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OECD GUIDELINES. BETWEEN SOFT-LAW AND HARD-LAW IN TRANSFER PRICING MATTERS

Abstract

Transfer pricing is a crucial issue in international tax law, yet its legal regulation at the level of international law is rather limited. Provisions on transfer pricing are contained in both the OECD Model Tax Convention on Income and on Capital and its US and UN equivalents (Article 9 in all three models). Their wording, however, is rather general. This leaves plenty of matters to be regulated at the domestic level, which cannot properly serve the aim of international law in this regard – namely, elimination of economic double taxation. However, Article 9 of the OECD Model is developed in far more detailed guidelines developed by the OECD, which are used in numerous countries. The OECD guidelines are not the only piece of soft-law in transfer pricing matters available worldwide. The author analyses their legal status and on that basis makes certain forecasts as to their further application in the future.

Keywords

double tax conventions – transfer pricing – OECD – economic double taxation – sources of law

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I. Transfer pricing – overview of sources of law

Transfer pricing stipulations in double tax conventions (DTCs) are usually based on Article 9(1) of the OECD Model Tax Convention on Income and on Capital (OECD Model), according to which, where:

– 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
– 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 (primary adjustment).

This provision is aimed at eliminating economic double taxation as certain general standards of disregarding transactional conditions are developed and bilaterally recognized by state-parties to DTCs. Stipulations contained in DTCs based on Article 9 of the OECD Model do not constitute a legal basis for primary adjustments. Such a basis must stem from a domestic legal order. This reflects an old principle – currently a constitutional principle adopted by many countries, including Poland – namely, no taxation without representation, under which only laws adopted by representative bodies such as parliaments can impose taxes. The author's understanding of the role of provisions on transactions between associated enterprises seems to be confirmed by the historical development of the DTC between Hungary and the United States concluded in 1979, where the usual content of Article 9(1) of the OECD Model was included in the technical explanations to the treaty of 1980 where the parties stated that primary adjustment was allowed and the legal basis for such an adjustment stemmed from national laws.

Numerous DTCs also contain provisions based on Article 9(2) of the OECD Model, which states that 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 (corresponding adjustment).

This provision is clearly meant to eliminate economic double taxation, as a primary adjustment in one contracting state (increasing taxable income by a decision of tax authorities) shall result in a corresponding adjustment in the other contracting state (decreasing taxable income).

The wording of Article 9 of the U.S. Model Tax Income Tax Convention (US Model) is highly similar to Article 9 of the above-mentioned OECD Model. The same can be said of Article 9 of the United Nations Model Tax Convention between Developed and Developing Countries (UN Model), which, however, unlike the two previously mentioned models, also contains Article 9(3) limiting the scope of situations where the application of Article 9(2) regarding corresponding adjustment is required.

All three major models definitely lack detailed legal regulation of transfer pricing issues. It is easily noticeable that the exact transposition of Article 9 of the OECD Model into national legal orders without their further development would probably lead to problems that would eventually result in failure to achieve the objective of DTCs based on the OECD Model (as well as on the other two major models), i.e. elimination of economic double taxation. For instance, the concept of direct or indirect participation in management, capital or control is very broad. A person who holds 0,1% stake in a company that is a 0,1% shareholder of another company indirectly participates in capital of the latter company, though it does not really exert impact on that company. Moreover, Article 9 of the OECD Model contains prerequisites of departing from transactional values in transactions between associated enterprises, but it does not indicate how to arrive at proper values,

i.e. such as can be reconciled with the arm's length principle. The methods of calculating prices acceptable under Article 9 of the OECD Model were only proposed in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD TPGs). The difference in length between Article 9 of the OECD Model and the OECD TPGs is particularly striking. Article 9 is less than one standard page long while the OECD TPGs are 247 pages long (2009 edition) and 371 pages long (2010 edition), though one must admit they do, in part, refer to articles of the OECD Model other than Article 9 (Article 25). Similar guidelines were prepared by other organizations – for instance the UN prepared the United Nations Practical Manual on Transfer Pricing for Developing Countries (UN Manual), which was published in 2013.

National transfer pricing provisions that serve as legal bases for the decisions made by tax authorities are frequently based on the OECD Model, but they are more detailed than the model and double tax conventions based thereon. The details developed at the national level – at least in part – reflect the OECD TPGs. New countries introduce transfer pricing provisions that - up to a certain extent - mirror the basic content of the OECD TPGs (for instance, Belarus introduced such rules in 2012[1], Russia modified its rules with effect from 2012 as well[2], Iceland changed its provisions to reflect the OECD TPGs in 2014[3]).

