# Transfer pricing global reference guide

November 2010


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# Transfer pricing global reference guide

Planning transfer pricing strategies, working to limit tax exposure and defending a company's return position and transfer pricing practices on a global basis require knowledge of a complex web of country tax laws, regulations, rulings, methods and requirements.

The Ernst & Young *Transfer pricing global reference guide* is a tool designed to enable international tax executives to quickly identify the transfer pricing rules, practices and approaches that have been adopted by more than 50 countries and territories. These various approaches must be understood in order to complete both compliance and planning activities.

The guide outlines basic information for the covered jurisdictions regarding their transfer pricing tax laws, regulations and rulings, Organisation for Economic Co-operation and Development (OECD) guidelines treatment, priorities and pricing methods, penalties, the potential for relief from penalties, documentation requirements and deadlines, statute of limitations, required disclosures, audit risk and opportunities for advance pricing agreements (APAs).

A web-based version of this brochure can be found at www.ey.com/transferpricingguide. Please check this web page periodically for late-breaking country developments. Commentaries from transfer pricing professionals are also available at this site.

For a more detailed discussion of any of the country-specific transfer pricing rules, or to obtain further assistance in addressing and resolving intercompany transfer pricing issues, please contact your local Ernst & Young office, the relevant country contact listed at the back of this brochure or send us a query at www.ey.com/transferpricingguide.

Please note the availability of other transfer pricing materials such as survey reports that share views of tax authorities and tax directors (www.ey.com/tp). Ernst & Young also annually produces *The Worldwide Corporate Tax Guide, The Global Executive and the Worldwide VAT, GST and Sales Tax Guide.*

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# Legend

*All rules are current as of November 2010.*

**Taxing authority and tax law:** Name of taxing authority and statutory provisions currently in effect in each country.

**Relevant regulations and rulings:** Current transfer pricing rules and regulatory provisions in effect in each country.

**OECD guidelines treatment:** Consideration given by the taxing authority to the OECD Transfer Pricing Guidelines.

**Priorities/pricing methods:** Transfer pricing methods allowed, as well as the priority of each method.

**Transfer pricing penalties:** Discussion of potentially applicable transfer pricing penalties if a taxpayer is determined not to be in compliance with the rules imposed by the taxing authority.

**Penalty relief:** Potential ways in which penalties may be reduced or avoided.

**Documentation requirements:** Governing tax authority requirements or recommendations that taxpayers prepare and maintain written documentation to confirm that the amounts charged in related-party transactions are consistent with the arm's-length standard.

**Documentation deadlines:** Deadline for preparing transfer pricing documentation.

**Statute of limitations on transfer pricing assessments:** Discussion of the applicable statute of limitations regarding transfer pricing examination and assessments.

**Return disclosures/related-party disclosures:** Information on disclosures required from taxpayers regarding related -party transactions.

**Audit risk/transfer pricing scrutiny:** Discussion of the level of risk of the tax authority scrutinizing related-party transactions. This is based on the past experience of our local tax professionals and is not a forward looking prediction.

**APA opportunity:** Discussion of the possibility of obtaining an advance pricing agreement with the tax authority.


# Glossary of terms

**APA (advance pricing agreement)**
An agreement between a tax authority and an MNE about the determination of the appropriate transfer pricing method to be used for pricing intercompany transactions. APAs may be unilateral, bilateral (two governments) or multilateral (three or more governments).

**Arm's-length principle**
The standard adopted by the OECD that transactions between members of an MNE should reflect conditions that would be made between independent enterprises.

**CFC (controlled foreign corporation)** A subsidiary and member of an MNE group.

**CPM (comparable profits method)**
Under the comparable profits method of US Treasury Regulations Section 1.482-5, an arm's-length result is determined by comparing the operating profit of the "tested" party with the operating profit of an uncontrolled party involved in comparable transactions. Thus, the CPM looks at profits rather than transactions. Generally, the tested party's profit is measured in terms of PLIs such as rate of return on capital employed or the ratio of gross profit to operating expenses. The regulations state that the tested party should normally be the "least complex" of the controlled entities. Treas. Regs. §1.482-5(b)(2).

**CSA (cost-sharing arrangements)**

**CUP (comparable uncontrolled price)**
A transfer pricing method that compares the price for property or services in a controlled transaction with the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances.

**ETR (effective tax rate)**

**EU (European Union)**
The European Union, currently consisting of 27 member states.

**EUJTPF (EU Joint Transfer Pricing Forum)**
The EU Joint Transfer Pricing Forum consists of representatives of governments and the private sector who advise and consult on transfer pricing issues.

**FTE (full-time equivalent)**
Used in this survey to indicate the number of resources employed by tax authorities to undertake transfer pricing reviews in their jurisdiction.

**GAAP (Generally Accepted Accounting Principles)**

**MNE (multinational enterprise)**
A member of a related group that carries on business directly or indirectly in two or more countries.

**MAP (mutual agreement procedure)**
A dispute resolution process found in Article 25 of the OECD Model Tax Convention. MAP is a government-to-government process of negotiation to resolve matters of taxation not in accordance with the particular tax treaty and to attempt to avoid double taxation.

**OECD (Organisation for Economic Co-operation and Development)**
An intergovernmental organization, based in Paris, formed to foster international trade and economic development. The OECD has 30 member states. Among its many concerns are the removal of tax barriers to the free flow of goods and services and the avoidance of double taxation of income or profits. The OECD has developed guidelines and a model tax convention; see below.

**OECD guidelines**
Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, published by the OECD between 1995 and 1998. The OECD guidelines endorse the arm's-length principle and consist of a statement of principles rather than a set of specific rules to be applied.

**OECD Model Tax Convention**
Model Tax Convention on Income and Capital, last published by the OECD in July 2005. The Model Tax Convention is to be used by member states in negotiations of bilateral double tax treaties. The OECD also provides commentary on the interpretation of the Model Tax Convention and states that member countries should follow this commentary, subject to their expressed reservations thereon, when applying and interpreting their double tax treaties.

**MoU (memorandum of understanding)**

**PLI (profit level indicators)**
Ratios that measure the relationship between an entity's profit and the resources invested or costs incurred to achieve that profit. Refer above to CPM for further discussion of their application.

**PATA (Pacific Association of Tax Administrators)**
An association of the tax administrations of Australia, Canada, Japan and the United States formed to foster cooperation and the exchange of information among them. PATA has published guidance on APAs, MAPs and documentation requirements.

**QCSA (qualified cost sharing arrangements)**

**TNMM (transactional net margin method)**
The transactional net margin method is a profits-based method that compares the profitability of an MNE member with the profits of comparable entities undertaking similar transactions. The CPM in the United States is similar to TNMM.


# Argentina

## Taxing authority and tax law

Tax authority: Internal Revenue Service (Administración Federal de Ingresos Públicos, or AFIP))

Tax law: Income Tax Law (ITL) and Regulations

## Relevant regulations and rulings

Regulations currently in effect:

- AFIP-DGI (AFIP-Dirección General Impositiva) Regulation No. 1,122 (Published 31 October 2001, but applicable for fiscal years beginning on 31 December 1999) as amended by several regulations (No. 1,227/02; No. 1,296/02; No. 1,339/02; No. 1,590/03; No. 1,663/04; No. 1,670/04; No. 1,918/05; No. 1,958/05, No. 1,987/05 and External Note No. 1/08)
- Binding tax rulings for general application are not provided
- Opinions from the tax authority are scarce and non-binding

## OECD guidelines treatment

Argentina is not an OECD member, and the OECD Transfer Pricing guidelines are not referenced in Argentina's Tax Law and Regulations. However, the tax authority usually recognizes the OECD Transfer Pricing guidelines in practice as long as they do not contradict the ITL and Regulations.

A first-level court case dated 15 August 2007 was based on the provisions of the OECD Transfer Pricing guidelines. Other more recent first-level court cases also recognized the use of the OECD Transfer Pricing guidelines as long as they do not contradict the ITL and Regulations.

## Priorities/pricing methods

The tested party must be the local entity (i.e., the entity based in Argentina). The taxpayer selects the most appropriate method, but the AFIP may oppose the selection. The accepted methods for transactions with related parties and tax havens pursuant to the ITL are the comparable uncontrolled price (CUP), resale price, cost plus, profit split and transactional net margin methods. The ITL does not prioritize methods. Regulation 1,122/01 states the best method rule.

The use of an interquartile range is mandatory. Unless there is evidence to the contrary, the market price must be used for tangible goods transactions with both related and independent parties where there is an international price in a transparent market.

For transactions involving grains, oleaginous products, other soil products, oil and gas and in general all goods with well-known prices in transparent markets and where the local company operates through international intermediaries that are not the final consignees of the goods, the applicable price is the prevailing price in the respective market on the day loading for shipment is finished, or the agreed-upon price if higher. This method may not apply, however, if the local exporter is able to prove the substance of the operations of the consignee abroad. The AFIP has the power to limit the application of this method or extend it to other transactions under certain circumstances.

Export and import transactions with independent parties not located in tax havens are subject to information requirements if the annual amount of the transaction exceeds ARS1m or the transactions are exports and imports of commodities. The requirements depend on different annual transaction amounts and, in some cases, may include calculations of profit margins.

