore subsidiary to the transaction.

Waegenaere, Sansing and Wielhouwer (2006) find that an increase in the probability of inconsistency with transfer pricing rules induces more aggressive auditing by governments. This could increase or decrease the taxpayer´s expected tax liability and could either increase or decrease the deadweight loss from auditing.

Taking account of the one of the basic law principles (namely the rule of law), the rules as set by law are of vital importance - they provide boundaries and limits for the exercise of the public power.

1.5 ARM'S LENGTH PRINCIPLE (ALP)

In the expert literature a special attention is paid to the crucial transfer pricing principle and its establishment. This principle arouses curiosity in many respects and perspectives as can be demonstrated by the research focused to it.

Ylönen and Teivainen (2017) provide a historical overview of the authors dealing with the arm's length principle, including also the development of this rule in the U.S. (mainly for the court purposes) and in other countries.

The arm's length principle establishes boundaries for domestic law to eliminate economic double taxation in the cross-border allocation of business profits of MNEs, which currently account for over 70 % of global trade (Pankiv, 2017). A coherent application of the arm's length principle as an international norm should enable the allocation of MNE profits in a way that neutralizes the effect of corporate income tax on foreign direct investment (FDI). The arm's length principle is a general principle of tax treaties, but on the other side the arm's length principle cannot be regarded as an anti-avoidance measure to combat malpractice by multinational firms under tax treaties.

Matsui (2011) demonstrates that a uniform imposition of the arm's-length principle on transfer pricing leads to coordination failure among countries in terms of economic welfare if the countries trade products in the form of intra-firm trades and exchanges by multinational firms. His results indicate that it is possible that enforcement of this principle has no positive effect at all in the world because economic welfare of all economic agents deteriorates when the principle is imposed. In the context of economic welfare, Gresik 1999 (cited in Matsui, 2011, p. 571) shows that a policy that seeks to attain the arm's-length transfer prices is consistent with broader welfare objectives when the multinational's home country is commensurate with income standard. Devereux and Keuschnigg (2008) illustrate that the application of the arm's length principle distorts financing and investment of multinational firms, the choice between outsourcing and direct investment and also leads to a reduction of global welfare. They also state that the imposition of tax penalty leads companies to choose a transfer price closer to the arm's length principle observed in outsourcing relationships. Kim et al. (2018) analyse the impact of the arm's length regulation on transfer pricing with a focus on offshoring and outsourcing in a global supply chain.

More recently, Gresik and Osmundsen (2008) pointed out the possibility that customary arm's length methods will not perform well in vertically integrated industries due to comparability rules that encourage firms under vertical integration to collude on transfer pricing.

Based on their investigations, Cheng and Zhang (2009) formulated two findings. The first one says that if the firm is compelled to follow the arm's length principle, it has an incentive to circumvent the arm's length principle by keeping two sets of books, one for internal management, and another for tax reporting purposes. The second finding is that the arm´s length principle can affect the MNC´s decision on whether or not to foreclose its competitor.

Pauwels and Weverbergh (2005) state that the arm's length interval is in principle derived from assessments based on comparable uncontrolled prices or market prices. However, monopolistic situations imply that a strict comparison is not possible. They come out with the golden rule in transfer pricing regulation in relation to tax coordination between the two countries. Under the golden rule, profit taxes should be higher in importing industries than in exporting industries (fair-profit principle).

Schäfer and Spengel (2003) state that formula apportionment seems to be more appropriate than the arm's length principle as regards to the issues of changed economic structures due to information and communication technologies. They further add that the ALP (arm's length principle) encounters difficulties regarding its feasibility in practice, as in some cases, the comparable transactions necessary for its implementation exist less frequently. According to them, the formula apportionment approach is preferable over the ALP in light of the principle of inter-nation equity and may constitute a suitable alternative for profit allocation especially for the EU.

Formulary apportionment is an old idea that has been adopted on a restricted basis, particularly within federal states (Couzin, 2013). According to Couzin (2013), the arm's length principle (or arm´s length method or arm´s length standard) should be regarded not as a definition of transfer pricing but instead as a particular and not inevitable decision about how it may be controlled. Arm's length price in the USA is often marked as "fair price" (Buckley and Hughes, 1997). Drtina and Correa (2011) state that transfer prices depend on developing an arm's length standard and making adjustments for comparability factors like risk, market conditions and strategy.

Durst (2010) states that the unenforceability of the arm's length standard derives not from the details of its implementation but from its central premises. He also adds that the practical costs of the unenforceability of arm's length transfer pricing rules are enormous. Specht et al. (2015) describe the internal TP in energy companies between divisions such as generation, sales and trading divisions. They further state that under specific conditions, like the existence of non-hedgeable profile risk caused by market incompleteness, the arm's length principle does not hold. Therefore, under certain conditions, the internal TP should be set above the market price to account for the un-hedgeable risk transferred between divisions.

Schjelderup and Weichenrieder (1998) state that a country which switches from price related transfer pricing rules to profit related measures can reduce the imports without changing firms' transfer price.

Raimondos-Møller and Scharf (2002) investigate the possibility that governments may use transfer pricing rules strategically when they compete with other governments and show that harmonisation according to the arm's length principle (according to OECD) may not be pareto improving.

1.6 COMPARABILITY ANALYSIS

To set the price in line with the Arm´s Length Principle is closely connected with comparability analysis which is sometimes difficult to carry out due to many obstacles – both for tax-payers and for tax authorities within tax audits aimed at transfer pricing. In relation to arm's length ranges and arm's length transfer pricing, Solilová and Nerudová (2013) state that according to the model we can only base new transfer prices on accessible real data that is publicly available from financial statements. Considering their model, as transfer prices and internal margins are part of business secrets it is not possible to perform a comparative analysis. The findings of Rathke (2015) suggest that governments may face a hard time challenging transfer prices if market values present high volatility or if market activity does not allow for accurate observations on delimitations of the accepted price range in order for businesses to benefit from it. Rathke (2015) further states that the influence of changes in the arm's length parameters is potentially relevant for studies on legislation efficiency and tax audits and it appears to be a path for further scientific investigation.

The last step of transfer pricing methodology is determining the arm's length range. There are many factors which determine return-on-sales or cost-plus mark-up, such as the type of the services or activities performed, and the level of risk assumed (varying across industries). It is very important to highlight that companies by their nature may differ slightly or widely (Tierney et al., 2009). Therefore, according to Solilová and Nerudová (2013), entities perform a comparability analysis which compares the entity's transfer pricing return-on-sale or cost-plus percentage with those of its competitors, in the same or similar industry or with functional profiles. The output of the comparability analysis is a range of acceptable percentages, which is called an arm's length range. Kratzer (2008) states that the application of interquartile range is required by many tax administrations and is highly recommended as it helps to eliminate extreme results and increases the reliability of the comparison of the results. The arm's length principle is respected if the interquartile range is followed. The interquartile range usually represents a range from the 25th to the 75th percentile of the results derived from uncontrolled transactions while only 50% of those observations which are closest to the median are considered reliable to the arm's length results (Solilová, Nerudová, 2019). Solilová and Nerudová (2013) state that it is suitable to determine the 10% percentile and 90% percentile, but the rest of the observations are kept avoiding the loss of 50% of the observations. This practice is recommended to exclude the outliers from statistical testing as they can unbalance the obtained results. Christian and Zdanowicz (2016) analysed the use of interquartile ranges in relation to the study of state corporate tax implications of abnormal transfer-pricing by U.S. companies involved in international trade.

Mura, Clive and Vallascas (2013) state that under profit-based transfer pricing methods, the selection of comparable companies (search for a set of comparable companies) is essential if the detection of transfer price manipulation is to be reliable. The results of their research suggest that the current comparability tests are likely to fail the identification of transfer pricing practices in countries where the comparative advantage of foreign-controlled companies is particularly pronounced. They question the reliability of these tests. Careful selection of comparable companies is vital in order to demonstrate that any differences in profitability between a tested party and unrelated parties are realistically attributable to transfer prices not in line with the arm's length profit principle. Emmanuel and Mehafdi (1994) consider the search for comparable companies as an important role in guaranteeing that they enjoy market positions, a level of efficiency, advanced technology so that they are similar to those of the tested party in order to realistically infer that eventual differences in profits relate to abuse on transfer pricing.

Sulik-Górecka (2018) in her paper proposes a methodology for comparability analysis that may be used by manufacturing entities to defend the conditions that determine transfer pricing. She introduces the different functional profiles of manufacturing entities and points out the difficulties they may encounter when preparing a comparability analysis. She further adds that the lack of uniform benchmarking legislation can cause inconsistencies in the selection of comparable data, resulting in differences in transfer pricing.

Nerudová et al. (2017) state that the arm's length principle application is based on comparability and functional analysis, which is very time consuming, places high demand on the financial and human resources of a company and for SMEs often very complex and onerous.

According to Smith (2015), the objective of comparability analysis is always to seek the highest viable degree of comparability, recognizing that there will be unique transactions and cases where applied methods cannot be relied on. The approximation of the arm's length price is dependent on the availability and reliability of comparables. When processing the transfer pricing analysis, the following factors should be considered during the determination of the comparability transactions:

- characteristics of the property or service,
- functional analysis (functions, assets and risks),
- contractual terms,
- market conditions (economic circumstances), and
- business strategies (corresponding to factors of comparability analysis stated in the OECD Transfer pricing Guidelines for Multinational Enterprises and Tax Administrations – OECD, 2017).

Smith (2015) further highlights some different characteristics, which could lead to differences in their values at open market. Such potential differences must be considered in a comparability analysis for tangibles, intangibles and services.

Rossing et al. (2017) state that a comparability analysis has the following four steps:

- identifying intra-group transactions subject to analysis;
- performing an analysis of the controlled transaction(s) under examination, with emphasis on functional analysis;
- establishing the proper transfer pricing method; and
- determining the transfer price.

Buckley and Hughes (1998) examine the difficulties which the tax authorities are facing in valuing cross-border flows from a transactions-based analysis, in conditions where intangibles and services are important and where the multinational company concerned is operating a system in which group-wide economic functions dominate decision making. They pay attention to economic function analysis and functional cost analysis in both Japanese and international conditions.

According to Garcia (2016), the arm's length standard literature demonstrates that the weakness of all transfer pricing regimes includes intangible related transactions and debt financing. One of the reasons is that the current transfer pricing rules are not properly adapted to the new digital economy as they were not designed to regulate intangibles or e-commerce cross border transactions. Visconti (2013) states that intangibles due to their immaterial nature are frequently negotiated within multinational groups and that's why they are so sensitive to transfer pricing issues. Intangibles are unique, they cannot paradoxically be universal, so in challenging arm's length comparisons, they are difficult to compare. He further highlights that wrong and illusionary comparables have a distorting impact on TP and bad (incorrect) data may potentially be manipulated or misused. His study suggests that further efforts are needed in order to improve the quality and comparability of databases, rulings and APAs, disentangling the intangibles' value chain and softening natural confidentiality. The main output of his analysis shows that since the segmentation of know-how is problematic, a possible feasible solution may be that of concentrating on the overall taxable base, where know-how is ingrained in its marginal utility, pushing up different types of economic and financial margins. Referencing cost, income or market approaches, traditionally used with an evaluation of intangibles, may well complement sophisticated OECD methods, which fit a general framework of valuation but hardly adapt to know-how specificity. Cardoso and Martinez (2014) conduct the comparative analysis of the Brazilian model with the OECD report (Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations) focusing on methods applied to transactions with intangibles. Johnson (2006) examines the effectiveness of three transfer pricing methodologies for an intangible asset that is developed through bilateral, sequential investment. She finds that a royalty-based transfer price that can be renegotiated provides better investment incentives than either a non-negotiable royalty-based transfer price or a purely negotiated transfer price and in some cases induces first-best investment.

The findings of Muhammadi, Ahmed and Habib (2016) suggest that Indonesian tax auditors face a number of difficulties during the audit of transfer pricing cases derived from intangible assets, including a lack of transparency in taxpayers' bookkeeping, limited taxpayer cooperation in providing data and documents, transfer pricing regulations and problems related to organisation and human resources. They further highlight that tax auditors handle transfer pricing cases by using a legal basis as reference and by performing several activities, especially comparable analysis.

1.7 TRANSFER PRICING METHODS

Within the arm's-length principle, various TP methods have been constructed, upon which practitioners, enterprises, and tax administrations principally focus their intensive and expensive attention. These methods are intended to provide a mechanical and objective means of implementing the arm's-length principle. They all rely on an external comparison with either a price or a margin in order to determine what one part of a MNE would have charged another in the absence of association (Couzin, 2013).

McGowan, Beauregard and Collier (1987) belong among the first authors who focus on the application of transfer pricing rules in multinational corporations and they provide an overview of TP methods and their practical examples of application.

Companies can choose between the five TP methods as stipulated by the OECD Guideline recommendations to determine the price in harmony with the arm's length principle: comparable uncontrolled price method (CUP), resale price method (RP), cost plus method (CP), transactional net margin method (TNMM) and profit split method (PS). The CUP method is the direct observation of comparable market prices, which can be applied to intra-group transactions. The other methods are all based on the observation of comparable market-based profit margins from which a market-based transfer price can be determined. Usually, the CUP method is preferred (because it provides a comparable market price for justifying the transfer price) if it is possible to use it, but selecting the most appropriate transfer pricing method depends on the circumstances of the case, i.e. that the methods are equivalent to each other.

In cases where the CUP method cannot be applied (mainly due to a lack of comparables), preference is given to methods that focus on gross margins, i.e. the RP and CP methods. If the two gross margin methods also cannot be applied (due to the lack of comparable market-based gross margins), the TNMN or PS should be used. Rossing et al. (2017) also further provide examples of TP methods application.

Doğan, Deran and Köksal (2013) state that there are many factors affecting the determination of transfer prices and selection of TP methods. Their study focuses on conditions in the U.K. and they provide an overview of used and preferred TP methods in different industries. They also made a classification of four groups that have an impact on TP method selection. These categories are as follows:

- legal factors,
- political and social factors,
- external economic factors, and
- internal economic factors.

The study of Verdes (2016) reveals significant differences between transfer prices calculated by classical methods and profit methods. She states that transfer price calculation, in both the testing and checking methods have shown different initial data than what is needed from the beginning. Traditional methods do require comparable transactions, while the transaction-related methods do not solve the transactions problem. She suggests that future guidelines on transfer pricing regulations contain more references and examples to be better personalized.

Li, Oyelere and Laswad (2004) conduct research focused on foreign owned New Zealand subsidiaries and found that the cost-plus method is the most commonly used international transfer pricing method. The preference for this method is reflective of the fact that many of the companies in the survey are from the manufacturing industry. As for sales and marketing companies (distributors), the resale price method is generally viewed as the most suitable. The divergence of other pricing methods, e.g. agreed price and the contract manufacturer approach could be as a result of their unique nature and of their intercompany transactions (Borkowski, 2001).

Mitter and Siems (2008) focus on transfer pricing for internal services and products, mainly on marketing perspectives of transfer pricing. They provide the comparison in terms of use and conditions for marked-based, cost-based and negotiated approaches to transfer prices.

Tono, Tanasal and Asri (2018) also describe transfer pricing methods, dividing by market-based, cost-based and negotiated price, and further highlight that each TP method has its own advantages and disadvantages with a focus on performance measurement. According to Blocher et al. (2019), the managers in the decision-making process related to transfer pricing must pay attention to a number of conditions, e.g. external suppliers, comparing variable cost of sales division and market price, and the company's operating capacity.

Pfeiffer, Schiller and Wagner (2011) in their paper compare the economic performances of alternative cost-based TP strategies. They got the following results: (1) centralised standard-cost based transfer pricing strategies dominate all others if the headquarters and the divisions ex-ante face low cost unpredictability; (2) actual-cost methods lead all others if the headquarters and the divisions ex-ante face high cost unpredictability and at the trading stage, the buying department receives adequate cost information and (3) reported standard-cost transfer pricing leads the other methods if the central office and the ex-ante face high cost uncertainty, and the buyer has insufficient cost information at the trading stage.

Nakonieczny (2017) presents comparable uncontrolled price method, resale price method and the reasonable profit margin cost-plus method and current practices and legal regulations in Poland. Challoumis (2018) describes the TP methods used in services and provides an analysis, which can be used by companies to tackle tax issues. He highlights that the appropriate selection of TP method and comparability analysis plays a critical role in following the arm's length principle.

Gresik and Osmundsen (2008) show that a strategic connection between vertically integrated businesses operating in the same final goods market can moderate and possibly reverse tax-differential incentives if the correct comparison method is used. They consider the cost-plus method as the most adequate in limiting the equilibrium amount of profit-shifting out of the high-tax jurisdiction. They view it yields the highest tax revenues for the high-tax state. If the firms have private cost information, these benefits are strengthened. Mădălina, Valer and Diana (2008) describe TP methods mainly in regard to transfer pricing as a profit-shifting technique and provide diverse categories of intangibles in this respect. Rajnoha, Slivková and Dobrovič (2014) analyse transfer pricing methods for depending transactions from the perspective theory as well as in terms of the legislative framework and methodological procedures applied on transfer pricing in selected OECD countries. They propose a generally applicable decision-making model for selecting the optimal transfer pricing method for each type of dependent transaction, which they verify in terms of selected economic aspects of optimisation. Solilová and Nerudová (2018) provide a detailed analysis of practical applications of transfer pricing methods together with the strengths and weaknesses for each traditional transaction and transactional profit methods. Perčević and Hladika (2017) investigate and identify which transfer pricing methods apply to related companies in Croatia. Their research results show that the majority of related companies in Croatia apply the cost method for determining transfer prices. Kouser et al. (2012) examine the most dominant transfer pricing methods and their structure with line of responsibility for transfer pricing decisions as used by different manufacturing companies in Pakistan. Neves and Samagaio (2006) highlight the importance of the strategy and the diversity of methods for determining transfer prices. They further state that the OECD arm's length principle is clearly a constraint to actual practices.

Terzioglu and Inglis (2011) compare the use of TP methods between selected countries and their results suggest that a full cost-based transfer price is the most widely used TP method, followed by market-based and negotiation-based TP methods.

1.8 TRANSFER PRICING DOCUMENTATION

Another hot transfer pricing issue is transfer pricing documentation which is set as obligatory in some countries showing different requirements as set for the scope and content. In this respect, e. g. Couzin (2013) highlights that corporate tax officers identify the burden of transfer pricing compliance costs as significant, excessive and rising. He primarily focuses on multi-country documentation requirements, unpredictable and unquantifiable audit risks, penalties and controversy management. Couzin also points to the fact that unlike domestic and even most international tax rules, transfer pricing demands double and sometimes multiple compliance and administration with respect to the same revenue.

According to the current principles and legal regulations, the transfer prices file must be filed at the moment of transaction processing or before submitting related declarations concerning the profit coming from that transaction (OECD, 2014).

Succio (2010) states that most taxpayers are not well informed about the nuances of identifying, evaluating and documenting their intragroup services for transfer pricing purposes. He also highlights that the lapse in documentation may invariably lead to large reassessments against the taxpayer as well as subsequent litigation at the tax courts. Transfer pricing documentation plays a crucial role when a taxpayer makes an adjustment in its tax return to its accounts profit resulting from the application of the arm's length principle. Besides, the TP documentation can also be an important tax planning tool as well.

Babatunde and Adedayo (2018) recommend that companies consult their TP documentation with experts in this field as TP documentation is coordinated through the arm's length principle, resp. helps to prove that transfer prices are in accordance with the arm's length principle.

Transfer prices are primarily documented by means of two dependent packages of information - documentation of facts (documentation of the company and the group as well as documentation of the business environment) and arm's length documentation (the identification of relevant related-party transactions is necessary) (Tucha and Brem, 2007). Tucha and Brem (2007) also provide the arm's length analysis in the context of transfer pricing documentation in the German environment.

Feleaga and Neacșu (2016a) state that TP documentation requirements discourage the practice of MNEs to shift their profits through transfer pricing mechanisms in low-tax jurisdictions. These transfer pricing concerns cause changes in national legislations, e.g. in Australia, Denmark, France, UK, Netherlands, Poland, South Korea or Mexico. From 2016 the preparation of a transfer pricing file by companies performing with associated persons will be mandatory and the authors will also provide an overview of selected countries in regard to transfer pricing documentation requirements. The difference between a transfer pricing file and an advance pricing agreement is that transfer pricing documentation analyses transactions which have already taken place between associated companies, while the advance pricing agreement analyses transactions that will be carried out in the future (Feleaga and Neacșu, 2016a).

Sulik-Górecka (2016) conducts a critical analysis of the latest regulations with a proper evaluation of transactions between associated parties and cost accounting challenges for the reason of transfer pricing documentation in Poland. She further states that the consequences of comparability analysis obligations and complying with the benchmarks may cause an increase in popularity of the net margin method in transfer pricing. Solilová (2012) provides an overview of TP documentation among the EU countries with a focus on SMEs.

Despite some problems related to transfer pricing documentation, one can conclude that transfer pricing documentation, when prepared properly, is a useful tool to empower the position of the tax-payer within the bearing the burden of proof and potential tax audits related to transfer pricing. To boost the position of the tax-payer when setting the transfer price, another tool can be utilized – namely an Advance Pricing Agreements.

1.9 ADVANCE PRICING AGREEMENTS (APAS)

An APA is a formal arrangement between a tax authority and a taxpayer involved in cross-border related party transactions where the goal is to determine an appropriate transfer pricing methodology for related party transactions according to the country's transfer pricing regulations (Eden and Byrnes, 2018). Many authors (e.g. Chugan, 2007 or Biyan and Yilmaz, 2013) consider advance pricing agreements (APAs) as a solution to encourage foreign investors, increase transparency, save both taxpayer's and tax authority's time and costs, reduce litigation, prevent any hesitations or penalties and comply with the instructions of the tax administration and finally to encourage foreign investors to invest more. Fadiga (2018) considers APAs as the most effective tool for companies to reduce the uncertainty and to reduce the fiscal liability arising out of transactions regulated by transfer pricing. MNCs use APAs to gain confidence in complicated operations and attain better efficiency. The aim of the APA procedure is to provide information that is more precise, unconditional and consistent than what a taxpayer can autonomously deduce from tax legislation (Fadiga, 2018). On the other side the author states that single, objectively correct results of the application of the arm's length principle cannot be obtained. The assessment of the lawfulness of an APA therefore cannot be objective.

Waegenaere, Sansing and Wielhouwer (2007) investigate the use of bilateral advance pricing agreements (BAPAs) as a tool to resolve transfer pricing disputes between a taxpayer and two tax authorities. They show that these agreements are more likely to arise when the amount of income potentially subject to double taxation is low and the difference in tax rates between the two countries is high. They also showed that the BAPA program can increase compliance costs. Chugan (2010) considers APA and safe harbours as the two most efficient ways of reducing litigation in the area of transfer pricing, which is developing as the most important taxation subject among chief executives and tax authorities. According to Singh et al. (2009), APA is the alternative approach, which is gradually gaining greater acceptability. The underlying difference between the two is that while safe harbour is universal, advance pricing agreements are taxpayer specific. If only one jurisdiction is involved, then an APA in unilateral, in case that two tax jurisdictions are involved then an APA is bilateral. Singh et al. (2009) further highlight that the main advantage of a unilateral APA is that this tool provides the certainty of the arrangement being accepted by both the tax authority and taxpayers, in case of bilateral APA by both the tax jurisdictions, thereby removing any chance of double taxation. Vogele and Brem (2002) find that an APA agreement is an excellent alternative in financial management strategy to prevent transfer pricing disputes. They further state that the main advantage of an APA agreement is to assure that the tax authorities will not challenge the transfer pricing position taken, unless a misrepresentation or unforeseen circumstances occurs.

Herath and Young (2012) consider APA as the best tool to accomplish the minimisation of a firm's global tax burden. Sawyer (2004) observed that business-world transfer pricing is a multi-entity issue where many routine and non-routine functions are performed in several tax jurisdictions along the value chain of the MNE. He further states that a major complicating factor taken into consideration in the negotiating process is the discrepancy between business-world transfer pricing and tax-world transfer pricing. Snowdon (2010) concludes that companies want to use APA in their management, on the other side the author highlights the system changes which should be implemented.

The findings of Borkowski and Gaffney (2014) suggest that the expected relationship between APAs and audit risk reduction was not supported. The results of their investigation provide no significance attached to APA status and the likelihood of a TP-related audit, or the outcome of that audit in selected countries comprising the Pacific Association of Tax Administrators (PATA). The conclusions of these authors are limited to TNCs and tax authorities in the four PATA countries and may not be automatically generally applicable to other countries. Their findings could be marked as unexpected results, given that tax authorities and consulting firms with transfer pricing expertise offer APAs as one of the best ways to mitigate transfer pricing audit risks. APA is a tool explicitly designed to address transfer pricing risk, current additional research in progress is focused on the use of general risk reduction strategies, specifically on enterprise risk management in a transfer pricing context. Enterprise risk management threats specific risks to the industry, economic environment and how to minimize and eliminate those risks.

Buus (2018) in his paper provides a guide for the reassessment of the principles of risk analysis regulation in transfer pricing and highlights how the standard view of risk and profit allocation between strategic and routine units is inconsistent with their relative risks or the relative risks of the multinational's subsidiary and independent company.

Advance Pricing Agreements are fundamentally tools that firms use to negotiate transfer prices before application. Companies give up some of their planning power in exchange for reducing possible tax litigation risk (Ylönen and Tevainen, 2017). As was already observed in some cases, the APAs can also be used for aggressive tax planning and in order to avoid taxes in other countries.

Chugan (2008) describes various matters of contention that may arise during a strict audit in the banking and insurance sectors and suggests concerned MNCs to adopt a proactive approach in their tax planning including proper maintenance of documentation and required information in line with the new legislation so as to avoid heavy penalties and harassment.

Eden and Byrnes (2018) recommend several changes which could be made to the APA and state aid policy processes that should lessen, but probably not eliminate the unintended consequences of APAs. They recommend that information on individual APAs be more publicly available and that tax authorities shift from unilateral to bilateral APAs when at least two tax authorities are involved. The next recommendation is regarding the improvement of an authorities' capacity to document and administer APAs. The last recommendation is that the European Commission restricts its investigation in APA cases to what they call stage 2 issues (assessment of tax benefit). According to the authors, the European Commission should accept the APA transfer pricing methodology (stage 1) except in situations where the transfer pricing rules and procedures at the national level either did not exist or were not followed and material violations likely occurred.

Brychta and Sulik-Górecka (2019) identify fundamental rules for Advance Pricing Agreements within OECD regulations and subsequently characterise, assess and measure the general rules for APAs in both Czech and Polish domestic legislation. They further find that Polish domestic legislation can be considered as a suitable and inspiring one for Czech domestic law.

Biyan and Yilmaz (2013) highlight that signing the APA does not mean that that taxpayer or taxpayers will not be analysed about the subject of an agreement. Taxpayers must comply with the terms and/or terms are still valid through the annual report presented by taxpayer during period determined by agreement with the financial administration.

Solilová et al. (2017) find that compliance costs are increasing through strict and difficult transfer pricing rules among European countries. They suggest that taxes and new obligations should be carefully designed so that they can address the disproportionately high tax compliance burdens faced by those enterprises. Based on the research results of SMEs with a tax residence in the Czech Republic, they conclude that the costs for managing transfer pricing requirements can reach from 6,430 EUR to 7,704 EUR per year, time needed for this issue between 27 and 35 working days and in comparison with corporate tax collection it represents between 3.90 % and 12.74 %. Couzin (2013) concludes that the relative costs of corporate income tax compliance are higher for small and medium-sized enterprises, but even with respect to the large, concentrated pools of income where transfer pricing is concentrated, efficiency is not impressive. He further adds that the burden of transfer-pricing compliance is confirmed by anecdotal evidence. His statement is also confirmed by the Transfer Pricing Survey Series worked out by Ernst&Young (2016). This survey also provides the analysis of trends in using APAs and BAPAs. According to this survey, the number of firms indicating tax risk management as their top transfer pricing priority has surged to 75 %. From this survey it was further revealed that among current users of APAs, a strong majority are satisfied with the process and its results, including 75% of those in the UK, 70 % in the US and 73 % from other countries (marked as rest of the world). Couzin (2013) also states that profit splits method(s) is often promoted as a solution commonly adopted in a mutual agreement procedure (MAP) and APA negotiation. Whitford (2015) finds that inward and outward FDI flows are associated with greater incidence of APAs. Another finding is that the countries that are most likely to adopt APAs are those with native MNCs that make significant investments in foreign economies.

According to the Joint Transfer Pricing Forum (JTPF) (European Commission, 2019a) Communication from 2007, *"an APA will provide in advance certainty concerning the transfer pricing methodology and therefore simplify or prevent costly and time-consuming tax examinations into the transactions included in the APA. This* *should lead to savings for all parties involved, cut compliance costs and provide more consistency in transfer pricing within the EU. This approach will reduce the obstacles for cross-border economic activities in the internal market."*

1.10 SAFE HARBOURS

Generally speaking, it seems that an establishment of so-called safe harbours has a potential to be another useful tool for easier application of the arm´s length principle. Solilová (2013) highlights the benefits of safe harbours mainly in:

- simplifying compliance,
- reducing compliance costs,
- providing certainty,
- shifting administrative resources to examinations of more complex or higher risks transactions and taxpayers, and
- minimal examination requirements.

Singh, et al. (2009) consider safe harbour as a simplified approach for the computation of income with a view to bringing more prospective taxpayers into the tax net. It minimizes not only the compliance cost for taxpayers but also the administrative cost for tax administration. Solilová and Nerudová (2018) provide an analysis of advantages and disadvantages of safe harbours for both taxpayers and tax authorities, describe the current situation of safe harbours as simplified measurements in the EU and formulate recommendations of the form and scope of safe harbours. Kostić (2018) recommends that developing countries, like Serbia for example, should focus more on introducing broad safe harbours rules, because these provide predictability (legal certainty) and would allow the tax administration to concentrate what resources it has at its disposal on the worst cases on non-arm's length transfer pricing. Singh (2016) states that in India safe harbours are a credible alternative to APA and lay down the framework under which the transfer price declared by taxpayers would be accepted by the tax department for five assessment years. These rules cover the following sectors: IT and ITES sectors, contract R&D in the IT and pharmaceutical sectors, financial transactions - outbound loans, financial transactions - corporate guarantees and auto ancillaries-original equipment manufacturers. The aim of safe harbours application in selected fields is to reduce aggressive scrutiny by tax department.

As can be evidently deduced from the above stated results of the realized research, in the expert literature the transfer pricing issues are commonly assessed (analysed) not only in relation to particular countries, but also in relation to industrial sectors. It is only logical because the industries show significant differences in their nature and principles on the basis of which they operate.

1.11 DIFFERENT SECTORS

Transfer pricing studies focus on domestic (e.g. Erickson, 2012) or international (e.g. Rossing, Cools and Rohde, 2017) associated parties in many areas of business, from marketing (Erikson, 2012 or Liu, Zhang and Tang, 2015), services (Terzioglu and Inglis, 2011), manufacturing companies (Abu-Serdaneh, Al-Okdeh and Gauher, 2008), agriculture (Han, 2010), intellectual property (Visconti, 2013), R&D (Barry, 2002), bank products (Castagna, 2013), medicine (Kuntz and Vera, 2005) to vertically integrated industries, e.g. food market (Gresik and Osmundsen, 2008) or their partial comparison (Talha, Alam and Sallehhuddin, 2005).

The following table Table 4 captures the selected investigations in TP with a focus on specific sectors.

Table 4: Overview of selected research papers with focus on transfer pricing in specific sectors

Year	Author(s)	Sectors, countries and supplementing information
1987	Von Grebmer	International transfer pricing in the pharmaceutical industry
1998	Young	TP methodology between integrated delivery systems (hospitals)
2004	Raetzell et al.	Implementation of an intern. TP system for anaesthesia services (GER)
2005	Schuster et al.	Transfer pricing for anaesthesia services (chances and risks) (GER)
2005	Talha, Alam and Sallehhuddin	TP, taxation implications disclosure in segmental reporting: Malaysia

Year	Author(s)	Sectors, countries and supplementing information
2006	Neves and Samagaio	ITP policy in American and German subsidiaries operating in Portugal
2007	Steiner	Negotiated TP: theory and implications for value chains in agribusiness
2010	Boulogne	TP of intangibles, a comparison between the Netherlands and the USA
2011	Solilová and Nerudová	Transfer pricing in agricultural enterprises in the Czech Republic
2011	Moisello	Managerial and accounting aspects of TP in the shipping sector
2011	Bateman and Westphal	Presence of TP and its impact in U.S. airline mergers
2011	Isley, Cassill and Cassill	Intergovernmental Agreement on TP in the Maquiladora industry
2011	Taylor, Knaus and Matthews	Transnational TP – example on chemical company, USA
2011	Terzioglu and Inglis	Transfer pricing in Australian service organisations
2012	Kouser et al.	Survey on TP practices in manufacturing sector in Pakistan
2012	Tumasyan	Fundamental aspects of FTP framework and its role in a bank
2012	Solilová	Small and medium sized enterprises (SMEs) and transfer pricing
2012	Lutz	TP, discounted cash-flow method, equity risk premium and automobile indus.
2014	Seppälä, Kenney and Ali-Yrkkö	TP in global supply chains in manufacturing sector
2015	Specht at al	Efficient steering of integrated energy firms using internal TP
2016	Hamid and Arshad	TP Practices among Public Listed Companies: Evidence from Malaysia
2016	Sekhar	Telecommunication company – Vodafone case
2016b	Feleaga and Neacsu	Disclosure of related party transactions and information regarding TP by the companies listed on Bucharest Stock Exchange
2017	Indriaswari and Aprilia	Transfer pricing decisions in manufacturing companies in Indonesia
2018	Nugroho, Wicaksono and Utami	TP policy of manufacturing companies listed on the Indonesia stock exchange
2018	Susanti and Firmansyah	Determinants of TP decisions in Indonesia manufacturing companies
2018	Roques	Transfer Pricing for Digital Platforms
2019	Li and Paisey	TP adjustments and differential products (chemical products)

Source: own elaboration.

Feinschreiber (2004) states that transfer-pricing regulations for services are much less developed than for goods and raw materials. Terzioglu and Inglis (2011) claim that most transfer pricing studies focus on international manufacturing organisations.

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CHAPTER 2
DESIGN OF EMPIRICAL INVESTIGATIONS

2.1 GENERAL BACKGROUND

Generally speaking, transfer pricing in connection with the application of the arm's length principle and efforts to reach fair allocation of tax bases amongst countries have been the subject of critique for many reasons (see for example Sikka and Willmott, 2010; Solilová and Nerudová, 2018a; Hsu, Xiao and Xu, 2019; Tax Justice Network, 2020). There are even some ideas and instruments which could improve, i. e. simplify, the situation whilst eliminating the need to apply the arm's length principle (see for example Lang et al. (eds.), 2013; Solilová and Nerudová, 2018b; Solilová and Nerudová, 2019). However, these proposals have not generated enough support on the part of the countries involved since it seems that there would not be a win-win situation considering the impact on the amounts of tax collected in specific countries (for some results regarding European Union see for example European Commission, 2016; Nerudová and Solilová, 2018). One can conclude that despite many problematic issues connected with transfer pricing, and followed by the application of the arm's length principle, there is currently no alternative that has sufficient support to replace them. In other words: observing the current situation and taking note of resistance on the part of the countries involved, transfer pricing and the arm's length principle seem to remain one of the key principles in the efforts of the countries to reach fair allocation of tax bases and fair taxation as such. It only reinforces the need in establishing both relevant and adequate rules for transfer pricing. The rules for transfer pricing as established by law represent, without any doubt, one of the key determinants for the allocation of above stated goal.

The law as such may be viewed both as one of the most complex systems operating in society (Večeřa and Urbanová, 2006), and at the same time one which should respond to changes in social reality[3]. If it does not, then the law cannot fulfil its target, which is to provide appropriate regulation of social relationships. Existing law (*de lege lata*[4]) has always been the subject of criticism for many reasons. To provide better and more suitable legal solutions (*de lege ferenda*[5] considerations), inspiration has traditionally been sought in either the legal regulations of other countries or in previous legal regulations – irrespective of which area of law is involved. In this respect, comparative law has played and continues to play an irreplaceable role. As a discipline of law, comparative law has undergone intensive development over the last century (for a complex analysis see, for example, the comprehensive handbook by Reimann, M. and Zimmermann, R. (eds.), 2008). Fauvarque-Cosson, B. (2008, pp. 62–63), in an analysis of French comparative law, draws generally valid conclusions when observing as follows, *"At a time when supranational legal systems and norms impact every national legal system, comparative law can no longer be viewed as merely the study of foreign law as classified into legal families. Such a view is thoroughly outdated. In today´s world, comparative law must incorporate the progress made by international law. … It is also both important and possible to use comparative law in the law-making process."*[6] Comparative law can, without any doubt, contribute to solving practical problems and compensate for the elements lacking in *de lege lata* while providing valuable input (impetus) to change: foreign legal orders can be inspiring (Melzer, 2011).

Transfer pricing is a complex and complicated economical and legal matter in which certain international aspects[7] must be taken into consideration. For these reasons, the arena of transfer pricing fits perfectly into comparative law and into efforts to find norms for regulations which have proved themselves and which are adaptable to other legal systems either with some modifications or without any modifications.

3 As aptly pointed out by Friedman (1969, p. 29), *"No major social changes occur or are put into effect in a society which are not reflected in some kind of change in its law."*

4 *"[Latin: of (or concerning) the law that is in force]. A phrase used to indicate that a proposition relates to the law as it is."* (Oxford University Press, 2020a)

5 *"[Latin: of (or concerning) the law that is to come into force]. A phrase used to indicate that a proposition relates to what the law ought to be or may in the future be."* (Oxford University Press, 2020b)

6 Regarding comparative law in the V4 countries, one can refer to Kühn (2008, p. 217 and p. 235) who, when providing an analysis of the development of comparative law in central and eastern European countries, observes that, *"The role of comparative law in the region of Central and Eastern Europe has traditionally been defined by practical needs rather than by theoretical interests"* and that *"The current situation of comparative law in the region of Central and Eastern Europe is characterized by both the extensive use of foreign models in legislating and underdeveloped comparative legal studies in academia"*.

7 Both the rules as embodied in soft-law (for example OECD standards OECD, 2017a; OECD, 2017b) and those in hard-law (for example concluded DTTs).

Furthermore, just on the basis of a more general overview one can conclude that transfer pricing legal regulations in the Czech Republic, Hungary, Poland and Slovakia show more or less significant differences despite the fact that transfer pricing legal regulations in these countries are based on the same principles (OECD and EU standards).

2.2 METHODOLOGY

The empirical study presented in the monograph uses a qualitative research approach, as the primary aim is to better understand the social phenomena under investigation (Neergaard and Ulhøi (eds.), 2007; Hendl, 2008; Disman, 2011). The advantage of using a qualitative research design, as opposed to a quantitative one, is that it can facilitate detailed description and insights when investigating individuals, groups, events and/or phenomenon (Hendl, 2008; Vanderstoep and Johnston, 2009; Disman, 2011).

The empirical investigation uses a comparative analysis approach for its methodology, which is in keeping with a qualitative research design. The subject being compared is *transfer pricing in V4 countries* with a focus given on to the *rules governing transfer pricing in V4 countries* as a strategic issue in the realized research. The empirical investigation was designed to address several research questions (issues) that arose in connection with the aim of the research. These questions are outlined in relation to the problem areas of the study and are shown in Table 5. In this respect, the subject and object matter of the empirical investigations are specified in Table 6.

Table 5: Problem areas covered and partial research questions (issues)

Problems areas covered	Fundamental partial research questions (issues)
General background	Which system of law rules in the country?
	What forms of domestic legal acts are established in the country?
	What is the relationship between EU, international and domestic law and how are potential conflicts settled?
OECD and EU standards	Which aspects of transfer pricing are covered by the OECD and EU standards?
	What are the basic (essential) rules as stated by the OECD and EU standards?
	What is the nature and position of the OECD and EU transfer pricing standards in domestic law in the country and how are these standards eventually implemented/reflected in the domestic law?
	Are the attitudes of the countries regarding the process of adopting OECD and EU standards different?
Basic legal framework in particular V4 country	In which type of legal acts/regulations are the rules for transfer pricing included?
	Definition of arm's length principle and associated persons/related parties?
	What is the most common (prevailing) platform for the wording of Art. 9 of Double Tax Treaties concluded by the country? Which one is the most frequent one in relation to the EU Member States?
	Which transfer pricing methods are set or recommended for setting transfer price? Is there a special one not included in the standard by the OECD (OECD, 2017)?
	What are the rules and requirements as set for comparability analysis/compliance analysis?
	Which types of administrative approaches to avoid and resolve transfer pricing disputes are included in the law of the country?
	What are the rules for transfer pricing documentation?
	Are there any special considerations for intangibles, intra-group services and/or cost contribution arrangements?
	Which types of the Advance Pricing Agreements are established by law and what are the rules as set for them?
	Are there any special penalties for breaching transfer pricing rules?
	Are there any special, additional obligations connected with declaration of the transactions between associated persons/related parties?
	Is there case law dealing with transfer pricing issues? What are the rules established therein?

Problems areas covered	Fundamental partial research questions (issues)
Summary – comparison of V4 legal regulation	Which aspects of transfer pricing issues are similar in V4 countries?
	Which aspects of transfer pricing issues differ significantly in V4 countries?
Identification of existing risks and lacks and *de lege ferenda* considerations	What are the significant lacks in material transfer pricing regulations?
	What are the significant lacks in procedural transfer pricing regulations?
	Which general recommendations can be observed regarding transfer pricing regulation in the country?
	Can the legal regulation in one country become an inspiration for legal regulation in another?

Source: own elaboration.

Table 6: Subject and object of the research

Subject of the research	Object of the research	Technique of gathering the data	Research method
Legal regulation as included in international, EU and domestic law	expert literature	study of the documents	content analysis of the text; comparative analysis of the text
	legal regulation (legal acts) in particular	study of the documents	content analysis of the text; comparative analysis of the text
Case law	decisions of the Courts related to transfer pricing in particular countries	study of the documents (decisions of the Courts)	content analysis of the text; comparative analysis of the text

Source: own elaboration.

The empirical analysis is structured as follows. In the first step, the authors of the monograph provide an overview of the standards as set by the OECD and EU. In the second steps, a deeper comparative study of the legal regulations in particular V4 countries was performed. In each of these chapters the authors provide an analysis directed towards a comparison of the standards as set by law and the way in which the V4 countries adopted the OECD and EU standards. In particular, the authors deal with:

a) selected general aspects of legal regulation (type of legal system, type and hierarchy of legal acts, relationships between international, EU and domestic law, position of the OECD standards in the system of law);
b) sources of law related to transfer pricing (international law, EU law and its adoption in the V4 countries domestic law);
c) definition of key terms as set in a particular V4 country (definition of the associated persons/related parties; definition of transfer pricing, if any, and basic principles for transfer pricing as established in domestic law);
d) legal regulation as included in DTTs (namely with the definition of associated enterprises as provided in DTTs and existing platforms of the wording of Art. 9 in DTTs concluded by a particular country);
e) selected issues of transfer pricing regulations (transfer pricing methods approved in a particular country and recommendations regarding their application, comparability analysis/compliance analysis obligation, administrative approaches to avoid and resolve transfer pricing disputes, provisions as provided to govern transfer pricing in specific areas);
f) transfer pricing documentation;
g) APAs;
h) penalties connected with breaking the rules as set for transfer pricing;
i) other obligations related to transfer pricing if any;
j) assessment of the influence of the OECD and EU standards;
k) problematic issues and related case-law;
l) summary of findings.

A comparison of the legal regulations in all the V4 countries is summarised in a separate chapter and the similarities and differences between the compared countries are highlighted with a focus on:

a) key terms in transfer pricing;
b) rules as embodied in DTTs concluded by a particular V4 country;
c) transfer pricing documentation;
d) special clauses for transfer pricing related to sectors/areas;
e) APAs;
f) safe harbours;
g) specific types of penalties relating to breaching of transfer pricing rules;
h) additional transfer pricing statements, and
i) rules for bearing the burden of proof and transfer pricing issues settled by case-law.

In another step the authors focus on identifying the shortcomings in *de lege lata* and present their *de lege ferenda* considerations. The proposals for specific three areas are presented: material law, procedural law and for the area of general and more complex issues. To conclude, the authors of the monograph provide political implications for transfer pricing legal regulation in V4 countries.

The realized study which is based on an extensive review of the related literature, legal acts and other relevant sources of information (e. g. information published on the official web-pages of the OECD, EU and Ministry of Finance of particular countries) and presents the legal state as valid and effective as of 01 January 2020 if not stated otherwise.

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CHAPTER 3
OECD BACKGROUND TO TRANSFER PRICING LEGAL REGULATIONS

3.1 INTRODUCTION

The Organization for Economic Cooperation and Development (OECD) was established in 1961, following on from the Organization for European Economic Cooperation (OEEC) founded in 1948 to implement the so-called Marshall plan, co-financed by the United States to reconstruct the continent after the war. The goal of the OECD is, among other things, to promote fair trade that does not discriminate against any country. The 36 OECD member states implement the organization's mission, that is: *"promoting practices to provide economic and social improvements in the lives of people around the world"* (OECD, 2019a).

MNEs have the possibility of transferring revenues from countries considered to be areas of high taxes, duties, and exchange rates, or high political risk. Transfer pricing may be used for tax optimization (Kim, 2008; Cooper et al., 2016; Martini, 2011; Cecchini et al., 2015). In response to the growing economic power of international OECD corporations, the Committee on Fiscal Affairs approved the Guidelines on Transfer Pricing for International Enterprises and Tax Administrations on July 27, 1995, as the aggregated document based on the previous separate reports (hereinafter referred to as "OECD Transfer Pricing Guidelines"). On the same day, the OECD Council approved a document for publication (OECD, 2017a). The aim of the OECD Transfer Pricing Guidelines is to assist tax administrations in preventing revenue shifting, although it also serves a useful role for taxpayers in proving compliance of transactions with market conditions. OECD Transfer Pricing Guidelines are the basis for shaping the law in individual countries.

The current version of the OECD Transfer Pricing Guidelines, published in 2017, contains the results of work carried out under the Project of the Organization for Economic Cooperation and Development, entitled "Basis of tax erosion and profit transfer" (OECD, 2015). The work was carried out in connection with analysis of tax revenues to the budgets of individual countries, which do not correspond with the growing revenue generated by international corporation. The initiative was aimed at developing tools to counter aggressive tax optimization, made possible due to differences in the tax systems of various countries. As a result of the efforts undertaken at the international level, the OECD and the G20 member states published a report in 2013 called "Action Plan on Base Erosion and Profit Shifting", the aim of which was to improve the coordination of tax authorities' action against the tax avoidance practised by global corporations (OECD, 2015). The report consists of 15 parts devoted to the most important problems in this area. The separate parts of the report contain deadlines for adjusting local regulations in OECD countries so that they are in line with BEPS requirements. Table 7 presents the structure of the reports.

Table 7: Structure of BEPS Reports

Action Number	Name of Action
1	Addressing the Tax Challenges of the Digital Economy
2	Neutralizing the Effects of Hybrid Mismatch Arrangements
3	Designing Effective Controlled Foreign Company Rules
4	Limiting Base Erosion Involving Interest Deductions and Other Financial Payments
5	Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance
6	Preventing the Granting of Treaty Benefits in Inappropriate Circumstances
7	Preventing the Artificial Avoidance of Permanent Establishment Status
8, 9, 10	Aligning Transfer Pricing Outcomes with Value Creation
11	Measuring and Monitoring BEPS
12	Mandatory Disclosure Rules
13	Transfer Pricing Documentation and Country-by-Country Reporting
14	Making Dispute Resolution Mechanisms More Effective
15	Developing a Multilateral Instrument to Modify Bilateral Tax Treaties

Source: own elaboration based on OECD (2015).

From the perspective of companies operating within a company groups, the most important actions are 8, 9, 10 and action13 regarding transfer pricing documentation and reporting by country.

3.2 OECD GUIDELINES ON TRANSFER PRICING FOR INTERNATIONAL ENTERPRISES AND TAX ADMINISTRATIONS AS THE BASIS FOR SHAPING NATIONAL LEGAL REGULATIONS

3.2.1 CONTENT OF OECD TRANSFER PRICING GUIDELINES

The OECD Transfer Pricing Guidelines on Transfer Pricing for International Enterprises and Tax Administrations consist of 9 chapters covering key aspects related to the valuation of benefits between related entities. The scope of the individual chapters is provided in Table 8.

Table 8: Content of OECD Guidelines on Transfer Pricing for International Enterprises and Tax Administrations

Chapter Number	Title
I	The Arm's Length Principle
II	Transfer Pricing Methods (Traditional transaction methods, Transactional profit methods)
III	Comparability Analysis
IV	Administrative Approaches to Avoiding and Resolving Transfer Pricing Disputes
V	Documentation
VI	Special Considerations for Intangibles
VII	Special Considerations for Intra-Group Services
VIII	Cost Contribution Arrangements
XIX	Transfer Pricing Aspect of Business Restructuring

Source: own elaboration based on OECD (2017a).

In the introduction to the latest version of the guidelines, attention was drawn to the particular impact of technological development in the area of communications on intra-group transactions. It was emphasized that differences in administrative requirements in the field of transfer pricing in individual countries may increase the costs of compliance to legal regulations. An important recommendation for tax authorities emerges from the OECD Transfer Pricing Guidelines: *"separate country rules for the taxation of MNE's cannot be viewed in isolation but must be addressed in a broad international context"* (OECD, 2017a).

The question arises whether the Visegrad fund countries comply with the aforementioned principle?

The main recommendations of the guidelines, briefly described below, should be a guide for shaping legal regulations in OECD countries. The scope of application of individual guidelines in various OECD countries would appear to be an important area for research.

3.2.2 CHAPTER I. THE ARM'S LENGTH PRINCIPLE

Regulations, both at the international and national level, provide tax authorities with the right to control and estimate the profits of multinational enterprises, allowing them to retain more of the profits and taxes in a given country. The basis for this approach is the generally accepted Arm's Length Principle, an international standard that was agreed between the OECD members. The Arm's Length Principle is the accepted basis for regulating transfer pricing, according to which the commercial and financial conditions of transactions should be settled as if they were determined by market forces. Associated enterprises should transact with one another as if they were enterprises that were not associated. The foregoing principles have been incorporated into the OECD Model Tax Convention on Income and on Capital, which contains the basic principles of double taxation agreements between OECD member countries (OECD, 2017b). Par. 1 of Article 9 of the OECD Model Tax convention contains the definition of the Arm's Length Principle:

"Where

a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or

b) *the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly."*

There is international consensus about the necessity of applying the arm's length principle as a way to avoid the risk of double taxation (OECD, 2017a, 1.15). However, one can read in the OECD Transfer Pricing Guidelines that tax administrations should not automatically assume that the motivation of associated enterprises is always profit shifting and tax avoidance (OECD, 2017a, par. 1.3).

The idea of global formulary apportionment exists as an alternative, but has been criticized for not protecting single taxation and requiring a common accounting system and complex cooperation among tax administrations (OECD, 2017a, par. 1.24).

The question therefore arises to what extent the arm's length principle applies in individual OECD countries, including the Visegrad fund countries.

One can read that at the heart of the Arm's Length Principle is comparability analysis (OECD, 2017a, par. 1.6). It is worth noting that the subject of comparison may not only be the price, but also financial indicators such as mark-up on costs, gross margin or net profit indicator (OECD, 2017a, par. 1.9). It cannot be forgotten that both taxpayers and tax administrations may have difficulties in obtaining and interpreting comparable data (OECD, 2017a, par. 1.13). There are two significant aspects of comparability analysis:

1) The identification of the economically relevant characteristics of the contractual terms of a transaction (OECD, 2017a, par. 1.1)
2) Comparison of the conditions of controlled transaction with the conditions of transaction between not associated parties (Chapter II and III of OECD Transfer Pricing Guidelines).

The practice of independent enterprises comparing terms of transaction with other options realistically available often appears in OECD Transfer Pricing Guidelines as a preferred behaviour in completing controlled transactions. The reason for this reads as follows (OECD, 2017a, par. 1.38):

"An independent enterprise would only enter into a transaction if it is not expected to make them worse off than their next best option"

The first aspect of comparability analysis is broadened into five issues:

a) the contractual terms of the transaction (OECD, 2017a, par. D. 1.1, 1.42-1.50)
b) the functions performed, assets involved and risks born by the parties to the transaction (OECD, 2017a, par. D.1.2, 1.51-1.106)
c) the characteristics of the subject of the transaction (property or service) (OECD, 2017a, par. D. 1.3, 1.107-1.109)
d) the description of the economic circumstances of the enterprises involved and the sector of the economy they operate in. (OECD, 2017a, par. D.1.4, 1.110-1.113)
e) the business strategy of parties to the transaction (OECD, 2017a, par. D.1.5, 1.114-1.118)

In recognizing the contractual terms of a transaction, a written contract is only the starting point, and other communications between parties as well as the conduct of the parties in performing the transaction should also be taken into account (OECD, 2017a, par. 1.42-1.48).

Functional analysis is the key point of comparability analysis. The economic significance should be considered of the functions performed, in terms of their frequency, nature and value. The comparison of assets used, their nature, age, value, and locations (OECD, 2017a, par. 1.54) is also a part of functional analysis, as well as risk analysis. The assumption of risk determines the profit potential of transactions under market forces, so the allocation of risk should also affect the pricing of controlled transactions[8].

Risk is the effect of uncertainty regarding the objectives of the business (OECD, 2017a, par. 1.71). It is more difficult to identify and assess risk than functions and assets, and it is necessary to identify which

8 There is additional Report of the Attribution of Profits to Permanent Establishments published by OECD, for regulated entities of financial sector.

functions of risk management are performed by the parties (OECD, 2017a, par. 1.82-1.98). This should be considered in connection with financial capacity to assume risk (1.64) and the capability to control risk (OECD, 2017a, par. 1.65).

A non-exclusive list of the most significant risks is presented in the OECD Transfer Pricing Guidelines and contains (OECD, 2017a, par. 1.72):

a) Strategic risks or marketplace risks;
b) Infrastructure or operational risks;
c) Financial risks;
d) Transactional risks;
e) Hazard risks.

3.2.3 CHAPTER II. TRANSFER PRICING METHODS

Chapter II of the OECD Transfer Pricing Guidelines is devoted to a description of transfer pricing methods, divided into (2.1):

a) traditional transaction methods:
   - comparable uncontrolled price method (CUP method) (OECD, 2017a, par. 2.14–2.26),
   - resale price method (OECD, 2017a, par. 2.27–2.44),
   - cost plus method (OECD, 2017a, par. 2.45–2.61),
b) transactional profit methods:
   - transactional net margin method (OECD, 2017a, par. 2.64–2.113),
   - transactional profit split method (OECD, 2017a, par. 2.114–2.251).

The crucial stage of transaction valuation is the choice of method. Important features of each method should be considered, such as (OECD, 2017a, par. 2.2):

- the appropriateness of the method in view of the nature of the transaction,
- the availability of reliable information and
- the degree of comparability between controlled and uncontrolled transactions, including the comparability adjustments needed.

When the traditional transaction method and the transactional profit method can be applied in an equally reliable manner, the first is preferable to the second, but no method is suitable for every possible situation. It is also worth mentioning that, according to the OECD Transfer Pricing Guidelines (OECD, 2017a, par. 3.55): *"transfer pricing is not an exact science, it will not always be possible to determine the single correct arm's length price, rather (…) the correct price may have to be estimated within a range of acceptable figures"*.

Moreover, one should notice that: *"MNE groups retain the freedom to apply methods not described in these Guidelines (hereafter "other methods") to establish prices provided those prices satisfy the arm's length principle in accordance with these Guidelines (…) A taxpayer should maintain and be prepared to provide documentation regarding how its transfer prices were established"* (OECD, 2017a, par. 2.9).

In view of the above, it seems that other methods should be acceptable, in addition to the five recommended. To what extent should the possibility of using other methods be regulated by domestic law?

3.2.4 CHAPTER III. COMPARABILITY ANALYSIS

This chapter contains guidelines for comparability analysis in the meaning of the typical process and alternative possible approaches. The typical process described in the OECD Transfer Pricing Guidelines is not compulsory, but can be considered as good practice. The steps in the process are provided in the Table 9 below.

Table 9: Comparability analysis steps

Steps	Activity
Step 1	Determination of years of analysis
Step 2	Broad-based analysis of the taxpayer's circumstances
Step 3	Analysis of the controlled transaction (Functional analysis, searching for the most appropriate method and the financial indicator that will be tested),
Step 4	Analysis of existing internal comparables, if there are any
Step 5	Searching for available sources of data on external comparables
Step 6	Selection of most appropriate method and the relevant financial indicator
Step 7	Selection of the most appropriate comparables
Step 8	Comparability adjustments
Step 9	Determination of the arm's length remuneration, interpretation of data

Source: own elaboration based on OECD (2017a, par. 3.4).

The chapter contains the definition of a comparable uncontrolled transaction, that is: *"a transaction between two independent parties that is comparable to the controlled transaction under examination"*.
Comparables can however be adjusted according to the following principle: *"To be comparable means that none of the differences (if any) between the situations being compared could materially affect the condition being examined in the methodology or that reasonably accurate adjustments can be made to eliminate the effect of such differences"* (OECD, 2017a, par. 3.47). Typical comparability adjustments include those that may arise from different accounting rules, adjustments for differences in capital, functions, assets or risks.

The steps in comparability analysis are thoroughly explained in the chapter. They are also preceded by the recommendation on not using data unavailable for taxpayers during the taxpayer's audit. Taxpayers should make every effort to justify the comparability of the transaction, but some data is available only for tax administration purposes.

The process of searching for potential comparables should be transparent, systematic and verifiable (OECD, 2017a, par. 3.46). The transparency of the process should be accompanied by appropriate documentation (described in chapter V of the guidelines).

It is worth drawing attention to the fact that foreign source or non-domestic comparables should not be automatically rejected, but require a thorough assessment of reliability, individually for each specific case (OECD, 2017a, par. 3.35).

In order to include or reject potential comparables, both quantitative and qualitative criteria should be used. Examples of recommended quantitative criteria are as follows (OECD, 2017a, par. 3.43):

- Size criteria in terms of Sales, Assets or Number of Employees,
- Intangible-related criteria such as Net Value of Intangibles/Total Net Assets Value, ratio of Research and Development/Sales,
- Criteria related to export sales (Foreign Sales/Total Sales,
- Criteria related to inventories in absolute or relative value and
- Criteria used to exclude third parties such as start-up companies and bankrupt companies.

A properly conducted analysis should enable the determination of remuneration in accordance with the arm's length principle. It is worth stressing that "where the range comprises results of relatively equal and high reliability, it could be argued that any point in the range satisfies the arm's length principle" (OECD, 2017a, par. 3.62). On the other hand, special investigations should be undertaken to identify potential comparables returning losses or abnormally large profits in relation to other potential comparables.

The guidelines also contain timing issues in relation to searching for comparables. In general, the most reliable comparable information should come from transactions carried out in the same period of time as a controlled transaction (OECD, 2017a, par. 3.68). In practice, however, there are some limitations on obtaining such information.

The issue of comparability analysis requirements remains to be resolved under national legal regulations. Should comparability analysis be mandatory for all entities? Should the procedure of conducting comparability analysis be covered by legal requirements? What level of detail should the results of a comparative analysis have in transfer pricing documentation? Can the tax authorities expect the results of a comparability analysis to be submitted in mandatory tax statements or reports?

3.2.5 CHAPTER IV. ADMINISTRATIVE APPROACHES TO AVOIDING AND RESOLVING TRANSFER PRICING DISPUTES

Despite the application of the guidelines in most countries, disputes are always possible when the legal systems of different countries meet. According to the guidelines (OECD, 2017a, par. 4.6):

"Differences in examination practices procedures may be influenced by some factors like system and the structure of tax administration, the geographic size and population of the country, the level of domestic and international trade and cultural influences."

The chapter presents various administrative procedures that can be used to minimize the risk of dispute. An example of a common situation in which a dispute may occur is determining the arm's length conditions that result in double taxation (OECD, 2017a, par. 4.2). The guidelines emphasize that administrative controls on transfer pricing require exceptional specialist knowledge and separate control procedures (OECD, 2017a, par. 4.7).

In the chapter a great deal of attention is paid to the issue of burden of proof. It has been noticed that in most OECD countries the burden of proof lies with the tax administration, while in some countries the opposite is true. These differences cause problems when the transaction is controlled by tax administrations from different countries. The guidelines recommend that, *"as good practice, the burden of proof should not be misused by tax administration or taxpayers as a justification for making groundless or unverifiable assertions about transfer pricing"* (OECD, 2017a, par. 4.16).

The issue that requires examination are the regulations on the burden of proof in individual countries. The motives of the tax authorities seem to be interesting in that they shift the burden of proof onto the taxpayer. What is the scope of regulations in this respect in OECD countries, including the Visegrad fund countries?

In the fifth chapter of the guidelines one can also find a recommendation about the penalties, whether civil or criminal, that tax administrations may adopt(OECD, 2017a, par. 4.18-4.28). The chapter notes that the penalty system should be fair and not unduly onerous for taxpayers.

The level of penalization in terms of transfer pricing in various countries is an interesting area to examine. Are there general or special penalties? What are the motives for more liberal tax administrations?

Special attention in the chapter was given to the Mutual Agreement Procedure (in accordance with the OECD Model Tax Convention) (OECD, 2017a, par. 4.29-4.78) and simultaneous tax examination (OECD, 2017a, par. 4.79-4.94). The question arises to what extent the Mutual Agreement Procedure has been implemented in individual countries. What motivates tax authorities to refrain from implementing this procedure?

Regarding the possibility of using safe harbour, the guidelines have evolved. In 1995, negative opinions prevailed in this respect. Currently, in accordance with the guidelines, the use of safe harbours should be possible for less complex transactions and for transactions which involve low transfer pricing risks (OECD, 2017a, par. 4.109). The guidelines note the benefits of safe harbour for both taxpayers and tax administrations, who can focus on more complex transactions.

Due to the above-mentioned benefits of safe harbours, the popularity of using safe harbours in individual countries is worth exploring.

It is also interesting whether countries that have implemented safe harbours confirm the existence only of benefits, or if they also notice negative consequences.

The guidelines also contain some concerns over safe harbours, such as (OECD, 2017a, par. 4.110):

1. Safe harbours may lead to taxable income that is not in accordance with the arm's length principle;
2. Safe harbours may increase the risk of double taxation or double non-taxation;
3. Safe harbours may enable inappropriate tax planning.

The last important issue described in the chapter are Advance Pricing Arrangements (APA), which determine, in advance of a controlled transaction, an appropriate set of criteria for the determination of transfer pricing over a fixed period of time (OECD, 2017a, par. 4.134). According to Action 1 of the BEPS Action Plan, APAs provide a greater level of certainty and may prevent transfer pricing disputes. In general, there is a recommendation for the implementation of bilateral or multilateral APA programmes, involving more than one tax administration. Unilateral APAs may cause certain problems with double taxation and corresponding adjustments (OECD, 2017a, par. 4.158).

Despite the recommendation to conclude an APA, the popularity of these agreements varies across countries, prompting researchers to investigate the reasons for this. The scope of regulations in individual countries is also an interesting area that can be examined, including forms of entering into agreements, duration, fees, etc.

3.2.6 CHAPTER V. DOCUMENTATION

The chapter about transfer pricing documentation has a significant meaning for taxpayers all over the world. The guidelines were especially valuable when the national legal systems of OECD countries did not contain adopted provisions on transfer pricing documentation. Nowadays, most countries have introduced these provisions into domestic law, but there are some who still refer to the guidelines.

There are crucial objectives in the use transfer pricing documentation. First of all, it helps taxpayers to give appropriate consideration to requirements in establishing transfer pricing and reporting the income derived from controlled transactions. The second aim is to provide tax administrations with information about transfer pricing risks. The third objective is to help tax administrations to conduct audits, although it may be necessary during an audit to complement the transfer pricing documentation with additional documents (OECD, 2017a, par. 5.5). Section C of the chapter consists of a three-tiered approach to transfer pricing documentation, which it is recommended should be implemented in all OECD countries. The approach contains:

a) a master file providing standardized information relevant for all MNE group members,
b) a local file describing local taxpayers' transactions,
c) a country-by-country report providing information referring to the global allocation of an MNE's income within the MNE group.

In the guidelines one can find the expected content of the master file: the nature of the global business operation, overall transfer pricing policies, global allocation of income and economic activity - in order to assist tax administration in evaluating the presence of significant transfer pricing risk, and important agreements. In particular, the information should be divided into the following sections (OECD, 2017a, par. 5.19):

a) the MNE group's organizational structure,
b) a description of the MNE's businesses,
c) the MNE's intangibles,
d) the MNE's intercompany financial activities,
e) the MNE's financial and tax positions.

In-depth information on the content of the master file can be found in Annex 1 to chapter V of the guidelines.

More detailed information about controlled transactions should be included in the local file. The main aim of the local file is to prove that "the taxpayer has complied with the arm's length principle in its material transfer pricing positions affecting a specific jurisdiction" (OECD, 2017a, par. 5.22). According to Annex II to Chapter V the local file should contain in particular:

1. Information about the local entity (among others: description of the management structure, and organization chart, description of the business strategy, key competitors);
2. Information about controlled transactions (among others: description of material controlled transactions, the amount of intra-group payments and receipts for each category of controlled transactions, identification of associated enterprises, detailed comparability and functional

analysis, an identification of the most appropriate transfer pricing method, description of adjustments, copies of APA's);
3. Financial information (among others: financial statements, schedules of relevant financial data, the sources from where the data was obtained).

Requirements referring to the Country-by Country Report are included in Annex III to Chapter V and contain a template for the Country-by Country Report with detailed instructions in terms of the purpose of the report, definitions included in the template, overview of allocation of income, taxes and business activities by tax jurisdiction.

It should be noted that individual countries regulate the scope of transfer pricing documentation and the obligation to prepare it to varying degrees. The question arises as to why there are such differences, and what are the consequences for taxpayers and tax authorities.

3.2.7 CHAPTER VI. SPECIAL CONSIDERATIONS FOR INTANGIBLES

In the contemporary world intangibles are a significant part of companies' assets and can be the source of a competitive advantage. The subject of this chapter is guidelines specially tailored to determining arm's length conditions for transactions involving intangibles. According to the chapter: *"the key consideration is whether a transaction conveys economic value from one associated enterprise to another, whether that be a benefit from tangible property, intangibles, services or other items"* (OECD, 2017a, par. 6.2). In cases where intangibles are used *"it is especially important to conduct a functional analysis on an understanding of the (…) manner in which intangibles are used by the MNE to add or create value across the entire supply chain"* (OECD, 2017a, par. 6.3). The main categories in the chapter recognized in the guidelines are as follows (OECD, 2017a, par. 6.19): patents, know-how and trade secrets, trademarks, trade names and brands, rights under contracts and government licenses, licenses and similar rights in intangibles, goodwill and ongoing concern value. The issue to be examined is the level of regulation of issues regarding intangibles. Do the tax authorities of different countries expect information on transactions involving intangibles to a similar extent?

The chapter in the guidelines is focused among others on such issues as (OECD, 2017a, par. 6.5 – 6.212): identification of intangibles, intangible ownership and contractual terms relating to intangibles, functions, assets and risks related to intangibles, transfer of intangibles, comparability analysis in relation to intangibles, hard-to-value intangibles, applications of transfer pricing methods in relation to intangibles.

It is worth remembering that the OECD has extended the intangibles guidelines by introducing so-called "DEMPE analysis" in the final Actions 8 – 10 „Base Erosion and Profit Shifting" projects in October 2015 (OECD, 2015). DEMPE abbreviation means: Development, Enhancement, Maintenance, Protection and Exploitation. OECD recommends attributing profits from intangible assets to their "economic" owner, which should be preceded by a DEMPE analysis.

The presence of these issues in the regulations of individual OECD countries, including the Visegrad fund countries, is an area worth examining.

3.2.8 CHAPTER VII. SPECIAL CONSIDERATION FOR INTRA-GROUP SERVICES

The chapter deals with the scope of services available to members of almost every MNE group, such as administrative, technical, financial and commercial services. The cost of management and coordination of those services may be borne by the parent company or member company, usually called "a group service centre". According to the guidelines, the most important issues in such transactions is "whether the intra-group services have in fact been provided" and the other issue concerns the compliance of the charge of service to the arm's length principle (OECD, 2017a, par. 7.5). In order to examine the first issue, benefits tests may be performed (OECD, 2017a, par. 7.6-7.8). The charge for services may be calculated by direct-charge methods or indirect-charge methods (OECD, 2017a, par. 7.21-7.26). The chapter notes that some intra-group services may be considered as low value-adding services, which should affect the remuneration for such services. OECD recommended a safe harbour equal to a 5% mark-up on fully-loaded costs for low-value services, what might be useful for valuation of intra-group services (OECD, 2017a, par. 7.43-7.64).

3.2.9 CHAPTER VIII. COST CONTRIBUTION ARRANGEMENTS

Cost Contribution Arrangements (CCA) are the subject of the next chapter of the guidelines. The CCA is defined in the chapter as *"a contractual arrangement among business enterprises to share the contributions and risks involved in the joint development, production or the obtaining of intangibles, tangible assets or services* (…)*"* (OECD, 2017a, par. 8.3). The principles of calculating incomes from the CCA are coherent with the other chapters of the guidelines (OECD, 2017a, par. 8.9), but there are some differences: *"part of all the compensation intended by the participants is the expected mutual and proportionate benefit from the pooling of resources and skills"*. Compliance of the CCA with the arm's length principle is understood in the guidelines to be that the *"value of each participant's contribution should be consistent with the value, that independent enterprises in comparable circumstances would have assigned to that contribution"* (OECD, 2017a, par. 8.25). The question arises whether there are CCA regulations in the national regulations of individual countries and whether they converge. This is important for MNE's.

3.2.10 CHAPTER IX. TRANSFER PRICING ASPECTS OF BUSINESS RESTRUCTURING

According to the chapter, business restructuring refers to the cross-border reorganization of commercial or financial relations between associated enterprises. The chapter provides a list of some examples of restructuring and describes the main issues. The crucial issue is that business restructuring is usually accompanied by a relocation of profit potential among the members of an MNE group, which should be done in accordance with the arm's length principle. The chapter deals with arm's length compensation for restructuring, and provides functional analysis on this matter. The chapter emphasizes that in the case of restructuring, it should always be assessed whether other realistically available options are possible (OECD, 2017a, par. 9.27-9.31). It cannot be forgotten that restructuring is subject to tax transfer pricing documentation (OECD, 2017a, par. 9.32).

Due to the recommendations contained in the guidelines, it is worth examining the expectations of different tax administrations regarding restructuring reporting and the preparation of transfer pricing documentation for restructuring.

3.2.11 FURTHER OECD ACTIONS ON TRANSFER PRICING

Currently, the OECD is working to facilitate the implementation of BEPS in individual countries.

It should be noted that under action 15 of the BEPS "Multilateral Instrument", on 24 November 2016, over 100 jurisdictions concluded negotiations on the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (OECD, 2016). The aim of the Convention is to help governments to modify existing bilateral tax treaties to implement the tax treaty measures developed during the BEPS Project, without the need to expend resources renegotiating each treaty bilaterally. The MLI entered into force on 1 July 2018. As at January 29, 2020, 94 jurisdictions have implemented the Convention (OECD, 2020c). The Convention should be expected to be implemented in other OECD countries.

Some work was carried out under Actions 8-10, which *"address transfer pricing guidance to ensure that transfer pricing outcomes are better aligned with value creation of the MNE group"*.

The following achievements can be mentioned in the area of updating final reports (OECD, 2020a):

1. Additional guidance was published in March 2018 on the attribution of profits to permanent establishments resulting from the changes in the Action 7 Final Report to Article 5 of the OECD Model Tax Convention.
2. Revised guidance on the transactional profit split method (Action 10) was published in June 2018 and will be incorporated into the next edition of the Transfer Pricing Guidelines.
3. Additional guidance addressed to tax administrations on the application of the hard-to-value intangibles (HTVI) approach (Action 8) was finalised in June 2018, and will be incorporated in the next edition of the Transfer Pricing Guidelines.
4. New transfer pricing guidance on financial transactions was published 11 February 2020 (OECD, 2020b).

One part of action 13 that is an important achievement is the release in December 2019 of the Guidance on the Implementation of CbC Reporting (OECD, 2019c).

The OECD Committee on Fiscal Affairs invites interested parties to attend consultations, submit comments or participate in public discussions on transfer pricing issues. There are no current request for input, but recent requests from 2019 are included in Table 10 below.

Table 10: Requests for input in 2019

Type	Topic
Call for input	BEPS Action 14: The OECD invites taxpayers to the tenth batch of dispute resolution peer reviews
Call for input /Public consultation meeting	Global Anti-Base Erosion (GloBE) Proposal under Pillar Two (Live streamed)
Call for input/ Public consultation meeting	Secretariat Proposal for a "Unified Approach" under Pillar One (Live streamed)
Call for input	Practical toolkit to support the successful implementation by developing countries of effective transfer pricing documentation requirements (Platform for Collaboration on Tax)
Call for input	The OECD invites taxpayers to the ninth batch of dispute resolution peer reviews - BEPS Action 14
Call for input	What is driving tax morale? An empirical analysis on social preferences and attitudes towards taxation
Call for input/ Public consultation meeting	The OECD invites taxpayer input on the eighth batch of dispute resolution peer reviews - BEPS Action 14
Call for input/ Public consultation meeting	Addressing the Tax Challenges of the Digitalisation of the Economy

Source: own elaboration based on OECD (2020d).

An important area of the OECD's activity is monitoring legal regulations regarding transfer prices in member countries. As part of the report „Transfer Pricing Country Profiles", countries' domestic legislation can be compared regarding such issues as the arm's length principle, transfer pricing methods, comparability analysis, intangible property, intra-group services, cost contribution agreements, transfer pricing documentation, administrative approaches to avoiding and resolving disputes, safe harbours and other implementation measures (OECD, 2019b).

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CHAPTER 4
EU LAW AND EU TRANSFER PRICING STANDARDS

4.1 EUROPEAN UNION LAW - BACKGROUND

The EU represents a very specific and unique supranational entity of which establishment and development have been connected with the efforts to end frequent and bloody wars between neighbours (European Union, 2019a). The various processes of European integration such as the reoccurring enlargements and simultaneous development of its wide-ranging legal scope and market regulatory powers, have had gradual but significant transformative effects on the countries within and even beyond Europe, as concluded by Knudsen (2015). In the course of time, the idea to unite European countries both economically and politically was gaining new and more extensive forms. It is only logical that these forms of mutual cooperation and "unification" have included tax issues and adoption of related legal regulation on the EU level.

The European Union and its functioning is based on the rule of law, while every action taken by the EU shall be founded on Treaties (for more details see for example European Commission, 2019a). The Treaties come under primary EU law, which represents the basis for secondary EU law. The rules as enshrined in EU primary law are very general in their nature, however, some of them have a direct effect – it is also valid for clauses governing the so-called "four freedoms" (for a more extensive analysis see the study by Savković, 2017). The category of Treaties includes, not solely, the Treaty on the European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU) – see Eur-lex (2020a, 2020b).

Secondary EU law gives more detailed rules on very general provisions as embodied in primary EU law. One can distinguish five basic types of secondary EU law that can be clustered into two basic groups, namely into binding legal instruments and non-binding legal instruments – for a general summary, see the information in Table 11.

Table 11: Secondary EU law

Type of Legal Instrument	Category	Description
Binding	Regulations	Binding legislative acts that must be applied in its entirety across the EU while having a direct effect.
	Directives	Legislative acts that set out a goal that all EU countries must achieve; at the same time, it is up to the individual countries to devise their own laws on how to reach these goals. A directive is capable of having a direct effect, however, some criteria (conditions) as established by the European Court of Justice[*] (ECJ) have to be met.
	Decisions	Binding on those to whom it is addressed (e.g. an EU country or an individual or a company); directly applicable. For the issues of taxation a special attention should be paid to the case-law of the ECJ due to its wider scope. Genschel and Jachtenfuchs (2001, p. 300) provides, regarding the ECJ case-law, this aptly summary, *"While each tax case concerns a particular tax rule in a particular Member State, the resulting case law has a harmonising effect across taxes and Member States because, by providing detailed reasons why the particular rule is (not) in line with EU law, it establishes general principles of acceptable tax policy for the EU as a whole."*

Type of Legal Instrument	Category	Description
Non-binding	Recommendations	A recommendation allows the EU institutions to make their views known (visible) and to suggest a line of action without imposing any legal obligation on those to whom it is addressed. However, sometimes some recommendations are sooner or later reflected in the proposals of legally binding instruments.
	Opinions	Instruments that allow the EU main institutions to make a statement in a non-binding fashion, i. e. without imposing a legal obligation on those to whom it is addressed. An opinion can be issued by the main EU institutions (Commission, Council, Parliament), the Committee of the Regions and the European Economic and Social Committee. The Committees provide their opinions from their specific viewpoint within EU law.

* After Lisboa Treaty titled as the Court of Justice of the European Union (for some basic facts see European Union, 2019c).
For a detailed analysis of the issue of direct effect see, for example, a study by Sophie (2014) and Mătuşescu (2017).
Source: own elaboration based on European Union (2019b).

4.2 EU AND TAXATION

There are different scopes of competencies for the European Union regarding indirect and direct taxes: the area of indirect taxes is extensively harmonised, unlike the area of the direct taxes (Týč, 2008). It is only natural due to the different scopes of competencies for the European Union (or previously European Community) for the areas of direct and indirect taxes. Currently, the basic provisions (boundaries) for establishing EU law in the area of taxation is embodied in TFEU (namely under Art. 110 et seq. (Tax Provisions)). Regarding indirect taxes, there is stated under Art. 113 of TFEU that, *"The Council shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market and to avoid distortion of competition."* (Eur-lex, 2020a) There is no such explicit statement for direct taxes, so the competencies of the European Union regarding direct taxes are currently based on the wording of Art. 115 TFEU which reads as follows, *"Without prejudice to Article 114, the Council shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment or functioning of the internal market."* (Eur-lex, 2020a) Considering taxation, neither fundamental rights as defined under Art. 26 TFEU can be omitted (Free Movement of Persons, Services and Capital; Free Movement of Goods).[9]

Regarding direct taxation, the main priority for tax policy is defined by the European Commission (2020a) as follows, *"addressing the concerns of individuals and businesses operating within the Internal Market by focusing on the elimination of tax obstacles to all forms of cross-border economic activity, in addition to continuing the fight against harmful tax competition and promoting greater cooperation between tax administrations in assuring control and combating fraud."*

The primary EU tax law represents a basis for the secondary one. Following the classification as presented and developed by Adamczyk (In Lang et. al., 2010, p. 23) one can distinguish two basic categories within positive integration in the area of EU direct taxation, namely:

a) harmonisation by *directives removing obstacles* and *directives enhancing cooperation among tax authorities* and
b) coordination for which *binding* and *non-binding* measures are taken.

9 For more details regarding EU tax policy see for example Eur-lex (2020c).

The establishment of another category of directives for a better understanding of the current situation can be perceived as suitable – namely a category of anti-tax avoidance directives. In this respect it should be noted that a strict classification (clustering) of the directives and other acts cannot be made. Directives and other measures comprehend a lot of aspects, thus the classification is made, and can only be made, on the basis of the prevailing features of the measure. For better clarity, the list of the measures for secondary EU law on direct taxation is given in Table 12.

Table 12: EU law on direct taxation

	Category	Acts (measures) adopted in the EU law*
Harmonization by Directives	Removing obstacles	Council Directive 2011/96/EU of 30 November 2011, on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, as amended (Eur-lex, 2020d).
		Council Directive 2009/133/EC of 19 October 2009, on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States, as amended (Eur-lex, 2020e).
		Council Directive 2003/49/EC of 3 June 2003, on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, as amended (Eur-lex, 2020f).
	Enhancing cooperation among tax authorities	Council Directive 2011/16/EU of 15 February 2011, on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC, as amended (Eur-lex, 2020g).
		Council Directive 2010/24/EU of 16 March 2010, concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures (Eur-lex, 2020h).
		Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union (Eur-lex, 2020i).
	Anti-tax avoidance	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, as amended (Eur-lex, 2020j) – called ATAD (Anti-tax Avoidance Directive).
		Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries (Eur-lex, 2020k) – called ATAD II.
Coordination	Binding	For example, Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (90/463/EEC), as amended (Eur-lex, 2020l).
	Non-binding	For example, a code of conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, as amended (Eur-lex, 2020m).
		Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council, of 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD) (Eur-lex, 2020n).

* The list is not an exhaustive one.
Source: own elaboration based on Adamczyk (In Lang et. al., 2010) and sources as listed in the table.

Above stated acts (measures) relate, at least partly, directly or indirectly with transfer pricing issues, and also relate with the category of directives removing obstacles for proper functioning of the single EU market. This fact is made more obvious for cases with an international element and taking into account the existence of different rules as embodied in the domestic law of EU Member Countries.

The relevance of transfer pricing and its connected issues (both in relation to the enabling of the single market functioning properly and elimination of base erosion and profit shifting activities) can be supported by the existence of a special advisory body at the European Commission – the *Joint Transfer Pricing Forum* (JTPF), which assists and advises the European Commission on transfer pricing tax matters (European Commission, 2020b).

4.3 EU TRANSFER PRICING STANDARDS

4.3.1 JOINT TRANSFER PRICING FORUM

Arising problems related to transfer pricing on the background of EU functioning have been extensively described in material by the Commission of the European Communities (2001) in which it was stated, *"the tax problems relating to transfer pricing take on a new dimension"* (Commission of the European Communities, 2001, p. 23) while stressing that a close cooperation of interested parties are of vital importance. To boost it, the JTPF was established. This advisory body of the European Commission has been a very helpful standards making authority for the EU.

The JTPF has one representative from each Member State´s tax administrations and 18 non-government organisation members[10]; chaired by an independent chairperson. Representatives from the candidate countries and from the OECD may be invited as observers (European Commission, 2020b). Priorities set by the JTPF for the period 2015-2019 were set as follows (European Commission, 2019b):

- Work on practical issues arising from country-by-country reporting and transfer pricing documentation;
- Use and improvement of comparable data and comparability methods within the EU;
- Economic valuation methods applied to transfer pricing in the EU;
- Stocktaking, review and assessment of the state of play of multilateral controls in the EU in the area of transfer pricing;
- Assessment of practical issues linked to the use of profit splitting within the EU, once the OECD conclusions will be available;
- Internal monitoring and follow up on the functioning of Dispute Resolution and APAs in transfer pricing.

Selected achievements of the JTPF within the above specified period are presented in Table 13 below.

Table 13: Selected achievements (contributions) by the JTPF (arranged by the date)

	Achievement	Focus/content/recommendations
March 2019	Report on the application of the profit split method within the EU	Analysis of the possibilities and obstacles within the application of the method. A guidance for the application of the method in the Annex 1 (When to apply Profit Split Method) and Annex II (How to apply Profit Split Method) in the document *"The Application of the Profit Split Method within the EU"* (European Commission, 2019c).
October 2018	Report on a coordinated approach to transfer pricing controls within the EU	Presentation of the best practices in the form of various recommendations for both tax administrations and tax-payers. The documents also include results of the survey regarding the implementation of Directive 2011/16/EU and selected related issues (for more details, see European Commission, 2018).
September 2017	Report on the use of Economic Valuation Techniques in Transfer Pricing	A comprehensive description of valuation techniques and the specific elements that should be taken into consideration when using those for transfer pricing purposes.

