ADVENTURES IN TRANSFER PRICING – PRACTICAL EXPERIENCE IN GERMANY

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INTRODUCTION

Among tax directors at multinational corporations ("M.N.C.'s") German tax authorities are viewed to be among the most aggressive and sophisticated tax authorities in challenging straightforward transfer pricing solutions. This article explains the reasons behind this view and highlights key takeaways from recent transfer pricing tax controversies in Germany.

GERMAN ECONOMIC AND REGULATORY LANDSCAPE

Germany is the most industrialized European economy with a broad range of large M.N.C.'s operating across major industries, in particular automotive, industrial suppliers, chemicals, and pharmaceuticals. Germany also has hundreds of mid-sized hidden champions that are globally successful under the "Made in Germany" label. These open market policies in conjunction with high G.D.P. and high per capita income make Germany an attractive market for M.N.C.'s, based in other European countries, the U.S., Japan, Korea, and China .

At the same time, Germany has remained a high tax country, with the effective corporate tax rate now close to 30%. As a consequence, Germany has experienced negative effects from a global race to the bottom in terms of international corporate tax. International tax planning in the golden age of globalization (roughly 1990-2015) put transfer pricing at the heart of tax planning by multinational corporations ("M.N.C.'s"). Tax-effective supply chains popped up, enabling M.N.C.'s to gain competitive advantages over locally based competitors.

M.N.C.'s discovered the potential to set up structures that serve the German market through low-risk, low-margin local operations. In particular, many U.S. M.N.C.'s have restructured their subsidiaries in Germany to move legacy I.P. to European affiliates established in low-tax jurisdictions. The remaining operations in Germany were converted to contract manufacturers, contract R&D centers, and low-risk distributors, allowing profits to be realized by European affiliates in low-tax jurisdictions. M.N.C.'s have also stripped German profits further through intragroup financing.

To overcome disadvantages of remaining barriers to free trade – such as customs barriers, the U.S. Inflation Reduction Act from 2022, and Chinese requirements for German M.N.C.'s to transfer technology to Chinese affiliates, and high taxation at home – German M.N.C.'s globalize their footprint to increasingly set up high-value functions in critical markets like the U.S. and China. They regularly transfer domestically developed intangibles to such territories.

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For many years, German tax authorities suspected that M.N.C.'s transfer pricing policies were not in line with the arm's length principle. Consequently, it comes as no surprise that Germany spearheaded international regulatory developments related to the arm's length standard.

This started with the German transfer of function rules established in 2008 that largely influenced the O.E.C.D. business restructuring rules. Then came the "base erosion and profit shifting" ("B.E.P.S.") initiative, which attacked traditional I.P. structuring and entrepreneurial profit capturing by principals with little economic substance established in low-tax jurisdictions. This translated into the paradigm shift of the O.E.C.D. transfer pricing guidelines in 2017. Legal I.P. and legal structuring of risk allocation within M.N.C.'s alone would no longer be acceptable identifiers to allocate consolidated group profit. In their place, functional development, enhancement, maintenance, protection and exploitation ("D.E.M.P.E.") contributions to intangible resources of company value became the key consideration. Finally, the German government is a key proponent of Pillar II and the O.E.C.D. B.E.P.S. 2 initiative, which seeks to achieve global minimum taxation and to prevent "unfair" distortion of international tax competition.

INCREASING TRANSFER PRICING CONTROVERSY IN GERMANY

Given local regulatory developments, international M.N.C.'s face ever increasing tax controversies in Germany related to transfer pricing matters across a broad range of areas. The challenges may be summarized as follows:

- **Challenges to transactional net margin method ("T.N.M.M.") for distributors.** M.N.C.'s with sales subsidiaries in Germany find that returns based on T.N.M.M. benchmarking are regularly challenged on the grounds that the German sales entity is considered to have made intangible-related D.E.M.P.E. contributions in the field of marketing. Following German administrative guidelines, the T.N.M.M. is rejected as inappropriate and the transfer pricing ("T.P.") documentation characterized as fundamentally flawed. This opens the ground for German tax authorities to make their own discretionary assessment of arm's length pricing, shifting the burden of proof to the taxpayer. In this context, it is important to know that, while the O.E.C.D. T.P. Guidelines and the related new intangible and D.E.M.P.E. concepts were first integrated into German tax law in 2022, the tax authorities maintain that the D.E.M.P.E. concept is only a clarification of previously existing rules because D.E.M.P.E. contributions were effectively already considered by German tax authorities in the past. Consequently, the analytical framework of the 2022 O.E.C.D. T.P. Guidelines is applied to auditing years prior to 2022.