There are other pieces of soft-law of relevance in transfer pricing matters. The OECD's official commentary to the OECD Model should definitely be named, among others, but it should certainly be stressed that it does not focus on transfer pricing.

1 V. Strachuk, *Belarus. Report*, Tax News Service 10.02.2012, available online: www.ibfd.org.

2 E. Variychuk, *The New Russian Transfer Pricing Law*, Bulletin for International Taxation 2011, no. 11, p. 640.

3 S.T. Jonsson, H.I. Birgisson, *New Transfer Pricing Rules as from 1 January 2014*, International Transfer Pricing Journal 2014, no. 4, p. 285.

II. TRANSFER PRICING GUIDELINES AND THEIR LEGAL STATUS – AN INTERNATIONAL PERSPECTIVE

1. THE OECD

The aims of the OECD, according to the Convention on the Organisation for Economic Co-operation and Development, signed in Paris on 14 December 1960 (the OECD Convention)[4], shall be to promote policies designed:

a) to achieve the highest sustainable economic growth and employment and a rising standard of living in Member countries, while maintaining financial stability, and thus to contribute to the development of the world economy,
b) to contribute to sound economic expansion in Member as well as non-member countries in the process of economic development, and
c) to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations.

According to Article 5 of the OECD Convention, in order to achieve its aims, the OECD may:

a) take decisions which, except as otherwise provided, shall be binding on all the members,
b) make recommendations to members, and
c) enter into agreements with members, non-member states and international organisations.

Under Article 6(1) of the OECD Convention, unless the OECD otherwise agrees unanimously as regards special cases, decisions shall be taken and recommendations shall be made by mutual agreement of all the Members. Article 6(3) states that no decision shall be binding on any Member until it has complied with the requirements of its own constitutional procedures. The other Members may agree that such a decision shall apply provisionally to them.

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[4] Dziennik Ustaw [Journal of Laws] 1998, No. 76, item 490.

There is nothing in the OECD Guidelines to suggest that the OECD TPGs should be viewed as a decision within the meaning of Article 6 of the OECD Convention binding the members of this organization. This suggests that they should be perceived as a recommendation under Article 5(b) of the OECD Convention[5].

The OECD TPGs describe themselves as a non-binding measure not only in their title – which includes the word "guidelines" – but also in their content.

2. The UN

The UN Manual was developed by the United Nations Committee of Experts on International Cooperation in Tax Matters. The aims of the United Nations are far broader than those of the OECD. The UN aims to solve international economic problems, and juridical and economic double taxation is among such problems. The objectives of the UN connected with the economy are just one of numerous other objectives mentioned in Article 1(3) of the Charter of the United Nations (Charter of the UN)[6], according to which the purposes of the United Nations are to achieve international co-operation in solving international problems of an economic, social, cultural, or humanitarian character, and in promoting and encouraging respect for human rights and for fundamental freedoms for all without distinction as to race, sex, language, or religion. If one proceeds to further provisions of the Charter of the UN, one will encounter chapter IX devoted to international economic and social co-operation. Under Article 55 of the Charter of the UN, while aiming to create conditions of stability and well-being which are necessary for peaceful and friendly relations among nations based on respect

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[5] K. Lasiński-Sulecki, *Status prawny Wytycznych OECD w sprawie cen transferowych dla międzynarodowych przedsiębiorstw oraz administracji podatkowych i ich znaczenie w orzecznictwie polskich sądów na tle praktyki wybranych innych państw* [*Legal Status of OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations and Their Significance in Case Law of Polish Courts with Practice of Other States in Background*], [in:] I. Mirek, T. Nowak (eds), *Prawo finansowe po transformacji ustrojowej. Międzynarodowe i europejskie prawo podatkowe* [*Financial Law after Systemic Transformation. International and European Tax Law*], Łódź: Wydawnictwo Uniwersytetu Łódzkiego 2013, p. 345.

[6] Dziennik Ustaw [Journal of Laws] 1947, No. 23, item 90.

for the principle of equal rights and self-determination of peoples, the United Nations shall promote:

1. higher standards of living, full employment, and conditions of economic and social progress and development;
2. solutions of international economic, social, health, and related problems; and international cultural and educational cooperation; and
3. universal respect for, and observance of, human rights and fundamental freedoms for all without distinction as to race, sex, language, or religion.

