

CMS Survey: VAT relevance of TP adjustments

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It is common practice, especially immediately after year-end financial results are available, that most of the multinational groups perform year-end transfer pricing adjustments that are generally connected to profit based methods.

However, the main concern - on top of any transfer pricing specific issue related to these adjustments - is related to the VAT treatment that shall apply. This aspect is not always straight-forward as it might generate uncertainty and potential liabilities.

Counting on its worldwide network, CMS has run a survey and prepared this preliminary and high-level snapshot on how VAT and TP adjustments interrelate across the main EU and not-EU jurisdictions.

This document does not have the aim to provide a full and comprehensive representation on the applicable VAT regime in the different countries, which might be subject to further detailed investigations. Conversely, the content is intended to help tax practitioners for VAT/TP diagnostics and risk management through an immediate comparative tool.

Table 1: Comparative assessment on VAT relevance of TP adjustments

		Country								
		Austria	Belgium	Croatia	France	Germany	Hungary	Italy	Netherlands	Norway
1	Is there any provision in your VAT code that provide for the VAT treatment of the TP adjustments?	✗	✗	✗	✗	✗	✗	✗	✗	✗ ¹⁰
2	Are there any guidelines on this matter?	✓ ¹	✗	✗	✗	✗	✗	✓ ⁷	✗	✓ ¹¹
3	Are there any Case Law on this matter?	✗	✗ ²	✗	✗	✗	✓	✗	✗	✓ ¹²
4	Are you aware of any tax auditors practice in your Country?	✗	✓	✗	✓ ⁴	✗	✓	✗	✗	✗ ¹³
5	How are usually qualified TP adjustments for VAT purposes?									
a	<i>out of scope of VAT</i>					✓ ⁵			✓ ⁹	✓
b	<i>price adjustments of previous supply of goods/services relevant for VAT</i>	✓	✓	✗	✓	✗				
c	<i>Consideration for a separate (subsequent) supply of service subject to VAT</i>					✗				✓ ¹⁴
d	<i>other</i>			✗ ³		✗	✓ ⁶	✓ ⁸		

Table 2: Comparative assessment on VAT relevance of TP adjustments (cont'd)

		Country								
		Poland	Portugal	Romania	Russia	Serbia	Spain	Switzerland	Turkey	United Kingdom
1	Is there any provision in your VAT code that provide for the VAT treatment of the TP adjustments?	✗	✓ ¹⁸	✗	✗	✗	✗	✗	✓ ²⁷	✗
2	Are there any guidelines on this matter?	✓ ¹⁵	✗	✗	✗	✗	✗	✗	✓ ²⁸	✓
3	Are there any Case Law on this matter?	✓ ¹⁶	✓ ¹⁹	✗	✗	✗	✗	✗	✓ ²⁹	✗
4	Are you aware of any tax auditors practice in your Country?	✓ ¹⁷	✗	✓ ²¹	✗	✗	✓ ²⁵	✗	✓ ³⁰	✓
5	How are usually qualified TP adjustments for VAT purposes?									
a	out of scope of VAT	✓			✗				✗	✓
b	price adjustments of previous supply of goods/services relevant for VAT	✓			✗	✓ ²⁴	✓	✗	✓	✓ ³¹
c	Consideration for a separate (subsequent) supply of service subject to VAT	✗			✗				✓	
d	other	✗	✗ ²⁰	✓ ²²	✓ ²³			✗ ²⁶	✗	

Notes to the tables:

- (1) Cf. Sec 4.1.4. of the TP Guidelines 2021 of the Austrian Ministry of Finance:

A TP adjustment generally leads to a VAT adjustment of the previous supply of goods/services pursuant to Sec 16 of the Austrian VAT Act. However, the VAT adjustment may be waived by the tax authorities if (i) the VAT adjustment has no effect on the tax revenue and (ii) the waiver does not lead to a "disruption" of the VAT Information Exchange System.

- (2) Not case law but the Belgian Office for Advance Tax Rulings has treated this subject in individual tax rulings, indicating that TP adjustments on VAT-taxable transactions should result in a subsequent change of the VAT-taxable base of that transaction.
- (3) Specifics of each case should be analysed separately. TP adjustments, if done by taxpayers through additional invoicing/discounts (debit/credit notes) at year-end, will likely be treated as price adjustments of previous supplies.
- (4) So far, auditors do not question the VAT treatment applied by companies when they audit transfer pricing policy.
- (5) It appears that the tax authorities are regularly satisfied if the international cross-check between intra-community supplies in the state of origin and the intra-community acquisitions in the state of destination (based on recapitulative statements etc) matches.