# Argentina (continued)

## Transfer pricing penalties

For unpaid taxes related to international transactions, the taxpayer is fined 100% to 400% of the unpaid tax. This fine is graduated depending upon the level of compliance with the formal duties related to the control of the taxes derived from international transactions established by the AFIP. Penalties for fraud are 2 to 10 times the unpaid taxes.

Criminal tax law stipulates imprisonment for two to six years if the unpaid tax exceeds ARS100,000 for each tax and fiscal year. If the unpaid tax exceeds ARS1m, the prison term will increase, ranging from three-and-a-half to nine years. For the late filing of tax returns containing international transactions involving the export/import of goods with independent parties, the taxpayer will be fined ARS9,000.

For the late filing of tax returns concerning other international transactions, the taxpayer will be fined ARS20,000. For the application of penalties related to late filing or lack of filing, it is irrelevant whether the transactions were at arm's length. For non-compliance with the formal duties of furnishing information requested by the AFIP, the taxpayer faces fines up to ARS45,000. The same applies to a failure to keep vouchers and evidence of prices on available files and failure to file tax returns upon request. If tax returns are not filed after the third request, and the taxpayer has income amounting to more than ARS10m, the fine is increased from ARS90,000 to ARS450,000. Interest is applicable on unpaid tax balances (from 1 July 2006, the rate is 2% on a monthly basis and 3% upon filing of a lawsuit).

## Penalty relief

Concerning underpayment and fraud, if the non-recidivist taxpayer voluntarily amends the tax returns before receiving a special notice (or vista) from the AFIP, the penalty is reduced to one-third of the minimum fine. If the tax returns are amended within 15 days of receipt of the notice, the penalty is reduced to two-thirds of the minimum fine. If the non-recidivist taxpayer accepts the adjustments assessed by AFIP and pays the amounts due, the penalties are set at the minimum amount. If the taxes due do not exceed ARS1,000 and are paid voluntarily, or within 15 days of the special notice, then no penalty shall be applied.

## Documentation requirements

Transfer pricing regulations require extensive contemporaneous documentation. Taxpayers are required to keep and eventually submit all the documents evidencing that prices, amounts received and profit margins have been established on an arm's-length basis. Furthermore, taxpayers are required to file an annual transfer pricing study for transactions, subject to transfer pricing methods, with related parties, deemed related parties and independent parties located in tax havens.

## Documentation deadlines

The transfer pricing documentation must be ready for filing with the AFIP by the date the corresponding transfer pricing return filings are due. An annual transfer pricing study, financial statements and certification must be filed with the tax authority by the end of the eighth month after the end of the fiscal year.

The annual transfer pricing return must also be filed by the end of the eighth month after the end of the fiscal year. However, the transfer pricing adjustments must be recognized when the income tax return is due (i.e., fifth month after the fiscal year-end). The semiannual returns must be filed by the end of the fifth month after the end of the relevant six-month period. The annual return for export and import transactions with independent parties not located in tax havens must be filed by the end of the seventh month after the end of the fiscal year.

## Statute of limitations on transfer pricing assessments

The general statute of limitations for federal tax matters is 5 years for registered taxpayers or those exempt from registration and 10 years for unregistered taxpayers. These periods begin on 1 January of the year following the year in which the tax return is due. The moratorium regime in place during calendar year 2009 added one year to the statute of limitations period for certain fiscal years. The transfer pricing documentation must be kept by the taxpayer and provided upon AFIP´s request for up to five years after the period established by the statute of limitations.

# Argentina (continued)

## Return disclosures/related-party disclosures

Taxpayers are required to file the following documentation with the AFIP:

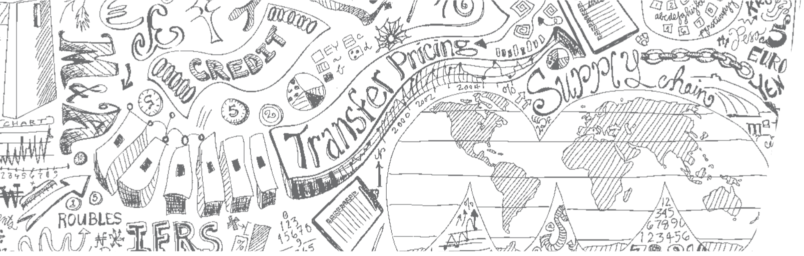
- An annual transfer pricing study
- Audited financial statements for the fiscal year
- An independent Certified Public Accountant's certification of certain contents of the transfer pricing study
- Annual Form 743 return
- Form 742 return (for the first six-month period of each fiscal year)
- Semi-Annual Form 741 return for commodities exports and imports with independent parties not located in tax havens
- Annual Form 867 return for other exports and imports with independent parties not located in tax havens

## Audit risk/transfer pricing scrutiny

Transfer pricing audits are becoming more frequent and intensive, so that a high risk may be assumed. In addition, the first-level court cases are being published. Although the taxpayer position prevailed in most of these cases, the most recent decision was in favor of the tax authority. It is likely that the tax authority will try to increase revenue and strictly enforce penalties with companies that are not complying with transfer pricing requirements.

## APA opportunity

APAs are not specifically addressed.




# Australia

## Taxing authority and tax law

Tax authority: Australian Taxation Office (ATO)

Tax law: Division 13 of Part III of Income Tax Assessment Act and relevant provisions of double tax treaties

## Relevant regulations and rulings

Taxation Ruling (TR) TR92/11: Loans, TR94/14: Application of Division 13, TR95/23: APAs, TR97/20: Methodologies, TR98/11: Documentation, TR98/16: Penalties, TR 1999/1: Services, TR2000/16: Relief from Double Taxation, TR2001/11: Permanent Establishments, TR2001/13: Interpretation of Australia's Double Tax Agreements, TR2002/2: Meaning of Arm's Length for the purposes of § 47A(7) Dividend Deeming Provisions, TR2002/5: Definition of Permanent Establishment, TR2003/1: Arm's Length Debt Test, TR 2004/1: Cost Contribution Arrangements, TR2005/11: Branch Funding for Multinational Banks, TR2007/1: Consequential Adjustments and TR2010/7: Interaction of Transfer Pricing and Thin Capitalization Provisions. TR2010/D2: Transfer Pricing Implications of Business Restructures (issued in draft).

Tax Determinations (TD) TD2002/20: Film Production Companies and the Impact of the Tax Offset Scheme, TD2202/28: Foreign Bank Election to not Apply Part IIIB of the Income Tax Assessment Act (1936), TD2007/1: Market Value of Goodwill of an Entity that becomes a Member of a Consolidated Group. Draft Tax Determinations, TD2007/D20: Interaction of Division 13 and the Thin Capitalization Rules, TD2008/20: Interaction of Division 13 and the Debt/Equity Rules.

ATO Booklets: Concepts and Risk Assessment, Applying the Arm's Length Principle, Advance pricing arrangements, Documentation and Risk Assessment for Small to Medium Businesses, Dependent Agent Permanent Establishments, Marketing Intangibles, Business Restructuring — Discussion Paper on application of Australia's transfer pricing rules, and ATO Discussion Paper on Intra-group finance guarantees and loans — Application of Australia's transfer pricing and thin capitalization rules.

## OECD guidelines treatment

The ATO accepts the principles of the OECD guidelines and indicates in the relevant ATO transfer pricing tax rulings where there are "differences in emphasis or extensions of OECD principles." The ATO will consider the use of all of the OECD-recognized transfer pricing methods and will also consider broader (or other) methods for particular facts and circumstances.

## Priorities/pricing methods

The ATO seeks to adopt the "most appropriate" method. Methods outlined in ATO rulings include traditional transaction methods (CUP, resale price and cost plus) and profit methods (profit split and TNMM). Although traditional transaction methods (e.g., CUP) may be preferred by the ATO, the TNMM is accepted as an appropriate method in circumstances where traditional transaction data is not available, comparable or reliable. Two recent transfer pricing decisions have placed more emphasis on transaction methods and have been critical of the particular applications of the TNMM.

## Transfer pricing penalties

If the Commissioner applies Division 13 and the relevant section of the International Tax Agreement Act, and it is determined that there is a transfer pricing adjustment resulting in a tax shortfall, a penalty of 25% applies, but is reduced to 10% where the taxpayer can demonstrate that it has a reasonably arguable position (RAP).

Where the tax Commissioner can demonstrate that the sole or dominant purpose is tax avoidance, a penalty rate of 50% applies, but is reduced to 25% where the taxpayer can demonstrate that it has a RAP. The taxpayer may have a RAP "if it would be concluded in the circumstances, having regard to relevant authorities, that what is argued for is about as likely to be correct as incorrect or is more likely to be correct than incorrect."

Penalties could increase by a further 20% if the taxpayer "took steps to prevent or obstruct" the ATO from discovering the tax shortfall or if a penalty was imposed for a previous accounting period.

# Australia (continued)

### Transfer pricing penalties (continued)

For 2004-05 and later income years, a Shortfall Interest Charge (SIC) will apply to any amount of tax shortfall from the day on which income tax under the first assessment for that income year was due and payable to the day on which the Commissioner gave notice of an assessment. SIC applies regardless of whether the taxpayer is liable for any shortfall penalty.

### Penalty relief

Penalties will be reduced by 20% for voluntary disclosure after notification of an audit or by 80% for voluntary disclosure before notification of an audit. Where the taxpayer has contemporaneous documentation (i.e., prepared prior to or at the time of filing the company's annual tax return and Schedule 25A) to support a RAP, the penalty may be reduced.