Problems of double taxation and transfer pricing are definitely covered by Article 55(1) and (2).

The UN Manual cannot be perceived as an act of international law.

The UN Manual also starts with the explanation that it comprises guidance sought by developing countries (p. iii). It does not seek to be prescriptive, as its drafters believe that earlier transfer pricing experiences of developed countries can be of special relevance to developing countries (p. v).

In the process of creating the UN Manual the drafters attempted to achieve consistency of this manual with the OECD TPGs, as they were required to do. This attempt to reach solutions not diverging from the OECD TPGs was justified by the assumption that there is a widespread reliance on the OECD TPGs in both developed and developing countries (p. vii).

The remarks concerning the OECD TPGs' impact on the interpretation of DTCs apply equally to the UN Manual, though nowadays the latter seems to be even less likely to be referred to by tax authorities or MNCs throughout the world.

3. INTERPRETATION OF INTERNATIONAL LAW

Numerous issues connected with international agreements and their interpretation were codified in the Vienna Convention on the law

of treaties concluded at Vienna on 23 May 1969 (Vienna Convention)[7]. Even if one assumes that the Vienna Convention applies only to DTCs concluded after its entry into force in state-parties of the DTCs, it is still applicable to at least hundreds of DTCs worldwide. Moreover, the aforementioned assumption, though technically correct, overlooks the fact that many stipulations of the Vienna Convention had earlier been treated as rules of international customary law.

It is of particular interest to assess whether or not the provisions of the Vienna Convention regarding interpretation of treaties can cast a certain light on the status of the OECD TPGs or the UN Manual.

Under Article 31(1) of the Vienna Convention 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.

The term context is explained in Art 31(2) of the Vienna Convention. 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 connection with the conclusion of the treaty;
b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

As Article 31(3) of the Vienna Convention states 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.

According to Article 32 of the Vienna Convention recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm

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7 United Nations Treaty Series [1980] Vol. 1155, I-18232, p. 331.

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 or unreasonable.

Starting the analysis with Article 31(1) *in fine* of the Vienna Convention it can undoubtedly be assumed that the OECD TPGs make it possible to reach the purpose of DTCs based on the OECD Model as far as the pricing of transactions between associated enterprises is concerned. Uniform understanding of stipulations based on Article 9 of the OECD Model in all tax jurisdictions may eliminate economic double taxation connected with reassessments of taxable amounts. One should bear in mind, however, that the elimination of economic double taxation is a very broadly understood purpose of DTCs and, at the same time, that certain provisions of DTCs clearly do not even allow full elimination of economic double taxation.

The OECD TPGs do not fit the broadened definition of context from Article 31(2) of the Vienna Convention. First of all, the OECD TPGs cannot be perceived as an agreement relating to the treaty (Article 31(2)(a)). Secondly, although the OECD TPGs can be seen as an instrument made by one or more parties to a treaty (this can be true in the case of the OECD members), they cannot be described as made in connection with the conclusion of the treaty and accepted by the other parties (as DTCs are bilateral) as an instrument related to the treaty (Article 31(2)(b)). The OECD TPGs were not described as such either in any DTC concluded by Poland or in any protocol to such a DTC, although special status was granted by means of a protocol to the official commentary to the OECD Model in the DTC with Austria.

For the reasons mentioned above the OECD TPGs cannot be seen as covered by Article 31(3)(a) of the Vienna Convention. If the OECD TPGs are followed with no exceptions, the practice thereby developed might be viewed as a practice within the meaning of Article 31(3)(b) of the Vienna Convention. Whether the OECD TPGs really follow Article 31(3)(b) of the Vienna Convention would have to be assessed on a case by case basis, i.e. with regard to state-parties to a particular DTC. It is highly unlikely that the whole content of the OECD TPGs will be followed with no exception by any two different states (if one takes into account

developed economies with the number of cross-border transfer pricing controversies high enough to draw general conclusions) and that this content will be identically understood in both jurisdictions. Moreover, as it will be signaled in further parts of this paper, fundamental differences in approach appear with regard to vital issues from the OECD TPGs between developed and rapidly developing countries and such differences can only be greater in the future.

The OECD TPGs can hardly be viewed as preparatory work in respect to DTCs. In certain cases the rejection of such a view has simple grounds – the conclusion of the DTC preceded publication of the OECD TPGs in general or at least it preceded publication of a current version of the OECD TPGs.

The remarks made above are equally applicable to the UN Manual.