10 For example, the BEPS Monitoring Groupe, EATLP (European Association of Tax Law Professors), International Tax Center Leiden (Transfer Pricing Research Center) (European Commission, 2020b).

	Achievement	Focus/content/recommendations
March 2017*	Report on the Use of Comparables in the EU	The document presents the best practices and solutions both for tax administration and tax-payers in the EU (European Commission, 2016). It covers aspects relating to: a) comparable search; b) specific aspects dealing with internal comparables; c) specific aspects dealing with external comparables; d) specific aspects of comparability adjustments; e) state of play and way forward on pan-European comparables, and f) assessing the reliability of the comparability analysis.
December 2016	Study on comparable data used for Transfer Pricing in the EU	The study provides an overview and assessment of the availability and quality of market data used for transfer pricing purposes in the EU. Furthermore the study provides assessments and evaluations of the situations characterising the lack and/or non-reliability of comparable data as well as the situation for pan-European comparable searches.
	Study on the application of Economic Valuation Techniques for Determining Transfer Prices of Cross Border Transactions between Members of Multinational Enterprise Groups in the EU	The study provides an overview on how valuation techniques can practically and most efficiently be used for transfer pricing purposes in the EU (especially for the transactions involving intangibles).

* In March 2017, the document was agreed, having been issued in October 2016 (European Commission, 2016).
Source: own elaboration based on European Commission (2020b) and sources as listed in the table.

The JTPF has been active in many other areas, for more details see Table 14 below.

Table 14: Selected achievements (contributions) by the JTPF (arranged by the date)

Year of publication	Achievement	Commentary
2004 (an update in 2009, 2015)	Code of conduct for the effective implementation of the Arbitration Convention	Originated in 2004, a revised Code of Conduct was adopted in 2009 and again in 2015. Concrete recommendations (measures) are proposed (see, for example European Commission, 2015).
2006	Code of conduct on transfer pricing documentation for associated enterprises in the EU	The document standardises the documentation that multinationals must provide to tax authorities on their pricing of cross-border intra-group transactions. The Code is a political commitment only. In this respect, it is stated that, *"It will **not** affect Member States´ rights and obligations or the respective spheres of competence of the Member States and the EU."*
2007	Guidelines for Advance Pricing Agreements (APAs) in the EU	The documents set out a framework for the overall procedure and provides details of how some specific problems could be resolved. The documents include examples of the necessary time frame and the types of areas which would need to be covered by the APA.
2011	Guidelines on low-value-adding intra-group services	The documents propose less resource-intensive approaches to evaluate given types of transactions against arm's length standards. The documents deal with some specific areas such as shareholder costs, cost pools and allocation keys.

Year of publication	Achievement	Commentary
2011	Potential approaches to non-EU triangular cases	The documents deal with non-EU triangular cases as in the cases where two States in a Mutual Agreement Procedure cannot fully resolve any double taxation arising in a transfer pricing case when applying the arm's length principle, because an associated enterprise situated in a third state is identified as being the source of non-arm's-length results in a chain of relevant transactions or commercial/financial relations.
2012	Report on Small and Medium Enterprises (SMEs) and Transfer Pricing	The document presents some ideas to address specific issues of SMEs in the field of transfer pricing; there are presented recommendations concerning areas such as access to information, training, documentation requirements, audit, existing best practices and dispute resolution.
2012	Report on Cost Contribution Arrangements on Services not creating Intangible Property (IP)	In the report the JTPF elaborates on the different concepts underlying Cost Contribution Arrangements on services and Intra Group Services. The report is providing a list of information items that should meet the requirements of most reviewers when determining whether a Cost Contribution Arrangement can be regarded as arm's length. The report provides recommendations to achieve a uniform treatment within the EU.
2013 (final report)	Report on Secondary Adjustments	The report presents some recommendations aimed at avoidance of double taxation and for dispute resolutions (putting in context the EU Parent Subsidiary Directive).
2014	Report on Transfer Pricing Risk Management	The report includes recommendations on managing transfer pricing risk in each of the three phases of examining a transfer pricing file. Furthermore the report contains an example of a work plan for a transfer pricing audit.
2014	Report on Compensating Adjustments	The material provides guidance on double taxation avoidance and double non-taxation in the application of compensating adjustments.

Source: own elaboration based on European Commission (2020b).

To sum above stated and the content of the document, the outputs of the JTPF activities specified above can be considered "mere" soft-law. However, using of the recommendations published in the materials by the JTPF represents (or can represent) a very useful guidance for the application of the general rules relating to transfer pricing. It is also worth mentioning that the standards of the JTPF are based, not surprisingly, on the arm´s length principle as the key principle governing transfer pricing.

4.3.2 ARBITRATION CONVENTION AND TRANSFER PRICING LEGAL REGULATION IN THE SECONDARY EU LAW (SELECTED ISSUES)

Due to the limited competences of the EU for the area of direct taxation, EU law (or the law that originated with the EU or its legal predecessor) covers cases with an international element.

One of the most important measures that originated within the European Community is the *Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (90/463/EEC) (*Arbitration Convention) (Eur-lex, 2020o). This international convention specifies the rules for the Mutual Agreement Procedure and the obligation to set up an Arbitration Procedure when the resolution has not been reached within the determined period. Regarding this Convention, the JTPF was very active (see the information in Table 14 above). Despite these efforts, the Arbitration Convention itself has not proven to be sufficient.

A description of existing problems within the application of rules valid at that time and reason for adopting of a new act to improve the inconvenient situation is provided in the Preamble of the *Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union* in the which the item (1) reads as follows, *"Situations in which different Member States differently interpret or apply the provisions of bilateral tax agreements and conventions or the Convention on the elimination of double taxation in connection with the adjustments of profits of associated enterprises (90/436/EEC) ('the Union Arbitration Convention'), can create serious tax obstacles for businesses operating across borders. They create an excessive tax burden for businesses, and are likely to cause economic distortions and inefficiencies and to have a negative impact on cross-border investment and growth."* The aim of the Directive is to, *"… establish an effective and efficient procedure to resolve disputes in the context of the proper functioning of the internal market, …"*. It should have been implement by 30 June 2019 at the latest[11]. The subject matter and the scope of the Directive is to lay down (European Commission, 2020p), *"… rules on a mechanism to resolve disputes between Member States when those disputes arise from the interpretation and application of agreements and conventions that provide for the elimination of double taxation of income and, where applicable, capital. It also lays down the rights and obligations of the affected persons when such disputes arise. For the purposes of this Directive, the matter giving rise to such disputes is referred to as a 'question in dispute'."* In connection with the application of the Directive, there are included rules for the interaction with national proceedings and derogations (Art. 16) and special provisions for individuals and smaller undertakings (Art. 17). (Eur-lex, 2020p)

The rules on the EU level have naturally been set even for administrative cooperation within which special clauses have been devoted to transfer pricing and closely related issues. The amendments to the Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC (Eur-lex, 2020g) are worth mentioning, above all:

a) *Council Directive (EU) 2015/2376 of 8 December 2015 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation* (so called DAC III) in which a duty to realise mandatory automatic exchange of information on advance cross-border rulings and advance pricing arrangements has been set (Eur-lex, 2020r);
b) *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* (so called DAC IV) in which mandatory automatic exchange of information on the country-by-country report has been set (Eur-lex, 2020q).

As far as the *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* and related acts are involved, one can observe that the issues (problems) covered are related (or better to say, can be related) to the issue of transfer pricing. For more details on the areas covered see for example Eur-lex (2020j).

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CHAPTER 5
LEGAL REGULATIONS IN THE CZECH REPUBLIC

5.1 GENERAL ASPECTS OF LEGAL REGULATION

The Czech legal system can be broadly described as having a "continental" legal system[12], more specifically, due to common historical roots, it comes under "Germanic" legal culture (Bobek, 2006). Bobek (2006) describes the basic features of the Czech legal system as follows:

a) principle areas of law and procedure are codified[13];
b) the system of legal sources is hierarchical, forming a pyramidal structure with constitutional law at the top;
c) only written law (legislature) is, at least in theory, recognised as the source of law.

Pouperová (2018) updated the summary of the Czech legal system provided by Bobek (2006) and states that, *"Only written law (statutes adopted by Parliament and regulations adopted by the Government and administrative authorities) is recognised as formal source law."* The description of the Czech legal system, provided by the official web-pages of the European e-Justice Portal (2019), states that, *"Czech law, which forms part of continental European legal culture, is founded on written law and includes acts and other legislative instruments, promulgated international treaties ratified by the Czech Parliament [Parlament ČR], and rulings of the Constitutional Court [Ústavní soud[14]] annulling all or part of a legislative provision."*

However, the conclusions found within expert Czech law literature, suggest that the legal system in the Czech Republic, as well as in other EU countries, cannot be considered to have a pure continental system – instead the Czech legal system is a mix of both continental and common legal systems. There are many factors in support of such a conclusion. Case law, in both private and public areas[15], is a supplement to written law. Večeřa et al. (2015) describe the way these unwritten sources of law play an important role within the current state and how the activity of judges represents more than a "mere" interpretation of the law - therefore, the legal system in the Czech Republic can be viewed as a mixed one. This conclusion is supported by the role played by the legal principles in the legal system of the Czech Republic. These principles are also relevant to the topic of transfer pricing. The material and procedural legal regulation of transfer pricing (as embodied in the acts) is relatively limited and does not provide clear and obvious rules that allow for solutions in transfer pricing cases, therefore the role of basic principles and of case law are undisputable in this respect.

When considering the legal hierarchy in the Czech Republic, the highest position is taken by the constitutional law norms. Constitutional principles[16] and their sources are respected and included when interpreting the law. The legal norms and their interpretation must also reflect the general introductory provision of Art. 1(1) of the Constitution of the Czech Republic (Constitution of the Czech Republic, Art. 1(1)[17]) from which many global principles governing Czech tax law have been drawn[18]. In relation to public law,

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12 In the continental legal system, the judge does not have the right to create the law; the judge "only" finds the law. Whereas, in common law (the Anglo-American system), the opposite is true: it is the judge who creates the law. Today, one cannot use this single value assessment when classifying a particular legal system. It is true that current legal systems of European countries cannot be described as purely continental due to the changes that occurred. Večeřa et al. (2015).

13 There are, for example, the Civil Code, Criminal Code, Civil and Administrative Procedure Code, etc.

14 For more information see Constitutional Court of the Czech Republic (2015).

15 Including the area of tax legal regulation.

16 For example, the Constitutional Court of the Czech Republic has repeatedly stated as follows, *"Out a number of possible interpretations of the law, it is in any case necessary to apply only the one respecting the constitutional principles (if such an interpretation is possible) and proceed to annulling a provision of an act owing to its unconstitutionality only if the provision concerned cannot be used without violating the constitutionality (the principle of minimising the intervention)."* (Judgement of the Constitutional Court of the Czech Republic of 03 February 1999, file No. Pl. ÚS 19/98)

17 The wording of the provision reads as follows, *"The Czech Republic is a sovereign, unitary, and democratic state governed by the rule of law, founded on respect for the rights and freedoms of man and of citizens."* (Constitution of the Czech Republic, Art. 1(1)) As stated, for example, in the official Commentary on the Constitution of the Czech Republic, to which the judges of the Constitutional Court contributed, it is a principle that has become an important interpretation starting point and an argumentation tool (see Rychetský et al., 2015).

18 For instance, the principle of transparency, accessibility and unambiguousness when handling the sources of law, the general prohibition of retroactivity, the requirement of unambiguousness and predictability, legal certainty, the protection of legitimate expectations, the prohibition of excessive formalism, the protection of confidence in law, and the protection of the acquired rights. In the context of the application of the law, in association with the supremacy of the tax administration bodies as the holder of the public authority, it is also worth mentioning the principle of proportionality, relatively frequently applied by the Constitutional Court of the Czech Republic when protecting the constitutional rights and freedoms (see for example, the Judgement of the Constitutional Court of the Czech Republic of 22 March 2011,

and also to tax law, one of the key principles includes excluding the arbitrary exercise of public power. This principle is explicitly stated in the Constitution of the Czech Republic (Constitution of the Czech Republic, Art. 2(3)[19]) and in the Charter of Fundamental Rights and Freedoms (Charter of Fundamental Rights and Freedoms, Art. 2(2)[20]). The principle of legality for imposing taxes and charges is explicitly enshrined in the Charter of Fundamental Rights and Freedoms (Charter of Fundamental Rights and Freedoms, Art. 11(5)[21]).

Hierarchy of domestic legal acts in the Czech Republic

There are many possible criteria according to which one can classify domestic legal acts (Harvánek et al., 1998), (Knapp, 1995), (Gerloch, 2013). One of them is the legal power criterion. In this respect, there is a pyramidal hierarchy of law in the Czech Republic. At the very top, there are constitutional acts represented by the Constitution of the Czech Republic, Charter of Fundamental Rights and Freedoms and other constitutional acts, followed by "Regular" acts and statutory measures[22]. These two categories are described as primary law (Knapp, 1995). Secondary legal regulations include government orders and regulations issued by the ministries, and subsequently other administrative authorities and local government authorities.

5.1.1 RELATIONSHIPS BETWEEN INTERNATIONAL, EU AND DOMESTIC LAW

In regards to issues of taxation in the Czech Republic, as in other EU countries, it is quite common that a case is regulated by international, EU and domestic law (standards). This is also true for transfer pricing cases; therefore, given this relationship, one could suppose that the number and frequency of collisions has been rising.

The relationship between international law rules and domestic law rules is determined by the Constitution of the Czech Republic (Constitution of the Czech Republic, Art. 10), *"Promulgated treaties, to the ratification of which Parliament has given its consent and by which the Czech Republic is bound, form a part of the legal order; if a treaty provides something other than that which a statute provides, the treaty shall apply."*[23] The obligation to observe international law is also set in the introductory part of the Constitution of the Czech Republic, *"The Czech Republic shall observe its obligations resulting from international law."* (Constitution of the Czech Republic, Art. 1(2)) The Czech Republic is, among others, a contracting party to the Vienna Convention on the Law of Tax Treaties[24] (United Nations, 1980), which also gives the background to its duty to observe international law as embodied in international treaties. It is also a contracting party to the European Convention on Human Rights (European Court of Human Rights, 2020), which covers issues of taxation (European Court of Human Rights, 2019). Therefore, regarding the relationship between international and domestic law one can speak of an *international treaties application priority*. Malenovský (2008) describes this feature more precisely as "a conditional international treaties application priority to the act".

EU law (previously Community Law) is applied on the same principle, as stated above for international law: if there is a collision between the rules set by EU law and rules set by domestic law, the EU law shall prevail as it is the dominant one. This relationship was historically established in the notorious case law of the European Court of Justice[25]: namely the decisions in Van Gend a Loos (Judgement of the European Court of Justice in the Case NV Algemene Transport- en Expeditie Onderneming van Gend & Loos (case 26/62)) and Costa v E.N.E.L. (Judgement of the European Court of Justice in the Case Flaminio Costa v E.N.E.L. (case 6/64)). However, there are some exceptions to the above given rule which relate to constitutional law clauses. For some cases, the principle of application priority is not valid. When there is a collision between

file No. Pl. ÚS 24/10). For more details, see the Judgement of the Constitutional Judgement of the Constitutional Court of the Czech Republic of 23 May 2000, file No. Pl. ÚS 24/1999 and Judgement of the Constitutional Court of the Czech Republic of 24 May 1994, file No. Pl. ÚS 16/1993. For more extensive reference to the related decision-making practice of the Constitutional Court of the Czech Republic see, for example , the Judgement of the Constitutional Court of the Czech Republic of 01 March 2011, file No. Pl. ÚS 55/2010 and Judgement of the Constitutional Court of the Czech Republic of 28 January 2004, file No. I. ÚS 546/2003.
A summary of the findings can also be found in expert literature by Rychetský et al. (2015), Klíma et al. (2009) and Wágnerová et al. (2012).

19 Art. 2(3) of the Constitution of the Czech Republic reads as follows, *"State authority is to serve all citizens and may be asserted only in cases, within the bounds, and in the manner provided for by law."*

20 Art. 2(2) of the Charter of Fundamental Rights and Freedoms reads as follows, *"State authority may be asserted only in cases and within the bounds provided for by law and only in the manner prescribed by law."*

21 Art. 11(5) of the Charter of Fundamental Rights and Freedoms reads as follows, *"Taxes and fees shall be levied only on the basis of an act."*

22 Statutory measures issued solely by the Senate of the Czech Republic.

23 The same rule can be found in the Income Tax Act (Income Tax Act, 1992, Sec. 37).

24 Published under No. 2/1988 in the Collection of Law.

25 Currently titled the Court of Justice of the EU.

the material core of constitutional law and EU law, the constitutional law should prevail (Týč, Sehnálek and Charvát, 2011, pp. 36 et seq.)[26].

In tax issues, including transfer pricing, a collision between EU and international law can occur. It is only logical that in such cases any potential collision is eliminated, as if there is a collision then, thanks to the application priority, EU law is favoured (Kučera, 2009)[27].

5.1.2 OECD STANDARDS IN THE CZECH REPUBLIC LAW SYSTEM

The Czech Republic has been an OECD member country since 1995 (OECD, 2019a) and since then has been bound by duties connected with being a Member State. However, in general the OECD standards seem to be "mere" soft law, and not legally binding, as such, in the Czech Republic. According to the knowledge of the author of this chapter, there is no direct reference to the OECD standards in the primary domestic laws of the Czech Republic. However, as a result of the implementation of the OECD BEPS action plan through EU law implementation, some of the OECD standards have been reflected in primary law acts of the Czech Republic[28]. At the same time, the OECD standards play an important role in the application of the rules embodied in domestic and international law: especially in the area of Double Tax Treaties (DTTs) and of transfer pricing.

The Czech Republic has been a contracting state in more than 80 DTTs (Ministry of Finance of the Czech Republic, 2019a). In this respect, the OECD Model Convention, and its commentary, play an important role, as they are generally recognized and extensively used[29]. However, Russo et al. (2007) highlight that the role of the Commentary to the OECD Model Convention as a tool for the interpretation of the OECD Model Convention is not routinely fully understood in the same way. In the Czech Republic, the Czech Supreme Administrative Court concluded that the Commentary to the OECD Model Convention represented a supplementary means of interpretation[30] (see, e.g., the Judgement of the Supreme Administrative Court of the Czech Republic of 10 February 2005, file No. 1 Afs 108/2004). Furthermore, the Czech Republic is a contracting party to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (OECD, 2020).

The legal regulation of transfer pricing in Czech domestic law (compared with the legal regulation in Slovakia, Hungary and Poland) can be considered to be a very limited one. Unlike the remaining V4 countries, there is no direct reference to the OECD transfer pricing standards in the primary law of the Czech Republic (i.e. in the acts). These OECD standards again take the position of soft-law. Their position has been defined in the case law of the Czech administrative Courts. For example, the Judgement of the Supreme Administrative Court of the Czech Republic of 25 June 2014, File No. 7 Afs 94/2012 states that, *"These instruments[31] for determination of real economic substance of the examined transactions represent without any doubt a valuable guidance for dealing with a specific particular case both for the purposes of the application of Sec. 23(7) of the Income Tax Act and purposes of the application of Sec. 35a(2) letter d) of the Income Tax Act, as well as for the purposes of the application of the bilateral Double Tax Treaties. They, however, shall not be considered as legal regulation in the strict sense of the term, but as a possible guidelines (aid) for the analysis of the real economical substance of the examined relationships and within the searching which functions and economic reasons existed on the part of particular entities participating in the business operations of the complainant in her business activities as a whole."*

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26 For more details, see Chapter III. of the book. This chapter deals with the issue of the EU Law Priority to Domestic Law of Member States and its Limits.

27 However, there is a departure from this rule. The relationship of international treaties concluded by the European Union (previously by the European Community) is granted an application priority to the secondary EU law (Malenovský, 2008).

28 For instance, Council Directive (EU) 2016/1164 of July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (Eur-Lex (2020a).

29 The first Czech official translation of the Commentary to the OECD Model Convention was published in the Czech Republic in 2009 (OECD, 2009).

30 Therefore, it has made a reference to Article 32 of the Vienna Convention on the Law of Treaties that reads as follows, *"Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstance of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:*
a) Leaves the meaning ambiguous or obscure; or
b) Leads to a result which is manifestly absurd of unreasonable." (United Nations, 1980).

31 Within the meaning of the interpretation documents of the OECD.

There are many references to the OECD standards (primarily in the OECD Transfer Pricing Guidelines (OECD, 2017a) in the 'D-series' Guidelines and instructions published by the General Financial Directorate, and previously by the Ministry of Finance of the Czech Republic. However, the D series Guidelines and instructions issued by the General Tax Directorate of the Czech Republic, as well as the instructions issued by the Ministry of Finance of the Czech Republic, do not have the nature of generally binding legal regulations. On the other hand, as stated in the Judgement of the Supreme Administrative Court of the Czech Republic of 16 August 2010 file No. 2 Afs 53/2010, *"… the instructions of the ministries are internal regulations which regulate and unify the practice of the administrative authorities. Although the instructions of the ministries are not generally binding legal regulations, the administrative authorities have an obligation to follow them in their legal practice, which is not the case only if such practice does not comply with generally binding legal regulations."* A summary of the conclusions relating to the issue of the obligatory nature of the D Series Guidelines can be found under items [23] and [24] of the Judgement of the Supreme Administrative Court of the Czech Republic of 04 October 2018 file No. 2 As 94/2018.

The financial administration of the Czech Republic (namely the General Tax Directorate of the Czech Republic, which can be considered an authority as it sets the standards for the financial administration), expressed its view on the updated OECD Guidelines on transfer pricing in the updated guidelines published in the Financial Bulletin of the Czech Republic Ministry of Finance (Ministry of Finance of the Czech Republic, 2019b). The Czech Ministry of Finance (Ministry of Finance of the Czech Republic, 2019b), when dealing with the relevance and "obligatory nature" of the OECD Transfer Pricing Guidelines, presented these remarks and comments:

a) Using the OECD standards (using the rules included therein) has become a respected and applied standard both on the part of tax subjects and tax authorities over the course of time.
b) The rules as included in the OECD Guidelines have been implemented even in relationships with no international element – thus a *"sui generis"* administrative practice has been established.
c) Using the OECD Guidelines contributes to legal certainty on the part of tax-payers and, at the same time, sets predictable rules applied by the tax authorities.

It is worth mentioning that in the aforementioned Financial Bulletin of the Czech Republic's Ministry of Finance, (Ministry of Finance of the Czech Republic, 2019b) the Czech General Financial Directorate, published another valuable document: a Czech translation of the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration 2017*. This publication diminishes the objections against the application of these standards in relation to solely domestic transactions and/or transactions realized with a subject from a non-contracting[32] country. It could be suggested that, when observing the development in the practice and rules as embodied in the 'D-series' Guidelines, the position of the OECD standards is becoming stronger.

Taking into account the position of tax subjects, despite the 'D-series' Guidelines not being directly legally binding, they are of great importance to them. Fučík (2015), a highly esteemed Czech tax expert, describes the position of the 'D-series' Guidelines as follows, *"… the instructions issued by the General Financial Directorate do not represent generally valid regulations, on the other hand they can be described as "a specific source" of tax law source, because they have certain legal power."*

In regards to the OECD standards for cases with international elements, there are no objections to the OECD transfer pricing as binding standards within the application of Art. 9 (*Associated Persons*) and other related provisions[33] as enshrined in DTTs. In the Czech Republic, the OECD transfer pricings standards are viewed as an interpretation rule according to Art. 31 of the Vienna Convention on the Law of Treaties (United Nations, 1980). For the rules, see Table 15.

32 I.e. a country which does not have a DTT concluded with the Czech Republic.
33 For example, Art. 5 (Permanent Establishment) in connection with Art. 7 (Business Profit), selected provisions of Art. 11 (Interest) and Art. 12 (Royalties) (for more details see e. g. (OECD, 2017b)).

Table 15: Summary of content of Art. 31 of the Vienna Convention on the law of treaties

<table>
<tr><th colspan="3">Provision</th><th>Content</th></tr>
<tr><td rowspan="4">General rule for the interpretation</td><td rowspan="4">Art. 31</td><td>para. 1</td><td>A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.</td></tr>
<tr><td>para. 2</td><td>The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
a) Any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty;
b) Any instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.</td></tr>
<tr><td>para. 3</td><td>There shall be taken into account, together with the context:
a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
b) Any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
c) Any relevant rules of international law applicable in the relations between the parties.</td></tr>
<tr><td>para. 4</td><td>A special meaning shall be given to a term if it is established that the parties so intended.</td></tr>
</table>

Source: own elaboration based on United Nations (1980).

5.2 SOURCES OF LAW INCLUDING (OR RELATED TO) TRANSFER PRICING

5.2.1 INTERNATIONAL LAW AND TRANSFER PRICING

The Czech Republic has been a contracting party to 88 DTTs. In these cases, the Czech Republic has been bound by the rules embodied under Art. 9 (*Associated Persons*) and other related provisions of particular DTTs.

Regarding the interpretation and application of Art. 9 and related provisions of a particular DTT, the *OECD Transfer Pricing Guidelines* (OECD, 2017a) is legally binding as an interpretation guideline. This conclusion has also been explicitly expressed in Guidance D-34 by the General Financial Directorate (which methodically manages the financial authorities) (Ministry of Finance of the Czech Republic, 2019b). In general, there are no reservations or observations for using the OECD standards in situations with an international element[34], since the Czech Republic is a contracting party to the Vienna Convention on the law of treaties and the OECD transfer pricing guidelines are understood as an interpretation aid.

In terms of cross-border tax procedures, it is also worth mentioning that the Czech Republic is a contracting party to the Arbitration Convention 90/436/EEC on the Elimination of double Taxation in Connection with the Adjustment of Profits of Associated Enterprises (hereinafter referred to as “Arbitration Convention” only)[35] (Eur-lex, 2020b). In terms of cross-border tax procedures (potentially also connected with transfer pricing) it is also relevant that the Czech Republic has been a contracting party to MLI (OECD, 2020). However, as of 23 January 2020 the MLI has not entered in force for the Czech Republic yet (OECD, 2020).

5.2.2 EU LAW AND TRANSFER PRICING

In general, there are two categories of EU standards that are implemented in Czech domestic standards – soft-law and hard-law. In the area of transfer pricing, there is a tendency to embody EU soft-law in Czech domestic rules using the D Series Guidelines (for more details see the text relating to the D series Guidelines below). In these guidelines there are frequent references to EU standards as established by the Joint Transfer Pricing Forum (JTPF) including:

a) a code of conduct for the effective implementation of the Arbitration Convention;
b) a code of conduct on transfer pricing documentation for associated enterprises in the EU;
c) guidelines for Advance Pricing Agreements (APAs) in the EU and
d) guidelines on low-value-adding intra-group services. (European Commission, 2020)

34 This issue is less problematic when compared with cases with a sole domestic element.
35 Despite having its origin in the European Union, the Arbitration Convention as a treaty comes under the legal sources of international law.

Other “standards” identified in the reports and recommendations by the JTPF could be utilised by taxpayers as well[36].

In hard-law, the Czech Republic, as an EU Member State, has been naturally bound by EU law. In this respect, the directives (as the source of secondary EU law) have been – as a rule – transposed in the acts. This way of implementing directives stays valid also for the directive that reflects the recommendations from the BEPS project – i.e. the Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, as amended (Eur-lex, 2020a), which has been implemented in the provisions of the Income Tax Act (Income Tax Act, 1992).

By the end of June 2019, the Czech Republic should have implemented the Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union (Eur-lex, 2020c), which followed the Arbitration Convention, whose aim is to make the settlement of tax disputes more effective. The Czech Republic has opted for drafting a special procedural regulation (an act) having the status of a special act (*lex specialis*) to the Tax Procedural Code (Tax Procedural Code, 2009). As of the last update of this part of the chapter[37], there has been a delay in the implementation of the Directive; only a bill has been submitted by the Government of the Czech Republic to the Chamber of Deputies of the Czech Republic (Chamber of Deputies of the Parliament of the Czech Republic, 2019).

Transfer pricing issues and its control in the international environment is conditioned by effective cooperation between states. The Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC as amended (Eur-lex, 2020d) is of great importance in this respect. Regarding transfer pricing it is worth mentioning its amendment by DAC IV – 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 (Eur-lex, 2020e)[38]. The standards set in this Directive and its amendments have been reflected in Act No. 164/2013 Coll., on international cooperation within tax administration and on amendments of other related acts, as amended (Act on International Cooperation within Tax Administration, 2013).

5.2.3 CZECH DOMESTIC LAW AND TRANSFER PRICING

The material provisions for transfer pricing are included in the Income Tax Act (Income Tax Act, 1992) and the procedural ones in the Tax Procedural Code (Tax Procedural Code, 2009)[39]. Not considering the rules as set by the ATAD Directive, the explicit legal regulation of transfer pricing as included in the Czech Income Tax Act is not an extensive one. The Income Tax Act contains only:

a) a definition of associated persons[40] (Income Tax Act, 1992, Sec. 23(7)),
b) a definition of the arm´s length principle (Income Tax Act, 1992, Sec. 23(7)),
c) rules for the taxation in cases of a transfer of the property realized without a change in the ownership (Income Tax Act, 1992, Sec. 23g),
d) rules for a binding ruling on the way in which the price negotiated between associated persons was set (Income Tax Act, 1992, Sec. 23 g).

The procedural aspects connected with transfer pricing are included, as stated above, in the Tax Procedural Code (2009). In the Tax Procedural Code (2009) there is, unlike in other countries, no special legal regulation for transfer pricing issues. Therefore, general clauses, as embodied in the Tax Procedural Code (2009), are used even in such a specific area. As a result of EU law, in future some procedural issues are supposed to be regulated by a special procedural act.

36 For example, Report on Small and Medium Enterprises (SMEs) and Transfer Pricing, Report on Cost Contribution Arrangements on Services not creating Intangible Property (IP), Report on Compensation Adjustments; for more details see (European Commission, 2020).

37 As of 01 February 2020.

38 Reflected under Sec. 13u et seq. (Automatic Exchange of Information on Tax Authorities Opinion for the cases with International Element) and under Sec. 13za et seq. (Automatic Exchange of Information Provided by Multinational Enterprises) of the Act No. 164/2013 Coll., on international cooperation within tax administration and on amendments of other related acts, as amended (Act on International Cooperation within Tax Administration, 2013).

39 This act takes a position of *lex generalis* compared to other acts (see Tax Procedural Code (2009, Sec. 4) – the standards stated therein shall be applied if not stated otherwise in another act.

40 If stated otherwise in a particular DTT, then such a definition prevails over the definition contained in the Income Tax Act due to application priority of international treaties over domestic law (Constitution of the Czech Republic, 1993, Art. 10).

Since the legal regulation, as contained in material and procedural law (acts), is relatively brief and general, the case law of the administrative Courts has played an important and irreplaceable role with the interpretation of general transfer pricing rules as enshrined in the acts (see, for example, Solilová and Nerudová, 2019; Brychta and Svirák, 2017). To eliminate any undesirable ambiguity, the Ministry of Finance and currently the General Financial Directorate[41] have published a series of guidelines. Their content is outlined in Table 16.

Table 16: Summary of the guidelines published by the Financial Administration of the Czech Republic that are relevant for transfer pricing issues

Title and year of publication	Areas covered	Previous regulation if any	Commentary
Guidance D-10 (2012)	Safe-harbours (Low Value Adding Intra-Group Services)	X	Specification of the conditions under which the simplified rules for setting the transfer prices can be applied.
Guidance D-22 (2015)*	Guidelines for the implementation of the provisions of the Income Tax Act including the rules as embodied under its Sec. 23 (7).	Guidance D-6	Specification of the rules as stated under Sec. 23(7) of the Income Tax Act and other provisions related to transfer pricing. A reference to other related guidelines for the area of transfer pricing is included.
Guidance D-32 (2018)	Binding ruling on transfer pricing and setting the tax base of a permanent establishment of a tax non-resident.	Guidance D-333	Previous guidelines dealt only with the first aspect, currently it covers also the guidelines for the application of Sec. 38nd of the Income Tax Act (setting of the tax base of a Czech tax non-resident).
Guidance D-34 (2019)	Communication on the implementation of the international standards for taxation of the transaction between associated persons – transfer prices. It covers also the guidelines for the application of the methods of setting the transfer price as set by the OECD (2017a).	Guidance D-332	While reacting to the BEPS, D-332 Guidance was replaced by the more extensive Guidance D-34 which includes the standards as established by the OECD (2017a). Current (Guidance D-34), and also a previous (Guidance D-332) version of the document, have summarized the basic rules as stated in EU, international and domestic law. These guidelines are the most extensive (they represent a summary of the OECD standards considered to be the most important from the view point of the Financial Administration of the Czech Republic).
Guidance D-334 (2010)**	Scope and form of transfer pricing documentation	Guidance D-293	The recommendations relate both to domestic and international transactions. The rules are very general, for the detailed rules related to functional and risk analysis, the use of Guidance D-34 is suitable.

* Guidance D-22 was published on 06 February 2015 but it could be used – as stated under its Art. III – already for the taxable period starting in the calendar year 2014 (General Financial Directorate, 2015).

41 It is connected with a change in the structure and changes in the competencies of the bodies established with the Financial Administration of the Czech Republic (for more information see Act No. 456/2011 Coll., on Financial Administration of the Czech Republic, as amended (Act on Financial Administration of the Czech Republic, 2011)).

** There is a presumption that Guidance D-333 will be replaced soon by a new one (Guidance D-35) – see the reference in Guidance D-34 by the (General Financial Directorate, 2019).

Source: own elaboration based on Ministry of Finance of the Czech Republic (2010a), General Financial Directorate (2012, 2015, 2018, 2019).

As already mentioned above, unlike the acts, the 'D-series' Guidelines do not take the position of a legally binding legal regulation. However, these documents are broadly accepted and in many aspects, if the Czech translation of the OECD transfer pricing guidelines is not taken into account, they represent the only available provisions governing transfer pricing issues.

5.3 DEFINITION OF KEY TERMS IN DOMESTIC LAW

5.3.1 DEFINITION OF ASSOCIATED PERSONS IN DOMESTIC LAW

In the Czech Republic the associated persons and arm´s length principle definitions are embodied in Sec. 23 (7) of the Income Tax Act (Income Tax Act, 1992). Czech material law includes two basic categories of the associated persons: persons associated through capital and persons otherwise associated (for detailed definitions see Table 17).

Table 17: Summary of associated persons as defined in Czech domestic law

Categories of associated persons	
Persons associated through capital	**Persons associated otherwise**
Persons associated directly 1. Where one person directly participates in the capital or voting rights of the other person, or where one person directly participates in the capital or voting rights of several persons; and where, simultaneously, this share constitutes at least 25 % of the registered capital or 25 % of the voting rights of such persons, then all such persons are persons directly mutually associated through capital. **Persons associated indirectly** 2. Where one person indirectly participates in the capital or voting rights of the other person or where one person directly or indirectly participates in the capital or voting rights of several persons; and where, simultaneously, this share constitutes at least 25 % of the registered capital or 25 % of the voting rights of such persons, then all such persons are persons mutually associated through capital.	1. Persons where one person participates in the management or control of another person 2. Where identical persons or close persons participate in the management or control of other persons, then such other persons are persons otherwise mutually associated. Persons otherwise associated shall not be deemed to be persons where one person is a member of the supervisory boards of two persons. The participation in a control committee or similar control body and carrying out a control for a reward is not considered participation in the control (Income Tax Act, Sec. 23(7) in fine). 3. Controlling and controlled persons and also persons controlled by the same controlling person. 4. Close persons. 5. Persons that created a legal relationship predominantly for the purpose of reducing a tax base or increasing a tax loss.

Source: own elaboration based on Income Tax Act (1992, Sec. 23(7)).

The share in capital or in voting rights in the taxable period or the period for which the tax return is submitted is set as a calculation of the month's average values (Income Tax Act, 1992, Sec. 23(7)). As stated in Guidance D-22 (General Financial Directorate, 2015), the meeting of the conditions, as specified under Sec. 23(7) of the Income Tax Act, is assessed at the time of the conclusion of the contract even in the event that the contracting parties cease from being the associated persons during the course of the fulfilling contract. The General Financial Directorate (General Financial Directorate, 2015) refers to the principles stated in the OECD Guidelines, and above all to the arm´s length principle.

A close person as defined under Sec. 23(7) of the Income Tax Act (Income Tax Act, 1992) means a close person as specified under Sec. 22(1) of the Civil Code (General Financial Directorate, 2015).

A close person is a relative in the direct line; a sibling and a spouse or a partner according to another act governing registered partnership. Other persons in a family or similar relationship are viewed to be close persons to each other if harm suffered by one of them is perceived as his or her own harm by the other. Persons related by marriage or persons permanently living together are also presumed to be close persons. (Civil Code, 2012, Sec. 22(1))

5.3.2 DEFINITION OF TRANSFER PRICING AND BASIC PRINCIPLES IN DOMESTIC LAW

An exact definition of transfer pricing is not included in any Czech domestic act. However, references to the OECD standards have been included in the D Series Guidelines. The most extensive description and guidance on transfer pricing has been provided by the General Financial Directorate in Guidance D-34 (General Financial Directorate, 2019), and in its predecessor Guidance D-332 (Ministry of Finance of the Czech Republic, 2010b).

The application of the arm´s length principle itself has been connected with two other related aspects of a particular transaction. Three basic principles (tests) applied by the Czech financial authorities within tax audits aimed purely or partly at transfer pricing are:

a) the substance test,
b) the benefit test and
c) the arm´s length test (principle). (Solilová and Nerudová, 2019)

The arm´s length test is not applied separately; its application is preceded by the application of the substance and benefit test. The aim of the substance test is to verify whether the transaction (operation) has been realized at all, the meaning of the benefit test is to assess whether the transaction (operation) was relevant from the point of view of the needs (typically whether the operation is related to the performance of business activity and serves to achieve, secure and maintain the income). The sequence is logical and has been affirmed by consistent, related case law (see, e.g., the Judgement of the Supreme Administrative Court of the Czech Republic of 02 March 2011 File No. 8 Afs 19/2010).

The definition of the arm´s length test (principle) has been embodied in the Income Tax Act since 1992 (Income Tax Act, 1992, Sec. 23(7)). The definition of the arm´s length principle until 31 December 2013 reads as follows, *"Where prices agreed between associated persons differ from the prices that would be agreed between independent persons in usual business relationships under the same or similar conditions, without such difference being properly justified, the tax administrator shall adjust taxpayer´s tax base by the ascertained difference …"*. The current definition of the arm´s length principle reads as follows, *"Where prices agreed between associated persons differ from the prices that would be agreed between independent persons in usual business relationships under the same or similar conditions, without such difference being properly justified, the taxpayer's tax base is adjusted by the ascertained difference …"*. Since 2014 the tax-payer can also make an adjustment to the tax base in the event he finds that the price set was not in harmony with the arm´s length principle.

When setting the transfer price, in the event that the price that would be agreed between independent persons in usual business relationships under the same or similar conditions could not be ascertained, then the value of the transaction is set according to special legislation governing the assets valuation[42]. Sec. 23(7) of the Income Tax Act provides a list of the situations in which the arm´s length principle cannot be applied:

a) when a contract on a precarious loan is concluded;
b) when a contract on a loan for use is concluded;
c) when the interest from the loan´s financial instrument between associated persons is lower than the interest that would be agreed between non-associated persons and, at the same time, the creditor is a tax non-resident or a member of a corporation that is a tax resident of the Czech Republic, or a tax-payer of natural person income tax.

Bearing of the burden of the proof

The rules for bearing the burden of proof for tax cases differ among OECD member countries (OECD, 2017a, p. 174). In the case of the Czech Republic the rules for the bearing of the burden of proof are embodied

42 Namely Act on Property Evaluation (1997).

under Sec. 92 of the Tax Procedural Code (Tax Procedural Code, 2009, Sec. 92). The fundamental rules are outlined in Table 18 below.

Table 18: Summary of the selected rules for bearing the burden of proof as embodied in the Czech Tax Procedural Code

Provision	Rule(s) stated therein
Sec. 92(2)	The tax authority shall ensure that the circumstances decisive for correct ascertainment and setting are ascertained as completely as possible, and, in doing so, is not bound by just the proposals of the tax subjects.
Sec. 92(3)	The tax subject shall have to prove all circumstances that it is obligated to state in a due tax return, additional tax return and other submissions.
Sec. 92(4)	If so required by the course of the procedure, the tax authority can call upon the tax subject to prove circumstances necessary for the correct setting of tax, provided that the necessary information cannot be obtained from its own official records.
Sec. 92(5) c)	The tax authority shall have to prove ... circumstances refuting the credibility, conclusiveness, accuracy or completeness of mandatory records, accounting records, as well as other records, documents and other means of evidence asserted by the tax subject.
Sec. 92(5) d)	The tax authority shall have to prove ... circumstances decisive for the evaluation of the actual content of a legal act or other circumstance.
Sec. 92(5) e)	The tax authority shall have to prove ... circumstances decisive for the application of consequences for breach of obligation in tax administration.

Source: own elaboration based on Tax Procedural Code (2009, Sec. 92).

The rules for the bearing of the burden of proof and their mutual relations have been established in the case law of the administrative Courts. As stated, for example in the Judgement of the Supreme Administrative Court of the Czech Republic of 27 June 2007 file No. 1 Afs 60/2006 and in the Judgement of the Supreme Administrative Court of 20 November 2014 file No. 9 Afs 92/2013, there are three specific cumulative conditions under which the arm´s length principle rule, as stated in the Income Tax Act (Income Tax Act, 1992), can be applied. These conditions - that have to be met at the same time - are as follows:

1. Associated persons are involved[43],
2. The prices agreed upon between them differ from the prices that would be agreed upon between independent persons in standard relationships under the same or similar conditions, and, at the same time,
3. Such a difference was not satisfactorily substantiated by the taxpayer.

The fulfilment of the first requirement is not, as a rule, problematic. It is an issue not disputed by the persons themselves due to publicly available data in the Register of Companies. The second condition relates to the obligation of the tax authority to ascertain the price agreed between associated persons[44] and to ascertain the so-called reference price[45]. However, the existence of the difference between the actual and reference price does not automatically lead to an adjustment of the tax base by the tax authority. In this respect, the tax-payer has to be provided with enough time (as deduced and set by the related case law) to prove the relevance of the transfer pricing that was set by him (he has to be provided with time for the justification of the existing difference; difference between the price insisted on by the tax authority and by him).

43 In the Judgement of the Supreme Administrative Court of the Czech Republic of 27 January 2011 file No. 7 Afs 74/2010, the Supreme Administrative Court described the associated persons as, *"… entities linked economically, personally or in another manner through a connection functionally equivalent to an economic or personal link"*.

44 This data is available in the obligatory records of tax subjects.

45 The reference price represents a simulation of the price that shall be set (calculated) on the basis of the consideration of what price such involved persons would agree upon in a situation identical to the situation of the related parties if they were nor related and if they had mutual standard business relations.

At the same time the case law[46] sets an obligation for the tax authorities to clearly and specifically notify the tax-payer of the amount of the actual common market price being extrapolated by the tax authority, and how the tax authority reached such a price (on the basis of what documents/criteria/tools). Following the conclusions stated, for example, in the Judgement of the Supreme Administrative Court of the Czech Republic of 31 October 2013 file No. 7 Afs 86/2013, the tax subject must be provided with time, not only to provide a statement in regard to the evidence shown or to the criteria, but also to propose other evidence or criteria which, according to tax-payer´s opinion, offer a different amount of the usual market price than that set by the tax authority. It is up to the tax-payer, as stated for example in the Judgement of the Supreme Administrative Court of the Czech Republic of 23 January 2013 file No. 1 Afs 101/2012 to, *"… prove unusual reasons, defying the standard conditions on the market, while being economically rational, for which the price between the tax-payer and the associated person was agreed upon differently from the reference price. Thus, it is then up to the tax subject to prove the occurring price difference ascertained and substantiated by the tax authority. If the tax-subject bears such burden successfully, the adjustment of the tax base by the tax authority is not allowed."*

The conclusions of the related case law bear witness of the need for a pro-active attitude on behalf of the tax-payer. If the tax-payer remains inactive for any reason, then the tax-payer faces the risk of additionally assessed tax or a reduction of the tax loss on the grounds of failing to bear the burden of proof successfully. However, it is possible to presume that the legal regulations and related case law have also placed significant procedural demands upon the tax authorities as well. (Brychta and Svirák, 2017) In the Judgment of the Supreme Administrative Court of the Czech Republic of 31 March 2009, file No. 8 Afs 80/2007, the Supreme Administrative Court of the Czech Republic gives a generally valid conclusion that, *"if a legal rule does not specify the mechanism for determining the common market price, and an administrative authority is called upon to determine it, the determination of the common market price must be approached with special attention and its amount must be determined on the basis of the objective criteria and in such a way that the conclusions of the administrative authority lead to a reliable opinion and, at the same time, it is possible to scrutinize the manner of its determination as well as the actual amount of the common market price ... Interfering in the selection of criteria, or determining which of the criteria the administrative authority shall take into consideration while determining the common market price, is not within the powers of the Supreme Administrative Court, and the choice of criteria is left upon the administrative authority; however, the Supreme Administrative Court reiterates that such criteria must lead to a reliable and objective conclusion."*

It is true (and the cases heard by the administrative Courts confirm) that the actual fulfilment of the generally and broadly defined criteria is a great challenge, due to the requirement of upholding due process while conducting a quantitative and qualitative analysis of suitable entities for the comparison.

5.4 LEGAL REGULATION AS INCLUDED IN DOUBLE TAX TREATIES

5.4.1 DEFINITION OF ASSOCIATED PERSONS IN DDTS CONCLUDED BY THE CZECH REPUBLIC

The Czech Republic can be described – in economic terms – as a small open economy (Žídek, 2006). Therefore, the existence of a relatively high number of concluded DTTs cannot be surprising. As of 20 August 2019 the Czech Republic has been a contracting party to 88 DDTs (Ministry of Finance of the Czech Republic, 2019a). Except for the MLI[47], the Czech Republic has not been a contracting party to a multilateral DTT[48].

The number of DTTs concluded has been continually growing. In this respect, it is interesting that the DTT concluded with Germany (an important business partner for the Czech Republic) is one of the oldest[49].

46 See, e.g., Judgement of the Supreme Administrative Court of the Czech Republic of 31 October 2013 file No. 7 Afs 86/2013.

47 The MLI has not come into effect in the Czech Republic yet (see OECD, 2020)

48 The legal predecessor of the Czech Republic (the Czechoslovak Socialistic Republic), however, was a party to multilateral DTTs; namely a DTT concluded for natural persons and a DTT concluded for legal entities with the countries of the RVHP (an abbreviation for the „Rada vzájemné hospodářské pomoci" – in English „Council for Mutual Economic Cooperation"). These two DTTs were published under Nos. 30/1979 Coll. and 49/1979 Coll.

49 Published in the Collection of Laws in 1984.

Not surprisingly, the DTTs concluded by the Czech Republic have been primarily based on the OECD Model Convention[50], and partly on the UN Model Convention.

The current definition of the associated persons as specified by the OECD (2017b) under Art. 9 (Associated Persons) para. 1 includes:

a) *An enterprise of a Contracting State that participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State and*
b) *The same persons that participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State.*

This definition is reflected in all the DDTs concluded by the Czech Republic and is entirely "coordinated" in this respect[51]. To understand the meaning of the general terms used, definitions regarding the procedure, as specified under Art. 3 para. 2 of the DTTs, can be found in Sec. 23 para. 7 (*Associated Persons*) of the Income Tax Act (Income Tax Act, 1992)[52].

5.4.2 EXISTING PLATFORMS OF THE WORDING OF ART. 9 IN DDTS

There are several scopes of the rules embodied under Art. 9 of DTTs. Within the classification of DTTs according to provisions embodied under their Art. 9 just three basic categories are used.[53] As can be seen in Table 19, the predominant platform (Category I) is the one according to which only the arm´s length principle and the definition of the associated persons are embodied under Art. 9 of the DTTs and every DTT includes these parameters. The second largest group of DDTs (Category II) (measured by the absolute number of DTTs coming under the category) is that in which an obligation to make a corresponding adjustment is set and, at the same time, this obligation is withdrawn for the situations going against *bona fide*. The lowest number (Category III) belongs to the group of DTTs in which there is set an obligation (or a possibility) to make a corresponding adjustment, having no explicit reference to the condition of *bona fide cases*[54]. After calculating the number of DTTs in categories II and III, one can conclude that the DTTs with corresponding adjustments are the prevailing ones.

Table 19: The scope of Art. 9 in DTTs in which the Czech Republic has been a contracting party – classification according to the criterion of the EU membership

Category	EU Member State	Non-EU Member State	Totally
I	14	27	41
II	7	6	13
III	6	28	34
Totally	27	61	88

Source: own elaboration based on Ministry of Finance of the Czech Republic (2019a).

The above conclusions are also valid for the criterion of OECD membership (for more details see the result of the comparison made in Table 20).

50 The Czech Republic has presented reservations in relation to some provisions of the OECD Model Convention (for more details see (OECD, 2017b), which has been reflected in particular DTTs).

51 A conclusion made on the basis of carried out comparison of all 88 DTTs.

52 The Art. 3 para. 2 of the OECD Model Convention (which is reflected, as a rule, also in the DTTs concluded by the Czech Republic) reads as follows, *"As regard the application of the Convention at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires or the competent authorities agree to a different meaning pursuant to the provision of Article 25, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State."* (OECD, 2017, Art. 3 para. 2)

53 A special category of DTTs which include a term for the corresponding adjustments was not considered. Stating a term under Art. 9 of DTT is very rare in DTTs concluded by the Czech Republic. However, the term is usually set under article covering mutual agreement procedure.

54 However, the absence of this explicit statement does not mean that this principle should not be applied: the spirit (principles) of DTTs should be observed, i. e. the advantage resulting from the DTT should be provided for justified cases. (Solilová, 2014)

Table 20: Extent of Art. 9 in DTTs in which the Czech Republic has been a contracting party – classification according to the criterion of the OECD membership

Category	OECD Member State	Non-OECD Member State	Totally
I	16	25	41
II	8	5	13
III	10	24	34
Totally	34	54	88

Source: own elaboration based on Ministry of Finance of the Czech Republic (2019a).

The complete list of DTTs containing the rules as embodied under Art. 9 of particular DTTs is presented in full in this chapter's Annex.

5.5 TRANSFER PRICING REGULATIONS – SELECTED ISSUES

5.5.1 TRANSFER PRICING METHODS

The Arm´s Length Principle is the key governing principle of transfer pricing generally accepted in the Czech Republic (for more details see chapter Definition of transfer pricing and basic principles in domestic law pgs. 11 et seq.). In respect of transfer pricing methods, the Czech Republic follows the recommendations as set by the OECD standards (OECD, 2017a). In the 'D-series' Guidelines (namely Guidance D-34) there is a separate chapter offering guidance on the methods used for setting the transfer price (Ministry of Finance of the Czech Republic, 2019b, Chapter 3). The classical classification into two basic groups of methods used for setting a transfer price is reflected in the categorisation:

a) traditional transaction methods (Comparable uncontrolled price method – CUP; Resale price method – RPM and Cost plus method – C+) and
b) profit transaction methods (Transactional net margin method – TNMM and Profit split method).

The General Financial Directorate (General Financial Directorate, 2019) recommends considering the following aspects when choosing a suitable method(s):

a) the weaknesses and strengths of the particular method;
b) the suitability of the method from the point of view of the transaction;
c) the availability of reliable data (above all the data on independent comparable transactions) that is necessary for the application of the selected method(s) and
d) the level of the comparability of controlled and uncontrolled transactions.

The General Financial Directorate stresses that sometimes the use of profit transaction methods can be more suitable (General Financial Directorate, 2019, Chapter 3). For example, when each of the party to the transaction brings or represents a valuable and unique contribution, or when there is no (or limited) information on the gross margin for independent subjects. A comparison of these methods using information published by the General Financial Directorate (2019) is presented in Table 21.

Table 21: Methods for setting the transfer price

Method	General attributes
Comparable uncontrolled price method – CUP	It is the price which is under examination. It is not necessary to examine the market price margin. Two types of CUP method (external CUP and internal CUP).
Resale price method – RPM	A distributor is usually the tested party; a distributor is buying the products from a supplier in the group (as a rule, the producer). An indicator of gross margin is used (gross profit/sales). Stress is put on the function analysis.

Method	General attributes
Cost plus Method – C+	A supplier/producer is usually the tested party of the transaction. Gross profit margin is the commonly used indicator (gross profit/production costs).
Transactional net margin method - TNMM	Both buyer and seller can be a tested party to the transaction (it is a party which performs less functions and bears less connected risks). Commercial databases are suitable source of information. In cases where there is aggregation of the transactions, i. e. when the transactions are interconnected and it is difficult to assess each of them separately.
Profit split method	This method can be used in cases when a unique and specific contribution of all parties to the transaction can be found (e. g. an ownership of a unique tangible or intangible asset and, at the same time, the parties involved in the transaction, are contributing with high added value and bearing relevant risk within the functions performed.

Source: own elaboration based on General Financial Directorate (2019, Chapter 3).

As shown, in this respect the Czech Republic more or less adheres to the OECD standards.

5.5.2 COMPARABILITY ANALYSIS/COMPLIANCE ANALYSIS OBLIGATION

In Czech domestic law – in respect of the legal regulations included in the acts – there are no set rules for comparability analysis. There are, however, again frequent references to the OECD standards in the 'D-series' Guidelines. The most extensive guidance on comparative analysis and its related issues can be currently found in Guidance D-34 published by the General Financial Directorate (General Financial Directorate, 2019)[55]. The key aspects are summarised in Table 22.

Table 22: Summary of the key aspects of the comparative analysis in Guidance D-34

Key factors	Assessed partial aspects
Factors determining the comparability	Contractual conditions of the transactions
	Functions, risks and assets (functional and risk analysis)
	Characteristics of the transferred property of provided services
	Economic circumstances related to the transaction and market
	Business strategy

Source: own elaboration based on General Financial Directorate (2019).

Guidance D-34 also outlines specific procedural steps[56] to be taken when undertaking the comparative analysis (General Financial Directorate, 2019, Art. 2.2). This procedure is summarized in Table 23.

Table 23: Summary of the comparative analysis procedure in Guidance D-34

Steps of the comparative analysis		Assessed aspects (covered features)	Commentary
1.	Analysis of the circumstances under which the business entity operates	Sector analysis	The aim of this part is to help to understand the conditions of the controlled transaction and conditions of uncontrolled transactions.
		Analysis of the competition	
		Analysis of the economic and regulatory factors	
		Analysis of other factors influencing the tax-subject	

55 Published in the Financial Bulletin by the Ministry of Finance of the Czech Republic (No. 5/2019) (Ministry of Finance of the Czech Republic, 2019b).

56 The procedure is not set as an obligatory one, any other procedure enabling identification of the reliable comparable data is also acceptable.

Steps of the comparative analysis		Assessed aspects (covered features)	Commentary
2.	Function and risk analysis*	Functions	The aim is to understand better the examined controlled transactions and to choose the tested party.
		Risks	
		Property (Assets)	
3.	Assessment of potential internal comparable data	Identification of internal uncontrolled transactions and evaluation of the possibilities of their use	Use of the existing internal comparable data is limited (if not impossible) in the event that the output within the uncontrolled transactions differs significantly from the one within the controlled transactions and/or the contractual conditions differ in a way that a factual and reliable adjustment cannot be made.
4.	Identification of the external data	Identification of the external comparable transactions	
		Identification of the external comparable subjects	
		Identification of the sources of information	
5.	Choosing the method for the setting of transfer price	Examination of the conditions of the transaction taking account of the testing party and setting relevant profitability indicator	Use of the methods as set by the OECD Transfer Pricing Guidelines (OECD, 2017a) is presumed. Using another method is not, however, excluded.
6.	Analysis of the situation in the "holding structure"	Finding and comparison of the profits and loss within the whole group of the associated entities (holding structure).	For instance, to compare whether remaining members (associated entities) declare a loss in the event a controlled entity in the group declares a loss.
7.	Identification of the set-offs	To identify where the set-offs are set in the contractual terms	A rule is set that in relation to the set-offs, not only the national accounting standards shall be applied - the results of the substance test and other circumstances of investigated controlled transaction should also be taken into consideration).

* For more details, see Chapter 2.1.2 of Guidance D-34 (General Financial Directorate, 2019).
Source: own elaboration based on General Financial Directorate (2019, Sec. 2.2).

As can be seen from the above stated steps, benchmark analysis is of key importance and Guidance D-34 also recommends a procedure for this (General Financial Directorate, 2019, Chapter 2.3). To ensure comparable independent entities are chosen, it is recommended that the rules as enshrined in the *Report on the use of comparables in the EU* by the EU Joint Transfer Pricing Forum (European Commission, 2016) and the *Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses* (published in a common output by the International Monetary Fund, OECD, United Nations and World Bank Group) (International Monetary Fund et al., 2017) are followed.

The benchmark analysis recommended in Guidance D-34 consists of two categories of benchmarking activities; firstly a quantitative benchmark analysis and secondly a qualitative one. The quantitative criteria presented in Guidance D-34 (General Financial Directorate, 2019) includes the following:

a) The status of the business entity (active, in insolvency, in liquidation, etc.).
b) The geographical area (the entities from the same or at least similar geographic area[57] (countries with the same or similar market) shall be chosen.
c) The branch (a selection of the branch according to the activities as set in the NACE codes (in relation to the activities of the tested party shall be made)).
d) Subject elimination:

57 In this respect, Guidance D-34 proposes a continual extension of the area covered (primarily, only the entities from the Czech Republic shall be taken into consideration; an extension of the area covered will take place in case of insufficient number comparable independent entities (for instance, V4 countries, EU countries, whole Europe).

- elimination of the subject to those that are independent in the meaning of the criteria as set by law;
- elimination of the subjects with start-up costs (i. e. entities started within 3 years before the examined year (period) – this criterion shall be applied depending on other conditions);
- elimination of the subjects according to set financial indicators (their boundaries);
- if the tested entity realizes only routine functions and bears limited risks, there is a recommendation to exclude entities with repeated loss and/or extreme profits (the loss-making ones should remain in the selection in justified cases)[58].

The guidelines published by the General Financial Directorate (General Financial Directorate, 2019) also contain recommendations relating to qualitative benchmark analysis. The qualitative benchmark analysis presents a deeper analysis, which includes rationales for the elimination of the subjects chosen by the quantitative analysis. For that reason facts[59] from publicly available information (published on the company's web pages, in annual reports, and in the Enclosure of the Financial Statements) are used. If there is an inconsistency between the selected independent subject and the tested one, or relevant data for qualitative analysis is missing, the first one shall be excluded from the sample (General Financial Directorate, 2019, Chapter 2.3.2).

In the Czech Republic, it is expert tax literature which provides detailed instructions[60] for comparative analysis. Further guidance on quantitative and qualitative analysis can be found, for example, in more detail and with some examples in the works of Solilová and Nerudová (2019) and Jelínek et al. (2018).

5.5.3 ADMINISTRATIVE APPROACHES TO AVOIDING AND RESOLVING TRANSFER PRICING DISPUTES

Following the publication of the manual for transfer pricing by the OECD, many administrative approaches can be identified[61] (OECD, 2017a), for more details see Table 24.

Table 24: Administrative Approaches to Avoiding and Resolving Transfer Pricing Disputes

<table>
<tr><th>Category</th><th>Partial category</th><th>Commentary</th></tr>
<tr><td rowspan="2">Transfer pricing compliance practices</td><td>Examination practices</td><td>In the Czech Republic, there are no specific procedural rules for examining practices for transfer pricing issues. However, the examination practices for transfer pricing, taking account of the specifics and existing legal regulation, have boundaries as established by the case-law of the administrative Courts (especially by the Supreme Administrative Court).</td></tr>
<tr><td>Burden of proof</td><td>The rules for bearing the burden of proof are stated in the Tax Procedural Code (Tax Procedural Code, 2011; Sec. 92) and in the Income Tax Act (Income Tax Act, 1993; Sec. 23 para. 7).

There is relevant case law which established (or more precisely defined) the rules for bearing the burden of proof in cases of transfer pricing.</td></tr>
<tr><td>Penalties</td><td colspan="2">Generally speaking, there are no specific provisions of penalties for breaching transfer pricing legal regulations. However, there is one exception from this general conclusion. In the event that the entrepreneur is granted tax credit for the investments and then breaches the rules for transfer pricing, then this entrepreneur, among others, looses this benefit – the tax credit.</td></tr>
</table>

58 Generally, as suggested by the EU material, an exclusion of the loss-making comparable independent entities is not, without an adequate justification, acceptable.

59 The facts, for example, the real type of economic activity, type of produced/sold products or provided services, property, and the ownership structure are under investigation.

60 Specification of the steps and criteria that should be followed.

61 For more details, recommendations and related risk see Chapter IV of the OECD Transfer Pricing Guidelines (OECD, 2017a).

<table>
<tr><th>Category</th><th>Partial category</th><th>Commentary</th></tr>
<tr><td rowspan="3">Corresponding adjustments and the mutual agreement procedure</td><td>Corresponding adjustments</td><td>Corresponding adjustments have been established in many DTTs concluded by the Czech Republic.</td></tr>
<tr><td>Mutual Agreement Procedure</td><td>A special clause on the Mutual Agreement Procedure has been established in some DTTs concluded by the Czech Republic.

Regarding this procedure, it is worth mentioning that the Czech Republic:
a) has been a contracting party to the Arbitration Convention 90/436/EEC on the Elimination of Double Taxation in Connection with the Adjustment of Profits of Associated Enterprises;
b) has an obligation to implement Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union* (Eur-lex, 2020c);
c) has been a contracting party to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI).</td></tr>
<tr><td>Publication of mutual agreement procedure programme guidance</td><td>Currently (as of 02 February 2020), there is no officially published guidance on the MAP and the Czech Republic has been criticized by the OECD (2018) for this.

However, an explanatory report on the Bill implementing the directive for tax disputes resolutions in which a tax-payer can find information related to MAP has recently been published (for more details see (Chamber of Deputies of the Parliament of the Czech Republic, 2019).</td></tr>
<tr><td>Simultaneous tax examinations</td><td colspan="2">There are general clauses enabling administrative cooperation at international level in DTTs concluded by the Czech Republic. Furthermore, the Czech Republic, as an EU Member State, has implemented the rules embodied in the Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC as amended (Eur-lex, 2020d).

The general provisions as established in international law have been specified (for direct taxation) in the Act on International Cooperation within Tax Administration and in amendments of other related acts as amended (Act on International Cooperation within Tax Administration, 2013).

For more information on administrative cooperation, see for example materials available at the official web pages of the Department 2502 of the Czech Ministry of Finance which deals with the issues of international cooperation in tax and duty issues (Ministry of Finance of the Czech Republic, 2019c).</td></tr>
<tr><td>Safe harbours</td><td colspan="2">In the Czech Republic, simplified rules for setting transfer prices can be applied in relation to Low Value Adding Intra-Group Services (established in Guidance D-10 (General Financial Directorate, 2012)).

The guidance covers only the intragroup services which:
a) have low added value and
b) do not represent the main activity of the subject,
c) represent routine functions and, at the same time,
d) do not create substantial cost or revenue for the enterprises involved.

A service not representing a substantial revenue for the provider of the service is one in which the total value for all the transactions does not exceed 10 % of the total turnover and, at the same time this value does not exceed the amount of 50 million CZK. As for the receiver of the service, the total value for all the transactions (payment costs) does not exceed 20 % of the operating costs and shall not be higher than 50 million CZK.</td></tr>
</table>

Category	Partial category	Commentary
Advance Pricing Arrangements (APA)	Unilateral	In the Czech Republic, there is not a concept of unilateral APA. The Binding Ruling as established by the Czech law does not meet all the criteria as set by the OECD (2017a) for the APA (for the comparison see e. g. Brychta and Sulik-Gorecka, 2019).
	Bilateral	According to the rules as embodied in DTTs.
	Multilateral	

* A Bill was submitted to the Parliament of the Czech Republic which has the nature of a special legal act (it represents a lex specialis). However, as of 02 February 2020, there has been a delay to its adoption.

Source: own elaboration based on OECD (2017a, chapter IV: Administrative Approaches) and sources as listed in the table.

5.5.4 PROVISIONS GOVERNING SPECIFIC AREAS

There are no special legal regulations (in the form of the norms included in the Acts) relating to **the intangibles** in the Czech Republic. This specific and currently very important area is "regulated" by Guideline D-34 (General Financial Directorate, 2019). However, this document does not provide specific, concrete guidance for the intangibles. There are many references to intangibles within the descriptions of potential profiles and a general clause on the DEMPE analysis is included in the chapter dealing with function analysis (General Financial Directorate, 2019, Chapter 2.1.2).

No specific legal regulations are explicitly embodied in Czech domestic acts regarding issues of **intra-group services and cost contribution arrangements**. The arm´s length principle and other rules resulting from the OECD and EU standards are naturally "quasi" bound for them. The absence of specific provisions in acts is partly compensated by case law which interprets some general clauses as embodied in the acts, while respecting the arm´s length principle. Furthermore, the Czech legal framework has got a regulation for low-value-adding services as included in Guidance D-10 (General Financial Directorate, 2012).

A slightly different situation is in relation to the transfer pricing aspects of business restructuring. In this respect, the OECD and EU standards, that comply with Czech law, are also "binding" and in the Czech Income Tax Act, a so called Anti-Tax Avoidance Directive (Eur-lex, 2020a) is included. In the Income Tax Act there are rules for the taxation of property relocated without a change in the ownership. For these types of transactions the arm´s length principle is of key importance for the assessment of the value of the property (see Income Tax Act, 1992, Sec. 23g).

5.6 TRANSFER PRICING DOCUMENTATION

Transfer pricing documentation is not obligatory in the Czech Republic; however some transfer pricing experts deduce a "quasi" obligation (not directly set in the act) by the wording of Sec. 92 para. 3 of the Procedural Tax Code which reads as follows, *"The tax subject shall have to prove all the circumstances that it is obliged to state in a due tax return, additional tax return and other submissions."* (Tax Procedural Code, 2009, Sec. 92(3)) The need to complete transfer pricing documentation has not been set in Czech domestic law[62], however to fulfil the obligation of setting the transfer price in harmony with the arm´s length principle, a tax-subject can utilize other means.

In the Czech Republic, in regards to the scope of transfer pricing documentation, there is specific guidance in the 'D-series' Guidelines (which contain information provided by the Ministry of Finance) (Ministry of Finance of the Czech Republic, 2010a)[63]. However as this has not been updated since 2010 it does not fully comply with the current OECD and EU standards. In Guidance D-334 the Ministry of Finance of the Czech Republic refers to the applicability of the OECD and EU standards both in relation to purely domestic business relations between associated persons within the territory of the Czech Republic and to cross-border business relations (i.e. to the entities being parts of a multinational groups having their seat in the Czech Republic) (Ministry of Finance of the Czech Republic, 2010a).

62 This issue has quite broadly been discussed in the Czech Republic.

63 The Ministry of Finance of the Czech Republic has published an English translation of this Guideline.

The Ministry of Finance (Ministry of Finance of the Czech Republic, 2010a, Chapter 5) provides a list of situations in which the tax-payer should present their transfer pricing documentation to the tax administrator, namely in cases:

a) when proving the correctness of setting the transfer price;
b) when applying for the Binding Ruling in respect of the correctness of setting the transfer price[64];
c) when initiating procedures with the aim to avoid double taxation within the process, according to a bilateral DTT or according to the Arbitration Convention.

In 2010 the Czech Republic decided to apply the European Code of EU Transfer Pricing Documentation[65], even in respect of the scope (scheme) of transfer pricing documentation, between domestic associated entities[66] (Ministry of Finance of the Czech Republic, 2010, Chapter 5). Guideline D-334 distinguish between two types of documents: basic documentation (or Master-file) and country specific documentation. The Master-file should contain information on the whole multinational enterprise group that is applicable for all the EU Member States. The guidelines state that this documentation should reflect all the economic circumstances of the business and should provide a general overview of the multinational group, including documentation of the group´s transfer pricing policy and all internal business relations (Ministry of Finance of the Czech Republic, 2010a, Chapter 4). The information that should be included in the Master-file is outlined in Table 25.

Table 25: Summary of a Master-file and its content

<table>
<tr><th>Area covered by master-file</th><th colspan="2">Description</th></tr>
<tr><td>Business activity and business strategy of the group of enterprises (holding)</td><td colspan="2">General description of these categories including changes in the business strategy as compared to the previous tax year.</td></tr>
<tr><td>Group´s organizational, legal and operational structure</td><td colspan="2">General description of stated aspects including an organization chart, a list of group members and a description of the participation/share of the parent company in the subsidiaries.</td></tr>
<tr><td>Identification of associated enterprises</td><td colspan="2">General identification of associated enterprises engaged in business relations involving related enterprises within the EU.</td></tr>
<tr><td rowspan="3">Description of the business relations</td><td rowspan="3">General description of the business relations involving associated enterprises in the EU.</td><td>Flows of transactions (tangible and intangible assets, services, finances, etc)</td></tr>
<tr><td>Flows of invoices</td></tr>
<tr><td>Scope of the transactions</td></tr>
<tr><td>Functions and risks and their changes</td><td>General description of function performed, risks assumed and description of changes in functions and risks compared to the previous tax year.</td><td>E. g. a change from a pure distributor to a commission entity</td></tr>
<tr><td>Intangible assets and their ownership</td><td>The ownership of intangible assets and royalties paid and received.</td><td>Patents, trademarks, brand names, know-how</td></tr>
<tr><td>Inter-company transfer policy</td><td colspan="2">Description of the inter-company transfer policy or a description of the group´s transfer pricing system that explains the arm´s length nature of the company´s transfer pricing.</td></tr>
<tr><td rowspan="3">Relevant documents related to transfer pricing</td><td colspan="2">A list of cost sharing agreements.</td></tr>
<tr><td colspan="2">A list of Advance Pricing Agreements (Binding Rulings).</td></tr>
<tr><td colspan="2">Rules covering transfer pricing aspects, if they apply to the associated entities within the EU.</td></tr>
<tr><td>A commitment of particular domestic tax-payers</td><td colspan="2">A commitment of each domestic tax-payer to provide supplementary information upon request and within a reasonable time limit in accordance with the national rules.</td></tr>
</table>

Source: own elaboration based on Ministry of Finance of the Czech Republic (2010a, Chapter 4).

64 Specified under Sec. 38nc of the Income Tax Act.
65 On the basis of which the Code of Conduct in Transfer Pricing Documentation for Associated Enterprise in the EU was adopted (see Council of the European Union, 2006).
66 In the end of the document there is pointed out that the rules given therein reflect all national specific circumstances (Ministry of Finance of the Czech Republic, 2010a, Chapter 5).

The recommended content of the country specific documentation is summarized in Table 26.

Table 26: Summary of country specific documentation and its content

Area covered by country specific documentation	Description
Business activity and business strategy	Detailed description of the business activity and business strategy, including changes in the business strategy compared to the previous tax year.
Description of the business relations, in which the entity is involved	Flows of transactions (tangible and intangible assets, services, finances, etc.)
	Invoice flows
	Scope of transaction
Comparability analysis	Characteristics of property or services
	Functional analysis (functions performed, assets used, risks borne)
	Contractual terms
	Economic circumstances
	Specific business strategies
Transfer pricing method(s)	Explanation of the selection and application of the transfer pricing method(s) (i. e. why a particular transfer pricing method was selected and how it was applied).
Information used	Information on internal and/or external comparables (if available).
Involvement of the company	Description of the way the company is involved in the group´s transfer pricing policy.

Source: Own elaboration based on Ministry of Finance of the Czech Republic (2010, Chapter 4).

The Ministry of Finance of the Czech Republic (Ministry of Finance of the Czech Republic, 2010a, p. 4) states that, *"Generally, it should be left at the discretion of the taxpayers what documentation will be processed for the group as a whole and what will be complemented by each company separately. The company should have the possibility of including some items of the country-specific documentation in the Master-file, keeping, however, the same quality and level of detail as in the country-specific documentation. The fact that the company should always have all the documentation required by the particular state available, would be maintained as the main principle."* The application of the Master-file is therefore voluntary for associated entities. It means, as stated by the Ministry of Finance of the Czech Republic (Ministry of Finance of the Czech Republic, 2010a, p. 5) that, *"the companies may decide themselves, whether to process basic documentation for the whole group together. If the group of associated entities selects this option, the Czech tax administration shall apply the provisions of the Code of Conduct on Transfer Pricing Documentation for Multinational Enterprise in the EU in accordance with respective Czech law."*

Irrespective of whether the entity applies the concept of the EU Transfer Pricing Documentation and decides to process the basic documentation for the whole group in a unified way or whether the company decides to document its transfer pricing independently, the documentation should contain information as specified in Table 27.

Table 27: Prescribed content of the transfer pricing documentation

General category	Details
Information concerning the group (the *Master-file*)	Description of business activities, complete ownership and organisational structure of the whole group, legal forms of the associated entities, information on related parties engaged in the business relations including an overview of financial results of particular related parties, allocation of functions within the group, allocation of risks, overview of intangible property ownership (licences, patent, know-how, etc.) and royalties flow, overview of the transfer pricing implemented, list of agreements regulating sharing of costs and expenditures, overview of Advance Pricing Agreements entered into by the associated entities (eventually Binding Rulings issued), commitment of the company to submit other evidence in a reasonable time if the presented information about the group is insufficient.
	NOTE: If there is an expectation that some of the above mentioned facts could be changed or will be changed in the near future, the changes (or potential changes) should also be stated, together with their reasoning.
Information concerning the company	A precise description of the business activities, complete ownership and organisational structure, financial results for the previous year and corresponding financial indicators, strategies adopted, etc.
Information concerning the business relation (transaction)	A precise description of the business relation (i.e. precise description of goods and services traded), financial and trading terms, all relevant agreements and contracts entered into by the entities concerned, volume of the transaction, functions and risk associated to the business relation concerned etc.
	When providing the intangibles (management and marketing services, consultancy, etc.), it is necessary to sufficiently describe the characteristics of the services rendered and to identify the purpose of the services and expected benefit arising thereof in detail.
Information on other circumstances effecting the business relation	The company´s marketing strategy, specific economic conditions of the market, legislation specific, etc.
Information concerning transfer pricing	The way of transfer pricing that has been used.
	An explanation as to why the particular way of pricing has been selected.
	Information concerning comparable business relations (internal comparables within the group and/or external comparable between two comparable independent companies).
	Comparable analysis (reference to the guidelines as provided by the OECD).

Source: own elaboration based on Ministry of Finance of the Czech Republic (2010a).

As the current content of Guidance D-334 is somewhat out of date, it does not fully reflect the developments in the standards for transfer pricing documentation. Information regarding the preparation of updated Guidance D-35, that would replace Guidance D-334, was stated in the Guidance D-34 (General Financial Directorate, 2019, p. 28).

However, in the case of the Czech Republic, it is not only the Czech Financial Administration that provides guidance for the documentation. Many useful proposals can also be found in expert literature. Jelínek et al. (2018) suggest that the basic structure for the documentation should contain[67]:

a) an introduction,
b) a description of the company,
c) a description of the market,
d) function analysis,
e) the selection of the method,
f) the selection strategy,
g) setting the market margin, and
h) conclusions.

67 Further guidance on individual categories can be found in Jelínek et al. (2018)

When one consider together the updated OECD Transfer Pricing Guidelines (OECD, 2017a) and the rules as established by EU law, there can be distinguished three documentation types in the Czech Republic. These include:

a) a **Local File** (local documentation containing information on each entity, that represents a part of the group and is, at the same time, a tax-resident in a particular jurisdiction);
b) a **Master File** (fundamental document containing data on the group as a whole);
c) and **Country by Country reporting** (reporting and passing information on the transactions between the associated entities in specified cases).

In relation to Country by Country reporting, there was an amendment to Act No. 164/2013 Coll., on International Cooperation within Tax Administration and on the amendments of other related Acts, as amended (Act on International Cooperation within Tax Administration, 2013)[68]. The Czech Financial Administration published a series of notifications and Q&A's relating to Country by Country reporting on its web-pages (Financial Administration, 2018). It is worth noting that the Czech Financial Administration again refers to the OECD standards. The Czech Financial Administration also referred to the Country-by-Country Reporting XML Schema: User Guide for Tax Administrations on its web-pages (Financial Administration, 2018). In the Czech Republic, there are two types of information obligations on the parts of the associated entities; notifications for Country-by-Country Report and Country-by-Country Report itself. The latter duty, i.e. to complete a Country-by-Country Report, relates only to the multinational enterprises that have a total consolidated group revenue of at least EUR 750,000,000.

In summary, the Czech legal regulations regarding transfer pricing documentation follow the rules, standards and recommendations as included in the OECD and EU standards.

5.7 ADVANCE PRICING AGREEMENTS IN THE CZECH REPUBLIC

In Czech domestic law, one can find only a legal regulation for **a Binding (Advance) Ruling**. The unilateral APAs, as understood by the OECD (2017a), have not been explicitly regulated in Czech domestic law.

Bilateral and multilateral APAs follow the rules as embodied in the DTTs, MLI (after it becomes effective) and the OECD standards and provide the specification of the rules for the DTTs application. To solve the problems within the application of a DTT; bilateral and/or multilateral APAs are possible under a mutual agreement procedure[69] (MAP). In this respect, one can speak of bilateral and multilateral advance pricing agreements existing, without there being explicit legal regulations in Czech domestic law. Currently, there is a bill implementing the rules as stated in the Council Directive (EU) 2017/1852 of 10 October 2017, on tax dispute resolution mechanisms in the European Union (Eur-lex, 2020c). This act should embody visible and clear rules for tax-payers. However, the rules will be, unlike in the originally presented version of the Bill, valid only for residents of other EU States.

In the Czech Republic, the current procedure for resolving disputes directly follows the wording of a particular DTT. There are no official guidelines or specific legal regulations specifying the steps that should be taken by a tax-payer. A summary of the procedure (steps and actions connected with resolving a dispute) can be found in the explanatory report which accompanied the Bill on Tax Dispute Resolutions (for more details, see Office of the Government of the Czech Republic, 2018).

The General Tax Directorate is typically the authority involved in cases concerning transfer pricing. The starting point for the initiation of the procedure includes:

a) a submission by a tax-payer who is a Czech tax resident or a national; or
b) the receiving of information from the competent authority of the contracting state that a submission has been made in the state where the taxpayer is a tax resident or a national (Office of the Government of the Czech Republic, 2018).

In the case of the submission of a Czech entity, the competent authority first analyses the documents submitted - in relation to the settling of a dispute - or will request completion of the documents by the taxpayer concerned or their local tax authority. If the competent authority finds the submission well-

68 The amendment represents a transposition of the 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 (Eur-Lex, 2020e). The amendment was realized by the Act No. 305/2017 Coll.

69 The rules are stated, as a rule, in a special article in DTTs.

founded, it will first attempt to resolve it unilaterally from its position. If it reaches a resolution, it will immediately notify the taxpayer concerned and their local tax authority in order to continue the procedure. In the event that the unilateral resolution is not possible, the competent authority of the other contracting state will be contacted with a request to submit an opinion on the matter, while all the relevant information available at the specific moment (including the opinion and draft resolution if any possible) is at the same time provided by the Czech authority. The next stage includes the exchange of opinions and views of the authorities of both state parties. Negotiations take place until an agreement is reached on resolving the case or a consensus that the agreement in the particular case is not possible. In both situations, the result is communicated to the taxpayer and their local tax authority. (Office of the Government of the Czech Republic, 2018)

The procedure for the settlement of a dispute is initiated exclusively on the basis of an application by the tax-payer concerned (it is implied in the DTT and the Arbitration Convention). This application follows the general provisions concerning submissions (Tax Procedural Code, 2009, Sec. 70 et seq.), including that the Czech language serves exclusively as the official language (Tax Procedural Code, 2009, Sec. 76). The procedure does not have the nature of an ordinary means of remedy: consequently, it means that a failure to use this procedure for settlement of the dispute, does not affect access to hearing the case before an administrative Court.

Table 28 below summarizes the available statistics on the APAs created between 2016 and 2018. When compared with other EU Member States one can conclude that bilateral and multilateral APAs are not frequently used by taxpayers in the Czech Republic. On the other hand, binding ruling (which is specified by the JTPF as a unilateral APA) is quite extensively used: one of the reasons could be its relatively low fee.

Table 28: Number of APAs in the Czech Republic

	2016 EU/non-EU	**2017 EU/non-EU**	**2018 EU/non-EU**
Total number of APAs in force each year	45/10	77/14	51/17
Total number of unilateral APAs (Binding Ruling) in force at the end of the year	44/10	77/14	48/15
Total number of bilateral and multilateral APAs in force at the end of the year	1/-	0/0	3/2
Number of APA requests received in the year	20/2	23/1	22/9
Number of APAs granted in the year	18/-	24/1	11/3
Number of applications rejected	1/4	2/-	3/-

Source: own elaboration based on European Commission (2018a, 2018b, 2019).

5.7.1 BINDING (ADVANCE) RULING

The OECD (2017a, item 4.143) states that, *"APAs, including unilateral ones, differ in some ways from more traditional private rulings that some tax administration issue to taxpayers."* The differences are outlined in Table 29 below.

Table 29: Summary of the differences between APAs and traditional private rulings

APA	**More traditional private rulings**
Generally deals with factual issues.	Tend to be limited to addressing questions of a legal nature based on facts presented by a taxpayer.
Facts are likely to be thoroughly analysed and investigated.	The facts underlying a private ruling request may not be questioned by the tax administration.
Usually covers several transactions, several types of transactions on a continuing basis, or all of a taxpayer´s international transactions for a given period of time.	Usually binding only for a particular transaction.

Source: own elaboration based on OECD (2017a), Brychta and Sulik-Gorecka (2019).

Observing the above classification, one can conclude that in Czech domestic law a Binding (Advance) Ruling is set – i.e. a type of more traditional private ruling. Rules governing the Binding Ruling in Czech domestic law are established in the Income Tax Act (Income Tax Act, 1992) and in the Tax Procedural Code (Tax Procedural Code, 2009). The legal regulation, contained in the latter, represents *lex generalis* (Tax Procedural Code, 2009, Sec. 4). In the event of a collision, the legal regulation contained in the Income Tax Act prevails over that contained in the Tax Procedural Code.

The Tax Procedural Code contains general provisions for the procedure of the Binding Ruling under Sec. 132 and 133 – the rules as stated are presented in Table 30.