The Commissioner of Taxation has discretionary power to remit penalties where he considers it fair and reasonable to do so. A taxpayer with an APA will not incur penalties except in relation to non-arm's-length dealings that are not covered by the APA or non-compliance with the terms and conditions of the APA.

### Documentation requirements

The ATO has outlined a four-step process in TR98/11 to assist companies in satisfying contemporaneous documentation requirements. This process is not mandatory but is highly recommended. The documentation should:

- Record the transfer price setting process and, in particular, verify the outcome of those transactions against the arm's-length standard
- Include business, economic and industry analyses
- Be relevant to the Australian operations (i.e., country- and company-specific)

In addition, taxpayers are expected to implement a review process to ensure that transactions and outcomes are reviewed at appropriate intervals and to ensure that the impact of material changes in the business is considered and documented.

### Documentation deadlines

Documentation should be contemporaneous with the relevant transactions. Documentation is generally only required to be submitted to the ATO following a specific notification, for example, during an ATO transfer pricing documentation review or audit.

### Statute of limitations on transfer pricing assessments

There is generally no statute of limitations with respect to transfer pricing adjustments. The tax legislation specifically empowers the Commissioner of Taxation to make amendments to tax assessments with respect to any year for transfer pricing adjustments.

Australia and Japan have recently signed a new double tax agreement that provides for a statute of limitations on transfer pricing adjustments. A tax authority must initiate an inquiry into an enterprise's profits within seven years from the end of the taxable year in which the profits at issue might have been expected to have accrued to the enterprise. However, the statute of limitations does not apply in the case of fraud, willful default, or if the inability to initiate the inquiry results from the actions or inaction of the enterprise.

# Australia (continued)

## Return disclosures/related-party disclosures

The ATO requires a Schedule 25A to be filed with each tax return where the aggregate amount of transactions or dealings with international related parties was greater than AU$1m. Information disclosed on the Schedule 25A includes:

- Industry classification code(s)
- Countries with which the taxpayer has international related-party transactions
- International related-party transaction types and quantum
- The percentage of transactions covered by contemporaneous documentation that has been prepared in accordance with the four-step process
- Transfer pricing methodologies selected and applied
- Interests in foreign companies or foreign trusts

The ATO is planning to introduce the International dealings schedule in 2010, which requires an increased level of disclosure in respect of international related party transactions and financing transactions. The International dealings schedule will replace the Schedule 25A and thin capitalization schedule.

## Audit risk/transfer pricing scrutiny

In determining whether an Australian taxpayer's transfer pricing should be reviewed or audited by the ATO, the ATO generally gives consideration to the size and nature of the related-party dealings, the quality of any transfer pricing documentation and whether or not the taxpayer's results appear to be commercially realistic. The ATO has developed a sophisticated risk engine which takes these factors, along with a number of other financial and industry data, into consideration in determining which taxpayers to review. Related-party transactions undertaken in connection with the following may receive particular attention by the ATO:

- Royalties
- Intangibles (both Australian and foreign-owned)
- Management services
- Financing arrangements, including interest-free loans, interest-bearing loans and guarantee fees
- Companies undergoing supply chain restructurings
- Transactions with recognised tax haven jurisdictions

The ATO also focuses on taxpayers whose overall operations do not achieve a commercially realistic result (e.g., incur losses or low returns in any particular year or over a range of years). Additionally, the ATO has been focusing on the arm's length nature of business restructures.

The ATO concentrates on a range of industries each year, including mining, energy and utilities, motor vehicles, pharmaceuticals, distributors, banking and insurance. The ATO continues to conduct transfer pricing reviews (documentation reviews) and transfer pricing audits. These reviews and audits target small and medium-sized enterprises as well as large enterprises.

The risk of transfer pricing audit in Australia would be assessed as medium/high as the ATO continues to perform transfer pricing audits and make transfer pricing adjustments.

## APA opportunity

The ATO actively promotes the use of APAs and has a well-established program for both unilateral and bilateral APAs. Circumstances that the ATO has indicated may be unsuitable for an APA include those where:

- Timely agreement is unlikely to be reached with respect to the methodology, comparable data and overall arm's length outcome
- There is a lack of materiality in the dealings in the context of the business
- There is insufficient complexity to warrant the level of certainty that is provided by an APA

or

- Obtaining a tax benefit in Australia or overseas was a principal element of the dealings


# Austria

## Taxing authority and tax law

Tax authority: Ministry of Finance (MF)

Tax law:

- Section 6(6) Income Tax Act
- Section 8(2) Corporate Income Tax Act
- Sections 124, 131 and 138 Federal Tax Code
- Section 118 Federal Tax Code regarding unilateral APAs

## Relevant regulations and rulings

- Transfer Pricing Guidelines 2010 (BMF-010221/2522-IV/4/2010, 28 October 2010)
- Income Tax Guidelines 6.13.3, 2511-2513
- Corporate Income Tax Guidelines 14.8.2, 1147
- Ministerial decrees AÖF Nos. 114/1996, 122/1997, 155/1998, and 171/2000
- Several opinions published by the MF regarding selected transfer pricing issues

## OECD guidelines treatment

As an OECD member country, Austria has fully adopted the OECD Transfer Pricing Guidelines by publishing them in the form of several ministerial decrees. According to the recently released Austrian Transfer Pricing Guidelines 2010 the arm's length principle contained in income tax law has to be construed in line with the OECD Transfer Pricing Guidelines and any updates thereto.

In addition to the OECD Transfer Pricing Guidelines, the tax authorities also observe the OECD Report on the Attribution of Profits to Permanent Establishments (AOA), although the AOA is currently not fully applicable as none of Austria's current double tax treaties already includes the new Article 7.

The Austrian Transfer Pricing Guidelines 2010 have also been released in the form of a ministerial decree. They are binding for the Austrian tax authorities, but are not binding for Austrian courts or the taxpayers.

## Priorities/pricing methods

Based on the OECD Transfer Pricing Guidelines and the Austrian Transfer Pricing Guidelines 2010, the MF accepts CUP, Resale Minus, Cost Plus, TNMM and Profit Split. The MF follows the replacement of the hierarchy of transfer pricing methods according to the latest update of chapters I to III of the OECD Transfer Pricing Guidelines, and in particular the TNMM and the Profit Split method are no longer considered methods of last resort. According to the Austrian Transfer Pricing Guidelines 2010 the method that provides the highest degree of certainty for the determination of an arm's length transfer price has to be selected.

## Transfer pricing penalties

There are no specific transfer pricing penalties. If the taxable income is increased because the arm's length criterion has not been met, non-deductible late payment interest in the amount of 2% points above the base rate (published by the European Central Bank) is levied on any additional prior year's corporate income tax payments for a maximum period of 48 months. Lacking or insufficient transfer pricing documentation does not lead to specific penalties, but increases the risk that the tax authorities will regard a transaction as non-compliant with the arm's length criterion, and thus assess a transfer pricing adjustment based on an estimate.

# Austria (continued)

## Penalty relief

If the taxpayer provides formerly lacking or insufficient documentation to the tax authorities, the tax authorities are obliged to base their consideration upon such documentation. However, late payment interest will become due on any additional prior year's corporate income tax payments regardless of whether there is sufficient documentation or not.

## Documentation requirements

The Austrian Transfer Pricing Guidelines 2010 state that there is an obligation to prepare transfer pricing documentation based on the Federal Fiscal Code's general provisions concerning bookkeeping, record-keeping and the disclosure requirement for tax purposes. Regarding content and scope, documentation must be in line with the documentation requirements according to the OECD Transfer Pricing Guidelines (in particular according to Chapters V and VIII). It is also permissible to prepare documentation that follows the Code of Conduct on transfer pricing documentation for associated enterprises in the European Union (EU).

## Documentation deadlines

Documentation should be prepared contemporaneously and must be provided to the tax authorities upon request (which is usually during a tax audit). Usually the competent tax auditor will determine a submission deadline, which can vary from case to case (e.g., from only one week to several weeks). Upon the tax auditor's consent, an extension of the deadline is possible. Given the recent release of the Austrian Transfer Pricing Guidelines 2010 and the included requirement to prepare transfer pricing documentation, short submission deadlines will be likely in the future.

## Statute of limitations on transfer pricing assessments

The statute of limitations on a transfer pricing adjustment usually is six years after the end of the calendar year in which the relevant fiscal year ends. The term may be extended up to 10 years.

## Return disclosures/related-party disclosures

No specific continuous disclosure is required in the annual tax return. In case of a tax audit, the auditors usually ask for a description of major related-party transactions as well as for disclosure of all contracts in place with related parties and transfer pricing studies available. In an increasing number of cases, an extensive transfer pricing questionnaire is discussed.

## Audit risk/transfer pricing scrutiny

Tax authorities regularly examine related-party transactions and transfer prices charged. There is a noticeable trend towards increased awareness of transfer pricing problems among tax auditors. Given the recent release of the Austrian Transfer Pricing Guidelines 2010, the transfer pricing audit risk can be considered high.

## APA opportunity

Based on a new law, effective as of 1 January 2011, it will be possible to apply for a unilateral, binding, appealable advance ruling issued by the competent tax office on the tax treatment of a particular (but yet-to-occur) transfer pricing issue. The fee for such a unilateral APA amounts up to EUR 20,000.