The outcome of the analysis of the OECD TPGs and the UN Manual presented in this section of the paper justifies the position that neither the provisions of the Vienna Convention regarding the interpretation of treaties nor the customary rules of international law in this regard grant any special status to the OECD TPGs or the UN Manual unless state parties to a particular DTC expressly grant such special status in the DTC itself or in a protocol thereto. Alternatively significant and uniform practice of both state parties to a DTC strictly and expressly following the OECD TPGs or the UN Manual in their entirety might, at times, be viewed as a practice within the meaning of Article 31(3)(b) of the Vienna Convention.

III. Transfer pricing guidelines – national perspectives

1. *Poland*

The catalogue of the sources of law from Article 87 of the Constitution of the Republic of Poland of 2 April 1997[8] excludes the possibility of treating the OECD TPGs as a binding law in Poland. Yet, the introduction of a transfer pricing regime based on the solutions

[8] Dziennik Ustaw [Journal of Laws] 1997, No. 78, item 483 with amendments.

developed by the OECD to the Polish legal order was connected with Poland's accession to the OECD[9]. DTCs concluded by Poland are based on the OECD Model and most of them reflect Article 9(1) of this Model[10]. Nowadays, Polish provisions resemble the recommendations from the OECD TPGs to a significant extent. Moreover, the Minister of Finance when preparing by-laws is – in a sense – at least partly bound by the OECD TPGs. Under Article 11(9) of Corporate Income Tax Act of 15 February 1992[11] the Minister of Finance shall determine, by regulation, the manner and procedure of estimating income and the manner and mode of eliminating double taxation in connection with the adjustment of profits of associated enterprises, taking into account in particular the guidelines of the OECD. The provision has its equivalent in Article 25(8) of the Personal Income Tax Act of 26 July 1991[12]. The OECD's soft-law cannot thus be ignored in the process of creating executive regulations.

Polish courts tend not to elaborate on the legal status of the OECD TPGs even when a complaint should prompt them to do so. Although it is at least disputable whether one can plead that a tax decision is illegal due to infringement of the OECD TPGs (such a plea would definitely be extremely risky at the level of the Supreme Administrative Court, which only gives judgment, as a matter of principle, within the limits set by a complaint and its pleas). In a judgment subsequent to such a plea a court has an opportunity to assess the legal status of the OECD TPGs (see, for instance, the judgment of the Regional Administrative Court in Cracow of 15 October 2010, I SA/Kr 1188/10, and the judgment of the Regional Administrative Court in Szczecin of 9 January 2008, I Sa/Sz 615/07). The OECD TPGs are used in the following ways by Polish courts:

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9 S. Sojak, *Ceny transferowe. Teoria i praktyka* [*Transfer Pricing. Theory and Practice*], Warszawa: Wydawnictwo Naukowe PWN 2001, p. 9.

10 See detailed review of Polish DTCs compared with the OECD Model: K. Lasiński-Sulecki, *Ceny transferowe w prawie podatkowym i celnym. Wpływ powiązania przedsiębiorstw na podstawę wymiaru podatków i ceł w prawie polskim, międzynarodowym i unijnym* [*Transfer Pricing under Tax and Customs Law. Impact of Associated Enterprises on Tax Base and Customs Value*], Warszawa: LEX a Wolters Kluwer business 2014, pp. 77-82.

11 Dziennik Ustaw [Journal of Laws] 2014, Item 851 with amendments.

12 Dziennik Ustaw [Journal of Laws] 2012, Item 361 with amendments.

- to find therein the meaning of certain expressions (see the judgment of the Regional Administrative Court in Lublin of 20 September 2006, I SA/Lu 96/06),
- as an indicator of the purposes of a DTC (judgment of the Regional Administrative Court in Cracow of 3 June 2009, I SA/Kr 1374/08; the judgment of the Supreme Administrative Court in Bydgoszcz of 22 December 2006, I SA/Bd 650/06), and
- as equal to evidence measures (the judgment of the Supreme Administrative Court of 18 August 2004, FSK 359/04).

The last approach presented above is at least controversial. Sometimes courts simply point out that the OECD TPGs were transposed into a Polish domestic legal order (judgment of the Regional Administrative Court in Cracow of 3 June 2009, I SA/Kr 1374/08). It also happens that courts make reference to the OECD TPGs themselves without further elaborating on the topic (the judgment of the Regional Administrative Court in Wrocław of 26 July 2012, I SA/Wr 706/12).

