

Taisiya Duda,

Research supervisor: Sergii Kadkalenko

Candidate of Law Sciences, Associate Professor

Language tutor: Viktoriia Klavdich

Candidate of Philological Sciences, Associate Professor

Taras Shevchenko National University of Kyiv

THE CONCEPT OF TRANSFER PRICING CONTROL UNDER THE ARM'S LENGTH STANDARD

The European Court of Justice has confirmed the compatibility of transfer pricing adjustments under the arm's length standard in its "SGI" judgment. In this decision, the ECJ has stated that transfer pricing control is justified as a means to fight "artificial arrangements" while commercially valid transactions have to be accepted by the tax authorities. This report shows that the economics of integrated business and the commercial purpose of transfer pricing (setting the right incentives for intra-firm services and supplies) justifies nonarm's length transfer pricing in many situations. Against this background, a new approach to international allocation of taxing rights is proposed: any "rents" derived by a group company from transactions with other group companies shall be taxable in the latter's country of residence by an extension of limited tax liability for foreign group companies [5, p. 110].

The concept of transfer pricing control under the arm's length standard as a means for the international allocation of profits and taxing rights sits on time-honored provisions under domestic law, international law and European law. Most countries have long ago introduced provisions into their tax codes targeting cross-border transactions among related commercial entities[1, p. 19-20; 4, p. 73].

This standard has become accepted both internationally and within the European Union. "Dealing at arm's length" was the starting point for the model treaties elaborated under the auspices of the League of Nations since the days of the Carroll Report of 1932; today both Art.9 of the OECD Model Double Tax Convention and Art. 9 of the UN Model Treaty subscribe to it [2; 3]. Moreover, they provide for an obligation of the other involved state to make a countervailing adjustment in order to avoid double taxation of the same profit.

In their 2017 update of their Transfer Pricing Guidelines, the OECD proudly exposes the worldwide acceptance of the arm's length principle, a fact which – as everybody will agree – is of high value in itself [3]. Nevertheless, the arm's length standard is under attack –conceptually, politically and legally.

The main thrust of the academic debate on the concept of the arm's length standard refers to its compatibility with the very rationale for the existence of large firms[1, p.105; 4, p. 203].

On the whole, the economic, political and legal arguments against the arm's length standard seem to press for the introduction of global or regional profit consolidation for corporate groups accompanied by a formulaic apportionment of the tax base.

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