

COVID-19 AND NEED TO UPDATE TRANSFER PRICING POLICIES



Multinational groups operating in different geographic areas will have to face the need to update their transfer pricing policies, in order to manage the economic repercussions deriving from the change in commercial, financial and tax conditions, both in the short and medium-long term.

In particular, the current exceptional situation requires multinational groups to update their current transfer pricing policies or to implement new strategies in order to pursue the following objectives:

- 1) identify, in the short term, the group companies required to bear the possible negative economic consequences deriving from both the reduction in sales and the incurring of exceptional costs for the protection and safety of workers (e.g. costs for the decontamination and sanitation of company premises, costs for the purchase of personal protective equipment) or costs related to the early termination of contracts / projects (e.g. penalties);
- 2) reorganize, in the medium-long term, the functional profiles of the companies belonging to the group, also through the implementation of business restructuring transactions, in order to safeguard the group's profitability or, at least, to limit losses.

With reference to the first objective, the parent company could decide to fully bear the losses deriving from the economic crisis from Covid-19, believing that the pandemic risk, although exceptional, is one of the risks to be borne by the parent company.

However, it cannot be excluded that the tax authorities of the country of residence of the parent company challenge this decision, requiring that the other group entities also participate in the assumption of this risk and its effects.

On the contrary, if always with reference to the first objective the parent company deems it appropriate to allocate the negative effects of the economic crisis from Covid-19 also to the other foreign entities of the group, this choice could lead to a reduction, even significant, in the marginality of the foreign entity and could therefore be challenged by the tax authorities of the country of residence of the same, especially where the marginality of the affiliated company falls below the allowed minimum limit of the so-called *arm's length interquartile range*.



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Regardless of the choice that will be made by the parent company, it will be essential to analytically support the reasons for the choice, preparing and providing an adequate set of documents that also gives evidence of the behaviors adopted by third parties, or towards third parties, in comparable circumstances.

With reference to the second objective, the parent company may decide to carry out corporate business restructuring transactions aimed at:

- containing the overhead costs of all or some of the group entities;
- centralizing or decentralizing some activities to exploit economies of scale;
- reorganizing its supply chain, adopting leaner and more flexible procurement and marketing solutions;
- locating financial and human resources on the most profitable markets and less impacted by the effects of Covid-19;
- focusing, where possible, on the implementation and/or development of e-commerce.

These medium-long term solutions could involve revising business models, closing-down some local companies, transferring functions, assets and risks between the various group entities, as well as could have an impact (also significantly) on the global value creation chain of the multinational group.

BACCIARDI and PARTNERS remains available to assess with the companies the adoption and implementation of the most appropriate strategies, as well as to update the transfer pricing set of documents.