2. USA

The United States of America is one of the founding members of the OECD along with Canada and 18 European countries. Despite this fact, the approach of the US towards transfer pricing soft-law developed by the OECD is ambivalent, to say the least. The US does not consider itself to be bound by the OECD TPGs and does not include references to these guidelines in its domestic provisions[13]. From time to time tax professionals witness huge disputes over the compatibility of US regulations with the OECD TPGs where the US is said to depart from the arm's length principle by introducing provisions that cannot be linked to the OECD TPGs (for instance, departure from transactional methods[14],

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13 OECD, Transfer Pricing Country Profile: United States, February 2009, http://www.oecd.org/tax/transfer-pricing/38437095.pdf [last accessed: 1.10.2014].

14 L. Eden, *Taxing Multinationals: Transfer Pricing and Corporate Income Taxation in North America*, Toronto-Bufallo-London: University of Toronto Press 1998, p. 394.

the best method rule[15], commensurate with income standard[16]). Typically, following a few years of discussions, the OECD aligns its soft-law with the US approach rather than the US stepping back.

The OECD TPGs are at times referred to by American courts[17] and applied to interpret DTCs concluded by the US[18] (see, for instance, the judgment in case *National Westminister Bank PLC v. the United States*[19]).

3. Australia

Australia has based its transfer pricing provisions to a huge extent on the OECD TPGs[20]. Australian tax rulings and guidance from tax administration refer to the OECD TPGs[21]. Courts in Australia happen to refer to the OECD TPGs, but they do not analyze their legal status. Sometimes judges repeat certain phrases from the OECD TPGs, claiming that these guidelines make it possible to reach an arm's length price (judgment of Administrative Appeals Tribunal, Sydney, of 28 July 2008 in case *Roche Products Pty Ltd and Federal Commissioner of Taxation*[22]). In numerous judgments the courts stress, however, that there is no obligation to apply the OECD TPGs (judgment of Federal Court of 24 May 2001 in case *Daihatsu Australia Pty v. Federal Commissioner of Taxation*[23]), the OECD TPGs do not impose the obligation to apply any specific transfer pricing method (the judgment of Federal Court,

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15 M. Maliszewski, *Metody określania cen transferowych w prawie podatkowym Stanów Zjednoczonych* [*Transfer Pricing Methods under Tax Law of United States*], Kwartalnik Prawa Podatkowego [Tax Law Quarterly] 2003, no. 1, pp. 106-108.

16 K. Vogel, H.A. Shannon III, R.L. Doernberg, K. van Raad, *United States Income Tax Treaties*, The Hague-London-Boston: Kluwer 1995, pp. 442-443. See also F. C. de Hosson, *Transfer pricing: the break-down of consensus*, Intertax 1992, no. 6/7, p. 414.

17 A. Vögele, M. Collardin, [in:] A. Vögele, T. Borstell, G. Engler, *Handbuch der Verrechnungpreise*, Munich: C.H. Beck 2004, p. 1713.

18 J. A. Becerra, *Interpretation and Application of Tax Treaties in North America*, Amsterdam: IBFD 2007, p. 92.

19 Case 95-758T, 58 Fed. Cl. 491 (2003).

20 A. Joseph, *Transfer Pricing Comparability: Perspectives of OECD, Australia and United States*, International Transfer Pricing Journal 2007, no. 2., p. 96.

21 OECD, *Transfer Pricing Country Profile: Australia*, November 2006, available online: http://www.oecd.org/tax/transfer-pricing/44071214.pdf [last accessed: 6.10.2014].

22 [2008] AATA 639.

23 [2001] FCA 588.

Melbourne, of 25 July 2010 in case *SNF (Australia) Pty Ltd v. Federal Commissioner of Taxation*[24], the judgment of Federal Court of Taxation, General Division, of 1 June 2011 (in case *Commissioner of Taxation v. SNF (Australia) Pty Ltd*[25])[26].

IV. Should guidelines become binding?

1. MNC's perspective

The guidelines developed by international organizations should facilitate the application of transfer pricing provisions by MNCs. Multinational groups of companies cannot obey transfer pricing rules throughout the world if these rules are not identical or at least highly similar. In any other case they always take the risk that conditions of their cross-border transactions might be questioned in at least one jurisdiction. It would not be possible to arrange transactional conditions in such a way that tax authorities in all jurisdictions involved would be satisfied.

The MNCs would, therefore, definitely benefit in terms of limiting their exposure to tax controversies if the guidelines developed by the OECD or by another organization were binding. Similarly, it is also advantageous for MNCs when such guidelines, even if they are not legally binding, are adhered to by legislators and tax authorities worldwide[27].