Table 30: Summary of general rules for Binding Ruling included in the Tax Procedural Code

	General principles as stated by the Tax Procedural Code
Sec. 132	• initiation by a taxpayer • assessment of tax consequences resulting from already occurred or future tax relevant facts • procedure applicable for the cases where a particular act admits so
Sec. 133	• specification of the conditions on which the decision on binding assessment is/is not effective: • decision effective towards a tax administration authority which decides on the tax duty of the taxpayer • effective in cases when the factual state is in harmony with the data on the basis of which the decision was delivered • decision becomes ineffective in the event of a change in relevant legal regulation on the basis of which the decision was delivered • time limitation for the decision • decision cannot be used in case conditions under which the decision was delivered are not met (i.e. the facts insisted by the tax-payer will be revealed as not being true)

Source: own elaboration based on Tax Procedural Code (2009, Sec. 132 and 133), Brychta and Sulik-Gorecka (2019).

The 1992 Czech Income Tax Act sets the rules for several types of Binding Ruling. One of which - Binding Ruling on the Way in which the Price Negotiated Between Associated Entities Was Created (Income Tax Act, 1992, Sec. 38nc) - has been has effective since 01 January 2006. The rules for it are outlined in Table 31.

Table 31: Summary of the rules found in *Binding Ruling on the Way in which the Price Negotiated between Associated Entities Was Created*

	Description
Situation covered	• assessment whether the price negotiated between associated subject corresponds to the price that would be negotiated between non-associated subjects in common business relationships on the same or similar conditions
Content of the application	• specification of all parties in the business relation for which the application for a decision on Binding Ruling on the price is asked • description of the organizational structure in which participating entities are included (even those from abroad) • description of business activities of participating entities • description of business relation for which the application is submitted • specification of taxable period to which the decision shall be related • description and documentation of the way in which the price was created including all relevant facts • proposal of the statement for the decision on Binding Ruling

Source: own elaboration using Income Tax Act (1992, Sec. 38nc), Brychta and Sulik-Gorecka (2019).

The administrative charge for the binding ruling (regardless of the matter involved) amounts to CZK 10,000.00 (Act on Administrative Charges, 2004, Table of Charges, part I, item 1, letter n). Neither Income Tax Act (1992), nor Tax Procedural Code (2009) specify whether the charge relates to one transaction or one submission. Detailed information is provided in Guidance D-32 (General Financial Directorate, 2018) which specifies that:

a) the application for a binding ruling can be submitted for the tax period in which the application is submitted or for the following tax periods (i.e. for already passed tax periods this application is not acceptable);
b) the application is usually submitted in respect of one transaction;
c) if there are several transactions closely related (several transactions between the same entities concerning the same business: combined transactions), it is more appropriate to aggregate these transactions and consider the business as a whole; they are then evaluated as a group of associated transactions altogether by one method;
d) a tax-payer can submit also an application relating to assessment of a set of transactions which do not closely relate to each other; for such a case every transaction will be considered independently from the others and separate decisions (which can be positive or negative) are issued; the total fee required is derived from the number of transactions or number of the sets of the closely related transactions;
e) there is only one decision presented in the final statement: either the price is accepted or not.

The term for issuing the decision following the submission of an application for binding ruling has been set at three months, if not set otherwise according to the rules in the act (Ministry of Finance of the Czech Republic, 2015).

5.8 PENALTIES FOR BREAKING THE RULES RELATED TO TRANSFER PRICING

In general there are no specific penalties, with an exemption (see below), relating to a violation of the standards valid for the arm´s length principle. In the event of failing to meet the obligation to set the prices in harmony with the arm´s length principle, two general types of penalties can arise (see Table 32).

Table 32: Selected penalties as set in the Tax Procedural Code

Type of the sanction	When the sanction arises	Amount of the sanction	Possibility of the moderation
Penalty (Sec. 251 of Tax Procedural Code)	The tax-payer is obliged to pay the penalties for the amount of additionally assessed tax that was determined in contradiction with the last known tax, with the exception of a tax base and taxes or tax losses additionally assessed pursuant to a supplementary tax return.	20 % of the amount of additionally assessed tax, if the tax is increased, or 1 %, if the tax loss is reduced	Yes
Default interest (Sec. 252 et seq. of Tax Procedural Code)	The tax debtor is obliged to pay late charges for every day of default, beginning with the day following the maturity day, up to the date of payment, including the period from the original maturity day.	The default interest amount is comparable to the annual amount of repo rate determined by the Czech National Bank, increased by 14 %, payable of the first day of the relevant calendar half-year.	Yes

Source: own elaboration based on Tax Procedural Code (2009, Sec. 251 and Sec. 252 et seq.).

The above stated sanctions can be waived on conditions set by law (Tax Procedural Code, 2009, Sec. 259 et seq.). Up to 75 % of the amount of the penalty set can be waived on the basis of a submission by the tax-payer and after consideration of the extent of the tax-payer´s cooperation with the procedure connected with the additional tax assessment (Tax Procedural Code, 2009, Sec. 259a). The default interest can be waived (again the basis of a tax-payer´s submission) fully or partly if the delay in tax payment was caused by justifiable reasons (namely by relevant economic and social aspects). (Tax Procedural Code, 2009, Sec. 259b)

There is, as pointed in the text above, one specific and strict type of a penalty (sanction) related to a violation of arm´s length principle when setting the tax base. It relates to tax-payers which are provided a tax credit for investments. If the tax-payer violates the arm´s length principle when setting the transfer price between him and the associated person, then he loses the tax credit (Income Tax Act, 1992, Sec. 35a and Sec. 35b).

Considering the situation in the Czech Republic there is logically no penalty if a transfer pricing documentation is missing – there is no duty to make out a transfer pricing documentation in this country.

5.9 OTHER OBLIGATIONS RELATED TO TRANSFER PRICING

In the event that the contractual price between associated persons does not correspond to the price as it would have been set according to the arm´s length principle, then a tax-payer is obliged to make an adjustment in their tax return. However, when setting the tax base, the price shall be set according to the arm's length principles. This change is not made in the accounting, but in a form of an adjustment of the tax base as calculated in the tax return (Income Tax Act, 1992, Sec. 23 para. 3 point 17). Regarding the corporate income tax return it is worth mentioning to refer to a special annex. During the last several years, one can observe both growing competence and experience on the part of employees' of Czech tax administration and more precise and focused tax audits. The latter fact can be accredited, at least partly, to the "new" annex in the corporate income tax return – *Summary of transactions with the associated persons*. Its effectiveness could be said to be due to the clear criteria set (see Table 33).

Table 33: Summary of the criteria under which the summary of transactions with associated persons shall be completed in corporate income tax return

Observed criteria (at least one of them shall be met)	Type of the transaction	Extend of declared transactions
total assets of more than 40 mil. CZK. By assets it is meant the total assets determined from the balance sheet pursuant to section 1d subsection 1 of the Accounting Act OR annual net turnover of more than 80 mil. CZK calculated according to section 1d subsection 2 of the Accounting Act OR average number of employees over 50, by which it is meant the figure specified according to partial instructions at row 2 of the Table K of Tax Return	the taxpayer realized transactions with a related person located abroad.	the taxpayer fills this annex only with respect to these foreign related person
	the taxpayer reported a tax loss stated on row 200 of the Tax Return, and at the same time the taxpayer realized transactions with a related person, either foreign and/or domestic one	the annex is filled in relation to all related persons
	the taxpayer is a recipient of an investment incentive in the form of tax relief in accordance with the Act no. 72/2000 Coll., on investment incentives, as amended, and simultaneously realized a transaction with a related person, either foreign and/or domestic one	the annex is filled in relation to all related person

Source: own elaboration based on Financial Administration (2020).

Considering the situation in the Czech Republic there are, however, some additional statement obligations closely connected with transfer pricing. According to Czech accounting regulations, some information relating to transfer pricing is published in the Financial Statements of the accounting entity. The extent of the information provided depends on the category of the accounting entity (Act on Accounting, 1991, Sec. 18 et seq.), (Decree No. 500/2002 Coll. implementing some provisions of the Act on Accounting, 2002, Sec. 3 et seq.). The Decree accompanying the 2002 Act on Accounting sets an obligation to provide – in the Financial Statements – the amount of advance payments, earnest money, loans provided to the members of management, control or executive boards showing, at the same time, the interest rate, fundamentals conditions and all currently paid, written down or remitted payments and all other fulfilments provided to these persons (the total amount should be stated for each category of persons) (Decree No. 500/2002 Coll.

implementing some provisions of the Act on Accounting, 2002, Sec. 39 para. 1 letter f). In practice, these statements are accompanied by a declaration that these persons were provided with goods, services, etc. under conditions which correspond to common market price (arm´s length principle).

5.10 INFLUENCE OF THE OECD AND EU STANDARDS

5.10.1 OECD (AND EU) STANDARDS AND THEIR REFLECTION IN CZECH DOMESTIC LAW – A SUMMARY[70]

The Czech Republic is included in the list of countries in which transfer pricing legal regulations, as embodied in its law, is not very extensive but, at the same time, promotes and recommends applying the OECD and EU transfer pricing standards.

In the Czech Republic, as well as in other countries, controlled transactions can be classified on the basis of the existence of an international element in the relationship as follows:

a) domestic controlled transactions (i. e. controlled transactions without the existence of an international element);
b) controlled transactions with an international element when the controlled transaction is related to a non-contracting State[71] and
c) controlled transactions with an international element when the controlled transaction is related to a contracting State[72]. (Brychta and Svirák, 2020)

Position of the OECD (and EU) standards transactions with an international element (contracting States)

In the case of the Czech Republic, the number of concluded and, at the same time, valid DTTs is quite high[73]. If a tax resident of another contracting country is involved in the controlled transaction, then such a relationship is governed by the rules as embodied under Art. 9 and the related provisions of the DTT. Despite the different scope of the rules in the DTTs concluded by the Czech Republic or by her legal predecessor, all these DTTs have included at least the definition of the associated persons and the arm´s length principle. The position of the OECD standards seems to be quite clear in respect of such a type of controlled transaction. As the Czech Republic has been a contracting party to the Vienna Convention on the Law of Treaties, the OECD transfer pricing guidelines represent a binding interpretation tool for the application of Art. 9 of a particular DTT. This position has not been disputed and has been confirmed in many sources including, among others, in the new updated Guideline D-34 (General Financial Directorate, 2019). From the legal point of view, the use of the OECD transfer pricing guidelines for controlled transactions in cases when a tax resident comes from a contracting state appears to be without problems.

Position of the OECD (and EU) standards in domestic transactions and transactions relating to non-contracting States

As confirmed by the statement of the General Financial Directorate (General Financial Directorate, 2019), the procedures and methods specified in the OECD transfer pricing guidelines have not been explicitly embodied in any Czech tax act nor has there been included a direct reference to the OECD transfer pricing guidelines. In Guidance D-332 (Ministry of Finance of the Czech Republic, 2010b) - the predecessor to the current Guidance D-34 (General Financial Directorate, 2019) - the possibility of using the OECD transfer pricing guidelines for purely domestic (intrastate) controlled transactions was deduced, contrary to established legal principles – with reference to the Vienna Convention on the Law of Treaties and to the obligation to observe this Convention within the application of Art. 9 of DTTs (Ministry of Finance of the Czech Republic, 2010b). However, a new and properly justified basis for the application of the OECD standards in domestic controlled transactions was subsequently published in the current Guidance D-34.

70 Based on (Brychta and Svirák, 2020).
71 It means that this State has no DTT or any contract of this nature concluded with the Czech Republic.
72 I.e. a State which has concluded a DTT or any contract of similar nature with the Czech Republic.
73 Almost 90 DTTs.

The General Financial Directorate (General Financial Directorate, 2019, pp. 8 – 9) presents their rationale as follows:

a) Over the course of time use of the OECD transfer pricing guidelines, or rather use of the rules stated therein, has established a standard which is acknowledged and applied both by the tax subject and tax authorities.
b) Using the OECD transfer pricing guidelines contributes to the legal certainty on the part of tax subjects and, at the same time, sets predictable rules for the action of tax authorities.

Taking account of the fact that even the predecessors of the current 'D-series' Guidelines included references to the OECD, and subsequently to the OECD and EU standards, the position and opinion of the Financial Administration of the Czech Republic is quite clear and unambiguous. The binding nature of the 'D-series' Guidelines for tax authorities has been confirmed by the case law of the supreme Courts of the Czech Republic (for more details see the summary as provided under issues [23] and [24] of the Judgement of the Supreme Administrative Court of 04 October 2018 File No. 2 As 94/2018). Despite the fact that the 'D-series' Guidelines have not been strictly legally binding, one cannot conclude that they have no relevance for tax subjects.

5.11 EU STANDARDS AND THEIR REFLEXION IN THE CZECH DOMESTIC LAW – A SUMMARY

The above stated conclusions are valid for EU transfer pricing soft-law as well. With some exceptions, the Czech Republic seems to observe (or at least promote) EU soft-law governing transfer pricing and related issues. There are, however, even some hard-law legal acts, with relevance to transfer pricing, reflected in Czech domestic law. For a basic summary, see Table 34.

Table 34: Reflection of selected transfer pricing EU law (hard-law and soft-law) in Czech domestic law

EU law (or law having its origin with the EU)	Implemented by/ published in	Commentary
Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (90/463/EEC)	Published in the Notification of the Ministry of Foreign Affairs under 93/2006 Coll. of International Treaties	The Czech Republic became a party to this Convention in 2004, the Convention became effective for the Czech Republic in 2006. (Eur-lex, 2020b) The Czech Republic has not adopted any specific domestic legal regulation for the implementation of the general rules as stated in the Convention. For the Czech Republic, this Convention relates to Personal Income Tax and Corporate Income tax.
Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union	Not implemented yet (currently there is only a Bill).	This Directive is intended to be implemented in a separate procedural act which will take the position of a special legal regulation (lex specialis) to (Tax Procedural Code, 2009).
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	Implemented in the Income Tax Act (Income Tax Act, 1992, Sec. 23g)	The implementation has been carried out in harmony with the Directive (within the discretion as provided for the Member States). There is reference to a common market price for the assessment of transferred property.

EU law (or law having its origin with the EU)	Implemented by/ published in	Commentary
Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC as amended	Act on International Cooperation within Tax Administration and on amendments of other related acts as amended (Act on International Cooperation within Tax Administration, 2013)	This Directive has been amended several times. These amendments have, or could have, a relation to transfer pricing. In this respect, an amendment as provided by DAC IV (Council Directive (EU) 2016/881 of 25 May 2016) is noteworthy.
EU Codes of Conduct related to transfer pricing	Reference made to it in the D Series Guidelines	The EU Codes of Conduct are is considered to be a soft-law. However, there are many references to the Code in the D Series Guidelines –therefore it helped to establish administrative practice.

Source: own elaboration based on specified sources as listed in the table.

5.12 PROBLEMATIC ISSUES AND RELATED CASE-LAW

5.12.1 RISKS AND SHORTCOMINGS IN THE LEGAL REGULATION OF TRANSFER PRICING

Consideration for intangibles, intra-group services and cost contribution arrangements

The Czech Republic is governed by the rule of law, which means that in order for a tax obligation to be set, there has to have been a rule embodied in the relevant acts (Income Tax Act, etc.). A tax duty cannot be set by guidelines if there is no background in law. There are no special clauses governing special considerations for intangibles, intra-group services and cost contribution arrangement in any relevant act, however sources of general information or recommendations can be found in Guidance D-34 (General Financial Directorate, 2019). An update of the guidance is desirable in this respect, with special attention paid to considerations for intangibles. There is a reference to DEMPE analysis in Guidance D-34 (General Financial Directorate, 2019), however the guidance provided is quite short and it would be beneficial for tax-payers to have access to more detailed guidance.

Advance pricing agreements in the Czech Republic

In the Czech Republic the situation concerning APAs is not an ideal one and it could be argued that there are many deficiencies in this area.

1. **Czech law has no grounded unilateral APA**, in the meaning as it has been established by the OECD standards (for more information on this aspect of the APA see OECD, 2017a; Brychta and Sulik-Gorecka, 2019).
   The legal instrument grounded in the Czech Republic is the Binding Ruling. This Binding Ruling, however, does not meet the requirements as set (recommended) for an APA by the OECD (OECD, 2017a). This fact complicates the position of the tax-payers. To avoid a negative decision (only two results are at stake in case of the Binding Ruling – a negative or positive decision), the tax-payers sometimes withdraw their applications for binding ruling and submit their applications corrected again (if at all). It is true that the financial administration tends to reach an agreement, however, the legal regulation is quite strict and only two possible results are at stake as mentioned above.
2. **Absence of guidelines for bilateral and multilateral APA**s
   The Czech Republic was criticized for the absence of publicly available guidelines for bilateral and multilateral APAs (OECD, 2014). This situation should have been remedied by the implementation of the Directive on tax dispute resolution (Eur-Lex, 2020c), which should be – according to the statement of the Czech Republic – accompanied by the guidelines for APA procedures. The very first document describing the existing procedures was that of the explanatory report which accompanied the Government Bill. Although this report is freely available, it does not represent official guidance as such and it does not represent the typical type of information source which is used by tax-payers to find information for the solution to an already existing problem.

3. **The narrow scope of the Act on Tax Dispute Resolution**
   The Government Bill for the Act implementing the Directive on Tax Dispute Resolution (Eur-Lex, 2020c) had an extensive scope covering not only situations related to EU countries, but to all contracting States (Office of the Government of the Czech Republic, 2018). However, the scope of the Bill was narrowed and now it covers only situations related to EU tax residents (Chamber of Deputies of the Parliament of the Czech Republic, 2019). Therefore the potential of a new procedural act will not be fully utilized.

5.12.2 TRANSFER PRICING CASE-LAW

There is quite extensive case law relating to transfer pricing. In this respect, the administrative Courts (especially the Supreme Administrative Court) have established and developed many rational rules for the application of the arm´s length principle and the rules serving for the elimination of the arbitrary exercise of public power by tax authorities. A summary of the most significant case law for transfer pricing and related issues can be found in Table 35 below.

Table 35: Summary of selected case law for transfer pricing and related issues

Area covered	Specification of the decision	Conclusion stated therein (the rule as established for transfer pricing or related issue(s))
Burden of Proof	Judgement of the Supreme Administrative Court of 27 June 2007 File No. 1 Afs 60/2006	Adjustment of the tax base according to Sec. 23 para. 7 can be applied if all the below stated conditions are met at the same time: a) associated persons are involved in the transaction, b) the price as set is different from that which would have been set for a transaction between non-associated persons and c) the difference has not been duly and reasonably justified.
Associated Persons - definition	Judgement of the Supreme Administrative Court of 13 June 2013 File No. 7 Afs 47/2013	Associated persons are also the persons which created a legal relationship with the predominant aim to lower the tax base of increase the tax loss. This rule impacts on all the persons in the chain which participated therein (directly or indirectly) and reached a profit due to their participation (lowering the tax base or increasing the tax loss).
Associated Persons - definition	Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010	Associated persons are those who are connected economically, personally or by another functionally equivalent connection to that of economic or personal.
Proof of Burden on the part of the tax authority	Judgement of the Supreme Administrative Court of 04 August 2005 File No. 2 Afs 13/2005 (with a reference to the decision of the Supreme Court of the Czechoslovak Socialistic Republic of 24 March 1970 File No. 7 Tz 84/69)	A chain of indirect evidence is a good enough to prove the investigated fact (i.e. a person acting with the aim to fraudulently transfer tax base). There is set a requirement that only one conclusion can be deduced from the chain of indirect evidence and, at the same time, another potential conclusion does not come into consideration.
Setting the Transfer Price by the Tax Authority	Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010	In the event that the tax authority does not accept the existing transfer price as presented by the tax-payer, then it is the tax authority which shall find out and justify the tax authority insisted market (common) price.

Area covered	Specification of the decision	Conclusion stated therein (the rule as established for transfer pricing or related issue(s))
Setting the Transfer Price by the Tax Authority	Judgement of the Supreme Administrative Court of 31 October 2013 File No. 7 Afs 86/2013	An obligation is set upon the tax authority to inform the tax-payer in an unambiguous way of the set common market price and the way this amount was calculated (it means, among other, the tax authority is obliged to specify the grounds/criteria/instruments used). This obligation shall be fulfilled before the calculation of the difference between the price as stated by the tax-payer and the transfer price as set by tax authority.
Rights of the tax-payer when the price stated by him is not accepted on the part of tax authority	Judgement of the Supreme Administrative Court of 31 October 2013 File No. 7 Afs 86/2013	Tax-payer shall be provided the possibility: a) to state why (for which specific factual and legal reasons) he does not consider the price set by the tax authority to be correct (e.g. for the reasons of a defective choice of criteria or indicators, or a comparison of an incorrect period); b) to state his opinion of the evidence and criteria as set by tax authority and c) to propose other evidence and/or criteria. The tax-payer shall be always provided with information on the consequences when he does not duly justify the differences in the prices.
Limitation of Court Protection within Transfer Price Setting	Judgement of the Supreme Administrative Court of 31 October 2013 File No. 7 Afs 86/2013	The administrative Court shall judge the price, criteria and the procedure leading to finding the price. The administrative Court has no authority to calculate the transfer price itself (or the difference between the prices). The administrative Court shall judge by observing the conditions and the reasonable boundaries whether the conditions for setting the transfer price were observed.
Burden of Proof – an Exemption from the General Rule	Judgement of the Supreme Administrative Court of 13 March 2013 File No. 1 Afs 99/2012	A switch of the burden of proof on the tax-payer in the event he changes his position on the value of transfer prices as declared in his supplementary tax return.
Possible Ways of Setting the Transfer Price by the Tax Authority (definition of so called Reference Price)	Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010	The tax authority can use two ways to set the price: a) using a comparison of the real prices of the same or a similar commodity between existing real independent subjects (a possibility when there is existing and available data on such prices) or b) as a hypothetical estimation based on logical and rational consideration and economical experience (a simulated price for the situation when data on the prices do not exist or are available).
Setting the Transfer Price by the Tax Authority	Judgement of the Supreme Administrative Court of 31 March 2009 File No. 8 Afs 80/2007 Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010	A transfer price as set by the tax authority cannot be set as one figure. For setting the difference between the prices, the tax authority shall set the range and adjust* a tax-payer´s transfer price only to the endpoint of the range that is the most beneficial for the taxpayer.

Area covered	Specification of the decision	Conclusion stated therein (the rule as established for transfer pricing or related issue(s))
Choice of the Subjects for the Comparison (excluding of Loss-making Companies)	Judgement of the Regional Court in Hradec Králové (a branch in Pardubice) of 16 March 2016 File No. 52 Af 34/2014	It is not *a priori* possible to exclude subjects with negative profitability of capital (loss-making companies cannot be automatically excluded from the sample.
Sequence of the Tests Applied	Judgement of the Supreme Administrative Court of 02 March 2011 File No. 8 Afs 19/2010	The sequence of the tests is as followed: substance test, benefit test and finally arm's length tests.
Use of ranges (intervals)	Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010	The price cannot be set, as a rule, as one figure, an interval should be set when determining the so called "reference price" on the part of tax authority. The tax authority shall adjust a taxpayer´s transfer price only to the endpoint of the range that is the most beneficial for the tax-payer.

* If all other conditions for making so are met.
Source: own elaboration based on the judgements as listed in the table.

5.13 SUMMARY OF FINDINGS

The Czech Republic, as well as other EU and non-EU countries, faces tax avoidance and tax evasion activities undertaken by tax subjects. Thus, there is a tax gap – a difference between the tax due and the tax collected (for general information, see OECD, 2017). It seems that the VAT gap has in the long term been brought to the forefront of investigations into tax avoidance (see, for example, studies by Moravec, Hinka and Kaňka, 2018; Institute for Advanced Studies, 2019). This targeting is quite understandable since VAT is considered one of the most important sources of tax income out of the total amount of tax collected and, at the same time, is the most problematic tax in terms of the huge sums involved in tax evasion. However, the tax gap in relation to the issues of income taxes and fair taxation (above all in relation to MNEs) have been attracting more and more attention globally in the last few decades (for research on some aspects see Tax Gap Project Group, 2018). This has also been the case in the Czech Republic (see, for example, studies by Finardi and Vančurová, 2014; Moravec, Rohan and Hinke, 2019). The existence of the tax gaps in connection with breaches in the principles of fair taxation have initiated an OECD action plan (OECD, 2013), which naturally includes the issue of transfer pricing.

Generally speaking, the tax gaps in the V4 countries are relatively high (Frizis, Głowacki and Hoskova, 2017). Regarding the losses to the state budget, the Ministry of Finance of the Czech Republic (2016a) refers to economic analysis showing that the annual loss to state budgets due to aggressive planning by MNEs amounts to 4% to 10% of global corporate income tax revenue (which, according to this estimate, represents a loss of 6 – 15 billion CZK in the case of the Czech Republic[74]). These estimates are very high and despite not being precise, it is evident that it is worth fighting against aggressive tax planning and boosting international administrative cooperation between the Czech Republic and other countries in order to collect a more reasonable proportion of the tax base and tax yield. It is only logical that the Czech Republic has responded to the changes, which have been provoked to a large degree by the OECD project.

One group of changes was connected with the adoption of the obligation of the Czech Republic, as an EU Member State, to adopt and implement the ATAD Directive. The requirements as set out by this piece of secondary EU legislation have their origin in the OECD BEPS action plan, and have been established in Czech tax law, as have other related issues concerning, for example, the exchange of information. The Czech Republic, however, has failed to transpose the directive for tax dispute resolutions (Eur-lex, 2020c), and as a result this relatively important directive has not yet been implemented in the Czech legal system.

74 To compare, see Moravec, Rohan and Hinke (2019).

The second group of changes resulted from the acceptance (adoption) of the updated soft-law related to the OECD Model Convention and OECD Transfer Pricing Guidelines. Despite not being strictly legally binding, these standards have been broadly applied in the Czech Republic. Last but not least, to improve enforcement of the law for transactions with international elements (above all in relation to countering treaty abuse and improvement of dispute resolution mechanisms) the Czech Republic has become a contracting party to the MLI. This multilateral treaty has not yet entered into force, but was signed by the Czech Republic on 07 June 2017 (OECD, 2020)[75].

On the part of the financial tax administration of the Czech Republic, special attention is devoted to transfer pricing, and to be honest, there is good reason for this. As the results included in expert literature suggest, transfer pricing is considered to be a profit shifting technique (see for example Swenson, 2000; Gao and Zhao, 2015; European Commission, 2015), or at least to be an instrument capable of being exploited for profit shifting (Chan, Lo and Mo, 2015). The focus of tax audits on transfer pricing is merely a logical consequence of this, as is the focusing of the competencies of tax authority employees on the area of transfer pricing (Fučík & partneři, 2018). Tax audits for transfer pricing do not only represent control over the correct setting of the transfer price for tax purposes, they represent thorough and far-reaching control of the tax subject. That is to say, the arm´s length principle test is the last to be applied, with substance and benefit tests preceding that of the arm´s length principle. In this respect, one cannot forget another very effective control tool, that is the special appendix to the tax return for Corporate Income Tax, which has made tax audits better targeted (Ministry of Finance of the Czech Republic, 2016b; KPMG, 2017). Thus, considering tax audits in the area of direct taxation, transfer pricing seems to be a very suitable target.

When speaking about legal regulations and the way the rules for transfer pricing have been established, the Czech Republic displays significantly specific differences compared to the remaining V4 countries. However, as the results of studies suggest, the Czech Republic can be classified as a member of certain clusters in terms of transfer pricing rules. According to a study by Rathke and Rezende (2016), the Czech Republic comes under Group III (Subgroup III). For Group III countries, transfer pricing systems are highly reflective of internationally disseminated transfer pricing standards – these countries follow OECD guidelines with respect to transfer pricing methods and their application. Within Group III, Subgroup III includes the following countries: *Chile, the Czech Republic, Greece, Peru, the Philippines, Romania, Venezuela* and *Vietnam*. These countries, with some exceptions, have a weaker tradition of agreement schemes between tax authorities and the taxpayer, since the tax rules do not formally implement competent authority procedures for undertaking double-taxation cases, while APA rules are considered relatively recent for most of these countries. Rathke and Rezende (2016) claim that competent authority procedures are available only in the Czech Republic and Greece; however, the chances of resolving double taxation cases in these countries can be considered as low. In this respect, it is worth mentioning that the Czech Republic suffers from insufficient rules explicitly embodied in law (OECD, 2018), and that these are not visible for the taxpayer. This omission will remain since the Bill for the act implementing the tax dispute resolution directive consists of a significantly narrowed down version. The current version of the Bill includes the minimum as required by the directive, while the previous and more suitable version of the Bill also covered situations related to all contracting countries, not only to EU Member Countries as it is now (compare the versions of the Bill as given by the Office of the Government of the Czech Republic, 2018 and Chamber of Deputies of the Parliament of the Czech Republic, 2019).

A study by Ignat and Feleagã (2017) placed the Czech Republic in Category 1 together with *Azerbaijan, Belgium, Finland, Germany, Latvia, Lithuania, Sweden* and *Switzerland*. These countries, as observed by the authors of the study, show less strict transfer pricing regulations:

a) An annual transfer pricing documentation file is not required.
b) There is no fixed deadline for preparing transfer pricing documentation; the deadline for the submission of the transfer pricing file upon the request of the tax authorities is (with exceptions) over 30 days.
c) There are no penalties for not complying with transfer pricing documentation requirements (with some exceptions).
d) The benchmark analysis does not have to be updated annually (with exceptions).

75 The status for the Czech Republic: *"Deposit of Instrument of Ratification, Acceptance or Approval – not realized yet"* (OECD, 2020).

e) BEPS action 13 and/ or Action 8-10 are not implemented in local legislation.
f) The statute of limitation is lower than 5 years (with the exception of Sweden).
g) APAs are available (with the exception of Azerbaijan).

Within the classification provided by this study, the Czech Republic, Belgium and Finland obtained the lowest score for transfer pricing rigour. As for the conclusions stated above, the conclusions stated under letters a) – d) can be considered to be still valid. The Czech Republic is a country in which transfer pricing documentation is not obligatory and, as a result, no duties or penalties related to the obligation to prepare transfer pricing documentation can be imposed. However, this instrument is broadly understood to mean that it is much easier for a taxpayer to bear their burden of proof if they have transfer pricing documentation. BEPS action plan 13 and action plans 8-10 are actually implemented, or reflected, in domestic law. BEPS action plan 13 was reflected in Czech law thanks to the adoption of the rules stated in EU secondary law. The measures stated in actions 8-10 are depend on the implementation, or more precisely in many case the 'mere' promulgation, of OECD standards as those applicable for transfer pricing.

As for the APA criterion, it must be noted that the legal regulations of the Binding Ruling are far from the APA as understood by OECD standards (Brychta and Sulik-Gorecka, 2019). However, to sum up, one can conclude that the observation presented several years ago in a study by Lohse, Riedel and Spengel (2012) on the low rigorousness of transfer pricing in the Czech Republic remains valid. It is worth mentioning that due to the absence of explicit rules embodied in the acts, case-law plays a vital and indisputable role in setting the rules for transfer pricing.

As already stated above, from the legal point of view, the use of the OECD Transfer Pricing Guidelines for controlled transactions in cases when a tax resident comes from a contracting state appears to be without problems.

Regarding the position of the OECD (and EU soft-law) standards in domestic controlled transactions and transactions relating to non-contracting States, their position doesn´t seem to be so strong due to their introduction in the legal system by means of 'D-series' guidelines. On the other hand, one can conclude that departing from the problematic aspect of 'D-series' guidelines[76], the facts and circumstances listed below argue in favour of the use of soft-law included in 'D-series' guidelines on the part of tax subjects:

a) OECD standards, or rather OECD and EU soft-law standards, have become acknowledged and broadly applied standards – both on the part of taxpayers and tax authorities;
b) these standards are broadly applied even in purely domestic (intrastate) controlled transactions;
c) familiarity with these standards has been continuously growing, not only on the part of the expert public, which increases their relevance for administrative practice (this is at least partly attributable to the growing number of publications and seminars dealing with this topic[77]);
d) the 'D-series' guidelines fundamentally eliminate the gaps caused by the very general legal regulation embodied in the Income Tax Act;
e) the instructions stated therein provide guidance whose observance boosts the legal certainty on the part of the taxpayer and strengthens their position in bearing burden of proof;
f) the application of the 'D-series' guidelines has also been approved by administrative Courts for purely domestic controlled transactions, despite a taxpayer objection that it was impossible to use the guidance for their case (from more recent decisions, see e.g. the Judgement of the Supreme Administrative Court of the Czech Republic of 19 September 2019 File No. 5 Afs 341/2017), and last but not least,
g) a Czech translation of the OECD Transfer Pricing Guidelines exists, which enables the actual and potential addressees of the rules to become familiar with the OECD Transfer Pricing Guidelines and the standards established therein. (Brychta and Svirák, 2020)

On the other hand, in terms of the manner in which promulgation of the OECD and EU standards was introduced in intrastate controlled transactions and controlled transactions in relation to non-contracting countries, a tax authority cannot insist on rigorous fulfilment of everything in the manner prescribed (suggested) in the OECD transfer pricing guidelines and/or the 'D-series' guidelines. After all, this is not even possible, since the OECD transfer pricing guidelines are not strict and rigid. For this reason, the

76 In the meaning of the absence of their direct binding nature.
77 There are even university subjects focused only on transfer pricing at some economic faculties in the Czech Republic.

conclusion also remains valid for controlled transactions related to a contracting State. Due to the absence of legal enactments, the tax authority seems to be obliged to accept any equivalent form of fulfilling the requirements as set out under Sec. 23 para. 7 and related provisions of the Income Tax Act (Income Tax Act, 1992).

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ANNEX

Table 36: Overview of DTTs in which the Czech Republic is a contracting party – categories of the rules as included under Art. 9 (*Associated Persons*)

Contracting country	EU Country	OECD Country	Year of publishing in the Collection of Laws/ Collection of International Treaties	Amendment by an Proto-col (Year)	Type of DTT according to the rules as embodied under Article 9		
					category I	category II	category III
Albania	NO	NO	1996	x			X
Armenia	NO	NO	2009	x	X		
Australia	NO	YES	1996	x			X
Austria	YES	YES	2007	2012	X		
Azerbaijan	NO	NO	2006	2006			X
Bahrain	NO	NO	2012	x	X		
Barbados	NO	NO	2012	x			X
Belarus	NO	NO	1998	2011	X		
Belgium	YES	YES	2000	2015	X		
Bosnia and Herzegovina	NO	NO	2010	x			X
Brazil	NO	NO	1991	1991	X		
Bulgaria	YES	NO	1999	x	X		
Canada	NO	YES	2002	x			X
Columbia	NO	NO	2015	x			X
Croatia	YES	NO	2000	2012			X
Cyprus	YES	NO	2009	2009	X		
Denmark	YES	YES	2013	2013		X	
Egypt	NO	NO	1995	x	X		
Estonia	YES	YES	1995	x	X		
Ethiopia	NO	NO	2008	x			X
Finland	YES	NO	1996	x			X
France	YES	YES	2005	2005	X		
Georgia	NO	NO	2007	x			X
Germany	YES	YES	1984	x		X	
Great Britain	YES	YES	1992	x	X		
Greece	YES	YES	1989	x	X		
Hong Kong	NO	NO	2012	x			X
Hungary	YES	YES	1995	x	X		
Chile	NO	YES	2017	x			X
China	NO	NO	2011	x			X
Iceland	NO	YES	2001	x	X		
India	NO	NO	1999	x	X		
Indonesia	NO	NO	1996	1996	X		
Iran	NO	NO	2016	2016			X
Ireland	YES	YES	1996	x		X	
Israel	NO	YES	1995	x			X
Italy	YES	YES	1985	1985	X		
Japan	NO	YES	1979	x	X		

Contracting country	EU Country	OECD Country	Year of publishing in the Collection of Laws/ Collection of International Treaties	Amendment by an Proto-col (Year)	Type of DTT according to the rules as embodied under Article 9		
					category I	category II	category III
Jordan	NO	NO	2007	x	X		
Kazakhstan	NO	NO	2000	2016			X
Kuwait	NO	NO	2004	x			X
Latvia	YES	YES	1995	x	X		
Lebanon	NO	NO	2000	x			X
Liechtenstein	NO	NO	2016	2016			X
Lithuania	YES	YES	1995	x	X		
Luxembourg	YES	YES	2014	2014		X	
Macedonia	NO	NO	2002	x	X		
Malaysia	NO	NO	1998	x	X		
Malta	YES	NO	1997	x			X
Mexico	NO	YES	2003	x	X		
Moldavia	NO	NO	2000	2005	X		
Mongolia	NO	NO	1999	x	X		
Morocco	NO	NO	2006	x			X
Netherlands	YES	YES	1974	1997 (2013)	X		
New Zealand	NO	YES	2008	x			X
Nigeria	NO	NO	1991	1999		X	
North Korea	NO	NO	2006	x		X	
Norway	NO	YES	2005	x		X	
Pakistan	NO	NO	2015	x	X		
Philippines	NO	NO	2003	2003	X		
Poland	YES	YES	2012	x			X
Portugal	YES	YES	1997	x		X	
Republic of Panama	NO	NO	2013	x			X
Romania	YES	NO	1994	x		X	
Russia	NO	NO	1997	2009	X		
Saudi Arabia	NO	NO	2013	x			X
Serbia and Montenegro	NO	NO	2005	2011	X		
Singapore	NO	NO	1998	2014			X
Slovakia	YES	YES	2003	x			X
Slovenia	YES	YES	1998	x			X
South Africa	NO	NO	1997	x		X	
South Korea	NO	YES	1995	x	X		
Spain	YES	YES	1982	x		X	
Sri Lanka	NO	NO	1979	x	X		
Sweden	YES	YES	1981	x	X		
Switzerland	NO	YES	1996	2013		X	
Syrian Arabic Republic	NO	NO	2009	2009			X
Tajikistan	NO	NO	2007	x	X		
Thailand	NO	NO	1995	x	X		

Contracting country	EU Country	OECD Country	Year of publishing in the Collection of Laws/ Collection of International Treaties	Amendment by an Protocol (Year)	Type of DTT according to the rules as embodied under Article 9		
					category I	category II	category III
Tunisia	NO	NO	1992	x		X	
Turkey	NO	YES	2004	2004			X
Turkmenistan	NO	NO	2018	x			X
Ukraine	NO	NO	1999	2016	X		
United Arab Emirates	NO	NO	1997	1997; 2004	X		
USA	NO	YES	1994	1999			X
Uzbekistan	NO	NO	2001	2012			X
Venezuela	NO	NO	1998	1998	X		
Vietnam	NO	NO	1998	x	X		

Source: own elaboration based on Ministry of Finance of the Czech Republic (2019a).

Note: the categorisation is based on the basic rules; specific provisions have not been taken into consideration.

CHAPTER 6
LEGAL REGULATIONS IN HUNGARY

6.1 SPECIFICATION OF THE SOURCES OF LAW WHICH INCLUDE (OR ARE RELATED TO) TRANSFER PRICING

6.1.1 GENERAL ASPECTS OF LEGAL REGULATION

This chapter contains a short description of the legal system in Hungary. Hungary has a civil law system and applies the universally accepted rules and regulations of international law. Hungary has become a member of EU in 2004, therefore Hungary should adapt the European Union law.

The supreme law of Hungary is the Fundamental Law. It regulates two classical constitutional areas: state administration (national government, local government, and organizations for the protection of rights) and the fundamental rights of citizens. Hungary had recognized the generally accepted standards of international law and had ensured the harmonisation of international obligations with the domestic law. In 1989 the political and economic transition in Hungary was accompanied by a peaceful 'civil rights revolution'. As a result, a Parliamentary Act significantly extended the catalogue of rights in the Fundamental Law. The Hungarian Constitutional Court was established in 1989. Its field of authority provided the possibility for citizens to challenge the constitutionality of any legal standards and judicial decisions on the ground of unconstitutionality. (Unesco, 2020)

There is basically two approaches to the relationship between international and domestic law: dualistic and monistic approach. The Hungarian legal system is dualistic, therefore international agreements must be promulgated in Hungary by law or government decree, given the dualistic nature of the Hungarian legal system. With the promulgation of international treaties, they become part of the domestic law: by the proclamation, they create rights and transfer obligations to state organs and individuals. According to the Hungarian legal system, the international treaty proclaimed by law is subordinate to the Fundamental Law, but above in the hierarchy of regulations, and the international treaty proclaimed by government decree is subordinate to the law but above government decrees. (Cserny and Téglási, 2014; Őry 2016)

The Fundamental Law entered into force on 01.01.2012. Article T. determines the sources of law:

„ (1) Generally binding rules of conduct may be laid down in the Fundamental Law or in-laws, adopted by an organ having legislative competence and specified in the Fundamental Law, which is promulgated in the official gazette. A cardinal Act may lay down different rules for the promulgation of local government decrees and of laws adopted during a special legal order.

(2) Laws shall be Acts, government decrees, prime ministerial decrees, ministerial decrees, decrees of the Governor of the Hungarian National Bank, decrees of the heads of independent regulatory organs and local government decrees. In addition, decrees of the National Defence Council adopted during a state of national crisis and decrees of the President of the Republic adopted during a state of emergency shall also be laws.

(3) No law shall conflict with the Fundamental Law.

(4) Cardinal Acts shall be Acts, the adoption and amendment of which requires the votes of two-thirds of the Members of the National Assembly present" (Fundamental Law, Article T, 2012)

The Fundamental Law determines the sources and hierarchy of law (Article T, Section 2):

- Acts of Parliament;
- Decrees:
  - Government decrees;
  - Prime Ministerial Decrees;
  - Ministerial Decrees;
  - Decrees by the Governor of the National Bank of Hungary;
  - Decrees by the Heads of Autonomous Regulatory Bodies;
  - Local Government Decrees.

The definition of the Acts of Parliament is the following: *"Acts are adopted by the National Assembly. According to the Fundamental Law, the rules for fundamental rights and obligations are determined by acts. The National Assembly adopts Acts by a simple majority of votes (more than half of the votes of the members present), except for so-called cardinal Acts defined by the Fundamental Law, the adoption and amendment of which require a two-thirds majority of the votes of Members of the National Assembly present. According to the Fundamental Law the authorisation to recognise the binding nature of the European Union's founding and amending Treaties, the declaration of a state of war, conclusion of peace and declaration of a state of special legal order require a two-thirds majority of the votes of all Members of the National Assembly"*. (Fundamental Law, Article T, Section 2)

The government's authority to enact decrees may be primary or based on legislative authority. The government may issue decrees within its sphere of authority on any matter not regulated by an act. No decree of the government should conflict with any act. This does not restrict the powers of the National Assembly, which may consider any regulatory field under its authority.

The Prime Minister can also issue decrees, e.g. appoint a deputy prime minister from among the ministers by decree. Prime ministerial decrees are ranked at the same level as ministerial decrees in the hierarchy of legislation.

Ministerial Decrees are ranked below government decrees in the hierarchy of legislation. Ministers adapt decrees by authority of an act or a government decree (issued within their original legislative competence), whether independently or in agreement with any other minister; such decrees may not conflict with any act, government decree or decree of the Governor of the National Bank of Hungary.

Acting within his or her competence defined by a cardinal act, the Governor of the National Bank of Hungary may issue decrees by statutory authorisation, which may not conflict with any law.

Acting within their competence defined by a cardinal Act, the heads of autonomous regulatory bodies issue decrees by statutory authorisation, which may not conflict with any Act, government decree, Prime Ministerial decree, ministerial decree or with any decree of the Governor of the National Bank of Hungary.

Local governments may adopt local decrees in order to regulate local social relations not regulated by an Act or by the authority of an Act. Local government decrees may not conflict with any other legislation. (European E-Justice, 2020)

6.1.2 LEGAL REGULATIONS IN HUNGARY RELATED TO TRANSFER PRICING

An overview of the Hungarian legal regulations on transfer pricing is provided in this chapter. The Hungarian regulations are adapted to the OECD Transfer Pricing Guidelines, and after their renewal, the Hungarian regulations have been adapted to the arm's length principle, therefore the of maximum transparency and comparability is realized (Government Decree 32/2017. (X.18.)). However, several laws on transfer pricing and affiliated companies also provide guidelines. The transfer pricing rules for affiliated corporate taxpayers are fundamentally in line with the arm's length principle, i.e. the three-level obligation for taxpayers: the submitting, the tax base adjustment and the documentation obligation have not changed. The regulations have entered into force in January of 2018 and determined a new set of rules regarding the documentation obligation. Although a new regulation has been introduced in Hungary due to changes in the form and content of the documents, the transfer pricing rules are based on the principles laid down in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Authorities (OECD, 2010, 2017). The documentation obligation has become a three-level obligation or has remained two-level if a given condition is met.

The current **three-level documentation** requires the following types of documents:

- Country by Country Report (CbCR);
- Master File: analysis of financial, economic data; organisational structure, value chain and main activities for the whole group;
- Local File: the market share and position of the enterprise; financial indicators, organisational structure and presentation of activities.

On the legal background the following sources of laws are the most important regulations on transfer pricing and the definition of the associated person:

- Act XXXVII of 2013 on Certain Rules for International Administrative Cooperation in Tax and Other Public Duties;
- Guideline on the obligation to keep records of the transfer price. Government Decree 32/2017. (X.18.);
- Act LXXXI of 1996 on Corporate Tax and Dividend Tax. Act (from now on: Corporate Tax Act).

Previously, the taxpayers had the opportunity to prepare the Master File and the Local File separately, and the law also allowed preparing a joint register (e.g. the parent company prepared the Master File, what the members of the group applied into their own documentation without changes). The current regulation requires the preparation of the Master File and the Local File for all taxpayers separately with much more detailed data content, complex analyses and diagrams. The Master File for the company group must be prepared separately in every case because it is not guaranteed that the same companies should be determined as a group within an international group of companies, and it is not certain that each member is connected to each other.

The Country by Country Report[78] does not have to be prepared for all taxpayers, only where the group-level turnover is above 750 million (EUR). Hungarian subsidiaries must also pay attention to this threshold, but the lack of information makes the fulfilment of their obligations difficult, they may not know the entire group chain. The superior parent company is obligated to prepare the documentation. Due to the characteristics of the Hungarian economy (there are mostly subsidiaries with foreign investors), only a few companies are obliged to prepare the CbCR in Hungary (i.e. MOL Plc.).

The Corporate Tax Act (Section 18. (5)) defines the **taxpayer who is obligated to prepare a transfer pricing documentation** if it has an affiliated person:

- business associations (general partnership, limited partnership, limited liability company, joint venture, joint-stock company),
- merger,
- European company joint-stock company,
- cooperative,
- European cooperative and foreign entrepreneur.

The details of the documentation and some exceptions are set out in Government Decree 32/2017. (X.18.)

There are **exemptions of transfer pricing documentation obligation** in several cases, the most important of them are the followings:

- companies qualified as *small-and-medium-sized companies* on the last day of the tax year: in the last two fiscal years the number of employees should not exceed fifty persons and the amount of the net sales or the balance sheet total should up to 10 million EUR (at group level);
- *non-profit organisations* of public interest;
- companies where the *state has a major influence;*
- the annual transaction value of *less than 50 million HUF at the group level* (approximately 156 thousand EUR): it is important that after consolidation, it should be analysed at transfer price;
- *free value-added service*: it must be confirmed that the cost has been billed without a profit margin. If it had been billed to more than one person, the distribution method must be in line with the arm's length principle.

However, companies exempted from the documentation obligation should also pay attention to the transfer price and the tax base adjustment. The Hungarian corporate tax regulations classify the difference between the transfer price and the applied price as a tax-base reduction item. In case of discrepancies, the increase of the tax base is mandatory and may be reduced under certain conditions. For subjects on the

78 Act XXXVII of 2013 on Certain Rules for International Administrative Cooperation in Tax and Other Public Duties

Small Business Tax[79], the tax base should be determined as if the related parties had contracted at transfer price. In case of discrepancies, the tax base must also be corrected here (Berényi, 2017).

6.2 DEFINITION OF KEY TERMS IN DOMESTIC LAW

6.2.1 DEFINITION BY THE ACCOUNTING ACT AND IAS 24

Fist of all, for an enterprise in order to keep a transfer pricing documentation, it is necessary to examine whether it has an associated relationship or not. However, the definition of an associated person is not unified for each source of law. The provisions of the Corporate Tax Act must be applied for the transfer pricing, but the Accounting Act, other tax regulations (e.g. VAT, local taxes, small business tax) and international accounting standards also have their own interpretation for an associated person. This chapter describes the definitions of affiliated companies in Hungarian legal regulations with highlighting the differences.

The parent company and the subsidiary, as well as the jointly controlled entity, are considered to be associated person **under Act C. of 2000 on Accounting**. According to the law, the *parent company* is the entrepreneur who directly or indirectly has a dominant influence over another entrepreneur (subsidiary) because it is in line with at least one of the following conditions:

- based on its ownership percentage in the share capital, it solely controls the majority (over 50 per cent) of the votes of the owners (shareholders),
- it solely controls the majority of votes based on an agreement with the other owners (shareholders),
- in its capacity as an owner (shareholder) of the company, it is entitled to elect or dismiss the majority of executive employees or members of the supervisory board
- based on a contract concluded with the owners (shareholders), or a provision of the instrument of the constitution, it exercises dominant supervision and control, irrespective of its percentage in the share capital, voting ratio and the right to elect and dismiss executive employees.

According to the Accounting Act, a *subsidiary* is the business entity in which the parent company has a dominant influence. A *jointly controlled entity* shall mean a business association in which, on the one hand, the parent company (or the consolidated subsidiary of the parent company), and on the other hand, one (or several) another enterprise (s), have at least 33 per cent voting rights. *Associated company* shall mean a business association that is not fully consolidated, in which the parent company or a consolidated subsidiary thereof has a substantial share and exercises considerable influence over the business and financial policy of the business association. A company that controls, directly or indirectly, owns a minimum of 20 per cent of the votes in another business association shall be determined as a considerable influence. Also, the Accounting Act refers to IAS 24 for the definition of a related party.

Under IAS 24, an entity is classified as a *related party* as follows (IAS 24, 2020):

- Controls; is controlled by; or is under common control with the entity (this includes parents, subsidiaries and fellow subsidiaries.
- Has an interest in the entity that gives it significant influence over the entity or has joint control over the entity.
- The party is an associate of the entity, or the party is a joint venture in which the entity is a venturer.
- The party is in a key position is under the control or significant influence of the entity or its subsidiary, or close relatives of that individual, or their relatives.

A *related party transaction* is a transfer of resources, services or obligations between related parties, regardless of whether a price is charged.

79 A simplified form of taxation for the replacement of corporation tax can be chosen for small enterprises, which can be selected at the group level with a value of 1 billion HUF and a maximum of 50 employees (Act CXLVII of 2012 on the Fixed-Rate Tax of Low Tax-Bracket Enterprises and on Small Business Tax).

Close members of the family of an individual are those family members who may be expected to influence or be influenced by, that individual in their dealings with the entity. They may include:

- the individual's domestic partner and children;
- children of the individual's domestic partner; and
- dependants of the individual or the individual's domestic partner.

6.2.2 DEFINITION BY THE CORPORATE TAX ACT

For transfer pricing, the definition of an associated person appearing in the **Corporate Tax Act** should be taken into consideration. The Corporate Tax Act also lists an individual person as an associated person, as the IAS 24. The definition of an associated person under the Corporate Tax Act is the following: 'the taxpayer has a direct or indirect majority of influence and if a third party establishes an associated relationship by having a majority of influence in both parties'. According to the law, the status of the affiliated parties is also applicable to individuals. It is important that the votes of close family members are added up (spouse, relatives and siblings).

From 2015, the relationship will be realised even in case of the identity of the executive. However, in this case, the act does not examine the close relatives (e.g. two siblings in a different company are not associated).

The Corporate Tax Act cites the Civil Code in the rules of an associated person and does not mention the definition of the majority of control. The Civil Code determines the definition for majority control (more than 50%). In addition, the Corporate Tax Act determines that 25% of direct or indirect voting power shall be considered as an associated person too. For a summary see Table 37.

Table 37: Interpretive provisions of Corporate Tax Act for the definition of the associated person

Provision	Rule(s) stated therein
Sec. 4:23 (a)	the taxpayer and the person in which the taxpayer has a majority control - whether directly or indirectly - according to the provisions of the Civil Code
Sec. 4:23 (b)	the taxpayer and the person that has majority control in the taxpayer - whether directly or indirectly - according to the provisions of the Civil Code
Sec. 4:23 (c)	the taxpayer and another person if a third party has majority control in both the taxpayer and such other person - whether directly or indirectly - according to the provisions of the Civil Code, where any close relative holding a majority control in the taxpayer and the other person shall be recognized as third parties
Sec. 4:23 (d)	a non-resident entrepreneur and its domestic place of business and the business establishments of the nonresident entrepreneur, furthermore, the domestic place of business of a nonresident entrepreneur and the person who maintains the relationship defined under Paragraphs a)-c) with the nonresident entrepreneur
Sec. 4:23 (e)	the taxpayer and its foreign branch, and the taxpayer's foreign branch and the person who maintains the relationship defined under Paragraphs a)-c) with the taxpayer
Sec. 4:23 (f)	the taxpayer and the other person in which the taxpayer has a decisive influence over business and financial policy
Sec. 4:23 (g)	notwithstanding points (a) to (c), an affiliated relationship shall be established for the purposes of point 11, point (controlled foreign company) 53 (independent company) and point (f) of Article 8 (1) if at least one taxpayer and another person has a 25% direct or indirect shareholding or at least 25% direct or indirect equity participation or at least 25% interest in profits, without prejudice to subparagraph (f) for the purposes of these provisions

Source: own elaboration based on Act LXXXI of 1996 on Corporate Taxation, Sec. 4:23.

The concept of the majority of influence is described by the Civil Code (Act V of 2013, § 8 (2)): more than 50% of the voting power and the dominant influence are the majority (for more details see Table 38). We can consider a decisive influence when it comes to the majority of the votes based on the agreement between the members and holds the right of manager selection and recall. In this respect, a similar definition to the Accounting Act can be observed.

Table 38: Interpretive provisions of Civil Code about "Control"

Provision	Rule(s) stated therein
Sec. 8:2 (1)	Controlling interest is a relationship through which a natural person or a legal person (controlling shareholder) alone has more than half of the votes or significant influence.
Sec. 8:2 (2)	The controlling shareholder shall have a significant influence in a legal person if he is its member or shareholder and a) is entitled to elect or remove the majority of the executive officers or members of the supervisory board of this legal person, or b) other members or shareholders of the legal person vote in the same way as the controlling shareholder do or exercise their voting rights through the controlling shareholder provided that they have more than half of the votes together.
Sec. 8:2 (3)	Controlling interest also prevails if the controlling shareholder has the entitlements under paragraphs (1) to (2) through indirect control.
Sec. 8:2 (4)	A person having control in another legal person (intermediate legal person) having voting right in the legal person shall have indirect control in the legal person. The extent of indirect control shall be the same share of control of the intermediate legal person that the controlling shareholder has in the intermediate legal person. If the controlling shareholder has a control exceeding half of the votes in the intermediate legal person, the control of the intermediate legal person in the legal person shall be fully considered as the indirect control of the controlling shareholder.
Sec. 8:2 (5)	Direct and indirect shares of ownership or voting rights of close relatives shall be counted together

Source: own elaboration based on Act V of 2013 on the Civil Code, Sec. 8:2.

It is clear that the Accounting Act, IAS 24 and the Corporate Tax Act are not unified in the definition of an associated person. This can cause difficulties for businesses identifying associated persons and administrative burdens. It may confuse the companies that the definition of associated person could be found in two different acts (Corporate Tax Act, Civil Code).

6.2.3 AFFILIATED RELATIONSHIPS OF MUNICIPAL DOMINANT COMPANIES AND OTHER ORGANIZATIONS

According to the Corporate Tax Act, companies owned by a majority of municipalities could be defined as affiliated companies even the taxpayer is a subject to corporate tax and the other party, the municipality is not. The concept of an associated person is more general in the law. For the purposes of an associated person shall include all legal entity established under domestic law, including the local government as a separate legal entity. The local authority (local government) is a legal entity too. The threshold of the majority of influence, as in all other cases, is reached if the municipality has more than 50% of the taxpayer's votes. In addition, the municipality typically has the right to elect and remove senior executives and considered to have a decisive influence, which may also determine the affiliated relationship. Companies established by the municipality often operate under the same managing director, which also determines the affiliated relationship. (Berényi, 2016)

There are other entities listed by law as taxpayers:

- a foundation, including a public foundation,
- association,
- the legal entity of the church,
- a law office, a patent law office, an enforcement office, a notary's office,
- funds,
- housing associations.

These organizations need to answer the following questions if they have an associated person. Is there any other person who is the establisher (or current owner) of these organizations, ie. the taxpayers, and has a decisive influence? Have they created (or currently own) an organization other than taxpayers in which they have decisive influence? Is there another person who has a decisive influence on the taxpayer and in the other person? Do they have a foreign establishment or own a foreign organization? Is there a related party for executive compliance? In order to answer the questions, they need to look at who the 'other person' is.

An affiliate relationship could exist between a business and a foreign establishment in another country too:

a) in relation to the foreign contractor and its domestic establishment; and
   - between the domestic establishment and the foreign establishment of the foreign entrepreneur, and
   - between the domestic location and other related enterprises of the foreign entrepreneur;
b) in the relation of a resident taxpayer and its foreign establishment; and
   - the foreign establishment of the domestic taxpayer; and
   - between the foreign location of the domestic taxpayer and its affiliated enterprises.

A foreign entrepreneur (a foreign person is defined by the Corporate Tax Act) is obligated to pay corporate tax, but only on income attributable to a domestic establishment, as if it were an independent company (Berényi, 2016).

6.3 LEGAL REGULATIONS AS INCLUDED IN DOUBLE TAX TREATIES

The purpose of concluding double taxation treaties is to reach an agreement between the contracting states on the issue of taxation so that no double taxation or under-taxation is incurred by taxable persons. The model convention established by the OECD provides the basis for these treaties, the model of which is not only used by OECD member countries but also by many other countries around the world on this scheme. In these taxation treaties, the parties determine and regulate at each taxation point which contracting state's regulation may acceptable in given taxation issue, in respect of individuals and companies and in respect of certain income. Once the treaties have been legalized and ratified, the elements of the agreement contained therein may be applied. Hungary has double tax treaties with more than eighty countries. The full list is in this chapter´s annex.

In the most case, the wording of the double tax treaties in Hungary is the same, as the text of the OECD Model Convention's Artice 9. Article 9 contains two chapters, the first one is for the definition of associated parties[80] and the second is for the taxation of profit.[81] We classified the DTTs into four different groups. The first group includes double tax treaties where only the first chapter of Article 9 is mentioned (1), the second group is for countries where the DTT contains the first and second chapter too (1, 2). The third group is the category for special definitions, e.g. a boarder definition of associated parties or the existence of any time limitations. The last group is a special case, the double tax treaty with the United States is uncommon, the conduct is different from the others. The prevailing category is the II with 43 DTTs, therefore one can conclude that more than half of the conducts have exactly the same wording as Article 9 in the first and second chapters.

Table 39 contains the classification of DTTs with EU countries. The dispersion is less significant by EU members, half of them are category while the other group of countries are in category II.

80 Article 9. Associated enterprises. 1. Where a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly. (OECD 2017)

81 Article 9. 2. Where a Contracting State includes in the profits of an enterprise of that State — and taxes accordingly — profits on which an enterprise of the other Contracting State has been charged to tax in that other State and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other State shall make an appropriate adjustment to the amount of the tax charged therein on those profits. In determining such adjustment, due regard shall be had to the other provisions of this Convention and the competent authorities of the Contracting States shall if necessary consult each other. (OECD 2017)

Table 39: Scope of Art. 9 in DTTs in which Hungary has been a contracting party – classification according to the criterion of the EU membership

Category	EU Member State	Non-EU Member State	Totally
I	12	20	32
II	13	30	43
III	3	3	6
IV	0	1	1
Totally	28	54	82

Source: own elaboration.

For the OECD countries is a similar situation, category I and II are the most common groups. (Table 40). Hungary implements Article 9 in double tax treaties as well as in EU or non-EU countries and applied the text for double tax treaties with OECD and the non-OECD Member States too.

Table 40: Extend of Art. 9 in DTTs in which Hungary has been a contracting party – classification according to the criterion of the OECD membership

Category	OECD Member State	Non-OECD Member State	Totally
I	15	17	32
II	13	30	43
III	4	2	6
IV	1	0	1
Totally	33	49	82

Source: own elaboration.

6.4 TRANSFER PRICING REGULATIONS

6.4.1 THE ARM'S LENGTH PRINCIPLE

The transfer price is used between affiliated companies, which in some cases corresponds to the normal market price and in other cases differs from it. The deliberate planning of the transfer price and the deviation of the applied price from the normal market price allows a significant reallocation of income between countries and enterprises. Businesses are trying to shift their income to more favourable tax rates, or to companies that pay less corporate taxes, or may have tax advantages or losses. (Berényi, 2017; Nagy and Földi, 2017)

In 01.01.2018, a new three-level transfer pricing regulation was introduced in Hungary in line with the international legal environment. Affiliated corporate taxpayers are required to apply transfer pricing rules based on stricter regulations due to international transparency. In terms of control, the tax authority can audit the taxpayer concerned with digitalized selection and control systems, high efficiency and in large number. Today, in Hungary, the value of the fines imposed on the transfer price is considerably higher than the value of the fines imposed on the VAT. The focus of the tax audit is the transfer price.

6.4.2 THE REPORTING OBLIGATION

Companies with affiliated companies must submit their related parties to the tax authority. The submitting obligation should be applied only for affiliated companies under the rules of the Corporate Tax Act[82]. The submission must be made within fifteen days of the first conclusion of the contract between the related parties. It is very important that the notification should be made even if the contract has not been fulfilled.

An enterprise has established a subsidiary in a neighbouring country with the first day of the tax year. At the time of its foundation, in addition to its capital, it wanted to secure the current financing with an owner's loan. Therefore, when concluding the activity, a framework contract was concluded based on which the subsidiary

82 The notion of transfer pricing affiliated entity does not affect either the Accounting Act (Act C of 2000 on Accounting), IFRS or other laws that use concepts other than the Corporate Tax Code, such as the VAT Act (Act CXXVII of 2007 on Value Added Tax). However, it should be noted, for example, that the Commercial Tax Act (Act C of 1990 on Local Taxes), the Small Business Tax Act (Act CXLVII of 2012 on the Fixed-Rate Tax of Low Tax-Bracket Enterprises and on Small Business Tax uses the concepts of the Corporate Tax Act).

could, if necessary, use the loan from its parent company for commercial supplies, operating costs. It was not necessary to use the loan in the first tax year only from the second tax year. There was no other transaction between them in the first tax year. Therefore, the Hungarian taxpayer only reported the parent company of a related party in the second year, when the loan was used. The tax authority's audit found that the taxpayer was wrong because the contract should have been made within 15 days of the first day of the contract year. Its fine is 500 thousand HUF (~1560 EUR) for each unrelated affiliated company.

6.4.3 TAX BASE CORRECTION OBLIGATION

At the end of each tax year, a taxpayer with an associated person must determine whether the fulfilment has been effected during the year in the framework of a contract with its affiliated person. If there was a fulfilment, it is necessary to determine the transfer price and, if there is a difference, the corporate tax base should be adjusted. If the tax base has been reduced due to the applied price, it is possible for the taxpayer to set the difference as a deduction item for the corporate tax base, but only if it has a statement from its affiliated company that it increases its tax base with the same value as a Hungarian company.

The difference in the tax base is therefore based on a quantification of the difference between the transfer price and the applied price. However, it is necessary to apply domestic legislation based on international standards to determine the transfer price. These laws, and in particular the OECD Transfer Pricing Guidelines, defines the method to be used for determining the transfer price or price range, the relevant facts and circumstances to be taken into account. In order to determine the transfer price, the Corporate Tax Act provides a brief list of the five methods and other methods defined in the OECD Transfer Pricing Guidelines, provided that the previous methods do not provide a sufficiently comparable sample and the market-narrowing process with an interquartile range.

Legislation in force prior to the current Corporate Tax Act has allowed the tax authorities to change the tax base of affiliated companies since 1992 when they used higher or lower rates in their contracts than those charged by independent partners in comparable circumstances. Until 1996, in determining the transfer price, the tax authority was obliged to accept the market value determined by an authorized expert when adjusting the tax base.

From 1996 onwards, this practice was abolished and the regulation provided for the methods to be used to determine the normal market price, in line with international practice, such as the reference price method, the resale price method and the cost-income method, and subsequently the optional methods. The scope was extended by another method, which allowed taxpayers to apply a normal market price when it could not be determined by any of the three previous methods. As a prerequisite for applying the arm's length principle, the related companies could adjust the tax base by the difference between transfer price and the applied price.

As of 1 January 2001, the possibility of reciprocal adjustment of tax bases was abolished and stricter procedural rules were introduced. Their purpose is that the income is actually accounted for and paid to the company in which it is generated. While retaining the obligation to increase the tax base, the regulation did not allow for a reciprocal and unconditional tax base reduction. The tax base could henceforth only be reduced under certain conditions. (Berényi, 2016)

An **increase** in the tax base is required if, as a result of the actual applied price, the earnings before taxes is lower than it would have been at transfer prices.

It is possible to **reduce** the tax base if, as a result of the actually applied price and the earnings before taxes are higher than what would have been obtained at the transfer price and if the required conditions are met.

From the beginning of 2002, it was introduced in the legislation that the taxable person would not be obligated to the tax increase if its contract with a private individual resulted in a lower EBIT than normal market price. For 2003, similarly to most Western European countries, transfer pricing requirements included a documentation obligation for non-micro or small business, mergers and cooperatives. The document had to include the method used by the taxpayer to determine the transfer price and the facts and circumstances. From the beginning of 2004, the scope of the documentation obligation was extended to include foreign entrepreneurs who were not small businesses. In 2006, the European Cooperative also became one of the obligors. Since 2010, the taxpayer and its foreign establishment have been classified as affiliated companies. From the same year, direct relatives were classified as third parties. And from 2015, executive compliance also established a related business relationship. Affiliated companies, irrespective of their value threshold, are required to apply the arm's length principle and, in the event of a deviation, the tax base adjustment. From 2011, the range of methods that can be used to determine the transfer price has been expanded to include income-based methods. In 2015, the use of a quartile range became mandatory when needed. (Berényi, 2016)

6.4.4 INTRA-GROUP SERVICES

In all cases, it should be determined whether an independent business would be willing to pay for the service, or whether the service represents business value to the other group member, and whether the group member using the service can increase its business potential. For intra-group services, there is a compelling question to ascertain, as it appears in the OECD Transfer Pricing Guidelines, is always whether there has been intra-group service for the application of the transfer pricing principle. (Berényi, 2016)

Typical intra-group services are the deployment of sub-functions to a member of a group of companies, or (e.g. accounting, IT services, etc.) when jointly implemented activities are more economical due to centralization of resources or other rational business reasons. E.g. the joint organization of research and development can be carried out at a lower cost than separately. In addition, there is a typical case of over-invoiced costs, where the common advantage is that the group of companies collectively has a larger, so-called. fleet discounts. (Berényi, 2017)

The OECD Transfer Pricing Guidelines analyzes in detail the issue of transactions that are classified as low value-added intra-group services and the principles for applying the transfer price to intra-group services.

Until January 1, 2012, under domestic regulations, the re-invoicing at constant prices and the related normal market price of services not provided within the group's non-core activities were not highlighted and listed. At that time, a change was made to the law, and the exemption rule, which does not require the registration of a transaction that continues to charge the actual cost bearer group member for consideration for independent third-party service, came into effect.

At first, this exemption rule was applicable only to non-principal invoiced services and supplies, and the rule was extended with effect from 21 June 2013, which was applicable for the first time to non-different taxable persons for the tax year 2013. in such a way that it was not only in the case of principal activities that the company could be exempted from the obligation to register and tax base adjustments in respect of supplies of goods or services invoiced for further invoicing.

In the case of taxpayers with different business years, the change of the law could be applied to the 2012 register as well, provided that the deadline for the registration is not earlier than 1 January 2013.

For billed costs, compliance with the transfer price also means that there is no tax base adjustment on these transactions. As of January 1, 2012, the rules for recording intra-group transactions have changed and the safe harbour rule has been introduced, which is a safety margin that accepts a standard range, in this case, a profit margin of 3% to 7%, as normal market price. With the above secure margins, intra-group services can be taken into account, subject to other appropriate conditions, for the purposes of tax base adjustment or registration, which are included in the itemized list of legislation. The legislation was amended with effect from 21 June 2013; on this basis, for the first time applicable to the tax year 2012, for non-different taxpayers, the amendment rule was enacted to change the 3-7% to 3-10%. In the case of taxpayers with different business years, the 2012 register may also be subject to a change in legislation provided that the deadline for preparing the register is no earlier than 1 January 2013. If the above conditions are met, the profit margin applied within the normal profit range will normally be normal market price and there is no need for a tax base adjustment. (Berényi, 2016)

Article 5 (1) of the Government Decree 32/2017. (X.18) defines that the taxpayer's documentation obligation for low value-added intra-group services listed by Section (2) can be fulfilled (if this type of service is only provided to affiliated companies during the tax year) if the net value of the transaction at transfer price does not exceed HUF 150 million in the tax year and does not exceed 5% of the net sales of the provider for the tax year, or the service should be up to 10 % of the operating costs of the taxpayer.

The documentation shall include:

- the name of the related undertaking involved in the controlled transaction and the tax number or equivalent ID, registration number, and the name of the authority maintaining the commercial register; and headquarter;
- the subject(s) of the contract and the date of its conclusion and modification and the duration of the contract;
- the transfer price (based on information available without comparative analysis);
- the date of preparation.

The profit margin applied by the related party involved in the controlled transaction in accordance shall be from 3 per cent to 7 per cent. (Government Decree 32/2017. (X.18)). This type of low value-added services can be mentioned as safe harbours in transfer pricing (see Table 41 below).

Table 41: Low value-added intra-group services as listed in Annex 1 of Government Decree 32/2017(X.18)

Service group	Name of the service	Statistical number of the activity (in Hungary: TESZOR)
I. Information technology services	1. Computer programming	62.01
	2. Information technology consulting	62.02
	3. Computer operation	62.03
	4. Other information technology services	62.09
	5. Data processing, web hosting services	63.11
II. Real estate transactions	1. Property management	68.32
III. Professional, scientific, research and technical activities	1. Legal services	69.10
	2. Accounting, bookkeeping and tax advisory services	69.20
	3. Translation and interpretation	74.30
	4. Market research	73.20
IV. Educational activities	1. Other educational services	85.59
	2. Supporting activities to education	85.60
V. Administrative services	1. Supporting administrative services	82.1
	2. Other postage services	53.2
VI. Transportation and storage services	1. Storage services	52.1
	2. Transportation services	49.41
	3. Supporting services to transportation	52.2
VII. Other	1. Other accommodation services	55.9
	2. Business catering	56.29.2
	3. Security guard services	80.10.12

Source: own elaboration based on Annex 1 of Government Decree 32/2017(X.18).

6.4.5 TRANSFER PRICING METHODS

In order to determine the transfer price, the registrar must apply one of the following methods (Berényi 2017; Nagy and Földi, 2017):

- comparable price method,
- resale price method,
- cost-plus method,
- Transactional Net Margin Method,
- profit-sharing method,
- other methods.

By incorporating the comparable price method, a company can obtain comparative data and information from internal and external sources. Internal sources arewhere either the obligated company itself or one of the companies involved in the transaction has entered into similar contracts with other independent entities under substantially similar terms; obsession. External sources are the prices used for similar transactions with unrelated parties.

The resale price method is applicable when the product or service purchased from an affiliated company is resold to an unrelated party. The transfer price under this method is the resale price minus the reseller costs and normal profit. The best way to determine the reseller margin for comparison is to minimize the time between the original purchase and resale so that there are no market factors, exchange rates, etc. factors affecting the development of ordinary profit.

In practice, it is not the purchase price corresponding to an industry average after resale rebate that is compared to that of its related affiliates but the gross profitability of the trader compared to the industry average, simply put.

This method is applicable when the margin of the transactions included in the comparison is known. In practice, this information may come from several sources (study, analytical article, chamber of commerce opinion, etc.) or from a series of annual reports. In this case, it should be noted that only those companies in which comparable margins are found for the transaction under consideration can be included in the comparison since the majority of the company's sales were generated by sales of goods similar to that transaction. Since sales prices to unrelated parties can be accepted as being normal market prices, it can be assumed that normal gross margin is based on normal market purchase prices.

The advantage of the method is that it requires much less comparability between products, as it examines compliance with the normal market price by determining normal profit, while the differences arising from activities and business positions need to be carefully considered and thoroughly analyzed. (Berényi, 2016)

In the Cost plus method, the value of the cost plus the usual profit is considered to be the transfer price. The method is typically applicable to product manufacturing companies. The additional benefit to the related party of selling the product or rendering the service in excess of its cost price is related to the normal profit for independent transactions.

During production, due account must be taken of the separate production processes, the semi-finished and the finished product stream, in the pricing of each stage. The full benefits of the manufacturing process can be realized with a global cost-effective benefit for each process independent party. Independent parties, when contracted, agree on cost-effective benefits for the sub-processes of the entire production vertical. At the same time, this cost-benefit sharing also presents the difficulty of the method. Obtaining external information about this is almost impossible, but at least very difficult because it belongs to the category of business secrets.

In this method, the comparability of the product manufactured and the service provided is not negligible, but not the main consideration. More importantly, the evolution of functions, costs, capital structure and different risks. Rather than simply comparing the normal range of profit and the gain from a controlled transaction, it is important to determine the cost structure of the profit for both the taxpayer and the benchmarked companies as a whole, if the transaction under investigation typically represents the whole or cost structure of the transaction. For comparison purposes, adjustments for differences in accounting and adjustments for miscellaneous cost elements that may arise are essential. This ensures that the same cost base has the same benefits, which will form the basis of the comparison. (Berényi 2016)

The Transactional Net Margin Method (TNMM) examines the net profitability of a transaction on an appropriate basis at the industry level and compares this net profitability with the registrant to the net profitability of the controlled transaction. The TNMM method is fundamentally similar to the resale price and cost-plus method and is also a profit-based method. Again, this method compares the profitability data on an industry average basis with the profitability achieved in the controlled transaction. The difference is that the TNMM method compares transactions between affiliated and unrelated parties based on net profit rather than gross profit.

The difference between the analysis of gross and net profit is based on the consideration of different cost levels. The range of costs validated in the indicator should be considered for comparability. Whether interpreted narrowly or broadly, it requires a uniform interpretation of both the sample and the audited transaction.

Gross profit is defined as the ratio of gross margin to gross profit over the cost of production in relation to revenue, assets or expenditure. Net profitability is the ratio of operating profit to revenue, assets or expenses. Its gain compared to other methods is due to the fact that many businesses face limitations in obtaining information regarding business secret information when preparing records. The results of operations and the value of sales or assets, as well as the value of expenditures, can be obtained from the official reports. The Net Profit Based Transaction Method requires a comparative analysis of only one of the related companies, as does the comparative pricing and resale pricing method.

The application of this method is subject to the condition that the major part of the enterprise's principal activity, sales, and profits is derived from the controlled transaction being compared since TNMM takes into account the operating costs of the enterprise as a whole to its operating profit level. (Berényi, 2016)

Under the Transactional Profit Sharing Method, the cumulative profit from a transaction is allocated on an economically justifiable basis to the extent that it would have been distributed by independent parties. The difficulty of the method used is the need to know the total profit realized on the transaction, which was achieved jointly by the related companies involved in the transaction. Consolidated gains can be total gains on transactions or residual gains, in other words, so-called gains. residual profit. Residual profit is the profit that cannot be clearly attributed to one or other related party by other means.

The division may be made on the one hand in proportion to the costs borne by the parties, the functions performed, the risks assumed, supplemented as far as possible by external market data indicating how, in similar circumstances, independent undertakings would have distributed their profits.

The residual profit distribution is done in two steps. In the first step, each participating group member shall be assigned a profit that provides a basic rate of return for each type of transaction it carries, which may be based on market returns achieved by independent entities in similar types of transactions. Allocating the basic yield disregards the yield generated by any unique and valuable asset owned by the participants. In the second stage, any profits remaining after the distribution that has already been made shall be distributed to the participating group members, taking into account special circumstances, such as an individual and valuable assets owned by the participants, or any rights in part. (Berényi, 2016)

It may be used if the above methods do not allow the determination of the transfer price. There is no obstacle to establishing a customary market price by developing a specific method, provided that the procedure complies with the arm's length principle and the principles of the OECD Transfer Pricing Guidelines.

6.4.6 COMPARABILITY ANALYSIS ANALYSIS/COMPLIANCE ANALYSIS OBLIGATION

The documentation is made up of similar modules. Every module is independent of each other. The individual components of the analysis cannot be mechanically applied; however, it is common for all registers to address at least the following topics in addition to the mandatory factual information and the main activities, organizational structure and division of responsibilities of the group. (Berényi, 2016)

- **industry analysis**: by focusing on a particular product or service in a regional and local approach - including the group of companies, the record-keeping company;
- **competition analysis**: mapping of market relationships, opportunities, market conditions of products sold, services rendered or used, their substitutability, their competitive position, transfer pricing policy of the group of companies or the registrar;
- **functional analysis**: allocation of activities, resources, and risks between the group members and within the registrar, with respect to the group of companies and then the registrar, strategic objectives;
- **other methods**: choice of method and reason for it, the indication of transfer price, adjustment procedure, comparison.

In accordance with the OECD Transfer Pricing Guidelines, documentation should be kept in mind when preparing records: Taxpayers should be aware that, despite limitations on documentation requirements, tax authorities are required to determine the transfer price even if the information available is incomplete. Consequently, the taxable person must take into account that the appropriate records and the voluntary provision of documents can provide more convincing evidence of the correctness of the transfer pricing method. (Berényi 2016; Nagy and Földi, 2017)

One of the key areas of analysis is the industry analysis. It is essential that the company making the registration and the transaction to be registered are placed in the surrounding environment and present their activities, products and services in relation to the characteristics of the industry. It is important that the company covers the entire time span, past, present and future trends and extends the analysis to a minimum of 3–5 years.

Information for industry analysis can be drawn from multiple sources. Typically, analyzes published by Hungarian scientific and economic institutions are available (e.g. Central Statistical Office, Institute for Economic Research, Finance Research Co., Hungarian National Bank, various economic chambers). In a cost-reimbursement system, companies also carry out industry-specific analysis, and they can also generate data from paid and free databases. (Berényi, 2016)

In the competition analysis the company must position its product, service, itself or its group of companies in the market for similar products. The company has to show whether it is a defective product or a mass product or a service, whether it is easy to replace your products, services in the market, what is its uniqueness, where the product, service has evolved and in what direction it is developing. What position do similar businesses have in terms of market gain, dominance, comparative advantage? Overall, what market prospects do the business need to be able to stand in their own market.

In this respect, the transfer pricing policy of the group of companies in relation to the division of tasks between the individual group members should be described. (Berényi, 2016)

From 2012, Hungarian legal regulation defines functional analysis as follows:

1. by affiliated companies in controlled transactions;
   - activities carried out, including research and development, design, production, advertising, marketing, transportation and others,
   - resources used, including costs, expenses, investment and others;
   - business risks are undertaken, including foreign exchange risk, guarantee risk, inventory risk, financial risk and others;
2. operation allocation;
3. resource allocation;
4. risk allocation.

Functional analysis is the most important and crucial part of transfer pricing accounting. It describes how the function sharing was established between the business relationship with the affiliate and the group members. With regard to the allocation of activities, it is useful to present the division of activities among the members of the group of companies and within the company, in a structure that is comparable to the activities of independent companies in similar circumstances. When analyzing resources, it is important to consider how much investment or capital investment is required by the record company to perform specific activities compared to group members. (Berényi, 2016)

The company shall record whether its conduct was in line with the transfer pricing principle and shall establish for the relevant transaction the transfer price, the facts and circumstances which support it and compared the transaction price to the transfer price using an appropriate method, taking into account the adjustment factors.

Based on the above, the taxpayer shall justify the extent, direction or absence of the tax base adjustment included in his tax return. The records must be audited by the tax office at the time of the audit and the claims should be rejected and the findings, procedures, principles and methods used should be challenged if they do not agree with them.

Similarly to contracts with independent companies, information on the transfer prices is typically available at the time of the contract with an affiliated company for all rationally operating enterprises.

An enterprise seeking economic activity knows exactly under what conditions, for what consideration, and in what price range its products, services in free circulation, and what decisions are motivated if a different price is applied to the contract with an independent or affiliated company. Enterprises applying the technique of strategic planning also lay down in their internal documents the bases of their pricing, the factors influencing them, which they apply during the application of the price. There is no statutory obligation to make transfer pricing rules, so companies are not required to make them. However, there are benefits to having a well-written policy that builds on the business processes.

Comparative data collected during the tax year or at the time of contract conclusion, contract modification, price changes, systematic collection of facts and circumstances influencing pricing, integration of the enterprise into production and commercial processes, systematic collection of documents, accurate recording of data sources filling the report and the Corporate Tax Act Declaration to be prepared with sufficient data, that is, establishing the tax base based on well-founded conclusions of the transfer pricing register and then determining the corporate tax. (Berényi, 2016)

For the comparatibility analysis companies can use interquartile range with different methods For the elements of the filtered sample determined by the objective filtering criteria, ie the companies remaining in the sample, further filtering is needed before the companies are finally included in the comparative sample. This additional filtering, after objective filtering, should be filtered based on subjective data from the public media. This workflow involves verifying that the company selected in the sample was automatically selected based on real data and comparing activity, resource and risk sharing between the controlled company and the independent company in terms of functional analysis. The transfer pricing register should include the steps of objective screening, the individual screening of the companies remaining in the sample, the actual compliance with the filtering parameters and the independence criterion, as well as the same platform for functional analysis. (Berényi, 2016)

For the comparative sample, it is necessary to decide on the basis of which indicator the comparison should be made and what should be the basis of profitability projection. The indicator can be selected based on the functional analysis performed. There are few net profit indicators:

- **Operating profit / total assets**, ie return on assets or operating profit/return on capital, ie return on capital. Typically, companies with a large portfolio of assets have a reason to have these indicators (such as an asset management company with real estate assets).
- **Operating profit / operating cost**, ie net income. Typically, companies operating at a minimum cost level, with minimal returns, should use the indicator to compare the comparison factors with the comparative sample (eg. municipal companies, manufacturing companies under certain conditions).
- **Operating profit/sales net sales**, ie return on sales. The net profitability of a sample, in the case of a well-filtered sample, represents an industry average, to which the net profitability of a controlled company's transaction becomes comparable.

For the remaining enterprises in the sample, the selected period (typically 3 years) and the selected indicator (typically net operating income/sales) are collected. If the value range contains more values due to a large number (e.g. 100 companies for 3 years), it is advisable to select the characteristic values by interquartile calculation and also to look at the median value that is the centre of the range. The median extracts the lower, upper quarter values from the range, and the median focuses on the midpoint of this intermediate 'two quarter or half' range. It is worth comparing the profitability indicators of the companies included in the comparative sample not for one year, but for several years in order to have more reliability and to follow the tendencies. In practice, therefore, the net profitability of the remaining sample companies should be multiplied over a period of 3 to 5 years and then converted into an interquartile range by the above procedure.