In addition, it is possible to obtain a unilateral ruling from the competent tax office on transfer pricing questions which is only binding for the tax authorities to a limited extent and cannot be appealed against.

Finally, under specific circumstances it should be possible to ask the Austrian tax authorities to participate in negotiations of a bilateral APA on the basis of Article 25(3) of the respective double tax treaty.


# Belgium

## Taxing authority and tax law

The taxing authority responsible for transfer pricing in Belgium is the Belgian Administration of Direct Taxes, which is part of the Federal Public Service Finance. While transfer pricing issues can be raised in the course of an ordinary tax audit, a specific transfer pricing audit team has been created within the Belgian Tax Authority. This highly specialized team, which has nation-wide authority, operates autonomously and selects its audit targets, but also provides support to other field inspectors if requested.

While no specific transfer pricing legislation exists in Belgium, the arm's length principle was formally introduced into the Belgian tax law by the law of 21 June 2004, introducing Article 185, §2 of the Belgian Income Tax Code (ITC) (entered into force on 19 July 2004). This article's content is equivalent to Article 9, §§1 and 2 of the OECD Model Tax Convention.

In addition, the ITC contains various provisions which directly or indirectly relate to transfer pricing. These provisions can be found in Articles 26, 49, 54, 55, 79, 207, 344 and 345 of the Belgian ITC. These articles deal with the notion of abnormal and gratuitous benefits (indirectly embodying the arm's length principle), the deductibility of expenses and avoidance of the shifting of profits.

The general provisions of the Belgian ITC, e.g., regarding penalties, late interest payments, etc., also apply in transfer pricing matters.

A general advance ruling (or APA) regime was introduced through the law of 24 December 2002 and became effective as of 1 January 2003.

The Royal Decree of 10 August 2009, obliges Belgian companies to provide in their statutory annual accounts certain additional information linked to transfer pricing in the notes/annexes of their annual accounts

The Budget Law of 23 December 2009 introduced a new reporting obligation (Article 307, §1, s. 3 ITC) and a related tax deduction denial for unreported or payments lacking underlying bona fide business purposes (new Article 198, 10° ITC). Many important practical aspects still need to be detailed and illustrated by the Belgian tax authority by means of Administrative Guidelines, but the main characteristics of the new requirements, can be summarized as follows.

For reference, this reporting obligation applies as from tax year 2010 for payments made as from 1 January 2010 onwards made directly or indirectly to persons established in tax havens by resident or non-resident entities (Belgian permanent establishments) liable to Belgian corporate income tax, other than privately owned business, totaling more than EUR 100,000 per taxable period.

Tax havens have been defined with reference to the 'black list' determined by the Royal Decree dated 6 May 2010 published in the Belgian Official Gazette of 12 May 2010; it currently contains 30 jurisdictions that either do not levy corporate income tax or where the nominal corporate income tax rate is lower than 10% (e.g., Cayman Islands, the Channel Islands, the United Arab Emirates, Monaco, Moldavia, etc.). Whether or not the OECD 'grey-listed' jurisdictions are also to be taken into account is still unclear.

A Royal Decree dated 7 May 2010 determining the model form (n° 275 F) for reporting direct or indirect payments to persons established in tax havens has been published in the Belgian Official Gazette of 25 May 2010. This new reporting obligation is Irrespective of the forms to be filed according to Article 57 ITC ('secret commissions').

Failure to report is sanctioned by non-deductibility of expenses relating to such payments. In addition, expenses relating to reported payments will nonetheless only be deductible upon proof by the Belgian payer that these payments relate to actual and bona fide at arm's length transactions and with persons other than artificial constructions.

# Belgium (continued)

## Relevant regulations and rulings

The tax administration has issued various guidelines on transfer pricing:

- Administrative guidelines on the offensive aspects of transfer pricing, issued in 1999
- Administrative guidelines on the defensive aspects of transfer pricing, issued in 2000 and 2003
- Administrative guidelines providing the tax authority's view on the interpretation of Article 185, §2 ITC, which introduced the arm's length principle into Belgian tax law, issued in July 2006
- Administrative guidelines regarding the formal creation of a transfer pricing audit team within the tax authority, issued in July 2006Administrative guidelines on transfer pricing documentation, the transfer pricing code of conduct and transfer pricing audits, issued in November 2006

Rulings are provided on the basis of a general ruling practice (see APA opportunity, below). APAs are provided on an individual basis, taking into account the specifics of each case. The Belgian government has furthermore implemented a regime which provides, for tax purposes, a deduction on risk capital (i.e., qualifying equity), also known as a Notional Interest Deduction.

In addition, the government also introduced a special tax deduction for income derived from the use of patents. As a result of this deduction, income that is patent-related is subject to an effective tax rate of 6.8% or less.

## OECD guidelines treatment

The tax authority indicates several times in its administrative guidelines that taxpayers should generally follow the guidance mentioned in the OECD Transfer Pricing Guidelines.

## Priorities/pricing methods

Although taxpayers are in principle free to choose any OECD transfer pricing method as long as the method chosen results in arm's length pricing for the transaction, conceptually, transaction-based methods are preferred over profit-based methods.

Taxpayers are not required to use more than one method, although they should be able to support their decision to apply a particular method.

## Transfer pricing penalties

The general tax penalty framework applies to transfer pricing adjustments. These penalties vary from 10% up to (in very exceptional cases) 200% of the additional tax; the rate depends on the degree of intent to avoid tax or the degree of the company's gross negligence.

Furthermore, interest for late payments is due on additional tax assessments (including assessments resulting from a transfer pricing adjustment).

## Penalty relief

Since additional tax assessments depend on the degree of intent to avoid taxes or on the company's gross negligence, penalties can be reduced or eliminated if the taxpayer can demonstrate its intent to establish transfer prices in accordance with the arm's length principle (e.g., through its documentation efforts).

# Belgium (continued)

## Documentation requirements

No legislative guidance regarding the nature and content of proper transfer pricing documentation exists. However, the 1999 administrative guidelines state that documentation should demonstrate that the taxpayer's pricing complies with the arm's length principle to avoid an in-depth transfer pricing audit. These 1999 guidelines recommend that documentation include, at a minimum:

- Activities of the group (including competitive position, level of market, economic circumstances, business strategies, etc.)
- Identification and characterization of intercompany transactions and contractual relationships among affiliates
- Functional analysis (including an overview of the functions, risks and intangibles)
- Transfer pricing methods used=Economic analysis

The 2006 administrative guidelines on transfer pricing confirm Belgium's agreement with the principles outlined in the EU Code of Conduct. Therefore, the information expectation contained in this Code of Conduct should also be considered from a Belgian transfer pricing documentation perspective. These administrative guidelines also refer to the concept of a prudent business manager in order to encourage companies to ensure that transfer pricing documentation is available.

Although the burden of proof lies with the tax authority, the taxpayer needs to provide information on its transfer pricing policies applied to allow the tax authority to verify the company's tax position.

## Documentation deadlines

Given the absence of any formal transfer pricing documentation requirements, there is no statutory deadline for the preparation of transfer pricing documentation. However, upon a tax audit, a taxpayer has a one-month period to provide all information requested (including all information that allows verification of its taxable income and thus, the arm's length nature of the transfer prices), it is recommended that each transaction be documented at the time it is executed. This one month-period can be prolonged if valid reasons exist.

Additionally, the 1999 guidelines provide that if the taxpayer can demonstrate upon a tax audit that it has made sufficient efforts to prepare transfer pricing documentation, the tax inspector does not need to carry out an in-depth tax audit.

## Statute of limitations on transfer pricing assessments

The general rules regarding the statute of limitations apply to transfer pricing assessments. Therefore, generally speaking, the tax authority is entitled to make additional assessments during a period of three years starting from the closing of the accounting year.

However, in the case of fraud, the tax authority has the right to adjust the income during a five-year period, provided that the taxpayer receives prior notice of serious indications of fraud. In case of tax losses, the statutes of limitations do not run until these tax losses are effectively used to offset taxable income. Some other, exceptional statutes of limitations also exist for specific situations.

## Return disclosures/related-party disclosures

No specific disclosure requirements exist for filing the tax return. However, the accounting rules introduced through the Royal Decree of 10 August 2009 oblige companies to provide in their statutory annual accounts in Belgium certain additional information linked to transfer pricing in the notes/annexes of their annual accounts:

- Companies must provide information as regards the nature and business purpose of their relevant off-balance sheet arrangements, if underlying risks and benefits are considered material and when the disclosure is necessary to assess the financial position of the company correctly (e.g., intra-group guarantees, pledges, factoring liabilities; and especially relations with special-purpose entities, whether transparent or not, and offshore entities).

# Belgium (continued)

## Return disclosures/related-party disclosures (continued)

- Companies must disclose their material transactions with affiliated parties that can be considered as not at arm's length. Depending on the type of company a different scope of information is to be provided, ranging from a mere listing of such transactions to the mentioning of the amounts involved as well as all other information necessary to provide a correct view of the financial position of the company.

While this new rule is as such not included in the Belgian tax code, it creates an obligation for the relevant entities to review (and document) the arm's length nature of their intercompany transactions. Non-compliance may potentially result in, amongst others, director liability. In addition, any such information disclosed will provide an excellent source of information for a tax inspector to initiate a (targeted) transfer pricing audit.

