
**What are the critical factors when
litigating a transfer pricing case?**

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Why?

Why focus on litigation when very few transfer pricing cases result in a contested appeal?

- Any TP exercise may end up in the FTT
- If it does, everything that has happened matters, every e-mail and every document matters
- Bearing this in mind leads to a particular mindset

'The judge over your shoulder'

- ★ **Civil Service uses a document called 'the Judge Over Your Shoulder'**
- ★ **What is said in darkness shall be heard in light**
- ★ **What you whispered in an ear (or these days put in an e-mail) will be shouted from the rooftops**

The right mindset at the outset

- The parties involved must have a clear understanding of what the TP rules require
- They must understand the concept of an arm's length provision between two independent enterprises
- This understanding must underlie their actions and communications

Anatomy of a TP dispute

- The transaction or structure
- Return
- Inquiry
- Amendment to assessment
- Negotiation
- Acceptance, compromise
- If all else fails, a contested appeal before the FTT

Likely areas of factual dispute

- Unlikely to be any significant dispute about whether provision has been made by a series of transactions or whether the participation condition is met
- A key area will be whether the actual provision differs from what an arm's length provision would have been between two independent enterprises
- Assuming the actual provision confers a potential advantage, how is the calculation made on the basis of the arm's length provision?

Documentary Evidence

- Documentary evidence, subject to legal professional privilege, pretty much all documents are likely to end up in court, including drafts of agreements, e-mails, notes of meetings and calls.
- The documents may be produced by the taxpayer to prove their case, obtained by HMRC under their powers or disclosed under the Tribunal rules or orders
- What narrative emerges from these documents? HMRC will tell one story and the taxpayer another

Witness evidence – witnesses of fact

- Witnesses of fact – these are likely to be those who were involved in arranging the structures or transactions in question, for historical structures dating back years, they may be difficult to obtain
- They will speak to the factual background, the documents and what happened, what negotiations were there, what comparables –if available – were considered, what methodologies of pricing were considered, which one was used and why

Evidence – expert witnesses

- It is almost certain that expert witnesses will be required in the TP field more probably than in any other field of tax dispute
- The role of the expert – not to answer the ultimate questions but rather to provide material to assist the Tribunal
- The best assistance and most persuasive evidence will come from independent experts with no connection to the taxpayer or the dispute

Types of expert witness

- Experts on the business or sector concerned
- They will speak to the factual background, the type of structures that are normally used and the type of transactions that typically occur between two independent enterprises
- Economic experts, they will be used to analyse the pricing structure, money flows and what types of return (for example on capital) are typical within a particular business sector

Choice of experts is crucial

- Given the likely complexity of a transfer pricing dispute in terms of the numbers and methodologies of transfer pricing, the expert must be capable of giving objective, clear and comprehensible evidence
- Tribunals are likely to rely heavily on the expert witnesses they prefer

The essence of the dispute

- Transfer pricing is not an exact science, it requires the exercise of judgment on the part of both the administration and the taxpayer
- Which party has the most compelling narrative in the light of the contemporary documentation, the witness evidence and the expert evidence
- Does the taxpayer's narrative fit within the framework of the transfer pricing methodology?
- Was the transaction arm's length?
- What really happened at the inception of the transaction?

Summary – the crucial factors

- Preparation for a dispute begins at the inception of the transaction
- The parties must have the right mindset and understand what compliance with transfer pricing involves
- It is an area where frontloading is never wasted – get it right at the outset
- Whatever you e-mail will end up in a file or on a screen in court
- How good is your narrative and can it beat HMRC's?
- Will your witnesses of fact still be around when the matter comes to trial?
- Industry/economic experts play a crucial role

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Disclaimer

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Specific specialist advice should be sought in relation to and in the light of the particular facts and circumstances of each case.