The outlier values of the interquartile ranges, that is, the lower quartile and the upper quartile, delimit the transfer price range for a particular sector, including the transaction being compared. The median of this is the most representative value of the price range presented by the companies involved in the comparison. If the taxpayer 's profitability ratios are in the interquartile range, ie, their profitability is in the order of magnitude above the industry average, no adjustment is needed, and even if the taxpayer' s relevant indicator is around the median, the level of uncertainty is considered low. (Berényi, 2016)

Example of subjective definition of an interquartile range:

One company has found that the net profit method was the most appropriate method to support the price used in its agreements with its affiliated companies. The company applied the selection steps in the selection process and 11 companies remained in the comparative sample. It showed the net profitability of these companies and then formed an interquartile range. Your own business indicator was not even in the profitability range, let alone in the interquartile range. The company began to analyze a sample previously considered comparable and to exclude, for various reasons, that its own profitability did not correspond to the range of the range. This way, he could already describe in the documentation that the price used for the particular transaction corresponded to the normal market price because the company's net profitability fell within the net profitability range of the average industry adjusted as above. During the audit, the tax office accepted the method and went through the selection steps itself, but the comparative sample did not match. It was not accepted that the company was taken out of the sample on a subjective basis - the individual reasons were not appreciated, the lack of taxes and fines were the result of incorrect selection.

The legislation specifies exactly what information may be used in the preparation of the documentation in the view of the contract with the affiliated company for determining the transfer price and for comparative information. In one hand, if the company has a contractual relationship with independent companies for the sale of the same or a substantially similar product or service to related companies, the prices of the company in its contract with the independent party may serve as a basis for comparing transfer prices. In the other hand, if the company has a contractual relationship with independent companies for the sale of the same or a substantially similar product or service to related companies, the prices of the company in its contract with the independent party may serve as a basis for comparing transfer prices (Berényi, 2016)

If neither the company nor its affiliate has a contractual relationship with an independent party for the supply of goods or services such as that between the company and its affiliate, contracts between independent entities may be considered as a source of comparative data.

If there are publicly available data (e.g., industry indicators, market analysis) for a comparable product or service, or stored in a database or available from other sources, it may also be used as a comparative data source. (Until 31.12.2009, only the public database was designated as a potential data source by law.). Furthermore companies can use data on a comparable business in a public or taxable database or available from other sources, publicly available (eg industry indicators, market analysis)

In order to assist the taxpayer in determining its transfer price and to monitor taxpayers' procedures, the tax authority shall, wherever possible, include in its toolbox all database access facilities that may be available to taxpayers on the Internet, professional chambers, that it contains paid or publicly available information.

Amadeus and Orbis, two large, globally acquired, widely acquired databases used by the tax authority, contain not only domestic but also international data, by region, based on their annual accounts. It also contains non-public data on a given company and international group of companies stored in national and international company registers. This database is able to show the ownership structure of the companies, to display the network of relationships and to provide complete financial-economic mapping of a group of companies. The tax office also has other types of database access, such as assisting in its analysis of interest, credit rating or property valuation. Access to the databases available to the tax office is open to any business. However, the cost of access is inappropriate for some taxable persons subject to registration and cannot be incorporated cost-effectively into their cost structure.

Comparisons required by law when compiling the register can only be made using appropriate databases. The international databases, Amadeus and Orbis provide an appropriate basis for conducting regional and sectoral analyzes, and for identifying market components and trends. The Hungarian tax office has these, and among the large domestic companies, those with international backgrounds also have access. The right of access to these databases for some medium-sized and large companies goes beyond what they are still willing and willing to pay for the database.

In the case of domestic enterprises, comparisons with companies operating in a given industry in the domestic circumstances may be most appropriate, taking into account the domestic specificities regarding taxation and the economic environment. Exceptions to this are domestic taxpayers who are heavily exposed to international processes, as international comparisons are more appropriate in their case. For analysis, industry analysis, sector trends, industry comparisons of each activity are required, and in addition to industry analysis available from the Opten database, Qualidat's Tása and Datax databases are also available, as the data source is based on the many corporate tax declarations available at Hungarian Tax Office while maintaining anonymity.

For example, with regard to financial and business databases, the Bloomberg International Database can be used; in the domestic context, the application of the Hungarian National Bank statistics, government bond yields and domestic banks' lending practices may be appropriate. All of these meet the requirements of the regulation, ie. they come from a publicly verifiable source, provided the taxpayer specifies the exact source of data in the documentation. (Berényi, 2016)

In preparing and modifying the documentation, all of the relevant facts and circumstances affecting the transfer price should take into consideration at the time of the conclusion of the contract, when changing the contract, but at the latest upon completion with the expected maximum caution of the company.

6.5 TRANSFER PRICING DOCUMENTATION

6.5.1 DOCUMENTATION OBLIGATION OF GROUPS UNDER 750 MILLION (EUR)

The changes since 2018 primarily concern the transfer pricing obligation. The first task of the group is to determine the transfer price documentation obligation in order to decide whether two-level or three-level is required. Groups with revenue above 750 million euros are subject to three-level registers, and groups with smaller total revenues are subject to two-level registration.

If it has been established that the group does not reach the above threshold by mapping up to the superior parent company, the corporate taxpayers of the group are required to prepare a two-level transfer pricing documentation.

The documentation consists of Master Files and Local Files. Unlike the rules of previous years, starting from the 2018 tax year is no longer an option to create a joint register. In the past, the company had the opportunity to make an independent record, regardless of the group members, or a joint register that required coordinated work. The latter has become mandatory in the same way, for example, for a two-member group of national companies as well as for multinationals.

By international law, Hungarian legislation grants exemptions from the obligation to register transfer prices in some instances or exempts from registration of a particular transaction. The list of those who are obliged to prepare the transfer pricing documentation is listed in the Corporate Tax Act. First of all, on the last day of the tax year, companies, unions and cooperatives that are not exempt (e.g. small business) are obliged to prepare transfer pricing documents. European joint-stock companies, European cooperatives and foreign entrepreneurs are also required. However, under this law, a non-profit company is exempt, but only if it has a public benefit status. The taxpayer in which the state has a direct or indirect majority influence is also exempt.

It is important that if a business company has a business with a non-profit public company in the tax year, then it is true that the non-profit company is not obliged to register, but the taxpayer is obliged to record the transaction between the two. Also, it is essential that the taxpayer is obligated for corporate tax base adjustment if it has a transaction with an affiliated non-profit organization or it has the majority of influence of the state.

The other option for exemption from the transfer pricing documentation obligation is that it is considered a small enterprise based on the combined indicators of the group. This is a legal requirement in the SME Act[83], which is based on EU regulations.[84]

The **Master File** needs to be prepared at the group level. However, at the same time as the Local File is created, all group members need to be localised. Since there are no similar definitions in each country, maybe the Hungarian company has little focus, after its share may be small at the international group level although it is possible that this represents a significant revenue for the Hungarian taxpayer in Hungary. The

83 Act XXXIV.of 2014 on Small and Medium Enterprises, Supporting Their Development

84 Commission Recommendation 2003/361 of 6 May 2003

Master File contains three main topics. In addition to presenting the group in several aspects, the first topic is the primary management processes, the value and decision chain, and the functional analysis, which illustrates the contribution of the actors within the group to value creation. The second topic analyses the intangible rights and research and development processes of the group. The third topic analyses the financial situation, processes, revenues, expenditures, results and, in this context, the tax consequences of the group. The subject of the analysis is whether tax consequences follow the value creation process. The Master File contains two different types of necessary elements, one of them is the analysis detailed above, and the other is object-oriented information (for example the date of documentation). Overall, it is crucial to have information about the company that can produce the Master File. At the same time, it is very important for the Hungarian taxpayer to have an appropriate weight in the analysis. For a local business that produces the Master File itself, it should, if necessary, develop significant collaboration with other members of the group to provide them with the information they need.

The **Local File** requires no less detailed analysis from the taxpayer. It also has two main parts. The first part is the presentation of the enterprise and the analysis of the processes; the second part is the transfer price per transaction made by the methods prescribed by law.

The first part is the presentation of the organisation, in which the organisational chart of the enterprise, the diagram of the decision-making chain and its presentation should be included. The purpose of the presentation is to stand out from the degree of independence in economic decisions. The taxpayer has to list the countries, including those whose management reports, to whom they report on their business. Subsequently, the main business processes and strategies of the company have to be presented, whether they have been affected by corporate group reorganisation, and if so, what impact this has had. Furthermore, it is obligated to list the leading domestic and foreign competitors of the taxpayer. It is necessary to compile and list a transaction list. The values of the transactions must be given for each related party, and the actual and the amount paid for it should be indicated. The nature of the transaction, the identity of the affiliated party involved in the transaction, the most appropriate market pricing method, compliance with the transfer price or non-compliance shall be listed per transaction. Subsequently, the documentation should include the date of making the local file.

In the second part, a transaction-by-transaction analysis is performed, so there are as many sub-chapters as the number of transactions involved. For all transactions, the following content requirement must be met. First of all, the presentation of the transaction should be related to the presentation of the environment and the relevant market. It should also be listed below, together with the identification of the affiliated companies with which the company had a contract and performance in the tax year. In the following, the evolution of payments made and receivable from the counterpart of the transaction is to be included in the affiliated undertakings. Subsequently, the contract for the transaction and all the modified versions thereof must be attached. If the contract is made orally, its detailed description is required. This is followed by a detailed comparative and functional analysis of the affiliated companies involved in the transaction about the changes in previous years. The next step is to present the most appropriate transfer price -setting and the determination of the transfer price. In some cases, a simpler-than-transfer pricing method is acceptable for low value-added services.

Some transactions are not mandatory in the transfer price documentantion. These **exemptions** are listed in Government Decree N32/2017. The most important of them is the exemption of the transaction-level of less than 50 million HUF (~156 thousand EUR) transaction values. However, it is important to emphasise that the transaction must be valued at transfer price, below the market value of 50 million per year in order not to be included in the register. However, companies often include these transactions as the tax base adjustment obligation also covers these transactions, and it may also be useful to document the transfer price shown to meet the threshold. Also, an official price transaction is exempted (but only by specific price), the cost burden (but the related party distribution is already supported by the register) is also exempt from the transaction for which the tax authority has determined the transfer price (APA = Advance Pricing Arrangement).

6.5.2 DOCUMENTATION OBLIGATION OF GROUPS OVER 750 MILLION EUR

The legalisation requires the Hungarian members of groups with a turnover of over 750 million EUR to have three-level documentation. The above-described two-level documentation (Master File + Local File) expands with the obligation to create a Country by Country Report (CbCR.).

The superior parent company of a group is obligated to submit the aggregated country report. Due to the automatic data exchange agreements, this information is available to the tax authorities of all member companies of the group and can be used for tax audits. Although it is not possible to base the finding on data received in the context of automatic data exchange, it may be the starting point for an additional investigation. The measure aims to track the value creation of the group of companies and its tax consequences. It is necessary to examine whether the tax is paid in the country of value creation, or whether the income was allocated to a tax haven.

It is essential for taxpayers to follow the list of valid recognised conventions providing for the automatic sharing of country-by-country reports published on the tax authority's website, as the signatory countries are regularly joining this system. The list is continually updated for the acceding countries and the financial year concerned with the first reporting.

Few of the Hungarian companies are affected by the status of the superior parent company. They are rather members of a multinational group of companies that exceeds 750 million EUR in total net sales. In this case, the Hungarian group member has two tasks. It primarily sends the Country by Country Report (CbCR) for its superior parent company or of the entrusted enterprise of the superior parent company in connection with its domestic activities and taxation. Secondly, the tax authority must notify which member of the group will be the submitter of the aggregated country report. This taxpayer is also affected by the special rule for the Master File. If it is not available in the country of the superior parent company due to the relevant provisions, the Master File can be made later, within a maximum of 12 months and attached to the Local File.

There is still a need to speak of a **group corporation tax entity** in force since 01.01.2019 in Hungary[85]. The Corporate Tax Act does not provide for a transfer price analysis for transactions between group corporate taxpayers, a tax base correction obligation, and therefore a registration obligation, but non-group members still have a triple charge on transfer pricing.

6.6 ADVANCE PRICING AGREEMENTS IN HUNGARY

Since 01.01.2007, the taxpayer can apply to the tax authority for the transfer price the APA (Advance Pricing Arrangements) procedure. The request is for the tax authority to determine by the decision whether it is valid for future transactions

- the method to be used when establishing the transfer price,
- the facts and circumstances on which the finding is based,
- the normal market price, price range - if applicable.

Prior to the preliminary price agreement, the company may initiate a consultation procedure with the tax authorities, which uniquely provides for consultation prior to a tax authority decision. The consultation shall take at the request of the taxpayer, during the prior conciliation procedure or the price determination procedure. The consultation typically sets out the terms of the agreement on the transfer pricing method, the applicable price and the price range for the particular application. During the consultation procedure, the applicant and the acting tax authority consult in advance:

- the conditions for conducting the proceedings,
- time scheduling
- possible ways of cooperation.

The APA procedure may be a possible means of reducing the tax risk by 100%, if the conditions are right, for the period and transaction covered by the agreement. In the course of proceedings, it may be requested that the company intend to conduct unilateral, bilateral or multilateral proceedings in respect of a particular contract or transaction. In the case of a unilateral agreement, an agreement is reached between the taxpayer and its tax authority, and if the transaction is also subject to foreign income tax rules, the agreement does not bind the tax authority of another country. In the case of a bilateral or multilateral procedure, the tax authority consults with the foreign tax authority. In the case of an agreement, there is

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a binding force for the foreign tax authority concerned as well as for the Hungarian tax authority and the main objectives of the OECD Transfer Pricing Directive, the protection of national tax bases and the duality of the enterprise are achieved. It should be noted that the tax administration procedure for establishing the transfer price is different from the conditional tax assessment procedure. Both are taxable transactions for a future transaction, but the conditional tax assessment determines the tax liability of taxpayers directly affected by the transaction or, if possible, the tax base and the tax, based on detailed facts. An application for the determination of the transfer price cannot be made under the conditional tax assessment procedure. (Kerényi, 2011)

The procedure for determining the normal market price may be initiated by taxpayers who are required to record transfer prices. They will be exempted as since 2011. The initiation and conduct of the APA procedure may, by law, only be initiated or conducted by a tax advisor, tax expert, chartered tax expert or attorney and since 2015, by an auditor.

The documentation to be submitted in the course of the procedure shall be in accordance with the legislation required by the record-keeping obligation relating to the determination of the transfer price. In practice, a record of the future transaction is to be made on the basis of assumed data, relationships, trends, and once submitted, the tax authority will make a decision to accept the documentation provided, the method to be used, the underlying facts and circumstances and the normal market price or price range. On the basis of the domestic legal background, in the case of applications filed in practice, the acting tax authority carries out complex, wide-ranging analysis based on various databases, gathering information besides the active fact-finding activity of the applicant company.

In the course of the procedure, the tax authority carries out an authenticity check at the company before making its decision, sometimes inviting the taxpayer to include additional information, facts and circumstances, and then closes the procedure by making a decision. The time limit for the procedure is 120 days, which can be extended twice by 60 days, taking into account that this does not include contact with the foreign tax authorities, the time taken for verification and the rectification. The decision in the case giving rise to the application for the determination of the transfer price is binding on the tax authorities for three to five years. If the taxpayer informs the tax authority about the changing circumstances, facts and circumstances in the course of the annual reporting obligation, or if there is a new fact relevant to the case, he may initiate the amendment of the decision. Consequences of changing facts and circumstances, if the taxpayer does not initiate the amendment of the agreement, shall be borne by the taxpayer. (Kerényi, 2011)

The APA procedure is subject to a fee. Under the current condition, the APA procedure fee can range from HUF 500,000 to HUF 10 million, depending on the used method. In Hungary, there are unilateral, bilateral and multilateral types of APA (Kerényi, 2011).

Since 2015, the Government Decree and Corporate Tax Act Sec. 18 (9) have changed again. Under the new legislation, using the resale price method, the cost-income method, the net profitability method or the cost-sharing method to determine the transfer price of a transaction, contains publicly available tax - controlled information from other sources when using data sources. (Berényi, 2016)

If a taxpayer compares its data in an individual or joint documentation, it is required to determine the transfer price in the documentation as an interquartile range. In determining the transfer price, the taxpayer is entitled to apply adjustments when there are price influencing factors. In determining transfer price, the taxpayer is entitled to apply adjustments in accordance with a pre-existing recommendation in the OECD Transfer Pricing Guidelines if there are factors affecting the price.

The current regulation is clearly described in the new Act on Tax Administration and the Regulation of Tax Administration (Act CLI of 2017). The validity of the APA is generally five years, but it can extend with an additional two years

6.7 PENALTIES FOR BREAKING THE RULES RELATED TO TRANSFER PRICING

According to Act CLI of 2017 on Tax Administration and the Regulation of Tax Administration (Article 29. Sec 215 (1)) tax penalty shall be payable in the event of failure to pay taxes. The tax authority also imposes a tax penalty if the taxpayer has unlawfully submitted the application for subsidy or tax refund. The tax penalty is 50% of the tax deficiency. The tax penalty can be as high as 200% if the tax deficiency results in the concealment of revenue or other serious misconduct and if the taxpayer has unlawfully submitted the application for a subsidy, tax refund, and the tax authority determines the failure before granting it. In such a case, the taxable amount shall be based on the amount unduly claimed. According to Act CLI of 2017, Article 30. Sec. 220 there are fixed-rate penalties for failures in documentation obligations (see Table 42).

Table 42: General Tax Penalties in Hungary

Type of penalties	When the sanction arises	Amount of the sanction
General Tax Penalty	Unless otherwise provided in this Act, the tax penalty shall be fifty per cent of the tax deficiency or unauthorized claim. (Sec 215 (4) For example in general cases and failures to pay taxes	50% of the tax deficiency.
Raised tax penalty (200%)	The amount of the tax penalty is two hundred per cent of the tax deficiency or unauthorized claim if the tax deficiency is related to the concealment of revenue, the production or use of false documents, books, records or the falsification or destruction of documents, books or records. (Sec 215 (4))	200% of the tax deficiency
Fixed-rate penalties	Unless otherwise provided by law, the tax authority may impose a penalty for failure to comply with the tax obligation. (Sec 220 (1)). This type of penalties are for failures in documentation obligation	500.000 HUF for general cases 1.000.000 HUF for special cases

Source: own elaboration based on Act CLI of 2017.

For transfer pricing, there are special rules in penalties. Lack or failure to complete the transfer price register may result in a fine up to 2 million HUF (~6,25 thousand EUR) per transaction. If the taxpayer does not prepare the record on demand, it is 4 million HUF per transaction and then 8 million HUF (25 thousand EUR) for each transaction. Today, auditors are typically asked for transfer pricing records during every tax audit. Documentation goes through strict content control.

The deadline for preparing the transfer pricing register is the date of submission of the corporate income tax, but no later than 31 of May. In practice, it must be available before the preparation of the report, as it can be stated based on this whether the application of the tax base adjustment is necessary for the tax year, or not. The transfer pricing register is not and cannot be submitted to the tax authority. It must be kept together with the report, the corporate tax declaration and with all of its mandatory annexes (i.e. complete contract records and the complete attachment of the contracts to each transaction) in case of a tax audit without delay.

The CbCR obligation is very important, with a fine of 20 million HUF (62,5 thousand EUR) for those who fail to do it. A company that does not fulfil its reporting obligation i.e. does not enter the Country by Country Report of the Group as obligated, is also liable to a fine of 20 million HUF.

If the taxpayer concludes a contract with its affiliated company at a price different from the transfer price, and as a result, the EBIT is lower, it is obliged to increase the tax base. Failure to make a mandatory tax base adjustment for a price other than the transfer price, given that the normal market price adjustment is applied independently of any other tax base item, results in a tax deficiency, leading to the imposition of a late payment surcharge and a tax penalty.

6.8 OTHER OBLIGATIONS

6.8.1 TAX BASE ADJUSTMENT

The duty to increase the tax base due to the deviation from the transfer price is independent of the duty to increase the tax base prescribed by other laws of the Corporate Tax Act, such as the capitalization rule. Where appropriate, a doubling of the tax base is mandatory. With the exception of the following, the obligation to increase the tax base applies to taxable persons who have a contractual relationship with each of its affiliates.

The taxpayer shall be exempt from the obligation to increase the tax base in respect of the following contracts:

- if the taxpayer has a contractual relationship with an individual and the individual does not act as an individual entrepreneur;
- in the case of a long-term contract concluded by a taxpayer with the status of small and medium-sized enterprise for the purpose of eliminating a competitive disadvantage, which is established by the founders for joint purchasing and sale and is predominantly owned by small and medium-sized enterprises;
- according to the transaction to which the taxpayer is subject by law, and in the course of which, transfers to the state or local government, free of charge, subsidies, allowances, assets, investments;
- in the case of a transaction between a resident taxpayer's foreign establishment and its affiliated company, where, under an international convention, income is subject to income tax treatment and any adjustment would not affect the Hungarian tax base.

In the case of an individual, a deviation from the normal market price in respect of the consideration used does not give rise to an obligation to increase the tax base, because the contract with the individual does not (by law) increase the tax base. (Berényi, 2016)

Of the two related parties, a lower or higher tax rate due to the application of a price different from the normal market price, as if the contract had been made between independent parties, obliges the lesser party to increase the tax base but does not automatically allow the lower taxable person.

Conditions for reduction of tax base:

- the taxpayer's EBIT for the tax year would be higher than applying the transfer price, and
- an affiliated company in a contractual relationship with the taxpayer as a resident taxpayer, or a foreign person who is obligated to corporation tax, in which it is resident and who is not a controlled foreign company, and
- has a document signed by the other party indicating the amount of the difference.

The three conditions above must be satisfied at the same time in order for the taxpayer to be entitled to a reduction in his tax base in respect of the transfer price. (Berényi, 2016)

The tax be should be increased or decreased in several cases. The Earnings before Taxes has to be adjusted in the year in which the revenue and expense appear in the income statement and it is determined that the profit or loss is less than it would have been at normal market prices. A taxpayer with affiliated companies must adjust the tax base for each transaction that has a valid contract in the tax year and has been settled within the framework of the contract. However, it should be clarified whether the determination of the transfer price for a particular transaction should be made in writing by the taxpayer or its written obligation in this respect. It is important to know that the transfer price is determined either in writing or verbally, and then the comparison of the transfer price with the applied price, the tax base correction obligation applies to all transactions from the first forint. Also, it is essential to pay attention to invoiced transactions, non-invoiced, occasionally free transactions. (Berényi, 2016)

A well-run, high-turnover Hungarian family business has established its second business. The affiliated business relationship is based on majority influence, after there is a joint ownership group - a private individual and a direct relative - which has a decisive influence on both companies. The affiliated relationship was also established by the executive identity, and the same individual became the managing director of the two companies. The new business has expanded its former wholesale profile with its retail profile. The supply of goods remained with the first company, which then resold a significant proportion of the purchased goods to its affiliated company. The related company resold the goods purchased from the related party in retail trade. This high-value invoiced transaction was complicated between the two companies in the tax year; the transfer price was examined and compared with the applied price. Since the first company sold to independent companies at the same price and terms as its affiliated company by comparative pricing method, it was able to support the transfer price; this transaction did not generate a tax base adjustment. The owner tried to optimise the operation of the group by not setting up an organisational unit performing economic tasks at the newly established subsidiary. The company was also managed by the first company with a car and IT tools registered in the books of the first company. The first company was also accounting for its accounting, and even the IT equipment was the first company. Also, the headquarters of the second company was registered at the site of the first company. All these *without a separate contract, without any consideration. The management of the company thought that it was only the billed events that had to be dealt with in terms of transfer pricing. The tax authority found during an inspection that services were provided free of charge by the first company since the related costs were incurred only by the first company, while the revenue side of the first company was not. The tax authority has established a tax shortage in addition to imposing a tax penalty. The tax deficit is based on the transfer price of the above activities.*

The deadline for establishing the transfer price and comparing the applied price is indirectly included in the legislation. After the corporate tax return forms part of the tax base adjustment items, its latest deadline is the deadline for filing a corporate tax return according to the Corporate Tax Act, 31 May after the tax year in Hungary, but if the taxpayer has previously filed a corporate tax return, the date of filing. However, corporate income tax is included in the company's financial statements, the determination of which is also subject to tax base adjustments for transfer price. Thus, the investigation of transfer pricing should be available before the report is adopted and when the report is prepared. This is the deadline for practice. (Berényi, 2016)

6.9 INFLUENCE OF THE OECD AND EU STANDARDS

6.9.1 MUTUAL AGREEMENT PROCEDURE

Hungary integrates the OECD Transfer Pricing Guidelines and EU Standards for transfer pricing legalisation in domestic low. In the field of income and property taxes, Hungary concludes its double taxation conventions based on the OECD Model Tax Convention on Income and on Property. The list of effective and applicable tax conventions is contained in the Hungarian Tax Authorities' Tax Information on the Hungarian tax conventions applicable since 01.01.2018.

Existing and applicable tax conventions, pursuant to Article 25 of the OECD Model Convention, provide taxpayers with the opportunity to initiate a Mutual Agreement Procedure (MAP), in the event of a possible or possible occurrence of double taxation. The mutual reconciliation procedure is an international dispute settlement mechanism whereby the competent authorities of the contracting states may communicate directly with each other for the purpose of reaching an agreement in individual cases concerning taxation in Hungary and in other states. Mutual consultation may also take place to resolve any difficulties or doubts arising as to the interpretation or application of the tax conventions. (Berényi, 2016)

Since 01.01.2018, the new Taxation Act (Act CLI of 2017 on Tax Administration and the Regulation of Tax Administration) is in force. The document retention obligations are extended until the mutual settlement procedure is completed or if arbitration is subsequently initiated until the arbitration procedure is completed. If the payer and the employer are required to comply with the provisions of this section, the custody obligation shall be extended at the request of the tax authority until the end of the mutual settlement procedure or arbitration. (Hungarian Taxation Office, 2019)

6.9.2 ATAD – ANTI-TAX AVOIDANCE DIRECTIVE (REFLEXION OF THE OECD BEPS PROJECT IN THE EU LAW) AND DAC

Member States are required to transpose the Council Directive (EU) 2016/1164 to national law by 31 December 2019 and to apply its provisions from 1 January 2020. Hungary has changed the Corporate Tax Act (Act. LXXXL of 1996) regarding the definition of associated person and elimination of capital (Eur-Lex 2020b). For a summary see Table 43.

Table 43: Reflexion of the OECD BEPS project in the Hungarian law

Section	Details
Section 1. (23) g):	Clarification of the concept of a related company.
Section 4. (57-60)	In relation to the obligation to transpose Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules for the prevention of tax evasion practices directly affecting the functioning of the internal market, the concept of a hybrid enterprise and a permanent establishment not considered as a single taxable person.

Section	Details
Section 2	Special provisions on the withdrawal of capital: Specific provisions on the elimination of capital are introduced in relation to the obligation to transpose Council Directive (EU) 2016/1164 laying down rules for the prevention of tax evasion and avoidance directly affecting the functioning of the internal market. In accordance with EU requirements, the tax base will be increased by the amount of the market value of the assets and activities transferred at the date of the deduction, or the book value at the time of the withdrawal.

Source: own elaboration based on Act LXXXL of 1996.

Hungarian legislation is fully in line with EU legislation, which is based on Council Directive 2011/16/EU as transposed in 2013 and its amendments. Tax cooperation shall cover all financial obligations imposed by a territorial or administrative unit of a Member State. (Eur-Lex 2020c; Infoszolg, 2017)

The DAC2 Directive has been amended for the first time due to the increasing level of cross-border tax fraud and tax evasion. The amendment (Council Directive 2014/107 / EU, DAC 2) has, among other things, widened the scope of the automatic exchange of information to include data on financial accounts. The change is effective from the tax assessment period beginning at 01.01.2016, ie the first transfer will take place until September 30, 2017. (Eur-lex 2020d)

The second amendment (at the end of 2015) was made necessary by the increasing cross-border tax evasion and harmful tax competition. The amending directive (DAC 3, 2015/2376 Council Directive) included conditional tax assessment for cross-border transactions and APA decisions (transfer price determinations) within the scope of automatic exchange of information. (Eur-lex 2020e)

The following amendment (Council Directive 2016/881, DAC 4) was justified by the aggressive tax planning practices of multinational companies, which adversely affected domestic small and medium-sized enterprises. To remedy this, the DAC 4 Directive required a mandatory automatic exchange of information on the structure and transfer pricing information. The report shall include information and data on the income, profits, taxes paid and the number of employees of multinational companies. (Eur-lex 2020f)

The purpose of the last amendment to the Administrative Cooperation Directive is to to provide Member State tax authorities with access to money laundering regulatory information. It allows including the verification that financial institutions are appropriate whether they comply with the due diligence obligation and the related reporting. Access to money laundering information for the tax authorities become available regarding the identity of the beneficial owner information. The Member States shall apply the relevant rules by 31 December 2017 they had to accept. (Varga, 2019)

A significant change in the Hungarian tax rules is the implementation of the provisions of information and automatic exchange of information on cross-border tax planning transactions under the European Union DAC6 Directive, as well as the detailed procedural rules for dispute settlement procedures under tax conventions. It will be detailed as follows (Varga, 2019):

- the institution of the complaint and the decision on it;
- the mutual consultation procedure;
- details of interactions and conflicts with national procedures;
- the rules for initiating dispute settlement itself;
- the establishment, operation and procedure of the advisory committee;
- cost and decision;
- subject to the agreement of the competent authorities of the member states, the possibility of setting up an advisory committee.

Despite the standardized procedures and the uniform data format, the resulting data cannot be used without further human intervention. The data from the source tax authority must first be decrypted and clarified. In order to make the data usable, the Hungarian receiving authority has a number of tasks to do, besides automated procedures, the preparation of the data for use may require significant manual intervention. If this is not possible without the assistance of the authority of the sending State, the foreign authority should be contacted to clarify the inaccuracies. The data obtained will then be used by the tax authorities. An important question for Hungarian taxpayers is how the tax authorities use the data prepared in the framework of the automatic exchange of information prepared as described above. (Varga, 2019) For a summary of introducing DAC in Hungary see Table 44.

Table 44: Introducing DAC in Hungary

Data	Legalisation	Period
Interest, employment, senior management, pension, real estate, insurance	DAC	2016-
Inancial account information	DAC2	2016-
Conditional tax assessment, preliminary price determination	DAC3	2012-
Country reports	DAC4	2016-
Money laundering data	DAC5	2018-
Automatic exchange of information	DAC6	2019-

Source: own elaboration based on Varga (2019).

6.10 PROBLEMATIC ISSUES AND RELATED CASE-LAW

6.10.1 PROBLEMATIC ISSUES

Hungarian rules in transfer pricing are strict and consistent and require documentation for each tax year. Serious sanctions are imposed on the taxpayer due to faulty preparation or non-production. In terms of control, a high-level auditing system filters out the risky business to be controlled based on anomalies and internal contradictions

One can distinguish five main types of typical problems regarding transfer price:

1. Definition of the associated person;
2. Reporting obligation;
3. The obligation of corporate tax base adjustment;
4. Transfer price reporting obligation;
5. CbCR.

Regarding to the **definition of the associated person** the main problem is that the indirect association is not considered. The second type of this category if that the ownership shares are examined instead of votes or votes of individual members (domestic partner and children, parents, siblings) are not summarized. Common problem is that no relationship is established (or needless established) on executive identity or close family members are also considered. Often not only the same executives but also the members of the management establish a relationship Other type of problems is that municipality and its business association do not apply transfer pricing rules and are not considered to be related parties

The international groups of companies may have no information about the ultimate parent company and the percentage of major influence differ by countries (50%, 25%). It may cause difficulties fort companies managing the transfer pricing documentation when a business is associated under one country's rule and not in another

Regarding to the **reporting obligation** there are lot frequent mistakes. The associated company must be notified to the tax authorities, but only when the contract is first concluded. The penalty could be 500 thousand HUF / partner. Also the end of the affiliation must be reported. The penalty could be 500 thousand HUF / partner too. The CbCR requires to report to the tax authority the final parent company, or who is required to report. Failing this obligation may couse a penalty of 20 million HUF. Freqent mistake is that The CbCR is often missing because they do not know the ultimate parent company or they are not able to reportthere is no announcement. The report may missing due to negligence or only one of the associated companies reports or false stated association.

There may be double taxation. For example, a foreign parent company is associated with 25%, its tax authority has raised the tax base, the Hungarian party cannot deduct it because it is not affiliated. If the taxpayer accounted for the 50 million HUF transaction value limit in invoiced value and did not examine the value of the transaction at transfer price. On this basis, it was wrong to conclude that the transaction was less than 50 million HUF, and it was not necessary to register the transaction.

Regarding to the **obligation of corporate tax base adjustment** it is a common mistake,that anyone who is not required to keep a transfer price record does not take into account the tax base adjustment obligation, as the company does not think the rule applies.The tax base correction may incompatible with the transfer pricing documentation and the corporate tax return. The taxpayer did not set up a tax base adjustment in his tax declaration, although according to the register there was less tax base due to the difference between the applied price and the transfer price. Therefore, the corporate tax base should be increased by a certain amount - this is reflected in the transfer price register.Other type of mistakes is that the free transactions were not taken into account by taxpayers. The taxpayer has given a guarantee for the credit of his affiliated company. Unfortunately, the affiliated company did not pay the loan, which resulted that the taxpayer should have been paid, but its transfer price register did not include the transaction.

It can lead to double taxation if, for example, a Hungarian and foreign group members have been contracted at transfer price for years, but this is overruled by the foreign tax authority and increases the tax base outside. Hungarians cannot reduce it because they have been considering the price as a TP for years, possibly in their audited records.

Regarding to the **transfer price reporting obligation** it is a frequent mistake that the tax base recorded in the transfer pricing documents does not match the tax return. The order of the used methods may not correct. There are methodological disputes because the database cannot be verified or reconstructed, the taxpayer also averages his profitability for 3 years, the sample does not contain the returns at least 3 years of profitability or the losses are not excluded from the sample or function analysis is not acceptable or is not in line with real risk. For a domestic database, it is even more difficult to find at least 10 sample elements.

By international database, country characteristics, price levels, efficiency, etc. are different and they were not unadjusted for analysis.

It is failure that in the comparative sample, the profitability of the companies accounting under IFRS was compared without any adjustment.

The most significant failure in **the CbCR documentation** is that without the knowledge of the final parent company, the Hungarian is unable to describe the group, and it is not certain whether the group reaches the threshold and becomes obligated to CBCR. A joint document is not always prepared by the parent company and may contain very incomplete information. Mostly, the Hungarian subsidiaries have no insight into intangible assets, R&D. There is typically no final parent company in Hungary, as it has a turnover of over 750 million Euro, only few companies reach the threshold (OTP, MOL). There are typically subsidiaries.

Hungarian companies typically report to the final parent company. Pay attention to the announcement (see above).

6.10.2 CASE LAW

According to Article 25 of the Fundamental Law, the "Curia" is the supreme court of Hungary. The Supreme Court shall ensure the unity of the courts' application of law and its decisions on the unity of law shall be binding on the courts. Act CLXI of 2011. on the Organization and Administration of Courts describe the tasks of the Supreme Court of Hungary:

a) consider, in cases specified by law, the appeal lodged against the decision of the Tribunal and of the ruling panel,
b) consider the application for review,
c) make a binding uniformity decision for the courts,
d) carry out case-law analysis of cases which have been finally disposed of, including the examination and examination of the case-law of the courts,
e)publishes court judgments and decisions in principle,
f) decide on the contravention and annulment of the local government decree,
g) decide on the failure of the local government to fulfil its statutory legislative obligation,
h) acts on other matters within its competence.

The issue of transfer pricing may depend on the underlying factual situation and maybe purely legal. The subject matter of the proceedings is not the rating of the underlying legal relationships, but the determination of the remuneration for the legal relationships closest to the parameters of the given transaction. In this chapter, we present some of the decisions of the Curia regarding transfer pricing.

1. case (Decision of the Curia No. Kfv. I. 35.774/2014)

"The applicant is involved in the distribution of trademark rights. He obtained the rights to use the trademark rights from his affiliated companies and also passed them on to his affiliated company. For the purpose of determining the consideration, only one company had a transfer price record. According to this, the basis for this was the actual turnover achieved. By contrast, the value of the user charges payable by the applicant was fixed, since the value of the charges was fixed at the beginning of the business year, after which it could not be adjusted.

The tax authorities examined the nature of the prices charged between the parties and found that they were not the normal market price and, accordingly, determined the consideration for the trademark rights payable by applying a weighted average cost of capital to the net profit margin. In the 2006 business case, this rate was set at an interest rate of 12% applied at the group level. On that basis, he reduced the amount of the trademark acquisition, thereby increasing the corporate tax base by HUF 209,357,000 for the period April 8, 2005, and February 28, 2006, and consequently charged the corporation tax liability of HUF 33,497,000. It explained that, in addition to its own market risk, the applicant, in addition to its own market risk, also assumed the market risk of the companies holding the right to use the trademark, owing to its position as purchaser and license fee.

By judgment of the Court of First Instance, the defendant annulled the defendant's decision in excess of the default judgment, including the decision of the court of the first instance, and ordered the court of the first instance to reconsider. On the basis of the forensic evidence obtained by the court and of the applicant's submissions, the WACC indicator was not appropriate for determining the level of profit margin. It agreed with the defendant that it had opted for a so-called "normal market price". The Net Profit Based Transaction Method (TNMM) was appropriate, but the WACC was not applied. He stressed that the WACC indicator is not suitable for measuring the company's market profit, measuring short-term one-year returns. It also stated, on the basis of private expert opinion, that the transfer price is a price range, not a specific abstract price, thus there is no specific price from which to deviate. In its view, it is necessary to present a price range against which the adequacy of the applicant's calculation and, consequently, the correctness of the tax return data should be examined. The defendant has applied for a review of the final judgment by the annulment of the final judgment and new judgment, requiring the defendant to act in the new proceeding on the basis of the opinion of a forensic expert and to apply the profit margin established therein. He also contested the classification of the transfer of trademark rights as a capital reserve.

According to the decision of the Curia, the development of the Corporate Tax Act it is the responsibility of the defendant to apply the calculation based on the net profit margin of the transaction referred to in Article 18 (2) (d). This cannot be delegated to the court by ordering, following the opinion of a forensic expert obtained by it, to follow and apply the new procedure. This follows from Section. XX. of the Act, which provides that in administrative proceedings the court is to rule on the lawfulness of the decision contested by the action." (Decision of the Curia Nr. Kfv. I. 35.774/2014)

2. case (Decision of the Curia No. Kfv. I. 35.550/2018/12)

"The Group used the cash pool method for providing liquidity. At the end of each month, the balance of the group members' short-term positions is transferred to the long-term position between the parent company and the member company. The plaintiff acted as an intermediary between the members and the Parent Company, and partly deposited and received funds in the parent company's main account. The applicant classified each transaction as a 'deposit' in the transfer price register and, in applying the transfer pricing rules, taking account of the current account deposit rates. The Parent Company is not a credit institution and is not entitled to collect deposits. The transactions between the applicant and the Parent Company correspond to this, and the transfer price must be compared with the interest rate of the loans granted. The tax authority imposed a tax differential on the applicant because of the application of a lower than normal market rate. Due to the effect of other tax changes on the pre-tax profit, the defendant reversed the decision at first instance and otherwise upheld it. The Court of First Instance considered that it was a purely legal matter that had to be decided. The applicant is not allowed to collect deposits due to its rules, the claimant may receive interest on the loan instead of the deposit, and the normal market price must be determined accordingly. It, therefore, dismissed the action.

The Curia, acting on the applicant's application for review, assumed that the issue of transfer pricing could be a specialized matter and a purely legal question, depending on the underlying facts. In the litigation, the defendant transformed the decision into a legal issue by basing it on the Hpt. However, when determining the normal market price, the issue is not to determine the underlying legal relationship, but rather to determine *the counter value applied to the legal relationship closest to the parameters of the transaction. In this case, it cannot be decisive whether or not the Parent has the right to raise funds."* (Decision of the Curia Nr. Kfv. I. 35.550/2018/12)

3. case (Decision of the Curia No. Kfv. VI. 35.585/2017)

"The tax office of the first instance carried out an ex-post audit of various tax types with the applicant in the trade-in cereals and seeds. In its decision, the tax authority of the second instance emphasized that in each case the economic substance of the given transaction and the purpose to be achieved by the transaction are relevant. In contrast, clearing transactions are not settled by the delivery of the subject of the transaction and the payment of the forward price, but by the financial settlement of the difference between the market price of the commodity and the forward price. With regard to the transfer pricing record, it accepted the application of the method chosen by the applicant but stated that the comparison was arbitrary and therefore no normal market price could be established.

The Court of First Instance found the plaintiff's claim to be partly well-founded and ordered the tax authorities to reopen the proceedings. As regards the options, it noted that, according to the expert opinion obtained in the litigation, the applicant had correctly applied passive accruals and had correctly booked the transactions under consideration as clearing transactions. With regard to the transfer pricing records, it was noted, in the light of the expert opinion obtained in the litigation, that neither the method of resale applied by the applicant nor that of the defendant nor the classification of the transactions was correct.

Following requests for review by the defendant and the plaintiff, the Court of First Instance partially set aside the judgment of the Court of First Instance and ordered the Court of First Instance to reopen the proceedings and to give a new decision. With regard to futures contracts, he emphasized that the Court of First Instance did not rule on the issue of whether the transactions were clearing or delivery. It is not excluded that the examination of the facts necessary for deciding a particular point of law may require particular expertise, but the legal nature of the transactions cannot be inferred from the findings of expert and other experts. The legal valuation of legal transactions, based on accounting standards and actual implementation, is a legal issue from which the expert may decide on the applicability of accruals as a professional issue. With regard to the transfer pricing record, the Curia pointed out that the Court of First Instance did not take into account the fact that the defendant had accepted the method used by the plaintiff and did not challenge it in the plaintiff's application. However, the expert seconded by the court changed the method used by the applicant and accepted by the defendant and drew his professional conclusions from that new method. This was not evaluated by the court and therefore provided guidelines for the repeat procedure which were unenforceable.

Concerning the reopened procedure, among other things, the Curia stipulated that, in the case of futures contracts, the first step was to determine whether they were correctly classified by the authority as delivery transactions. The method used by the applicant for recording the transfer price must be based on expert judgment." (Decision of the Curia No. Kfv. VI. 35.585/2017)

6.11 SUMMARY OF FINDINGS

The issue of the Hungarian transfer pricing is mainly investigated by practising experts, and a scientific examination is rarely undertaken. It is important to mention that transfer pricing can be examined from both a legal and an economic perspective. From a legal point of view it is the regulations and compliance with international directives, as well as the presentation of specific cases (Nagy and Földi, 2017; Szabóné Veres, 2014) that are the primary concerns. From an economic perspective, on the one hand, there is the approach of the tax expert, the application of the rules, and the examination of whether a company is subject to the documentation obligation or what penalties it faces (Kerényi, 2011; Berényi 2016; Berényi, 2017). On the other hand, there is the management approach for investigating documentation, the structure of the group and management processes. (Szabóné Veres, 2014)

Transfer pricing can also be examined from the perspective of the tax authorities (the experiences of tax audits), from the point of view of tax advisors (raising the awareness of the topic, providing information, advertising services) and more broadly as a complex issue (the legal, tax and management aspects).

There is no international outlook or comparison in Hungarian transfer pricing studies yet. The legal approach and the description of the regulations are the more frequently discussed topics. Szabóné (2014) conducted comprehensive research and evaluation of transfer pricing from the management approach in her doctoral thesis (Szabóné, 2014).

Hungarian tax regulations follow international standards, as does general law. EU directives and OECD regulations are implemented into the legal regulations. Therefore, it can be said that Hungarian transfer pricing regulations are in line with international standards. The current regulations follow EU and international standards, for example, the full text of the Hungarian double taxation treaties is identical to Article 9 of the OECD Model Convention (OECD, 2017b), 43 of the 82 conventions are contained in both documents.

Hungarian transfer pricing regulations impose obligations on businesses as companies have to register themselves whether they have associated persons. According to OECD regulations (Hungary also has three levels of obligations, preparing a CbCR, a Master File and a Local File for those obliged to submit documentation). It is a peculiarity of Hungary that only a few companies (e.g. MOL) have to produce a CbCR since most companies do not exceed the EUR 750 million threshold. In the case of the Master File and Local File, it is important to recognize who is required to produce documentation. This is often difficult, as businesses are not aware of the task (Berényi, 2017) or do not consider the document important enough (Szabóné, 2014). It can also be beneficial for management if they are aware of the structure and business processes of the company group. The obligation to keep records of transfer prices, as well as documentation on comparative prices, is also a crucial point. In addition, the transfer price is included as a tax base adjustment item in the corporate tax return.

There are several exceptions in Hungary, for example, SMEs do not have to keep a transfer price register, and the transaction-by-transaction exemption can be applied, as long as these do not each exceed HUF 50 million.

In many cases, businesses are not aware of their obligations due to a lack of knowledge of the rules and a lack of clarity about the affiliated relationship. For this reason, it is useful that there are many professional articles about the obligation, as these serve the purpose of raising awareness. However, studies focus on the documentation obligation and regulatory requirements, and there is a lack of empirical analysis or scientific articles providing higher added value.

There are five main problematic issues of transfer pricing in the business approach:

a) the definition of an associated person,
b) the documentation obligation,
c) the tax base adjustment obligation,
d) the transfer price recording obligation, and
e) CbCR related issues.

Further to the corporate approach, tax experts may have problems with changing regulations, the lack of Hungarian-language OECD Guidelines, and the lack of awareness among entrepreneurs.

From the point of view of the tax authorities, a taxpayer's lack of preparedness and incomplete registers can be problematic issues. Transfer pricing documentation does not have to be submitted to the tax office like tax returns. This gives the tax office less information and less data that can be used to produce statistics.

From a researcher's point of view, it is also a problem that transfer pricing documents are considered to be business secrets and are not part of other mandatory disclosures such as the annual report. Consequently, opportunities for analysis are also limited. In conclusion, one can say that in Hungary it is difficult to investigate the issue of transfer pricing empirically due to a lack of data, business secrets and confidential tax office information. At the same time, it can be said that the Hungarian Tax Office publishes news and updates on transfer pricing audits on its website, and we can also find legal cases on the website of the Curia. A further direction for research could be to consider investigation of companies' attitudes towards transfer pricing, as in Szabóné's (2014) questionnaire-based research, with the focus on new domestic or international regulations.

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ANNEX

Table 45: Overview of all double tax treaties signed by Hungary according to Article 9 category

Country	EU country	OECD country	Promgulated	Type of DTT according to the rules as embodied under Article 9		
				CAT I	CAT II	CAT III
Albania	NO	NO	Act XCI of 1996		X	
Armenia	NO	NO	Act X of 2010		X	
Australia	NO	YES	Act XXXVI of 1993			X
Austria	YES	YES	Decree-Law 2 of 1976	X		
Azerbaijan	NO	NO	Act LXXXIX of 2008		X	
Bahrein	NO	NO	Act XLIX of 2014		X	
Belarus	NO	NO	Act CXII of 2004		X	
Belgium	YES	YES	Cabinet Council Decree 20 (18 April) of 1984	X		
Bosnia and Herzegovina	NO	NO	Decree-Law 6 of 1988	X		
Brazil	NO	NO	Act XXVII of 1992	X		
Bulgaria	YES	NO	Act XCII of 1996		X	
Canada	NO	YES	Act XVI of 1995			X
China	NO	NO	Act XV of 1999	X		
Croatia	YES	NO	Act XVIII of 2000		X	
Cyprus	YES	NO	Cabinet Council Decree 82 (29 December) of 1982	X		
Czech Republic	YES	YES	Act XCIII of 1996	X		
Denmark	YES	YES	Act LXXXIII of 2011		X	
Egypt	NO	NO	Act XVII of 1995		X	
Estonia	YES	YES	Act CXXVIII of 2004		X	
Finland	YES	YES	Cabinet Council Decree 66 (16 December) of 1981	X		
France	YES	YES	Cabinet Council Decree 65 (16 December) of 1981	X		
Georgia	NO	NO	Act XIV of 2012		X	
Germany	YES	YES	Act LXXXIV of 2011		X	
Greece	NO	YES	Cabinet Council Decree 33 (1 July) of 1985	X		
Hong Kong	NO	NO	Act CXXIX of 2010		X	
Iceland	NO	YES	Act CXLV of 2005		X	
India	NO	NO	Act CXLIV of 2005		X	
Indonesia	NO	NO	Act X of 1999	X		
Ireland	YES	YES	Act XI of 1999	X		

Country	EU country	OECD country	Promgulated	Type of DTT according to the rules as embodied under Article 9		
				CAT I	CAT II	CAT III
Iran	NO	NO	Act IV of 2016			X
Israel	NO	YES	Act LXIII of 1993	X		
Italy	YES	YES	Cabinet Council Decree 53 (22 December) of 1980	X		
Japan	NO	YES	Decree-Law 18 of 1980	X		
Kazakhstan	NO	NO	Act XIV of 1999		X	
Kosovo	NO	NO	Act CLXXXVII of 2013		X	
Kuwait	NO	NO	Act XVI of 1999		X	
Latvia	YES	YES	Act CXXX of 2004		X	
Liechtenstein	YES	NO	Act CL of 2015		X	
Lithuania	YES	YES	Act CXXIX of 2004		X	
Luxemburg	YES	YES	Act XCI of 2015		X	
Macedonia	NO	NO	Act XXXV of 2002		X	
Malaysia	NO	NO	Act LX of 1993	X		
Malta	YES	NO	Act LXVII of 1993			X
Mexico	NO	YES	Act CXLV of 2011		X	
Moldova	NO	NO	Act XVIII of 1999	X		
Mongolia	NO	NO	Act LXXXII of 2000		X	
Montenegro	NO	NO	Act XXV of 2003	X		
Morocco	NO	NO	Act VIII of 2002	X		
Norway	NO	YES	Cabinet Council Decree 67 (16 December) of 1981	X		
Northern Ireland (UK)	YES	NO	Act CXLIV. Of 2011.		X	
Oman	NO	NO	Act. CLXXVII. Of 2016.		X	
Pakistan	NO	NO	Act II of 1996		X	
Philippines	NO	NO	Act XVII of 2000		X	
Poland	YES	YES	Act XCV of 1996	X		
Portugal	YES	YES	Act XIX of 2000		X	
Qatar	NO	NO	Act XV of 2012		X	
Romania	YES	NO	Act XCIX of 1996	X		
Russian Federation	NO	NO	Act XXI of 1999	X		
San Marino	NO	NO	Act CXXXII of 2010		X	
Saudi Arabia	NO	NO	Act LII of 2014		X	
Serbia	NO	NO	Act XXV of 2003	X		
Singapore	NO	NO	Act XXI of 2000	X		
Slovakia	YES	YES	Act C of 1996	X		
Slovenia	YES	YES	Act CXLVI of 2005			X
South Africa	NO	NO	Act VII of 1999		X	
South Korea	NO	YES	Act XXVIII of 1992	X		
Spain	YES	YES	Cabinet Council Decree 12 (10 March) of 1988	X		
Sweden	YES	YES	Cabinet Council Decree 55 (22 October) of 1982		X	
Switzerland	NO	YES	Decree Law 23 of 1982		X	
Taiwan	NO	NO	Act CXXXIII of 2010		X	

Country	EU country	OECD country	Promgulated	Type of DTT according to the rules as embodied under Article 9		
				CAT I	CAT II	CAT III
Thailand	NO	NO	Government Decree 13 (25 July) of 1990	X		
The Netherlands	YES	YES	Cabinet Council Decree 10 (10 March) of 1988			X
Tunisia	NO	NO	Act XXVIII of 1999	X		
Turkey	NO	YES	Act CI of 1996		X	
Turkmenistan	NO	NO	Act. XCVI. Of 2016.		X	
Ukraine	NO	NO	Act XXX of 1999		X	
United Arab Emirates	NO	NO	Act CLXI of 2013		X	
United Kingdom	YES	YES	Act CXLIV of 2011		X	
United States of America*	NO	YES	Act XXII of 2010			
Uruguay	NO	NO	Act XXXI 1999	X		
Uzbekistan	NO	NO	Act XC of 2008		X	
Vietnam	NO	NO	Act CII of 1996	X		

*CAT IV: special contract
Source: own elaboration (based on the list of countries and laws: Acce, Hungarian Taxation Office 2019).

CHAPTER 7
LEGAL REGULATIONS IN POLAND

7.1 SPECIFICATION OF THE SOURCES OF LAW WHICH INCLUDE (OR RELATE TO) TRANSFER PRICING

The basis of the Polish legal system is the continental legal system (based on the tradition of civil law), and contains certain German and French influences (Sozański, 2014). The sources of law in Poland are the Constitution, acts, ratified international agreements and regulations. The Constitution of the Republic of Poland of April 2, 1997 is considered the most important source of Polish law (Constitution of the Republic of Poland, 1997). It contains provisions governing the Polish legal system, organization of institutions, the judicial system and local government bodies. The constitution also regulates citizens' freedoms and rights. The current constitution was adopted in 1997 (Górecki, 2012, p.29). Acts are a source of universally binding law and the subject of their regulations are important issues. The law may regulate every case. In some cases, the constitution provides that the law regulates matters of particular importance, for example, the budget or the legal status of citizens.

Sources of law include two categories, i.e. sources of applicable law and acts of public law.

Pursuant to Article 87 of the Constitution of the Republic of Poland, the sources of universally binding law of the Republic of Poland are as follows:

a) Acts – basic acts in force, adopted by Parliament;
b) Ratified international agreements - acts of international law;
c) Regulations – acts issued by bodies indicated in the Constitution (i.e. the President, Prime Minister, Council of Ministers, ministers);
d) Acts of local law – local government bodies and local government administration bodies, on the basis and within the limits of the authorizations contained in the Act, establish local binding legal acts in the area of operation of these bodies.

Pursuant to the Constitution of the Republic of Poland, the ratification of certain international agreements requires consent expressed in an act adopted by Parliament and signed by the President. This applies to alliances, political or military arrangements, freedoms, citizenship rights and obligations, membership of the Republic of Poland in international organizations and other matters provided for in the constitution.

Regulations are issued by governmental bodies indicated in the Constitution on the basis of the detailed authorization contained in an act. The competence of the Council of Ministers is to issue internal resolutions that are binding only for organizational units subordinate to the institution issuing the resolution. However, resolutions may not be the legal basis for issuing decisions regarding citizens, legal entities or other entities.

Territorial self-government bodies and local government administration bodies may issue local binding acts of law in given administrative districts on the basis of statutory authorization.

The Supreme Court is a body of judicial power, not legislative. Therefore, it is not its duty to legislate, but only to resolve legal issues. A Supreme Court judgment binds other courts only with regard to the case to which it relates. For other courts it is only a guide.

It should be remembered, however, that the lower courts' interpretation of the Supreme Court's interpretation may be later disapproved. It would seem that once the Supreme Court's view is established with regard to a particular case, then in similar cases this court will be consistent in its position.

Therefore, it cannot be concluded that common courts are not sensitive to the case law. Recalling Supreme Court rulings can be of great importance in a case and be a strong argument in a lawsuit or other pleading (Rola, 2009).

Poland does not recognize the automatic primacy of EU law over the Constitution. The Constitutional Tribunal has ruled that EU law can only take precedence over Polish acts of law, only if it is consistent with the Polish Constitution (Kalisz, 2007, p. 20). Practice shows that an important role in disputes and discussions on this subject is played by the rulings of the European Court of Justice (Deneka, 2019).

On November 22, 1996, an instrument of accession to the OECD Convention on the Organisation for Economic Cooperation and Development was signed in Paris by the depositary of the OECD Convention

(OECD, 1960). Thus, Poland became a full 28th member of the organization. Most of the investments in Poland come from OECD countries, therefore respecting the provisions of this document is of significant economic importance to Poland. Poland has also accepted the OECD Guidelines on Transfer Pricing for International Enterprises and Tax Administrations (OECD, 2017a) and the OECD Model Tax Convention (OECD, 2017b). The last reflected in the Double Tax Treaties (abbr. DTTs), which were also signed by Poland.

Due to the fact that Poland became a member of the European Union in 2004, it was obliged to accept the so-called acquis communautaire, i.e. the *acquis communautaire* from the Treaty, under which the European Coal and Steel Community was founded (1951). This obligation also applies to transfer pricing regulations, for example regulations of the EU Joint Transfer Pricing Forum, which deals with transfer pricing issues at the European Union level, as well as the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (Eur-Lex (2019a). The Convention has been binding for Poland since February 1, 2007. All agreements on the avoidance of double taxation concluded by Poland provide for a mutual agreement procedure.

The Polish Ministry of Finance, while conducting legislative work on transfer prices, takes into account the achievements of the OECD and the EU such as:

a) OECD Transfer Pricing Guidelines on transfer pricing for multinational enterprises and tax administrations (OECD, 2017a),
b) The Base Erosion and Profit Shifting program co-implemented by the OECD and the "G20" Group, (OECD, 2015),
c) Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council, of 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union (Council of the European Union, 2006),

According to the Supreme Administrative Court: *"OECD publications and some forms of activity of EU bodies (e.g. EU Joint Transfer Pricing Forum reports) are not universally binding. However, the theses and solutions contained in these documents should be treated by taxpayers and tax (audit) authorities as a set of good practices and a reference point that serves the proper interpretation of tax regulations regulating transfer prices"* (Judgment of the Supreme Administrative Court of 27 April 2012; Judgment of the Supreme Administrative Court of 21 October 2008).

Both OECD Regulations and EU Regulations were implemented into domestic transfer pricing regulations. These are mostly covered by tax regulations, particularly by the act of February 5, 1992 on Corporate Income Tax (Act on CIT) and the act of July 26, 1991 on Personal Income Tax (Act on PIT). The issue of transfer pricing is regulated there in Chapter 1a of the Act on CIT and in Chapter 4b of the Act on PIT. Chapter 1a of the Act on CIT, entitled "Transfer prices", contains the following subsections:

1. General provisions (articles 11 a and 11 b);
2. Arms' length principle (from article 11 c to 11 j);
3. Transfer Pricing Documentation (from article 11 k to 11 t).

The implementing regulations to the acts on taxes are presented in Table 46.

Table 46: Regulations to the acts on taxes in Poland

Regulations to the Act on Corporate Income Tax	Regulations to the Act on Personal Income Tax
Regulation of the Minister of Finance of December 21, 2018 on transfer pricing in the area of corporate income tax (Journal of Laws 2018 item 2491)	Regulation of the Minister of Finance of December 21, 2018 on transfer pricing in the area of personal income tax (Journal of Laws 2018 item 2502)
Regulation of the Minister of Finance of 21 December 2018 on the manner and procedure for eliminating double taxation in the event of adjustment of affiliates' profits in the scope of corporate income tax (Journal of Laws 2018 item 2474) (valid until 29.11.2019)	Regulation of the Minister of Finance of December 21, 2018 on the manner and procedure for eliminating double taxation in the event of adjustment of affiliates' profits in the scope of personal income tax (Journal of Laws 2018 item 2499) (valid until 29.11.2019)

Regulations to the Act on Corporate Income Tax	**Regulations to the Act on Personal Income Tax**
Regulation of the Minister of Finance of December 21, 2018 regarding information on transfer prices in the scope of corporate income tax (TP-R CIT) (Journal of Laws 2018 item 2487)	Regulation of the Minister of Finance of December 21, 2018 regarding information on transfer prices in the area of personal income tax (TP-R PIT) (Journal of Laws 2018 item 2515)
Regulation of the Minister of Finance of December 21, 2018 regarding transfer pricing documentation in the field of corporate income tax (TPD CIT) (Journal of Laws 2018 item 2479)	Regulation of the Minister of Finance of December 21, 2018 regarding transfer pricing documentation regarding personal income tax (TPD PIT) (Journal of Laws 2018 item 2509)
Announcement of the Minister of Finance of December 21, 2018 regarding the announcement of the type of base interest rate and margin for the purposes of transfer prices in the field of personal income tax and corporate income tax (M.P. 2018 item 1286)	
Regulation on the Minister of Finance of March 28, 2019, on determining countries and territories that apply harmful tax competition for the purposes of corporate income tax (Journal of Laws 2019, Item 600)	
Ordinance of the Minister of Finance of July 2, 2018 on specifying the template for a simplified corporate income tax report (CIT-TP) Journal of Laws 2018, item 1300 Valid until the end of 2018	Ordinance of the Minister of Finance of July 2, 2018 on specifying the template for a simplified personal income tax report (PIT-TP) (Journal of Laws 2018 item 1301) Valid until the end of 2018
Regulation of the Minister of Development and Finance of September 12, 2017 regarding information contained in tax documentation in the field of corporate income tax (Journal of Laws 2017 item 1753) Valid until the end of 2018	Regulation of the Minister of Development and Finance of September 12, 2017 regarding information contained in tax documentation in the field of personal income tax (TPD PIT) Journal of Laws 2017 item 1752 Valid until the end of 2018
Regulation of the Minister of Finance of 10 September 2009 on the manner and procedure for determining corporate income tax by way of estimation and the manner and procedure for eliminating double taxation of corporate income in the event of adjustment of profits of related entities (Journal of Laws 2014. item 1186) Valid until the end of 2018	Regulation of the Minister of Finance of 10 September 2009 on the manner and procedure for determining personal income tax by way of estimation and the manner and procedure for eliminating double taxation of personal income in the event of adjustment of profits of related entities (Journal of Laws 2014 item 1176) Valid until the end of 2018
Regulation of the Minister of Finance of 10.10.1997 on the method and procedure for determining taxpayers' income by estimating prices in transactions made by these taxpayers (Journal of Laws Nr 128, item 833) Valid until the end of 2009	
Regulation of the Minister of Finance of April 9, 2013 on determining countries and territories that apply harmful tax competition for the purposes of corporate income tax (Journal of Laws 2013, item 494). Valid until 29.03.2019	

Source: own elaboration.

Procedural tax law in Poland is contained in the Act of 29 August 1997 - Tax Ordinance (2017) together with the Act of 9 March 2017 on the exchange of tax information with other countries (Act on tax exchange, 2017). Important legal regulations are also included in the Act of October 16, 2019 on the settlement of disputes regarding double taxation and the conclusion of advanced price arrangements (Act on APA, 2019).

Moreover, from 2019 in Poland, the Penal Fiscal Code is also applicable to the issue of transfer pricing, in the context of criminal consequences for non-compliance of transactions with the arm's length principle (Penal Fiscal Code, 1999).

7.2 DEFINITION OF KEY TERMS IN DOMESTIC LAW

7.2.1 DEFINITION OF ASSOCIATED PERSONS IN DOMESTIC LAW

The definitions of associations in Polish domestic law have changed in recent years. Until the end of 2018, the definition was included in art. 11. par. 1 of the Act on CIT with the following wording:

"If a natural person, a legal person or an organizational unit without legal personality, residing, headquarters or management in the territory of the Republic of Poland (or outside the territory of the Republic of Poland), (...)

participates directly or indirectly in the management or control of another enterprise or has share in the capital of these enterprises. Holding a share in the capital of another entity means a situation in which the entity directly or indirectly holds in the capital of another entity a share of not less than 5%."

The threshold of 5% has changed from the beginning of 2017 to 25%. Moreover, according to art. 11 par. 6 of the Act on CIT and art. 25 par. 6 of the Act on PIT, family relationships are recognized as follows: marriage, kinship or second-degree affinity.

In the currently binding version of the Act on CIT, Chapter 1 General regulations Art.11a. par.1, related entities are defined as:

"a) the entities from which one entity has significant influence over at least one other entity, or
b) entities which are significantly influenced by:
- *the same other entity or*
- *a spouse, relative or relative to the second degree of a natural person who has significant influence over at least one entity, or*

c) a company without legal personality and its partners, or
d) the taxpayer and his foreign establishment, and in the case of a tax company group - a capital company that is part of it and its foreign establishment".

According to the Act on CIT, Article 11a. Par. 2 exerting significant influence is understood as:

"1. owning directly or indirectly at least 25%:
a) equity interests or
b) voting rights in controlling, constituting or managing bodies, or
c) shares or rights to participate in profits or assets or their expectation, including units and investment certificates, or
2. the actual ability of a natural person to influence the taking of key economic decisions by a legal person or an organizational unit without legal personality, or
3. remaining married or having a relationship or affinity to the second degree"

In turn, having an indirect share or right means (Act on CIT, Art. 11a.par. 3):

"a situation in which one entity holds a share or right in another entity through another entity or more entities, the amount of indirectly held share or right corresponds to:

1. *the size of the share or right joining any two entities among all entities taken into account when determining indirect ownership of the share or right - if all the shares or rights connecting these entities are equal;*
2. *the lowest share size or right connecting entities between which the amount of indirectly held share or right is determined - if the size of shares or rights connecting these entities are different;*
3. *the sum of indirectly held shares or rights - in cases where entities between which the indirectly held share or right is determined, combines more than one indirectly held share or right."*

An additional situation when entities are considered to be associated according to the Polish legislator is the case when there are relations between entities that are not established or maintained for justified economic reasons, including those aimed at manipulating the ownership structure or creating circular ownership structures (Act on CIT, art. 11a. Par. 4).

The consequence of the status of a related party is special treatment by tax authorities, specified as: in the case when the tax authority considers that in comparable circumstances unrelated entities with economic rationality would not have entered into a given controlled transaction or would have entered into another transaction, or would have carried out another activity, hereinafter referred to as the "relevant transaction", this authority determines the taxpayer's income (loss) without taking into account the controlled transaction, and when justified, determines the taxpayer's income (loss) from the transaction relevant to the controlled transaction (Act on CIT, art. 11c par. 4)

7.2.2 DEFINITION OF TRANSFER PRICING AND BASIC PRINCIPLES IN DOMESTIC LAW

There was no definition of transfer price in Polish regulations until the year 2019. The definition of transactional price existed instead in the Act of Tax Ordinance, as the price established in transactions among related entities (Tax Ordinance, 1997, art. 23 par. 10).

Nowadays, the definition is included in the Act on CIT (art. 11a. Par. 1) and reads:

"the financial result of the conditions established or imposed as a result of existing relationships, including price, remuneration, financial result or financial indicator".

Other legal acts, e.g. the Act of Tax Ordinance, refer to the above definition.

7.3 LEGAL REGULATIONS INCLUDED IN DOUBLE TAX TREATIES

7.3.1 DEFINITION OF ASSOCIATED PERSONS IN DDTS CONCLUDED BY POLAND

A crucial part of the definition of associated persons as specified by the OECD is included in Art. 9 of the OECD Model Convention (OECD, 2017b):

"a) An enterprise of a Contracting State that participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State and

b) The same persons that participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State".

The above-mentioned definition is reflected in 90 agreements on the avoidance of double taxation concluded by Poland. The list of double tax treaties concluded by Poland is attached in this chapter´s Annex.

In the currently binding version of the Act on CIT, Chapter 1 General regulations Art.11a. par.1, related entities are defined more broadly as:

"a) the entities from which one entity has significant influence over at least one other entity, or

b) entities which are significantly influenced by:

- *the same other entity or*
- *a spouse, relative or relative to the second degree of a natural person who has significant influence over at least one entity, or*

c) a company without legal personality and its partners, or

d) the taxpayer and his foreign establishment, and in the case of a tax company group - a capital company that is part of it and its foreign establishment".

Significant influence is further explained in Article 11a. Par. 2 of the Act on CIT.

Comparing the abovementioned definitions, one may conclude that the definition of associated party as treated by double tax treaties is more general than that included in the Polish provisions.

7.3.2 EXISTING PLATFORMS OF THE WORDING OF ART. 9 IN DDTS

In Poland, as part of international tax cooperation, double taxation conventions and agreements on the exchange of information in tax issues apply. The basis of double taxation conventions is the OECD Model Convention on the avoidance of double taxation in the field of taxes on income and property (OECD, 2017b).

In addition, other multilateral laws are also binding, such as:

- The Multilateral Convention implementing Treaty Tax Law measures aimed at preventing the erosion of the tax base and the transfer of profit, concluded in Paris on November 24, 2016, signed in Paris on June 7, 2017 (OECD, 2016),
- The Convention on mutual administrative assistance in tax matters, concluded in Strasbourg on January 25, 1988 (Council of the European Union, 1988).

Poland is party to 90 agreements on the avoidance of double taxation (Ministry of Finance, 2019). The list of double tax treaties concluded by Poland is attached in Annex 1.

The overview of the signed double tax treaties according to the three categories[86] is shown in the following Table 47. The most common are the double tax treaties in the second category.

86 The first category contains only the definition of associated persons in paragraphs 1 and 2. The second category also contains, apart from category 1, the procedure of the contracting states in the case that one contracting state makes an adjustment to tax base in accordance with

Table 47: Overview of double tax treaties signed by Poland according to Article 9 category Regulations to the acts on taxes in Poland

Category	EU Member State	Non-EU Member State
I	12	7
II	19	13
III	12	6
Totally	27	63
MLI Convention	12	12

Source: own elaboration based on Ministry of Finance (2019).

Moreover, in Poland, the following legal acts are also in force:

- The Act of 14 April 2000 on international agreements,
- The regulation the Council of Ministers of August 28, 2000 on the implementation of certain provisions of the act on international agreements,
- The Act of 9 March 2017 on the exchange of tax information with other countries (Act on tax exchange, 2017).

With the available appeal tools for double taxation in Poland, it will be possible to use the procedure for settling disputes regarding double taxation between member states of the European Union - which is a procedure for resolving disputes within the EU, introduced on the basis of the provisions of Council of the European Union of 10 October 2017 on tax dispute resolution mechanisms in the European Union (Council of the European Union, 2017).

It should be noted that on September 11, 2019, the Polish Parliament held the first reading of the Government draft Act on the Settlement of disputes regarding double taxation and the conclusion of advanced price arrangements.The Act sets out, inter alia, the method and procedure for conducting cases aimed at resolution of double taxation disputes (Act on APA, 2019). There are three important chapters in the act regarding double taxation: "Settlement of double tax disputes between Member States of the European Union", "Procedure for eliminating double taxation in the case of adjusting the profit of related entities" and "Mutual communication procedure based on avoidance agreements for double taxation". With the entry into force of the Act on APA, certain regulations ceased to apply, such as the Regulation of the Minister of Finance of December 21, 2018 on the manner and procedure for eliminating double taxation in the event of adjustment of affiliates' profits in the scope of corporate income tax, and the appropriate act in the scope of personal tax.

7.4 TRANSFER PRICING REGULATIONS – SELECTED ISSUES

7.4.1 THE ARM'S LENGTH PRINCIPLE

The arm's length principle is nowadays included in separate subsection 2 of Chapter 1 of the Act on CIT (art. 11c. par. 1 to 11c. par. 5) and provides the right of the tax authority to determine the taxable income if it recognizes a violation of the arm's length principle. The wording of the arm's length principle is consistent with the definition included in par. 1 of art. 9 of the OECD Model Tax Convention (OECD, 2017b) and point b of chapter 1 of the OECD Transfer Pricing Guidelines (OECD, 2017a):

"1. Related entities are obliged to set transfer prices on terms that unrelated entities would set among themselves.

2. If, as a result of existing connections, conditions are set or imposed which differ from those that would be agreed between unrelated entities, and as a result the taxpayer shows a lower income (higher loss) than would be expected if the said connections did not exist, the tax authority determines the taxpayer's income (loss) without taking into account the conditions arising from these connections."

From 2019, thanks to being included directly in the Act and not in the Regulation, as it was before, the importance of the following finding increased:

its domestic legal regulation (the so-called mirror procedure). The third category contains double tax treaties which also contain the anti-abuse clause against the application of paragraphs 1 and 2 of Article 9 (Based on chapter 8.3.2)

"When determining the amount of income (loss), the tax authority uses the method adopted by the related entity, unless the use of another method is more appropriate in the circumstances". Art. 11 d of the Act on CIT contains methods for verification of transfer prices in accordance with OECD methods and allows for a sixth method if it is not possible to apply the widely recognized methods.

Subsection 2 also includes adjustment regulations, confirming that the taxpayer can make adjustments to transfer prices under certain specified conditions by changing the amount of revenues obtained or the costs of obtaining revenues. Exemplary conditions are as follows (Act on CIT, art. 11e):

"1. in controlled transactions carried out by the taxpayer during the tax year, conditions were established that would be determined by unrelated entities;
2. there has been a change in significant circumstances affecting the conditions determined during the tax year or the costs actually incurred or revenues obtained being the basis for the calculation of the transfer price are known, and ensuring their compliance with the conditions that would be determined by unrelated entities requires an adjustment of transfer prices;
3. at the time of making the adjustment, the taxpayer has a statement by a related entity that the entity has made a transfer price adjustment in the same amount as the taxpayer;
4. a related entity referred to in point 3 has its place of residence, registered office or management in the territory of the Republic of Poland or in a country or territory with which the Republic of Poland has concluded a double taxation agreement and there is a legal basis for exchanging tax information with this country;
5. the taxpayer will confirm the transfer price adjustment in the annual tax return for the tax year to which the correction relates."

Additionally, when the taxpayer's income is recognized by the tax administration of another country as the income of a related entity having its place of residence, registered office or management outside the territory of the Republic of Poland and included in the taxable income of that entity, the taxpayer's income is adjusted if the provisions of relevant international agreements, to which the Republic of Poland is a party, provide for such a correction (Act on CIT art. 11h). The adjustment of income described above serves to eliminate double taxation by specifying the taxpayer's income that would be obtained by the taxpayer if the conditions agreed with the related entity having their place of residence, registered office or management outside the territory of the Republic of Poland corresponded to the conditions that would be agreed between unrelated entities.

Poland has introduced "safe harbours" into its legal system for certain specific transactions. For example, in the case of controlled transactions constituting services with low added value, the tax authority refrains from determining the taxpayer's income (loss) in terms of the mark-up on the costs of these services, if all of the following conditions are met (Act on CIT, art. 11f par. 1):

"1. the mark-up on the costs of these services was determined using the method referred to in art. 11d paragraph 1 point 3 or 4, and amounts to:
a) no more than 5% of costs - in the case of purchasing services,
b) not less than 5% of costs - in the case of the provision of services;
2. the service provider is not an entity having a place of residence, registered office or management in a territory or country applying harmful tax competition;
3. the recipient has a calculation covering the following information:
a) the type and amount of costs included in the calculation,
b) the method of application and justification for the selection of allocation keys for all related entities using the services."

It should be emphasized that low value-added services are listed in the Annex to the Act on CIT and should have the following features (Act on CIT, art. 11f par. 2):

"1. they are supporting the recipient's business activity;
2. they are not the main subject of activity of a group of related entities;
3. the value of these services provided by the service provider to unrelated entities does not exceed 2% of the value of these services provided to related and unrelated entities;
4. are not subject to further resale by the customer, with the exception of resale of services purchased in his own name, but for another related entity (re-invoicing)."

There is also “safe harbour” for loan transactions, which means that the tax authority refrains from determining the taxpayer’s income (loss) in terms of the interest rate on this loan if the following conditions are met (Act on CIT, art. 11g):

“1. the interest rate on the loan as at the date of the contract is determined based on the type of base interest rate and margin specified in the announcement of the minister competent for public finance as at the date of the contract87;
2. no payments other than interest related to the granting or servicing of the loan, including commissions or bonuses, are foreseen;
3. the loan was granted for a period not longer than 5 years;
4. during the financial year, the total level of liabilities or receivables of a related entity under the capital of loans with related entities calculated separately for loans granted and contracted is not more than PLN 20,000,000 or the equivalent of this amount;
5. the lender is not an entity with a place of residence, registered office or management in a territory or country applying harmful tax competition.
6. The loan amounts expressed in foreign currency are converted into PLN according to the average exchange rate announced by the National Bank of Poland in force on the last business day preceding the day of payment of the loan amount.”

The above-mentioned provisions shall apply accordingly to loans and bond issues. When calculating loans, a taxpayer may apply a margin above the base interest rate (or actually a margin above the base rate) set out in the Minister of Finance’s notice published at least annually, and when the conditions set out in the provisions are met. For example, for 2019, a 2% margin and base interest rates were determined depending on the loan currency (e.g. WIBOR 3M for a loan in PLN, LIBOR USD 3M, - for a loan in US dollars) (Announcement of the Minister of Finance, 2018).

7.4.2 TRANSFER PRICING METHODS

In Poland, according to the Act on CIT (art. 11d), transfer prices are verified using the most appropriate method in the circumstances, selected from the following methods:

1. comparable uncontrolled price;
2. resale price;
3. cost plus;
4. transactional net margin method;
5. distribution of profit.

From 2019, an additional possible method was added:

“If it is not possible to apply the methods referred to in paragraph 1, another method shall be used, including valuation techniques, most appropriate in the given circumstances.”

It should be noted that for the legislator, the selection of the most appropriate method in the given circumstances shall take into account, in particular, the conditions that have been established or imposed between related parties, the availability of information necessary for the correct application of the method and the specific criteria for its use.

Detailed regulations concerning acceptable transfer pricing verification methods are included in Chapter 3 of the Regulation of the Minister of Finance of December 21, 2018 on transfer pricing in the area of corporate income tax (Regulation of MF, 2018a), but these are also consistent with the OECD Transfer Pricing Guidelines (OECD, 2017a).

For example, the method of comparable uncontrolled price consists of comparing the price of the subject of a controlled transaction with the price used in comparable transactions by unrelated entities and determining on this basis of the market value of the subject of the controlled transaction. The comparisons

87 The minister competent for public finance shall announce, at least once a year, by way of a notice, in the Official Journal of the Republic of Poland "Monitor Polski", the type of base interest rate and the margin referred to in para. 1 point 1, taking into account the types of base interest rates used on the interbank financial market

shall be made on the basis of prices used by the given entity on a comparable market with unrelated entities (internal price comparison), or on the basis of prices used in comparable transactions by unrelated entities (external price comparison) (Regulation of MF, 2018a, par. 10).

The resale price method involves calculating the purchase price of a good or service from a related entity by reducing the sale price of that good or service to an unrelated entity by a resale price margin. The resale price margin should ensure that the reseller covers its direct and indirect costs related to the resale of the subject of the controlled transaction, and ensure a profit adequate to the functions performed by that entity, the assets involved and the risk incurred. The market value of the resale price margin is determined by reference to the level of the margin that the related entity applies in comparable transactions with unrelated entities, or the margin used in comparable transactions by unrelated entities (Regulation of MF, 2018a, par. 11).

The cost plus method consists of determining the price of the subject of a controlled transaction at the level of the sum of the cost base and the profit mark-up calculated in relation to the cost base. The cost base is the sum of costs directly related or the sum of costs directly or indirectly related to the production of the subject of the controlled purchase. The market value of the profit mark-up in relation to a specific cost base is determined by reference to the level of the mark-up of profit that the same entity uses in comparable transactions with unrelated entities in relation to the same cost base, or the mark-up of profit used in comparable transactions by unrelated entities in relation to a comparable cost base (Regulation of MF, 2018a, par. 12).

The profit distribution method consists of determining the total profit that related entities have achieved in connection with a given controlled transaction and the distribution of this profit among those entities in a proportion in which such unbundled entities would make this division, in particular taking into account the parties' controlled transaction functions, assets involved and risks incurred. The distribution of profit referred to in para. 1 shall be made by specifying the revenues obtained by each of the related entities and the costs incurred related to a given controlled transaction. In the event that the costs so determined exceed the associated sum of revenues, the loss shall be apportioned (Regulation of MF, 2018a, par. 13). The distribution of the profit shall be carried out by means of:

1. residual analysis or
2. participation analysis.

It is worth noting the difference in the definition of the "transactional net margin method"", in force since 2019, compared to the previous definition. According to the current definition (Regulation of MF, 2018a, par. 14):

"The transactional net margin method involves determining a financial indicator that reflects the relation of the net profit margin that a related entity obtains in a controlled transaction to the appropriate base. The net profit margin shall be determined by deducting from the revenue generated as a result of a controlled transaction the costs associated with the implementation of this transaction. If, for the purposes of calculating the net profit margin, it is justified to take into account costs that cannot be directly assigned to a given transaction, the allocation of such costs is done by using an allocation key that rationally reflects the process of creating value in a controlled transaction in the best way possible. The base may in particular constitute revenues, costs, assets or elements of revenues, costs or assets. Choosing the appropriate financial indicator referred to in para. 1 shall be made taking into account the specifics of the industry and the material circumstances of the transaction. The market value of the financial indicator shall be determined by reference to the level of the financial indicator:

1. *which the entity obtains in comparable transactions with unrelated entities in relation to the same base or*
2. *obtained in comparable transactions by unrelated entities in relation to a comparable base, or*
1. *obtained by entities conducting activities comparable to the scope of the transaction being tested in relation to a comparable base."*

According to the previous definition, the transactional net margin method involved examining the net profit margin that an entity obtains in transactions with another related entity, and determining it at the level of the margin that the same entity obtains in transactions with independent entities, or the margin obtained in comparable transactions by independent entities. The transactional net margin was determined by deducting from the income generated as a result of the transaction the costs incurred to achieve this income, including overheads.

Referring to the newly introduced sixth method, in accordance with regulations it should be used as follows (Regulation of MF, 2018a. par. 15):

"1. where the application of the valuation technique requires that the analysis is based on forecasts – the forecasts prepared for financial planning are used first;
2. the values or indicators used in the valuation technique should correspond to the market value;
3. in the case in which the correct application of the valuation technique requires the use of a discounting factor:
a) the choice of the discounting factor takes into account the way in which the measured subject of the controlled transaction generates cash flows,
b) the amount of the discounting factor takes into account the level of related party's business risk and the level of fluctuations in future cash flows generated by the valued object of the controlled transaction;
4. the analysis takes into account the level of value of the subject of the controlled transaction expected by each party to the controlled transaction."

An example of the sixth method can be the valuation techniques of independent experts, e.g. on the real estate market. Calculation of remuneration based on stock exchange quotations for basic products in the oil and gas processing industry is another example of using the sixth method. Although such valuations have been used by taxpayers for many years, until 31 January 2018 taxpayers were not certain that such valuations would be accepted by tax authorities.

7.4.3 COMPARABILITY ANALYSIS/COMPLIANCE ANALYSIS OBLIGATION

The obligation to conduct comparability analysis has existed in Poland since 2017. Regulations were introduced for entities whose revenues exceeded EUR 10,000,000 in the financial year. From 2019, all entities obliged to prepare transfer pricing documentation should include the results of a comparability analysis.

According to the Act on CIT (art. 11r), the comparative and compliance analysis shall be updated at least every 3 years, unless a change in the economic environment that significantly affects the analysis justifies an update in the year of the change.

Much attention is devoted to the analysis of comparability in Chapter 2 of the Regulation of the Minister of Finance of December 21, 2018 on transfer pricing in the area of corporate income tax, called a "comparability study" (Regulation of MF, 2018a). In particular, regulations include comparability criteria such as (Regulation of MF, 2018a, par. 3):

"1. characteristics of goods, services or other benefits,
2. the course of the transaction, including the functions performed by entities in the compared transactions, the assets they engage and the risks they take, taking into account the ability of the parties to the transaction to perform a given function and to bear the risk,
3. the terms of the transaction specified in the contract, agreement or other evidence documenting these conditions,
4. economic conditions occurring at the time and place where the transaction took place,
5. economic strategy - to the extent that these criteria have or may have a material effect on the conditions set or imposed between related parties".

Specific regulations concerning comparability analysis of intangibles are presented in point 7.5.1 of this study.