## Audit risk/transfer pricing scrutiny

The transfer pricing audit risk may be regarded as medium-high.

The tax authority has demonstrated an increased interest in transfer pricing since the first circular letter on transfer pricing, introduced in 1999. Thereafter, the introduction of the arm's length principle in the Belgian legislation in 2004 and the organization of a special transfer pricing team in 2006 increased the focus on transfer pricing. This transfer pricing audit team is expected to be informed of every transfer pricing investigation performed by the local tax audit teams to ensure a consistent and experienced approach.

The transfer pricing audit team is also involved in cross-border transfer pricing audits (e.g., in case of a restructuring), which are held jointly with the tax authorities of neighboring countries. In addition to this special team's increased audit activity, field tax inspectors are also increasing their focus on transfer pricing during general tax audits.

The 2006 administrative guidelines contain a list of events that could trigger a high transfer pricing risk and lead to increased audit scrutiny:

- Structural losses
- Business reorganizations
- Migration of businesses
- The use of tax havens or low-tax rate countries
- Back-to-back operations
- Circular structures
- Invoices for services sent at the end of the year (i.e. management services)

The tax authority indicated in its November 2006 circular that transfer pricing cases associated with business restructurings will be among the priorities in their audit efforts.

These developments will further increase the focus on transfer pricing, especially considering the evolution of the Belgian transfer pricing audit relationship with other tax authorities. Transfer pricing audits have become more aggressive. They are being approached from an economic perspective and are focused on such specific issues as business conversions and restructurings.

In our experience with the Belgian tax authority, the recent developments will result in more focus on transfer pricing, especially considering the evolution that the Belgian transfer pricing audit cell is working closely together with other tax authorities.

## APA opportunity

The 2003 corporate tax reform introduced a general ruling practice under Belgian tax law. Additional guidance in this respect is provided through various Royal Decrees.

As a result of the law of 21 June 2004, the Service for Advance Decisions became an autonomous department as of 1 January 2005. More than 100 specialists in various domains of taxation, including transfer pricing, assist the committee. This service has increased flexibility in the ruling process and shortened the decision period (usually less than three months from the filing date for unilateral APAs). This committee is also able to rule prospectively on corresponding downward profit adjustments under Article 185, §2, thus offering significant transfer pricing planning opportunities.


# Brazil

## Taxing authority and tax law

Tax authority: Brazilian Internal Revenue Service (IRS)

Tax law: Internal Revenue Code by Decreto 3000, 26 March 1999 (RIR99)

## Relevant regulations and rulings

- Ordinance No. 222/08 provides guidance with respect to requests for changing statutory profit margins
- Normative Instruction No. 243, promulgated 11 November 2002, changed application of Resale Minus 60%
- Law No. 9.959, enacted 27 January 2000, introduced the Resale Minus 60% method (applicable for raw materials)
- Law No. 9.430, enacted 27 December 1996, introduced transfer pricing rules in Brazil

Coefficients to compensate exports for Brazilian currency appreciation:

- 2009 coefficient: 1.00 (Normative Instruction No. 1010/10)
- 2008 coefficient: 1.20 (Normative Instruction No. 898/08 and Ordinance No. 310/08)
- 2007 coefficient: 1.28 (Normative Instruction No. 801/07 and Ordinance No. 329/07)
- 2006 coefficient: 1.29 (Normative Instruction No. 703/06 and Ordinance No. 425/06)
- 2005 coefficient: 1.35 (Normative Instruction No. 602/05 and Ordinance No. 436/05)

## OECD guidelines treatment

Brazil's transfer pricing rules deviate significantly from international standards (including the OECD guidelines) in that there are no profit-based methods. Intercompany transactions need to be documented on a strict transactional basis, and fixed statutory profit margins (generally not arm's length) apply. No functional or industry analyses are required. Instead, the local subsidiary will have to document for each imported (or exported) product or service that it complies with at least one of Brazil's statutory transactional methodologies (CUP, Resale Minus or Cost Plus).

## Priorities/pricing methods

As a first step in the transfer pricing documentation process, Brazilian companies have applied the Brazilian Resale Price less Profit Method (Método do Preço de Revenda menos Lucro or "PRL") to document a company's transfer prices. Brazilian companies have started the documentation process with the PRL because the method relies entirely on import cost, local production cost and resale price information available internally, relieving the company of the burden of soliciting data from its foreign-related suppliers. In addition, since the PRL is the method favored by the Brazilian tax authority in the case of an audit, this approach provides a reliable estimate of Brazil's potential transfer pricing exposure.

## Transfer pricing penalties

Since there are no special penalties for transfer pricing, general tax penalties are applicable. The amount of the penalty may be up to 20% of the omitted tax (or 0.33% per day) if the taxpayer pays the related taxes late but before an audit. Meanwhile, if the tax authority assesses the taxpayer as part of a transfer pricing audit, the applicable penalties may range from 75% to 225% of the omitted taxes.

## Penalty relief

Currently no penalty relief is available.

# Brazil (continued)

## Documentation requirements

Brazilian taxpayers are required to document their international intercompany transactions on an annual basis. The Brazilian annual tax declaration (DIPJ) contains five specific forms that require taxpayers to disclose detailed information regarding their main intercompany import and export transactions. As part of these contemporaneous documentation requirements, taxpayers need to disclose the total transaction values for the most traded products, services or rights, the names and locations of the related trading partners, the methodology used to test each transaction, the calculated benchmark price, the average annual transfer price and the amount of any resulting adjustment.

Given the detailed transactional focus of the Brazilian regulations and the absence of any basket approach, taxpayers are required to document their transfer prices on a product code by product code basis, service type by service type and right by right. In this context, product code refers to a company's internal product codes used for inventory management purposes and not the much broader fiscal nomenclature used for customs and indirect tax purposes.

Taxpayers are expected to have the calculations and documentation necessary to support the information filed as part of the annual tax declaration ready for potential inspection by the tax authority as of the declaration's filing date (i.e., usually the end of June of the ensuing calendar year).

## Documentation deadlines

The contemporaneous documentation required as part of the DIPJ usually has to be filed by the end of June of the following fiscal year. Taxpayers are expected to have the detailed calculations and documentation necessary to support the information filed as part of the DIPJ ready for potential inspection as of the declaration's filing date.

## Statute of limitations on transfer pricing assessments

A general statute of limitations applies, which is five years from the first day of the following fiscal year.

## Return disclosures/related-party disclosures

The transfer pricing adjustments must be effected in December and reflected in the annual income tax return (usually due June of the next year), when the company will also have to disclose the transfer pricing methods chosen and any related information.

## Audit risk/transfer pricing scrutiny

In an effort to expedite audits in Brazil's data-intensive transfer pricing documentation environment, Brazilian audit teams have been equipped with new computers and specialized software applications, including internally developed systems capable of analyzing and auditing large volumes of accounting and transaction data.

The Brazilian tax authority expects the International Affairs Special Office (DEAIN) and the regional audit groups to continue to increase their numbers of specialized transfer pricing auditors. It is believed that the DEAIN and the regional transfer pricing auditors are becoming increasingly sophisticated in their audit approaches as they grow in number and experience.

There is a growing concern that many transfer pricing auditors, because of their particular training and tools, tend to rely on mechanical approaches to audits, while they ignore, or are unaware, of possible underlying business economics. While efforts are being made to increase auditors' knowledge of economics, it is expected that this approach to auditing will continue for the next few years.

## APA opportunity

APAs are not specifically addressed.


# Canada

## Taxing authority and tax law

Tax authority: The Canada Revenue Agency (CRA) is responsible for ensuring that taxpayers meet the requirements of the law.

Tax law: Section 247 of the Income Tax Act (Canada) (ITA) received Royal Assent on 18 June 1998 and became generally applicable to taxation years that began after 1997. It constitutes Canada's transfer pricing legislation and deals with the determination of transfer pricing adjustments, the re-characterization of transactions, penalties, records/documents required to be made or obtained, contemporaneous documentation requirements and the timing of their provision to the Minister when requested, as well as ministerial discretion regarding acceptance of downward adjustment requests.

## Relevant regulations and rulings

The CRA does not set out its views and positions on transfer pricing issues by legal doctrine or in a detailed fashion or examples. The CRA prefers to outline its views in general principles.

It provides its administrative interpretations and guidance with respect to §247 and its application through the release of Information Circulars (IC), Transfer Pricing Memoranda (TPM) and pronouncements at public conferences, symposia and conventions. ICs usually address major subjects from a general perspective, while TPMs typically provide supplementary detailed explanations and guidance on specific issues related to the major subject.

CRA's current key pronouncements on transfer pricing are:

- IC87-2R, International Transfer Pricing, 27 September 1999
- IC94-4R, International Transfer Pricing: Advance Pricing Arrangements (APAs), 16 March 2001
- IC94-4R (Special Release), Advance Pricing Arrangements for Small Businesses, 18 March 2005
- IC71-17R5, Guidance on Competent Authority Assistance Under Canada's Tax Conventions, 1 January 2005

The CRA issued TPM 12 on 12 December 2008, providing formal guidance regarding the Accelerated Competent Authority Procedure (ACAP). Taxpayers may request assistance for subsequent assessed (but unaudited) taxation years on the same issues included in a mutual agreement procedure (MAP) process. The main objective of the ACAP is to streamline certain steps in the MAP process, such as being able to simultaneously negotiate with the foreign competent authority for both MAP and ACAP years.