Hence, it is key that whatever taxpayers do, they need to do it group-wide in an aligned manner. In case of a dispute it seems rather unclear whether a TP adjustment is relevant for VAT purposes.

The key question should be whether there is a sufficient link to the underlying supplies or services. This probably depends pretty much on the individual circumstances.

- (6) All the 5 a, b, c treatments are possible, depending on the nature of the price adjustment and whether there is any performance behind.
- (7) Currently the Italian Tax Authorities have issued few Resolutions in which they confirmed the approach suggested by the EU commission to be evaluated, in any event, on a case-by-case basis.
- (8) The TP adjustment is relevant to VAT purposes if:

- it is foreseen a consideration for the TP adjustment (e.g. adjustments made directly as changes for direct tax purposes are not relevant for VAT purposes);
 - the transactions to which this consideration relates are identified;
 - there is a direct link between the supplies of goods or services and the consideration.
- (9) It is assumed that there are no actual payments (only TP adjustments for Dutch corporate income tax purposes).
- (10) Not directly, but a change in how the consideration between supplier and recipient will result in a change in the VAT treatment as a consequence of the VAT system.
- (11) Guide concerning customs value, including import VAT.
- (12) Caselaw in connection to the calculation of import VAT: LB-2008-11968, LB-2016-77476, LB-2015-16048.
- (13) Not directly concerning TP, but rather a consequence of price adjustment.
- (14) VAT Act Section 4-4 – regulates turnover if there is a commonality of interest.
- (15) Yes, the Ministry of Finance guidelines from 2021 regarding the TP adjustments. Under the guidelines, in a case where the transfer pricing adjustment does not change the remuneration for transactions - specific supplies of goods or services to related entities - but is aimed at adjusting the company's profitability to the market level, such adjustment is outside the scope of VAT taxation.
- Consequently, it is not documented with a VAT invoice. However, if the TP adjustments changes the remuneration for particular transactions, the VAT invoice should be corrected, therefore the amount of VAT due may also change.
- (16) Yes, see e.g. the Individual Tax Rulings no. 0114-KDIP2-2.4010.47.2020.1.SJ, 0111-KDIB1-2.4010.98.2019.5.AW or 0111-KDIB3-1.4012.754.2019.1.KO. The approach presented by the Polish authorities is generally in line with the above-mentioned guidelines.
- (17) Yes, the approach presented by the tax auditors is generally in line with the above-mentioned guidelines.
- (18) VAT Code, Article 16.º, number 10 – Is applicable when a transaction is carried out between related entities (as defined in the CIT Code, but including relationships between employers and employees, their family or other closely connected people) when one of the entities does not have

a full right to a VAT deduction and it establishes that the taxable amount is the open market value when, inter alia, the value of the transaction is lower than the open market value and the recipient does not have a full right to deduct VAT.

- (19) CAAD (Arbitral court) Proc. nº 751/2019-T - The exceptional consideration of an objective value is subsumed in cases of tax fraud or evasion, which in Portugal are covered by article 16(10) of the CIVA, in which the legislator allows adjustments considering the normal value of the transactions as the taxable amount.

Thus, VAT corrections in cases of "transfer pricing" between entities with special relations are only exceptionally allowed, in accordance with European Union Law.

- (20) Transfer pricing adjustments are preferably a matter of income tax (CIT or even PIT) and, as a general rule, they do not trigger any impact on other taxes. As for VAT, the corresponding correction as a result of transfer pricing adjustments would depend on the issue of a corrective invoice.

However, considering VAT neutrality (because of the right to deduct input VAT), as a general rule, there is no need for price adjustments for VAT purposes as a result of transfer pricing adjustments.

This notwithstanding, the VAT Code provides for a VAT-specific transfer pricing rule applicable when a transaction is carried out between related entities (as defined in the CIT Code, but including relationships between employers and employees, their family or other closely connected people) when one of the entities does not have a full right to a VAT deduction.