According to the Regulation of the Minister of Finance, a comparability study involves the following stages (Regulation of MF, 2018a, par. 4):

"1. specification of the period that should be included in the study;
2. analysis of information about the related entity and its economic environment;
3. analysis of all the circumstances of the audited controlled transaction that may have a significant impact on the level of the transfer price, taking into account the functions performed, assets involved

and risks incurred, and, when the application of the most appropriate method requires it, the choice of the audited entity;

4. *verification whether there are internal comparative data that can be used for the purposes of comparability testing;*
5. *identification of available external sources of comparative data;*
6. *selection of the most appropriate method and financial indicator, if the analysis of the financial indicator is necessary for the correct application of the most appropriate method;*
7. *analysis of available comparative data, in particular in terms of their comparability with the transaction tested;*
8. *making comparability adjustments if they are necessary to obtain a higher level of comparability of comparative data for the controlled transaction;*
9. *calculation of the results of the comparability test and their interpretation."*

It should be noted that widely available comparability data is used to conduct comparability testing based on external data, and when conducting comparability testing, comparative information, its source, method of acquisition and any other information used for this purpose are disclosed.

When assessing the comparability of transactions, only those differences between compared transactions or entities that have a significant effect on the level of the transfer price, determined using the most appropriate method in a controlled transaction, shall be taken into account. Comparable transactions can be considered in which none of the possible differences between the compared transactions or entities could significantly affect the price of the subject of such a comparable transaction, or reasonably accurate comparability adjustments can be made to eliminate the significant effects of such differences.

Some regulations are very detailed, such as the one below (Regulation of MF, 2018a, par. 9 p. 2):

"If, as a result of controlled transactions, a related entity shows lower income in one financial year than would be expected if the terms were agreed between unrelated entities, and in a three-year period covering that financial year, it shows as a result of controlled transactions higher income than would be expected if the conditions were established between unrelated entities, determining the amount of income (loss) of the taxpayer by estimation, the tax authority takes into account the fact that lower income obtained in one financial year is offset by higher income from this three-year period."

Despite the fact that comparability analysis is described so broadly in Polish regulations, the requirements give rise to taxpayers' misunderstandings and questions. This is one of the reasons why the Minister of Finance appointed the Transfer Pricing Forum, operated by the Ministry of Finance (The Ordinance of MF, 2018). The aim of the Forum is to prepare recommendations, opinions, analyses, and proposals regarding the simplification and sealing of the operation of the tax system in the field of transfer pricing. The works are carried out in the form of working groups appointed for the elaboration of a chosen problem. Preparation of descriptions of compliance of transaction conditions established with related entities compared to conditions that would be established between independent entities and the technical aspects of preparing comparative analyses, are the fields of interest of one of such working groups

Tax explanations, in terms of the technical aspects of comparability analysis and descriptions of compliance were published by the Ministry of Finance in June 2019, based on the results of the Transfer Pricing Forum. The explanations relate to the legal status until December 31, 2018.

The document includes issues such as (Forum cen transferowych, 2019):

- comparability of data and their locality,
- possibility of using internal data,
- possibility of using offer data,
- the legitimacy of using secret comparables,
- the justification for rejecting comparative data due to extreme sample values, (including entities operating at a loss),
- minimal sample size in comparative data analysis,
- update of comparative data analysis.

Tax documentation is considered by the legislator as the basic source of evidence containing information enabling assessment of whether the remuneration in a transaction concluded between related entities has been set at market level. It should be noted that the documentary obligation did not shift the burden of proof onto the taxpayer. In administrative proceedings, including tax proceedings, the administrative body is the authority, which shows that the burden of proof of facts lies with the administrative body and cannot be passed on to the taxpayer. However, the party is entitled to provide the necessary evidence. (Jamroży, 2018).

7.5 TRANSFER PRICING DOCUMENTATION

7.5.1 GENERAL REGULATIONS

Subsection 3 of chapter 1a of the Act on CIT is focused on the obligation of providing transfer pricing documentation, which has existed in Poland since 2001.

In Poland, related parties are required to prepare local transfer pricing documentation for the financial year to demonstrate that transfer prices have been set on terms that unrelated entities would agree upon (Act on CIT, art 11.k). The duty to inform the Tax Office of the existence of tax transfer pricing documentation rests with the Management Board, together with a statement that the transfer prices of controlled transactions covered by local transfer pricing documentation are set on terms that unrelated entities would establish between themselves (Act on CIT, art 11.k, art. 11m).

A three-level hierarchy of transfer pricing documentation has been adopted in Poland since 2017: local file, master file and country-by-county report.

Local transfer pricing documentation is prepared for a homogeneous controlled transaction whose value, minus value added tax, exceeds the following documentation thresholds in the financial year (Act on CIT, art. 11.l):

1. PLN 10,000,000 - in the case of commodity transactions;
2. PLN 10,000,000 - in the case of a financial transaction;
3. PLN 2,000,000 - in the case of a service transaction;
4. PLN 2,000,000 - in the case of a transaction other than those specified in points 1-3.

The local file thresholds have undergone changes, presented in Table 48.

Table 48: "Local file" transfer pricing documentation thresholds

Until the end of 2016	The end of 2018
1. EUR 100,000 - if the value of the transaction does not exceed 20% of the share capital, or 2. EUR 30,000 - in the case of the provision of services, sale or provision of intangible assets, or 3. EUR 50.000 - in other cases.	Related entities whose revenues or expenses exceeded the equivalent of EUR 2,000,000 in the year preceding the tax year and which carried out transactions with related entities in the tax year that had a significant impact on their income (losses): 1) EUR 2,000,000, but not more than the equivalent of EUR 20,000,000 - threshold of EUR 50,000 increased by EUR 5,000 for each EUR 1,000,000 of revenue over EUR 2,000,000; 2) EUR 20,000,000, but not more than the equivalent of EUR 100,000,000 - a threshold of EUR 140,000 increased by EUR 45,000 for every EUR 10,000,000 in revenue above EUR 20,000,000; 3) EUR 100,000,000 - threshold of EUR 500,000

Source: own elaboration based on the Act on CIT previously in force.

What is more, taxpayers are also required to prepare local transfer pricing documentation (Act on CIT, art. 11.o):

"1. making, directly or indirectly, payment of receivables to the entity residing, having its seat or management in a territory or country applying harmful tax competition, if the total amount resulting from the contract or actually paid in the financial year, or the total amount of benefits due this year exceeds PLN 100,000 or its equivalent, or

2. concluding with an entity having a place of residence, seat or management in a territory or country applying harmful tax competition:

a) the articles of association of a company which is not a legal person, if the total value of contributions made by the partners exceeds PLN 100,000 or the equivalent, or

b) *a joint venture agreement or other agreement of a similar nature, in which the value of the jointly implemented undertaking specified in the agreement, and in the event that the value is not specified in the agreement, expected at the date of conclusion of the agreement, exceeds PLN 100,000 or the equivalent".*

The deadline for preparing the "local file" documentation is by 30 September after the end of the tax year. Previously, the deadline date for 2017 and 2018 was until March 31 after the end of the tax year, but this was prolonged by the Minister of Finance until the 30 September after the end of the tax year. Until the end of 2016, there was no such deadline included in the regulations. The only deadline obligation was for submission of documentation within 7 days at the request of the tax authority. The obligation is still binding (Act on CIT, art. 11s).

If there is a probability of the value of a controlled transaction being undervalued, the tax authority may request a taxpayer who is not obliged to have transfer pricing documentation to submit such documentation within 30 days (Act on CIT, art. 11 s).

Related entities that are consolidated using the full or proportional method and which are obliged to prepare local transfer pricing documentation, attach to this documentation the group transfer pricing documentation (master file) prepared for the financial year by the end of the twelfth month after the end of the financial year, if they belong to a group of related entities (Act on CIT, art. 11p):

"1. *for which the consolidated financial statements are prepared;*
2. *whose consolidated revenues exceeded PLN 200,000,000 or its equivalent in the previous financial year.*
3. *The amounts of revenues referred to in para. 1 point 2, expressed in a foreign currency, is converted into PLN at the average exchange rate announced by the National Bank of Poland in force on the last business day of the reporting financial year preceding the financial year to which the group transfer pricing documentation applies.*
4. *Group transfer pricing documentation may be prepared by an associated entity obliged to attach group transfer pricing documentation or another entity belonging to the group of related entities. The preparation of group transfer pricing documentation by another entity from the group of related entities does not release from liability for compliance of this documentation with Article 11q section 2.*
5. *If the group transfer price documentation has been prepared in English, the tax authority may request that, within 30 days from the date of delivery of that request, the group transfer price documentation be prepared in Polish."*

7.5.2 EXEMPTIONS FROM TRANSFER PRICING DOCUMENTATION

There are some exemptions from the obligation to draw up local transfer pricing documentation, in particular for transactions that are (Act on CIT, art. 11n):

"1. *concluded only by related entities having their place of residence, registered office or management in the territory of the Republic of Poland in the tax year in which each of these related entities jointly meets the following conditions:*
a) *does not benefit from the exemption referred to in art. 6*
b) *does not benefit from the exemption referred to in art. 17 clause 1 points 34 and 34a,*
c) *has not incurred a tax loss;*
2. *covered by the decision on the agreement referred to in art. 20a of the Tax Code, during the period covered by this decision (APA);*
3. *whose total value does not permanently constitute income or a tax-deductible cost, except for financial transactions, capital transactions and transactions regarding investments, fixed assets or intangible assets;*
4. *between companies forming a tax company group;*
5. *where the relations result exclusively from the relation with the State Treasury or local government units or their associations;*
6. *in which the price was determined by means of an open tender pursuant to the Act of 29 January 2004 – Public Procurement Law (Journal of Laws of 2018, item 1986);*
7. *implemented between a group of agricultural producers entered in the register referred to in art. 9 item 1 of the Act of 15 September 2000 on agricultural producer groups and their associations, and on the*

amendment of other acts (Journal of Laws of 2018, item 1026), and its members regarding the sale of a fee:

a) for a group of producers of agricultural products or groups of products produced on the holdings of members of such a group,

b) by a group of agricultural producers for the benefit of its members, of goods used by a member for the production of products or groups of products referred to in point a, and the provision of services related to this production".

7.5.3 DEFINITION OF HOMOGENEOUS TRANSACTION

In addition to specifying documentary thresholds, the regulation provides guidance on identifying a homogeneous transaction. When assessing whether a controlled transaction is homogeneous, the uniformity of the controlled transaction in economic terms, the comparability criteria and the methods of transfer pricing verification should principally be taken into account, (Act on CIT, art. 11 k). The value of the controlled transaction corresponds to (Act on CIT, Art. 11l):

"1. capital value - loan and credit case;
2. face value - in the case of bond issue;
3. guarantee sum - in the case of a surety or guarantee;
4. the value of assigned revenues or costs - in the case of assigning income (loss) to a foreign plant;
5. the correct value for a given controlled transaction - in the case of other transactions."

To determine the value of a controlled transaction, account should be taken of:

1. invoices received or issued for a given financial year, or
2. contracts or other documents - if an invoice has not been issued or in the case of financial transactions, or
3. payments received or forwarded - if it is not possible to determine this value pursuant to points 1 and 2.

7.5.4 CONTENT OF TRANSFER PRICING DOCUMENTATION

Part of the regulations regarding the content of "local file" documentation are included in the Act of CIT (art. 11q. 1) and says that the documentation should contain:

"1. a description of the related entity;
2. transaction description, including analysis of functions, risks and assets;
3. transfer pricing analysis, including:
a) analysis of the data of unrelated entities or transactions concluded with unrelated entities or between unrelated entities considered comparable to the conditions established in controlled transactions, hereinafter referred to as "comparative analysis", or
b) an analysis showing compliance of the conditions under which the controlled transaction was concluded with the conditions that would be determined by unrelated entities, hereinafter referred to as "compliance analysis" when a comparative analysis is not appropriate in the light of a given method of transfer pricing verification or due diligence is not possible;
4. financial information."

Regarding transfer pricing documentation, the Regulation of the Minister of Finance of December 21, 2018 regarding transfer pricing documentation in the field of corporate income tax is of particular importance because it contains the meaning of the requirements described more broadly (Regulation of MF, 2018b).

For example, as part of the above-mentioned "description of the related entity", the following should be included (Regulation of MF, 2018b, par.2):

a) description of the management structure and organizational chart of the related entity,
b) a description of the related entity's principal activities, including:
   - indication of the subject of the business,
   - indication of the geographic markets in which the related entity operates,

- description of the industry and market environment in which the related entity operates, with an indication impact of economic and regulatory conditions and indication of key competitors,
- description of the economic strategy,
- information on economically significant functions, assets or risks affecting the related entity that were transferred in the financial year and in the year preceding the financial year, if such a transfer occurred;

In the "transaction description", the taxpayer should present:

a) the subject and type of controlled transaction,
b) information on related entities participating in the execution of the controlled transaction containing:
   - the name and seat or place of management,
   - the tax identification number, and in the absence of a tax identification number, together with the identification its type,
   - indication of the subject of the principal activity,
   - the type of relationships between these entities,
c) functional analysis of the related entities participating in making the controlled transaction, including significant changes compared to the previous financial year, including the description of:
   - functions performed,
   - risks incurred, including the ability to bear them,
   - assets involved,
d) method of transfer price calculation, together with the adopted assumptions,
e) the value of the controlled transaction determined in accordance with Article 11l paragraph 2 of the Act, divided among contractors,
f) payments received or transferred related to a controlled transaction, including mutual deduction debts,
g) agreements, intra-group agreements or other documents regarding a controlled transaction,
h) tax arrangements or interpretations regarding controlled transactions, including prior pricing arrangements concluded with tax administrations of countries other than the Republic of Poland or issued by these administrations.

In the field of "transfer pricing analysis" the following should be included:

a) an indication of the method used to verify the transfer price, along with a concise justification for the choice,
b) an indication of the party or transaction being investigated as part of the transfer pricing analysis, if this is evident from the method indicated in accordance with point a), together with the justification for the choice,
c) a description of the comparative analysis referred to in Art. 11q section 1 point 3 of the Act, carried out with the use of the method indicated in accordance with point a), containing:
   - description of the data search and selection process and indication of the sources of such data, together with the justification for the selection,
   - search criteria and significant assumptions made for the purposes of the analysis,
   - comparative data presented in electronic form enabling its editing, grouping and sorting, and verifying of the calculations made, including financial ratios accepted and rejected as part of this analysis together with their description, relating to transactions concluded by a related entity with an unrelated entity (internal data) or concluded between unrelated entities (external data), if available,
   - justification of the reasons for accepting data from many years or one year for this analysis,
   - justification for the choice of financial indicator used for this analysis, if used,
   - description of the comparability adjustment, including justification, if used,
   - an indication of the point or range determined as a result of this analysis, together with a description of statistical measures, if used,

d) description of the compliance analysis if a description of the comparative analysis is not prepared, with indication, in accordance with point a), the method constituting the valuation technique. The description should include: :
   - justification for the selection of the valuation technique used,
   - description of the data sources used for the valuation,
   - description and justification of the assumptions adopted for the valuation, in particular the assumptions used in the indicators of the valuation, and a description of how these indicators are calculated,
   - description and justification of assumptions made for forecasts, description of the source of data used and indication of the purpose of the forecast - if the application of the valuation technique requires the use of forecast,
   - sensitivity analysis indicating the impact of changes in individual assumptions on the valuation result,
   - justification of the adopted point from the value range of the subject of the controlled transaction,

e) reference of the transfer price to the result of the analyses referred to in Art. 11q section 1 point 3 of the Act, together with justification deviations, if any.

As part of "financial information", the taxpayer should disclose:

a) the approved financial statement for the financial year, prepared on the basis of accounting regulations,
b) a description enabling the mapping of financial data regarding the controlled transaction into items on the financial statement referred to in point a, or to other information contained therein

Master file documentation, according to the Act on CIT, (Art.11q. par.2), should contain the following elements for company groups within the meaning of art. 3 clause 1 point 44 of the Act on Accounting:

1. a description of the group;
2. a description of the material intangible assets of the group;
3. a description of significant financial transactions of the group;
4. financial and tax information about the group.

As with the local file, more details about the master file are contained in par. 3 of the Regulation of the Minister of Finance of December 21, 2018 regarding transfer pricing documentation in the field of corporate income tax ((Regulation of MF, 2018b).

For example, in reference to "description of the group", the following should be disclosed:

a) a description or diagram of the ownership structure of the company group, including the name and registered office or place of management entities included in it,
b) a description of the subject and scope of activities carried out by the company group, including:
   - a description of the most important factors determining the competitive advantage and development opportunities of the group,
   - a description or value chain diagram of the five most relevant product groups in terms of revenue or services, and such groups of products or services, the revenues of which constitute over 5% of consolidated revenues of the company group, together with an indication of the main geographical markets for these groups of products or services,
   - a specification and brief description of significant agreements or arrangements concluded between related entities of a company group in the field of services other than research and development services, including in particular a description of the ability of major service providers to provide significant intra-group services and information on the group's transfer pricing policy regarding the allocation of service costs intra-group and pricing policies for these services,
   - a brief description of the functional analysis demonstrating the significant involvement of related parties in creating value within the company group, including significant functions performed by these related entities, significant risks incurred by them and significant assets involved,

– information on significant restructuring transactions and transactions related to ownership changes, including takeovers, mergers and liquidations carried out in the reporting financial year for the company group.

In the scope of "description of significant intangible assets" of the company group, the master file should contain:

a) a general description of the company group's strategy in terms of creation, development, ownership and use of value of intangible assets and legal entities, together with information about the location of significant research and development centres, and the location of centres managing research and development functions,
b) a list of intangible assets or groups thereof significant from the point of view of transfer prices, together with an indication of the entities holding legal titles to these intangibles
c) a list of significant agreements or arrangements concluded between related entities of the company group concerning intangible assets, including cost sharing contracts, work contracts, and research and development and license agreements,
d) a description of the company group transfer pricing policy in the area of research and development and intangibles e) a general description of significant changes in the control and ownership of intangible assets and use of these values, together with an indication of the entities involved, their registered office or place of management and amounts paid due to such changes in remuneration or compensation.

By "information on significant financial transactions", the legislator understands:

a) a general description of the method of financing the operations of the company group, including information on significant contracts regarding financing concluded with unrelated entities,
b) an indication of the entities performing central financing functions within the company group and their registered office and place of effective management,
c) a general description of the transfer pricing policy for financing between related parties.

In the scope of the company group's financial and tax information, the following should be attached to the master file:

a) the annual consolidated report of the company group,
b) a list and brief description of unilateral prior agreements concluded by related entities of the company group on pricing or other tax interpretations regarding the allocation of income between countries.

The country-by-country reporting mechanism has been developed as part of the OECD Action Plan on Counteracting Tax Base Erosion and Profit Shifting (OECD, 2015).

The country-by-country report, considered by some as a third level of documentation, is actually part of the information on transfer prices submitted in Poland to tax authorities pursuant to the Act of 9 March 2017 on the exchange of tax information with other countries (Act on tax exchange, (2017). Executive regulations to the Act are:

1. Regulation of the Minister of Development and Finance of June 13, 2017 regarding the detailed scope of data provided in the information about the group of entities and how it is to be completed (Regulation of MF, 2017a),
2. Regulation of the Minister of Finance of 14 March 2018 amending the regulation on the detailed scope of data provided in the information about the group of entities and how it is to be completed, Journal of Laws 2018 item 629, (Regulation of MF, 2017b).

According to art. 5. par. 1 of the Act on tax exchange, (2017):

"The competent authority of the Republic of Poland in matters of exchange of tax information with other countries is the Head of the National Tax Administration and in this respect he has the rights of a tax authority".

Section four of the Act contains the rules of "Automatic exchange of information on tax interpretations and decisions on transfer pricing issues" (Act on tax exchange, 2017, art. 76-81), and chapter five of the Act contains regulations on "Automatic exchange of tax information about incoming units in the group of entities" (regulations on Country-by-Country reporting).

It should be noted that art. 82 contains the definition of the "group of entities" to which the reporting obligation to the Head of the National Tax Administration applies. According to this definition, a group of entities means a company group (Act on tax exchange, 2017, art, 82):

"a) for which the consolidated financial statements are prepared in accordance with the accounting policies in force in this group (...)

b) which includes at least two units established or managed in different countries or territories (...)

c) whose consolidated revenues last year exceeded the threshold amount:

1. PLN 3,250,000,000 - if the company group prepares consolidated financial statements in PLN;

2. EUR 750,000,000 or its equivalent, converted according to rules set by the country or territory in which the parent entity has its headquarters or management (...)."

The purpose of art. 82 is that only the highest-level parent company is required to submit the CbCR.

Information about the group of entities (CbCR) should contain (Act on tax exchange, 2017, art. 87. par. 1):

"1. identification data of entities included in the group of entities;

2. information on the amount of revenue generated, realized pre-tax profit (loss), income tax paid, Income tax due, share capital, undistributed profit from previous years, number of employees, tangible assets (fixed assets and current assets) other than cash, and cash equivalents of type of activities of entities included in the group of entities - broken down into countries or territories;

3. additional information or explanations regarding the data or information referred to in points 1 and 2."

7.5.5 SPECIAL CONSIDERATIONS FOR INTANGIBLES

The special measures on transfer pricing of intangible goods in connection with BEPS Action 8 proposed by the OECD include, in particular, guidelines on how to revise the tax assessment of transactions between related enterprises regarding intangible assets. (Jamroży, 2016)

In Poland, some regulations concerning the analysis of comparability of intangibles are included in Chapter 2 of Regulation of the Minister of Finance of December 21, 2018 on transfer pricing in the area of corporate income tax (Regulation of MF, 2018a, par. 3. p. 2).

For controlled transactions involving intangible assets, the comparability test also includes an assessment of the ability of the parties to the transaction to perform a given function and to bear the risk in terms of:

"1. having a legal title to intangible assets, its protection and maintenance;

2. creating intangible assets, including their development;

3. developing intangible assets, including their improvement;

4. the use of intangible assets".

For controlled transactions involving intangible assets that are difficult to measure, the comparability test shall also take into account the assessment of:

1. whether unrelated entities in comparable circumstances:

a) would recalculate the amount of the originally agreed price based on the contractual clause regarding the price change,

b) renegotiate the originally agreed conditions, including the amount of the transaction price,

c) accept contingent payments for settlement of a comparable transaction.

2. whether, when carrying out the transfer price forecast as at the transaction date, all the foreseeable circumstances affecting the amount of the transfer price were taken into account.

If the transfer price of intangible assets has been determined based on information or financial data on future events, including financial forecasts, then in order to assess its market value, it should be assessed whether the information or financial data taken into account in its calculation does not indeed differ from actual data and financial information (Regulation of MF, 2018a, par. 8).

In the case of a discrepancy between the forecast and actual data leading to a difference in the amount of the transfer price of intangible assets amounting to at least 20% of the value of the transfer price calculated based on forecast data, when determining the amount of income (loss) of the taxpayer by estimation, the authority tax is not bound by the restriction under par. 7 p. 1 (*"When determining the taxpayer's income (loss) in a controlled transaction by estimation, the tax authority does not take into account circumstances, including* *comparative data, which could not be known to its parties on the day of its conclusion, and which, if known, could result in determination by the parties of a higher or lower value of the subject of such a transaction")*[88] .

7.5.6 SPECIAL CONSIDERATIONS FOR INTRA-GROUP SERVICES

As regards the valuation of intra-group services, general regulations regarding transfer prices apply. Reporting requirements for transfer pricing include the need to separately disclose intra-group services, in particular production, distribution, research and development services, rental and leasing, and intragroup services, including in particular management fees and joint centre services - accounting, legal, IT, HR (Regulation of MF, 2018c), Taxpayers should also report the level of costs associated with management fees by demonstrating the legitimacy of the costs incurred and the economic benefits achieved.

7.5.7 COST CONTRIBUTION ARRANGEMENTS

Cost Contribution Arrangements (CCAs) are contractual arrangements entered into by permitted parties in order to share the contributions and risks involved in either the development, production or acquisition of intangible or tangible assets, or the execution of services, with the expectation that the parties will enjoy the anticipated benefits to be derived from their contributions equitably (Doonan, Haro de, 2015).

The CCA is defined in point 7.3 of the OECD Transfer Pricing Guidelines (2017a). The amended definition is also included in the Final Report on Actions 8-10 BEPS (OECD, 2015, pp.161-177).

In Poland, legal regulations regarding CCAs were included in Section IIA of the Tax Ordinance (1997) until 28.11.2019, together with provisions regarding APA.

In particular, in accordance with art. 20a par. 2: *"The competent authority for the agreement, at the entity's domestic request, recognizes the comparability of material conditions set out in the contract on the contribution of costs concluded with the related entity or entities with conditions to be agreed between independent entities, including:*

1. *the functional profile of related entities between which was a cost sharing agreement concluded, covering in particular the performed functions, risks incurred and assets involved;*
2. *a cost sharing algorithm;*
3. *other cost sharing rules."*

In addition, art. 20f. par 2 contained the range of conditions that the taxpayer must take into account in the application for CCA:

"1. the cost sharing method chosen;
2. a description of how the proposed method will be applied to subject of the decision on the agreement (...)
3. circumstances that may affect the correct determination of the price transfer, in particular: (...)
a) analysis of the assets, functions and risks of related entities that have been covered by the decision on the agreement,
b) a description of the expected costs and the value of associated contributions with the subject of the application,
c) a description of the economic strategy of related entities,
4. documents having a significant impact on the amount of the transfer price (...),
5. proposed duration of the decision (...),
6. a list of related entities between which the contract on cost sharing was concluded (...)"

7.5.8 TRANSFER PRICING ASPECT OF BUSINESS RESTRUCTURING

Business Restructuring regulations have existed in Polish tax law since 2017. Since that time, taxpayers whose revenues or costs within the meaning of accounting regulations exceed EUR 10 million and have been restructured will be obliged to inform the authority about this fact by ticking the appropriate boxes

88 Except in the case that a controlled transaction involving the transfer of intangible assets that are difficult to measure is covered by the decision on Advanced Pricing Arrangements.

on the CIT-TP form, which is a simplified report on transactions or other events occurring between related entities (Regulation of MF, 2018c) .

Wider restructuring regulations have been in force since 2019. Poland is a country with a detailed, quantitative definition of business restructuring.

It can be found in the Regulation of the Minister of Finance of December 21, 2018 on transfer pricing in the area of corporate income tax (Regulation of MF, 2018a, par. 2):

"Whenever the regulation refers to:

1. *restructuring - it means reorganization:*
   a) *involving a significant change in commercial or financial relations, including the termination of existing contracts or a change in their essential terms, and*
   b) *involving the transfer of functions, assets or risk categories between related entities, if as a result of this transfer the expected average annual financial result of the taxpayer before interest and taxation (EBIT) in the three-year period after the transfer would change by at least 20% of the valid annual average EBIT over the same period were the transfer not carried out."*

There are certain dilemmas concerning the way this 20% of EBIT is counted, and the Ministry of Finance is working on official explanations of the definition.

Detailed requirements comprising comparability analysis in the case of restructuring are included in chapter 4 "Business Restructuring" (Regulation of MF, (2018a).

For example, in the case of restructuring, the comparability test also takes into account the legitimacy of the introduction and the amount of remuneration paid under restructuring.

Moreover, in the case of restructuring, the comparability test shall also include the following stages:

"1. identification of commercial or financial relations between related entities before and after restructuring, including:
   a) *the correct identification of actual transactions constituting the restructuring, in particular by determining the actual functions, risks and assets of related entities before and after restructuring, including the ability of related entities to perform the functions assigned to them as a result of the restructuring of functions, incurring of risks and asset involvement,*
   b) *an analysis of the economic reasons for the restructuring, as well as the benefits expected from the restructuring, in particular synergies,*
   c) *analysis of options realistically available to related parties;*

2. specification of the tax consequences of actual transactions constituting the restructuring;

3. a definition of the extent to which the restructuring resulted in a potential for profit generation being transferred, in particular as a result of the transfer of valuable assets or rights to those assets, including non-material values, the termination or significant renegotiation of existing contracts, or the transfer of an organized part of an enterprise;

4. specification of whether the remuneration for restructuring that is due takes into account the value of the transferred potential to generate profit; if the remuneration is due - determination whether its amount is justified, in particular taking into account:
   a) *revenues and profits that could be expected by the transferring entity if the restructuring did not occur,*
   b) *the obligation to pay compensation under other legal provisions, whereby such compensation is assessed in the light of whether in the given circumstances unrelated entities would agree to such compensation and whether the compensation provided for in other legal provisions is not too high or too low in relation to the damages that unrelated parties would agree on under the circumstances,*
   c) *the relationship between the remuneration for the restructuring and the remuneration of transactions with the acquiring entity expected by the transferee".*

7.6 ADVANCE PRICING AGREEMENTS IN POLISH DOMESTIC LAW

7.6.1 TYPES OF APAS IN DOMESTIC LAW

In Poland, from January 1 2006, provisions entered into force on the conclusion of Advanced Price Arrangements (APA) on the determination of transaction prices.

The body competent for the agreement is the Head of the National Tax Administration. Until 28 November 2019, legal regulations in this respect were included in the Act of 29 August 1997 Tax Ordinance in the Section II a "Agreements regarding transfer pricing" (Tax Ordinance, 1997, art. 20a – 20r).

On November 29 2019, a new Act on APA entered into force: The Act 16 October 2019 on the settlement of disputes regarding double taxation and the conclusion of advanced price arrangements (Act on APA, 2019). Section III includes provisions regarding Advanced Price Arrangements.

The purpose of introducing changes to APA procedures is to adapt and refine them to current practice and to improve them by increasing accessibility for taxpayers. The Act contains rules for issuing advanced pricing agreements (Act on APA, 2019, art. 83 - 102) and rules for verifying the use of prior price agreements (Act on APA, 2019, art. 103 - 106). The Act sets out, inter alia, the scope of the APAs, which should include (Act on APA, 2019, art. 83. Par.2):

"1. Controlled transactions subject to prior price agreement and entities related participating in their implementation;
2. the functional profile of related entities participating in the controlled transaction, including in particular functions performed, risks incurred and assets involved;
3. the method of transfer price verification;
4. the method of transfer price calculation;
5. critical assumptions on the basis of which it was assumed that the method indicated in point 3 accurately reflects the transfer price;
6. the scope of individual information to be indicated in the report on prior price agreement implementation."

Poland has a model of arrangements based on centralization, in which consists of separating the APA procedure from the tax and tax audit procedures at the local level. This model based on centralization ensures that there is a uniform substantive level of persons dealing with APA, that the procedure is unified, and that efforts are made to achieve consistency in the interpretation of regulations and the practice of concluding APAs. There are 3 types of agreement possible:

- unilateral agreements – regarding transactions between domestic related entities,
- bilateral agreements – in which negotiations take place between the competent authorities of the countries in which the entities applying for an agreement are established or operate,
- Multilateral Agreement – covering transactions between related parties from 3 or more countries.

The Head of the National Tax Administration *"at the entity's request, recognizes the comparability of material terms agreed between the domestic entity and its related entity or entities with conditions which independent entities would establish among themselves, and confirms the correctness of transfer pricing method chosen"* (Act on APA, 2019, art. 83 par.1).

This confirmation includes:

1. a functional profile of related entities to which recognized conditions apply, covering in particular functions performed, risks incurred and assets involved;
2. the transfer price calculation algorithm;
3. other rules for applying the transfer pricing method.

Where a controlled transaction has been concluded between a domestic related party and a foreign related entity, the Head of the National Tax Administration, at the request of a national related entity, shall communicate with one competent foreign authority (bilateral agreement) or more than one competent foreign authority (multilateral agreement) (Act on APA, 2019, art. 87). Before submitting the application referred to in art. 84 par. 1, an entity interested in concluding an agreement may contact the authority competent for the agreement to clarify any doubts regarding individual matters related to concluding the agreement, in particular the purposefulness of concluding the agreement, the scope of necessary information, mode and the presumed date of conclusion of the agreement.. It is possible to organize an introductory meeting in the form of a teleconference (Act on APA, 2019, art. 89).

A correctly completed application for an APA pricing agreement should include (Act on APA, 2019, art. 87), art. 90 par.1):

1. a description of how to use the proposed method in relation to the subject of the application, in particular:
a) the transaction price calculation algorithm,
b) financial forecasts on which the transaction price calculation is based,
c) the analysis of comparative data that was used to calculate the transaction price;
2. circumstances that may affect the correct determination of the transaction price, including:
a) conditions established between entities, including a description of the course of transactions between related entities,
b) analysis of the assets, functions and risks of related entities (functional analysis) and a description of the expected costs associated with the transaction,
c) a description of the economic strategy of related entities and other circumstances, if this strategy or circumstances affect the transaction price,
d) data on the economic situation in the industry in which the applicant operates, including data on business operations concluded by unrelated entities that were used to prepare the transaction price calculation,
e) organizational and capital structure of the applicant and related entities, and a description of the financial accounting principles used by those entities;
3. documents having a significant impact on the conditions agreed between related entities, including texts of contracts, agreements and other documents indicating the intentions of related entities;
4. a proposal of the duration of the agreement, together with an indication of whether the application concerns an agreement starting from the date of submission of the application;
5. a list of related entities involved in determining the conditions, together with their written consent to submit to the authority competent for the agreement all documents regarding the subject of the decision on the agreement, and to provide necessary explanations for such decision;
6. a description of the critical assumptions on which the method's ability to accurately reflect transaction prices is based on the market price principle.

The conclusion of an APA in Poland involves the taxpayer paying a fee, the amount of which depends on the type of agreement, and which comes to 1% of the value of the transaction being the subject of the agreement, where (Act on APA, 2019, art. 98, par. 1):

- For a unilateral domestic agreement, the fee is not less than PLN 5,000 and not more than PLN 50,000,
- For a unilateral foreign agreement, the fee is not less than PLN 20,000 and not more than PLN 100,000,
- For a bilateral or multilateral agreement, the fee is not less than PLN 50,000 and not more than PLN 200,000.

The regulations of the Act on APA (2019, art. 97) set deadlines for the end of proceedings in a case agreement:

- unilateral - no later than within 6 months from the date of its initiation,
- bilateral - no later than one year from the date of its initiation,
- multilateral - no later than 18 months from the date of its initiation.

If the proceedings cannot be completed within the statutory deadline, the tax authority notifies the taxpayer thereof, stating the reasons for the default deadline and indicating a new deadline. The APA can be issued for a maximum of 5 calendar years

Table 49 presents data on Advanced Pricing Arrangements concluded so far in Poland.

Table 49: Number of APAs in Poland

Year	Unilateral	Bilateral	Multilateral	Total
2006	1	0	0	1
2007	2	0	0	2
2008	6	0	0	6

Year	Unilateral	Bilateral	Multilateral	Total
2009	2	0	0	2
2010	7	0	0	7
2011	2	2	0	4
2012	5	0	0	5
2013	4	0	0	4
2014	0	0	1	1
2015	5	1	0	6
2016	5	1	0	6
2017	7	4	0	11
2018	6	4	0	10
2019	13	1	1	15
Total	65	13	2	80

Source: Ministry of Finance (2020).

Unilateral agreements are concluded on average within 10 months, while the procedure for concluding bilateral agreements takes on average 29 months. The majority of agreements concluded (61 cases) used the net transaction margin method. In 8 cases, the agreement was based on the method of comparable uncontrolled price, in 5 cases an agreement was made using the cost plus method, and in 6 cases the profit distribution method was used. The Ministry of Finance published information on the types of transactions to which advanced price agreements relate. Transactions on the sale of material goods to Poland and transactions on the sale of material goods to Poland are the most common transactions (31 APA procedures). 10 agreements concerned transactions of services rendered by a domestic entity. The service purchase transaction occurred five times, as did the use of intra-community acquisition of goods by a domestic entity. Business restructuring transactions have followed the APA procedure six times, while the APA procedure has been applied to plant settlements twice. Only once was the procedure used for financial services (Ministry of Finance, 2020).

If the Advanced Price Arrangement is not applied, the Head of the National Tax Administration issues a decision on its expiry (Act on APA, 2019, art. 104) and in the event of a change in the economic relations of the parties to the agreement, the agreement may be amended or repealed (Act on APA, 2019, art. 105). The act specifies the reporting obligation in the form of a report on the implementation of the advanced pricing agreement, which should be submitted by the date of submission of the income tax return to the Head of the National Tax Administration for each tax year covered by the agreement (Act on APA, 2019, art. 106).

7.7 PENALTIES FOR BREAKING THE RULES RELATED TO TRANSFER PRICING

Tax Ordinance includes general provisions about additional tax liability, which amounts to 10% of the sum of the tax loss unduly declared or overstated and not declared in whole or in part of taxable income in the scope resulting from this decision (Tax Ordinance, 1997, Art. 58b par. 1).

The legal act containing penalties for violating the provisions of tax, customs, foreign exchange and gambling laws in Poland is the Act of 10 September 1999 of the Penal Fiscal Code (Penal Fiscal Code, 1999).

A fiscal offence is an act prohibited by the Penal Fiscal Code on pain of either a fine specified in daily rates, restriction of liberty or imprisonment.

When imposing a fine, the court determines the number of rates and the amount of one daily rate, and unless the Code provides otherwise, the lowest number of rates is set at 10 and the highest at 720. the amount of the daily rate may not be less than one thirtieth of the minimum wage[89] or exceed the minimum wage fourfold (Penal Fiscal Code, 1999, Art. 23). When determining the daily rate, the court takes

89 The minimum remuneration is the remuneration for work determined on the basis of the Act of 10 October 2002 on the minimum remuneration for work (Journal of Laws No. 200, item 1679, as amended). In turn, in accordance with the Regulation of the Council of Ministers of September 11, 2018 regarding the amount of the minimum remuneration for work and the minimum hourly rate in 2019 (Journal of Laws of 2018, item 1794), from January 1, 2019 the minimum remuneration for work is PLN 2,250.

into account the perpetrator's income, his personal and family conditions, property relations and earning potential.

The period of imprisonment may last from 5 days to 5 years, unless the Code provides otherwise, and is imposed in days, months and years.

If the amount of receivables depleted, or the value of the object of the act does not exceed five times the amount of the minimum remuneration at the time of its commitment, this is deemed to be a tax offence and it is an act prohibited by the Penal Fiscal Code under the threat of a fine imposed for committing a tax offence within the range of one tenth to twenty times the amount of the minimum remuneration, unless the Code provides otherwise.

The Penal Fiscal Code contains in separate chapters penalties for such types of tax offences and for tax offences such as:

- Chapter 6 Tax offences related to tax obligations and settlements due to subsidies;
- Chapter 7 Tax offences related to customs obligations and rules of foreign trade in goods and services;
- Chapter 8 Tax offences related to foreign exchange trading;
- Chapter 9 Tax offences related to the organization of gambling.

In addition to the above-mentioned penalties for tax offences and fiscal offences, which may also be a consequence of transfer prices, the Penal Fiscal Code contains specific penalties in relation to reporting on transfer prices and the compliance of transactions carried out in accordance with the arm's length principle.

Penalties for the lack of a statement from the Management Board on transfer pricing documentation are specified separately in the Penal Fiscal Code, and penalties for lack of information on transfer prices submitted on the TP-R form are specified separately.

For example, Art. 56 c par. 1 of the Code provides:

"That whoever does not submit a declaration (required under Article 11 m of the CIT Act) on transfer prices, or submits this declaration after the deadline or certifies in it information that is inconsistent with the actual state, is subject to a fine of up to 720 daily rates".

In turn, according to art. 80e § 1 of the Fiscal Penal Code:

"whoever does not submit information on transfer prices (TP-R) referred to in Article 11 t of the CIT Act to the Head of the National Tax Administration, or submits this information after the deadline or submits false information, is subject to a fine of up to 720 daily rates ".

7.8 OTHER OBLIGATIONS RELATED TO TRANSFER PRICING (ADDITIONAL STATEMENTS OBLIGATION)

7.8.1 ADDITIONAL STATEMENTS OBLIGATION

One of the reporting obligations in the scope of the transfer prices of entities who are corporate income tax payers is to include required information in the CIT 8 declaration, constituting a statement on the amount of income achieved by a corporate income tax payer. The taxpayer must among others disclose whether they are required to prepare transfer pricing documentation and a comparability analysis.

Taxpayers to whom the Head of the National Tax Administration issued an advanced pricing agreement (APA), submit a report to the head of the National Tax Administration on the implementation of the advanced pricing agreement for each tax year covered by the previous price agreement, within the time limit appropriate for submitting the annual tax return (Act on APA, 2019, art. 107 par 1).

Since 2017, there have been two additional reporting obligations in Poland in the field of transfer prices. The first obligation applies to providing local tax offices with a statement on the preparation of tax transfer pricing documentation by the end of the ninth month after the end of the financial year. Since 2019, the statement should include the information that "the transfer prices of controlled transactions covered by local transfer pricing documentation are set on terms that would be agreed between unrelated entities" (Act on CIT, Art. 11m par. 1.). The above-mentioned obligation lies with the head of the entity within the meaning of the Accounting Act, which is the Management Board. Each of the persons authorized to represent the entity shall submit and sign a declaration specifying the function they perform, and it is not permissible to make such declaration by proxy. A statement on the preparation of local transfer pricing documentation should be submitted by electronic means in accordance with the provisions of the Tax Ordinance.

The second reporting obligation that has existed since 2017 is information on transfer prices submitted to the Head of the National Tax Administration.

The submission of information about transfer prices to the Head of the National Tax Administration has been obligatory since 2017. For the years 2017 and 2018, corporate income tax payers submitted a CIT TP declaration, and personal income tax payers a PIT TP. This was regulated by 2 executive legal acts:

1. Regulation of the Minister of Finance of July 2, 2018 on the establishment of a simplified model of the report on personal income tax (PIT-TP) Journal of Laws 2018 item 1301.
2. Regulation of the Minister of Finance of July 2, 2018 on the establishment of a simplified model of the corporate income tax report (CIT-TP) Journal of Laws 2018 item 1300.

It should be noted that current reporting obligations have been significantly expanded.

Pursuant to those effective from 1 January 2019, the obligations regarding the reporting of transfer prices were extended by introducing to the Act on CIT that related entities obliged to prepare local transfer pricing documentation - in the scope of controlled transactions covered by this obligation - should provide the Head of the National Tax Administration, by the end of the ninth month after the end of the tax year, by electronic means, information on transfer prices for the tax year, prepared on the basis of an electronic document template included in the Public Information Bulletin on the Ministry of Finance website (art. 11t par. 1).

Information on transfer prices includes (art. 11t par. 2):

1. the purpose of submitting information and the period for which it is submitted;
2. identification data of the entity submitting the information and the entity for which the information is submitted;
3. general financial information on the entity for which the information is submitted;
4. information on related entities and controlled transactions;
5. information on transfer methods and prices;
6. additional information or explanations regarding the data or information referred to in items 2 to 5.

Additional provisions of law on transfer pricing declarations are included in the Regulation of the Minister of Finance of December 21, 2018 regarding information on transfer prices in the scope of corporate income tax, along with an attachment containing explanations as to how to prepare information about transfer prices (Regulation of MF, 2018c). The taxpayer should submit a declaration called TP-R C for corporate income tax, and TP-R P for personal income tax.

Information on transfer prices that is submitted to the Head of the National Tax Administration for the first time in 2019 by 30 September, should first contain information about the purpose of submitting the information (whether the information is submitted for the first time or is a correction) and the tax year to which it relates as well as entity identification data, together with the predominant type of activity.

In addition, the information should include "general financial information on the entity for which information on transfer prices is submitted, including the values of financial indicators measuring the financial situation of that entity" (Regulation of MF, 2018c, par. 2. p.3).

The annex to the above-mentioned regulation contains indicators, the values of which should be provided in information submitted by entities other than banks and insurance companies:

1. operating margin,
2. gross profit margin,
3. return on assets,
4. return on equity.

The taxpayer should also provide information on controlled transactions, assigning them to the individual categories listed in Table 50. The extended version of the table is included in this chapter´s Annex.

Table 50: Codes and categories of controlled transactions in TP-R

Codes and categories of controlled transactions
100x Transactions related to trade in goods - sales 110x Service transactions - sales 120x Financial transactions - sales 130x Asset transactions 130x Real estate 140x Access to intangible assets 150x Other transactions - sales 200x Transactions related to trade in goods - purchase 210x Service transactions - purchase 220x Financial transactions - purchase 230x Asset transactions 240x Use of intangible assets 250x Other transactions - purchase

Source: own elaboration based on Regulation of MF (2018c, par. 2.4a).

It should be emphasized that transactions in intangible assets are subject to clarification by selecting a code corresponding to the type of intangible asset that is the subject of the transaction (Table 51).

Table 51: Codes and Types of intangible assets in TP-R

Codes and Types of intangible assets
DN01 Brand / trademark
DN02 Patent
DN03 Technical or organizational knowledge (know-how) in the field of production
DN04 Technical or organizational knowledge (know-how) other than production
DN05 Franchise (intangible asset package including in particular DN1 and DN3 or DN4)
DN06 Software
DN07 Other intangible assets
DN08 A set of intangible assets for which a uniform common transfer price arrangement has been established

Source: own elaboration based on Regulation of MF (2018c, par. 2.4a).

For each of the controlled transactions, the code of the country of the contractor's seat from the ISO 3166 alpha 2 Country Code classification should be provided as well as information on possible exemptions from the need to prepare tax transfer pricing documentation. In addition, the value of the controlled transaction should also be provided (Regulation of MF, 2018c, par. 2. p. 4b). For specific transactions such as granting or obtaining financing, granting or obtaining guarantees or sureties, or liquidity management this should also include:

- the amount of capital or the amount of the guaranteed or guaranteed liability,
- the actual amount of these controlled transactions,
- the currency of these controlled transactions,
- the amount of interest together with additional commissions or fees, if any, on financing, or the amount of remuneration for providing or obtaining a guarantee or surety.

Another reporting obligation is to provide information on the transfer price verification method from one of the following in Table 52.

Table 52: Codes of transfer price verification methods in TP-R

Codes of transfer price verification methods
MW01 Comparable uncontrolled price method
MW02 Resale price method
MW03 Cost plus method

Codes of transfer price verification methods
MW04 Profit distribution method
MW05 Net transaction margin method
MW06 Another method - independent specialist valuation
MW07 Another method - other

Source: own elaboration based on Regulation of MF (2018c, par. 2.4a).

It should be indicated whether the "safe harbour" mechanism was used, according to the Act on CIT art. 11.f and 11g.

Pursuant to legal regulations, the information should also include the values of the transfer prices used respectively for each of the selected methods. For example, for the method of comparable uncontrolled price, this should detail the value of the minimum price and maximum price used for a given transaction during the year.

In the case of the resale price method, the cost plus method or the net transaction margin method, this should indicate the value of the profitability index used in the transfer price comparability analysis.

A description of the comparability analysis for each of the transactions specified should be presented separately in the information provided. It should include, inter alia, sources of comparative data, how to verify the market price level and a description of the comparability criteria used.

Information reported to Head of the National Tax Administration should also include any possible transfer price adjustments if they took place in the given tax year, along with additional explanations.

7.9 PROBLEMATIC ISSUES AND RELATED CASE-LAW

7.9.1 TRANSFER PRICING CONTROLS

Analysis of the number of completed proceedings regarding transfer pricing in recent years shows that tax and customs authorities are becoming more and more effective.

In the years 2016-2017, the number of inspections carried out in the area of transfer prices increased by 50%, with an almost fourfold increase in the value of estimated taxpayer income as a result of establishing non-market terms in transactions with related entities.

With a comparable number of completed procedures in 2017 and 2018 (239 and 267 respectively), the total value of the cases uncovered increased significantly. The reduction of losses in the area of transfer prices and tax optimization reached a value of just under PLN 850 million, which is a 12% better result compared to 2017. The total value of tax liability in the area of transfer prices and tax optimization resulting from tax and customs audits completed in 2018 amounted to over PLN 1.1 billion (a result better by over 70% compared to 2017) (Crido Report, 2019).

The tax office draws on CIT-TP and PIT-TP declarations as one of the sources of knowledge about potential transactions aimed at the transfer of income abroad.

It should be noted that the National Tax Administration began inspections in 2018 due to the risk of irregularities in the area of transfer prices and tax optimization in 166 entities, which is a significant decrease compared to the total of 341 in the previous year.

However, according to the National Tax Administration, the reason is the change in operating methods through a more detailed selection of entities for audit on the basis of risk analysis, and by conducting checks where irregularities exist.

7.9.2 TRANSFER PRICING CASE-LAW

Judicial decisions in Poland concern a number of various issues related to the subject of transfer pricing, although the jurisprudence of administrative courts is not extensive in decisions regarding transfer pricing. In anticipating a potential dispute with the tax authorities, it is not easy to predict the outcome based on Supreme Administrative Court rulings.

Examples of areas subject to judicial decisions are given in Table 53.

Table 53: Judicial decisions in Poland

Subject of the procedure	Date of decision	Reference number
Relationship	2013-05-28 2012-09-18	I SA/Kr 514/13 I FSK 617/12
Documentation obligation	2013-01-15 2012-07-25 2012-05-10 2011-01-10 2010-05-21 2012-02-09 2015-01-15	II FSK 1052/11 III SA/Wa 2659/11 II FSK 1894/10, II FSK 1894/10 III SA/Wa 2647/10 II FSK 41/09 III SA/Wa 1506/11 II FSK 1052/11
Guarantees Income estimation	2010-10-27	I SA/Sz 501/10
Loans	2012-01-27 2011-10-07 2011-01-05	ILPB4/423-406/11-3/MC IPPB5/423-677/11-2/AS ITPB3/423-548/10/MK
Cash-pooling	2013-01-29	I SA/Gd 1222/12
Sanction tax rate	2012-01-10 2010-12-14	II FSK 1319/10 II FSK 1402/09
Income estimation	2010-12-16 2013-01-08 2010-07-21 2012-10-11 2011-11-29	I SA/Wr 1145/10 II FSK 975/11 I SA/Go 475/10 II FSK 385/11 I SA/Wr 1107/11
The cost plus method	2011-07-12 2010-08-16	I SA/Bk 217/11 I SA/Wr 678/10
Comparability analysis	2011-03-11 2010-08-16	II FSK 1924/09 I SA/Wr 678/10.

Source: own elaborations based on DMS (2019).

Certain doubts have long been caused by the identification of transactions recognized in statutory thresholds, especially in the context of the provisions in force before 1 January 2019, in which there was no definition of a transaction. For example, in accordance with the verdict of the Supreme Administrative Court (NSA) of 10.05.2012 (II FSK 1893/10), the obligation to prepare documentation arises when the value of all services provided of the same type in transactions with a related entity exceeds the amount of the statutory threshold. However, if the taxpayer carries out several transactions with one entity, but they have a different scope then the value of these transactions is not added up. It should be noted that the deciding factor for different transactions is not the price, which may vary within the same transaction. Similar rulings were issued by the Supreme Administrative Court in the following cases: January 15, 2015, reference number II FSK 1052/11, as well as in the Provincial Administrative Court in Warsaw of February 9, 2012, reference number alt III SA / Wa 1506/11.

It should be noted that until the end of 2018, a 50% penalty tax rate was imposed in Poland for income estimated by the tax authority where there was an absence of tax transfer pricing documentation (Act on CIT, art. 19.1, wording until 31.12.2018 and art. 19a, wording until 31.12.2016). This was widely understood in such a way that it was enough to have any transfer pricing documentation to avoid the 50% sanction tax rate. Pursuant to the judgment of the Supreme Administrative Court of December 14, 2010, reference number II FSK 1402/09, the accuracy of a taxpayer's transfer pricing documentation was questioned because of too high a degree of generality, as well as non-compliance with mandatory documentation requirements. The sanction tax rate can be used not only in the absence of documentation, but also when it is incomplete.

Before this was regulated in detail in the light of legal provisions, there were many doubts among taxpayers on whether they needed to include comparability analyses in tax documentation. The court rulings at the time confirmed the view that in the absence of the need to submit market analyses in document form, the tax authorities had to prove that the prices used were non-market. An example of such a position is the judgment of the Supreme Administrative Court of March 11, 2011 reference number II FSK 1924/09, as well as the judgment of the Provincial Administrative Court in Wrocław of August 16, 2010 (reference number I SA / Wr 678/10).

Undoubtedly, emotions may run high among taxpayers due to the possibility of additional income being added by the tax authorities. When valuations of this nature occur, taxpayers usually appeal against such decisions. An example of the subject of an appeal may be the use of a different method of determining the transfer price than was used by the taxpayer. In the current legal provisions, the act introduces the need for the tax authorities to use the same method as the taxpayer used, but earlier such cases were decided by the courts. An example is the judgment of the Provincial Administrative Court in Wrocław of 16 December 2010, reference number file I SA / Wr 1145/10 and the judgment of the Supreme Administrative Court of January 8, 2013 reference number Act II FSK 975/11, where it was stated that the taxpayer should duly justify the adopted method of determining transfer prices, and due to the lack of such method, the authorities could make an estimation on the basis of the method chosen by him as appropriate.

On the other hand, there were also judgments which stated that the estimation of income by the tax authorities should be based on a set of comparative data and not only on the basis of individual data. An example in this respect was the ruling of the Provincial Administrative Court in Gorzów Wielkopolski of July 21, 2010, reference number act I SA / Go 475/10, confirmed by the judgment of the Supreme Administrative Court of 11 October 2012, reference number act II FSK 385/11. Additionally, in the judgment of the Provincial Administrative Court in Wrocław of November 29, 2011 reference number act I SA / Wr 1107/11, the evaluation of the control body regarding the sale price of land was questioned, arguing that the body did not have a sufficient comparative basis but only a single observation.

The use of comparative data is limited by access to such data and by the possibilities of generalizing it. This problem may appear in methods other than the method of comparable uncontrolled price, e.g. in the cost plus method. For example, in accordance with the judgment of the Provincial Administrative Court in Białystok of July 12, 2011, reference number act I SA / Bk 217/11, a producer of dairy products in the form of cheese, butter and whey could consider a processor of similar products as a comparative entity, despite differences between the entities' functional profiles. This was confirmed by the Supreme Administrative Court judgment of December 5, 2012, reference number Act II FSK 813/11 specifying, however, that if it is not possible to identify entities with the same functional profile, income can be estimated on the basis of the price corresponding to the sum of direct costs related to the purchase of goods, and the corresponding profit at the level of the average profit used in transactions with an associated entity.

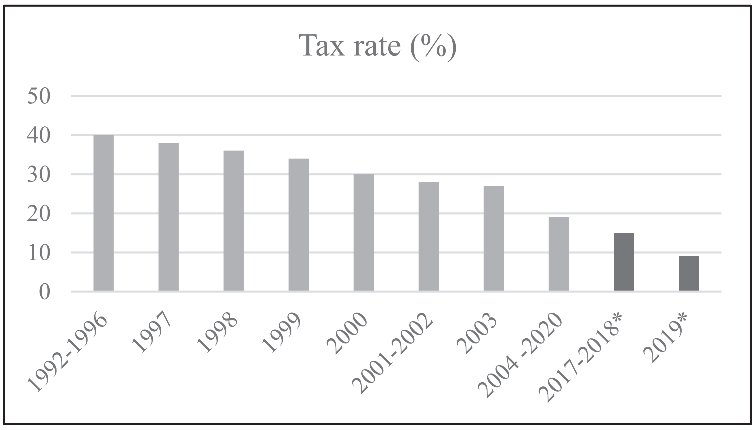
7.10 SUMMARY OF FINDINGS

Legal regulations regarding transfer pricing in Poland result, among others, from changes in regulations regarding corporate income tax (CIT). This tax was introduced in Poland in 1989, and in 1992 a new Corporate Income Tax Act came into force, containing Article 11, which introduced the arm's length principle into Polish regulations (Act on CIT, 1992). Despite criticism in the literature of the arm's length principle (Matsui, 2011; Devereux and Keuschnig, 2008; Cheng and Zhang, 2009), no alternative approach has yet been developed in Poland or other countries.

During analysis of the legal regulations presented in chapter 7, it should be stated that Poland is one of the countries that has intensively implemented OECD and EU regulations. The effect of Poland's accession to the OECD in 1996 was the first regulation to art. 11 in 1997 (Regulation of the Minister of Finance of October 10, 1997 on the method and procedure for determining taxpayers' income by estimating prices in transactions made by these taxpayers), based on the OECD Guidelines (2017a). In 2001, Article 9a was introduced to the Act on CIT, implementing the obligation of preparing transfer pricing documentation. This obligation is sometimes treated by taxpayers in Poland as troublesome and difficult to fulfil, which is in accordance with opinions presented in the literature (Couzin 2013; Succio, 2010).

It seems that the changes in corporate income tax reflect the desire to maintain a balance between the interests of the state and those of the taxpayer (EY, 2014). Additional evidence of this are the changes in CIT tax rates in Poland presented in Figure 2.

Figure 2: Corporate Income Tax Rates in Poland



* for small taxpayers[90] and start-ups

Source: own elaboration.

The decrease in the CIT rate is accompanied by a desire to tighten up the tax system, among others by creating legal regulations preventing the shifting of revenues to subsidiaries from countries with lower tax rates. The BEPS project (OECD, 2015), which caused revolutionary changes to the Polish legal regulations in force in 2017 and 2018, as well as later ones (Gupta, 2018; Dumiter and Boiță, 2017), was a breakthrough in this respect for Poland. The implementation of regulations preventing profit shifting is confirmation that, for the Polish tax authorities, international corporations are entities that may use harmful tax optimization, which is in accordance with the common view in the literature (among others Nugroho, Wicaksono and Utami, 2018; Chan, Lo and Mo, 2015; Kaur and Kaur, 2015).

The result of the BEPS project for Poland was, among others, introduction in 2017 of the obligation to include comparative analysis or compliance analysis results in transfer pricing documentation. Thus, taxpayers in Poland faced such challenges as: access to databases, selection of a comparative sample and comparative parameter, the possibility of using foreign benchmarks and other problems of comparability analysis described in the literature (Johnson, 2006; Rossing et al., 2017; Smith, 2015; Nerudová et al., 2017; Sulik-Górecka, 2018).

Poland is a country that not only implements solutions recommended by the OECD or the EU Joint Transfer Pricing Forum, but is also a leader in implementing innovative solutions, e. g. in the field of safe harbour. The literature lists numerous benefits of safe harbours, such as simplifying compliance, reducing compliance costs, providing certainty, shifting administrative resources to examination of more complex or higher risk transactions and taxpayers, and so on (Solilová, 2013; Singh, et al., 2009, Kostić, 2018). Safe harbour regulations for low value-added services have been in force in Poland since 2017, and for loans from 2019. It should be noted that the regulations contain references to specific market margins. For example, for 2019 and 2020, a 2% margin and base interest rates were determined depending on the loan currency (e. g. WIBOR 3M for a loan in PLN, LIBOR USD 3M for a loan in US dollars) (Announcement of the Minister of Finance, 2018).

Poland has also taken advantage of innovative solutions in the field of transfer pricing methods. Factors affecting the determination of transfer prices and the selection of TP methods are the subject of scientific research by many authors. Researchers highlight the need to take into account a number of conditions, e. g.

90 A small taxpayer is an entity whose value of sales revenue (together with the amount of value added tax due) did not exceed in the previous tax year the amount expressed in zlotys corresponding to the equivalent of EUR 1.2 million. Amounts expressed in euro are converted according to the average euro exchange rate announced by the National Bank of Poland on the first business day of October of the previous tax year, rounded to the nearest 1000 PLN. (Act on CIT, Art. 4a (10))

external suppliers, comparing variable sales division costs and market price, and the company's operating capacity (Blocher et al., 2019, Verdes, 2016). In the face of the difficulties that may arise in connection with the choice of method, Polish regulations propose a so-called sixth method, used when other methods are not possible. One example of the sixth method are valuation techniques by independent experts, e.g. on the real estate market. Calculation of remuneration based on stock exchange quotations for basic products in the oil and gas processing industry is another example of using the sixth method. Although such valuations have been used by taxpayers for many years, until 31 January 2018 taxpayers were not certain that such valuations would be accepted by the tax authorities.

It should be noted, that the expectations of the Polish tax authorities regarding the reporting of transfer pricing have increased significantly in recent years, as evidenced, among others, by the extensive TP-R form. Meeting reporting requirements requires a much greater commitment of the Management Board than it used to be when the input of financial and accounting services was sufficient. The requirement for the Management Board to submit an annual statement of prices compliance with the arm's length principle, also demonstrates that tax authorities want to be sure that members of the Management Board have a real impact on transfer pricing policy in corporate groups. Meanwhile, production or distribution functions of multinational corporate groups are located in Poland, but the strategic headquarters of large corporations are based in other countries (Błażejewska-Gaczyńska, 2019)

Operating in a global world requires both MNEs and tax administrations of different countries to use advanced communication and dispute resolution procedures. In this context, Poland should be assessed positively as a country that has implemented international conventions such as:

- The OECD Model Convention on the avoidance of double taxation in the field of taxes on income and property (OECD, 2017b),
- The Multilateral Convention implementing Treaty Tax Law measures aimed at preventing the erosion of the tax base and the transfer of profits, concluded in Paris on November 24, 2016, and signed in Paris on June 7, 2017 (OECD, 2016),
- The convention on mutual administrative assistance in tax matters, concluded in Strasbourg on January 25, 1988 (Council of the European Union, 1988).

In the face of globalization, Advance Pricing Agreements are becoming an extremely important instrument, especially in bilateral and multilateral agreements involving tax administrations of at least two countries. The benefits of concluding APAs and the difficulties associated with them are widely analysed in the literature (among others Eden and Byrnes, 2018; Biyan and Yilmaz, 2013; Singh et al., 2009; Herath and Young, 2012). Taking into account the advantages of concluding an APA and wanting to counteract the difficulties, since 2006 Poland has developed detailed procedures for preparing applications that enable taxpayers to conclude APAs. It should be emphasized that in 2019 a new comprehensive Act of October 16 2019 on the settlement of disputes regarding double taxation and the conclusion of advanced price arrangements (Act on APA, 2019) entered into force.

Comparison of Polish regulations in the field of transfer prices with Czech, Slovak and Hungarian regulations reveals many differences, despite the dominant influence of OECD Guidelines and EU Joint Transfer Pricing Forum standards. Although perhaps not all Polish solutions are perfect, it seems that Polish legislation may be a source of inspiration for the amendment of the law in the other Visegrad countries analysed.

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ANNEX

Table 54: Overview of all Double tax treaties signed by Poland as at 30/09/2019

No.	Contracting state	Signature Date	Valid from	Act of Law	Cat. 1	Cat. 2	Cat. 3
1	Albania	05.03.1993	01.01.1995	1994 - item 492		X	
2	Algeria	31.01.2000				X	
3	Saudi Arabia	22.02.2011	01.01.2013	2012 - item 502		X	
4	Armenia	14.07.1999	01.01.2006	2005 - item 576		X	
5	Australia	07.05.1991	01.01.1993	1992 - item 177		X	
6	Austria	13.01.2004	01.01.2006	2005 - item 1921		X	
		04.02.2008	01.01.2009	2008 - item 1450			
7	Azerbaijan	26.08.1997	01.01.2006	2008 - item 52		X	
8	Bangladesh	08.07.1997	01.01.2000	2000 - item 1121	X		
9	Belgium	20.08.2001	01.01.2005	2004 - item 2139		X	
		14.04.2014	01.01.2019	2018 - item 1094			
10	Belarus	18.11.1992	01.01.1994	1993 - item 534		X	
11	Bosnia and Herzegovina	10.01.1985	01.01.1986	1986 - item 102		X	
		04.06.2014	01.01.2017	2016 - item 590			
12	Bulgaria	11.04.1994	01.01.1996	1995 - item 679		X	
13	Chile	10.03.2000	01.01.2004	2004 - item 1976		X	
14	China	07.06.1988	01.01.1990	1989 - item 65	X		
15	Croatia	19.10.1994	01.01.1997	1996 - item 370		X	
				2016 - item 1083			
16	Cyprus	04.06.1992	01.01.1992	1993 - item 523		X	
		22.03.2012	01.01.2013	2012 - item 1383			
17	Montenegro	12.06.1997	01.01.1999	2001 - item 1137		X	

No.	Contracting state	Signature Date	Valid from	Act of Law	Cat. 1	Cat. 2	Cat. 3
18	Czech Republic	24.06.1993	01.01.1994	1994 - item 189			X
		13.09.2011	01.01.2013	2012 – item 991			
19	Denmark	06.12.2001	01.01.2003	2003 - item 368		X	
		07.12.2009	01.01.2011	2010 - item 1613			
20	Egypt	24.06.1996	01.01.2002	2003 - item 690			X
21	Estonia	09.05.1994	01.01.1995	1995 - item 388		X	
22	Etiopia	13.07.2015	01.01.2019	2018 - item 329		X	
23	Philippines	09.09.1992	01.01.1998	1997 - item 817		X	
24	Finland	26.10.1977	01.01.1980	1979 - item 84		X	
		28.04.1994	01.01.1996	1995 - item 517			
		08.06.2009	01.01.2011	2010 - item 205			
25	France	20.06.1975	01.01.1974	1977 - item 5	X		
26	Greece	20.11.1987	01.01.1992	1991 - item 524	X		
27	Georgia	05.11.1999	01.01.2007	2006 - item 1820		X	
28	Guernsey	08.10.2013	01.01.2015	2014 - item 1341	X		
		08.10.2013	01.01.2015	2014 - item 1339			
29	Spain	15.11.1979	01.01.1983	1982 - item 127		X	
30	The Netherlands	13.02.2002	01.01.2004	2003 - item 2120		X	
31	India	21.06.1989	01.01.1990	1990 - item 46		X	
		29.01.2013	01.01.2015	2014 - item 1337			
32	Indonesia	06.10.1992	01.01.1994	1994 - item 187			X
33	Iran	02.10.1998	01.01.2007	2006 - item 1770		X	
		15.12.2004	01.01.2007	2006 - item 1772			
34	Irleand	13.11.1995	01.01.1996	1996 - item 129			
				2019 - item 1733			
35	Iceland	19.06.1998	01.01.2000	1999 - item 890		X	
		16.05.2012	01.01.2014	2013 - item 1353			
36	Israel	22.05.1991	01.01.1992	1992 - item 124	X		
37	Japan	20.02.1980	01.01.1983	1983 - item 60	X		
38	Jersey	02.12.2011	01.01.2013	2012 - item 1177	X		
		02.12.2011	01.01.2013	2012 - item 1179			
39	Jordan	04.10.1997	01.01.2000	1999 - item 654			X
40	Canada	04.05.1987	01.01.1989	1990 - item 216			X
		14.05.2012	01.01.2014	2013 - item 1371			
41	Katar	18.11.2008	01.01.2010	2010 - item 93		X	
42	Kazakhstan	21.09.1994	01.06.1995 01.01.1996	1995 - item 586		X	
43	Kyrgyzstan	19.11.1998	01.09.2004 01.01.2005	2004 - item 2304		X	
44	South Korea	21.06.1991	01.01.1991	1992 - item 126		X	
		22.10.2013	01.01.2017	2016 - item 1977			
45	Kuwait	16.11.1996	01.01.1996	2000 - item 811		X	
46	Lebanon	26.07.1999	01.01.2004	2004 - item 2445		X	
47	Lithuania	20.01.1994	01.01.1995	1995 - item 277		X	
48	Luxembourg	14.06.1995	01.01.1997	1996 - item 527		X	
		07.06.2012	01.09.2013	2013 - item 964			
			01.01.2014	2019 - item 1244			

No.	Contracting state	Signature Date	Valid from	Act of Law	Cat. 1	Cat. 2	Cat. 3
49	Latvia	17.11.1993	01.01.1995	1995 - item 285		X	
50	Macedonia	28.11.1996	01.01.2000	2002 - item 1744		X	
51	Malaysia	16.09.1977	01.01.1977	1979 - item 62		X	
		08.07.2013					
52	Malta	07.01.1994	01.01.1995	1995 - item 256		X	
		06.04.2011	01.01.2012	2011 - item 1661			
53	Morocco	24.10.1994	01.01.1997	1996 - item 529		X	
54	Mexico	30.11.1998	01.01.2003	2003 - item 131			X
55	Moldova	16.11.1994	01.01.1996	1996 - item 166	X		
56	Mongolia	18.04.1997	01.01.2002	2002 - item 1746	X		
57	Germany	14.05.2003	01.01.2005	2005 - item 90		X	
		17.08.2015	01.01.2016				
58	Nigeria	12.02.1999				X	
59	Norway	24.05.1977	01.01.1976	1979 - item 157		X	
		09.09.2009	01.01.2011	2010 - item 899			
		05.07.2012	01.06.2013 01.01.2014	2013 - item 680			
60	New Zealand	21.04.2005	01.01.2007	2006 - item 1822		X	
61	Pakistan	25.10.1974	01.01.1973	1976 - item 47	X		
62	Portugal	09.05.1995	01.01.1999	1998 - item 304		X	
				2017 - item 1101			
63	South Africa	10.11.1993	01.01.1996	1996 - item 124		X	
64	Russia	22.05.1992	01.01.1994	1993 - item 569	X		
65	Romania	23.06.1994	01.01.1996	1995 - item 530		X	
66	Serbia	12.06.1997	01.01.1999	2001 - item 1137		X	
67	Singapore	23.04.1993	01.01.1993	1994 - item 139		X	
		04.11.2012	01.01.2015	2014 - item 443			
68	Slovakia	18.08.1994	01.01.1996	1996 - item 131		X	
		01.08.2013	01.01.2015	2014 - item 1046			
69	Słowenia	28.06.1996	01.01.1999	1998 - item 198		X	
70	Sri Lanka	25.04.1980	01.01.1983	1988 - item 38			X
		06.10.2015	14.06.2019 01.01.2020	2019 - item 1334			
71	United States of America	08.10.1974	01.01.1974	1976 - item 178		X	
		13.02.2013					
72	Syria	15.08.2001	01.01.2004	2004 - item 1972		X	
73	Switzerland	02.09.1991	01.01.1993	1993 - item 92			X
		20.04.2010	01.01.2012	2011 - item 1533			
74	Sweden	19.11.2004	01.01.2006	2006 - item 193		X	
				2017 - item 2177			
75	Tajikistan	27.05.2003	01.09.2004 01.01.2005	2005 - item 92		X	
76	Thailand	08.12.1978	01.01.1983	1983 - item 170	X		
77	Tajwan		01.01.2017	2016 - item 2244		X	
78	Tunisia	29.03.1993	01.01.1994	1994 - item 357		X	
79	Turkey	03.11.1993	01.01.1998	1997 - item 58		X	

No.	Contracting state	Signature Date	Valid from	Act of Law	Cat. 1	Cat. 2	Cat. 3
80	Ukraine	12.01.1993	01.01.1995	1994 - item 269		X	
81	Uruguay	02.08.1991			X		
82	Uzbekistan	11.01.1995	01.01.1996	1995 - item 559		X	
83	Hungary	23.09.1992	01.01.1996	1995 - item 602	X		
		27.06.2000	01.09.2002	2002 - item 946			
84	United Kingdom	20.07.2006	01.01.2007	2006 item 1840		X	
85	Vietnam	31.08.1994	01.01.1996	1995 - item 258	X		
86	Italy	21.06.1985	01.01.1984	1989 - item 374	X		
				2019 - item 597			
87	Isle of Man	07.03.2011	01.01.2012	2011 - item 1663	X		
		07.03.2011	01.01.2012	2011 - item 1667			
88	Zambia	19.05.1995				X	
89	Zimbabwe	09.07.1993	01.01.1995	1995 - item 318		X	
90	United Arab Emirates	31.01.1993	01.01.1995	1994 - item 373		X	
		11.12.2013	01.01.2016	2015 - item 312			

Source: own elaboration based on Ministry of Finance (2019).

Table 55: Codes and categories of controlled transactions in TP-R

CODES AND CATEGORIES OF CONTROLLED TRANSACTIONS
Transactions related to trade in goods - sales
1001 Sale of finished products by the manufacturer with extended functions and risks
1002 Sale of finished products by the producer with limited functions and risks
1003 Provision of production service (toll manufacturing)
1004 Sale of commercial goods by a central entrepreneur
1005 Sale of commercial goods by a distributor with extensive functions and risks
1006 Sale of commercial goods by a distributor with limited functions and risks
1007 Provision of agency services in relation to goods or products
1008 Commission sales of goods or products
1009 Sales of raw materials, semi-finished products for production needs
1010 Sale of spare parts
Service transactions - sales
1101 Sale of services with low added value
1102 Sale of research and development services
1103 Sale of brokerage services in the sale or purchase of services
1104 Sale of intangible services related to real estate (e.g. property management, asset management)
1105 Sale of intangible services other than services with low added value, research and development, real estate and brokerage
1106 Sale of other services
Financial transactions - sales
1201 Transaction related to the granting of financing (credit, loan, acquisition) bonds or other form)
1202 Liquidity management transactions (cash pooling) - positive items
1203 Guarantee or surety issued
1204 Depositing funds
1205 Sale of services related to insurance (e.g. insurance, reinsurance, insurance brokerage)
1206 Other financial transactions - sales (including service related services payments, hedging, factoring)
Asset transactions
1301 Sale of intangible assets
1302 Contribution of intangible assets

CODES AND CATEGORIES OF CONTROLLED TRANSACTIONS
1303 Revenues from rent, lease, leasing of intangible assets
1304 Sale of real estate
1305 Contribution in kind
1306 Revenues from rent, lease, leasing of real estate
1307 Contribution of assets other than intangible assets and
Real estate
1308 Revenues from rent, lease or leasing of assets other than real estate and intangible assets
1309 Sale of shares, other property rights or participation rights in units
1310 In-kind contribution of an enterprise or part of an enterprise
1311 Sale of other assets
Access to intangible assets
1401 Granting of a license to use or rights to use the mark trade, know-how, patent, other intellectual property
Other transactions - sales
1501 Restructuring resulting in a transfer of functions, assets or risks to affiliate - for remuneration
1502 Restructuring resulting in the transfer of functions, assets or risks to affiliate - without remuneration
1503 Revenue from re-invoices (resale of the subject of the transaction at purchase price from an unrelated entity)
1504 Payment of remuneration for the management of a company which is not a legal person
1505 Receipt by a partner of a company which is not an appropriate legal person part of the company's profit
1506 Other controlled transaction not mentioned previously, related to generating income
Transactions related to trade in goods - purchase
2001 Purchase of finished goods from a manufacturer with extensive functions and risks
2002 Purchase of finished goods from a manufacturer with limited functions and risks
2003 Purchase of production service (toll manufacturing)
2004 Purchase of commercial goods from a central entrepreneur
2005 Purchase of commercial goods from a distributor with extensive functions and risks
2006 Purchase of commercial goods from a distributor with limited functions and risks
2007 Purchase of agency services for goods or products
2008 Purchase of goods or products for commission sale
2009 Purchase of raw materials, semi-finished products for production needs
2010 Purchase of spare parts
Service transactions - purchase
2101 Purchase of services with low added value
2102 Purchase of research and development services
2103 Purchase of brokerage services in the sale or purchase of services
2104 Purchase of intangible real estate services (e.g. management real estate, asset management)
2105 Purchase of intangible services other than services with low added value, research and development, real estate and brokerage
2106 Purchase of other services
Financial transactions - purchase
2201 Transaction related to obtaining financing (credit, loan, acquisition) bonds or other form)
2202 Liquidity management transactions (cash-pooling) - negative items
2203 Obtaining a guarantee or a surety
2204 Acceptance of a deposit of funds
2205 Purchase of insurance-related services (e.g. insurance, reinsurance, insurance brokerage)
2206 Other financial transactions - purchase (including services related to payment processing, hedging, factoring)
Asset transactions
2301 Purchase of intangible assets
2302 Receipt of an intangible asset contribution
2303 Costs for renting, leasing, leasing of intangible assets
2304 Purchase of real estate
2305 Receipt of real estate in kind
2306 Costs for renting, leasing or leasing of real estate

CODES AND CATEGORIES OF CONTROLLED TRANSACTIONS
2307 Receipt of an in-kind contribution of assets other than intangible assets and real estate
2308 Costs of renting, leasing or leasing assets other than real estate and intangible assets
2309 Purchase of shares, other property rights or participation rights in units
2310 Receipt of an enterprise or part of an enterprise contribution
2311 Purchase of other assets
Use of intangible assets
2401 Obtaining a license to use or obtaining a right to use trademark, know-how, patent, other intellectual property
Other transactions - purchase
2501 Restructuring resulting in a transfer of functions, assets or risks from affiliate - for remuneration
2502 Restructuring resulting in a transfer of functions, assets or risks from affiliate - without remuneration
2503 Costs for re-invoices (acquisition of the subject of the transaction at the original price acquisitions from an unrelated entity)
2504 Payment of remuneration for the management of a company which is not a legal person
2505 Payment from profit by a company which is not a legal person to its partners company
2506 Other controlled transaction not mentioned previously, related to incurring a cost

Source: own elaboration based on Regulation of MF (2018c).

CHAPTER 8
LEGAL REGULATIONS IN SLOVAKIA

8.1 GENERAL ASPECTS OF LEGAL REGULATION

The legal system of the Slovak Republic consists of the constitution of the Slovak Republic, European Union regulations (legal acts of the EU), ratified international treaties and constitutional laws. A part of the Slovak legal order is increasingly becoming the so-called soft law, which is, however, voluntary and is not generally binding. Soft law may become binding on all parties at contract law level, where it expressly outlines its observance and determines sanctions for its infringement (Mazák and Jánošíková, 2009).

Each country has its own legal culture that one can perceive as *"… a specific way of understanding, creating and applying law that reflects certain geopolitical and historical peculiarities"* (Tóthová, 2011, p. 31). From the perspective of the division of legal cultures or legal systems, the Slovak Republic falls under the Continental Legal System.

In recent years, one can observe a slight change in the legal culture from the continental legal culture, where laws are in written form and constituted by the state authorities, to a mixed legal culture with an increasing importance on uniform interpretation of the law and guaranteeing legal certainty by creating case law on which judges participate, which is a typical character for common law. Each country has its own legal order and in the context of international cooperation, situations arise, where the laws of the cooperating countries contradict each other. With EU membership it is also necessary for the Slovak Republic to solve the question of the relationship between EU law and the domestic law of the Slovak Republic. The relationship between Slovak and EU law is regulated in Article 7(2) of the Constitution of the Slovak Republic, which states that *"The Slovak Republic may, by an international treaty, which was ratified and promulgated in the way laid down by a law, or on the basis of such treaty, transfer the exercise of a part of its powers to the European Communities and the European Union. Legally binding acts of the European Communities and of the European Union shall have precedence over laws of the Slovak Republic. The transposition of legally binding acts which require implementation shall be realised through a law or a regulation of the Government according to Art. 120, para. 2."*

Legally binding EU legal acts simply mean regulations and directives. *"The binding nature of EU primary law standards as a subject of international public law therefore derives from the principle of pacta sunt servanda and the principles of international contract law arising from the Vienna Convention on the Law of Treaties of 1969, while the binding nature of secondary Union law (acquis de l'Union) derives from the binding nature of the Treaty on European Union (which does not contain a provision analogous to Article 249 of the EC Treaty which would directly establish the binding nature of secondary sources of Union law) and arises from the commitment of Member States to the EU"* (Corba, 2003, p. 35).

The regulations are directly binding to EU member states and their citizens, and they do not need to be transposed into the Slovak legal order. There is a different procedure in place for EU directives, which are also legally binding acts, but implementation must be executed by the Slovak legal order. Implementation is carried out through regulations, as a type of normative legal act of Slovakia issued by the government or by adopting legislation by the National Council of the Slovak Republic. EU directives that have been implemented in the Slovak legal order and EU regulations take precedence over the laws of the Slovak Republic. In the event of a conflict of interpretation of law or EU law with national law, these conflicts are resolved by the European Union Court of Justice, which by establishing jurisprudence prevents a different legal interpretation, which may also eliminate conflicts between EU and national law (Jánošíková, 2019).

From international law, only international treaties on human rights and fundamental freedoms, international treaties whose implementation is not required by law and international treaties directly establishing rights or obligations for natural or legal persons and which have been ratified and promulgated take precedence over Slovak law. In the event of a conflict of laws, it is necessary to determine *"… the relevant rule of law and its application to a particular legal situation"*, while this procedure "… *is a matter for the judicial authority to do so ex officio in accordance with the principle of iura novit curia"* (European e-Justice Portal, 2019).

Within national law, one can distinguish several types of normative legal acts. By a normative legal act, we mean the result of regulatory activity of an entity entitled to legislative power. Normative legal acts are divided into several groups, namely:

- Normative legal act – regulatory activity of an entity that is authorised to create laws, this group includes the constitution, constitutional laws and laws, and
- Subordinate normative legal acts – in this group we include all the results of normative activities, which have neither the legal force of the law nor legal form.

It is necessary to distinguish between normative legal acts, which are binding for all and individual legal act (like the result of an application of the law), which is binding only for the entity against which this application of the law occurred and only in specific cases. It is further necessary to distinguish between the normative legal act and individual legal act on one side and so-called soft law[91] (Vrabko, et al., 2018).

With soft law it is typical that this specific part of the legal order can be questioned or contested. For example, there is no sanction for breach of this rule, or the sanction is just not enforceable. Soft law is only a recommendation and that is the same for OECD guidelines. It is a set of recommendations for ethical international behaviour in the framework of mutual cooperation, the use of which should be recommended by EU member states. It is an internationally recommended code of ethics, but it is not legally enforceable. An example of a soft law can be an instructional methodology, which is understood as an instruction or manual with no binding character and its use is voluntary. The use of soft law cannot be enforced and at the same time it cannot be punished if it is not used. Currently, the OECD sources (in our case the OECD Transfer Pricing Guidelines) could be characterised as legal source material, and with high probability as a future formal source of law.

Based on the above, it can be stated that EU regulations are directly binding for Slovak citizens and they do not need to be adopted in the Slovak legal order. The EU directives are implemented as a normative legal act of the Slovak Republic in the form of regulation. OECD guidelines and methodological guidelines as soft law are not legally binding in the territory of the Slovak Republic and therefore do not bind anyone to their application and their non-application cannot be sanctioned by any fine.

8.2 SOURCES OF LAW INCLUDING (OR RELATED) TO TRANSFER PRICING

Transfer pricing law in the Slovak Republic is based on legal regulations from material law sources, mainly the OECD transfer pricing guidelines. Legal standards and principles are included in the Income Tax Act. Part of the legal standards is contained in legal form and legal implementation and application problems are in practice solved by reference to OECD documents. This implies a limited use of sub-legal acts and regulations to regulate transfer pricing issues.

In Slovak tax legislation the issue of transfer pricing is outlined and implemented via its domestic tax regulations.

The legal framework of transfer pricing in the Slovak Republic consists of the Slovak Income Tax Act No. 595/2003 Coll. as later amended [Zákon č. 595/2003 Z. z. o dani z príjmov v znení neskorších predpisov], the Tax Administration Act (Tax Procedure Code) of the Slovak Republic No. 563/2009 Coll. as later amended [Zákon č. 563/2009 Z. z. o správe daní (daňový poriadok) a o zmene a doplnení niektorých zákonov] and the Slovak Civil Code No. 40/1964 Coll. as later amended [Zákon č. 40/1964 Zb. Občiansky zákonník]. Domestic legal regulation in the transfer pricing field in Slovakia is also contained in the Journal of Law [Finančný spravodajca] No. 14/1997, 20/1999, 3/2002 where the OECD Transfer Pricing Guidelines from 1995 and 1997 were published in the Slovak language and the Journal of Law [Finančný spravodajca] No. 1/2009, 8/2014, 5/2015, 7/2016, 12/2018 where the administrative guidelines of the Slovak Ministry of Finance on the content of Transfer Pricing documentation were published.