- **German tax authorities regularly reject external comparable uncontrolled transactions ("C.U.T.").** When challenging the arm's length nature of intragroup license arrangements, the German tax authorities contend each intangible is unique by definition. They aim to force taxpayers to determine and disclose consolidated profit jointly generated by the licensor and the licensee in order to assess appropriate royalties through a *de facto* profit split analysis.

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- **German tax authorities have adopted a very broad definition to what qualifies as a transfer of a valuable function.** Regarding business restructurings, German transfer pricing rules entitle the transferor to be compensated for both (i) the present value of the profit potential that is relinquished and (ii) a share of business and tax synergies realized by the transferee. The transfer pricing rules in the latest regulatory update no longer require the transfer of intangible assets owned by the transferor as part of a package to apply transfer of function valuations.. When computing such valuation, an infinite time horizon is the general default rule. It is the responsibility of the taxpayer to prove that a shorter time horizon should be applicable and to demonstrate what the shorter horizon should be. Exit tax charges of double or triple digit millions USD can easily arise in such cases.
- **German tax audits involving transactions with economic principals in low-tax jurisdictions require excessive data from taxpayers.** German tax authorities regularly aim to extend requirements in the tax audit so that the taxpayer is effectively forced to document at a fairly granular level the economic substance and value contribution of the principal based in a low-tax jurisdiction. German tax authorities are widely aware that U.S. M.N.C.'s manage the group effective tax rate through use of licensing companies in low-tax jurisdictions. When the German tax authorities conclude that the profit of the licensing company is unreasonably high in comparison to its deemed value-add, they reduce the transfer price paid by the German subsidiary, even when the original distortion may be a too low transfer price / license fee from the U.S. to the European principal. In rare cases, German tax authorities have recharacterized transactions when they considered the economic substance of the principal to be inadequate, which, by definition, is a highly subjective finding.
- **On intragroup financing, German tax authorities have regularly challenged interest rates.** Interest rates charged to affiliates by a low-tax financing company are regularly determined to be too high when based on a stand-alone rating benchmark. While this position has successfully been challenged in the Federal Financial Court, the issue remains controversial.

Given this environment, it is not surprising that the number of tax disputes has increased significantly. Most tax audits end up with "horse-trading" deals involving some amount of double taxation, as field tax inspectors have become experts in applying smart "blackmailing" strategies. Taxpayers are incentivized to accept some adjustment in conjunction with a commitment to avoid mutual agreement procedures ("M.A.P."), under threat that the tax authorities will impose much higher tax assessments to achieve more favorable settlements in future M.A.P. negotiations. Still, more than 700 new M.A.P. cases are now initiated in Germany every year, roughly 50% involving transfer pricing. The Federal Tax Office has increased domestic resources for dealing with such requests, so that roughly as many cases get settled as new cases are opened, and the average settlement process time has been brought down to below two years. In parallel, the numbers of A.P.A. requests is increasing, and close to 80 new A.P.A. applications are opened each year.

Regarding tax litigation, the statistics are blurred as many cases are settled before a decision is issued. This often arises when judges assigned to a case indicate to the parties the argument they may tend to favor, pointing out remaining uncertainties,

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especially when it comes to economic quantification in the grey zone of transfer pricing. Judges often recommend an out-of-court settlement in order to reduce their workload and to avoid having to make quantitative decisions for which they have no proper economic expertise. Recent Financial Court decisions primarily related to financial transactions and business restructurings are relatively favorable to the taxpayer, which is fairly good news given that the lower Financial Courts are generally presumed to have a bias in favor of the German tax authorities.

CASE STUDY I: CHALLENGING THE SWISS PRINCIPAL STRUCTURE OF A U.S. CONSUMER PRODUCT GIANT

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The client operates in a highly profitable market segment with captive customers. A specific family of products together with brand campaign attributes were developed in the U.S. many years ago, with clearly U.S.-tailored brand imaging. Around the year 2000, the U.S. headquartered M.N.C. decided to test the promotion of the product in Germany. A subsidiary in Germany ("G-Co") licensed the brand I.P. from a U.S. affiliate ("U.S.-Co") at moderate royalty rates and rolled out a local marketing campaign in line with U.S. guidelines. G-Co was tasked with determining a German-specific go-to-market approach and developing distribution channels. G-Co purchased key product input from the U.S. (invoicing on cost-plus basis) and out sourced finished product manufacturing to third party suppliers operating on its behalf. While investing little in advertising, G-Co grew decently and was highly profitable from the very beginning.