The VAT transfer pricing rule applies automatically whenever one of the following situations verifies:

- the consideration is lower than the open market value and the recipient of the supply does not have a full right to a VAT deduction;
- the consideration is lower than the open market value and the supplier does not have a full right to a VAT deduction and the supply is subject to an internal exemption; or
- the consideration is higher than the open market value and the supplier does not have a full right to a VAT deduction.

In these cases, the corresponding taxable amount for VAT purposes should be the open market value (as defined in Article 16, No. 4 of the VAT Code), with the value of the consideration being disregarded.

- (21) Based on our experience, the tax inspectors would not analyse the applicable VAT treatment when they audit the transactions performed

with related parties and make TP adjustments. Also, the Romanian tax law does not provide explicitly for the possibility that the taxpayer would perform voluntary TP adjustments. Thus, the situations of voluntary TP adjustments need to be carefully analysed from all tax angles.

(22) Please refer to above answer.

(23) Russian tax legislation regulates the rules of adjustment of the tax base by a taxpayer, rather than conduction of a price adjustment between the parties involved.

Thus, following the rules provided in the Tax code, a Russian taxpayer should adjust its taxable base to meet the arm's-length level, without the obligation to adjust the prices for the supplied goods / services, or otherwise claim a consideration from another party to a controlled transaction.

However, in practice the taxpayers normally still seek to formalize the adjustment in a way, that would allow its foreign counterparty to adjust its tax base accordingly, thus choosing among the following options:

- price adjustments of previous supply of goods/services relevant for VAT; or
- consideration for a separate (subsequent) supply of service (other flow) subject to VAT; or
- payment of extraordinary consideration (e.g. in form of a bonus), etc.

However, these additional measures introduced rather stand for a commercial form of a price / profitability adjustment selected by the parties (and not per se regulated by the Tax code), then a TP adjustment explicitly regulated by the Russian tax legislation.

The VAT treatment of such alternative way of TP adjustment formalization thus depends on the type of the flow giving rise to a TP adjustment, and a form of such adjustment, chosen by a taxpayer, each giving rise to its specific VAT considerations.

In practice indeed the VAT treatment of such alternative forms, as well associated tax risks, are usually carefully analyzed by the parties for each specific case concerned, and may act as a driver behind choosing one form of price adjustment formalization against another.

(24) Please note that there are no guidelines nor practice with regard to VAT treatment of TP adjustments (at least no publicly available practice), but there are reasons to believe that price adjustments of previous supplies would be the VAT outcome of a TP adjustment.

(25) Usually, auditors do not question the VAT treatment applied by companies when they audit transfer pricing policy. Moreover, it shall be noted that on the yearly so called "Tax Audit Control Plan" for 2021 it was stated that transfer pricing audits and market valuation controls would be conducted on customs, although we honestly have had no experience on this.

(26) Swiss VAT law explicitly stipulates the arm's length principle for transactions among related parties (art. 24 (2) Federal Act on VAT).

However, there is neither administrative guidance nor case law how to deal with TP adjustments which are not transaction based (e.g. a profit based method); such situations seem highly problematic.

Effectively, a "global profit split" can lead to a forbidden netting of transactions and an evasion of VAT. The only easement conceivable exists at the level of import VAT, where a specific import transaction need not be adjusted due to the subsequent price correction if the recipient was entitled to a full input VAT deduction at the time.

(27) Through the amendment to Article 30/(d) of the VAT Law, in addition to the VAT paid during importation or through reverse charge mechanism within the scope of disguised profit distribution through transfer pricing, the VAT paid to sellers during seller's delivery of goods and services in Turkey and then duly declared and paid by the seller in the relevant taxation period can also be offset by the buyer from its output VAT.

This provision entered into force on 6 April 2018. From the Turkish Co. perspective, if the TP adjustment is made with a credit note from the foreign related party, the VAT can also be offset by the Turkish Co. from its output VAT, and no adjustment for VAT will be calculated.

If there is a debit note for TP adjustment, the difference between paid VAT/Customs Duty and the additional amount will be paid to customs or revenue administration.

(28) There is no guideline, and it is only explained Article 30/(d) of the VAT Law.

(29) The rule is described in the VAT Law.

(30) Yes, tax auditors are aware of this practice.

(31) In the UK market value, rule only applies where the supply is taxable and the relevant input vat is not fully recoverable and HMRC issues an 'open market value notice' to the parties requiring them to apply market values for VAT.