Regarding transfer pricing framework, the following provisions from the Slovak Income Tax Act are of primary importance:

91 The division into normative and individual legal acts is of practical significance only to whom they bind. The distinction between normative and individual legal acts from the soft law is particularly important in the case of EU law. The results of the activities of the bodies of the European Union or of the bodies of international law are not always of a binding nature but may have the characteristics of legal norms.

- Section 1(2) (legal priority clause on the primacy of an international treaty to national tax legislation),
- Section 2(n) – (r) definition of associated persons,
- Section 17(5) primary adjustments to the tax base due to transfer pricing,
- Section 17(6) corresponding adjustments to the tax base due to transfer pricing,
- Section 17(7) permanent establishment of a tax base and its adjustments due to transfer pricing,
- Section 18 adjustment of tax bases of associated parties, and
- Section 18a procedures on tax penalties imposed relating to transfer prices.

From the Tax Procedure Code, the following provisions are primarily important:

- Section 162 legal priority clause on the primacy of an international treaty to national tax legislation,
- Section 3(6) basic principles of tax administration - the essence of the legal act prevails over its form (substance over form), and
- Section 160(4) competences of the Ministry of Finance in relation to foreign countries.

Individual provisions on transfer pricing have been refined and tightened in recent years. In respect to the application of transfer pricing rules, the guidelines are issued.

Currently, the following guidelines are important to follow in relation to transfer pricing rules in Slovakia:

- Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 to determine the content of documentation according to Section 18(1) of the Income Tax Act No. 595/2003 Coll.,
- Methodological guidelines on applying transfer pricing methods,
- Methodological guidelines on the application of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and Transfer Pricing Legislation in the Slovak Republic (the Internal Steering Act No. 79/2014),
- Methodological Guidelines No. MF/020525/2017-724 on the processes under the mutual agreement procedure, and
- Methodological guidelines on the approval of the use of a specific transfer pricing method according to Section 18(4) and (5) of the Income Tax Act 595/2003 Coll. as later amended (Internal Steering Act No. 65/2014).

Slovak legislation often refers to OECD sources. The OECD Transfer Pricing Guideline is not legally binding but accepted as an explanatory instrument (administrative guideline). The Financial Directorate of the Slovak Republic published the Internal Steering Act No. 79/2014 as a Methodological Guideline on the application of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and Transfer Pricing Legislation in the Slovak Republic. The main aim of this methodological guideline is to guide the tax administrator in the area of transfer pricing legislation and to ensure a consistent approach by the tax administrator in the interpretation and application of the OECD Transfer Pricing Guidelines.

Within the Slovak Republic, methodological guidelines are an internal steering (advisory) act ensuring uniform application of special regulations and international treaties to which the Slovak Republic is bound in the area of taxes, fees and customs. Methodological guidelines are not a formal source of law, but their publication shall be considered as an important step towards increasing legal certainty.

Methodological guidelines highlight Section 3(6) of the Tax Procedure Code in the application of tax regulations in a tax administration, where it is stated that *"a legal act, several legal acts or other facts carried out without a proper business reason or any other reason reflecting economic reality and for which at least one of the purposes is to circumvent tax liability or obtain a tax advantage, are not taken into account in the administration of taxes"* (substance over form). This provision is considered as one of the most important against aggressive tax planning and was implemented by an amendment which has been in force since 2015.

In the area of bilateral and multilateral relations, transfer pricing rules are mainly linked to international tax treaties and signed Double Tax Treaties (DTTs). International tax treaties deal with transfer pricing in Article 7 (Business profits, including the principles of tax base determination of permanent establishments based on transfer pricing rules), Article 9 (Associated enterprises), Article 24 (Non-discrimination), Article 25 (Mutual agreement procedure) and Article 26 (Exchange of information).

Article 9 is reflected in Section 17(5) of the Income Tax Act, the tax base of an associated party shall also include the difference between the prices agreed in the business transaction of associated parties (including the prices of services, loans and credits), and the prices applied between unrelated parties in comparable business transactions, as long as such difference results in a reduction of the tax base or increase of tax loss. The difference shall be determined according to Section 18 (Adjustment of Tax Bases of Associated Parties). The formulation of Section 17(5) is based on Article 9(1) of the OECD Model Tax Convention.

According to the Income Tax Act amendment in place since 2015, the adjustment of the tax base of an associated party in the territory of the Slovak Republic shall be permitted by the tax administration where the tax administration made an adjustment of the tax base of other associated parties in the territory of the Slovak Republic as set out in Section 17(5) or where the tax administration of the country which has a double tax treaty in place with the Slovak Republic made an adjustment of the tax base of the associated party abroad which is in compliance with the arm's length principle under Section 18, subsection 1 (Section 17(6)). A written notice shall be given by the tax administration to the taxpayer to that effect. The cited provision of the Income Tax Act in domestic tax regulation creates scope for fulfilling the Slovak Republic's obligations as a member of the OECD to make appropriate adjustments pursuant to Article 9(2) of the OECD Model Tax Convention.

The requirements of the corresponding tax adjustments are unlikely to prevent full economic double taxation due to different tax rates, barring adjustments to the tax base to the required extent or its total rejection. In this case, it is possible to look for a solution to the problem through the mutual agreement procedure (MAP), which is under the competencies of the Ministry of Finance of the Slovak Republic based on Section 160(4) of the Tax Procedure Code. According to the mentioned provision, the ministry may decide on the method of taxation in cases where taxpayers are domiciled or reside outside the territory of the Slovak Republic, and in relation to foreign parties to ensure reciprocity or retaliatory measures for the purpose of mutual settlement. In domestic legislation, this provision creates scope for the legal application of Article 25 (Mutual Agreement Procedure), which is part of many international tax treaties. Instructions on how to proceed are contained in the commentary on Article 25 of the OECD Model Tax Convention and also in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations in chapter IV (Administrative approaches to avoiding and resolving transfer pricing disputes), part C (Corresponding adjustments and the mutual agreement procedure: Articles 9 and 25 of the OECD Model Tax Convention).

Additionally, Slovakia as a member of the EU adheres to the EU Code of Conduct on Transfer Pricing documentation for associated enterprises and to the rules of the EU in ensuring the functionality of the internal market. In applying transfer pricing rules, the Slovak Republic takes into account documents adopted within the EU that have already been implemented in domestic law or are merely a political obligation of an EU member state resulting from its membership.

Financial administration of the Slovak Republic [Finančná správa Slovenskej republiky] on its website[92] publishes opinions on particular cases associated with transfer pricing. There one can see published opinions in classical areas of transfer pricing, e.g. different cases on transfer pricing documentation, filling in a tax return and its annexes, tax base adjustments, assessment of dependency of persons and specific cases (e.g. transfer pricing when donating or applying transfer pricing to state-owned taxpayers).

8.3 DEFINITION OF KEY TERMS IN DOMESTIC LAW

8.3.1 DEFINITION OF ASSOCIATED PERSONS IN DOMESTIC LAW

The definition of an associated person or key terms related to transfer pricing are primarily outlined in the Income Tax Act and signed double tax treaties. Indirectly, the definition related to associated persons can also be found in the Act on Accounting.

The term "**associated person**"[93] is defined in Section 2(n), (o), (p) and (r) of the Income Tax Act. The term „**associated party**" means a close person or a person with economic, personal or other ties (Section 2(n)). Since the amendment of the Income Tax Act in effect from 1 January 2018[94] , there has been an addition to

92 https://podpora.financnasprava.sk/245926-Stanovisk%C3%A1-FR-SR (Financial Administration of the Slovak Republic, 2019a)
93 The English version of the Slovak Income Tax Act uses the term "related party" instead of "associated party".
94 Act No. 344/2017 Coll. amending the Act No. 595/2003 Coll. on Income Tax (Income Tax Act) as later amended and amending the Tax Procedure Code (Act No. 563/2009 Coll. as later amended). Before 2018, this definition criteria category of associated party was only part of the Act on accounting. By this amendment, the definition of associated person is extended by adding the word "entity".

the definition of associated party to include "person or entity which is part of the consolidated group for consolidation purposes" (Income Tax Act, Section 2 (n) (3)).

1. **Close persons** are defined in Sections 116 and 117 of the Slovak Civil Code no. 40/1964 Coll. as later amended. According to Section 116 of the Slovak Civil Code, a close person shall be defined *"as a relative in direct line, brother or sister and the spouse; other persons in a family or other relation shall be considered close to each other if a detriment suffered by one of them is reasonably felt as own by the other"*. Further, according to Section 117 of the Slovak Civil Code, *"the level of relationship between two persons shall be ascertained according to the number of births from one person originating from the direct line of the other and from both persons originating from a common ancestor"*.
2. **Economic and personal ties**. *"The term economic or personal ties means the participation of a person or entity in the property, control or management of another person or entity or a mutual relationship between persons or entities, which are under the control or management of the same person, its close person or entity or in which this person or its close person or entity has a direct ownership interest or indirect ownership interest while participating in two main categories, property or control and management:*

a) ***property or control*** *means the direct, indirect or indirect derived interest with more than a 25% share of capital, direct interest, indirect interest or indirect derived interest with more than 25% in voting rights or interest with more than 25% in profit where indirect interest shall be calculated as a product of the percentage of direct interests divided by one hundred and the result calculated in this manner shall be multiplied by one hundred and the indirect derived interest shall be calculated as a total of indirect interests where; the indirect derived interest shall only be used to calculate the interest of one person or subject in the property or control of other person or subject where the one person or subject has interest in the property or control of multiple persons or entities each of which has interest in the property or control of the same other person or subject; where the indirect derived interest exceeds 50%, all persons or subjects used in the calculation shall be deemed to have economic ties irrespective of the actual amount of their interest; where for the purposes of this point the person or entity acting jointly with other person or subject; in the case of voting rights or an interest in the share capital, it shall be deemed to be a person or entity which holds an interest in all the voting rights or is the owner of this interest in the share capital held by that other person or entity.*

b) the term ***management*** *means the relationship between the members of the statutory bodies or the members of the supervisory bodies of a business company or other similar bodies of a legal entity to that legal entity" (Section 2 (o));*

Other ties. *"The term other ties means a legal relationship or transaction created for the purposes of a tax base decrease or a tax loss increase" (Section 2 (p)).*

According to Section 2 letter r) of the Income Tax Act, *"the term non-resident associated party shall mean a situation, in which a resident natural person, resident legal entity or resident entity has ties to a non-resident natural person, non-resident legal entity or resident entity as provided in letter n) (close persons according to Sections 116 and 117 of the Civil Code; economic, personal or otherwise associated persons or entities or persons or entities, which are part of a consolidated group for the purpose of accounting).*

The above shall apply also to:

- *the relationship between a taxpayer with unlimited tax liability and its permanent establishments abroad, and*
- *the relationship between a taxpayer with limited tax liability and its permanent establishment in the territory of the Slovak Republic, and*
- *the relationship between permanent establishments of taxpayers with ties as set out in letter n) and the mutual relationship between these permanent establishments and these taxpayers"*[95]

According to Section 2 letter ad), for the purpose of the Income Tax Act, associated persons also include the legal entity (subject) (amendment in force since 2018). The entity (for this purpose) may be a legal arrangement of assets or a legal arrangement of persons that do not have legal personality, or it may be another legal arrangement that owns or manages property. These are primarily trusts or personal

95 With effect from 1/1/2018.

companies (partnerships) which are commonly used abroad. These types of arrangements for property or persons occur very rarely in the Slovak Republic (e.g. consortium) (Fischerová, 2018, In Daňový a účtovný poradca podnikateľa). According to Kočiš (2019), the *entity definition* appears as very broad and unclear, thus contributing to legal uncertainty. Kočiš (2019a) further highlights that the amendments to the Income Tax Act and the extension of the associated person definition are a result of the ATAD transposition. The ATAD transposition into Slovak legislation contributed to significant change in the personal scope of transfer pricing. The current domestic concept of associated enterprises could result in double taxation due to the possible different approaches to the association in various tax jurisdictions.

"Other ties (associated persons otherwise)" institute means any relationship (e.g. legal or other similar relationship or transaction) between associated persons that is primarily focused on tax cuts (aggressive tax planning), i.e. deliberately decreasing the tax base or increasing tax loss.

Persons or subjects (entities), which are part of the consolidated group. The Slovak Act on Accounting No. 431/2002 Coll. as later amended does not define associated persons, but implicitly imposes an obligation on the defined dependent entity (consolidated entity) to prepare consolidated financial statements (Section 22). A subsidiary is an enterprise in which another enterprise (the parent company) exercises control or has a controlling influence over it (share or voting rights of more than 50%). A joint venture is an enterprise where one entity (partner) exercises joint control with other entities that control that venture through the exercise of significant influence that is at least 20% of the share capital and joint control is explicitly stated in the contract. An associate enterprise is an enterprise in which another enterprise (investor) exercises significant influence. It holds at least a 20% share in the registered capital, either through direct or indirect participation. It follows from the above that the Act on Accounting defines associated parties with less dependence criteria compared with the Income Tax Act. The consolidated financial statement shall be prepared according to IFRS (Krištofík, Saxunová and Šuranová, 2011).

Associated persons are also persons or entities (subjects) acting in concert with another person or entity (subject) (joint action of persons) in respect to voting rights or a share in the registered share capital, while the shares of these persons or entities are no lower than 25%. Associated persons are all persons and subjects (entities) involved in the above-mentioned relationship, irrespective of whether they are in superior, equivalent or in a subordinate position. Accordingly, all persons and entities (subjects) to whom the above criteria apply are dependent for the purposes of the Income Tax Act (parent company, subsidiary, sister company in the group of companies, as well as shareholders and members of these companies) (Fischerová, 2018, In Daňový a účtovný poradca podnikateľa).

Related to the definition of associated persons, a significant change was made with the amendment of the Income Tax Act which has been in force since 2015. From Section 2 letter n) the word "non-resident" was deleted. This has a direct impact on the application of the arm's length principle on transactions between domestic associated persons. Other than an extension of the personal scope of transfer pricing to domestic associated parties, this change affects the application of the primary adjustment of the tax base according to Section 17(5), as well as the corresponding adjustment of the tax base according to Section 17(6).

Amendment of the Slovak Income Tax Act with effect from 2014 significantly complements the criteria for formal dependence with the concept of factual dependence. According to Section 2 (p) of the Slovak Income Tax Act, the so-called *"persons associated otherwise (other ties)"* are also considered to be associated persons. By this term one understands that a commercial relationship is established solely for the purposes of tax base reduction or tax loss increase as was already stated above.

According to Kočiš (2015), with this definition, there is no requirement to fulfil the quantitative or the purely formal characteristics of dependence and the nature of the business relationship between the persons assessed becomes decisive. In the new definition of dependency, the legislator's intention to extend the personal scope of transfer pricing standards to cases where a reduction in the tax base or an increase in tax loss is not the only objective, but it is one of the primary objectives of a business transaction. The previously mentioned amendment is intended to increase legal certainty for the tax administrator and taxpayers by clearly defining that a business relationship whose main purpose is to reduce the tax base or increase the tax loss in violation of the law is also considered associated for the purpose of transfer pricing. Kočiš (2015) is further of the opinion that the very general formulation of definition extension is likely to be considerably problematic in many practical cases, in particular in the assessment of the same transactions in different contractual relationships in view of different business intentions. The new amendment can have in similar cases a paradoxically negative effect on the legal certainty of tax subjects.

From 2017[96], the Income Tax Act introduced in Section 2 letters ab) the concept of a **controlled transaction** that replaces the concept of a business relationship. A controlled transaction is a legal relationship or other similar relationship between two or more associated persons according to Section 2 letter n) and r), where at least one is a taxpayer with income according to Section 6 (Enterprise Income, Other Self-Employment Income, Lease Income and Income from the Use of Work and Artistic Performance) or a legal entity achieving a taxable income (revenue) from an activity or disposal of an asset, and the controlled transaction does not qualify as a lease giving rise to income under Section 6(3), in case of immovable property not classified under business assets according to letter m), and the lessee is a natural person, who uses this property for personal purposes. In assessing a controlled transaction, the actual content of the legal relationship or similar relationship is taken into account. Kočiš (2019a) states that as from 2018, the associated enterprises definitions are more sensitive to de facto association (control). However, even after the recent changes in Slovak legislation, associated enterprises still do not cover pure de facto association.

Obligations and rights of taxpayers related to transfer pricing (tax adjustments are covered primarily in Section 17(5) and (6) of the Income Tax Act)

"According to section 17 (General provisions Applicable to the Determination of the Tax Base) (5) of the Income Tax Act, the tax base of an associated party pursuant to Section 2 letter n) and r) shall also include the difference between the prices or conditions in controlled transactions differ from prices or conditions which would be applied among the unrelated persons in comparable uncontrolled transactions, as long as such difference results in a reduction of the tax base or increase of tax loss.

At the determination of the tax base of an associated party, it shall also be allowed to include in the tax expenses a proportional part of the expenses (costs) which were incurred by another person to which it is related, as long as[97]*:*

- a) *these expenses (costs) are demonstrably related to the subject of the dependent's activity;*
- b) *the related party would have to bear the expenses (costs) itself or would have ordered the service from independent persons if it had not been provided by a party to which it is associated;*
- c) *the amount of expenses (cost) or price of the service corresponds to the principle of the arm's length principle (according to Section 18(1)); and*
- d) *the party shall submit evidence of the aggregate amount of expenses (costs) related to or incurred in the provision of such service, and their distribution among the beneficiaries of such service."*

The Income Tax Act states in Section 17(6) that:

"Adjustment of the tax base of the associated party in the territory of the Slovak Republic shall be permitted by the tax administration (which will be published on the website of the Financial Directorate) if the tax administration of a country with which the Slovak Republic has concluded a double tax treaty has made adjustments to the taxable person's tax base abroad, which is in accordance with the arm's length principle according to § 18 para. 1. Written notice shall be given by the tax administration (which will be published on the website of the Financial Directorate) to the taxpayer to that effect. If the taxpayer with unlimited tax liability has made the adjustment of the tax base pursuant to paragraph 5 or if the tax administrator has adjusted the tax base of another associated person in the territory of the Slovak Republic pursuant to paragraph 5, which complies with the arm's length principle pursuant to § 18 para. 1, another dependent who is a taxpayer with unlimited tax liability may adjust the tax base for controlled transactions that have been subject to the adjustment referred to in paragraph 5. If an adjustment of the tax base of another dependent person in the territory of the Slovak Republic pursuant to paragraph 5 has been made and a taxpayer with unlimited tax liability applies a tax relief pursuant to § 30a or § 30b, this taxpayer is obliged to adjust the tax base for controlled transactions. If a taxpayer claiming tax relief pursuant to § 30a or § 30b reduced the tax base and at the same time applied the procedure under § 30a para. 8 or § 30b par. 8, another dependent in the territory of the Slovak Republic is obliged to adjust the tax base for controlled transactions pursuant to paragraph 5. At the same time, the taxpayer is obliged to submit to the tax administrator, before the deadline for submitting the tax return or additional tax return, a notice of adjustment of the tax base, the model of which will be determined by the Financial Directorate and published on its website."

96 The amendment of the Income Tax Act effective from 2017 brings several changes and modifications to the definition of associated person.
97 The wording of selected parts of Sections 2, 17 and 18 changed as to the amendment of the Income Tax Act in force since 2017.

A taxpayer with unlimited tax liability who is an associated person and who has carried out a domestic controlled transaction which is subject to a primary tax adjustment on the other side of the transaction (e.g. tax base increase according to Section 17(5)) and who has itself made a reciprocal corresponding tax base adjustment to this adjustment according to Section 17(6) of the Income Tax Act, has a reporting obligation to report this fact to the tax administrator. It has been necessary to file and submit the notice of the tax base adjustment since 2017.

According to Section 17(7) of the Income Tax Act, the taxpayer may ask the tax administrator in written form to approve the use of a specific method of determining the taxable amount of a permanent establishment.

8.3.2 DEFINITION OF TRANSFER PRICING AND BASIC PRINCIPLE IN DOMESTIC LAW

Domestic law currently does not contain a normative definition of transfer pricing as such. However, domestic law does contain the core aspects and what is regulated.

8.4 LEGAL REGULATION AS INCLUDED IN DOUBLE TAX TREATIES

Slovakia has already signed 70 double tax treaties as of 2020. Double tax treaties are concluded based on the OECD Model Tax Convention[98]. Slovakia decided to use the Multilateral Instrument (MLI) to ensure compliance in its double tax treaties through MLI beyond the minimum standard and became a signatory of MLI on 7th June 2017. The provisions outlined for MLI adjustments in the national position of the Slovak Republic do not automatically mean material changes in double tax treaties.

The selected provisions for adjustment by the Slovak Republic must meet with the final position of the other contracting state which it submitted when depositing its national instrument of approval/ratification of the MLI to the depositary. The issued Explanatory Statement to MLI is adhered to by Slovakia. The following Table 56 contains the current status of modifications of relevant double tax treaties (since 1st January 2019) with the impact on bilateral double tax treaties already concluded with Slovakia.

Table 56: Current status to modification of relevant double tax treaties (MLI entry into effect from 1st January 2019)

Contracting state	Ratification	Withholding tax	Other taxes	MAP
Australia	26/9/2018	1/12019	1/7/2019	1/1/2019
France	26/09/2018	1/1/2019	1/7/2019	1/1/2019
Israel	13/9/2018	1/1/2019	1/7/2019	
Japan	26/09/2018	1/1/2019	1/7/2019	1/1/2019
Lithuania	11/9/2018	1/1/2019	1/7/2019	
Poland	23/1/2018	1/1/2019	1/7/2019	1/1/2019
Austria	22/9/2017	1/1/2019	1/7/2019	
Slovenia	22/3/2018	1/1/2019	1/7/2019	
Serbia	5/6/2018	1/1/2019	1/7/2019	1/1/2019
United Kingdom	29/6/2018	1/1/2019	1/7/2019	1/12019
Sweden	Special post ratification procedure			

Source: own elaboration based on the Ministry of Finance of the Slovak Republic (2019) and Slivková (2019).

All double tax treaties with MLI entry into effect from 2019 and 2020 contain amendments of principle purpose test/limitations of benefits (MLI Article 7 – new article on double tax treaties). Not all double tax treaties contain the same amendments in selected articles[99]. The new double tax treaty article (MLI Article 10) for anti-abuse rules for permanent establishments situated in the third jurisdictions was introduced

98 The MLI is implemented in Slovak primary law and published in the Law Collection (wording of MLI both in English and Slovak languages) in compliance with the Readers´ Guidance of the MLI Modifications to the DTT (toolkit OECD).

99 Mutual agreement procedure (MLI Article 16/DTT Article 25), Savings clause (MLI Article 11/DTT Article 1), PE-Commissionaire arrangements and similar strategies (MLI Article 12/DTT Article 5), PE – Specific activities exemption and new anti-fragmentation rule – 13/4 (MLI Article 13/ DTT Article 5), SP – Splitting-up of contract (MLI Article 14/DTT Article 5), SP-Definition of a person closely related to an enterprise (MLI Article 15/DTT Article 5), Corresponding adjustments (MLI Article 17/DTT Article 9), Transparent entities (MLI Article 3/DTT Article 1), Dual resident entities (MLI Article 4/DTT Article 4), Dividend transfer transactions – time limit test (MLI Article 8/DTT Article 10), Capital gains – time limit

only in amendments of double tax treaties with MLI entry in force since 2019 with Israel, Japan, Austria and Slovenia. Corresponding adjustments in double tax treaty Article 9 (MLI Article 17) are implemented in double tax treaties with MLI entry in force since 2019 with France, Japan, Austria, Serbia and Sweden.

The following Table 57 contains the overview of MLI entry in effect from January 1st, 2020 by breakdown of contracting states and particular fields.

Table 57: Overview of MLI entry into effect from 1st January 2020

Contracting state	Withholding tax	Other taxes	MAP
Finland	1/1/2020	1/12/2019	1/1/2020
Georgia	1/12020	1/7/2020	
Ireland	1/12020	1/11/2019	1/1/2020
Malta	1/12020	1/10/2019	
Singapore	1/12020	1/10/2019	

Source: own elaboration based on the Ministry of Finance of the Slovak Republic (2019) and Slivková (2019).

Guidelines of the Ministry of Finance of the Slovak Republic on the application of double tax treaties contains additional information on selected articles.

8.4.1 DEFINITION OF ASSOCIATED PERSONS IN DDTS CONCLUDED BY SLOVAKIA

In connection with the definition and analysis of the so-called factual dependency for the purpose of transfer pricing, it is important to monitor the effect of double tax treaties on domestic legal regulation, especially in the area of potential cases of double taxation.

According to Kočiš (2015), the previous explanatory reports did not pay attention to the amendments of the Slovak Income Tax Act in the field of transfer pricing. The Slovak Republic concludes double tax treaties according to the OECD model. Generally, double tax treaties view Article 9 (Associated Enterprises) in relation to the personal scope of transfer pricing standards much narrower (less detail) compared to the individual provisions in the domestic Slovak legislation (Income Tax Act). The newer (approximately since 2000) and also some older double tax treaties (e.g. with Germany in force since 1984) contain in Article 9 (Associated Enterprises) an adaption of the procedure for individual contracting states to proceed in the case of tax base adjustment or taxation of profits in one contracting state. In some cases (e.g. with Singapore), double tax treaties also contain a clause regarding the non-application of paragraphs related to associated persons in the case of fraud or conscious neglect of duty or negligence.

According to Kočiš (2015), Article 9 of the double tax treaty does not constitute a legal obstacle to the implementation of the primary adjustment of an associated person's tax base in case of factual dependency with another person, if such adjustment is to be carried out within the national tax legislation (primary focus on tax residence). In certain cases, domestic legal regulation may prevent the fulfilment of Article 9, whereas the other contracting state could make a corresponding adjustment to the tax base that is required only if the provisions of the Article 9(1) have been complied with. The result may therefore be an increased risk of double taxation and an overall reduction in the legal certainty of taxpayers regarding the adjustment of the tax base. For this reason, it is necessary to analyse the individual signed double tax treaties between the Slovak Republic and individual contracting states.

Since the definition of associated persons is described in detail and relatively intensely within domestic law, it could be stated that the definition of associated person as stated in the double tax treaties is by default narrower. The definition of associated party as treated by the double tax treaties is relatively general, it frames the characteristics, but it is questionable in relation to selected transactions whether the state can extend this definition. It follows that in certain cases, the corresponding adjustment of tax base may be refused.

test (MLI Article 9/DTT Article 13), Application of methods for elimination of double taxation (MLI Article 5/DTT Article 23), Anti-abuse rule for permanent establishment situated in third jurisdictions (MLI Article 10/DTT new article) (Slivková, 2019).

8.4.2 EXISTING PLATFORMS OF THE WORDING OF ART. 9 IN DDTS

In terms of the content of Article 9, individual double tax treaties can be divided into three categories. The first category contains only the definition of associated persons in paragraphs 1 and 2. The second category also contains the definition like in category 1, but also the procedure of the contracting states in case that one contracting state may make an adjustment to the tax base in accordance with its domestic legal regulation (so-called mirror procedure). Some double tax treaties e.g. signed with Switzerland or Spain include a time test (5 years by default) during which the contracting states do not adjust tax bases (not adjusting the amount of profits/revenues) in accordance with domestic legal regulation. The third category contains double tax treaties, which also contain an anti-abuse clause against the application of paragraphs 1 and 2 of the Article 9. The overview of signed double tax treaties according to individual categories is contained in the following Table 58. The most common are double tax treaties from the second category.

Table 58: Overview of double tax treaties signed by Slovakia according to Article 9 category

Category	EU Member State	Non-EU Member State
I	12	7
II	19	13
III	12	6
Total	43	26

Source: own elaboration.

The detailed breakdown by individual double tax treaties is provided in this chapter´s Annex.

Ministry of Finance of the Slovak Republic issued the Methodological Guideline No. MF/020525/2017-724[100] on the processes under the mutual agreement procedure (MAP). This guideline applies to:

- mutual agreement procedures initiated by the taxpayer based on the double tax treaty, and
- mutual agreement procedures, which are initiated by the taxpayer based on the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (90/463/EEC).

All signed double tax treaties by the Slovak Republic contain provisions for resolving cases by agreement, so they implement mutual agreement procedures.

8.5 TRANSFER PRICING REGULATIONS

8.5.1 THE ARM'S LENGTH PRINCIPLE

The Slovak Income Tax Act describes the basic rules and regulations which must be followed by the taxpayer. As was already mentioned, the tax administrator also issues the methodological guidelines for selected areas in order to increase the legal certainty. The published methodological guidelines are by default based on the OECD Transfer Pricing guidelines and models.

General Transfer Pricing rules have been implemented in Slovak legislation before 2001, but only since 2001 have the specific methods of application of the arm's length principle been introduced by the Slovak Income Tax Act. The arm's length principle was already included in Slovak tax legislation since the formation of the country in 1993. At the very beginning, the arm's length principle had a general form requiring the application of market prices for tax purposes, primarily in cases where the agreed prices differed from market prices and such a difference was not justifiable. The legal regulations from 2000 restricted the arm's length principle application in cases where transaction prices caused a lowering of the tax base compared to a situation when the arm's length principle would be applied. The Slovak Income Tax Act (Section 17(5)) till the end of 2013 was focused only on the tax base lowering in the case of foreign associated persons. Since 2014, the Slovak Income Tax Act more precisely establishes that the tax base includes the differences

100 The Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union was implemented in 2019 by the Act No.11/2019 Coll. on tax dispute resolution rules.

that reduced tax base or increased tax loss. Since 2015, the arm's length principle shall also apply on transactions between domestic associated persons.

The definition of the arm´s length principle is defined in the Income Tax Act (Section 18). *"The arm's length principle is based on a comparison of the terms which were agreed in any business or financial transaction between associated parties and the terms which would have been agreed between unrelated parties in similar business or financial transactions, in comparable circumstances. The review of comparability of the terms is made by confronting in particular the businesses conducted by the parties, including, but not limited to, their production, assembly works, research and development, purchase and sale, the scope of their business risks, the characteristics of the compared property or the service, the terms agreed between the parties to the transaction, the economic environment in the marketplace, and the business strategy. The terms shall be considered comparable if there is no difference at all or if only minor adjustments would compensate any such a difference".*

8.5.2 TRANSFER PRICING METHODS

Comparability analysis is considered to be a key factor in determining the most appropriate transfer pricing method and determining the correct transfer price for tax purposes. If the taxpayers find that both transactions are reliably comparable or if only minor adjustments would compensate any such difference, then they may proceed to verify the correctness of the transfer price by using transfer pricing methods. The purpose of such comparisons is to verify that the price in the controlled transaction is determined correctly and that there is no need to make a primary adjustment to the tax base in accordance with Section 17(5) of the Income Tax Act and with Article 9(1) of the relevant double taxation treaty.

According to Section 18(1), *"the difference referred to in Section 17(5) above shall be determined using any of the methods pursuant to subsection 2 or 3 or their mutual combination or, as appropriate, other methods, which are not described in subsections 2 or 3. Only such methods may be used if they comply with the arm's length principle"*.

Any traditional or other transfer pricing methods according to OECD Transfer Pricing Guidelines can be used while the best method principle (most appropriate) shall be applied. Also, combining more methods is possible when necessary. If appropriate, other methods may be used by Slovak taxpayers, too. The methodological guideline on applying transfer pricing methods (Methodological Guideline No. 21/2013 on application of transfer pricing methods) offers the methodology, formulas and a few illustrative examples on using each method. The mentioned methodological guideline defines the term transaction as a business or financial relationship between two or more persons. Internal comparable transaction is a transaction which is performed by a person with another independent person (uncontrolled transaction) and which could be compared with another transaction of the associated person (controlled transaction). The transactions can only be compared with other transactions when all economically significant characteristics are met (Financial Directorate, 2013).

The methodological guidelines highlight that the content and use of transfer pricing methods are regulated by the OECD Transfer Pricing Guidelines. The methods shall be used for investigation or testing of transactions. Sometimes it is useful to test aggregate transactions, but only if they are of the same kind or are interconnected, closely linked and implemented under similar conditions that affect their valuation.

The guideline (Methodological Guideline No. 21/2013 on application of transfer pricing methods) splits the methods into direct and indirect methods[101] and into unilateral and bilateral[102] categories. For the selection of the most appropriate transfer pricing methods, the following criteria shall be considered:

- the strengths and weaknesses of the selected method,
- the appropriateness of the chosen method in the context of the nature of the transaction to be ascertained by performing a functional and risk analysis,
- the availability of comparable independent information necessary for comparability analysis, and

101 Under the direct method one directly compares the price of the controlled transaction and the price of the uncontrolled transaction. Under the indirect methods, the price of the controlled transaction is adjusted indirectly using other indicators, e. g. gross or net profit margin.

102 The unilateral method examines only one of the contracting parties, usually the one that performs fewer complex functions and bears lower risks. For analysis, both domestic and cross-border entity can be selected. The bilateral method examines both contracting parties of the transaction and their contribution to realised profit. The aggregate profit is subsequently divided among associated persons in accordance with the arm's length principle.

- the degree of comparability between controlled and uncontrolled transactions, including the level of adjustment necessary to eliminate differences between these transactions.

Based on comparability analysis, it is perfectly adequate to exclude any transfer pricing method whose application is not suitable (Financial Directorate of the Slovak Republic, 2013). The amendment of the Income Tax Act in force since 2014 removed the previously preferred preference for using traditional transactional methods over transactional profit methods. However, if in a specific case, the use of traditional transactional methods and transactional profit methods are equally reliable, then traditional transactional methods take precedence. In some situations, the use of transactional profit methods is more suitable. Such cases arise, e.g. when both contracting parties have a unique and valuable contribution in a controlled transaction (e.g. ownership of unique intangible assets) or when they carry out highly interconnected activities. The use of traditional profit methods is suitable in situations when the comparable information from internal or from external sources is not available.

The Income Tax Act presents methods based on a comparison of prices (Section 18(2) and methods based on a comparison of profits (Section 18(3)). The provisions of the Income Tax Act also allow the selection of another method compared to those stated in the act. The used methods must comply with the arm's length principle. If another method is chosen compared to those stated in the act, then the taxpayer must justify this selection.

The following are the methods based on a comparison of prices (as stated by the Income Tax Act according to Section 18(2)):

a) **Comparable uncontrolled price method** *"consisting of a comparison of the price of a transfer of property or service agreed between associated parties, and the comparable fair market price agreed between unrelated parties; if there is any difference between the two prices, the price agreed between associated parties shall be replaced with the fair market price, which would be used by unrelated parties in a comparable business or financial transaction at similar terms"*. This method is mainly used for transactions with tangible (e.g. raw materials) and intangible assets (e.g. licence fees) and financial transactions (interest rates). The application of this method is based on the comparability analysis that examines the comparability of terms and conditions, market and economic environment in controlled and uncontrolled transactions;

b) **Resale price method**, *"whereby the price of the transfer of the assets purchased by an associated party is converted to the fair market price using the price, at which the associated party resells the assets to an unrelated party, after deducting the trading margin, which is usually applied by comparable independent resellers"*. This method is used mainly for distributors of products;

c) **Cost plus method**, *"whereby the fair market price is determined with reference to actual direct and indirect costs of the assets or services transferred between associated parties, increased by the trading margin applied by the same supplier vis-à-vis unrelated parties, or by a trading margin, which would be applied by an unrelated party in a comparable transaction on comparable terms"*. This method is mainly used for transactions related to the manufacture and sale of semi-finished products or finished products (goods or services) which do not include high added value, e.g. in the form of unique intangible assets. It is usually used to value long-term contracts (e.g. in contractual manufacture).

The following are the methods based on a comparison of profits (Income Tax Act, Section 18(3)):

a) **Profit split method**, *"which is based on a split of the anticipated profit generated by associated parties, which would be expected from unrelated parties engaged in a joint venture, while respecting the arm's length principle"*. The use of this method is appropriate in situations where the transactions are highly integrated and when the contractors contribute in a unique way within the transaction or when they own valuable intangible assets;

b) **Net trading margin method** *"used to determine a profit margin in a business or financial transaction between associated parties in relation to costs, revenues or other basis, which is then compared with a profit margin used vis-à-vis unrelated parties"*. This method can be applied only after consistent implementation of functional and risk analysis. The use of this method is limited, e.g. in cases when the contracting parties of a transaction possess valuable intangible assets or their contribution to the transaction is unique.

In the conclusion of the Guideline on the application of transfer pricing methods, it is stated, that in general, the tax administrator and the taxpayer should come to a reasonable compromise, taking into account possible inaccuracies in the methods and preferring a higher degree of comparability plus a more direct and closer relationship to the transaction.

8.5.3 COMPARABILITY ANALYSIS/COMPLIANCE ANALYSIS OBLIGATION

Regarding comparability analysis, the Slovak domestic legal regulation refers to Chapter III (Comparability analysis) of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. The methodological guidelines on the application of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and Transfer Pricing Legislation in the Slovak Republic states that the OECD Transfer Pricing Guidelines put great emphasis on comparability analysis, starting with initial analysis of conditions of a controlled transaction, through selection of the most appropriate transfer pricing method, identifying potential comparable transactions or subjects, ending with a decision on whether the transaction checked conforms to the arm's length principle.

Comparability analysis in Slovak domestic legislation is primarily linked to Section 18(1) of the Income Tax Act and by an amendment in force since 2014 of this section. Slovak domestic legal regulation refers to the wording of OECD Guidelines and adheres to its stated rules. Slovak law has created conditions to eliminate the differences in the interpretation of comparability between different countries.

The concept of Slovak domestic legal regulation on comparability analysis is, as was already stated, based on the rules contained in the OECD Transfer Pricing Guidelines. It means that Slovak legislation follows (also in practice) the guidelines on comparability analysis outlined in the Transfer Pricing Guideline (Chapter III). As was already stated, the OECD Transfer Pricing Guidelines are not legally binding but acceptable as an explanatory instrument. The Slovak Income Tax Act does not contain a more detailed description of the rules under which the comparability analysis is to be carried out.

Although domestic legislation does not specify an obligation to always execute a comparability analysis, on the other hand, it is assumed that the comparability analysis shall be performed at every determination of the transfer price. The goal of the comparison of the transactions is to test if the price is determined correctly and if there is any need to make the primary adjustment of the tax base in accordance with Section 17(5) of the Income Tax Act and Article 9(1) of the relevant double tax treaty. Experts in most cases recommend to their clients to have prepared a complete (full-scope) documentation as the costs related to the preparation of this type of documentation could be significantly lower than compared with potential tax base adjustments including related penalties (Kočiš, 2019b).

According to the guidelines on the application of transfer pricing methods, based on the analysis of comparability factors, the taxpayer may exclude any methods whose use is unsuitable.

The new guidelines (Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 to determine the content of documentation according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended) specifies the obligations and mentions the obligation of elaborated comparability analysis only in specific documentation (Local File) for full-scope transfer pricing documentation. According to this new guideline, the local file must contain the selection of testing for the purpose of comparability analysis including the justification of the selection if relevant (point 6). Further, the local file must also contain the internal comparable transactions, external comparable transactions or data of independent persons, including a description of sources and methods of obtaining this data and comparability analysis (information on the factors determining the comparability of controlled transactions with uncontrolled transactions, property or service characteristics, functional analysis, contractual terms and conditions, economic environment and specific business strategies) (point 7).

The obligation of a taxpayer is to find comparable data and defend the prices used in transfer pricing documentation. Here we see the principle of independent relationship used, which is based on a comparison of the conditions in controlled transactions with those in uncontrolled transactions.

If the taxpayer performs a comparable transaction with both associated and independent persons, then an internal uncontrolled transaction can be used as a comparison. In most cases, it is considered more appropriate to use comparable data obtained from an internal uncontrolled transaction than data from an external uncontrolled transaction. Only when there is no internal comparable transaction, is it necessary to examine external comparable data. External comparable data can be obtained from several databases. For this purpose, the commercial databases are often used in the conditions of the Slovak Republic (e.g. Amadeus, ORBIS, TP-Catalyst or other).

The preference to use domestic comparables is not directly laid out in domestic legislation. The general rule is to use domestic comparables first and if there is no other possibility, then the next step is to use foreign comparables. The Financial Administration of the Slovak Republic does not use secret comparables for transfer pricing assessment purposes. The use of the arm's length range and statistical measurements is not directly defined in domestic legislation, but in practice followed via the recommendations of the OECD Transfer Pricing Guidelines (Karelová and Slivková, 2019). As was already stated, the definition of comparability adjustments is outlined in Section 18(1) of the Income Tax Act.

Comparability analysis is the first step when applying for an Advance Pricing Agreement (APA). The Slovak Income Tax Act does not require the use of local comparables in a benchmarking study or comparative analysis. It is enough for firms to use the Amadeus database[103] and maintain their own internal comparables. The Slovak tax authority considers the interquartile range as arm's length in cases where the transnational net margin method is applied.

8.5.4 ADMINISTRATIVE APPROACHES TO AVOIDING AND RESOLVING TRANSFER PRICING DISPUTES

The new Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union[104] (in force since July 2019 in the Slovak Republic) streamlines the mechanism of settlement concerning disputes in the EU. The new Act No. 11/2019 Coll. on dispute settlement rules concerning taxation[105] combines and tries to unify the procedure according to the Directive (2017/1852) and divides groups into another EU member states (procedure for the avoidance of double taxation); states with which the Slovak Republic has concluded a double tax treaty[106] (procedure for the avoidance of double taxation based on the treaty) and contracting states where such disputes arise from the interpretation and application of an international double tax treaty in connection with the adjustment of profits of associated enterprises ratified and declared in the manner provided by the Notification of the Ministry of the Interior of the Slovak Republic No. 562/2006 Coll.[107] (procedure for the avoidance of double taxation based on the Convention).

8.5.5 PROVISIONS GOVERNING SPECIFIC AREAS

Domestic legal regulation does not contain guidelines specific to the valuation of controlled transactions involving **intangible property** (applied general transfer pricing rules and following the OECD Transfer Pricing Guidelines) or specific guidelines or special measures regarding hard to value intangibles.

Similar to intangibles, there is no specific guideline on **intra-group services**. One understands that there is no simplified approach to low value-adding intra-group services. On the other hand, the increased cost attitude is generally accepted in the case of low value-adding intra-group services, like e.g. accounting or administrative support activities (5%). Slovakia has relatively many so-called shared customer centres or the Slovak subsidiaries often provide administrative, accounting and similar support to other entities located abroad (Slovak Investment and Trade Development Agency, 2019).

103 Or any other databases (e.g. ORBIS, TP-Catalyst or RoyaltySource).

104 It applies to disputes between Member States and covers only those situations that arise as a result of transfer pricing or the attribution of profits to a permanent establishment.

105 The act also regulates the procedure for resolving any disputes with the Contracting States with which the Slovak Republic has concluded double tax treaties with regard to their interpretation and application. Further, this act regulates the procedure for resolving disputes of the Slovak Republic with the Contracting States of Convention 90/436/EEC of 23 July 1990, on the elimination of double taxation in connection with the adjustment of profits of associated enterprises as amended, insofar as such disputes result from its interpretation and application.

106 Where such disputes result from the interpretation and application of the double tax treaty (for the first two mentioned groups).

107 Convention on the accession of the Czech Republic, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Slovenia and Slovakia to the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises – Notification of the Ministry of the Interior of the Slovak Republic No. 562/2006 Coll.

There is also no specific legislation or regulation on cost contribution arrangements for **intangibles and R&D**. Slovak domestic legislation has no rules on safe harbours concerning certain industries, types of taxpayers or types of transactions[108].

There is also no specific legislation or regulation on **business restructuring**, only the Methodological Guidelines on the application of OECD Guidelines refer to the OECD Guidelines and provide information on Chapter IX (Business Restructuring). There are no further specific rules treating **intercompany financing**. However, it is generally expected from the taxpayer that the adequate arm's length consideration for the financing services shall be determined according to the financial market and based on similar financing services rendered under similar circumstances (credit rating, duration, guarantee, sum, etc.) as between unrelated comparable parties. By the amendment of the Income Tax Act in force since 2015, the thin capitalisation rule was implemented (tax deductible expenses limited by the indicator of 25% of EBITDA) as another measure against aggressive tax planning.

8.6 TRANSFER PRICING DOCUMENTATION

According to Section 18(1), the taxpayer is obliged to keep documentation on controlled transactions and the method used in determining the pricing method and conditions that would be applied between independent persons in comparable transactions.

The Ministry of Finance of the Slovak Republic according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended and Section 160(2) of the Tax Procedure Code No. 563/2009 Coll. and amending certain other acts to ensure uniform practice issued guidelines (Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 to determine the content of documentation according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended) determining the content of documentation on used methods in order to determine the prices or conditions in controlled transactions, which would be applied among independent persons in comparable relationships. The taxpayer is obliged to keep transfer pricing documentation even if no adjustment to the tax base under Section 17(5) of the Income Tax Act occurred. Transfer pricing documentation is a collection of information, data and facts that demonstrate and explain the methods and procedures that determine price in controlled transactions. Transfer pricing documentation should serve as evidence that the taxpayer in business with associated parties is following transfer pricing rules.

The content definition of a taxpayer that is considered an associated person according to Section 2(n) of the Income Tax Act or a taxpayer executing transactions with a permanent establishment to the extent defined according to Section 2(r) of the Income Tax Act is based on the principles and rules laid down by the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council, of 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD).

Whereas the last version of the methodological guidelines to determine the content of documentation is perceived positively mainly due to the simplification of duties for small and medium-sized entrepreneurs, frequent changes to individual guidelines can be considered a negative. Currently in force is the 5th version (No. MF/019153/2018-724) of this guideline. The following is the overview of the guidelines since 2009:

- Guidelines of the Ministry of Finance of the Slovak Republic No. MF/8288/2009-72 on determining the content of documentation and valuation method used by a taxpayer according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended;
- Guidelines of the Ministry of Finance of the Slovak Republic No. MF/8120/2012-721 on determining the content of documentation and valuation method used by a taxpayer according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended;
- Guidelines of the Ministry of Finance of the Slovak Republic No. MF/011491/2015-724 on determining the content of documentation according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended; and

108 Similarly, the Slovak domestic regulation and guidelines do not contain nor signification measures for SMEs or another segment of taxpayers (e. g. domestic transactions).

- Guidelines of the Ministry of Finance of the Slovak Republic No. MF/014283/2016-724 on determining the content of documentation according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended.

The taxpayer shall prepare transfer pricing documentation prior to the controlled transaction based on the information available at the time. Subsequently, during its realisation, the transfer price shall be monitored to see if it has been set out correctly. Under the assumption that no conditions or circumstances that would have impacted the valuation method occurred, the taxpayer may refer to information stated in the transfer pricing documentation from the previous taxation periods. The taxpayer is obliged to retain the transfer pricing documentation for the period during which the right to levy a tax or tax difference has not expired for the relevant taxation period (according to Section 69 of Tax Administration Act No. 563/2009 Coll.). In effect from 2014, the deadline for the taxpayer to submit a transfer pricing documentation at the tax administrator's request has been reduced to 15 days (previously 60 days). The deadline of 15 days for submitting documentation cannot be extended. Generally, due to this short period, it is recommended having the documentation prepared in advance. Transfer pricing documentation is generally not considered as an annex to a tax return.

A request by the tax administration or financial directorate for documentation for the relevant tax period may not be sent earlier than the first day following expiration of the tax return submission period for that tax period (according to Section 49 of the Tax Procedure Code). At the same time, the tax administrator has the right to require the submission of documentation at any time when it is justified, i.e. not only during the tax audit. The taxpayer shall submit the records in the state language. The tax administration or financial directorate may, upon the taxpayer's request, agree that the records be submitted in a language other than the Slovak language.

Further, according to Section 18(11) of the Income Tax Act, the correct use of the method and quantification of the difference according to Section 17(5) is verified by the tax administration or financial directorate during the tax audit based on the arm's length principle, used method and the comparability analysis.

When submitting the documentation, taxpayers may experience several complications not only in terms of content, but also by lack of knowledge between taxpayers that arises in a mutual relationship (controlled transaction), i.e. the documentation was not continuously prepared.

The obligation to keep transfer pricing documentation came into effect from 2009. Since 2015, this obligation applies not only to foreign associated persons, but also to domestic associated persons. Pursuant to domestic legal regulation, all associated parties are obliged to prove the applied method for determining the prices of controlled transactions (both domestic and cross-border) between associated parties and to keep relevant documentation authorising this method.

Slovak domestic legal regulation provides no exemption from transfer pricing documentation obligation. However, there exists simplification on documentation requirements for individuals, small and medium-sized enterprises and domestic transactions. There are also no formal requirements for functional and risk analysis and no requirements for benchmark analysis for transactions of individuals, small and medium-sized enterprises and insignificant domestic transactions.

The new guidelines (Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 to determine the content of documentation according to Section 18(1) of Income Tax Act No. 595/2003 Coll. as later amended) provides a relatively significant simplification and clarification of the requirements for documentation preparation.

- Most taxpayers do not need to keep documentation of insignificant domestic controlled transactions (except taxpayers applying for tax relief under Section 30a of the Income Tax Act) and insignificant cross-border controlled transactions (except taxpayers conducting controlled transactions with associated parties from non-contracting states – in this case the basic documentation must be kept). If there are no documentation requirements, then the obligation is fulfilled by filing the tax return and filling in the relevant annexes;
- For the sake of clarity and with the intent to reduce the administrative burden, keeping the abridged documentation, which has not yet been specified in a specific form, was designed in order to fill in the information in the structure as set out in the annex; and

- For selected taxpayers, the documentation obligation is considered to be fulfilled by duly completing tax returns in the sections concerning the associated persons.

If according to the Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 to determine the content of documentation according to Section 18(1) of Income Tax Act No. 595/2003 Coll. as later amended, in order for the taxpayer to fulfil documentation duty, it is sufficient to properly fill in the forms of an income tax return (for both personal and corporate income taxes) relating to transactions of associated persons, but if the taxpayer does not fill these parts properly, then the taxpayer on the basis of a tax administrator call will have to submit abridged documentation, which is understood as the completion of Annex of the Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 – Overview of transactions with associated parties (part of the tax return).

If the legal entity meets the conditions of an associated person according to the Slovak Income Act and ticks the box in the first part of the tax return, subsequently the taxpayer shall fill in the table of transactions with associated persons according to Section 2 (n) (to the row 100, second part), if in the corresponding tax period there were controlled transactions with the associated person(s). The mentioned table is included in Annex 2 of the tax return and is divided into 2 columns of revenues and expenses within the categories affected by the transactions that affected row 100 (profit/loss before tax) in the tax return (Financial Directorate of the Slovak Republic, 2017b).

The content of documentation in Slovak domestic legal regulation is determined by the following sources:

- Income Tax Act No. 595/2003 Coll. as later amended – Section 18(1),
- Tax Procedure Code No. 563/2009 Coll. as later amended – Section 160(2),
- Guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 to determine the content of documentation according to Section 18(1) of the Income Tax Act No. 595/2003 Coll. as later amended (this guideline replaces the Guideline No. MF/014283/2016-724),
- OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, and
- Resolution of the Council and of the representatives of the governments of the Member States meeting within the Council, of 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD).

The guidelines for determining the content of the documentation determines the minimum scope of documentation and the tax administrator may exhort the taxpayer to submit additional information providing that prices used in the controlled transactions are in accordance with the arm's length principle. The guideline No. MF/019153/2018-724 shall be used for the first time when submitting documentation for a tax period beginning after 31st December 2017.

The guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724 and No. MF/014283/2016-724 divide taxpayers (based on the types of controlled transactions) into three groups according to predetermined criteria and on this basis recognises 3 types of documentation (Article 3 Scope of documentation), which differ from each other in scope of information (there is no exemption from documentation elaboration, but three types of documentation may be prepared). While the categorisation of documentation types in the past was based primarily on the taxpayer category, the new guidelines introduce categorisation based on the controlled transaction group.

The new guideline (No. MF/019153/2018-724) affects mainly small and medium-sized enterprises and defines the content of documentation as follows:

The purpose of **complete documentation (full scope)** is to document the stetting of prices of controlled transactions of a taxpayer and other facts affecting the setting of prices of these controlled transactions. The complete documentation is a set of data and facts that prove and explain how prices are set in controlled transactions and demonstrates compliance with the arm's length principle (according to Chapter V Documentation of the OECD Guidelines on Transfer Pricing) and is divided into a general group file (Master File) and specific file (Local File). The general part contains information that gives an overall picture of the group of associated parties, while the specific part contains specific information related to the taxpayer and to the controlled transactions in which the taxpayer is engaged. The content of this type of documentation is broadly harmonized with the content of the documentation recommended by the OECD under the project BEPS.

The purpose **of basic (simplified) documentation** is to document the price determining behaviour of controlled transactions of the taxpayer and other facts, which have an impact on price setting. The basic documentation is a set of data and facts which proves and explains how prices in controlled transactions are created. Similarly, to complete the documentation, the basic documentation consists of a master and local file.

Abridged documentation (extra simplified documentation) contains information in a structure according to the annex of the guidelines. This type of documentation is in prescribed form and mentions only significant controlled transactions. For insignificant controlled transactions, it is obligatory to complete the income tax return for the relevant tax period.

The scope of the documentation depends on the type of transaction being checked (significant/insignificant and domestic/cross-border). The new guideline (No. MF/019153/2018-724) cancels the minimum transaction value of 1 mil. EUR above that the transaction must be described. The new guidelines on TP documentation changes the approach on how the documentation shall be kept. The previous guidelines determined which documentation must be kept based on the category of taxpayers, while now, the current guidelines set which category of documentation must be prepared based on the transaction. According to the new rules, the size of principal is being investigated when preparing the documentation (previously there was a connection to the size of interest).

a) **Abridged documentation**. This document consists only of general information of the group and the description of related transactions. The abridged documentation shall be kept for:
   - Significant transactions by the taxpayer where the taxpayer is obligated to have the financial statements verified by an auditor according to Section 19 of the Act on Accounting for the relevant tax period;
   - Significant transactions of natural persons determining the tax base or tax loss according to Section 17 of the Income Tax Act;
   - Significant controlled transactions with associated persons, who are taxpayers with unlimited tax liability (according to Section 16(2) of the Income Tax Act), except controlled transactions in relation to permanent establishments of those taxpayers located in abroad;
   - Significant controlled transactions of the taxpayer who is consolidating or a consolidated accounting entity according to Section 22a of the Act on Accounting, for domestic controlled transactions with other persons, who are consolidating or a consolidated accounting entity according to Section 22a of the Act on Accounting;
   - Insignificant controlled transactions of the taxpayer applying for tax relief in the tax period.

b) **Basic (simplified) documentation**. This document consists of a master file and a local file. The local file contains among other things the analysis of functions, risks and assets of the taxpayer and relevant associated persons in the context of a certain transaction. The basic documentation is obliged to be kept by those taxpayers who do not keep the abridged or complete documentation. Furthermore, the basic documentation shall be kept for:
   - Significant cross-border controlled transactions, if the taxpayer's total operating and financial revenues per tax period exceed 8 mil. EUR;
   - Controlled cross-border transaction or group of controlled cross-border transactions that can be merged and if the value of this controlled transaction or group of transactions exceed 1 mil. EUR;
   - Significant domestic controlled transactions, if the taxpayer claims a tax relief in the tax period;
   - Non-significant transactions with an associated party who are taxpayers in a non-contracting state[109].

c) **Complete documentation (the full scope)**. This documentation consists of a master (detailed information regarding the entire group) and a local file (detailed information regarding the Slovak entity and its related transactions performed). The complete documentation is more extensive compared to basic documentation in both master and local files and shall be kept for:
   - Significant cross-border transactions of the taxpayer who reports accounting results in the individual financial statements according to IFRS;

109 Not signed the relevant double tax treaty, tax and bank information exchange agreement or agreement in tax administration cooperation.

- Cross-border controlled transaction or a group of cross-border controlled transactions that can be merged, with the value of such a controlled transaction or group of transactions exceeding 10 mil. EUR;
- Significant controlled transactions with associated persons resident in non-contractual counties;
- Controlled transactions where the taxpayer requests the tax authority to issue a decision on approving the TP method (APA);
- Controlled transactions where the taxpayer requests an adjustment of the tax base (Section 17(6) of the Income Tax Act), except for adjustment of the tax base in relation to domestic controlled transactions;
- Controlled transactions where a tax dispute settlement mechanism has been requested for the relevant tax period (application of Article 25 of the double tax treaties (Mutual Agreement Procedure));
- Significant cross-border controlled transactions of the taxpayer claiming tax relief in the relevant tax period.

A significant transaction is understood for the purpose of the guideline to determine the content of transaction documentation, which fulfils significant characteristics according to Section 17(9)[110] of the Act on Accounting or according to Commission Regulations (EC) No. 1126/2008 of 3 November 2008, adopting certain international accounting standards in accordance with Regulation (EC) No. 1606/2002 of the European Parliament and of the Council. The taxpayer doesn't need to prepare any type of documentation in relation to transactions with no effect on tax base.

According to Section 18(12) of the Income Tax Act, the taxpayer is obliged to keep the documentation during the period stipulated by special regulation (Section 69 of the Tax Procedure Code of the Slovak Republic No. 563/2009 Coll. as later amended). Depending on the situation, it is for five years after the end of the year in which they were obliged to submit the tax return or where the taxpayer was liable to pay the tax without having to file a tax return or where the taxpayer was entitled to claim the amount under special regulations. If before the period expiration an action has been taken to charge a tax or a tax difference or claim an amount under special regulation, the time limit shall run again from the end of the year in which the tax subject was informed. If charging a tax or a tax difference or filing a claim for the amount according to special regulation, it can be assessed no later than ten years after the end of the year where there was an obligation to submit the tax return or when the taxpayer was obliged to pay the tax without the obligation to submit the tax return or in the year in which the taxpayer is entitled to claim the amount according to special regulations. It means in practice that the tax authority can assess a tax difference (charge a tax or tax difference or claim an amount under special regulations) up to 10 years after the end of the year, in which the obligation to submit a tax return has arisen, so the tax return can be subject to a tax audit for a maximum of 10 finished taxation periods (11 calendar years).

According to Section 18(13) of the Income Tax Act[111], the taxpayer shall submit the documentation to the tax administrator, Financial Directorate or to the Ministry of Finance together with the application if the taxpayer requests:

a) A tax base adjustment according to Section 17(6), i.e. in cases where the tax administrator allows a tax base adjustment of an associated person in the Slovak Republic, if the tax administrator from another contracting state made an adjustment of the tax base in accordance with the arm's length principle; and
b) An initiation of the mutual agreement procedure under the relevant article of the double tax treaty relating to the elimination of double taxation of associated persons and Convention 90/436/EEC from 23 July 1990 on the elimination of double taxation in connection with the adjustment of profits of associated enterprises.

In Slovakia, the DAC4/CbCR notification obligation is imposed on all entities of the transnational group companies (including branch and permanent establishments) with a consolidated turnover of over

110 *"Information shown in the financial statements shall be valued in terms of significance; it must be useful to the user as well as comprehensible, comparable and reliable. Information shall be considered significant if its absence or incorrect presentation in the financial statements could influence the judgement or decision-making of the user"* (Article 17(9) of the Act on Accounting).

111 Income Tax Act No. 595/2003 Coll., as later amended.

750,000,000 EUR. In case of a failure to fulfil the notification obligations, a penalty of up to 3,000 EUR can be imposed. The tax office may impose a fine of up to 10,000 EUR for failure to report by country.

As was already stated, according to Section 18(1) of the Income Tax Act, the taxpayer must keep the documentation. The Income Tax Act contains no provisions on exemption from documentation obligation. Even the new guidelines on documentation does not use the term "exempt", but the guidelines state several situations where by filing the annex to the tax return the taxpayer fulfils the obligation for documentation preparation (e.g. non-significant domestic transactions or public administration entities).

8.7 ADVANCE PRICING AGREEMENTS IN THE DOMESTIC LAW OF SLOVAKIA

The procedure of APA application is treated in the Income Tax Act and in the methodological guidelines.

According to Section 18(4) of the Slovak Income Tax Act, *"a taxpayer may file a written request to the tax administration (tax administrator posted on the website of the Financial Directorate) asking to issue a decision on the approval of the use of a specific method or other method (decision on the approval of the valuation method) no later than 60 days before the beginning of the tax period during which the agreed valuation method will apply. The tax administration shall issue a decision on the approval of the valuation method valid for no more than five tax periods. Upon the taxpayer's request, filed no later than 60 days prior to expiry of the period specified in the decision on the approval of the valuation method, the tax administration (tax administrator posted on the website of the Financial Directorate) may issue a decision on the approval of the valuation method applicable for not more than next five tax periods, if the taxpayer demonstrates that no change occurred in the conditions under which the previous decision on the approval of the valuation method was issued".*

If according to Section 18(8), the taxpayer fails to comply with the deadline for filing the request approval on the use of the valuation method, the application shall be deemed not to have been submitted. This fact will be announced by the tax administrator, which shall be published on the website of the Financial Directorate and no contribution paid will be transferred back to the taxpayer.

By this procedure, taxpayers can approve the chosen methodology and avoid potential disputes as far as the method is concerned. Currently, only the Tax Office for the Selected Tax Entities [Úrad pre vybrané daňové subjekty] (recently renamed as the „Office for Selected Economic Entities" [Úrad pre vybrané hospodárske subjekty]) can potentially approve not only the methods, but also the set of data used for determining the transfer price (no transfer prices themselves, no applicable mark-ups or margins are part of the approval process).

The application for an APA shall be submitted to the specialized Office for Selected Economic Entities based in Bratislava. The application for approval of the use of the method(s) shall be submitted to this tax office in written form. There is no illustrative form for applying for an APA, it must by formulated by the taxpayer. However, according to Section 18(6) of the Income Tax Act, this application must contain a few essential elements.

An application for transfer pricing method approval must contain transfer pricing documentation (according to subsection 1) and the following:

- identification of persons in assessed controlled transaction(s), namely first and second name, business name, residence or registered office, place of business, tax identification number and organization identification number if assigned;
- tax period to which the approval decision should apply;
- description of controlled transaction;
- estimated value of considered controlled transaction; and
- suggested transfer pricing method.

As was already stated, the decision to approve the transfer pricing method is valid for a maximum of five taxation periods. Afterwards, the taxpayer may request the tax authority to issue a further approval decision on the use of the transfer pricing method for up to five additional tax periods. This must be requested at least 60 days prior to the expiry of the approval decision.

Types of APAs in domestic law

According to Section 18(5) of the Income Tax Act, the taxpayer may submit a request for unilateral, bilateral or multilateral approval of a transfer pricing method (advance pricing agreement). The requests differ whereas the method is approved by the tax authority of one state or by the tax authorities of two states. If the taxpayer requests approval of the method for domestic controlled transactions, it is always a unilateral approval of the method. In this case, only the Slovak tax authority is involved in the process of approving the method. If the taxpayer requests approval of the method for foreign controlled transactions, it is a bilateral or multilateral approval of the method. Then the approval method is carried out based on signed double tax treaties and the tax authorities of two or more states participating and approving the method. When issuing a decision approving the use of the valuation method based on the application of a double tax treaty, the competent authorities may also agree to use the valuation method for the taxation periods prior to the application. If, as a result of the decision to approve the use of the valuation method based on the application of the double tax treaty, the tax base is adjusted, such adjustment is not considered to be in breach of the arm's length principle and by filing an additional tax return, the taxpayer does not commit an administrative offense under a special regulation. If no agreement is reached, then the method can only be approved by the Slovak tax authority. Then it is only unilateral method approval.

Since 2017, there has been a change in the fees for applying an APA. It no longer depends on the particular value of the business transaction, but it is determined as a fixed amount. The fee in the case of a unilateral APA is in the amount of 10,000 EUR (for domestic controlled transactions). A fee in the amount of 30,000 EUR shall be paid when requesting a bilateral or multilateral APA based on the double tax treaty (for cross-border controlled transactions). The application fee for APA approval is due without a payment request or call from the tax office and is payable at the time of the submission of the application. If the taxpayer fails to do so, the tax authority will send the written request to pay this fee within 15 days. If even after the written request the fee is not paid within the prescribed period or is paid by an incomplete amount, the application shall be deemed as not to have been lodged. This fact is then subsequently reported and published by the tax administrator which will be published on its website by the Financial Directorate and subsequently no reimbursement is returned to the taxpayer. If the tax administrator publishes on the website a notice refusing a request, any consideration paid will not be refunded to the taxpayer (Income Tax Act, Section 8(7)).

The Income Tax Act allows the tax administrator, which is published on the website of the Financial Directorate, to change or revoke issued approval in the following cases (Section 8(10)):

- the tax administrator shall revoke the issued approval if the decision was made based on inaccurate or false information provided by the taxpayer;
- the tax administrator shall revoke or change the decision to approve the method if the substantive conditions under which the decision on method approval have been changed and the taxpayer does not request for its change;
- the tax administrator may revoke or change the decision on method approval if the taxpayer so requests while demonstrating that the substantive conditions under which the decision was issued have been changed.

The decision to approve the use of the valuation method cannot be appealed. If the tax administrator does not grant the approval request, the tax administrator which is published on the website on the Financial Directorate, sends the taxpayer a written notice, whereby no decision is given (Section 18(9) of the Income Tax Act). As was already mentioned, Slovak domestic legal regulation does not specify the hierarchy of methods. The taxpayer shall select the most appropriate method.

The following Table 59 contains the available statistics on APAs between 2016 and 2018. The comparison with other EU member states shows that the use of an APA tool is not typically used by Slovak taxpayers. During the investigated period, neither bilateral or multilateral APAs were requested, granted or in force[112].

112 We were unable to obtain more detailed statistics on APAs due to tax secrecy.

Table 59: Number of APAs in Slovakia

	2016 EU/non-EU	2017 EU/non-EU	2018 EU/non-EU
Total number of APAs in force of the year	1/0	7/0	11/0
Total number of unilateral APAs in force at the end of the year	1/0	7/0	11/0
Total number of bilateral and multilateral APAs in force at the end of the year	0/0	0/0	0/0
Number of APA requests received in the year	5/2	11/0	3/0
Number of APAs granted in the year	5/2	4/0	1/0

Source: own elaboration based on European Commission (2018a, 2018b and 2019a)

In 2014, the Financial Directorate of the Slovak Republic issued the Methodological Guideline on approving specific transfer pricing methods according to Section 18(4) and (5) of the Income Tax Act 595/2003 Coll. as later amended (Internal Steering Act No. 65/2014). The aim of this methodological guideline is to describe in detail the procedure for applying the provisions as stated in Section 18(4) and (5) according to which the taxpayer has the right to request the tax administrator to issue a decision to approve the use of a transfer pricing method (APA). This guideline should help the taxpayer to verify in advance, before carrying out a transaction with an associated person, that the proposed valuation method of the transaction complies with the arm's length principle. The guideline is composed of 9 sections and 5 annexes in the following structure:

1st Section Aim and basis definitions of terms used in the guideline,

2nd Section Types of measures prior to valuation (unilateral, bilateral and multilateral APAs),

3rd Section Procedure for decision approval on used valuation methods,

4th Section Data collection,

5th Section Preliminary discussions,

6th Section Submission of an application,

7th Section Analysis and evaluation,

8th Section Conclusion of precautionary measure, and

9th Section Monitoring of conclusion of precautionary measure, potential changes or cancellations.

Annexes to this guideline also contain an illustrative model for notifying a failure to comply with the request and an authorisation for the use of a valuation method, together with the illustrative model notice on decision annulment. Since 2018, the Office for Selected Economic Entities has been given capacity to issue "binding rulings" in the area of APA.

Although it was not possible to obtain a more detailed statistical breakdown for APAs due to tax secrecy, it can be stated that individual applicants have a diverse distribution of sectors (e.g. pharmaceutical, distribution, wood and wood-production, IT or service-providers) with the most frequent occurrence of companies in the automotive sector. Representatives of the Financial Administration of the Slovak Republic are aware of the fact that fees related to APAs are among the highest in the EU. However, the approval process is very demanding and lasts a longer period. The potential future reduction of fees would probably directly affect the process quality and it would also seem important to consider the target group. No significant changes in this area are currently planned. The possibility to request an APA is most frequently used by companies operating in the automotive industry (Karelová and Slivková, 2019).

Bilateral and multilateral APA

Currently there are no bilateral and no multilateral APAs approved in Slovakia (European Commission, 2018a, 2018b and 2019a).

8.8 PENALTIES FOR BREAKING THE RULES RELATED TO TRANSFER PRICING

Fines may be imposed on taxpayers for transfer pricing when they fail to perform some of their obligations. In Slovak practice, it is possible to identify several types of fines that could be imposed by tax offices on associated parties in accordance with the Income Tax Act (Section 17(5), (6), Section 18 and Section 18a) and the Tax Administration Act (mainly Sections 154 Administrative offences, 155 Penalties and 156 Interest for late payment).

The most frequently penalties in the field of transfer pricing are:

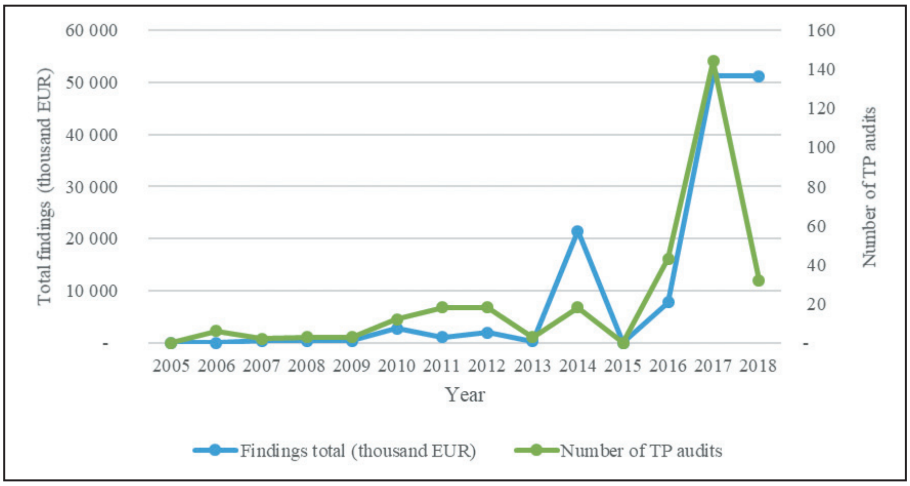
- penalty for failure to increase the income tax base,
- penalty for failure to elaborate the transfer pricing documentation, and
- penalty for unauthorized corresponding adjustment of the tax base (Ronnes, 2018).

The Financial Administration of the Slovak Republic, or more precisely the Office of Selected Economic Entities, mainly focuses on group services, licence fees and functions, and risks and their impact on determining transfer prices during tax audits. They investigate whether the selling prices of products, goods and services are in accordance with the arm's length principle. During a tax inspection focused on transfer pricing, they generally assess all items that appear in the accounts. In the case of licence fees, dividends and interests, the final recipient is assessed. Then it is analysed whether the transaction could be exempt from withholding tax according to the Income Tax Act and signed double tax treaty or based on the relevant EU directive. The assessment of the ultimate beneficial owner of the income and the adjudication of prices from dividends, licence fees and interests and price determination are also very important. The benefit test is mainly performed for services and licence fees. The most common violation in the area of services is that the taxpayer fails to prove the benefit test, that is, the taxpayer has not demonstrated the benefit of the service. Furthermore, it can be stated that the greatest emphasis in tax audits is on risk transactions (Karelová and Slivková, 2019).

A Tax audit is considered to be a large-scale activity which serves to examine or verify the tax base or other matters decisive for correct tax determination or chargeability. In general, the tax audit serves as an important preventative tool and as such, together with other inputs, promotes voluntary tax compliance by taxable persons.

Since the Financial Administration of the Slovak Republic started to focus on international taxation and transfer pricing and initiated intensive tax audits in this area by allocating specialized inspectors, we observe the change in the development of these audits' findings. Since 2009, an increase in the number of tax audits in the area of transfer pricing has been recorded along with a dramatic increase since 2016 (data for 2015 is not available) (see Figure 3).

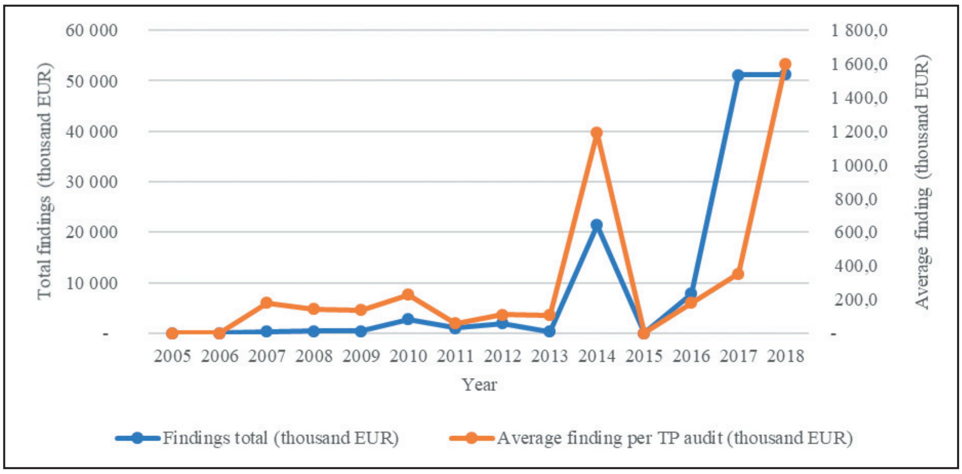
Figure 3: The overview of TP audits and total findings between 2005 and 2018



Source: own elaboration based on the annual reports of the Financial Administration of the Slovak Republic (2019b) (data for 2015 unavailable).

In 2017 the number of tax audits reached its highest point. In that year tax inspectors carried out not only transfer pricing audits but also network audits, multilateral audits and audits focusing on double tax treaties. Altogether, there were 144 such tax audits carried out with a tax finding of 51,152 thousand EUR. In 2018 the number of tax audits focused on transfer pricing dropped to 32. On the other hand, the average finding per one tax audit reached the historical maximum with 1,600 thousand EUR per one tax audit with almost the same number of total findings compared to 2017[113] (own elaboration based on the Financial Administration of the Slovak Republic, 2019b) (see Figure 4).

Figure 4: The overview of average findings of TP tax audits between 2005 and 2018



Source: own elaboration based on the annual reports of the Financial Administration of the Slovak Republic (2019b) (data for 2015 unavailable).

The application of BEPS is a certain area which has had an impact, indirectly increasing the number of tax audits. In 2014 and 2015 there were newly trained professionals, mainly from the Office for Selected Economic Entities, and this fact led to the increased number and effectiveness of tax audits. Since this period, the Financial Administration of the Slovak Republic started to focus more on the issues of international taxation, even on transfer pricing. The reason for the low number of tax audits focused on transfer pricing in the past is due to an absence of a specialized department and the controls were carried out by divisions focused on income tax audits. Currently, the Office for Selected Economic Entities has four divisions[114], which focus on transfer pricing audits of all entities in the Slovak Republic. The Financial Administration of the Slovak Republic[115] published nine risk indicators which are evaluated when selecting an entity for tax inspection (the same criteria for domestic and cross-border transactions). Most frequently, tax audits involve entities linked economically (associated persons linked through the share capital). The area of transfer pricing is probably one of the most comprehensive and up-to-date areas in the fight against tax evasion and tax avoidance within corporate income tax in Slovakia.

Regarding a coordinated approach to transfer pricing audits within the EU, this area is treated mainly by the Act No. 442/2012 Coll. on international assistance and cooperation in tax administration, as later amended.

113 Average finding in 2017 was 355 thousand EUR.

114 This specialised tax office and group of specialised tax inspectors was created in 2013 and currently has about 90 professionals (with countrywide scope).

115 Since 2013, the Financial administration of the Slovak Republic consists from A) Financial Directorate of the Slovak Republic; B) Tax offices (8 Tax offices, 1 Office for selected economic entities, 39 branches of tax offices and 24 contact points of tax offices), C) Customs office (9 Customs offices, 62 branches of customs offices and 16 stations of customs offices); and D) Criminal office of the Financial administration (Financial Administration of the Slovak Republic, 2019b).

8.8.1 PENALTIES WHEN THE PRICE USED DOESN´T CORRESPOND TO THE ARM´S LENGHT PRINCIPLE – IN THE CASE OF INCOME INCREASE OR TAX LOSS DECREASE BY THE TAX AUTHORITY

Penalty for failure to increase the income tax base

Pursuant to Section 17(5) of the Slovak Income Tax Act, the adjustment of the tax base (tax base increase) is always applied to associated persons when all the following conditions are simultaneously met:

- prices or conditions of mutual transactions of associated persons did not correspond to those that would be used in comparable transactions between independent persons, and
- this difference (between prices or conditions used in transactions between associated persons and prices or conditions in comparable transactions of independent persons) caused a decrease of the tax base or an increase of tax loss. Therefore, the adjustment of the tax base is made only for one associate person involved in the transactions.

Penalty for unauthorized corresponding tax base adjustment

A corresponding tax base adjustment is a decrease in the tax base due to transfer pricing. The taxpayer has the right to adjust the tax base in relation to domestic controlled transactions when another associated person increases its tax base, or its tax base was increased by the tax authority. In relation to cross-border transactions, the taxpayer can make a corresponding adjustment of the tax base only if it is authorized by the tax authority. The amount of corresponding tax base adjustment cannot exceed the sum of a primary tax base adjustment of another associated person. The penalty may be imposed also if the taxpayer makes the corresponding tax base adjustment, but another associated party did not make the primary tax base adjustment. Unauthorized corresponding tax base adjustment can be determined by tax office during the tax audit. If the tax authority determines an unauthorised corresponding tax base adjustment, then in the assessment procedure will increase the tax position in the tax return by the relevant amount.

In cases where the arm's length principle is infringed, then a penalty of three times the European Central Bank (ECB) prime interest rate or 10% (the higher of them) based on the amount of unpaid taxes (Section 155(5) of the Tax Procedure Code) is applied. In the case of late payment, the interest rate is either four times the ECB basic interest rate or 15% (the higher of them) is applicable (Section 156(2) of the Tax Procedure Code). The amount of the penalty shall be calculated for each day from the day following the date on which the tax return period expires until the 15th day from the date of receipt of the tax audit notice. If the taxpayer deliberately decreases the tax base due to the applied transfer prices (so-called aggressive tax planning), then a double penalty of the interest rate (20%) can be applied according to Section 18a(1) of the Income Tax Act.

Section 18a (in subsections 1, 2 and 3) also deals with other situations which can have an impact on the calculated penalty increasing or decreasing. If the taxpayer does not appeal against a decision of the tax office and pays the difference of the levied tax within the period of lodging an appeal, the double increase of the penalty shall not apply. The lower penalties shall be imposed on taxpayers who requested the tax administrator to approve a transfer pricing method (APA). If the tax office starts a tax audit for the tax period in which the request of method approval was applied for, one or two tax periods prior to the tax period in which the method was applied for, and during the tax audit the tax levy difference is determined, then the tax office imposes a penalty in the amount of basic interest rate of the ECB (at least 3%) from the amount of additional charged tax or the difference of tax. Also, in cases where the taxpayer submits an additional tax return through which is declared a higher tax liability compared to the previous tax base, a penalty equal to the basic rate of the ECB (at least 3%) of the additional tax liability shall be applied for each day. If the tax difference is determined by the tax office, the penalty shall be three times the basic interest rate of the ECB (at least 10%). If the additional tax return declaring the higher tax liability is submitted within the period for submitting the tax return, then no penalty shall be imposed.

The Financial Administration of the Slovak Republic does not keep statistics of imposed penalties for breaking transfer pricing rules according to Section 18a of the Income Tax Act.

8.8.2 PENALTIES RELATED TO TRANSFER PRICING DOCUMENTATION

If the taxpayer fails to submit the transfer pricing documentation to the tax authority within the stipulated deadline, then the taxpayer commits an administrative offense according to the Tax Procedure Code (Section 154(1) letter j). This is followed by the imposition of a fine.

The penalties may be generally imposed in an amount up to 3,000 EUR for the administrative offence of failing to comply with any of the non-financial obligations according to the Income Tax Act, Tax Procedure Code and other special regulations.

Under the Tax Administration Act, the tax authority may also impose this penalty multiple times. This is applied in cases where imposing a penalty did not lead to a correction of the shortcomings and if the legal provisions were still not followed. It means in practice, that if the taxpayer doesn't prepare and doesn't submit upon the request of documentation, then the fine will be imposed. If the documentation is not elaborated and not submitted to the tax administrator repeatedly, then the fine can be imposed again. No other penalties are applied except those mentioned above.

8.9 OTHER OBLIGATIONS RELATED TO TRANSFER PRICING

8.9.1 ADDITIONAL STATEMENTS OBLIGATION

There are no additional statements except those mentioned above. Other obligations may be linked with adjustments or corresponding adjustments of the tax base (e.g. filing and submitting a notification on tax base adjustment).

8.9.2 SEPARATE DECLARATION IN THE FIELD OF TRANSFER PRICING IN THE ANNUAL TAX RETURN

Corporate income tax returns contain a separate table (An overview of the taxpayer's transactions with associated persons – Table 1), in which it is necessary to fill in the figures (summary) of all controlled transactions with associated parties. Another obligation is to mark on the front page of the tax return that the taxpayer has economic, personal or other ties with associated persons (transactions of associated parties according to Section 2 letter n) of the Income Tax Act) (Financial Directorate of the Slovak Republic, 2017b). In the tax return, it is mandatory for the taxpayer to state only the information and data required in the form.

The table contains information on revenue (sales) and expenses (purchases) with associated persons (affecting the row 100 of the tax return) broken down by transaction types for loans and borrowings, services and licence fees. The table contains also information of revenue (sales) from intangible, tangible and financial assets and inventory (affecting row 100 of the tax return) together with additional information of the acquisition cost.

8.9.3 OTHER OBLIGATIONS

There are no other obligations except those mentioned above, but current trends do recommend recording and keeping as much evidence on supporting the determined transfer price or on the accuracy of procedures, e.g. written contracts, marketing analysis, production and sales plans, internal directives and procedures.

8.10 INFLUENCE OF THE OECD AND EU STANDARDS

BEPS are generally considered an effective tool in the fight against aggressive tax planning. In the conditions of the Slovak Republic, BEPS is not currently treated and implemented in the area of intangible assets and transfer pricing.

According to the Methodological Guidelines on the application of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and transfer pricing regulation of the Slovak Republic (Internal Steering Act No. 79/2014), in the application of transfer pricing rules one must also take into account the documents adopted within the EU, which have either been implemented in the Slovak domestic legal regulation or are merely a political obligation of a member state of the European Union resulting from its membership. Such documents include:

- Code of Conduct in Transfer Pricing Documentation for Associated Enterprises in the EU (Official Journal of the European Union 2006/C 176/01);
- Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (Official Journal L 225, 20/08/1990; Official Journal C 202, 16/07/99);
- Convention on the accession of the Czech Republic, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Slovenia and Slovakia to the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises – Notification of the Ministry of the Interior of the Slovak Republic No. 562/2006 Coll.;
- Code of conduct for the effective implementation of the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (Official Journal of the European Union 2006/C 176/02); and
- Revised code of conduct for the effective implementation of the convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises.