In 2006, U.S.-Co decided to expand European operations and established a European principal structure headquartered in Switzerland. G-Co was converted into a limited risk distributor ("L.R.D.") and as of 2007 only bought finished products from Swiss-Co, a related party, to resell on the German market. Swiss-Co licensed the U.S.-I.P. and became the regional entrepreneur for Europe. The U.S. transfer pricing to Swiss-Co was largely the same as previously in effect with G-Co. As an L.R.D., G-Co now earned a benchmarked operating margin of 3%, which translates into a dramatic margin reduction in contrast to previous years, while sales increased considerably.

In a German tax audit covering the financial years 2007 to 2010, the margin reduction in Germany in conjunction with the introduction of a Swiss principal structure were red flagged by the field tax inspectors. Interestingly, they did not pursue an assessment of a deemed transfer of functions, very likely because they could not identify the transfer of any valuable intangible assets from G-Co to Swiss-Co. Instead, they challenged the taxpayer to demonstrate (i) that a major change of business operations actually occurred and (ii) that Swiss-Co was entitled to earn margins that were previously earned by G-Co.

Amazingly, despite having become the principal for the German market, Swiss-Co was loss-making in the relevant tax audit period. The reason was that, in those years, Swiss-Co invested significant amounts to expand in other European markets, while economic circumstances for the relevant products became less favorable. However, the client management information system of Swiss-Co was not able to provide a proper P&L segmentation demonstrating the segment profits Swiss-Co was making in relation to the German market. The German authorities became

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completely distrustful of the submitted P&L data, and raised a general suspicion that profits had been shifted from Switzerland to some Caribbean island known to host a group subsidiary.

In the view of the tax inspectors, the taxpayer failed to demonstrate a critical amount of substance in Switzerland. For example, G-Co continued to have a direct communication and ordering process with third party manufacturers, even though the manufacturers contracted with Swiss-Co. The tax inspectors came to the conclusion that, in material terms, G-Co had the same functional profile as in its license manufacturer period through 2006. Consequently, they recharacterized the transactions between G-Co and Swiss-Co and treated the latter as an empty shell. Additionally, they rejected benchmark studies justifying G-Co's L.R.D. return as inappropriate because in their view G-Co's marketing activities went beyond those of an L.R.D. In post-B.E.P.S. language, they effectively claimed that G-Co made significant D.E.M.P.E. contributions driving the brand value in Germany.

Challenging the new model from two fundamental factual sides – supervision responsibilities for manufacturing and contribution to marketing intangibles – the field tax inspectors concluded the submitted T.P. documentation was fundamentally flawed. In line with German administrative guidelines, the field inspectors made an independent assessment of arm's length pricing. Referring to the pre-audit years and with a rather ludicrous interpretation of facts and bad economics, they assessed the arm's length return for G-Co to significantly exceed 30% of sales, more than ten times the actual results.

In view of this assessment, a M.A.P. was not an option for the M.N.C., both because (i) the starting position of the German tax inspectors made it almost impossible to expect a reasonable dispute resolution and (ii) Swiss-Co was not profitable in the period even without taking the adjustment into account. The M.N.C. selected a law firm to initiate tax litigation in Germany challenging the assessment. The law firm retained economic T.P. advisors to support the litigation.

The litigation dragged on for approximately three years. An in depth value chain and functional analysis were performed that aligned the economic environment with the factors relevant for the case. Internal documents were identified demonstrating that, notwithstanding limited headcount, (i) the leadership team in Switzerland initiated and pushed business initiatives in Germany, (ii) G-Co was no longer driving the controlling contracting activities with third parties, and (iii) G-Co was not making any D.E.M.P.E. contributions in the field of marketing.

Having substantiated that G-Co was really doing no more than an L.R.D, the M.N.C.'s T.P. advisers corroborated the results of the benchmark studies in the G-Co's T.P. documentation through three complementary sets of technical analysis based on client-specific information. Forensic analysis of the tax authorities audit trail, which was released in the course of the tax litigation, was found to contain factual and analytical errors that demonstrated a bias against the taxpayer.