2. The perspective of tax administration

The legally binding character of transfer pricing guidelines is not overly important for tax administrations. The lack of details in DTCs' provisions on transfer pricing even allows exchequers to look

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[24] [2010] FCA 635.

[25] [2011] FCAC 74.

[26] For an overview of other countries and more detailed comments concerning Australia, Poland, and the UE see Lasiński-Sulecki, supra note 2, pp. 350-356.

[27] A. Storck, *OECD Transfer Pricing Guidelines – A Business Perspective*, [in:] *Practical Experience with the OECD Transfer Pricing Guidelines. Proceedings of a Seminar held in London in 1998 during the 52nd Congress of International Fiscal Association*, vol. 23b, The Hague-London-Boston: Kluwer Law International 1999, p. 14.

for the financially most advantageous way of interpreting these provisions without being bound by a highly precise set of internationally adopted rules. Yet, the efficiency of tax administrations would definitely gain from such a character of transfer pricing guidelines or from their rather exact transposition in domestic legal orders (transposition word for word in their entirety is impossible as guidelines are structured and worded in a different manner than is usual for tax provisions). They would not be involved in as many mutual agreement procedures as they are nowadays, as discrepancies in approach between different tax jurisdictions would occur more rarely. Once tax arbitration becomes more common, tax administrations will save time that they would otherwise have had to devote to such proceedings. Thus, turning guidelines into hard-law would also be beneficial for tax administrations.

The conclusion that replacing soft-law on transfer-pricing with hard-law would be a good solution for both tax administrations and MNCs, though for different reasons, leaves one question unanswered – which set of soft-law should prevail if discrepancies between existing sets arise?

V. OECD Guidelines v. UN Manual – prospects for the near and distant future

The following countries are currently members of the OECD: Australia, Austria, Belgium, Canada, Chile, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, the Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. In 2007 the OECD members agreed to open discussions concerning membership with Russia. Enhanced engagement programs were open to Brazil, India, Indonesia, and South Africa. The number of members of the OECD as compared with the number of members of the UN is obviously very limited.

The UN Manual was created, inter alia, thanks to the efforts of the Subcommittee on Transfer Pricing – Practical Matters that comprised

experts from the public sector, private sector and academia from a whole string of countries: Australia, Brazil, China, France, India, Italy, Japan, Korea, Malaysia, Netherlands, Nigeria, Norway, South Africa, and the USA. The representatives of the OECD also participated in the work of this subcommittee.

Rapid development of the economies of non-OECD countries, particularly China and India, in recent years, along with the development of competencies of tax administrations has led to the growth of potential fields of dispute between typically richer OECD countries and poorer, but rapidly developing, non-OECD nations as to the understanding of provisions concerning transfer pricing in DTCs. The problem of location savings seems to be the best example of cross-jurisdictional controversy, where the tax administrations of richer and poorer countries typically have entirely opposite views. This situation may lead to one of three possible developments. Either the rapidly-developing countries will gain more influence on the outcome of the work of the OECD (for instance by becoming members of this organization) or they will tend to stress that the OECD TPGs are not binding on them and plausibly will prefer to rely on other sets of soft-law which are created with the stronger impact of developing countries. Another option is that the OECD will emphasize strongly incorporating non-members to join in its work on tax related documents, including the OECD TPGs. The documents prepared by the OECD are even now being made public at the preparatory stage, thus allowing stakeholders to express their views during the drafting process.

VI. Summary

There is a huge gap between the hard-law and soft-law applicable in transfer pricing matters if one takes into account their size and level of detail. DTCs’ provisions on these matters can be described as vague when compared to detailed soft-law. One could even risk claiming that actual cross-border transfer pricing disputes are nearly always connected with the content of soft-law, rather than the wording of the DTCs as such. Teams of experts on transfer pricing discuss the details of transfer pricing methods that are dealt with exclusively in the OECD TPGs.

Pieces of soft-law, though not entirely dissimilar, slightly differ and these differences will probably become more significant in the future. This may in turn lead to situations where certain pieces of soft-law will lose importance in practice while others gain importance. Such a situation may be overcome either by attempting to broaden the content of the OECD Model and subsequently re-negotiating the whole network of DTCs based thereon, or by trying to grant the OECD TPGs special status of aid in the interpretation of DTCs by means of, for instance, protocols to DTCs. The common acceptance of such changes in international taxation would most likely depend on tackling the most important differences in approach between the most significant figures in world economy.