The Anti-Tax Avoidance (ATAD) Directive[116] consists of legally binding provisions that the Slovak Republic is obliged to apply in order to prevent aggressive tax planning transactions. By the implementation of the principle of the ATAD Directive, the Income Tax Act and Tax Procedure Code have been amended. The Income Tax Act defines Controlled Foreign Corporation "CFC"[117] according to Section 17 letter h) as the legal person or entity with a foreign headquarters, if:

- a Slovak resident, either alone or with associated parties, has a direct or indirect share in the share capital, voting rights or is entitled to a share in profits of more than 50% and at the same time;
- income tax of the legal person payable by the controlled foreign company is less than 50% of the tax that would be paid by the controlled foreign company in Slovakia, calculated according to Section 17 to Section 29 of the Income Tax Act.

8.11 PROBLEMATIC ISSUES AND RELATED CASE-LAW

Problematic issues and related case-law could be generally divided into two groups. The first group contains mainly legislative and technical legal areas and the second group consists mainly of pure practical applications of transfer pricing rules and procedures.

8.11.1 RISKS AND SHORTCOMINGS IN THE LEGAL REGULATION OF TRANSFER PRICING

Current home legislation status in transfer pricing

As was already stated, part of the transfer pricing rules is treated by domestic legislation and legal-implementation and legal-application problems are in practice addressed by reference to OECD documents. Subordinate legislation for transfer pricing regulation is focused solely on documentation issues and the relevance of the OECD Guidelines on Transfer Pricing is highlighted as a material source of law. Kočiš (2015) highlights that the guidelines issued by the Ministry of Finance of the Slovak Republic are not generally binding legal provisions and therefore are not formal sources of law. According to Section 160(2) of the Tax Administration Code, the ministry can issue methodological guidelines to ensure a uniform procedure of law and specific rules. The issued guidelines are legally binding for tax authorities. On one side, the methodological guidelines are not considered to be a formal source of law, on the other, the guidelines are considered to be an important element in increasing legal certainty primarily in the area of applying tax-legal norms by tax authorities.

116 The Slovak Republic by the amendment of the Income Tax Act in force since 1 January 2020 implements the EU Directive (Anti-Avoidance Directive 2) 2017/952 of 29 May 2017, so-called ATAD II (hybrid mismatch arrangements).

117 By applying CFC rules, the Slovak Republic can tax the profits (at least partially) which are shifting to another jurisdiction and to minimize the potential corporate income tax revenue losses (e. g. by using transfer pricing as an aggressive profit-shifting channel).

Lack of clearly defined term "other ties" as the part of associated persons definition
According to Kočiš (2015), Slovak legislation in the area of "other ties" (associated parties) as part of the definition of associated persons according to Section 2(p) of the Income Tax Act is characterised by relatively limited information and a lack of requirements for the continuous existence of dependency criteria.

Advance pricing agreements
As was already mentioned, the use of APAs can provide in advance, increased legal certainty concerning transfer pricing methodology and therefore simplify or prevent costly and time-consuming tax examinations[118]. Statistical data shows that there is minimal use of APAs in the Slovak Republic compared to many other EU member states. As was already demonstrated, e.g. in 2018 there were only 3 APA requests received, 3 APAs granted and 2 APA applications rejected. This is due to many reasons, but mainly:

- relatively high fees (10,000 EUR for unilateral and 30,000 EUR for bilateral and multilateral APAs) which are not reimbursed back to the taxpayers in cases where the request is denied;
- the APA application is accompanied by additional administrative and time-consuming burden;
- there are certain risks in relation to previous and upcoming tax periods;
- the Income Tax Act on one side provides information on what must be submitted in an APA application, but there is no standardised application form; and
- the typical problem of the Slovak tax legislation is the risk of very frequent changes in domestic legal regulations (both Income Tax Act and associated guidelines) and persistent uncertainty in the application of the OECD Transfer Pricing Guidelines based on the judgement of the Supreme Court of the Slovak Republic.

Relatively low awareness of SMEs about the current obligations
Based on experience, one can state that a typical problem is often the absence of elementary knowledge by the entrepreneurs from the SME category about the obligations related to transfer pricing. This may result in failure to comply with the current legislation and the resulting potential consequences could be the additional increase of the tax base or an imposition of fines (non-deductible expenses).

The following areas could be considered also as a weak point in applying transfer pricing methodology:

a) Reliability of the comparability analysis mainly consists of identifying independent persons for comparison purposes and adjusting comparable transactions (internal or external). Comparability analysis belongs within the key areas of determining the transfer price. Domestic legal regulation in this case refers to the OECD Transfer Pricing Guidelines and does not deal with it in detail. As a potential solution one could introduce minimal comparability standards, which would have a direct impact on the legal certainty for determining prices in controlled transactions. Kočiš (2015) states that the implementation of these standards would be suitable not only for internal or external controlled transactions, but also for their combination. Minimum standards in terms of comparison conditions of transactions are missing in legal regulation or in subordinate legislation.
b) Methodological guidelines generally regulate the availability of data entering the comparability analysis. More detailed and precise regulation of this area in domestic legal regulation would contribute to an improved status of taxpayers and would increase the legal certainty.
c) In the case of tax base adjustment according to Section 17(5) of the Income Tax Act, it is not exactly clear whether the tax base of an associated person needs to be adjusted for differences on an individual or aggregate basis. Again, more practical examples or additional information could be assessed as suitable.
d) The application of safe harbours is currently absent in Slovak domestic legal regulation. More detailed rules and procedures of individual areas, like e.g. services or intangible assets would increase the legal certainty of the taxpayers. Currently, it is accepted use to calculate the transfer price by calculating costs and adding 5% in the so-called low-value added activities. This practice could potentially be expanded to more areas depending on their significance within the economic structure. Introduction of safe harbours is very likely in the future and it is definitely a challenge given their benefits. On the other side, it should be noted that their implementation is very demanding in

118 The request approval of APA does not automatically mean that the taxpayer will be exempt from a tax audit with focus on transfer pricing or international taxation.

terms of capacity (e.g. administrative burden or quantification of the impact on the state budget), especially in the case of small states, such as Slovakia.

e) Domestic legal regulation does not apply statistical methods[119], tests and statistical procedures (primarily the application of interquartile range) when determining transfer prices. Introduction of a basic framework in this area would also increase the legal certainty of the taxpayer.

f) The database Amadeus is often used and accepted in Slovakia. On the other hand, there is a limited amount of information on the use of other databases or minimum standards to be followed. One can conclude that the anonymous disclosure of the decisions of APA approvals would potentially lead to improved level of practice in this area (provided that tax secrecy is respected).

g) A problematic area is also the very limited number of judgements on transfer pricing. The current status forces the Slovak taxpayers to study the judgements from foreign jurisdictions (mainly from the Czech Republic). This can sometimes be misleading in a practical application as the Slovak legal regulations could be different compared with foreign ones.

h) Kočiš (2019a) states that the scope of the Slovak domestic transfer pricing regime may not be considered as identical for international and domestic transactions as the definition of the "arm's length principle" may differ for domestic transactions[120] and for different versions of the OECD Transfer Pricing Guidelines[121].

8.11.2 TRANSFER PRICING CASE-LAW

There has been a very low number of judgements in the Supreme Court of the Slovak Republic in the field of transfer pricing. In this area, the judgements of the Czech courts are monitored quite intensively in Slovak tax practice.

A relatively significant judgement is the judgement of the Supreme Court of the Slovak Republic No. 2Sžf/76/2014 from 15/4/2015 regarding the application of the OECD Transfer Pricing Guidelines. According to this decision "… *from the perspective of international law, the rules stated in the OECD Transfer Pricing Guidelines are not legally binding but are adopted with the purpose of achieving the practical effect and can be transformed to legally binding if applied within the national system by the tax authorities and courts. From the perspective of national law, the OECD commentaries do not exist as standards and can only influence the interpretation of international treaties"… The Supreme Court further states that "… under the circumstances where the legal norm has not been duly published, where there is an absence of well-established practice, where the OECD Model and commentaries are not available in the official language and where there are contradictory opinions on the binding nature of the interpretative rules "… it cannot be expected from the taxpayer to follow such interpretative rules, until they become part of the international tax treaty "…*

The Supreme Court of the Slovak Republic ruled (judgement No. 8 Sžf 15/2015) that "… *the OECD Transfer Pricing Guidelines, unless duly published, shall not be regarded as a binding source of law under Slovak legal order… it is not binding on the taxpayers or the tax authority… the same applies for the OECD Commentary that has not been published in the Collection of laws and therefore shall be regarded as a non-binding recommendation that can only be used for the interpretation of international treaties"…*

The Regional Court Bratislava ruled (judgement No. 1S/231/2016) that "… *it can be concluded that the tax authority referred to the OECD Transfer Pricing Guidelines only to explain its procedural steps, as it is a guideline for the application of the arm's length principle in cross-border controlled transactions … although the taxpayer disputes the applicability of the OECD Transfer Pricing Guidelines, at the same time the taxpayer refers to the guideline when explaining the application of the transfer pricing methods[122]"…*

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119 Reference to OECD sources.

120 Different regimes may also potentially arise due to the different definitions of associated persons as stated by the Income Tax Act and signed double tax treaties.

121 And due to the relationship between the Slovak Income Tax Act and international (mostly double) tax treaties or OECD Transfer Pricing Guidelines. Kočiš (2019a) further states that there is no explicit recognition of the latest TP developments in Slovak legislation and thus Slovak legislation consequently does not explicitly provide for revised treatment of multiple areas, e.g. intellectual property or services.

122 *"The OECD guidelines outline that if the CUP (Comparable Uncontrolled Price) method cannot be applied, the Cost-Plus method is generally the most appropriate for the valuation of transactions"* (considering the operating activity of the taxpayer as stated in the judgement). As a result of the tax audit, the penalty for violation of Section 18(1) of the Income Tax Act was imposed (according to Section 68(5) of the Tax Procedure Code No. 563/2009 Coll as later amended) because the taxpayer did not prove the use of the arm's length principle when determining transfer prices by using the CUP method (in the sale of finished products to foreign associated persons). In the appeal, the taxpayer also referred to the

The current status of using the OECD Transfer Pricing Guidelines could be considered as a weakness in the Slovak tax regime. The Supreme Court of the Slovak Republic ruled (judgement No. 3 Sžf 101/2008) *"… that the methodological guidelines of the Ministry of Finance shall not be considered source of law, but rather interpretation tools for the application of law"..* The Supreme Court of the Slovak Republic further ruled (judgement No. 2 Sžf 18/2012) that *"… the state authority shall not be expected to apply any source of law that is not available to it and to the taxpayer in the official language"… "… the taxpayers and state authorities are not governed by the sources of law that have not been published"…* On the other hand, the Supreme Court of the Slovak Republic finds that *"… it is well known and respected practice that the OECD Model Tax Convention and its commentary does not represent binding law, however it is the most common reference that is used for the preparation of international tax treaties … ".*

Following this, the current status of the Income Tax Act could be in certain provisions marked as inaccurate. Considering its current status in domestic legislation, 2 systems may arise – one system for domestic associated persons and one system for foreign controlled associated persons.

Another de lege ferenda proposals

Generally, it could be noted that the current definitions of associated parties by the Income Tax Act are sufficient and clear. On the other side, the Income Tax Act does not explicitly regulate the combination of economic, personal or other ties in regards to the establishment of a mutual relationship between persons or the formation of associated persons. According to Kočiš (2015), the combination of economic and personal ties should be clearly stipulated by the Income Tax Act to remove ambiguous interpretations and to support legal certainty of the tax subjects.

As the OECD documents are not generally binding legal acts, the more detailed implementation of these documents into domestic legal regulation would contribute to an increase in legal certainty. The current status in this area could be considered problematic, as on one side the guidelines refer to these documents, on the other side the judgement of the Supreme Court on legal non-binding nature is known. As already stated, the Commentary on OECD Guidelines (also on the OECD Transfer Pricing Guidelines) is currently considered as a means of interpretation. The Slovak Republic applies the so-called dynamic approach, this takes into account the guidelines in force at the moment of a double tax treaty application rather than the guideline in force at the time of signature of the particular double tax treaty (so-called static attitude). From a practical point of view, the translation of the current version of the OECD Transfer Pricing Guidelines to Slovak language would help in the practical application of transfer pricing rules and such a document could also be served as a tool to be included in tax audit protocols[123] (there would therefore be a possibility to refer to this document and as the result increase legal certainty).

Methodological guidelines are relatively general and contribute minimally to solving specific problems arising in the application of transfer pricing rules. The methodological guidelines focus on method application or the domestic legal regulation deals only to a minimal extent to comparability analysis of controlled and uncontrolled transactions or to specific areas or questions associated with the application of transfer pricing rules (e.g. services or intangibles). Regular publishing of practical examples on the use of the methodological guidelines with a focus on selected sectors or different sizes of enterprises would definitely help entrepreneurs to better handle transfer pricing issues.

8.12 SUMMARY OF FINDINGS

In the Slovak Republic, the field of international taxation has for a long time been in the shadow of other taxes, specifically indirect taxes and especially value added tax. Significant changes in domestic legislation regarding corporate income tax started to appear from 2014 as the Slovak Republic was massively affected by the previous financial crisis on one hand, and by increasing pressure from the OECD and EU on the other. In the context of changes related to transfer pricing, we can divide the amendments and changes into two main groups. The first ones, the international amendments, were adopted mainly due to the Slovak Republic's membership of the EU and OECD and the overall setting of the domestic legal order. The amendments from the second group are linked with domestic legislation, especially with the Income Tax

unavailability of the OECD Transfer Pricing Guidelines in the Slovak language (published neither in the Law Collection of the Slovak Republic nor in the Financial Reporter by the Ministry of Finance of the Slovak Republic).

123 The Czech translation is not applicable for this purpose.

Act and the Tax Procedure Code supplemented by the methodological guidelines. As was already stated, the European Commission (2019b) has taken over the classification of aggressive tax planning channels as classified by Ramboll and Corit (2015) and ZEW (2016) studies. Our analysis of the available literature suggests, similarly to the findings of Brada and Buus (2009) or Singh (2016), that among the channels of aggressive tax planning, transfer pricing is investigated between the authors the most. A similar situation can also be observed in the reaction of the Financial Administration of the Slovak Republic. The Tax Office for Selected Tax Subjects (recently renamed the "Office for Selected Economic Entities") was established in 2013 and this office currently employs about 90 professionals. The establishment of this specialised office together with the close cooperation of the Financial Directorate of the Slovak Republic (Division of Taxation Methodology - Department of International Taxation Methodology) brings significant results in many areas of transfer pricing. As stated by many authors (e.g. Bãndoi, Dãnciulescu and Tomitã, 2008 or Melnyk, 2017), the approach of the financial administration has a direct impact on how companies consider risk management strategies. It could be assumed that the increased interest in transfer pricing issues by the Financial Administration of the Slovak Republic has a direct impact on the use or intensity of aggressive tax planning channels.

Despite the relatively high interest in transfer pricing issues and some significantly positive results, one can assume that the rules set in Slovak legislation do not deliver the results that one would expect. As an example, the use of debt by Slovak companies could be mentioned. The Slovak Republic introduced some tax rules treating tax deductible expenses relatively late compared to other European countries. For example, the thin-capitalization rules were implemented within the Slovak Income Act by an amendment in force since 2015 (Section 21a of the Income Tax Act) and allowing for the possibility of including interest and associated costs for loans and borrowings up to a maximum of 25% EBITDA into tax deductible expenses (excluding the bonds[124]). Based on the available investigations (e.g. Ištok and Kanderová, 2019a and 2019b) it is clear that Slovak companies after transferring their headquarter/registered office to a low tax jurisdiction reported an increase of indicator interest expenses over total assets e.g. by 75% for 2015. This is clear evidence that the use of debt is massively practiced by Slovak companies as a profit-shifting technique. Regarding what is stated, two questions arise. The first one is: *"How did transfer pricing rules work before and during the investigated period in relation to loans and borrowings?"* The second one is: *"In general, are the set transfer pricing rules and principles reliable enough to prevent artificial profit-shifting (both on a national and international level) or must these rules be supplemented by other fixed indicators treating non-deductible tax expenses?"* One can conclude that these questions are important to investigate in future research when considering the underlying tax system setting. What could be perceived positively is the increased number of professional articles and studies focused on determining correct transfer prices in connection with loans and borrowings in the Slovak conditions.

Rathke and Rezende (2016) executed this study and based on similarities in transfer pricing systems created 6 groups of countries. The Slovak Republic is included in Group II together with Finland, Hungary, Norway, Slovenia and Russia. The authors state that transfer pricing systems in this group are consistent with the core of international transfer pricing principles within OECD guidelines. Similarities have been identified e.g. for ordinal internal transactions in relation to withholding taxes, statutory requirements in transfer pricing documentation and the vague statute of limitations when intentional non-compliance is identified. Furthermore, these countries do not have a tradition in mutual agreement procedures (MAP) or APA. Mutual agreements between taxpayers and tax authorities are relatively new within this group of countries. As was already mentioned, the rules for APA requests have recently changed and the related fees can be considered excessively high by taxpayers. The Financial Administration of the Slovak Republic primarily justifies this situation by demanding verification at multiple levels (e.g. personnel capacity, process length or financial demands). As is further stated by Rathke and Rezende (2016), the Slovak Republic's transfer pricing system is consistent and refers to OECD sources. It was also mentioned that the issued methodological guidelines which have no binding nature often refer to OECD TP guidelines or Commentary. One can conclude that the selected areas[125] treated by the OECD TP guidelines shall be more

124 To the best of our knowledge, since the implementation of the thin-capitalization rules, many companies started to use the bonds significantly more intensely as a consequence of being excluded from the calculation formula.

125 For example, comparability analysis, arm's length range or the application of TP methods (already partially treated by the methodological guidelines) possibly supplemented by uniqueness and specifics of the Slovak conditions. Additional information to the information and

vigorously included in Slovak domestic legislation with a binding nature and avoid potential application problems. On the other hand, the Slovak Republic currently does not even have a Slovak translation of the current version of OECD TP guidelines and Commentary. This is mainly caused by the limited staffing of the departments focused on international and domestic taxation in corporate income tax and a limited budget dedicated for this area.

On one hand, the increased attention from the Financial Administration of the Slovak Republic on transfer pricing since 2013 could be assessed as positive, on the other hand, there are insufficient resources allocated to achieve even better results and procedures. Our research shows that there is increased pressure to pay more attention to direct national and cross-border taxation (currently VAT is the dominant focus).

The study of Ignat and Feleagã (2017) placed the Slovak Republic in Group II together with Poland. The Czech Republic is placed in Group I and Hungary in Group IV. The authors found that countries from Groups I and II have less strict transfer pricing regulations. According to this study, the rules are the strictest in Hungary. As we can see from comparing the studies of Rathke and Rezende (2016) and Ignat and Feleagã (2017), the changes in selected fields of transfer pricing legislation can have a significant impact on the classification and perception of the actual transfer pricing regulations' status within the relevant country. These two studies reveal that the south-west part of Europe have stricter transfer pricing regulations compared with the central-eastern part of Europe, which could be partially explained by the more intense action against artificial profit-shifting and a higher interest in direct taxation compared to V4 countries. According to a study of Lohse, Riedel and Spengel (2012), all V4 countries could be classified in the same group when it comes to the date of introduction of transfer pricing regulations (1990-2000). In the context of the introduction of statutory documentation requirements, of all V4 countries only the Czech Republic stands alone with no statutory documentation requirements[126]. Following the study, Lohse, Riedel and Spengel (2012) and Ignat and Feleagã (2017) state that the rules in Europe are less strict compared to countries outside of Europe. One can conclude that stricter rules can be useful in the combat against artificial profit-shifting, on the other hand, of equal importance is the concurrent increase of the legal certainty of taxpayers. For this reason, even countries outside the EU could be an inspiration to V4 countries.

Safe harbours according to many authors (e.g. Singh et al., 2009; Solilová 2013 or Kostić, 2018) offer many benefits and help to minimise not only the compliance cost for taxpayers but also the administrative cost for tax administration. The implementation of safe harbours is generally recommended. On the other hand, the implementation and its related procedures are time consuming, budget draining and labour intensive. In this case we are again encountering the problem of insufficient personnel capacity intended and available for this purpose. To the best of our knowledge, there are no studies or analyses on corporate income tax revenue losses as a result of transfer pricing in the Slovak Republic. It could be assumed that these revenue losses (as transfer pricing is considered as one of the most aggressive tax planning channels) could be markedly decreased by paying more attention and increasing personnel capacity. We find that future tax research with a focus on profit-shifting techniques out of the Slovak Republic should be one of the main priorities to be conducted in the near future. Safe harbours can on the one hand bring many benefits, also to the taxpayers, which include the previously mentioned potential compliance cost savings and the increased legal certainty. On the other hand, it must be admitted that the implementation of safe harbours is much more difficult in terms of resources in small countries, such as e.g. the Slovak Republic. However, we can find some countries in this area which could be an inspiration to the Slovak Republic or V4 countries. One of these countries could be e.g. India where safe harbours are considered to be an alternative for APA. Singh (2016) states that safe harbours in India cover significant sectors of the economy (e.g. IT and ITES sectors, R&D in the IT and pharmaceutical sectors, financial transactions and auto ancillaries-original equipment manufacturers).

Of all V4 countries, Polish domestic legislation can be considered as a suitable and inspiring one for Slovak domestic law e.g. in the area of transfer pricing aspects of a business restructuring (implementation of restructuring regulations) or safe harbour for loans and issued bonds transactions[127].

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procedures as referred to the OECD TP guideline could be provided e.g. for comparability analysis in the part focused on comparables (the range, sources-databases, regions, group of operators etc.).

126 Currently the strictest documentation requirements can be observed in Poland.

127 The Slovak Republic has currently no safe harbours or rules for business restructuring. Rules for safe harbours for low value-added services are implemented directly in the Polish Act on Corporate Income Tax.

One can conclude that the introduction of safe harbours can in many situations replace the APAs or fulfil many similar benefits which are expected from using APAs despite the differences between safe harbours and APAs as stated e.g. by Singh et al. (2009)[128]. Such introduction of safe harbours can therefore also reduce litigation, prevent any hesitations or penalties, comply with the instructions of the tax administration, increase transparency and ultimately encourage foreign investors to invest more in the Slovak Republic (as stated e.g. by Chugan, 2007; Biyan and Yilmaz, 2013 or Fadiga, 2018). It is generally accepted that the quality of the tax system of a country has a direct impact on the inflow of foreign direct investments (FDI).

Transfer pricing documentation requirements are currently a fixed part of many national tax systems worldwide. Transfer pricing documentation analyses transactions which have already taken place between associated parties. Currently there are two main approaches to transfer pricing documentation regarding profit-shifting. The first main approach says that transfer pricing documentation requirements discourage the use of transfer pricing as an aggressive tax planning channel to low-tax jurisdictions (e.g. Feleaga and Neacşu, 2016 or Ylönen and Tevainen, 2017). The other opinion stream[129] says that transfer pricing documentation (as a compulsory attachment to APAs) can on the other hand support aggressive tax planning activities (e.g. Herath and Young, 2012). Statutory requirements for transfer pricing documentation are subject to relatively frequent changes in the Slovak Republic. The Ministry of Finance of the Slovak Republic publishes the guidelines on determining the content of documentation. Frequent changes and amendments of documentation requirements (currently the fifth version of the guideline is in force in just 10 years) can be considered as a weakness. On the other hand, many changes can be assessed as positive, especially linking the documentation requirements not to the taxpayer group, but to the type of controlled transaction or reporting simplification for insignificant transactions. In Slovak practice, there is no unanimous view on shortening the deadline for the taxpayer to submit transfer pricing documentation at the tax administrator's request (from previously 60 days to just 15 days). Considering the nature and main intent of transfer pricing documentation preparation, one can conclude that the period of 15 days is suitable. The strictest deadline for submitting documentation within 7 days at the request of the tax authority is currently in force in Poland[130]. The period of 7 days is considered by many Polish entrepreneurs and advisory companies as too short and also due to the tightening of transfer pricing documentation obligations, many Polish entrepreneurs are setting up companies abroad, e.g. in the Slovak or Czech Republic just to avoid the strict Polish documentation requirements.

Generally, it can be stated that the Slovak domestic and cross-border direct taxation practice is relatively weakly supported by scientific research. Due to this fact, many potential areas of future research could be determined on both a macro and micro levels, e.g. the following:

- to analyse transfer pricing as a profit-shifting technique out of the Slovak Republic considering the underlying tax system setting;
- to analyse and measure tax revenue losses due to transfer pricing with a special focus on low-tax jurisdictions;
- to analyse the impact of transfer pricing regulation changes on the possibilities to use transfer pricing as an aggressive tax planning channel;
- to analyse and measure the compliance costs for taxpayers and administrative costs for tax administration related to transfer pricing;
- to analyse the possibilities of safe harbours implementation into Slovak legislation in relation to the potential benefits and associated costs;
- to analyse the problematic aspects related to transfer pricing tax audits and to offer the potential solutions to minimise the difficulties from the perspective of both taxpayers and tax administrations;
- to analyse and offer the possibilities and procedures how legal certainty could be increased with a focus on specific areas, e.g. intangibles, financing, R&D or other selected areas which are significant over the Slovak economy; and
- to analyse and offer solutions regarding the taxation of a digital economy with a focus on transfer pricing.

128 Safe harbours are general in their characteristics, whilst APAs are specific to the taxpayer.
129 Especially older studies before 2015.
130 Poland currently has the strictest TP statutory documentation requirements among all V4 countries.

Considering the nature and development of domestic and cross-border direct taxation and the above-mentioned challenges within Slovak conditions, one can conclude that future high-quality scientific research will need extensive cooperation between academicians, the professional sphere and state institutions, such as the Ministry of Finance of the Slovak Republic and the Financial Administration of the Slovak Republic.

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ANNEX

Table 60: Overview of all double tax treaties signed by Slovakia according to Article 9 category

Contracting state	EU member	Date of signature	Date of entry into force	CAT 1	CAT 2	CAT 3
Armenia	NO	15/05/2015	01/02/2017		X	
Australia*	NO	24/08/1999	22/12/1999		X	
Austria*	YES	07/03/1978	12/02/1979	X		
Belarus	NO	12/07/1999	05/07/2000			X
Belgium	YES	15/01/1997	13/06/2000		X	
Bosnia and Herzegovina	NO	02/11/1981	17/04/1983	X		
Brazil	NO	26/08/1986	14/11/1990	X		
Bulgaria	YES	12/11/1999	02/05/2001		X	
Canada	NO	22/05/2001	18/12/2001			X
China**	NO	11/06/1987	23/12/1987		X	
Croatia	YES	12/02/1996	14/11/1996		X	
Cyprus	YES	15/04/1980	30/12/1980	X		
Czech Republic	YES	26/03/2002	14/07/2003			X
Denmark	YES	05/05/1982	27/12/1982		X	
Estonia	YES	21/10/2003	29/03/2006			X
Ethiopia	NO	01/10/2016	26/02/2018			X
Finland	YES	05/02/1999	06/05/2000			X
France*	YES	01/06/1973	25/01/1975		X	
Georgia	NO	27/11/2011	29/07/2012		X	
Germany	YES	19/12/1980	17/11/1983		X	
Greece	YES	23/10/1986	23/05/1989	X		
Hungary	YES	05/08/1994	21/12/1995	X		
Iceland	NO	15/04/2002	19/06/2003			X
India	NO	27/01/1986	13/03/1987	X		
Indonesia	NO	12/10/2000	30/01/2001			X
Iran	NO	19/01/2016	01/05/2018		X	
Ireland	YES	08/06/1999	30/12/1999		X	
Israel*	NO	08/09/1999	23/05/2000			X
Italy	YES	05/05/1981	26/06/1984	X		
Japan*	NO	11/10/1977	25/11/1978	X		
Kazakhstan	NO	21/03/2007	28/07/2008		X	
Kuwait	NO	13/11/2012	15/04/2014	X		
Korea	NO	27/08/2001	08/07/2003	X		
Latvia	YES	11/03/1999	12/06/2000			X
Libya	NO	20/02/2009	21/06/2010			X
Lithuania*	YES	15/03/2001	16/12/2002			X
Luxembourg	YES	18/03/1991	30/12/1992		X	
Macedonia	NO	05/10/2009	27/04/2010		X	
Malaysia	NO	25/06/2015	11/04/2016		X	

Contracting state	EU member	Date of signature	Date of entry into force	CAT 1	CAT 2	CAT 3
Malta	YES	07/09/1999	20/08/2000		X	
Mexico	NO	13/05/2006	28/09/2007		X	
Moldova	NO	25/11/2003	17/09/2006			X
Mongolia (individuals)	NO	27/05/1978	01/01/1979	Not treated		
Mongolia (corporate)	NO	27/05/1978	01/01/1979	Not treated		
Montenegro	NO	26/02/2001	15/10/2001	X		
Nigeria	NO	31/08/1989	02/12/1990		X	
Norway	NO	27/06/1979	28/12/1979	X		
Poland*	YES	01/08/2013	01/08/2014		X	
Portugal	YES	05/06/2001	02/11/2004		X	
Romania	YES	03/03/1994	29/12/1995		X	
Russia	NO	24/06/1994	01/05/1997		X	
Serbia*	NO	26/02/2001	15/10/2001	X		
Singapore	NO	09/05/2005	12/06/2006			X
Slovenia*	YES	14/05/2003	11/07/2004			X
South Africa	NO	28/05/1998	30/06/1999		X	
Spain	YES	08/05/1980	05/06/1981		X	
Sri Lanka	NO	26/07/1978	19/06/1979	X		
Sweden*	YES	16/02/1979	08/10/1980	X		
Switzerland	NO	14/02/1997	23/12/1997			X
Syria	NO	08/02/2009	27/02/2010			X
Taiwan	NO	10/08/2011	24/09/2011		X	
The Netherlands	YES	04/03/1974	05/11/1974	X		
Tunisia	NO	14/03/1990	25/10/1991		X	
Turkey	NO	02/04/1997	02/12/1999		X	
Turkmenistan	NO	08/08/1996	26/06/1998		X	
Ukraine	NO	23/01/1996	22/11/1996	X		
United Arab Emirates	NO	21/12/2015	01/04/2017		X	
United Kingdom*	YES	05/11/1990	20/12/1991	X		
USA	NO	08/10/1993	30/12/1993			X
Uzbekistan	NO	06/03/2003	17/10/2003		X	
Vietnam	NO	27/10/2008	29/07/2009		X	
TOTAL				19	32	18

Source: own elaboration based on the list of double tax treaties (Ministry of Finance of the Slovak Republic, 2019).

Note: *) Double taxation conventions with these states are modified by Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting – Communication of Ministry of Foreign and European Affairs of the Slovak Republic No. 339/2018 Coll. (hereinafter as "MLI"), which the Slovak Republic entered into force on 1 January 2019. Sweden has reserved the right to apply modifications in double taxation convention with the Slovak Republic due to the MLI with later effect.

CHAPTER 9
COMPARISON OF TRANSFER PRICING LEGAL REGULATIONS IN THE V4 COUNTRIES

This chapter deals with comparison of selected features of transfer pricing, starting with a general description of the legal system provided in Table 61. Other areas covered by the comparative analysis are as follows:

a) key terms in transfer pricing;
b) rules as embodied in DTTs concluded by a particular V4 country;
c) transfer pricing documentation;
d) special clauses for transfer pricing related to sectors/areas;
e) APAs;
f) safe harbours;
g) specific types of penalties relating to breaching of transfer pricing rules;
h) additional transfer pricing statements, and
i) burden of proof and transfer pricing issues settled by case-law.

Table 61: Legal system

Issue	Czech Republic	Hungary	Poland	Slovakia
Type of legal system	Continental Legal System – currently can be described more as a Mixed Legal System	Continental Legal System	Continental Legal System	Continental Legal System (there is a slight change currently observed from the Continental Legal System to a Mixed Legal Culture).
Position of OECD standards	OECD is considered to be a form of soft-law			
Translation of OECD standards into the domestic language	A Czech translation was published in 2019 for the current version	Not for the current version	Not for the current version	Not for the current version
Position of case-law	Interpretation of the law and elimination of the lack of legal regulations in the field of interpretation			
Position of EU / international law	Supremacy and application priority over domestic law			

Source: own elaboration based on CZ: (Brychta and Svirák, 2020; Constitution of the Czech Republic, 1993; Gerloch, 2013; Harvánek et al., 1998; Judgement of the Supreme Administrative Court of the Czech Republic of 10 February 2005, File No. 1 Afs 108/2004; Judgement of the Supreme Administrative Court of the Czech Republic of 25 June 2014, File No. 7 Afs 94/2012; Knapp, 1995; Malenovský, 2008; Pouperová, 2018; Týč, Sehnálek and Charvát, 2011; United Nations, 1980; Večeřa et al., 2015); HU: (Cserny and Téglási, 2014; European E-Justice, 2020); PL: (Constitution of the Republic of Poland, 1997; Sozański, 2014; Górecki, 2012; Rola, 2009; Kalisz, 2007; Deneka, 2019, OECD, 1960); SK: (Jánošíková, 2019; Mazák and Jánošíková, 2009; Tóthová, 2011).

Generally speaking, the bases of the legal systems are very similar, if not the same, for the observed aspects (Table 61). In Hungary and Poland, the type of the legal system is continental, while in Slovakia and in the Czech Republic, the legal system can currently be assessed more as a mixed system. The position of OECD standards can be considered as a soft-law in all the V4 countries. Apart from the Czech Republic, there are no translations into the domestic language for the current version of the OECD Transfer Pricing Guidelines. In the Czech Republic, the translation of the latest version was published in 2019 (in a Financial Bulletin issued by the Ministry of Finance) as an attachment to the D-34 Guidance. The position of the case law is similar in the investigated countries. The position of EU and international law in all the V4 countries, which are also EU countries, occupies, not surprisingly, the same position based on its supremacy and application priority over domestic law.

Table 62 below provides a comparison of fundamental definitions relevant for transfer pricing.

Table 62: Key terms

Issue	Country	Description
Definition of associated person	CZ	Two basic categories – persons associated through capital or voting rights (directly or indirectly – a threshold of at least 25%) AND persons otherwise associated (including persons with economic or personal ties).
	HU	Associated person means the taxpayer and the person: • over which the taxpayer has majority control • that has majority control over the taxpayer • if a third party has majority control over both (notwithstanding whether directly or indirectly). The criterion for major influence is 50%. In addition, the taxpayer's foreign business is considered to be an associated person and the votes from relatives shall be counted together.
	PL	a) entities from which one entity has significant influence over at least one other entity, or b) entities which are significantly influenced by: • the same other entity or • a spouse, relative or relative to the second degree of a natural person who has significant influence over at least one entity, or c) a company without legal personality and its partners, or d) the taxpayer and his foreign establishment, and in the case of a tax capital group - a capital company that is part of the group and its foreign establishment.
	SK	Associated party means a close person or a person with economic, personal or other ties (partly otherwise associated). A threshold of capital share or voting rights is used as the decisive criterion (direct derived interest of 25 % and indirect derived interest of 50 %).
Number of changes in 10 years	CZ	One significant change in relation to the possibility of making adjustments relating to transfer price; some changes relating to the specification of the situations for which the arm´s length principle shall not be applied.
	HU	Important changes in 2015 to the definition and approaches.
	PL	Since 01 January 2017 – change in the capital share threshold from 5 % to 25 %. Since 01 January 2019 – a significant change of wording of the definition.
	SK	4 important amendments to the definition and approaches in force since 2014, 2015, 2017 and 2018.
Challenges in the definition	CZ	Reference to the Act on Property Evaluation in case a market price cannot be set (its stricto sensu application can be contrary to the idea of the arm´s length principle).
	HU	For TP, the rules of the Corporate Tax Act shall apply, but this act refers to the Civil Code's definition of "control" and major influence.
	PL	None.
	SK	Extension of "other ties" (otherwise associated party) category as the current state could be assessed as insufficient in some situations (currently missing are the quantitative or purely formal characteristics of dependence).

Issue	Country	Description
Problems in the definition	CZ	Generally speaking, it seems that there are no serious problems in the definitions since case-law has established and explained general and "problematic" clauses.
	HU	Other acts (for example Accounting Act) contain a definition of an associated person, but companies should apply the definition of the Corporate Tax Act for transfer pricing. This might be confusing for deciding whether they are associated parties or not.
	PL	The purpose of legislative work is to remove problematic issues in definitions on an ongoing basis.
	SK	Problems may occur for category identification of "other ties" (otherwise associated party) and for the mutual combinations of individual categories of associated persons as a more detailed description and dependency criteria are missing.
Definition of transfer price	CZ	There is no explicit definition of transfer price in Czech law.
	HU	The definition of transfer price or transfer pricing does not exist.
	PL	This definition has existed since 01 January 2019: *"the financial result of the conditions established or imposed as a result of existing relationships, including price, remuneration, financial result or financial indicator"*.
	SK	The definition of transfer price or transfer pricing does not exist.

Source: own elaboration based on CZ: (Act on Property Evaluation, 1997; Civil Code, 2012; General Financial Directorate, 2015; General Financial Directorate, 2019; Income Tax Act, 1992; Judgement of the Supreme Administrative Court of 20 November 2014 file No. 9 Afs 92/2013; Judgement of the Supreme Administrative Court of the Czech Republic of 27 June 2007, file No. 1 Afs 60/2006; Solilová and Nerudová, 2019; Tax Procedural Code, 2009); HU: (Act on Corporate Tax, 1996; Act on Accounting, 2000; Civil Code, 2013); PL: (Act on CIT; Act of Tax Ordinance); PL: (Act on CIT; Act of Tax Ordinance); SK: (Income Tax Act, 2003; Kočiš, 2015; Kočiš, 2019a; Kočiš, 2019b).

The wordings of the definitions of associated person/related parties in the law of the V4 counties are different and there are some distinct characteristics, but generally speaking there are many similarities. Every V4 country's definition contains two main categories of associated parties: persons associated through capital (ultimately voting rights) and other ties (relationships). The threshold for being considered an associated person differs between countries: in the Czech Republic there is a threshold of at least 25 %, while in Hungary it is 50 %, Slovakia applies 25 % by direct share and 50 % for indirect. In Poland, the definition of related entities includes the concept of significant influence, which among others is understood as owning directly or indirectly at least 25 % of:

a) equity interests or
b) voting rights in controlling, constituting or managing bodies, or
c) shares or rights to participate in profits or assets or their expectation, including units and investment certificates.

The changes in the definitions are moderate. The Czech Republic and Poland have no significant problems and challenges in the current definition of associated persons, but Hungary and Slovakia have difficulties in the legal regulation of key terms. In Hungary, there are many sources of law referring to associated parties and it might be confusing as to which rules should be applied. In Slovakia, the challenges come from the extension of the "other ties" category, as the current status could be assessed as insufficient in some situations (currently missing are the quantitative or purely formal characteristics of dependence). Problems may occur as a result of this, and more detailed descriptions of dependency criteria for mutual combinations of individual categories of associated persons are missing. The definition of transfer price or transfer pricing does not exist in the Czech Republic, Hungary or Slovakia. The legislation contains the obligation to follow the arm´s length principle in these countries.

Regard transfer pricing, the legal regulation as embodied in DTTs is also of high importance. The definition of associated persons as provided in DTTs and the prevailing concept of the rules as embodied under Art. 9 of DTTs are summarised in Table 63.

Table 63: Double tax treaties

Issue	Czech Republic	Hungary	Poland	Slovakia
Definition of associated person – if different from model tax convention	In line with the OECD Model Tax Convention.			
Scope of the definition compared to the definition as provided in domestic law	Narrower			
Prevailing category (taking account of the absolute figure)	First category	Second category	Second category	Second category
MLI convention	Undersigned, not yet entered into force.	Undersigned, but not yet entered into force.	Binding since 01 January 2019.	First MLI modifications entered into force in 2019.

Source: own elaboration based on (OECD, 2017a, 2017b); CZ: (Ministry of Finance of the Czech Republic, 2019; OECD, 2020; Solilová, 2014); HU: (Acce, 2019); PL: (Act on CIT; OECD, 2016; Council of the European Union, 1988; Ministry of Finance, 2019; Act on tax exchange, 2017; Eur-lex, 2020b; Act on APA, 2019); SK: (Kočiš, 2019a; Ministry of Finance of the Slovak Republic, 2019).

The definitions applied by the V4 countries are in line with the OECD Model Tax Convention. The definition as provided by DTTs to which all of the V4 countries are a contracting party can be considered narrower compared to the definition as provided by their domestic law. There are several concepts of Art. 9 embodied in DTTs. The first category includes DTTs in which only the arm´s length principle and a definition of associated persons are enshrined; another, regarding the extent of legal regulation of a more extensive category of DTTs, also includes corresponding adjustments, while the last category of DTTs includes an explicit limitation of the corresponding adjustment to *bona fide cases* (Solilová, 2014). Apart from the Czech Republic, the second category prevails in the other countries, when strictly considering the absolute figures for particular categories.

The MLI convention has been undersigned by all the V4 countries. Slovakia became a signatory to the MLI in 2017. The issued Explanatory Statement to the MLI is adhered to by Slovakia, and the first MLI modification entered into force in 2019, while the Czech Republic has undersigned the MLI, but it has not entered into force in this country yet. Hungary has undersigned the MLI, but despite making plans (at the end of 2019), it has not entered into force.

A comparison of the aspects relevant for transfer pricing is presented in Table 64 below.

Table 64: Transfer pricing documentation

Issue	Country	Description
Three-level approach	CZ	Since 16 August 2017
	HU	Since 01 January 2018
	PL	Since 01 January 2017
	SK	Since 01 January 2017
Structure and thresholds (local file, master file, CbCr)	CZ	Transfer pricing documentation is not obligatory in the Czech Republic (the recommendations regarding transfer pricing documentation reflect OECD and EU standards – thus, there are rules for the local and master files). Since the obligation to make out a CbCR report has been established in a Directive and as such it has been transposed in the Act, the CbCR report is obligatory for situations as set out by law.

Issue	Country	Description
Structure and thresholds (local file, master file, CbCr)	HU	**Documentation obligation** The Corporate Tax Act (Section 18. (5)) defines taxpayers who are required to register if they have a related party: business associations (general partnership, limited partnership, limited liability company, joint venture, joint-stock company), merger, European joint-stock company, cooperative, European cooperative and foreign entrepreneur. **Master file and Local file** Taxpayers with associated persons, if the revenue of the group remains under 750,000,000 EUR. **CbCR** Taxpayers with associated persons, if the revenue of the group is over 750,000,000 EUR.
Structure and thresholds (local file, master file, CbCr)	PL	Thresholds binding since 01 January 2019 **Local file** 1) PLN 10,000,000 - in the case of commodity transactions; 2) PLN 10,000,000 - in the case of financial transactions; 3) PLN 2,000,000 - in the case of service transactions; 4) PLN 2,000,000 - in the case of transactions other than those specified in points 1-3. **Master file** For taxpayers belonging to a group of related entities for which consolidated financial statements are prepared, and for whom consolidated revenues exceeded PLN 200,000,000 or its equivalent in the previous financial year. **CbCR** For taxpayers belonging to a group of related entities: a) for which consolidated financial statements are prepared in accordance with the accounting policies in force in this group (...); b) which includes at least two units established or managed in different countries or territories (...); c) whose consolidated revenues last year exceeded a variable threshold amount: 1) PLN 3,250,000,000 - if the capital group prepares consolidated financial statements in PLN; 2) EUR 750,000,000 or its equivalent, converted according to rules set by the country or territory in which the parent entity has its headquarters or management (...).

Issue	Country	Description
Structure and thresholds (local file, master file, CbCr)	SK	**Abridged documentation** is understood as the completion of an annex to the tax return. The abridged documentation shall be kept for: • Significant transactions by a taxpayer where the taxpayer is obliged to have financial statements verified by an auditor; • Significant transactions of natural persons determining the tax base or tax loss according to Section 17 of the Income Tax Act; • Significant controlled transactions with associated persons who are taxpayers with unlimited tax liability, except controlled transactions in relation to permanent establishments of those taxpayers located abroad; • Significant controlled transactions of a taxpayer who is consolidating or is a consolidated accounting entity; • Insignificant controlled transactions of a taxpayer applying for tax relief in the tax period. **Basic (simplified) documentation shall be kept for:** • Significant cross-border controlled transactions, if a taxpayer's total operating and financial revenues per tax period exceed 8 million EUR; • Controlled cross-border transactions or a group of controlled cross-border transactions that can be merged, and if the value of this controlled transaction or group of transactions exceeds 1 million EUR; • Significant domestic controlled transactions, if a taxpayer claims tax relief in the tax period; • Non-significant transactions with an associated party who are taxpayers in a non-contracting state. **Complete documentation (the-full scope) shall be kept for:** • Significant cross-border transactions of a taxpayer who reports accounting results in individual financial statements according to IFRS; • Cross-border controlled transactions or a group of cross-border controlled transactions that can be merged, with the value of such a controlled transaction or group of transactions exceeding 10 million EUR; • Significant controlled transactions with associated persons resident in non-contractual counties; • Controlled transactions where a taxpayer requests the tax authority to issue a decision on approving the TP method (APA); • Controlled transactions where a taxpayer requests an adjustment of the tax base, except for adjustment of the tax base in relation to domestic controlled transactions; • Controlled transactions where a tax dispute settlement mechanism has been requested for the relevant tax period; • Significant cross-border controlled transactions of a taxpayer claiming tax relief in the relevant tax period. The DAC4/CbCR notification obligation is imposed on all entities of transnational group companies (including branch and permanent establishments) with a consolidated turnover of over 750,000,000 EUR.

Issue	Country	Description
Exemptions	CZ	See above.
	HU	The exemptions from transfer pricing documentation are as follows: • companies qualifying as small companies on the last day of the tax year: in the two business years preceding the reference year, the number of employees did not exceed 50 and the net sales or balance sheet total was EUR 10 million (at the group level); • non-profit organisations of public interest; • companies where the state has a majority influence; • an annual transaction value of less than 50 million HUF at the group level (approximately 156 thousand EUR): it is important that after consolidation, this should be analysed at the transfer price; • free value-added service: it must be confirmed that the cost has been billed without a profit margin. If it has been billed to more than one person, the distribution method must comply with the transfer price principle.
	PL	Described in the Act on CIT, art. 11n, for example for transactions: *"concluded only by related entities having their place of residence, registered office or management in the territory of the Republic of Poland in the tax year in which each of these related entities jointly meets the following conditions (...)"*; covered by the decision on the agreement referred to in art. 20a of the Tax Code, during the period covered by this decision (APA), *"between companies forming a tax capital group, where the relations result exclusively from a relation with the State Treasury or local government units or their associations"*.
	SK	No exemptions, but there exists simplification of documentation requirements for individuals, small and medium-sized enterprises, and for domestic transactions. There are also no formal requirements for functional and risk analysis and no requirements for benchmark analysis for transactions by individuals, small and medium-sized enterprises and insignificant domestic transactions.
TP methods	CZ	The methods as set by the OECD standards are recommended; use of another suitable method is not excluded. a) Comparable uncontrolled price method; b) Resale price method; c) Cost-plus method; d) Transactional net margin method; e) Distribution of profit; f) Other methods (these, however, must follow the arm´s length principle).
	HU	
	PL	
	SK	
Comparability/ compliance analysis	CZ	Not obligatory, however, in practice there is a need to carry out it for successful bearing of the burden of proof.
	HU	Comparability analysis is a mandatory part of the documentation.
	PL	Since 01 January 2017, the results of the comparability analysis or compliance analysis must be part of the transfer pricing documentation.
	SK	A comparability analysis is a mandatory part of the full-scope documentation.

Source: own elaboration based on CZ: (Act on International Cooperation within Tax Administration, 2013; Council of the European Union, 2006; General Financial Directorate, 2019; Jelínek et al., 2018; Ministry of Finance of the Czech Republic, 2010a, 2010b; Ministry of Finance of the Czech Republic, 2019; OECD, 2017a; Tax Procedural Code, 2009); HU: (Act on Corporate Tax, 1996; Berényi, 2016; Government Decree No 32/2017); PL: (Act on CIT; Regulation of MF, 2018b; OECD, 2015; Regulation of MF, 2017a; Regulation of MF, 2017b; Act on tax exchange, 2017; Jamroży 2018); SK: (Income Tax Act, 2003; Guideline of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724).

The three-level approach to transfer pricing documentation was introduced in 2017 in Poland, Slovakia and the Czech Republic, and lastly, on 01 January 2018 in Hungary. There are many differences regarding transfer pricing documentation in the V4 countries. For example, it is not obligatory in the Czech Republic. Hungary follows the rules of the OECD standards, and these are implemented into domestic law. Poland has special thresholds which determine the type of the documentation that shall be submitted. In Poland, the Local File documentation obligation differs by areas, while the obligation to prepare a Master File is applicable on reaching a 200,000,000 PLN threshold. In Slovakia, the scope of the documentation depends on the type of transaction being checked (significant/insignificant and domestic/cross-border). Three types of documentation are applied: full-scope (complete), basic (simplified) and extra-simplified (abridged). Local and Master files are a mandatory part of full-scope and simplified (basic) documentation. Hungary and Poland have exemptions from transfer pricing documentation, but the categories are different. The most important exemptions are the category of small-sized companies and a maximum level of 50,000,000 HUF for annual transactions. The exemptions for Poland are listed above. For example, domestic companies *"in which each of the related entities jointly meets the following conditions (...); covered by the decision on the agreement referred to in art. 20a of the Tax Code, during the period covered by this decision (APA)"*, and *"between companies forming a tax capital group"*.

In the Czech Republic and Slovakia no exemptions are specified.

The transfer pricing methods are the same in the V4 countries. The methods as set by the OECD standards are recommended, while other methods are also acceptable if they follow the Arm´s Length Principle.

Table 65 below provides a comparison of special clauses for transfer pricing related to special sectors or areas in the countries investigated.

Table 65: Special clauses for transfer pricing related to sectors/areas

Issue	Country	Description
Special clauses	CZ	No specific clauses.
	HU	No specific clauses.
	PL	Reporting requirements for transfer pricing include the need to separately disclose intra-group services, in particular production, distribution, research and development services, rental and leasing, and intragroup services, including in particular management fees and joint service centres - accounting, legal, IT, HR. Cost Contribution Arrangements: Provisions exist and include a detailed, quantitative definition of business restructuring and comparability analysis requirements. Transfer Pricing Aspect of Business Restructuring: Business Restructuring regulations have existed in Polish tax law since 2017.
	SK	No specific clauses - the increased cost attitude is generally accepted in the case of low value-adding intra-group services such as accounting or administrative support activities (5 %).
Intangibles	CZ	No specific clauses.
	HU	No specific clauses.
	PL	For example: provisions exist regarding analysis of comparability of intangibles.
	SK	No specific clauses.

Source: own elaboration based on CZ: (Eur-lex, 2020a; General Financial Directorate, 2012; General Financial Directorate, 2019; Income Tax Act, 1992); HU: (Government Decree No 32/2017); PL: (Jamroży, 2016; Regulation of MF, 2018a; Regulation of MF, 2018c; Doonan, Haro de, 2015; OECD, 2015; OECD, 2017a); SK: (Income Tax Act, 2003; Karelová and Slivková, 2019; Kočiš, 2019b).

Apart from Poland, there are no specific clauses for transfer pricing related to special sectors or areas. Generally speaking, there is very limited regulation of transfer pricing regarding special areas and intangibles as embodied in the acts/regulations/instructions in the Czech Republic, Hungary and Slovakia. In Hungary and Slovakia the increased cost is generally accepted in the case of low value-adding intra-group services such as accounting or administrative support activities (5 %). Entities can take the costs/ expenses incurred, add a 5% profit mark-up, and a transfer price determined in this way is accepted. For intangibles, recommendations as provided by the OECD standards should be followed.

The characteristics (type, fees, deadlines and validity) of APAs are presented in Table 66.

Table 66: APAs

<table>
<tr><th>Issue</th><th>Country</th><th>Description</th></tr>
<tr><td rowspan="4">Types of APA</td><td>CZ</td><td>The Czech domestic legal regulation does not include regulation for the APA. There is, however, another unilateral measure which differs from the unilateral APA – a binding ruling.
Bilateral and multilateral APAs are possible according to DTTs.</td></tr>
<tr><td>HU</td><td rowspan="3">Unilateral, bilateral, multilateral.</td></tr>
<tr><td>PL</td></tr>
<tr><td>SK</td></tr>
<tr><td rowspan="4">Types of fees</td><td>CZ</td><td>10,000 CZK for a binding ruling.</td></tr>
<tr><td>HU</td><td>The APA procedure fee can range from 500,000 HUF to HUF 10,000,000 HFU depending on the method used.</td></tr>
<tr><td>PL</td><td>For a unilateral national agreement: PLN 5,000 - 50,000;
For a unilateral foreign agreement: PLN 20,000 - 100,000;
For a bilateral or multilateral agreement: PLN 50,000 - 200,000.</td></tr>
<tr><td>SK</td><td>10,000 EUR for unilateral APAs and 30,000 EUR for bilateral or multilateral APAs (fixed fees).</td></tr>
<tr><td rowspan="4">Deadline for finishing the procedure</td><td>CZ</td><td>Binding ruling - no later than 3 months (set by an internal instruction of the tax authorities, not explicitly stated by the act).</td></tr>
<tr><td>HU</td><td>The APA procedure shall be conducted within 120 days. The time limit may be extended twice by sixty days.</td></tr>
<tr><td>PL</td><td>The end of proceedings in a case agreement from the date of its initiation:
unilateral - no later than within 6 months;
bilateral - no later than within 12 months;
multilateral - no later than 18 months.</td></tr>
<tr><td>SK</td><td>No later than 60 days before the beginning of the tax period for which the APA is requested.</td></tr>
<tr><td rowspan="4">Validity of the decision</td><td>CZ</td><td>Generally speaking, the decision remains valid for 3 years from the date when the decision became final (a tax authority can set a shorter validity).</td></tr>
<tr><td>HU</td><td>At least 3 years, max. 5 years. It could be prolonged for 2 years upon request.</td></tr>
<tr><td>PL</td><td>5 calendar years.</td></tr>
<tr><td>SK</td><td>5 tax periods.</td></tr>
</table>

Source: own elaboration based on CZ: Act on Administrative Charges, 2004; Brychta and Sulik-Gorecka, 2019; Eur-lex, 2020b; General Financial Directorate, 2018; Income Tax Act, 1992; Ministry of Finance of the Czech Republic, 2015; OECD, 2017a; Office of the Government of the Czech Republic, 2018; Tax Procedural Code, 2009); HU: (Act Tax Administration, 2017; Berényi, 2016; Kerényi, 2011); PL: (Tax Ordinance, 1997; Act on APA, 2019; Ministry of Finance, 2020); SK: (Financial Directorate of the Slovak Republic, 2013; Income Tax Act, 2003; Karelová and Slivková, 2019).

There are three types of APA (unilateral, bilateral and multilateral) in the V4 countries, except for the Czech Republic, where only bilateral and multilateral agreements can be found, and where there is no unilateral APA, just a Binding Ruling. The types of fees differ in countries by the type of APA, but in Hungary and in Poland there is a range of fees, while the Czech Republic and Slovakia apply fixed rates. The ending of the procedure differs from country to country. The duration of validity of the decision varies from 3 to 5 years.

When speaking of transfer pricing, safe harbours and the rules related to them cannot be omitted; for more details see Table 67 below.

Table 67: Safe harbours

Issue	Country	Description
Types of safe harbours	CZ	Simplified rules for setting transfer prices can be applied in relation to Low Value Adding Intra-Group Services.
	HU	Simplified rules for setting transfer prices can be applied in relation to Low Value Adding Intra-Group Services.
	PL	Controlled transactions constituting services with low added value, loans and bond transactions.
	SK	There is a generally accepted margin of 5% added on to costs for low value-added services (e.g. accounting or administrative support).
Threshold and approved margin requirements	CZ	A margin to the amount of 3% - 7% of costs is approved (depending on the specific situation). Services not representing a significant expense or revenue are those for which the total value of all transactions does not exceed 10% of the turnover (total revenues) and, at the same time, the amount of 50 million CZK on the part of the provider, and 20% of the operating costs and50 million CZK on the part of the recipient of the services.*
	HU	The value of the transactions in the tax year should be: • up to HUF 150 million (or maximum 10% of the taxpayers' operating costs); • and maximum 5% of the revenue of the service provider; The profit margin applied by the related party should be between 3% and 7%.
	PL	For services: a) no more than 5% of costs - in the case of purchasing services; b) no less than 5% of costs - in the case of the provision of services. For loans: the interest rate on the loan as at the date of the contract is determined based on the type of base interest rate and margin specified in the announcement of the minister competent for public finance as at the date of the contract during the financial year, and the total level of liabilities or receivables of a related entity under loan capital with related entities calculated separately for loans granted and contracted is not more than PLN 20,000,000 or the equivalent of this amount.
	SK	There is a generally accepted margin of 5% added on to costs for low value-added services (e.g. accounting or administrative support).

* To assess the limits for individuals who do not do book-keeping, data from the evidence of income and expenditure is utilized.

Source: own elaboration based on CZ: (General Financial Directorate, 2012); HU: (Government Decree No 32/2017); PL: (Act on CIT; Announcement of the Minister of Finance, 2018); SK: (Income Tax Act, 2003; Karelová and Slivová, 2019; Kočiš, 2019b).

Low value-added services and intra-group services are usually classified as a safe harbour in the most of the V4 countries. In Slovakia, no safe harbours are currently in use, but their implementation is considered as beneficial, so their introduction can be predicted following the approaches provided by the OECD. Poland has the most extensive categories of safe harbours compared to other V4 countries, namely: controlled transactions constituting services with low added value, loans and bond transactions. The acceptable profit margin in the Czech Republic and in Hungary is similar, between 3 and 7 per cent, and the regulations show other similarities. In the Czech Republic, rules are applied for Intragroup services which:

a) have low added value,
b) do not represent the main activity of the subject,
c) represent routine functions and, at the same time,
d) do not create substantial costs or revenue for the enterprises involved.

Hungary defines safe harbours in a similar way in that low value-added intragroup services should not belong to the main operating activity of the taxpayer.

In Poland, for services with low added value, the following conditions should be met (Act on CIT, art. 11f and art. 11g):

"1. the mark-up on the costs of these services was determined using the method referred to in art. 11d paragraph 1 point 3 or 4, and amounts to:
a) no more than 5% of costs - in the case of purchasing services,
b) no less than 5% of costs - in the case of the provision of services;
2. the service provider is not an entity having a place of residence, registered office or management in a territory or country applying harmful tax competition;
3. the recipient has a calculation covering the following information:
a) the type and amount of costs included in the calculation,
b) the method of application and justification for the selection of allocation keys for all related entities using the services."

For loans:

"1. the interest rate on the loan as at the date of the contract is determined based on the type of base interest rate and margin specified in the announcement of the minister competent for public finance as at the date of the contract (for example for 2019 and 2020, a 2% margin and base interest rates were determined depending on the loan currency);
2. no payments other than interest related to the granting or servicing of the loan, including commissions or bonuses, are foreseen;
3. the loan was granted for a period no longer than 5 years;
4. during the financial year, the total level of liabilities or receivables of a related entity under loan capital with related entities calculated separately for loans granted and contracted is not more than PLN 20,000,000 or the equivalent of this amount;
5. the lender is not an entity with a place of residence, registered office or management in a territory or country applying harmful tax competition.
6. The loan amounts expressed in a foreign currency are converted into PLN according to the average exchange rate announced by the National Bank of Poland in force on the last business day preceding the day of payment of the loan amount."

Many differences can also be found in the types of penalties for breaching transfer pricing rules. Table 68 lists the types of specific penalties relating to transfer pricing issues.

Table 68: Specific types of penalties relating to breaching transfer pricing rules

Issue	Country	Description
Existence of specific penalties	CZ	Yes
	HU	
	PL	
	SK	

Issue	Country	Description
Types of specific penalties	CZ	• When a taxpayer is granted a tax credit for investments and, at the same time, the taxpayer violates the arm´s length principle when setting the transfer price between him and an associated person, then he loses tax credit. Thus, the penalty for this specific case is losing tax credit provided. • In case of a failure to fulfil the notification obligations for CbCR, a penalty of up to 500,000 CZK can be imposed. The tax office may impose a fine of up to 1,500,000 CZK for failure to provide a CbCR report.
	HU	• General Tax Penalty (50%) and Increased tax penalty (200%) for failure to pay taxes. • Fixed-rate penalties – for failure in general documentation and administration. • Penalties for TP documentation: – up to HUF 2,000,000; – up to HUF 20,000,000 for a missing CbCR.
	PL	Penalties for the lack of a Management Board statement on transfer pricing documentation, penalties for lack of information on transfer prices submitted on the TP-R.
	SK	• Penalty for failure to increase the income tax base. • Penalty for failure to elaborate TP documentation. • Penalty for unauthorized corresponding adjustment of the tax base.
Existence of moderating conditions	CZ	No
	HU	
	PL	
	SK	Yes
General penalties applied	CZ	Penalty and default interest. The penalty can be waived by up to 75% and the default interest by up to 100% (depending on the criteria as set by the Tax Procedural Code being met).
	HU	50% or 200% of tax loss in case of failure in paying taxes. General fixed rate penalties in case of missing documentation (for example corporate tax return) up to 500,000 – 1,000,000 HUF. Penalties for missing TP documentation up to 20,000,000 HUF.
	PL	Additional tax liability amounts to 10% of the sum of the tax loss undisclosed or overstated, and not disclosed in whole or in part as taxable income in the scope resulting from this decision.
	SK	In cases where the arm's length principle is infringed, a penalty of three times the European Central Bank (ECB) prime interest rate or 10% (whichever is higher) is applied. If the taxpayer deliberately decreases the tax base due to applied transfer prices, then a double penalty of the interest rate (20%) can be applied. In case of a failure to fulfil the notification obligations for CbCr, a penalty of up to 3,000 EUR can be imposed. The tax office may impose a fine of up to 10,000 EUR for failure to report by country. If the taxpayer fails to submit transfer pricing documentation to the tax authority within the stipulated deadline, then the taxpayer commits an administrative offense and penalties may be generally imposed up to the amount of 3,000 EUR (this penalty may be imposed multiple times).

Source: own elaboration based on CZ: (Income Tax Act, 1992; Tax Procedural Code, 2009); HU: (Act on Tax Administration, 2017; Berényi, 2016); PL: (Tax Ordinance, 1997; Penal Fiscal Code, 1999); SK: (Income Tax Act, 2003; Ronnes, 2018; Tax Procedure Code, 2009).

In all the V4 countries, there are some special penalties for failures relating to transfer pricing rules, but only in Slovakia are there moderating conditions for these specific types of penalties. If the taxpayer does not appeal against a decision of the tax office and pays the difference of the levied tax within the period of lodging an appeal, the double increase of the penalty shall not apply. The lower penalties shall be imposed on taxpayers who requested a tax administrator to approve the APA (the amount of basic interest rate of the ECB - at least 3%). Also, in cases where the taxpayer submits an additional tax return in which a higher tax liability compared to the previous tax base is declared, a penalty equal to the basic rate of the ECB (at least 3%) of the additional tax liability shall be applied. Apart from the Czech Republic, the V4 countries have specific penalties for infringements related to transfer pricing documentation; these are, as a rule, higher than general tax penalties.

Table 69 shows the types of additional transfer pricing statements.

Table 69: Additional transfer pricing statements

Issue	Country	Description
Existence of additional statements	CZ	Yes
	HU	
	PL	
	SK	
Types of statements/reports	CZ	A special annex to the tax return for Corporate Income Tax. There is, however, no such annex in the case of the tax return for the Personal Income Tax.
	HU	Obligation to fill in tax return annexes related to the transactions of the associated parties.
	PL	Since 01 January 2017: 1. Statement on the preparation of tax transfer pricing documentation by the end of the ninth month after the end of the financial year. 2. Information on transfer prices submitted to the Head of the National Tax Administration. 3. Report on the implementation of the advanced pricing agreement for each tax year covered by the previous price agreement, within the time limit appropriate for submitting the annual tax return.
	SK	Obligation to fill in tax return annexes related to the transactions of the associated parties. Annex to the tax return related to the transactions of associated parties and notification in case of tax base adjustment.

Source: own elaboration based on CZ: (Act on Accounting, 1991; Decree No. 500/2002 Coll. implementing some provisions of the Act on Accounting, 2002; Financial Administration, 2020; Income Tax Act, 1992); HU: (Act on Corporate Tax, 1996; Berényi, 2016; Government Decree No 32/2017); PL: (Act on APA, 2019; Act on CIT; Regulation of MF, 2018c; Błażejewska-Gaczyńska, 2019); SK: (Income Tax Act, 2003; Karelová and Slivková, 2019; Guideline of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724).

All V4 countries have an additional statement for transfer pricing documentation. In the Czech Republic, Hungary and Poland there are special annexes to the tax return for corporate tax.

The differences in burden of proof and transfer pricing issues settled by case-law are presented in Table 70.

Table 70: Burden of proof and selected transfer pricing issues settled by case-law

Issue	Country	Description
Burden of proof	CZ	Case-law has an established process (rules) for bearing the burden of proof for transfer pricing cases – there are some specifics compared to regular cases. Primarily on the part of the taxpayers, but if they are prosecuted by a tax authority then the burden of proof switches to the tax authority. Case-law has an established (confirmed) number of protective measures for the benefit of the taxpayer.
	HU	The burden of proof lies with the taxpayer.
	PL	The burden of proof lies with the administrative body.
	SK	Case-law has an established process (rules) for bearing the burden of proof. Primarily on the part of the taxpayers, but if they are prosecuted by a tax authority then the burden of proof switches to the tax-authority. Case-law has an established (confirmed) number of protective measures for the benefit of the taxpayer.
Areas	CZ	Covering above all procedural aspects when setting the rules that are valid for taxpayers and tax authorities, for example: Rules for bearing the burden of proof; Limits of judicial review; Use of Expert Opinions when setting the transfer price; Application of selected methods for setting the transfer price; Expert opinions on transfer pricing issues.
	HU	Application of different TP methods, loans, transactions in different countries.
	PL	Documentation obligation, guarantees, income estimates, loans, cash-pooling, sanction tax rate, , the cost plus method.
	SK	Application of OECD Transfer Pricing Guidelines, although these are not legally binding but are adopted with the intention of achieving a practical effect.

Source: own elaboration based on CZ: (Judgement of the Regional Court in Hradec Králové (a branch in Pardubice) of 16 March 2016 File No. 52 Af 34/2014; Solilová and Nerudová, 2019; Judgement of the Supreme Administrative Court of 04 August 2005 File No. 2 Afs 13/2005; Judgement of the Supreme Administrative Court of the Czech Republic of 27 June 2007 File No. 1 Afs 60/2006; Judgement of the Supreme Administrative Court of the Czech Republic of 31 March 2009 File No. 8 Afs 80/2007; Judgement of the Supreme Administrative Court of the Czech Republic of 27 January 2011 File No. 7 Afs 74/2010; Judgement of the Supreme Administrative Court of the Czech Republic of 02 March 2011 File No. 8 Afs 19/2010; Judgement of the Supreme Administrative Court of the Czech Republic of 13 March 2013 File No. 1 Afs 99/2012; Judgement of the Supreme Administrative Court of the Czech Republic of 13 June 2013 File No. 7 Afs 47/2013; Judgement of the Supreme Administrative Court of the Czech Republic of 31 October 2013 File No. 7 Afs 86/2013); HU: (Decisions of the Curia, 2020a; 2020b, 2020c); PL: (DMS, 2019); SK: (Judgement of the Regional Court Bratislava No. 1S/231/2016 from 20/9/2018; Judgement of the Supreme Court of the Slovak Republic No. 2 Sžf 18/2012 from 23/10/2012; Judgement of the Supreme Court of the Slovak Republic No. 2Sžf/76/2014 from 14/4/2015; Judgement of the Supreme Court of the Slovak Republic No. 3 Sžf 101/2008 from 23/4/2009; Judgement of the Supreme Court of the Slovak Republic No. 8 Sžf 15/2015 from 23/2/2017).

The burden of the proof lies primarily with the taxpayer, except in Poland. If a taxpayer is prosecuted by a tax authority, then the burden of proof switches to the tax-authority in the Czech Republic and Slovakia. It appears that the most extensive case-law governing transfer pricing issues is that in the Czech Republic. In the other countries, the most frequent issues heard by the Courts relate to the application of transfer pricing methods, loans, documentation obligation and the cash pooling sanction tax rate.

Generally, the similarities between the transfer pricing rules in the countries originate in the implementation of OECD Guidelines and EU directives. The main differences lie in the diverse legal systems, the characteristics of tax regulations, and the different ways benefits are provided, for example the exemption from the documentation obligation for SMEs in Hungary, or the simplified documentation in Slovakia.

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CHAPTER 10
SHORTCOMINGS IN *DE LEGE LATA* AND *DE LEGE FERENDA* CONSIDERATIONS

10.1 CZECH REPUBLIC

The results of the comparison with other V4 countries support the results presented in a study by Ignat and Feleagă (2017). The Czech Republic can be classified as a country with less strict transfer pricing legal regulations. The legal regulations as embodied in acts are extremely limited compared to Hungary, Poland and Slovakia. This fact can be viewed as an advantage or a disadvantage depending on the factor assessed and on the party providing the assessment. In Czech expert literature, one can find a number of critical assessments regarding the absence of specific and detailed transfer pricing rules (see e.g. Radvan et al., 2016; Solilová and Nerudová, 2019). Radvan et al. (2016)[131] summarize that Czech legal regulations are extremely vague, and as such do not provide enough 'instructions' for the tax authorities with regard to the procedure for setting the so-called reference price.

10.1.1 *DE LEGE FERENDA* CONSIDERATIONS – MATERIAL LAW

Definition of associated persons/related parties and related issues

Regarding the definition of associated persons/related parties as provided in the Income Tax Act (Income Tax Act, 1992, Sec. 23(7)) one can conclude that the definition is quite broad, and in many aspects very general. However, due to existing case-law[132], which defines the general terms, the wording as such (i.e. categories of taxpayers covered) can be considered sufficient. However, the category of persons otherwise associated, namely, *"Persons that have created a legal relationship predominantly for the purpose of reducing the tax base or increasing a tax loss"* (Income Tax Act, 1992, Sec. 23(7) letter b) item 5.), would appear to be problematic – much higher demands are placed on the tax authorities with regard to bearing the burden of proof. The rules for the application of this provision are, however, established by case-law. This provision was not established solely for cases of transactions with non-cooperating tax jurisdictions. The question is whether it would be suitable to establish a separate category of persons otherwise associated, which would explicitly cover transactions directed to these types of jurisdictions. On the other hand, one should not forget that the arm´s length principle is the last test applied (after substance and benefit tests). This fact makes it possible for the tax consequences of artificial transactions to be eliminated without the need to apply the rules of Sec. 23(7) of the Income Tax Act.

There is, however, a different problem in the definition of associated persons/related parties and in the way the 'market price' should be set. Without any doubt, there is, despite different rules and principles, a direct and obvious linkage between revenues/incomes and value added tax (VAT). It is a relatively common occurrence that when a tax audit focused on transfer pricing takes place, then the tax audit is connected (or subsequently extended) to a VAT tax audit. The VAT Act, however, contains its own definition of associated persons/related parties, provided under:

a) Sec. 5a where the group for the reasons of the VAT Act is defined (VAT Act, 2004, Sec. 5a) and
b) Sec. 36a where the rules for setting the VAT tax base for specific situations are included (VAT Act, 2004, Sec. 36a).

Considering the topic of transfer pricing, the latter provision of the VAT Act is more relevant, and the problems are as follows. Despite the fact that the rules as embodied under Sec. 36a of the VAT Act (VAT Act, 2004) relate to a limited number of situations, this still raises some potential problems since a tax-subject can potentially be forced to apply different rules to the same case in order to meet the requirements as set by the Income Tax Act and VAT tax Act.

131 They suggest implementing at least the traditional transactional methods in order to establish obvious and more appropriate rules for setting the reference price (Radvan et al., 2016, pp. 172-174). While presenting general *de lege ferenda* proposals for transfer pricing standards, these authors point to missing guidance in the case of tax residents from non-contracting countries, when for contracting countries the OECD Transfer Pricing Guidelines seem to be applicable.

132 For example, see the Judgement of the Supreme Administrative Court of the Czech Republic of 19 December 2018, file No. 5 Afs 214/2016 in which the Supreme Administrative Court refers to the case-law of the Supreme Court of the Czech Republic on the basis of which the first mentioned Court concludes that even a legal entity can be considered a close person to an individual, if certain conditions are met at the same time, and thus application of Sec. 23(7) of the Income Tax Act was possible.

The VAT Act defines associated persons/related parties in a similar way as:

a) subjects having a direct or indirect share in the capital or voting rights (at least 25%)[133];
b) subjects otherwise associated according to Sec. 5a (4) of the VAT Act; a person who is a member of the supervisory bodies of both subjects is not considered to be a person otherwise associated;
c) close persons;
d) shareholders of the same company. (VAT Act, 2004, Sec. 36a (3)).

In this respect, one can conclude that the definitions of associated persons/related parties in the Income Tax Act and VAT Act do at least overlap. However, total unification of the definitions for the purposes of the application of the VAT Act and Income Tax Act would seem to be reasonable.

A more serious problem regards the way (the rules) the 'transfer price' is set. The VAT Act refers strictly to the price as set by the Act on Property Evaluation, while for the Income Tax Act, the application of the Act on Property Evaluation (Act on Property Evaluation, 1997) and the rules embodied therein represent the last possible option. Furthermore, the *stricto sensu* application of all the principles/rules as given in the Act on Property Evaluation is, potentially at least, in conflict with the arm´s length principle. It is worth mentioning that the Act on Property Evaluation 'covers' only domestic situations[134]. Sec. 2(1) of the Act on Property Evaluation reads as follows, *"The valuation of assets or services shall be based on the usual price, unless this Act provides for a different method of valuation. For the purpose of this Act, 'usual price' shall mean the price that would be obtained when selling an identical or similar asset or when rendering identical or similar services in usual commercial relations in the Czech Republic as of the day of valuation. At the same time, all circumstances influencing the price shall be taken into account. However, the influence of extraordinary market circumstances, the personal situation of the seller or buyer, and any special preferences shall be disregarded. 'Extraordinary market circumstances' shall mean, for instance, a seller's or buyer's state of duress, the consequences of natural or other disaster. 'Personal situation' shall mean proprietary, family and other personal relations, in particular between the seller and buyer. 'Special preference' shall mean a particular value attributed to an asset or service arising from a personal relationship thereto."* (Act on Property Evaluation, 1997, Sec. 2(1)) Thus, the reference to the application of the Act on Property Evaluation as included under Sec. 23(7) of the Income Tax Act (Income Tax Act, 1992, Sec. 23(7)) should be modified in such a way so that even when the Act on Property Evaluation is applied, the arm´s length principle shall be observed. As a result of this modification, there would be clear instructions for the taxpayer and for experts preparing their expert opinion on the reasons for setting the price according to Sec. 23(7) of the Income Tax Act (Income Tax Act, 1992, Sec. 23(7)).

Rights and duties of relevant subjects

Considering the rights and duties of relevant subjects, many potential problems could arise due to the absence of precise rules in the acts. Thanks to the rather extensive and well-established case-law, one can conclude that many of these have been eliminated. The 'sword' of the absence of rigid legal regulation seems to be double-edged. The requirements as set by the relevant case-law of the administrative Courts charges the tax authorities with many duties and imposes many limitations (see for example Solilová and Nerudová, 2019[135]).

Transfer pricing documentation

Unlike other V4 countries, transfer pricing documentation is not obligatory in the Czech Republic. On the part of the Ministry of Finance of the Czech Republic there has been a consistent position: preparation of transfer pricing documentation shall be kept as optional (Kapoun, 2020). As far as *de lege ferenda* considerations regarding transfer pricing documentation are concerned, there is definitely no definitive recommendation. Generally speaking, taking into account the position of taxpayers, the absence of another obligation in the current complicated legal system may be seen as welcome. However, imposing an obligation for the creation of transfer pricing documentation can be beneficial for the reasons stated below:

a) when transfer pricing documentation is prepared properly, it helps with the understanding of relations and processes and, at the same time, it makes bearing the burden of proof easier when there is a tax audit focused on transfer pricing;

133 A reference is made to Sec. 5a of VAT Tax – a definition is partly taken from this provision while being modified; in this respect there is a decrease in the share in the capital or voting rights (from 40 % to 25 %). (VAT Act, 2004, Sec. 36a)

134 See the reference to the Czech Republic as included in the determination of Valuation Methods for Assets and Services (Act on Property Evaluation, Sec. 2(1)).

135 For more details see Solilová and Nerudová (2019, Chapter 7).

b) the position of Czech subsidiaries of parent companies abroad would improve since the subsidiary would be able to demonstrate the need to provide relevant data in order to meet the requirements as set down by law. Currently, the financial managers of Czech subsidiaries of parent companies abroad usually face the unfounded argument that there is no need be provide information since transfer pricing documentation is not obligatory in the Czech Republic.

When comparing the legal regulations with other V4 countries, many questions arise with regard to the concept of obligatory transfer pricing documentation:

a) What is the best/most appropriate solution regarding levels of transfer pricing documentation?
b) Which category of entities will be excluded from this obligation, if any at all?
c) What will the penalties be for failing to meet this obligation?
d) What will the rules be for the submission of transfer pricing documentation?

It would seem reasonable to introduce multilevel transfer pricing documentation (as in other V4 countries), and to establish some reasonable exemptions from the obligation to prepare transfer pricing documentation. If transfer pricing documentation is established obligatory, a special penalty should be imposed for failing to meet this obligation. However, a penalty in the form as set out by Polish law could be viewed as eccentric. If it is insufficient to include transfer pricing documentation as an annex to a tax return, this information should be submitted upon request.

As regards the current *status quo*, there is one more aspect that is worth mentioning. There is very limited explicit legal regulation of transfer pricing embodied in the acts. Establishing obligatory transfer pricing documentation for existing legal regulations (the existing *status quo*) would be contrary to basic law-making principles, and could be compared to building the walls of a house when there are no foundations in place.

10.1.2 *DE LEGE FERENDA* CONSIDERATIONS – PROCEDURAL LAW

Procedural legal regulations for transfer pricing are included in the Tax Procedural Code (Tax Procedural Code, 2008) and partly in material law (especially in the Income Tax Act, which also contains some procedural rules).

Bearing the burden of proof

The rules for bearing the burden of proof in transfer pricing cases have again been established by case-law, which fits perfectly with the protection of taxpayers as the weaker party in the public law relationship in situations of uncertain and vague legal regulations. In this respect, the situation can be considered to be stable and clear, and implementing any changes could be seen as breaching the idea of discreteness in legislation (that is not changing what works properly).

Advance Pricing Agreements/Binding Ruling

Advance Pricing Agreements are not included in the Czech legal system, there is only a Binding Ruling which does not meet the requirements set by the OECD (2017a) for Advance Pricing Agreements (for a comparison see Brychta and Sulik-Gorecka, 2019). It would be appropriate to replace the rules for the Advance Pricing Agreement with the APA, for which Polish legal regulations could provide inspiration. This change would be a significant one as the binding ruling is based on different principles and only allows for two possible results (a positive or negative decision; no compromise regarding the submission can be reached).

Mutual Agreement Procedure rules

The Tax Procedural Code (2009) can ultimately be considered as the only domestic procedural act that contains the rules for the mutual agreement procedure. In fact, the Tax Procedural Code does not contain specific rules for when this type of procedure includes an international element – thus, general clauses originally intended for domestic cases are applied. Furthermore, the Czech Republic has been criticized by the OECD for the absence of publicly available guidelines for bilateral and multilateral APAs (OECD, 2018). This situation should have been remedied by the implementation of the Directive on Tax Dispute Resolution (Eur-lex, 2020)[136]. The original intention was to respond to the criticism of the OECD and

136 The Member States should have brought into force laws, regulations and administrative provisions necessary to comply with this Directive by 30 June 2019 at the latest (Eur-lex, 2020; Art. 22 (Transposition)).

establish a separate act defining clear rules for mutual agreement procedures for all contracting states, as well as extra rules for EU Member States. Thus, this act would have gone beyond the obligations as set by the Directive. Unfortunately, the very first material explaining the rules and procedures was an explanatory report accompanying the Government Bill (Office of the Government of the Czech Republic, 2018). Disappointingly, the concept of the Government Bill underwent significant alteration, and its existing version[137] covers only 'a fragment' of the originally intended scope of material (Chamber of Deputies of the Parliament of the Czech Republic, 2019).

The final draft may meet the obligations resulting from the Directive on Tax Dispute Resolutions. It does not, however, eliminate qualified reservations presented by the OECD (OECD, 2018). A different concept (a separate act) is greatly needed to provide taxpayers with clear, detailed and transparent rules for tax dispute resolutions in general. A return to the original concept would be helpful. For example, Slovakia responded to the requirement of the last Directive by adopting an act which covers both EU and contracting states (Slovak Act on Rules for Tax Dispute Resolutions, 2019). Such a concept can be seen more suitable, and in order to eliminate gaps in the information provided to taxpayers, guidelines providing relevant information should be published by the General Financial Directorate.

10.1.3 *DE LEGE FERENDA* CONSIDERATIONS – GENERAL AND MORE COMPLEX ISSUES

Recommendations in the case of preservation of the *de lege lata* status quo

On the basis of the comparison of the manner and number of rules adopted from OECD and/or EU standards into domestic legal systems (in acts) in other V4 countries, one could claim that Czech legal regulations need significant improvements. However, as indicated above, there is a problem with this. The explicit legal regulation of transfer pricing embodied in the acts is very limited. Adoption of a number of the rules followed in other V4 countries would assume adoption of basic OECD and EU standards in the clauses of acts in order that the requirements for setting tax duty in the form of an act be met[138]. The principal question is whether there is in fact such a need. The Czech Republic's legal regulation of transfer pricing is by far the least strict compared to the legal regulation in the remaining V4 countries. Such a status has its pros and cons. However, even if there is no adoption of the amendments on the level of acts, then it is at least desirable that taxpayers be provided with:

a) more detailed guidance on the comparative analysis, including specification of the limits on the use of internal comparables for setting the transfer price;
b) more detailed guidance on the application of particular methods for setting the transfer price. This is necessary as existing guidance – despite representing a significant improvement compared to its predecessor – is very short and too general;
c) special guidance on specific situations/types of transactions – above all for transactions with intangibles and financial transactions[139];
d) more detailed guidance relating to databases and their use[140];
e) an update to the guidance for transfer pricing documentation (the existing one is out-of-date);
f) detailed guidance containing specification of the rules for international tax dispute resolutions.

Recommendations in the case of the adoption of OECD and EU standards into domestic law

If the legal regulation as embodied in the acts became similar to the one in force in Slovakia, then it would be possible to consider extending legal regulations to include other rules and standards. In this respect, it seems reasonable to:

a) adopt simplified rules for selected financial transactions (see for example the rules as embodied in Polish legal regulations);
b) establish obligatory transfer pricing documentation;
c) set up special (stricter) conditions if transactions are realized with subjects from a non-cooperative tax jurisdiction (tax haven).