Based on further financial information dating back up to 15 years, the M.N.C. was able to demonstrate that the loss-making position of Swiss-Co was not related to German business events and that the German market deteriorated during the period under examination. As a result, Swiss residual profit margins from German business

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operations fell dramatically in comparison to earlier years. The economic data demonstrated that the assessment made by German tax authorities was far beyond any reasonable range of objectivity and violated German regulatory guidelines.

In the course of the legal proceedings, tax authorities became ever more defensive, incoherent, and inconsistent in their factual and technical positions. This clearly irritated the investigating judge. Still, the tax authorities did not retreat from their initial assessment. Neither the field tax inspector nor the reviewers were impressed by the empirical evidence produced by the M.N.C. At some point, the court interrupted the proceedings, and in conference, suggested that the factual position of the M.N.C. seemed more likely to prevail than the position of the tax authorities. After eight years of dispute, the assessment was put aside, and a settlement was reached that was consistent with the position of the M.N.C.

To summarize, the taxpayer achieved a positive outcome because, apart from sloppy analysis and neglect of relevant economic factors, the tax authorities stumbled at the burden of proof hurdle in their factual interpretation. Today, however, M.N.C.'s operating in Germany should be aware that, in cases of legitimate doubt, revised German administrative guidelines facilitate acceptance of the positions of the tax authorities. As a result, it is quite likely the tax authorities would have achieved a better outcome in court if the case were to be raised today.

The key takeaway from all this is that, from a cost-benefit perspective, slim and standardized T.P. documentation that fails to address the industrial economic specifics of the underlying transaction parties is not a recommended tax compliance strategy. Indeed, it is doubtful that "canned" T.P. studies that crunch data with no context is not a winning strategy for taxpayers.

CASE STUDY II: GUIDANCE WHEN RELOCATION OF FUNCTIONS LEAD TO PITFALLS

In connection with a relocation of functions that has so far been performed by a German entity, many factors need to be considered in anticipation of a tax examination. Three main drivers for conflicts are (i) the definition of a function, (ii) identifying what was actually transferred and (iii) the determination of the value of the transferred function.

Pitfalls in the determination of the transfer price are well illustrated by an I.P.-centralization case of a U.S. M.N.C. that acquired a company in Germany. As part of acquirer's overall strategy for intellectual property, the M.N.C. held all technology patents in a Dutch entity, except for those related to North American use. The Dutch entity was responsible for the overall steering of R&D activities of subsidiaries. It also monitored potential infringements and undertook steps to protect and enforce I.P. rights. Following the acquisition of G-Co., the M.N.C. arranged for the transfer of the German patents to the Dutch entity and converted the previously independent German R&D activities into contract R&D on behalf of the Dutch entity. Other business activities were not changed, and access to the patents was licensed back to the German entity for a fixed sales-based royalty.

The M.N.C. recognized that this transaction would be considered as a relocation of function and calculated a corresponding compensation for both the patents and the entrepreneurial R&D function. The method applied closely followed the German

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guidelines and was based on a “Delta Approach.” This methodology examines the shifted profit potential by comparing (i) the actually expected profits of the entities following the restructuring to (ii) the hypothetical profits that would have been expected had no restructuring taken place. Both profits were calculated on a yearly basis in perpetuity and discounted to a respective present value for both cases. In this particular case, it was determined that G-Co would have earned profits with a present value of approximately €500 million, whereas after the transaction introduced the license payments and expected contract R&D payments, G-Co would expect reduced profits with a present value of €450 million from its remaining business. Consequently, the purchase price for the transfer of German technology I.P. was set at €50 million, which was paid from the Dutch to the German entity.

The M.N.C. felt relatively confident in the position, as it considered the approach to be in line with German regulations, having recognized and evaluated the transfer of functions. Nonetheless, the M.N.C. expected to be challenged about technical details, in particular the budgets for future years, discount rates, D.E.M.P.E. functions, and the capability of the Dutch entity to exercise effective control over ongoing research and development. Management of G-Co felt it had addressed these reasonably well and that no major reassessment could be made. Then, the tax audit began.

The local German tax authorities looked at the case and rather than challenging any particular technical aspect, they reinterpreted the valuation to imply that the entire business – not just the research and development – was transferred and then partially granted back. In particular, they stipulated that without the technology no other business activities could be carried on and that the German target company became fully dependent on the new licensor, even though the royalty payment actually left substantial profits in Germany. They used the valuation prepared by the taxpayer to imply that the entire business value of €500 million was transferred to the Netherlands. The tax authorities acknowledged that a value of €450 million might have been granted back to the German target company, but asserted that the transfer-back was properly categorized as a nontaxable capital contribution. They therefore increased the purchase price tenfold to €500 million.