Additional information and guidance on transfer pricing-related matters can be obtained from the CRA's website (www.cra-arc.gc.ca/tx/nnrsdnts/cmmn/trns/menu-eng.html)

## OECD guidelines treatment

While no mention is made of the OECD guidelines in §247 of the ITA, the legislative provision is intended to reflect the arm's-length principle as set out in the OECD guidelines. The CRA has also endeavored to harmonize its administrative guidance and approach to transfer pricing with the OECD guidelines. As noted in IC 87-2R, the "circular sets out the Department's views on transfer pricing and also provides the Department's position with respect to the application of the OECD guidelines."

When dealing with transfer pricing issues domestically, reliance is placed on the relevant Canadian statutory provisions. The CRA's related ICs and other administrative guidance are considered instructive but not definitive. Moreover, the OECD guidelines and other OECD reports are not usually recognized as authoritative; however, courts and other dispute resolution channels (e.g., competent authority) may consider the international principles and standards established by the OECD in reaching a decision.

# Canada (continued)

## Priorities/pricing methods

The CRA accepts the transfer pricing methods recommended in the OECD guidelines when such methods are applied correctly and result in an arm's length price or allocation. These transfer pricing methods specified in IC 87-2 include

- CUP method
- Resale Price method
- Cost Plus method
- Profit Split method (residual/contribution)
- TNMM

However, the CRA considers the use of the Profit Split method as a method of last resort.

Traditionally, the CRA considered that, notwithstanding that §247 does not so stipulate, there is a natural hierarchy in the application of the above-noted transfer pricing methods, with the CUP method providing the most reliable indication of an arm's length transfer price or allocation and the Profit Split method providing the least reliable indication of an arm's length result. Traditionally the CRA did not require or impose a "best method" rule. The CRA believes that the most appropriate method to be used in any situation will be that which provides the highest degree of comparability between transactions, following an analysis of the hierarchy of methods. The Tax Court of Canada, in the 2008 Glaxo case, has embraced the hierarchy of methods as outlined in the 1995 OECD Guidelines.

Following the 2010 revisions to the OECD guidelines, which CRA has endorsed, it is understood that the CRA will be updating its published guidance to reflect the revisions, moving away from its position on a natural hierarchy. Timing for these updates remains uncertain.

## Transfer pricing penalties

Subsection 247(3) of the ITA causes a taxpayer to be liable for a penalty of 10% of the net upward transfer pricing adjustments made under subsection 247(2) of the ITA, if such adjustments exceed the lesser of 10% of the taxpayer's gross revenue for the year and CA$ 5m, and if the taxpayer has not made reasonable efforts to determine and use arm's length transfer prices.

A taxpayer will be deemed not to have made reasonable efforts to determine and use arm's length transfer prices or allocations unless the taxpayer has prepared or obtained records or documents that provide a description that is complete and accurate in all material respects of the items listed in subsection 247(4) of the ITA, and such documentation is in existence as of the tax filing due date. In the case of corporate entities, such documentation must exist six months after the year-end. For partnerships, the due date is five months after the year-end. Further, a taxpayer will be deemed not to have made reasonable efforts to determine and use arm's length transfer prices or allocations if the taxpayer does not provide the records or documents to the CRA within three months of the issuance of a written request to do so.

Transfer pricing related penalties are exacted without reference to the taxpayer's income or loss for the relevant reporting year and are not tax deductible.

## Penalty relief

If a taxpayer is considered to have made reasonable efforts to determine and use arm's length transfer prices or allocations with respect to adjusted non-arm's length transactions, no penalty would be applicable to such adjustments.

As set out in by TPM-07, all proposed reassessments involving transfer pricing penalties are required to be referred to the Transfer Pricing Review Committee (TPRC) for review and recommendation for final action. The TPRC, after consideration of the facts and circumstances and representations by the relevant taxpayer, will conclude whether or not a transfer pricing penalty is justified.

No transfer pricing adjustments under subsection 247(2) of the ITA should arise regarding transactions covered by an APA as long as the APA remains in effect and the taxpayer complies with its terms and conditions.

When the CRA has reassessed a transfer pricing penalty and the Canadian competent authority and relevant foreign counterpart negotiate a change to the amount of the transfer pricing adjustment, the CRA will adjust the amount of the Canadian transfer pricing penalty accordingly. If the result of the change is that the adjustment no longer exceeds the penalty threshold, the penalty would be rescinded.

# Canada (continued)

## Documentation requirements

Subsection 247(4) of the ITA requires that a taxpayer must have records or documents, as a minimum, that provide a complete and accurate description, in all material respects, of the following items:

- The property or services to which the transaction relates
- The terms and conditions of the transaction and their relationship, if any, to the terms and conditions of each other transaction entered into between the persons or partnerships involved in the transaction
- The identity of the persons or partnerships involved in the transaction, and their relationship at the time the transaction was entered into
- The functions performed, the property used or contributed and the risks assumed by the persons or partnerships involved in the transaction
- The data and methods considered and the analysis performed to determine the transfer prices, the allocations of profits or losses, or contributions to costs for the transaction
- The assumptions, strategies and policies, if any, that influenced the determination of the transfer prices, the allocations of profits or losses, or contributions to costs for the transaction

In addition, although its views are not law, the CRA indicates in IC 87-2R that it expects a taxpayer's documentation to include certain additional information (e.g., details of cost contribution arrangements, translations of foreign documents and other general guidance).

The CRA issued TPM 09 on 18 September 2006. The purpose of this memo was to define the meaning of "reasonable efforts" under §247 of the Act. In practice, TPM 09 has not significantly enhanced clarity with respect to the reasonable efforts standard and, thereby, the potential application of transfer pricing penalties.

## Documentation deadlines

Taxpayers must prepare or obtain records and documents that provide a description that is complete and accurate in all material respects of the items listed in subsection 247(4) of the ITA, and such documentation must be in existence as of the tax filing due date. In the case of corporate entities, such documentation must exist six months after the year-end. For partnerships, the due date is five months after the year-end.

Taxpayers must provide documentation to the CRA within three months of the issuance of a written request.

## Statute of limitations on transfer pricing assessments

Under subsection 152(4) of the ITA, the Minister may not ordinarily reassess after the normal reassessment period as defined in subsection 152(3.1) of the ITA. For most multinational taxpayers, that period is four years beginning after the earlier of the day of mailing a notice of an original assessment for the year and the mailing of an original notification that no tax is payable for the year. The time limit applies unless the taxpayer has made misrepresentations, committed a fraud or filed a waiver, in which case the Minister may reassess a taxpayer at any time. Where a Notice of Reassessment is issued at a later date, the first assessment notice is still viewed as the original assessment for the purposes of determining the normal reassessment period under subsection 152(3.1) of the ITA. With respect to transactions involving non-arm's length dealings with non-residents, the reassessment period is extended an additional three years to seven years. This time period may be further extended if the taxpayer provides the CRA with a waiver (i.e., authorization by the taxpayer to the CRA to waive the normal reassessment period). As of March 2009 a waiver may be provided by the taxpayer within the seven - year extended reassessment period. Previously, waivers were only allowed to be filed within the four - year normal reassessment period.

## Return disclosures/related-party disclosures

Taxpayers are required to file a T106 information return annually, reporting the transactions undertaken with non-arm's length non-residents during the taxation year. The T106 is a separate information return but is usually filed together with the corporate tax return. Data from the T106 is entered into a CRA database and is used to screen taxpayers for international tax audits.

# Canada (continued)

### Audit risk/transfer pricing scrutiny

The CRA continues to receive additional funding for its audit of international activities and to focus its audit resources on the examination of international transactions, especially transfer pricing.

The risk of a transfer pricing audit in Canada is high. Canadian companies with cross-border transactions with related parties can expect a request from the CRA for their required transfer pricing documentation prior to or during the course of an audit. As noted in TPM-05, "Contemporaneous Documentation," effective October 2004, it is mandatory for field auditors to issue a formal written request to taxpayers for their transfer pricing documentation upon commencement of the audit or when cross-border non-arm's length transactions with non-residents are identified during the course of an audit.

### APA opportunity

The CRA launched its APA program in July 1993. As set out in IC94-4R, it offers taxpayers the opportunity to pursue unilateral, bilateral or multilateral APAs. In addition, the CRA has made a small business APA program available to Canadian taxpayers under certain conditions. The CRA charges taxpayers only travel costs it incurs in the completion of an APA.

On 20 August 2008, the CRA issued TPM 11, which discussed the CRA policy with respect to rolling an APA back to prior years. The main limitation imposed by TPM 11 is that APAs may not be rolled back to years for which a request for contemporaneous documentation under §247 has been issued. Effectively, this means that APAs cannot be rolled back to taxation years under transfer pricing audit.


# Chile

## Taxing authority and tax law

Tax authority: Internal Tax Service (Servicio de Impuestos Internos, or "SII")

Tax law:

- Chilean taxation rules are established in the Income Tax Law (ITL), enacted in 1974
- Tax Authority Circulars issued every year provide interpretation of the articles of the ITL, and are not modifications of it

## Relevant regulations and rulings

The only mention of transfer pricing issues is found in Article 38 of the current ITL. Also in Circulars No. 03 (1998), No. 72 (2002) and No. 49 (2010) introduce more detailed information on the application of arm's length principle, approaches, timing control, among others.