137 A version submitted to the Chamber of Deputies of the Parliament of the Czech Republic.
138 See Charter of Fundamental Rights and Freedoms (1993, Art. 11(5)).
139 Guidance for financial transactions is under preparation at the General Financial Directorate (Kapoun, 2020).
140 There is a serious problem with the reliability of the data, and a problem in finding a relevant sample for the comparison.

10.2 HUNGARY

10.2.1 *DE LEGE FERENDA* CONSIDERATIONS – MATERIAL LAW

In Hungary, the main problem with the definition of associated persons lies in the legal regulations. A large number of existing acts regulate this issue, and there are many acts that define an associated person (for example: Act on Accounting, 2000; Act on Corporate Tax and Dividend Tax, 1996) with different definitions of associated persons. The relevant regulation for transfer pricing is the definition in the Corporate Tax Act, where the wording refers to an additional legal source document the Civil Code (2013) in order to cite a definition of the major influence. One can conclude that finding the proper definition of associated person could be confusing for companies, as half of the definition can be found in the Corporate Tax Act while the other half is given in the Civil Code. Furthermore, the transfer pricing documentation obligation is legalised in an additional source of law - a government decree (Decree No. 32/2017. (X.18.)).

The most frequent mistake regarding the application of the definition is that the indirect association is not considered, and the votes of individual members are not summarized. Often, companies examined the shares instead of the votes. Another frequent mistake is that no association regarding executive identity is determined (or is needlessly determined), and often close family members are also falsely taken into consideration. In Hungary, it is necessary to take municipal corporations into consideration for associated parties, however, this is often omitted from the register. Furthermore, not only the executive but also the members of the management are to be considered as an associated person.

The documentation obligation could result in mistakes and inaccuracies related to transfer pricing. For example, it is not only the beginning of an associated relationship (the first time of conducting the activity, the first time that the associated persons make a transaction) that should be reported, but also the end of the relationship. There are several exemptions from the transfer pricing documentation obligation, the most important being the exemption of SMEs and the exemption of transactions up to 50,000,000 HUF (transfer price).

In Hungary, there is an obligation to conduct a corporate tax base adjustment. Taxpayers should increase the tax base if, as a result of the actual applied price, the earnings before taxes are lower than they would have been at transfer prices. Taxpayers should reduce the tax base if, as a result of the actually applied price, the earnings before taxes are higher than what would have been obtained at the transfer price, and if the required conditions are met. Companies often fail to meet this obligation and the documentation for transfer pricing does not correspond with the documentation for the corporate tax return.

A clear conclusion can be drawn here, which is that a simplification of the rules is needed. Currently, there are several sources of law regarding transfer pricing and the definition of associated parties. Simplified rules would make it easier for companies to find out whether they are obliged to submit documentation or not. Furthermore, the simplification could result in the decreasing of errors in transfer pricing documentation, as more companies would realise that they are under obligation to provide documentation. The suggestions regarding legal regulations and definitions are listed below:

a) translation of the current version of the OECD Guidelines,
b) reduction in the number of acts regulating transfer pricing issues,
c) harmonisation of the definitions stated in different source of law,
d) preparation for companies of short guidelines or summaries of given chapters of the acts referring to transfer pricing issues.

10.2.2 DE LEGE FERENDA CONSIDERATIONS – PROCEDURAL LAW

In Hungary, the burden of proof lies with taxpayers. Companies with associated persons must prove that they have followed the legal regulations regarding transfer pricing documentation and the applied transfer pricing method.

To decrease the risks related to taxation, Hungarian companies have the opportunity to demand an advanced pricing procedure from the tax authorities. The price depends on the type of APA procedure. The time limit for the procedure is 120 days, but this can be extended twice by 60 days due to the length of communication with foreign tax authorities. The validity of the APA is generally five years, but it can be extended by an additional two years. Problematic issues lie in the cost of the procedure, as smaller companies often cannot afford the price, and do the comparability analysis on their own or using a cheaper tax consultancy. The APA legal regulations are clearly defined in the Act on Tax Administration and the Regulation of Tax Administration (Act on Tax Administration and the Regulation of Tax Administration, 2017). Reducing the cost of APAs could increase the number of applicants.

In Hungary, there are generally two main types of tax penalties: general penalties in percentages, and fixed-rate penalties. The general tax penalty is 50%, but there is a higher-level tax penalty (200%) in cases of serious breaches. Fixed-rate penalties are applied in cases where documentation obligations are not met (the amount of the fine varies from case to case, and depends on the decision of the tax authorities – up to 500,000 or 1,000,000 HUF). For transfer pricing, there are higher penalties and the value of the fine can be up to 2,000,000 HUF for failure to submit transfer pricing documentation, while for a missing CbCR, there is an extremely high penalty of 20,000,000 HUF. One can conclude that the system of transfer pricing penalties is advanced and functions well in Hungary, since high transfer pricing penalties result in taxpayers paying even more attention to this issue of taxation and to tax audits. The *de lege ferenda* proposals are summarized below:

a) reducing the cost of APAs for companies (for example, depending on revenue),
b) maintaining the system of higher tax penalties for transfer pricing as this results in more attention being given to paying taxes and providing correct documentation.

10.2.3 *DE LEGE FERENDA* CONSIDERATIONS – GENERAL AND MORE COMPLEX ISSUES

Hungary has incorporated OECD and EU standards into its domestic legal regulations. Several chapters of the current acts simply contain the rules of the OECD Transfer Pricing Guidelines, however there is no translation of the current version of the OECD TP Guidelines.

Low value-added intra-group services could be mentioned as safe harbours. The value of transactions in the tax year may be up to 150,000,000 HUF (or maximum 10% of the taxpayer's operating costs), and a maximum of 5% of revenue for service providers. Low value-added intra-group services include IT services, administrative services and transportation services, but the rules are not different for each group as they are in Poland. One could suggest that the Polish regulations are an example of 'best practice', and their adoption would be beneficial in Hungary.

The documentation obligation (three-level documentation and comparability analyses) does not include any simplification, as in Slovakia, but there are some exceptions for taxpayers. The most important exemptions are for SMEs, who do not have to provide transfer pricing documentation. Non-profit organisations are exempt too, as well as companies with considerable state involvement. If the annual transaction value is lower than 50,000,000 HUF at the group level, this qualifies for the exemption. Furthermore, free services are not obliged to provide documentation. The large number of exemptions from submitting transfer pricing documentation are beneficial for taxpayers, but not for the tax authorities as this means there is less company transparency. A simplification of the transfer pricing documentation obligation, such as that applied in Slovakia, would be useful in Hungary, too.

The legal regulations describe acceptable transfer pricing methods, but a problematic issue for companies is that there is no scheme or sample file for the documentation with the expected format. We suggest that a sample file for TP documentation (comparative analysis) would be beneficial for both companies and the tax authority.

Companies and tax consultancies can use several databases for documentation, for example, Amadeus or other domestic databases. The problematic issue here is usually the cost of these databases, but there are methodological disputes too. In international databases, country characteristics, price levels, efficiency, etc. are different and are not unadjusted for analysis. For domestic databases, it is even more difficult to find at least 10 comparatives.

In Hungary, there is a frequent problem in the preparation of transfer pricing documents, in that companies often do not know the structure of the group, do not have enough information about the parent company or do not have an insight into its intangibles, R&D and operating processes.

The *de lege ferenda* proposals are summarized below:

a) Applying different rules and percentages for different groups of low value-added intra-group services, for example, transportation or IT services.
b) Applying simplified transfer pricing documentation for companies with different levels of revenue. The Slovak regulations could serve as 'best practice'.
c) Maintaining the system of exemptions (for example, SMEs and non-profit organisations)
d) Providing a sample file for transfer pricing documentation and the comparative analysis. This would be beneficial both for companies and tax authorities, as it could increase the amount of correct documentation submitted.

10.3 POLAND

10.3.1 *DE LEGE FERENDA* CONSIDERATIONS – MATERIAL LAW

Poland is very advanced in the field of implementing OECD and EU standards into domestic law. However, there are still specific areas of the regulations that need improvement.

For example, it should be pointed out that compared to other countries, e.g. Slovakia, there is no possibility of preparing simplified transfer pricing documentation. Preparation of transfer pricing documentation, which in Poland should also include a comparability analysis, is often a challenge for taxpayers. Perhaps the option of preparing simplified documentation should be implemented, provided that the conditions specified in the law are met.

Although Poland has implemented safe harbour solutions for some transactions, one issue that remains unresolved in the regulations is that of transactions using re-invoicing. It is worth considering proposals that allow for exemptions from the obligation to provide documentation, introduce simplified documentation, or even propose a safe harbour solution for re-invoicing. (Forum Cen Transferowych, 2019c)

The need to prove compliance of transactions carried out with the arm's length principle leads to difficulties in conducting comparability analyses. Currently, the provisions in Poland do not contain detailed information on how to conduct such analyses.

Recommendations are available from the Transfer Pricing Forum of the Ministry of Finance, these, however, do not have the status of legally binding legal regulations. Perhaps it would be necessary to include the conclusions in the acts on such detailed issues regarding comparability analysis as: the criterion of locality and data availability, the possibility of using internal data, the possibility of using offer data, the use of so-called secret comparables, the legitimacy of rejecting entities at a loss, minimum sample size, choosing a point from the range, and updating a comparative analysis (Forum Cen Transferowych, 2019b). Polish regulations include the option to conduct a compliance analysis when it is not possible to conduct a comparability analysis (Act on CIT, art 11q). However, the regulations do not contain details regarding the form and scope of the compliance analysis.

The following forms of compliance analysis should be allowed: independent expert valuations, generally available market or industry analyses, market quotations commonly used in a given industry or other data on prices used (which due to the nature of the transaction cannot be considered as data for a comparative analysis), information on price offers (including data from websites), terms of settled tenders, tariffs, indicators, multipliers, etc., which may indirectly apply to the transactions analysed (in case they cannot be considered as data for the preparation of a comparative analysis), data available internally to the taxpayer, e.g. contracts with contractors, internal company policies, others, product life cycle analysis, replacement value, residual value, alternative cost (e.g. losses that would have been incurred by the taxpayer if the transaction had not been concluded), benefits of the parties to the transaction, return on investment, other real options actually available to the taxpayer (Forum Cen Transferowych, 2019a).

Analysing the voices of the tax advisors and entrepreneurs, a topic that definitely requires extension of legal regulations are transfer price adjustments. Although Poland has introduced into legal acts since 01.01.2019 the possibility of applying corrections, some issues need clarification e.g. in the field of repatriation of income to the competent entity without the risk of re-taxation of previously taxable income (Bajgier, 2019).

As part of further adaptation of Polish law to BEPS, regulations regarding financial transactions, transactions related to trading in intangible assets as well as restructuring regulations require extension.

Referring to the fact that there is an exceptionally large number of acts regulating transfer pricing in Poland compared to other V4 fund countries, one should consider the possibility of limiting the disparity of regulations in order to simplify the tax system in this respect. Considering the fact that Polish regulations are based on OECD guidelines, it would be beneficial for taxpayers to translate them into Polish.

10.3.2 *DE LEGE FERENDA* CONSIDERATIONS – PROCEDURAL LAW

On November 14 2019, the act on settlement of disputes regarding double taxation and conclusion of advanced pricing agreements was published (Act on APA). The act implements, inter alia, the Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union (Eur-lex, 2020).

This combination of two very important issues in one document met with criticism in Poland, therefore in the future it may be appropriate to separate the subject of settlement of disputes regarding double taxation from the conclusion of advanced pricing agreements.

The original draft bill allowed for the possibility of simplified completion of APAs for controlled transactions regarding:

1. purchase of services with low added-value and
2. incurring of fees for the use or the right to use:
   - trademarks,
   - knowledge (information) related to experience gained, suitable for use in industrial, commercial, scientific or organizational activities (know-how).

The draft bill includes a deadline for concluding agreements of within three months, and an administrative fee of PLN 20,000. During the legislative process, the simplified APA procedure was abandoned. The only option left for opening an APA case is that of a foreign entity planning to conduct an investment in Poland, as a result of which a domestic entity will be created with which the foreign entity will enter into controlled transactions. This solution would increase the attractiveness of planned investments in Poland, but this case was not accepted (Szulc, 2019).

Under the aforementioned Act, the new chapter IIB 'Cooperation' was introduced to the Tax Ordinance (Act on APA, art. 111), which will come into force on 1 July 2020. This includes the possibility of concluding a cooperation agreement with a taxpayer whose income in the previous tax year exceeded the equivalent of EUR 50,000,000.

The legislator's goal was to "ensure compliance of the taxpayer with tax law provisions in conditions of transparency of actions taken, as well as mutual trust and understanding between the tax authority and the taxpayer, taking into account the nature of the taxpayer's business" (Tax Ordinance, art 20s).

The initiative was addressed to entities with the largest so-called strategic economic potential. It seems, however, that the provisions need to be clarified by the addition of implementation provisions.

Considering the fact that the number of advanced pricing agreements concluded in Poland is still relatively small, perhaps the implementation of a simplified APA procedure covering a broader scope of agreements should be reconsidered.

10.4 SLOVAKIA

Problematic issues and areas can generally be divided into two groups. The first group contains mainly legislative and technical legal areas and the second group consists mainly of pure practical applications of transfer pricing rules and procedures. The most common problems arise due to the fact that the current legislation related to transfer pricing issues refers to OECD sources which are not legally binding.

10.4.1 *DE LEGE FERENDA* CONSIDERATIONS – MATERIAL LAW

The definition of associated persons is quite often amended and complemented. There have been significant changes and amendments in recent years, mainly those in effect since 2014, 2015, 2017 and 2018. One can notice that the development of associated persons definition tries to connect the definitions or their characteristics to several laws[141]. The definition of associated persons is gradually expanding not only by the new categories of associated persons but also by using new terminology (e. g. entity). Kočiš (2019) states that the definition of associated persons in the category "other ties (associated parties otherwise)" according to Section 2(p) of the Income Tax Act provides relatively limited information and a lack of requirements for the continuous existence of dependency criteria. One can notice that the lack of a clearly defined "other ties" category can potentially cause the problem that taxpayers have no knowledge or are not aware that a dependent relationship exists. The current definition of other ties[142] could be assessed as too general and does not provide close significant characteristics. The amendment of this definition or definition characteristics would also definitely be a challenge due to the problematic issues linked to aggressive tax optimization[143]. The same situation also occurs for the combination of economic, personal or other ties in regards to the establishment of a mutual relationship between persons or the formation of associated persons. For this category, Kočiš (2019) also suggests that the mentioned category of associated persons should be clearly stipulated by the Income Tax Act to remove ambiguous interpretations and to support the legal certainty of the tax subject.

Subordinate legislation for transfer pricing regulation is focused solely on documentation issues and the relevance of the OECD Guidelines on Transfer Pricing is highlighted as a material source of law. As the guidelines issued by the Ministry of Finance of the Slovak Republic are not generally binding legal provisions[144] (and therefore are not formal sources of law), one can notice that the implementation of selected parts of the material nature of the OECD TP Guideline directly to Income Tax Act can significantly increase the legal certainty for both taxpayers and tax authorities[145]. On the other hand, the issuing of the guidelines has a positive effect for procedural law[146]. The issued methodological guidelines are relatively general and contribute minimally to solving specific problems arising in the application of transfer pricing rules. The regular publishing of practical examples with focus on selected sectors or different sizes of enterprises would definitely help entrepreneurs to better handle transfer pricing issues.

Another problem with the application of the current OECD TP Guidelines[147] is the lack of a translation into the Slovak language. Such available translations would significantly help in the practical application of transfer pricing rules and such a document could also be served as a tool to be included in tax audit protocols[148].

10.4.2 *DE LEGE FERENDA* CONSIDERATIONS – PROCEDURAL LAW

There is a relatively low interest in using APAs in the Slovak Republic. The APA approval process is very demanding, and the current conditions are mainly set for large companies. One can notice that the current conditions for the APA approval process are clear and relatively well described. Looking at current settings, the implementation of safe harbours seems to be another important step towards an increase of legal certainty for both taxpayers and tax authorities and an important step to improved level of transfer pricing legislation in the Slovak Republic.

The application of safe harbours is currently missing in Slovak domestic legal regulation. One can notice that more detailed rules and procedures of individual areas, e.g. services or intangible assets, can help

141 E. g. since the amendment of the Income Tax Act in effect from 2018, there has been an addition to the definition of associated party to include *"person or entity which is part of the consolidated group for consolidation purposes"* (Income Tax Act, 2003, Section 2 (n) (3)). Prior to the mentioned amendment, the definition criteria for consolidated entity as associated persons were provided mainly indirectly with reference to the Slovak Act on Accounting No. 431/2002 Coll. as later amended.

142 A legal relationship or other similar relationship created primarily for the purpose of reducing the tax base or tax loss increases.

143 E.g., there is no generally accepted definition of aggressive tax planning, aggressive tax optimisation or tax havens.

144 The issued guidelines are legally binding for tax authorities.

145 Such significant amendment or extension of the Income Tax Act will likely require the addition of a new Income Tax Act which has been discussed for a long time in the Slovak Republic. In the case that a new Income Tax Act is released, one can notice that an increase in attention and space should be given to transfer pricing issues.

146 E.g. the guideline treating the APAs request approval procedures.

147 Considering the judgement of the Supreme Court of the Slovak Republic.

148 With a direct impact in increasing the legal certainty.

to increase the legal certainty of the taxpayers and make work for tax authorities much easier. Currently, the only simplification accepted for determining transfer price is by calculating costs and adding 5% for the services from the so called low-value added activities. It could be stated that the implementation of safe harbours can bring significant benefits both for taxpayers and tax authorities, but the date of implementation remains questionable due to a very demanding process.

10.4.3 *DE LEGE FERENDA* CONSIDERATIONS – GENERAL AND MORE COMPLEX ISSUES

As transfer pricing issues have begun to recently attract attention, one can notice that there is an awareness from SMEs about the current obligations. Results are also visible in the absence of elementary transfer pricing knowledge amongst entrepreneurs of the SME category. The changes in transfer pricing issues[149] are often linked to the worsening of the business environment and increasing bureaucracy.

Current transfer pricing regulation and practices also have the following weak points:

a) Domestic legal regulation in the case of reliability and comparability analysis refers to the OECD Transfer Pricing Guidelines and does not deal with it in detail. Kočiš (2015) states that a potential solution could be the introduction of minimal comparability standards, which would have a direct impact on the legal certainty for determining prices in controlled transactions. Such implementation of these standards would be suitable not only for internal or external transactions, but also a combination of the two. Currently, the minimum standards in terms of comparison conditions of transactions are missing in legal regulation or in subordinate legislation.
b) Methodological guidelines generally regulate the availability of data entering the comparability analysis. More detailed and precise regulation of this area in domestic legal regulation would contribute to an improved status of taxpayers and would increase the legal certainty.
c) The Income Tax Act in Section 17(5) does not explicitly state whether the tax base of an associated person needs to be adjusted for differences on an individual or aggregate basis. More practical examples or additional information could be assessed as suitable.
d) Domestic legal regulation does not apply statistical methods, tests nor statistical procedures (primarily the application of interquartile ranges) when determining transfer prices. The issued methodological guideline refers to OECD TP Guidelines, to a large extent. Introduction of a basic framework in this area would also increase the legal certainty of the taxpayer.
e) Taxpayers often use various databases; the most widespread is database probably Amadeus. There are quite a number of other databases available in the market but on the other hand, there is limited a amount of information on the use of other databases or on the minimum standards to be followed. One can conclude that the anonymous disclosure of the decision for APA approval in specific areas would potentially lead to improved legal certainty.
f) As was already mentioned, the increased interest in transfer pricing has been noted relatively recently and due to this fact there are a very limited number of adjustments on transfer pricing. As judgements in specific areas from foreign jurisdictions could be misleading in practical application due to the differences in legal regulations, one can notice that future judgements in this area will have a significant effect on the legal certainty and a potentially positive effect in material and procedural improvements.
g) According to Kočiš (2019), the scope of the Slovak domestic transfer pricing regime may not be considered as identical for international and domestic transactions because the definition of the arm's length principle may differ for domestic transactions and may differ for the different versions of the OECD TP Guidelines (and the relationship between the Income Tax Act and double tax treaties due to the Income Tax Act providing a much broader definition of associated parties compared to individual double tax treaties).

149 E.g. further extending transfer pricing obligations to domestic transactions (domestically associated persons).

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CHAPTER 11
POLICY IMPLICATIONS

11.1 GENERAL INTRODUCTION

As pointed out by Bacik et al. (2019, p. 73), *"The countries of the Visegrad Group do not only share a common Central European space, apart from geographic location, but they are also linked with history, culture, values, priorities and interests to strengthen stability in the Central European region."* These facts seem to be the reasons for which the Visegrad Group has managed to profile itself as a significant collective actor (Cabada and Waisová, 2018). Results of the study carried out by Bacik et al. (2019) also bear witness to the fact that the economic situation of the Czech Republic, Hungary, Poland and Slovakia is very similar and these countries achieve the same results when one considers their economic performance or competitiveness (Bacik et al., 2019) This conclusion is not, however, generally valid when taking into account other indicators or focus of a study (see e. g. studies by Čiefová and Goda, 2019; World Economic Forum, 2019; Heritage Foundation, 2019; Kowalska et al., 2018). Existence of differences is only natural because each of these economies behaves as an individual living organism, whose behaviour reflects their own need, priorities and specifics while facing different economic problems which determine their economic status and position in the world (Bacik et al., 2019). Every country tries to respond to existing challenges both in the many forms of cooperation with other countries, as well as in the position of a separate and autonomous entity. To compete in the current turbulent economic environment is not an easy task – both for countries and subjects operating in the territory of the countries that have to adapt to new challenges.

As pointed out by Sacio-Szymańska, A. (ed.) (2016, p. 9), *"The main features of today's economy are fast changing customer demands, shorter production cycles, the shift of power eastwards, limited budgets, rapid change in technologies and the so-called "information pollution"; all these trends can straightforwardly affect the decision making and the strategy building of entrepreneurs who have to cope incessantly with a situation of uncertainty."* To operate in such an environment is not an easy task – it puts an increased requirement on laws which should establish necessary, clear and, if possible stable, legal regulations and which at the same time should establish a balance between the country and her needs and the subjects (legal entities and individuals) located in the territory of that country.

Regarding taxation and tax issues, there is usually a conflict between the interests of the countries and taxpayers. That is to say, the economically rational aim of a taxpayer is to maximise its utility which is determined by the obligatory payments and the quality and extent of the public goods available (or provided) to him (Wilson, 1999). The tax-subject when operating globally are seeking the best offer and try to utilize advantages/stimulus provided by different countries. There should be a counterbalance for such behaviour in order eliminate base erosion and profit shifting. It is only logical that the issue of transfer pricing is at stake in this respect. To establish relevant rules for transfer pricing, eventually for the application of the arm's length principle is a very demanding task and it is only logical to seek inspiration in the legal regulations of other countries.

This chapter summarises some conclusions (recommendations) for legal regulations of transfer pricing issues in V4 generally. One still must keep in mind the specific situation in the Czech Republic where very limited legal regulations governing transfer pricing are included in domestic acts. For that reason, the acceptance of the recommendations stated below would be conditioned by significant changes therein.

11.2 LAW GENERAL ATTRIBUTES

All the **legal systems of V4 countries** are based on the rule of law which is not always working properly within EU countries (European Commission, 2019). Legal systems in V4 countries can be described as continental legal systems while in some countries (Czech Republic and Slovakia) one can observe a more obvious move to a mixed legal system.

The **role of the courts and related case law** can be considered the same – interpretation of the law and the elimination of insufficient legal regulations while providing interpretation. Another significant role of case law is to unify (at least this role is attributable for the Supreme Courts). To fully meet this requirement, it is more than desirable to have the case law freely available – it was not the case of Poland, as observed by the researcher for this country.

Regarding the **position of the OECD standards**, the OECD standards are more or less viewed as a form of soft law which seems to be the correct position because only then is it possible to reflect specifics of the country and country's policy objectives (which could differ). The OECD standards are highly evaluated for not being a political issue and focused on the solution of existing problems. It is one of the reasons why these standards are broadly accepted and adopted (reflected) in the acts or at least in some form of guidelines in the V4 countries. These acts and guidelines cannot, however, include all the materials made by the OECD. To boost the position of the OECD standards and to support the legal certainty on the part of tax subjects there is a need to publish the OECD standards in the officialese of the particular country. For example, in Slovakia there is a persistent uncertainty in the application of the OECD Transfer Pricing Guidelines (OECD, 2017a) due to the judgement of the Supreme Court of the Slovak Republic of 15 April 2015, file No. 2Sžf/76/2014 in which the Court states as follows, *"under the circumstances where the legal norm has not been duly published, where there is an absence of well-established practice, where the OECD Model and commentaries are not available in the official language and where there are contradictory opinions on the binding nature of interpretative rules".*

For the current version of the OECD Transfer Pricing Guidelines (OECD, 2017a), which differs significantly from the previous one, it is only the Czech Republic which meets the condition to have this material published in the official language.

The **position of international and EU law** compared to its domestic counterpart is the same in all the V4 countries – not surprisingly. This fact can be attributable to common legal roots and the fact that all the countries are EU Member States.

11.3 KEY DEFINITIONS AND TERMS

Definition of **associated persons/related parties**[150] is one of the key terms since it represents the personal scope for the application of arm´s length principle. Despite different wording one can observe that similar categories are covered by the definition of associated persons/related parties. Hungarian and Polish legal regulation include a very extensive and complicated definition of associated persons. It is very difficult to find one's way around these definitions. A simplification and unification of the definitions would be very welcome. On the other hand, the adoption of the definition as provided for example by the Czech Income Tax Act (Income Tax Act, 1992, Sec. 23(7)) cannot be adopted. That is to say, the problems that have arisen in these countries have provoked changes in the personal scope of this definition. Getting back to a simplification and using more general terms would cause problems which were/or could potentially be eliminated by the adoption of more appropriate legal regulations.

The correct identification of associated persons/related parties determines the related obligations in terms of transfer pricing. Failure to correctly identify represents a risk of imposing relatively high sanctions on the taxpayer. The definition of associated persons in Polish regulation covers all possible cases but what may cause difficulties within the interpretation and application for taxpayers is very extensive.

Concerning Slovakia there is a challenge in defining "otherwise associated party" which suffers from some shortcomings (quantitative or purely formal characteristics of dependence are missing).

The category of "other ties" which was and remains very challenging within its interpretation and application seems to be very complicated to deduce. In this respect one can conclude general observations as follows:

a) Associated persons/related persons should be those who are connected economically, personally or by another functionally equivalent connection to that of economic or personal (according to the Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010);
b) A chain of indirect evidence should be good enough to prove the fact that a person is acting with the aim to fraudulently transfer tax base (according to the Judgement of the Supreme Administrative Court of 04 August 2005 File No. 2 Afs 13/2005).

150 Used as synonym.

For the Czech Republic it would be useful to specify the procedure when applying a way of setting the transfer price according to the Act on Property Evaluation (*stricto sensu* application of the rules stated therein could be contrary to the arm's length principle). For the definition of associated persons, it is quite typical (if not necessary) that there are references to the terms (definitions) as provided in other acts. This legislative technique is quite common. There is, however, a need for some simplification regarding for example the situation in Hungary.

The **definition of associated persons in DTT**s in which a V4 country is a contracting party is fully in line with the OECD Model Tax Convention on Income and on Capital (OECD, 2017b). The personal scope of Art. 9 (Associated Persons) in DTTs concluded is narrower compared to domestic law, which is a common platform.

Considering the **share in capital or voting rights** there is a risk, not only in V4 countries, that a company can be considered an associated person in one country but not necessarily in the other one. A unification of the limits in the threshold would eliminate potential problems occurring as a result of the previously mentioned fact. Such a unification would also require harmonisation in other aspects which is not realistic when considering the tax policy of particular countries.

Poland is the only V4 country which established **a definition of a transfer price**, which reads as follows, *"the financial result of the conditions established or imposed as a result of existing relationships, including price, remuneration, financial result or financial indicator"* (Act on CIT, Art. 11a, par. 1). The question is whether such a definition will help taxpayers to better understand transfer price or not. Czech, Hungarian and Slovak law-making bodies, or at least the Ministries of these countries, have not revealed an intention to establish a definition of a transfer price. However, a proper and clear definition of a transfer price can boost legal certainty and has significant information value for taxpayers. In other words: thanks to the inclusion of the definition of a transfer price, the doubts on the part of the taxpayers related to "aspects" for which arm's length principle shall be applied can be avoided or at least significantly decreased.

To sum it up, considering the term associated persons/related parties the legal regulations in V4 countries are similar in many aspects. Existing differences have been a demonstration of the autonomy of the countries in tax issues and the needs as came into existence as a reaction to existing problems and continually discovered shortcomings in domestic legal regulation. In fact, a generally valid conclusion or recommendation for domestic law for the above stated attributes cannot be set especially when considering the different levels of current legal regulations in particular V4 countries.

Regarding DTTs and existing situation there is a desire to include all the potential clauses under Art. 9 (Associated Persons) to increase legal certainty and include a „Limitation of Benefits" clause in newly negotiated DTTs at the same time.

11.4 TRANSFER PRICING DOCUMENTATION

Transfer pricing documentation has been a frequently discussed issue whose origin dates back to the end of the 1960s (Dumiter and Boiţă, 2017). The study by Lohse, Riedel and Spengel (2012) who analysed the development of different aspects of transfer pricing regulation among 44 countries in the period 2001-2009 have concluded that documentation requirements were introduced to a greater extent within this time period. This conclusion remains valid also for the V4 countries and the recent time period, excluding the Czech Republic in which transfer pricing documentation is not obligatory. An obligatory transfer pricing documentation is, without any doubts, an extra obligation connected with compliance expenses on the part of taxpayers. However, its elaboration has undisputable contributions:

a) It helps to understand the processes and mutual relationships between associated persons.
b) It makes bearing the burden of proof easier for a taxpayer when demonstrating the correct application of the arm's length principle.
c) It eliminates the objections of the parent company situated in one country which resists providing all necessary information to its subsidiary located in the other country showing that transfer pricing documents are not obligatory in the other one.

To sum up the issue of transfer pricing documentation, one can conclude (based on the comparison of legal regulations in V4 countries) that if transfer pricing documentation is set as obligatory, then:

a) Logical exemptions from this obligation should be set (see for example the legal regulation in Hungary – exemption of small companies, non-profit organisations of public interest, situations in which an annual amount of the transactions at the group level is less than set amount) (for more details see Act on Corporate Tax and Dividend Tax, 1996, Sec. 18. (5); Government Decree No. 32/2017, Sec 1.). For other examples the Polish legal regulations can be utilised (Act on CIT, 1992, Art. 11n).
b) Multi-level transfer pricing documentation should be established. The legal regulation in Slovakia can be set as a platform for potential changes in legal regulation. There are three level transfer pricing documentation:
   - an abridged documentation (extra simplified documentation),
   - basic (simplified) documentation and
   - complete documentation (full scope), while

   the scope of the documentation depends on the type of transaction being checked (significant/insignificant and domestic/cross-border) – for more details see guidelines of the Ministry of Finance of the Slovak Republic No. MF/019153/2018-724.

Regarding **comparative analysis/compliance analysis** they are, as a rule, a part of the transfer pricing documentation. It is a logical requirement. To carry out a comparability/compliance analysis of high quality is a very demanding task. To improve legal certainty, at least the minimum standards shall be established in law. Regarding the rules as provided in an act, Polish legal regulation can be considered as a good standard (see Act on CIT, 1992, Art. 11q; Regulation of MF, 2018, par. 2, p. 3).

There is also a logical need (demand) to be provided in detailing the rules at least in the form of guidelines which reflect the specifics of the countries, data availability and also the practice approved by tax authorities. This requirement is met only partly.

11.5 CLAUSES COVERING SPECIAL AREAS OF TRANSFER PRICING

In relation to **special clauses**, the Polish legal regulations can be considered the most extensive ones and the regulations most capable of serving as the background for the amendments of Slovak and Hungarian law[151]. It provides detailed rules for:

a) disclosing of intra-group services,
b) cost contribution arrangement, and
c) business restructuring.

All the above stated areas are those included in the OECD Transfer Pricing Guidelines (OECD, 2017a) and deserve to be paid extra attention. If not regulated in the Acts, then there is a need to establish the rules in the form of guidelines.

Neither should the **issue of intangibles** be omitted. There should be provided a more detailed guideline to DEMPE (Development, Enhancement, Maintenance, Protection and Exploitation) analysis.

11.6 APA

APAs are attracting attention both in theory and practice. They represent a formal arrangement between a tax authority (eventually tax authorities) and a taxpayer (taxpayers) involved in the transaction. APAs are considered as a tool to encourage foreign investors, increase transparency, save both taxpayers´ and tax authorities´ time and costs, reduce litigation, prevent penalties and comply with the instructions of the tax administration (Chugan, 2007; Biyan and Yilmaz, 2013). The APAs are considered as a tool for companies to reduce the uncertainty and to reduce the fiscal liability arising out of transactions regulations by transfer pricing (Fadiga, 2018).

Three types of the APA are distinguished, and it is desirable that **all the three types of APA** would be available in the country. Currently, this is not valid for the Czech Republic where a binding ruling is available

151 Due to current state of transfer legal regulations in the Czech Republic such a change is not desirable. Adopting such changes would definitely be preceeded by a complex change in the legal regulation of transfer pricing issues as embodied in the acts.

instead of the unilateral APA. Binding rulings, however, cannot meet all the criteria as established by the OECD for the APA (OECD, 2017a; Brychta and Sulik-Gorecka, 2019). At the same time detailed rules for the APA shall be embodied in an act /in the acts, which is not again the case for the Czech Republic. Taxpayers in the Czech Republic "suffer" from lack of obvious and clear rules. A detailed rule which can serve as an inspiration can be found in Polish legal regulations, which provides very detailed instructions.

Regarding the **fee for the APA**, it is logical that the price should reflect the demandingness of the consideration. Taking account, the legal regulation in Hungary, Poland and Slovakia, and putting all the principles altogether, one can conclude that the fee should be derived from:

a) the type of the APA (unilateral, bilateral and multilateral),
b) used method,
c) number of transactions evaluated, and
d) volume of the transaction(s).

At the same time, one can conclude that the rules for the procedure connected with the APA should be established in domestic law to boost legal certainty on the part of tax-subjects.

11.7 MUTUAL AGREEMENT PROCEDURE (MAP)

The MAP is a negotiating procedure between the competent authorities of states to a DTT with the aim to eliminate disagreement concerning its interpretation and elimination of double taxation (VERO SKATT, 2019). The contribution of and need for this instrument is thus indisputable.

Even though basic standards for its application have been established in international law, it is necessary to set more detailed rules also in domestic law (domestic acts), which is not always the case. For example, it was the Czech Republic which had not utilized the potential of the newly prepared procedural act within her reaction to a duty to transpose directive on tax dispute resolution (Eur-lex, 2020). A form which was chosen by Slovakia can be impactful regarding the scope of the newly adopted Slovak Act on Rules for Tax Dispute Resolutions (2019, Sec. 1) in which three types of disputes are covered, namely a dispute between the Slovak Republic and:

a) another EU Member State,
b) a contracting State (a state that has a DTT concluded with the Slovak Republic) and
c) a contracting State to the Arbitration Convention.

11.8 SAFE HARBOURS

Safe harbours seem to be a way in which it is easier to make an application of the arm's length principle easier. Solilová (2013) presented the benefits of safe harbours as follow:

a) simplifying compliance,
b) reducing compliance costs,
c) providing certainty,
d) shifting administrative resources to examinations of more complex or higher risks transactions and taxpayers, and
e) minimal examination requirements.

Every V4 country, except for Slovakia, has established rules for a **safe harbour for low-added value services** by law. In Slovakia only a practise which is approved (accepted by tax authorities) has been settled. This fact cannot be considered as enough from the legal point of view. Any safe harbour should be established – including specification of the conditions under it can be applied - by law in order that the requirement for legal certainty would be met.

Even for the safe harbours the Polish legal regulations can serve as an inspiration for legal regulation in other countries – Poland has introduced simplified rules for selected types of loan transactions. It is true that the OECD has recently published a *Transfer Pricing Guidance on Financial Transactions* (OECD, 2020a), however, this arena is so complicated, that any simplification without a need to apply barely available (and or expensive) data and/or using complicated models is more than welcome. Besides, OECD (2020a) focuses primarily on the transactions with an international aspect and it also seems on higher volume transactions. For some types of transactions, a simplification would be welcome by both taxpayers and tax authorities.

Considering Polish legal regulations one can conclude that the platform introduced in the Polish Act on CIT (1992, Art. 11g) can serve as an inspiration. The generalised rules for the adoption of a particular legal regulation can be as follow:

a) the interest rate of the loan at the date of the contract is determined based on the type of base interest rate and margin specified in the notification of the Ministry of Finance of a particular country;
b) no payments other than interest related to the granting or servicing of the loan, including commissions or bonuses, are foreseen;
c) the loan was granted for a set period (not longer than by a legally set time period);
d) during the taxable period, the total level of liabilities or receivable of a related entity under the capital of loans with related entities calculated separately for loans granted and contracted is not more than the set amount or the equivalent of this amount;
e) the lender is not an entity with a place of residence, registered office of a place of effective management in a territory or country applying harmful tax competition[152].

The loan amounts expressed in foreign currency are converted into domestic currency according to the average exchange rate announced by the National Bank of the country. The exchange rate is calculated from the last business day preceding the day of payment of the loan amount.

11.9 SELECTED PROCEDURAL ASPECTS

The rules for **bearing the burden of proof** are not the same in different countries (OECD, 2017a). The existence of differences cannot be a problem as such. A taxpayer operating in relationship with a state authority is facing a weaker position, since the state authority is entitled to impose unilaterally some obligations on tax subjects. For that reason, notwithstanding a concept applied in V4 country, a taxpayer has to be provided enough time to prove the relevance of the transfer pricing that was set by him (he has to be provided with enough time to justify the existing difference[153]) to prove the relevance of the transfer price that was set (presented) by him. In case a tax authority sets a reference price, then the tax authority shall impose an obligation to clearly and specifically notify the taxpayer of the amount of the actual common market price being extrapolated by the tax authority, and how the tax authority reached such a price (on the basis of what documents/criteria/tools). Following this, the tax subject must be provided with time, not only to provide a statement in regard to the evidence shown or to the criteria, but also to propose other evidence or criteria which, according to a taxpayer´s opinion, offer a different amount of the usual market price than that set by the tax authority. The above stated principles which were established in Czech case law[154] can generally be considered valid since they correspond to the ideas of fair procedure, when due to the weaker position of a tax subject, he has to be provided some protective measurements in their favour.

Considering the **rules for the sequence of the tests** applied when assessing the transaction, there is a recommendation to apply the arm's length test as the last one (after the substance and benefit test).

For the above stated reason and taking into account the reliability of data (to eliminate potential errors), a rule established in the Czech Republic by the case law of the Supreme Administrative Court is that if a taxpayer does not bear his burden of proof the **tax authority shall set the range** and adjust a taxpayer's transfer price only to the endpoint of the range that is most beneficial for the taxpayer (for example see Judgement of the Supreme Administrative Court of 31 March 2009 File No. 8 Afs 80/2007). This way of setting the transfer price can be, however, seen as problematic because this practice is not generally valid and accepted. This fact can cause double taxation in the event a transaction with an international element is involved and adjustment of the tax base is realised in the second contracting country (Kapoun, 2020).

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152 Such a clause would definitely provoke amendments on the level of existing law in particular V4 countries.

153 I.e. a difference between the price insisted on by the tax authority and by him.

154 See for example Judgement of the Supreme Administrative Court of 27 June 2007 File No. 1 Afs 60/2006; Judgement of the Supreme Administrative Court of 27 January 2011 File No. 7 Afs 74/2010; Judgement of the Supreme Administrative Court of 31 October 2013 File No. 7 Afs 86/2013; Judgement of the Supreme Administrative Court of 31 March 2009 File No. 8 Afs 80/2007; Judgement of the Supreme Administrative Court of 02 March 2011 File No. 8 Afs 19/2010.

11.10 DIGITAL ECONOMY – A CHALLENGE FOR TRANSFER PRICING LEGAL REGULATION

Transfer pricing is viewed as one of the strategies used by companies to erode their corporate tax base in high tax countries or to evade tax (see for example Devereux and Keuschnigg, 2008; Ramboll Management Consulting and Corit Advisory, 2015; Centre for European Economic Research, 2016; Nugroho, Wicaksono and Utami, 2018). On the other hand, even entities that criticise the situation in the tax systems admit that there is not always an intention of taxpayers to abuse transfer pricing. For example, Tax Justice Network (2020) which promotes some potential solutions to remedy inconvenient situations states that, *"Many companies strive to use the arm's length principle faithfully. Many companies strive to move in exactly the opposite direction. In truth, however, the arm's length principle is very hard to implement, even with the best intentions."* Application of the arm's length principle is and will be criticized for many reasons – difficulties within its application and its limited potential when fighting against tax erosion and profit shifting are some of the problems. The arm's length principle is also subject to a criticism since the arm's length principle itself is not good enough to face the challenges of digital economy (White, 2020) and for that reason even the OECD started to settle the question of what to do about the arm's length principle (OECD, 2019). The creation and establishment of new standards will take some time. The question is also what the attitude of countries will be to newly established platforms and ways of setting the transfer pricing, or even better ways of fighting against base erosions and profit shifting. Existing experience suggests that reaching a unanimous agreement between all the EU countries is problematic (see some facts on the Common Consolidated (Corporate) Tax Base (European Commission, 2020)).

The most difficult issues that tax administrations of the V4 countries should face in the near future are the challenges emerging from the recently published statement by the OECD/G20 Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy (OECD, 2020b).

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CONCLUSIONS

The aim of this scientific monograph was to extend the discussion on the issue of transfer pricing, focusing on the situation in V4 countries and to provide a comparative study of the legal regulation of transfer pricing issues in V4 countries, to identify existing risks and shortcomings in the legal regulation governing transfer pricing in particular V4 countries and to present *de lege ferenda* considerations. The monograph consists of two parts: conceptual and empirical. The first part provides the theoretical foundations of transfer pricing and refers to: the general ideas behind transfer pricing, transfer pricing as a profit shifting technique, the economic and legal perspectives of transfer pricing, and other areas connected with transfer pricing such as comparability analysis, transfer pricing documentation, advanced pricing agreements and issue of safe harbours. The second part of the monograph presents the results of the empirical investigation, summarises the existing rules as embodied in the OECD and EU standards, and presents both general legal regulations and more detailed analysis of transfer pricing legal regulations in V4 countries. Following the results of the comparative analysis the authors present their recommendations for transfer pricing legal regulations.

A comprehensive and extensive literature overview was undertaken which identified that transfer pricing is becoming increasingly of interest to a large number of academics and practitioners alike. This phenomenon has been confirmed by a growing number of scientific and professional articles and publications. Based on the relatively large amount of studied outputs, one can clearly view transfer pricing as a global topic. Nowadays it would be challenging to find a sector or jurisdiction for which there is no published article or study associated with transfer pricing. The literature focuses primarily on: legal regulation in particular jurisdictions and their mutual comparison, transfer pricing as a profit-shifting technique, economic perspectives on transfer pricing, basic principle/assumptions of transfer pricing – arm's length principle, comparability analysis, transfer pricing methods and documentation, and transfer pricing with a primary focus on particular sectors, jurisdictions or their combination. A relatively large number of authors also provide proposals on how to improve current legislations, procedures and rules. Some proposals presented in the literature could be perceived as relatively radical, e.g. the cancellation and replacement of the arm's length principle, while others aim to improve the current settings. There are proposals and recommendations in almost every area, but primarily in the field of legislation, comparability analysis, advance pricing agreements and the implementation of safe harbours.

Currently what seems to be at the centre of attention are proposals aimed at simplifying the existing systems, increasing legal certainty and reducing compliance costs - which are also the aims of the JTPF - a special body for transfer pricing established by the European Commission. The EU as a whole even "declared war" on base erosion and profit shifting activities, so when this is taken into consideration transfer pricing can be viewed as a potentially risky "instrument". However, the scope of the EU's legal regulation of transfer pricing, as embodied in EU secondary law, cannot be considered to be extensive when compared to other EU direct tax legal regulations - the predominant focus is on deepening cooperation among Member States (the tax authorities specifically), avoidance of double taxation and fighting against tax avoidance and tax evasion. The EU hard-law for transfer pricing issues can be considered to be very limited. However, there are a number of recommendations and guidelines issued by the JTPF which represent the soft-law, and these have been widely approved and accepted. A Directive for the Common Consolidated Corporate Tax Base, i.e. a measure which could at least eliminate the problems of transfer pricing for some tax-payers and on the part of tax authorities, has not, however, received enough support among all the EU Member States so far (for more details see for example European Commission, 2020; Nerudová and Solilová, 2019; Nerudová a Solilová, 2018). There are many differences in regards to domestic transfer pricing legal regulations in EU member countries. This is not entirely surprising as this area has not been harmonized and instead there has 'only' been some coordination based on the acceptance of the OECD and EU standards. Interestingly, some of the countries do show significant similarities in many aspects of transfer pricing legal regulation as identified by many studies (see for example, studies by Rathke and Rezende (2016) and Ignat and Feleagã (2017)).

Transfer pricing in all the V4 countries is currently generating a significant amount of coverage and discussion, both for tax administrators and tax-payers. The extent of the legal regulation as embodied in domestic law differs significantly. All the V4 countries are, however, facing issues with public budgets and, at the same time, the amount of taxes being collected has been diminishing due to practices connected with profit shifting and tax evasion. As transfer pricing has been associated with aggressive tax planning, it is not surprising that the area of transfer pricing has been a focus of tax audits (KPMG, 2017).

Generally speaking, the basis of the legal systems and the position of the OECD standards (which are considered to be a form of soft-law) in all the V4 countries is very similar. However only the Czech Republic has translated the current version of the OECD Transfer Pricing Guidelines. The position of EU and international law in all the V4 countries, which are also EU countries, occupies, not surprisingly, the same position based on its supremacy and application priority over domestic law. When speaking of transfer pricing legal regulation one can find many similarities due to the implementation of the same EU and OECD standards, but also many differences. In all V4 countries there are two basic categories of associated parties: persons associated through capital share and persons associated by other ties (relationships). The threshold for being considered an associated party differs in V4 countries and this can cause application problems within the effort of the parties to meet the different requirements as set in the countries involved. Currently Hungary and Slovakia are facing some difficulties in connection with the definitions of key terms, as well as the fact that legal regulation in Hungary is fragmentated. Even so, in all the V4 countries there remains an obligation to follow the arm´s length principle. With respect to the legal regulation as included in DTTs, those concluded by V4 countries follow the OECD Model Tax Convention and for that reason the definition of associated persons, compared to the definition as provided by their domestic law, can be considered narrower. The MLI convention has been undersigned by all the V4 countries.

It is also worth highlighting the differences between transfer pricing documentation. Three transfer pricing documentation types were introduced in all the V4 countries: Local File, Master File and CbCR. The rules for transfer pricing documentation, with the exemption of the CbCR which represents implementation of the EU secondary law, differs significantly. Unlike all the other V4 countries transfer pricing documentation (Local and Master File) is not obligatory in the Czech Republic. Poland and Hungary have some exemptions from the obligation of transfer pricing documentation. In Poland the Local File documentation obligation differs by area, while the obligation to prepare a Master File is only applicable on reaching a certain threshold. In Slovakia, the scope of the documentation depends on the type of transaction, and three types of documentation are applied (full-scope, basic and extra-simplified). In regards to the applicable transfer pricing methods, the situation is the same in all the V4 countries – the methods as set by the OECD standards are recommended, while other methods are acceptable as long as they follow the arm´s length principle. The legal regulation of transfer pricing in Poland is very extensive and there are many specific rules compared to the remaining V4 countries. In Poland, there are some specific rules for transfer pricing related to special sectors or areas. Poland also has the most extensive categories of safe harbour compared to other V4 countries (besides a safe harbour for low-adding value, there is also a safe harbour for certain loans and bond transactions).

The V4 countries are also very similar in relation to the regulations provided for APAs. There are three types of APA (unilateral, bilateral and multilateral) in all the V4 countries, apart from the Czech Republic, where only bilateral and multilateral agreements based on the rules as stated in DTTs can be found, and where there is no unilateral APA, just a Binding Ruling. There are, however, significant differences in the types and amounts of fees in all V4 countries, as well some significant differences relating to the procedural aspects. There are also significant differences in the types and amounts of penalties for failing to meet transfer pricing rules. Apart from the Czech Republic, where transfer pricing documentation (Local and Master File) is not obligatory, the V4 countries have specific penalties for infringements related to transfer pricing documentation; these are, as a rule, higher than general tax penalties. One of the most procedural issues connected with transfer pricing is the burden of proof. In the V4 countries, apart from Poland, the burden of proof lies primarily with the tax-payer.

To summarise the comparison of the legal regulations of transfer pricing in the V4 countries, it is evident that the similarities between the transfer pricing rules in the countries stem from the implementation of OECD Transfer Pricing Guidelines and EU law. The main differences lie in the diverse legal systems, the characteristics of tax regulations, and the different ways benefits are provided, for example the exemption from the documentation obligation for SMEs in Hungary, or the simplified documentation in Slovakia.

In regards to policy implications, the Czech legal regulations on transfer pricing (in the broader meaning of the term) need improving in order to enhance the legal certainty on the part of tax subjects. However it is difficult to assess whether the adoption of OECD and EU soft-law in the manner and extent to which Hungary, Slovakia and Poland have done would be beneficial for both parties, that is tax subjects and tax authorities. The criticism of the Czech transfer pricing legal regulations is that they are unclear, and partial changes to the system are proposed. If a new concept of transfer pricing legal regulation is accepted in the Czech domestic legal system, the change should be extensive and comprehensive, and should be included as part of the introduction of the new Income Tax Code. There is an ideal opportunity for this to be done, as submission of the new concept of the Income Tax Code has been postponed and should follow only after the recodification of the Act on Accounting (Komora daňových poradců ČR, 2019). This would provide a unique opportunity to change the existing rules, otherwise the changes made will further complicate an already complicated act. Hungary is at a very advanced level in terms of integration of OECD standards into domestic legal regulations. However, one can distinguish five main categories of typical problems related to transfer pricing issues: problems with the definition of an associated person; problems with the documentation obligation; problems regarding tax base adjustment; transfer price reporting obligation problems (methods) and problems with preparing the CbCR. These are problematic issues from the viewpoint of both the tax authorities and taxpayers, as errors in transfer pricing documentation have an effect on both parties. The most important *de lege ferenda* proposals for Hungary lie in simplification of the documentation and providing assistance with the documentation: reducing the number of acts that refer to transfer pricing, providing guidelines and a sample file for the documentation and applying simplified documentation for certain companies. Poland is also very advanced in the field of incorporating OECD and EU regulations into domestic provisions. The regulations analysed should be assessed positively in the context of an attempt to adjust the tax system to the changing economic environment. Adjusting the law to international regulations and the changing expectations of tax authorities and taxpayers requires constant legislative work. However, the large number of new regulations and the fast pace of change require constant monitoring of legal acts, which is a challenge for taxpayers. Despite the fact that Polish legal regulations are not perfect, they can be used as inspiration for legal regulations in other countries. Transfer pricing plays an increasingly important role also in the Slovak taxation system, which is reflected in both its legal regulation and its extensity. Over the last few years, amendments to the Slovak Income Tax Act have been adopted and many methodological guidelines have been issued. However, the current transfer pricing legal system has several weak points and solutions for this would provide an improved position for all involved parties. The suggested proposals could be divided into several categories. Some measures could be taken reasonably quickly and at a relatively low cost (e.g. the translation of the OECD Transfer Pricing Guidelines), some measures could be linked with the amendment and supplement of the Slovak Income Tax Act (e.g. a clear definition of "associated party" or implementation of selected areas from the OECD Transfer Pricing Guidelines) whilst some measures are very time consuming and resource intensive (e.g. implementation of safe harbours) but their adoption could bring significant benefits for both taxpayers and tax authorities.

One can conclude that the topic of transfer pricing is a large-scale research issue, which has been in the past and is still now a challenge for the digital economy (White, 2020; OECD, 2020). It is only logical that when trying to find an acceptable and appropriate response to the issue, that mutual cooperation between the research community, experts from practice and financial administrations, and between countries, is and always will be necessary. To find a solution there is a need to understand the status quo and to identify both the deficiencies and possibilities. The authors of this monograph hope that the results of their study, which is based on an empirical investigation in which both academics and experts from financial administrations and consultancy companies participated, will be a useful base for the following discussion and research activities in the area of transfer pricing.

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ABSTRACT

This scientific monograph is a result of the research conducted in the years 2019-2020 as part of the project supported by the Visegrad Fund entitled "Transfer Pricing in V4 Countries" (Visegrad Grant No. 21830038; for more details see www.transferpricing-V4.net). The monograph presents the results of the scientific cooperation between the Brno University of Technology, Faculty of Business and Management (Czech Republic), DUMA – Dunamenti Adóklaszter (Hungary), Széchenyi István University, Kautz Gyula Faculty of Economics (Hungary), University of Economics in Katowice (Poland) and Matej Bel Univeristy in Banská Bystrica, Faculty of Economics (Slovakia).

The subject of the monograph was taken on because of its importance in a changing global economic reality, in which a significant part of world trade takes place within related entities belonging to MNE's. One of the economic goals of conducting transactions between associated entities is to strive to pay appropriately low taxes, and no country, regardless of the level of her economic growth, wants to be deprived of the tax due. To get a fair proportion of the tax base, countries adhere to the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and regulations issued by the European Union Joint Transfer Pricing Forum (JTPF). The issue of a fair valuation of the transactions between associated entities from the tax point of view has become one of the focal points in the OECD "Base Erosion and Profit Shifting" (BEPS) project which deals with the issue of transfer pricing under its Actions 8-10. The aim of the authors of the monograph was to provide a deep analysis of transfer pricing legal regulations in the Czech Republic, Hungary, Poland and Slovakia, where, despite the generally accepted above-mentioned international and EU standards, there are many significant differences in the scope, degree and form of legal regulations.

The purpose of the monograph was to create a critical comparative study of the legal regulations related to transfer pricing in the V4 countries in order to identify existing risks and shortcomings in *de lege lata* and subsequently to present *de lege ferenda* considerations. The monograph consists of two basic parts: conceptual and empirical. The empirical investigation itself was based on a qualitative research approach – above all on comparative analysis approach for its methodology, which is in keeping with a qualitative research design. The subject being compared was *transfer pricing in V4 countries* with a focus given on to the *rules governing transfer pricing in V4 countries* as a strategic issue in the realized research.

In the conceptual part of the monograph, the authors provide a literature overview for the issue of transfer pricing, a description of the design of empirical investigations and an overview of the basic standards as set by the OECD and EU. These parts of the monograph create a background for the empirical part which deals, among others, with the way the V4 countries adopted these standards. The empirical part of the monograph consists of the chapters dealing with the legal regulation of transfer pricing in particular V4 countries. These chapters also include a basic summary of the case-law related to transfer pricing issues and the identified problems and inadequacies in the legal regulation. In the following part of the monograph a comparison of transfer pricing regulations in the V4 countries is presented. The next part of the monograph comprises the policy implications for transfer pricing legal regulation for V4 countries.

To the knowledge of the authors of the monograph, there has not been such a deep comparative study of legal regulations of V4 countries so far. Thus, the monograph contributes to current state of research and knowledge in the area of transfer pricing and the adoption of OECD and EU transfer pricing standards. The monograph may be useful both for researchers and academicians, as well as tax authorities and taxpayers both within and outside the V4 region.

ABSTRACT (CZECH LANGUAGE)

Tato vědecká monografie je výsledkem výzkumu prováděného v letech 2019-2020 v rámci projektu financovaného Visegradským fondem “Transfer Pricing in V4 Countries” (Visegrad Grant No. 21830038; pro více informací viz www.transferpricing-V4.net). Monografie prezentuje výsledky vědecké spolupráce mezi Vysokým učením technickým v Brně, Fakultou podnikatelskou (Česká Republika), daňovým clusterem DUMA – Dunamenti (Maďarsko), Univerzitou Széchenyi Istvána, Ekonomickou fakultou Kautze Gyula (Maďarsko), Ekonomickou univerzitou v Katowicích (Polsko) a Univerzitou Mateja Bela v Banské Bystrici, Ekonomickou fakultou (Slovensko).

V podmínkách měnícího se globálního ekonomického prostředí, ve kterém se významná část světového obchodu odehrává mezi spojenými osobami patřícími k nadnárodním společnostem, je zaměření této monografie aktuální. Jedním z ekonomických cílů realizace transakcí mezi spojenými osobami je snaha minimalizovat daňovou zátěž. Žádná země, bez ohledu na úroveň jejího ekonomického růstu, však nechce přicházet o odpovídající daňové inkaso. K získání férového podílu na základu daně tak státy přistupující k přijetí pravidel etablovaných ve Směrnici OECD o převodních cenách pro nadnárodní podniky a daňové správy a ve standardech vydaných v rámci EU forem pro převodní ceny - Joint Transfer Pricing Forum (JTPF). Otázka férového daňového ocenění transakcí mezi spojený osobami byla i jedním z ústředních bodů projektu OECD směřujícího proti nahlodávání daňových základů a přesunům zisků (BEPS); převodní ceny jsou náplní Akčních plánů 8-10. Záměrem monografie je prezentovat podrobnou analýzu právních úprav převodních cen v České republice, Maďarsku, Polsku a na Slovensku. V tomto ohledu je vhodné podotknout, že navzdory obecnému přijetí shora uvedených mezinárodních standardů a standardů etablovaných na poli EU existuje v těchto zemích mnoho významných rozdílů v rozsahu, hloubce a formě právní regulace převodních cen.

Cílem autorů monografie bylo vytvořit kritickou srovnávací studii právních úpravy převodních cen v zemích V4 za účelem identifikace existujících rizik a nedostatků ve stávající právní úpravě (*de lege lata*) a následně prezentovat potenciální návrhy změn (*de lege ferenda*). Monografie se skládá ze dvou částí: koncepční a empirické. Empirické zkoumání jako takové bylo založeno na kvalitativním výzkumu – především na komparativním analytickém přístupu, který odpovídal plánu prováděného výzkumu. Předmětem výzkumu byly *převodní ceny ve Visegradských zemích (V4)* se zacílením na *pravidla převodních cen ve Visegradských zemích (V4)* coby strategického bodu v realizovaném výzkumu.

V koncepční části monografie autoři uvádí výsledky sekundárního výzkumu v oblasti převodních cen, popis plánu empirického zkoumání a přehled základních standardů OECD a EU. Tyto části monografie tvoří základ pro empirickou část, která se mj. zabývá způsobem, jak země V4 implementovaly tyto standardy. Empirická část monografie se skládá z kapitol pojednávajících o právní úpravě převodních cen v jednotlivých zemích V4. Tyto kapitoly rovněž zahrnují základní shrnutí závěrů judikatury váznoucí k převodním cenám a identifikovaných problémů a nedostatků v právní úpravě. V následující části monografie je prezentováno srovnání právních úprav převodních cen v zemích V4. Další část monografie shrnuje návrhy pro právní úpravu převodních cen v zemích V4.

Pokud je autorům monografie známo, dosud neexistovala tak rozsáhlá a detailní komparativní studie právní úpravy převodních cen v zemích V4. Tato monografie tak rozšiřuje dosud existující výzkum a stav poznání v oblastí převodních cen a způsobu implementace standardů OECD a EU v oblasti převodních cen jednotlivými zeměmi. Tato monografie může být přínosná jak pro výzkumníky a akademiky, tak i správce daně a poplatníky nejenom v rámci regionu V4, ale i mimo něj.

ABSTRACT (HUNGARIAN LANGUAGE)

Jelen tudományos monográfia a Visegrádi Alap által támogatott 2019-től 2020-ig tartó „Transzferárazás a V4-es országokban" című kutatás eredményeként jött létre (Visegrádi Alap 21830038. számú projekt; további részletek: www.transferpricing-V4.net). A monográfia által bemutatott eredmények a résztvevő projektpartnerek tudományos kutatási együttműködésében valósultak meg: Brnoi Műszaki Egyetem Üzleti és Menedzsmenttudományok Kar (Cseh Köztársaság), DUMA- Dunamenti Adóklaszter (Magyarország), Széchenyi István Egyetem Kautz Gyula Gazdaságtudományi Kar (Magyarország), Katowicei Gazdaságtudományi Egyetem (Lengyelország) és a Besztercebányai Matej Bel Egyetem Gazdaságtudományi Kar (Szlovákia).

A monográfia témája a folyamatosan változó globális gazdasági környezetben aktuális és fontos, hiszen a világkereskedelem jelentős része multinacionális vállalatok kapcsolt vállalkozásain keresztül bonyolódik. A kapcsolt vállalkozások egymás közti tranzakcióinak egyik célja, hogy minél alacsonyabb adókat fizessenek, mialatt az egyes országok, függetlenül gazdasági fejlettségüktől, nem szeretnének elesni az adóbevételektől. Az adóalap országonkénti tisztességes felosztása érdekében az államok betartják az OECD transzferár irányelveit multinacionális vállalkozások és az adóhatóságok számára, valamint az Európai Unió Közös Transzferár Fórumának szabályozásait. A kapcsolt felek közti tranzakciók méltányos értékelése adózási szempontból az OECD Adóalap-erózió és Nyereségátcsoportási projektjének (BEPS) egyik kulcspontjává vált, a 8-10-es akcióterv foglalkozik a transzferárazás kérdésével. A monográfia fő célja, hogy a transzferárazás jogi szabályozásaiba nyújtson mélyebb betekintést a Cseh Köztársaság, Magyarország, Lengyelország és Szlovákia esetén, amely országok közt a korábban említett általánosan elfogadott nemzetközi és EU-s szabályozások ellenére számos különbséget fedezhetünk fel a jogi szabályozás mértékében és formájában.

A monográfia szerzőinek az volt a célja, hogy kritikai szemléletű összehasonlító elemzést készítsenek a transzferárakkal kapcsolatos jogi szabályozásokról a V4-es országokban különös tekintettel a hatályos jogszabályok (*de lege lata*) kockázatainak és hiányosságainak azonosítása, illetve a jövőben meghozandó szabályozások megfontolása (*de lege ferenda*) céljából. A monográfia két fő részből, elméleti összehasonlításból és empirikus elemzésből áll. Az empirikus elemzés kvalitatív kutatási megközelítésen, az összehasonlító elemzés módszerén alapul. Az elemzés tárgya a V4-es országok transzferár szabályozásának összehasonlítása volt nagy hangsúlyt fektetve a kutatás fő stratégiai irányára, a V4-es országok transzferárazásának jogi szabályozásaira.

A monográfia elméleti részében a szerzők részletes irodalmi áttekintést adtak a transzferárazással kapcsolatos kérdésekről, bemutatták az empirikus elemzés módszertanát, illetve az OECD és az EU vonatkozó sztenderdjeit is áttekintették. A monográfia ezen része megalapozza az empirikus elemzést, amely azt vizsgálja, az egyes V4-es országok hogyan adaptálták az említett sztenderdeket. A monográfia empirikus része az egyes V4-es országok transzferárakkal kapcsolatos jogi szabályozásait mutatja be. Továbbá ezen fejezetek összegzik az eset-jog transzferárakkal kapcsolatos vonatkozásait valamint a jogi szabályozások szerzők által azonosított problémáit és hiányosságokat. Az ezt következő részében a V4-es országok transzferárazási szabályainak összehasonlítása történik meg. A monográfia következő része pedig a transzferárazás jogi szabályozásával kapcsolatos javaslatokat tartalmazza a V4-es országok számára.

A monográfia szerzőinek tudomása szerint korábban még nem jelent meg ilyen mélyreható elemzés a V4-es országok jogi szabályozásáról. Jelen monográfia tehát hozzájárul a transzferárak területén a tudományos ismeretek bővítéséhez, valamint az OEDC és EU-s transzferár szabályzatok elfogadásához. A monográfia nemcsak a V4-es régióban, hanem azon kívül is hasznos lehet a kutatók és akadémikusok számára, valamint az adóhatóságok és az adóalanyok számára is.

ABSTRACT (POLISH LANGUAGE)

Niniejsza monografia naukowa jest rezultatem badań przeprowadzonych w latach 2019-2020, w ramach projektu finansowanego przez Fundusz Wyszehradzki pt. Ceny transferowe w krajach Funduszu Wyszehradzkiego" (Visegrad Grant Nr. 21830038, więcej informacji: www.transferpricing-V4.net). W monografii zaprezentowano wyniki współpracy naukowej realizowanej przez Brno University of Technology, Faculty of Business and Management (Czechy), DUMA – Dunamenti Adósklaszter (Węgry), Széchenyi István University, Kautz Gyula Faculty of Economics (Węgry), Uniwersytet Ekonomiczny w Katowicach (Polska) oraz Matej Bel Univeristy in Banská Bystrica, Faculty of Economics (Słowacja).

Temat badań podjęto ze względu na jego istotne znaczenie w zmieniającej się globalnej rzeczywistości ekonomicznej, w której istotna część światowego handlu odbywa się pomiędzy jednostkami powiązanymi należącymi do międzynarodowych grup kapitałowych. Jednym z celów ekonomicznych realizowanych transakcji pomiędzy podmiotami powiązanymi jest chęć płacenia odpowiednio niskich podatków, a żaden z krajów, niezależnie od poziomu rozwoju ekonomicznego, nie chce zostać pozbawiony należnych dochodów podatkowych. W celu opracowania zasad sprawiedliwego szacowania podstawy opodatkowania, poszczególne kraje wdrożyły Wytyczne Organizacji Współpracy Gospodarczej i Rozwoju (ang. Organisation for Economic Cooperation and Development, OECD) w sprawie cen transferowych dla przedsiębiorstw wielonarodowych i administracji podatkowych oraz regulacje wydane przez Wspólne Forum Unii Europejskiej ds. cen transferowych (ang. European Union Joint Transfer Forum, JTPF). Kwestia sprawiedliwej, z punktu widzenia podatkowego, wyceny transakcji pomiędzy podmiotami powiązanymi, stała się również jednym z kluczowym obszarów projektu pt. „Erozja podstawy opodatkowania i transfer zysków" (ang. Base Erosion and Profit Shifting, BEPS), realizowanego w ramach OECD.

W monografii analizie poddano regulacje prawne w zakresie cen transferowych w Czechach, Polsce, na Słowacji i na Węgrzech, gdzie pomimo wymienionych wyżej wzorcowych międzynarodowych źródeł prawa, występują istotne różnice w zakresie i stopniu uregulowania. Celem monografii było stworzenie krytycznego studium porównawczego regulacji prawnych dotyczących cen transferowych w analizowanych krajach Funduszu Wyszehradzkiego oraz identyfikacja nieuregulowanych obszarów oraz istniejących ryzyk a także opracowanie propozycji *de lege ferenda* w zakresie zmian prawa. Monografia składa się z dwóch części: koncepcyjnej i empirycznej. Badania empiryczne przeprowadzono z wykorzystaniem koncepcji badań jakościowych, zwłaszcza analizy porównawczej. Przedmiotem analizy porównawczej był problem cen transferowych w krajach Funduszu Wyszehradzkiego, ze szczególnym uwzględnieniem regulacji prawnych w tym zakresie.

W części koncepcyjnej monografii, autorzy dokonali przeglądu literatury z zakresu cen transferowych oraz standardów i wytycznych wypracowanych w ramach OECD oraz Unii Europejskiej. Na podstawie pierwszej części zaplanowano część badawczą, w której dokonano, między innymi, weryfikacji stopnia wdrożenia standardów i wytycznych w krajach Funduszu Wyszehradzkiego. Część empiryczna składa się z rozdziałów dotyczących regulacji prawnych w zakresie cen transferowych w poszczególnych krajach Funduszu Wyszehradzkiego. W rozdziałach tych zamieszczono ponadto odniesienia do orzecznictwa sądowego oraz wskazano kwestie problematyczne i wymagające zmian w zakresie regulacji prawnych. W kolejnej części monografii dokonano syntezy i porównania regulacji prawnych zakresie cen transferowych poszczególnych krajów, a następnie wskazano propozycje *de lege ferenda* w zakresie zmian prawa.

Zgodnie ze stanem wiedzy autorów, dotychczas nie przeprowadzono tak dogłębnego studium porównawczego regulacji w zakresie cen transferowych w krajach Funduszu Wyszehradzkiego. Monografia stanowi istotny wkład do rozwoju nauki w zakresie prawa dotyczącego cen transferowych oraz implementacji regulacji OECD oraz UE do przepisów krajowych. Publikacja jest skierowana do szerokiego grona osób zainteresowanych tematyką cen transferowych, zarówno naukowców i pracowników uczelni wyższych, jak i przedstawicieli władz podatkowych oraz podatników nie tylko w krajach Funduszu Wyszehradzkiego.

ABSTRACT (SLOVAK LANGUAGE)

Táto vedecká monografia je výsledkom výskumu realizovaného v rokoch 2019-2020 v rámci projektu financovaného Vyšehradským fondom "Transfer Pricing in V4 Countries" (Visegrad Grant No. 21830038; pre viac informácií viď www.transferpricing-V4.net). Monografia prezentuje výsledky vedeckej spolupráce medzi Vysokým učením technickým v Brně, Fakultou podnikatelskou (Česká Republika), daňovým klastrom DUMA - Dunamenti (Maďarsko), Univerzitou Széchenyi Istvána, Ekonomickou fakultou Kautza Gyula (Maďarsko), Ekonomickou univerzitou v Katowiciach (Poľsko) a Univerzitou Mateja Bela v Banskej Bystrici, Ekonomickou fakultou (Slovensko).

V podmienkach meniaceho sa globálneho ekonomického prostredia, v ktorom sa významná časť svetového obchodu odohráva medzi prepojenými osobami patriacimi k nadnárodným spoločnostiam, je zameranie tejto monografie aktuálne. Jedným z ekonomických cieľov realizácie transakcií medzi prepojenými osobami je snaha minimalizovať daňovú záťaž. Žiadny štát, bez ohľadu na úroveň jeho ekonomického rastu, však nechce prichádzať o zodpovedajúce daňové inkaso. K získaniu férového podielu na základe dane tak štáty pristupujú k prijatiu pravidiel etablovaných v Smernici OECD o prevodných cenách pre nadnárodné podniky a daňové správy a v štandardoch vydaných v rámci EÚ fórom pre prevodné ceny - Joint Transfer Pricing Forum (JTPF). Otázka férového daňového ocenenia transakcií medzi prepojenými osobami bola i jedným z hlavných bodov projektu OECD smerujúceho proti narúšaniu daňových základov a presunom zisku (BEPS); prevodné ceny sú náplňou Akčných plánov 8–10. Zámerom monografie je prezentovať podrobnú analýzu právnych úprav prevodných cien v Českej republike, Maďarsku, Poľsku a na Slovensku. V tomto ohľade je vhodné podotknúť, že napriek všeobecnému prijatiu vyššie uvedených medzinárodných štandardov a štandardov etablovaných na poli EÚ existuje v týchto štátoch mnoho významných rozdielov v rozsahu, hĺbke a forme právnej regulácie prevodných cien.

Cieľom autorov monografie bolo vytvoriť kritickú porovnávaciu štúdiu právnej úpravy prevodných cien v štátoch V4 za účelom identifikácie existujúcich rizík a nedostatkov v existujúcej právnej úprave (*de lege lata*) a následne prezentovať potenciálne návrhy zmien (*de lege ferenda*). Monografia sa skladá z dvoch častí: koncepčnej a empirickej. Empirické skúmanie ako také bolo založené na kvalitatívnom výskume – predovšetkým na komparatívnom analytickom prístupe, ktorý zodpovedal plánu vykonávaného výskumu. Predmetom výskumu bolo porovnávanie transferového oceňovania vo Vyšehradských štátoch (V4). Dôraz bol kladený na pravidlá stanovujúce prevodné ceny v štátoch Vyšehradskej štvorky ako strategický problém v realizovanom výskume.

V koncepčnej časti monografie autori uvádzajú výsledky sekundárneho výskumu v oblasti prevodných cien, popis dizajnu empirického skúmania a prehľad základných štandardov OECD a EÚ. Tieto časti monografie tvoria základ pre empirickú časť, ktorá sa okrem iného, zaoberá spôsobom ako štáty V4 implementovali tieto štandardy. Empirická časť monografie sa skladá z kapitol pojednávajúcich o právnej úprave prevodných cien v jednotlivých štátoch V4. Tieto kapitoly obsahujú aj základné zhrnutie záverov judikatúry viažucej sa k prevodným cenám a identifikovaným problémom a nedostatkom v právnej úprave. V nasledujúcej časti monografie je prezentované porovnanie právnych úprav prevodných cien v štátoch V4. Ďalšia časť monografie sumarizuje návrhy pre právnu úpravu prevodných cien v štátoch V4.

Pokiaľ je autorom monografie známe, doteraz neexistovala tak rozsiahla a detailná komparatívna štúdia právnej úpravy prevodných cien v štátoch V4. Táto monografia tak rozširuje doteraz existujúci výskum a stav poznania v oblasti prevodných cien a spôsobu implementácie štandardov OECD a EÚ v oblasti prevodných cien jednotlivými štátmi. Táto monografia môže byť prínosná ako pre výskumníkov a akademikov, tak pre správcu dane a daňovníkov nielen v rámci regiónu V4, ale i mimo neho.

ANNEX

I: Planned time schedule of the workshop in Brno (Czech Republic)

TRANSFER PRICING IN V4 COUNTRIES

Visegrad Fund Project No. 21830038
Implementation Period: 01/02/2019 – 30/04/2020

Brno Workshop – 04 June 2019
(room E339)

09:00 – 09:30	**Registration**
09:30 – 09:45	**Opening speech** (Mrs. Zdeňka Konečná, a vice-dean of the Faculty of Business and Management)
09:45 – 10:15	**How BEPS influenced the Transfer Pricing** (Mr. Daniel Szmaragowski, KPMG; Czech Republic)
10:15 – 10:45	**Legal regulations of transfer pricing in Poland - a challenge for taxpayers** (Mrs. Aleksandra Sulik-Górecka, University of Economics in Katowice; Poland)
10:45 – 11:15	**The regulation and problematic issues of Hungarian transfer pricing** (Mrs.Veronika Poreisz, Széchenyi István University; Mrs. Mariann Berényiné, DUMA; Hungary)
11:15 – 12:45	**Lunch**
12:45 – 13:15	**Mutual Cooperation of Financial Administrations in Transfer Pricing – Experience of the Czech Financial Administration** (Mr. Vítězslav Kapoun, General Financial Directorate; Czech Republic)
13:15 – 13:45	**Transfer pricing documentation as set by the guidance of the Ministry of Finance of the Slovak Republic – is there a conflict with ethical codex of the EU JTPF?** (Mr. Michal Jelínek, V4 Group (Tax, Audit & Legal Advisory Group); Czech Republic)
13:45 – 14:15	**Safe Harbours in Transfer Pricing: Who is the winner?** (Mrs. Veronika Solilová & Mrs. Danuše Nerudová, Mendel University in Brno; Czech Republic)
14:15 – 14:45	**Coffee break**
14:45 – 15:15	**Practice – transfer pricing in domestic transactions from the point of view of entrepreneurs** (Mrs. Marcela Bošková, A&T solutions s.r.o.; Slovakia)
15:15 – 15:45	**Transfer pricing from the perspective of the tax administrator** (Mrs. Zuzana Svinčáková, Tax Authority for Selected Tax Subjects; Slovakia)
15:45 – 16:15	**Summary and closing speech**

II: List of the participants of the workshop in Brno (Czech Republic)

	Surname	Name	Affiliation	Country
Mrs.	Bednářová	Marie	Financial Authority for the South-Moravian Region	CZ
Mr.	Bělehrádek	Pavel	Financial Authority for the South-Moravian Region	CZ
Mrs.	Bělušová	Kristýna	Brno University of Technology	CZ
Mr.	Brychta	Karel	Brno University of Technology	CZ
Mr.	Ďaďo	Jaroslav	Matej Bel University	SK
Mr.	Fabík	Adam	BDO Tax a.s.	CZ
Mr.	Fiala	Jan	Special Tax Authority	CZ
Mr.	Frnková	Veronika	Financial Directorate of the Slovak Republic	SK
Mr.	Hašan	Martin	D.C Profit, s.r.o	SK
Mrs.	Hodinková	Monika	Akademie Sting – Vysoká škola Brno	CZ
Mr.	Ištok	Michal	Matej Bel University	SK
Mr.	Jelínek	Michal	V4 Group	CZ
Mr.	Kapoun	Vítězslav	General Financial Directorate of the Czech Republic	CZ
Mrs.	Karelová	Silvia	Financial Directorate of the Slovak Republic	SK
Mrs.	Konečná	Zdeňka	Brno University of Technology	CZ
Mrs.	Koutná	Zuzana	Appellate Financial Directorate	CZ
Mr.	Mydlár	Gabriel	Deloitte Tax s.r.o. SK	SK
Mrs.	Nemšáková	Eva	V4 Group	SK
Mr.	Otevřel	Pavel	KPMG Česká republika	CZ
Mrs.	Poreisz	Veronika	Széchenyi István University	HU
Mr.	Sabol	Martin	Deloitte Tax s.r.o. SK	SK
Mr.	Sloboda	Marek	Financial Directorate of the Slovak Republic	SK
Mrs.	Solilová	Veronika	Mendel University in Brno	CZ
Mrs.	Sulik-Górecka	Aleksandra	University of Economics in Katowice	PL
Mrs.	Svinčáková	Zuzana	Tax Authority for Selected Tax Subjects	SK
Mr.	Szmaragowski	Daniel	KPMG Česká republika	CZ

III: Planned time schedule of the workshop in Banská Bystrica (Slovakia)

PROBLEMATIC ASPECTS OF TRANSFER PRICING REGULATION AND OTHER CHALLENGES IN TRANASFER PRICING ISSUES

Visegrad Fund Project No. 21830038
Implementation Period: 01/02/2019 – 30/04/2020

Banská Bystrica Workshop – 06 November 2019
(Lecture Room CAP1 – New Building of the Faculty of Economics, Matej Bel University)

Presentation	15 minutes for the presentation itself + 10 minutes for the discussion
09:00 – 09:30	**Registration**
09:30 – 09:45	**Opening speech** (Mrs. Emília Zimková, a vice-dean of the Faculty of Economics; Matej Bel University)
09:45 – 10:10	**Implementation of the BEPS project results into existing international treaties through Multilateral Instrument** (Mrs. Dana Slivková, Financial Directorate of the Slovak Republic; Slovakia)
10:10 – 10:35	**Objective reasons for sustaining losses according to the OECD TP Guidelines and their acceptance in tax audits in Slovakia** (Mr. Branislav Kováč Mrs. Frederika Silesky, VGD Slovakia, s.r.o.; Slovakia)
10:35 – 11:00	**The current legal issues of the Slovak transfer pricing regime** (Mr. Michal Kočiš, KOČIŠ & PARTNERS, s.r.o. law firm; Slovakia)
11:00 – 11:25	**The simplified documentation – form, problems, solutions** (Mr. Adam Čiffáry, CLIA agentúra s.r.o.; Slovakia)
11:25 – 12:30	**Lunch**
12:30 – 12:55	**Challenges in the area of comparative analysis and the problem of insufficient comparable data (impacts of the market consolidation on the choice of the comparables)** (Mr. Michal Jelínek, V4 Group (Tax, Audit & Legal Advisory Group); Czech Republic)
12:55 – 13:20	**Issue of comparability for V4 countries** (Mrs. Veronika Solilová, Mendel University in Brno; Czech Republic)
13:20 – 13:55	**Reporting obligations in Poland regarding transfer prices** (Mrs. Aleksandra Sulik-Górecka, University of Economics in Katowice; Poland)
13:55 – 14:30	**Coffee break**
14:30 – 14:55	**Transfer price in practice in Hungary** (Mrs. Veronika Poreisz, Széchenyi István University of Győr; Hungary Mrs. Mariann Berényi, DUMA; Hungary)
14:55 – 15:20	**Problematic aspects of domestic transfer pricing legal regulations** (Mr. Karel Brychta, Brno University of Technology; Czech Republic)
15:20 – 16:00	**Discussion**
16:00 – 16:15	**Summary and closing speech**

IV: List of the participants of the workshop in Banská Bystrica (Slovakia)

	Surname	Name	Affiliation	Country
Mrs.	Albertová	Vivien	Financial Directorate of the Slovak Republic	SK
Mrs.	Balogová	Eva	CLIA agentúra s.r.o.	SK
Mrs.	Berényi	Mariann	DUMA Taxation Cluster	HU
Mr.	Brychta	Karel	Brno University of Technology	CZ
Mr.	Čiffáry	Adam	CLIA agentúra s.r.o.	SK
Mrs.	Ďurčeková	Ina	Matej Bel University	SK
Mr.	Ďaďo	Jaroslav	Matej Bel University	SK
Mrs.	Frnková	Veronika	Tax office for selected business subjects	SK
Mr.	Huňady	Ján	Matej Bel University	SK
Mrs.	Ištočková	Mária	Matej Bel University	SK
Mr.	Ištok	Michal	Matej Bel University	SK
Mrs.	Jandorová	Agáta	CLIA agentúra s.r.o.	SK
Mr.	Jelínek	Michal	V4 Group	CZ
Mrs.	Karelová	Silvia	Financial Directorate of the Slovak Republic	SK
Mr.	Kočiš	Michal	KOČIŠ & PARTNERS, s.r.o. law firm	SK
Mr.	Kováč	Branislav	VGD Slovakia, s.r.o.	SK
Mrs.	Kurjaková	Gabriela	Matej Bel University	SK
Mrs.	Lacová	Žaneta	Matej Bel University	SK
Mrs.	Lapková	Marta	Lamart, s.r.o.	SK
Mr.	Mešťan	Michal	Matej Bel University	SK
Mr.	Motnyk	Marcin	WSB University in Dąbrowa Górnicza	PL
Mrs.	Mlynárová	Denisa	Matej Bel University	SK
Mr.	Mydlár	Gabriel	Deloitte Tax s.r.o.	SK
Mrs.	Poreisz	Veronika	Széchenyi István University of Győr	HU
Mr.	Sabol	Martin	Deloitte Tax s.r.o.	SK
Mr.	Sedliačík	Ivan	Matej Bel University	SK
Mrs.	Silesky	Frederika	VGD Slovakia, s.r.o.	SK
Mrs.	Slivková	Dana	Financial Directorate of the Slovak Republic	SK
Mr.	Sloboda	Marek	Tax office for selected business subjects	SK
Mrs.	Soliová	Veronika	Mendel University in Brno	CZ
Mrs.	Stašová	Jana	Matej Bel University	SK
Mrs.	Sulik-Górecka	Aleksandra	University of Economics in Katowice	PL
Mrs.	Svinčáková	Zuzana	Tax office for selected business subjects	SK
Mr.	Ščerba	Kamil	Matej Bel University	SK
Mrs.	Vidiečanová	Michaela	Matej Bel University	SK
Mrs.	Vlčková	Ivana	Financial Directorate of the Slovak Republic	SK
Mrs.	Zimková	Emília	Matej Bel University	SK