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EU Joint Transfer Pricing Forum. The application of the Profit Split Method within the EU (PSM)

The European Union's Joint Transfer Pricing Forum (JTPF) on March 29 issued a report examining the application of the profit split method (PSM) in the EU ("*The application of the Profit Split Method within the UE*" - DOC: JTPF/002/2019/EN).

It includes the following sections:

- Section 1- Introduction: in which it is specified that *"[…] due to the increased integration of multinational enterprises and the globalization of national economies and markets, the clarification of the PSM was one of the priorities identified in the action plan against Base Erosion and Profit Shifting (BEPS). Indeed, in order to develop rules that can prevent BEPS resulting from engaging in transactions which would not, or would only very rarely, occur between third parties, Action 10 called for clarification of the application of transfer pricing methods, in particular of the transactional profit split method, in the context of global value chains […]";*
- Section 2 - *Description of the profit split method;*
- Section 3 - *Use of the profit split method;*
- Section 4 - *How to split the profit;*
- Section 5 - *Concluding remarks.*

The documents also includes some annexes – which are interesting from an operating perspective as well – which show the indicators based on which the PSM is the most appropriate for transfer pricing. It is specified that: "*The OECD Guidelines on the use of the PSM list the following indicators for determining whether the PSM may be considered the most appropriate transfer pricing method in a specific set of circumstances: the existence of a unique and valuable contribution by each party to the controlled transaction, and/or; a high level of integration regarding business transactions to which the transaction relates, and/or the shared assumptions of economically significant risks or separate assumption of economically closely related risks by the parties to the transaction*".

EUROPEAN COURT OF JUSTICE

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«*Reference for a preliminary ruling — Value added tax — Directive 2006/112/EC Harmonisation of fiscal legislation — Deduction of input tax — Immovable property acquired as capital goods — Sale and lease back — Adjustment of deductions of VAT — Principle of VAT neutrality — Principle of equal treatment*». Judgement dated 27 March 2019, Case C-201/18

This request for a preliminary ruling concerns the interpretation of Articles 14, 15, 168, 184, 185, 187 and 188 of VAT Directive and has been made in proceedings between Mydibel SA and *État belge* (the Belgian State) concerning the adjustment of a deduction of VAT.

In the case at issue, in order to increase its liquidity, Mydibel and two financial institutions entered into sale and lease back transactions, not subject to VAT, relating to certain buildings; specifically, the company entered into an agreement establishing an emphyteutic right over those buildings and a real property leasing agreement in respect of such buildings.

There were two questions referred for a preliminary ruling. Firstly, the referring court has asked whether articles 184, 185, 187 and 188 be interpreted and applied as meaning that there is an obligation to adjust the VAT on immovable property which was initially deducted correctly, where that immovable property was the subject of a sale and lease back transaction not subject to VAT, as in the case at issue. Secondly, the court has asked whether an interpretation of Articles 184, 185, 187 and 188 of the VAT Directive as imposing an obligation to adjust the VAT initially deducted complies with the principles of VAT neutrality and equal treatment.

The Court has ruled as follows: "*Subject to verification of the relevant matters of fact and national law by the referring court, Articles 184, 185, 187 and 188 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, as amended by Council Directive 2009/162/EU of 22 December 2009, must be interpreted as not imposing an obligation to adjust value added tax (VAT) on a building which was initially deducted correctly, where that property was the subject of a sale and lease back transaction not subject to VAT in circumstances such as those at issue in the main proceedings.*
An interpretation of Articles 184, 185, 187 and 188 of Directive 2006/112, as amended by Directive 2009/162, as imposing an obligation to adjust the value added tax (VAT) initially deducted in circumstances

such as those at issue in the main proceedings complies with the principles of VAT neutrality and equal treatment".

The European Court of Justice has focused on the concept of 'capital goods' (please see judgement "*Eon Aset Menidjmunt*") which are goods used for the purposes of economic activity and distinguishable by their durable nature and their value and such that the acquisition costs are not normally treated as current expenditure but are written off over several years. The Court has also focused on the sale and lease back transactions and ruled that in the case at issue such transactions could not be classified as 'supplies of goods' in so far as the rights transferred to the financial institutions following those transactions did not empower them to dispose of the buildings as if they were their owners.

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