Currently, there are no specific rulings on TP matters.

## OECD guidelines treatment

Although the local legislation does not mention the OECD guidelines, the legislative interpretation contained in Circular 03 (1998) reflects the arm's length principle as set out in these guidelines. The OECD reference is made only through the listing of tax heavens, in order to determine when two or more entities are related from TP perspective. It is important to note that due to the inclusion of Chile as a full member of the OECD in 2010, is promoted in the medium term, any legislative reform in which direct reference is made regarding the adoption of transfer pricing guidelines.

On the other hand, there are no specific rules regarding the business restructuring issues in Chilean ITL.

## Priorities/pricing methods

Based on Circular No. 3 of 1998, the methods to be used for TP purposes for the analysis of the CUP intercompany transactions are: CUP, Resale Price Method and Cost Plus. Not expressly stated the use of established methods in the OECD (TNMM, Profit Split Method), but could be applicable.

## Transfer pricing penalties

The amount of the transfer pricing adjustment will be subject to a 35% in case of companies incorporated as "Sociedades Anónimas" (public limited companies). For companies distinguished as "Sociedad Limitada" (limited liability companies), the TP adjustment will be treated as a deemed dividend (also subject to 35% with corporate tax credit if the entity has foreign shareholders). However, general tax penalty framework applies for TP adjustments. In this case, the taxpayer must pay a fine equal to 60% of the unpaid tax, adding a late payment interest of 1.5% per month imposed retroactively as the date when the tax was supposed to be paid.

## Penalty relief

There is currently no penalty relief available. However, the existence of contemporary TP Documentation would be intended by the tax authority as a proof of "good faith" by the taxpayer. In these cases, the TP penalty risk is reduced.

## Documentation requirements

Neither the Chilean ITL nor its related circulars aforementioned provide specific guidelines to prepare a TP report or to file an informative TP Return. However, it is expected that the taxpayers keep the information support for all the intercompany transactions subjected to TP rules.

# Chile (continued)

## Documentation deadlines

Given the absence of any formal TP documentation requirements, no filing deadlines currently apply. The taxpayers must have information that supports intercompany transactions, if it is required by the tax authority.

## Statute of limitations on transfer pricing assessments

General statute of limitations is three years. It could be extended to six years in case no return is filed or if the authorities consider that the returns are maliciously false. Based on Circular No. 49 (2010), there are distinct limits to conduct audits, depending on the size, complexity and other characteristics that can arise. In this sense, in the case of TP audits, the period applicable will be of 12 months, in which the tax authority will test the proper application of the arm's length principle on the following cases:

- Where the net income to be determined taxpayers with taxable sales or revenues in excess of 5,000 monthly tax units
- Where a review of the tax effects of corporate reorganization
- Where a review of the accounting of transactions between related companies

## Return disclosures/related-party disclosures

Currently there is no obligation on the part of taxpayers to disclose transactions undertaken with related parties domiciled abroad. However, recent revisions made by the Chilean tax authority on compliance issues, has requested information about transactions carried out with related parties through a questionnaire.

## Audit risk/transfer pricing scrutiny

Chilean Tax Authority (SII) has the burden of proof and has the power to request at any time the documentation support of the intercompany transaction subject to TP rules. At this time, there are high probabilities that the tax authority begin a process of TP audits, due to the recent inclusion of Chile as a full member of OECD. However, it is important to mention that there are no known formal TP audit processes.

## APA opportunity

The Chilean income tax law does not currently include any statement to provide an opportunity to implement an APA.


# China

## Taxing authority and tax law

Tax authority: State Administration of Taxation (SAT)

Tax law:

- People's Republic of China (PRC) Corporate Income Tax Law, Chapter 6, Articles 41 – 48
- PRC Corporate Income Tax Law Implementation Regulations, Articles 109 – 123

## Relevant regulations and rulings

- Notice Containing Related Party Transaction Annual Reporting Forms (Guoshuifa (2008) No. 114)
- Implementation Measures for Special Tax Adjustments (Guoshuifa (2009) No. 2)
- Notice on the Tax Deductibility of Interest Expense Paid to Related Parties (Caishui (2008) No. 121)
- Notice on the Strengthening, the Monitoring and Investigation of Cross-border Related Party Transactions [for Single Function Entities] (Guoshuihan (2009) No. 363)
- Notice on Intensifying the Transfer Pricing Follow-up Administration (Guoshuihan (2009) No. 188)

## OECD guidelines treatment

In principle, the tax authority recognizes the OECD guidelines and the relevant transfer pricing methods.

## Priorities/pricing methods

The tax authority accepts a reasonable method. The tax authority will accept CUP, Resale Price and Cost Plus. Other methods, including the Profit Split, and the Transactional Net Margin Method (TNMM), are also considered. For the TNMM, the profit level indicators most often used are operating margin and total cost markup. Balance sheet profit level indicators such as return on assets or return on capital employed are rarely used.

## Transfer pricing penalties

Article 48 of the PRC Corporate Income Tax Law stipulates that interest will be applied to the under-reported tax resulting from special adjustments to tax payments, including transfer pricing adjustments. Article 122 of the PRC Corporate Income Tax Law Implementation Regulations references Article 48 and states that interest imposed on special tax adjustments is based on the base renminbi (RMB) lending rate published by the People's Bank of China plus an additional 5% interest charge.

Additionally, per Article 106 of Guoshuifa (2009) No. 2, taxpayers that refuse to provide contemporaneous documentation or those that refuse to file, file false information, and/or file incomplete related-party reporting forms are subject to monetary penalties pursuant to Article 70 of the PRC Tax Collection and Administration Law and Article 96 of the PRC Tax Collection and Administration Law Implementation Regulations, as well as Article 44 of the PRC Corporate Income Tax Law and Article 115 of PRC Corporate Income Tax Law Implementation Regulations.

## Penalty relief

According to Article 122 of PRC Corporate Income Tax Law Implementation Regulations, the additional 5% interest charge (applied on the basis of Article 48 of the PRC Corporate Income Tax Law) can be avoided if contemporaneous documentation has been prepared in accordance with the relevant law and regulations and can be provided within 20 days from the day of a request.

# China (continued)

## Documentation requirements

The PRC Corporate Income Tax Law and the PRC Enterprise Income Tax Law Implementation Regulations imply that taxpayers are expected to maintain contemporaneous transfer pricing documentation. Articles 13 through 20 of Guoshuifa (2009) No. 2 formally introduce and clarify China's contemporaneous transfer pricing documentation requirements.

Article 14 of Guoshuifa (2009) No. 2 specifies five primary components of China's contemporaneous documentation:

- Organization structure
- Information of business operations
- Information of related-party transactions
- Comparability analysis
- Selection and application of transfer pricing methods

Article 15 states that certain enterprises can be exempted from the preparation, maintenance, and provision of contemporaneous documentation:

- Those conducting RMB200m or fewer in annual related-party purchase and sale transactions and RMB40m or fewer in annual related-party "other" transactions (intangibles, services, and interest from financing transactions)
- Those with transactions covered by an advance pricing arrangement (APA)
- Those with a 50% or less share of foreign ownership that only conduct related-party transactions within China

## Documentation deadlines

Article 16 of Guoshuifa (2009) No. 2 specifies that taxpayers should finish the preparation of contemporaneous documentation on or before 31 May of the following year and that all documentation should be submitted to tax authorities within 20 days of a request.

## Statute of limitations on transfer pricing assessments

The statute of limitations for transfer pricing adjustments may vary; however, adjustments can be applied for a period of up to 10 years.

Article 20 of Guoshuifa (2009) No. 2 states that contemporaneous documentation should be maintained for a period of 10 years (starting from 1 June of the year following the transactions).

## Return disclosures/related-party disclosures

Article 43 of the Corporate Income Tax Law and Guoshuifa (2008) No. 114 requires that taxpayers complete and submit nine comprehensive Related Party Transaction Annual Reporting Forms along with their annual tax filing. Per Article 16 of Guoshuifa (2009) No. 2, these forms must be submitted on or before 31 May following the fiscal year, including related-party transactions conducted during fiscal year 2008 (i.e., Related Party Transaction Annual Reporting Forms for fiscal year 2008 are due on or before 31 May 2009).

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being reviewed under audit is high.

In 2009, 179 new transfer pricing audits were initiated and 167 cases were closed. Taxable incomes were adjusted by an aggregate of RMB16.09b during 2009 – a significant increase from the approximate RMB8.2b adjusted in 2008, RMB9b adjusted in 2007 and RMB5.9b adjusted in 2006.

The tax authority continues to focus on enterprises that have sustained losses in the past, especially those paying intercompany service charges or royalties. With the release of China's final implementation rules contained within Guoshuifa (2009) No. 2, we believe there will be an increase in transfer pricing audit activity in the coming years.

