OECD Financial Transactions paper

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In brief

On 11 February 2020, the OECD issued the long-awaited final version of the Financial Transactions paper (first issued as a non-consensus document in July 2018). The document evaluates the following issues:

- Delineating the transaction
- Intra-group lending
- Cash pooling
- Hedging
- Guarantees
- Captive insurance

In detail

Impact

The paper is the first to be issued by the OECD which reflects a consensus position with respect to the treatment and pricing of intercompany financial transactions. As such, companies need to assess the new guidelines (which will form Chapter X of the OECD Transfer Pricing Guidelines) against their existing group intercompany financing policy. Areas which are likely to be of greatest interest and impact include the application of implicit support, credit rating methodologies (tools and application), reconciliation against cost of external borrowing, application of the most appropriate terms and conditions for the transaction and interest rate pricing (including appropriate adjustments).

Why now

The new Chapter will form the foundation for local application of financial transactions transfer pricing rules (in particular in territories, including Cyprus, which follow the OECD Transfer Pricing Guidelines) and also for bilateral disputes and resolution on a go forward basis. It is therefore important that companies consider the impact now as tax authorities begin to implement and apply this new framework and the principles within. In some cases, these guidelines will reflect a step change in the way groups currently approach transfer pricing for intra group financial arrangements, requiring significant overhauls of their policies for such arrangements. Alongside the new OECD chapter, the abolition of LIBOR in 2021 is prompting businesses to review their external and internal financing arrangements and so there is opportunity to concurrently address the LIBOR abolition alongside bringing intra group policies into line with the Guidelines.

Why PwC

We have extensive experience having worked with a wide variety of groups on assessing their financial transactions transfer pricing policies and shaping practical, sustainable, defendable solutions, in particular in areas such as:

- Defining a group credit scoring policy for loan/guarantee pricing purposes, taking into account implicit support and sovereign credit rating nuances
- Developing pricing grids/frameworks which allow flexibility for duration, credit rating, currency etc. for intercompany group loan and guarantee pricing
- Determining the key terms, conditions and covenants to be included in intercompany legal agreements (and reflecting market changes such as the upcoming LIBOR replacement)
- Shaping cash pooling, hedging and captive insurance policy frameworks taking into account the functional activities, underlying risks and assets at risk
- Supporting with the implementation (including legal support), documentation (including for Master File purposes) and defence of such arrangements.

The takeaway

The most important first step for companies will be to analyse their existing financial transactions transfer pricing policy against the new OECD framework. We will collaborate with you to perform a desktop assessment of your existing policy and risk assess which areas need immediate remediation, along with providing recommendations as to potential options for adapting your existing approach.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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