From a technical standpoint, it was clear that the original valuation was not intended to imply that a value of €500 million was transferred; this just reflected one element of the “delta,” *i.e.*, an effort to determine the value of the I.P. by looking at the business value with and without the I.P. Nevertheless, giving off this impression might have been avoided had the taxpayer first calculated the difference in profit potential per year and then taken the difference from the present value. Mathematically, the result would have been the same, but it would have helped to avoid the dispute, at least to some degree.

More critical was the following underlying economic question. Was the transfer of the technology I.P. actually a transfer of the entire business, since the other activities, such as manufacturing, distribution, etc., could not work without the patents? Access to the patents had been granted back to G-Co via the license agreement, but the tax authorities stipulated that the Dutch entity could always terminate this agreement, especially since the terms and conditions did, of course, provide termination clauses. In the circumstances, it was decided to approach the issue through a value chain analysis to establish a comprehensive analysis of the entire value creation of the company, rather than limiting the analysis to the role of the technology in isolation.

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As a result, a series of interviews and comparative analyses was undertaken that allowed the main value drivers to be identified, including technology features, production processes, brand awareness, and the like. In a second step, the specific entities that contributed to specific value drivers were identified, and the value contribution of each entity to the respective value driver was computed. The end result was the determination that G-Co entity contributed significantly or exclusively to many of the value drivers that were indispensable to the business. While technology was clearly a critical success factor, it was one factor among many. Rather than a one-directional dependency by one entity on another, the study demonstrated that several entities depended on each other. As an illustration, it was determined that G-Co developed crucial and proprietary production processes, without which the products could not reasonably be produced at competitive prices. From an economic perspective, it was not realistically possible for the Dutch entity to simply terminate the license agreement without losing the entire business.

Ultimately, the comprehensive analysis showed that significant business drivers and associated intangibles had remained in Germany that were never under the effective control of the Dutch entity. Only the technology was transferred. Based on this analysis, the German tax authorities backed down and the original valuation was accepted.

CASE STUDY 3: AVERTING A MULTILATERAL TAX DISPUTE FOR A SWISS BASED GROUP WITH A GERMAN MEMBER

The M.N.C. was headquartered in Switzerland. It was far more profitable than its peer competitors. The largest market was Europe, where the M.N.C. operated a network of four manufacturers. Each specialized in distinct product categories. The manufacturers owned product related I.P. and process related I.P. Each sold directly to sales affiliates of the group.

The group developed a stringent go-to-market policy centered around the corporate brand that was rolled out consistently across European countries. It considered this to be the key differentiator that separated it from competitors, whereas the products as such have no unique selling position ("U.S.P.") that created a competitive edge.

The Swiss headquarters of the M.N.C. licensed the relevant trademarks directly to the sales affiliates. In conjunction, product transfer pricing for intercompany product sales from manufacturers to sales affiliates was coordinated such that the sales affiliates earned an operating margin in line with a Big Four database benchmarking study (2-4%). Consultants at a second Big Four firm determined that the trademark royalty rate of 3% payable by sales affiliates to the Swiss based M.N.C. for licensing the brands was arm's length. The advice was based on the application of a traditional C.U.T. benchmarking analysis.

G-Co operated as a sales affiliate for the German market. In a tax examination covering the 2013 to 2016 period, German tax authorities challenged the intercompany pricing setup and rejected the transfer pricing analysis of the Big Four consultants, contending that it was flawed. The tax authorities determined that the group effectively applied the T.N.M.M. method by setting a royalty rate and product transfer pricing mix that held the German operating margin at 3% of sales. As a matter of

policy, German tax authorities accept the T.N.M.M. as the best method only if the activities of the German taxpayer are purely routine. In comparison, when a distributor operates as licensee, German tax authorities assert that the distributor effectively becomes entrepreneurial and conducts non-routine D.E.M.P.E. functions to promote the trademarks in the German market. The field tax inspectors identified several business operations supporting that view.

Consequently, the tax examiners rejected the T.N.M.M. as inappropriate and the benchmark results as too low given G-Co's value adding functions. Further, they considered that a 3% sales royalty was too high in the B2B context, and found from "experience" that a 1% royalty was more appropriate. Overall, they made an assessment lifting up G-Co's operating margin from 3% of sales to 5%. They were open to the M.N.C. seeking double taxation relief through the M.A.P. process.

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In preparing a M.A.P. strategy, the group tax department was adamant that the trademark royalty of 3% should be upheld under all circumstances, both from a business and financial point of view. If one were to agree to an increase of G-Co's operating margins, a corresponding adjustment should be obtained from the group manufacturers. However, in preparing the M.A.P. submission and holding informal preparatory talks with the German authorities, the group tax department recognized nightmarish challenges. First, it was almost impossible to provide financial information about the profitability of manufacturers with intercompany sales to the German market, as any SG&A allocations of the manufacturers seemed to be arbitrary. Second, it was apparent that some manufacturers were highly profitable, while others were less profitable or loss-making. It became clear that any approach to tax authorities in the countries where manufacturing took place contained a risk that the whole pricing policy could end up being challenged.

The puzzle was solved through the following steps:

- Based on internal management information and external market research, economic data was generated in support of (i) the M./N.C.'s narrative that the go-to-market strategy was indeed centrally developed around the group brand and (ii) the M.N.C.'s view that G-Co purely executes the centrally developed market strategy and provides no self-developed intangible value. Economic data was generated evidencing continuous price premiums that the group generated in Germany in relation to well-known German competitors selling products of similar quality. Those premiums were attributable to brand recognition and good will generated from the range of the product portfolio for which G-Co was not responsible. All this supported the high value contribution from Swiss-Co and the hypothesis that the royalty rate was not excessively high.

- The foregoing conclusions were supported by what-if corroborative economic analysis. Starting with the hypothesis that G-Co was conducting more than routine operations, a contribution-based profit split analysis was performed with Swiss-Co, G-Co, and the manufacturing network as players. Applying the industrial economics concept of Shapley Value, which is well established between unrelated parties in other economic areas of joint value creation, it demonstrated that an arm's length profitability of G-Co would not have exceeded 4% of sales even if a profit split analysis had been conducted based on the factual assessment of the Germany tax authorities.

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When the value chain and profit split analysis was submitted to the German Federal Tax Office to discuss M.A.P. implications, the responsible officer immediately recognized that the whole M.A.P. apart from creating costs would not result in the creation of additional revenue to G-Co and tax to the German fisc. As a result, the responsible officer informally urged the field tax inspectors to negotiate a compromise directly with the M.N.C.

In only one round of negotiation, a favorable outcome was achieved. The Swiss M.N.C. accepted a small adjustment of the operating margin, but below 4% of sales without resorting to a M.A.P. This small downside was offset by the following benefits:

- It achieved an agreement on the taxable income implications for the subsequent tax audit.
- It was spared significant tax compliance costs, tax examination defense costs, and costs related to a tedious M.A.P. process.
- The risk for eight years of potentially significant tax adjustments was taken off the table.

In sum, the exercise demonstrated that tax authorities are open to innovative approaches to economic analysis that help provide a balanced view on joint value creation. To the extent available, it is a much more effective approach than conflict with tax authorities arising from the arbitrary question of whether the operations of a German entity qualify as being routine or entrepreneurial. In a world where there is inevitably a grey zone area around this question, this may help reduce tax disputes in cases where the financial outcome implications are less important, allowing tax authorities to concentrate on high stake - high value cases.

OUTLOOK

The German transfer pricing landscape has a rich history, a controversy-rich presence, and likely a turbulent future. Budgetary pressures are increasing due to investments in security infrastructure, renewable energy investments, and funding ever-increasing pension payments. Simultaneously, many of the foundations of the global free trade agreements that enabled German M.N.C.'s to expand and establish global supply chains are under attack due to looming trade wars and global conflict. On top of this, public pressure to tackle perceived tax-dodging practices are mounting.

One of the challenges in this context is that while German authorities have built up impressive technical capabilities in the past, they have also to a degree become accustomed to a brute-force approach under which aggressive assessments are asserted in the expectation that global corporations will shy away from court proceedings in tax matters. This approach clashes with the realities of the post-B.E.P.S. world, in which taxpayers have terminated highly aggressive structures and have developed an understanding of the importance of transfer pricing documentation that is not canned.

The new reality of forcibly well-prepared taxpayers means that M.N.C.'s are much less likely to a accept a halfhearted horse-trade compromise to settle an aggressive but unjustified audit assessment by aggressive tax authorities. With the backdrop of the B.E.P.S. developments and new regulations, a highly-skilled economic analysis supporting the taxpayer's filing position will become ever more important to achieve dispute resolution in line with taxpayer expectations rather than tax authorities' wishes.

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