## Audit risk/transfer pricing scrutiny (continued)

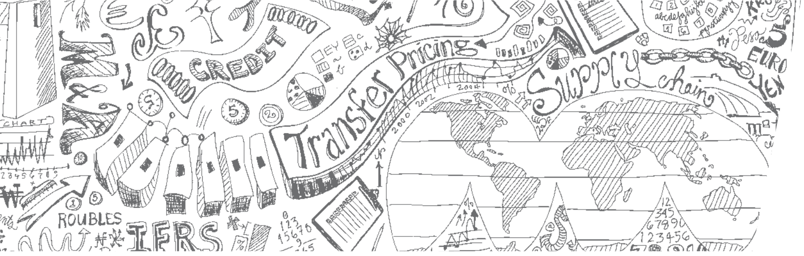
Within Guoshuihan (2009) No. 363, the tax authority also reiterated its position that "single-function" entities should not be subjected to losses. Any such "single-function" entity that generates losses is required to prepare and submit contemporaneous documentation, regardless of its quantum of related party transactions.

Additionally, Guoshuihan (2010) No. 323 spells out the tax authority's expectations that each of China's local tax bureaus is to prepare a list of taxpayers required to prepare contemporaneous documentation, the names of the companies for which documentation was reviewed, and comments on the quality and completeness of each of the reviewed report, covering all taxpayers except for 45 enterprises directly managed by the tax authority's Large Enterprise Taxation Department.

## APA opportunity

APAs are available in China. Guidance regarding the APA process and procedures is provided in Articles 46 through 63 of Guoshuifa (2009) No. 2.

The validity of an APA is generally between three and five years. Enterprises no longer need to have ten years of operating history before applying for an APA and the ban on enterprises with major tax evasion history has been lifted as well. Annual related-party transaction volumes must only be greater than or equal to RMB40m, rather than the previously required RMB100m. Applications for APAs involving more than one in-charge province can be submitted directly to the tax authority in Beijing.




# Colombia

## Taxing authority and tax law

Tax authority: Dirección de Impuestos y Aduanas Nacionales (DIAN)

Tax law:

- Law 788 enacted in 2002 and Law 863 enacted in December 2003 established transfer pricing rules; articles 260-1 to 260-10 of the Tax Code
- The definition of related parties is found in Articles 450 and 452 of the Tax Code; Articles 260, 261, 263 and 264 of the Commercial Code; and article 28 of Law 222 of 1995

## Relevant regulations and rulings

Regulatory Decree 4349 published in December 2004 provides the Transfer Pricing Guidelines applicable in Colombia, including the contents of the transfer pricing documentation and return, use of financial data and APA programs.

Resolution 11188 published on 29 October 2010 provides the content and technical characteristics of information to be provided to tax authorities in the transfer pricing return.

## OECD guidelines treatment

Although Colombia is not a member of the OECD, its guidelines are generally followed in the local regulations. According to Sentence C-460 of the Colombian Constitutional Court issued on 16 June 2010, OECD comments and guidelines are an auxiliary criterion for interpretation, but they are not mandatory for the tax authorities, that may or may not take them into account. However, OECD guidelines have been mentioned and have been used as a reference in recent audits.

## Priorities/pricing methods

The law establishes six methods: CUP, Resale Price, Cost Plus, Profit Split, Residual Profit Split and TNMM. The selection of the method should be based on the characteristics of the transaction under analysis. The selected method should be the one that better reflects the economic reality of the transaction, and one that provides the best information and requires fewer adjustments. Local companies' information is available and should be used for benchmark analyses when applicable. Since the transfer pricing regime is quite new in Colombia, it is advisable to analyze transactions under two methods, if applicable.

## Transfer pricing penalties

The Colombian transfer pricing regime penalizes faults in both the supporting documentation and the return, as follows:

### A. Transfer pricing documentation

In the case of lateness, errors, inaccuracy or information that does not allow to verify the application of transfer pricing, taxpayers bear penalties of 1% of the total value of transactions with foreign related parties during the relevant tax year or 0.5% of the taxpayer's net income or gross capital reported in the income tax return of the same tax year or in the last tax return filed. Penalties cannot exceed 28,000 UVT (Tax Value Unit).

Additionally, when the taxpayer does not provide the required documentation, the penalties are calculated in the same way as in partial noncompliance, which means that 1% of the total value of transactions with foreign relates parties or 0.5% of the taxpayer's net income or gross capital reported in the income tax return of the same tax year or in the last tax return filed. These penalties cannot exceed 39,000 UVT. Moreover, the costs derived from intercompany transactions about which information was not provided, will be disregarded.

Regarding transfer pricing documentation, penalties are reduced by 50% if the omission, mistake or inconsistency is corrected before penalty notification or reduced by 25% if corrected within two months after penalty notification.

# Colombia (continued)

## Transfer pricing penalties (continued)

### B. Transfer pricing return

As per the transfer pricing return, penalties for late filing and amendments are calculated in the same manner as penalties for noncompliance with documentation requirements, which means, 1% of value of the total intercompany transactions with related parties during the relevant fiscal year, but it increases on a monthly basis and cannot exceed 39,000 UVT If it is not possible to establish the base for the penalty, it will be calculated as 0.5% of the taxpayer's net income or gross capital reported in the income tax return of the same tax year or in the last tax return filed.

If the transfer pricing return is submitted after is has been required by the tax authorities, the penalty will be doubled. If the return is not filed during the term provided by the tax authorities' request, the penalty will be 20% of total intercompany transactions during the fiscal year. Additionally, if it is not possible to determine the value of the transactions with foreign related parties, the default fine is 10% of the taxpayer's net income or gross capital reported in the income tax return of the same tax year or in the last tax return filed. The penalties cannot exceed 39,000 UVT.

Once the taxpayer becomes liable for penalties for not filing the return form, such penalties can be reduced by 25% if the taxpayer files the return before the new deadline.

Regarding transfer pricing adjustments, when a taxpayer does not comply with the arm's length principle, the tax authorities administer an additional penalty of 160% of the unpaid income tax.

### C. Tax bill and penalty reductions

There is currently a legislative bill in the Congress which proposes a reduction of the maximum penalties for transfer pricing documentation and returns.

Specifically, regarding transfer pricing documentation, the tax reform looks to limit the maximum penalty for lateness, errors, inaccuracy or information that does not allow verifying the application of transfer pricing, to 15,000 UVT. Currently, the maximum penalty is 28,000 UVTs. Additionally, the tax reform proposes that in case the taxpayer does not provide the required documentation, the maximum penalty to be 20,000 UVT. Currently, that penalty is 39,000 UVT.

In relation to transfer pricing return penalties, the proposed changes in the tax code seek to set a maximum penalty of 20,000 UVT. The current maximum penalty is 39,000 UVT. This represents a potential reduction of 48.7% in penalties.

## Penalty relief

See above section for penalty relief regimes.

## Documentation requirements

Taxpayers must prepare supporting documentation proving each transaction with foreign related parties complies with the arm's length principle. The transfer pricing documentation includes a functional analysis (organizational structure, business descriptions, functions, assets, risks and detailed information of intercompany transactions, among others); a macro-economic analysis, an industry analysis and an economic analysis

Documentation is not required for transactions within the fiscal year that do not exceed 10,000 UVT. Regulatory Decree 4349 outlines the information to be included in transfer pricing documentation.

## Documentation deadlines

### A. Documentation

Documentation should be in existence and available by 30 June of the next fiscal year. However, documentation is submitted to the tax authorities only upon formal request.

For fiscal year 2009, all taxpayers that had submitted documentation the previous year, were requested to submit it by 1 July 2010.

# Colombia (continued)

## Documentation deadlines (continued)

B. Filing returns

For fiscal year 2009, transfer pricing returns were submitted between 9 July and 30 July 2010 depending on the taxpayers' Tax ID number.

## Statute of limitations on transfer pricing assessments

A. Documentation

The statute of limitations is five years. The tax authorities can request and review transfer pricing documentation at any time during this period.

B. Transfer pricing return

The statute of limitations is two years. However, if the transfer pricing return is not submitted to the tax authorities, they can request it for up to five years following.

C. Income tax return

The income tax return becomes final after two years of submission in most cases. However, when the taxpayer has the tax audit benefit, the return is final after six months. Since transfer pricing has effects only on the income tax return, in practice, TP assessments can be made during the statute of limitation.

## Return disclosures/related-party disclosures

As part of the transfer pricing return, taxpayers must disclose information on related parties such as country of residence and Tax ID number. Other information disclosed on the transfer pricing return includes the type of intercompany transaction, the amount of the transaction, the transfer pricing methodology applied, the company assessed, the price/margin obtained in the transaction and the arm's length interquartile range.

## Audit risk/transfer pricing scrutiny

A. Previous years

The tax authorities have been scrutinizing transfer pricing since 2006, requesting documentation from almost all of the taxpayers who had filed the transfer pricing return for fiscal year 2004 (1,250 taxpayers). In 2004, tax authorities requested clarification regarding non-declared transactions and amendments, and requested more information from six taxpayers, citing a lack of proper documentation.

The tax authorities' interest and knowledge in transfer pricing matters has increased during the last years. During 2007, approximately 350 taxpayers had requests for their transfer pricing documentation for fiscal year 2005 and 2006. In 2008, over 10 taxpayers were requested to deliver their transfer pricing studies for fiscal year 2007; these companies belonged mainly to the coal and oil industries.

B. 2009 and recent developments

Since 2009 all taxpayers that submitted transfer pricing returns were requested to present documentation. All taxpayers that did not comply with the arm's length principle were subject to a transfer pricing adjustment, which according to Article 2 of the Regulatory Decree 4349 of 2004 should be the median of the interquartile range. Moreover, the tax authorities have started to challenge technical issues, such as comparables and comparability adjustments. Transfer pricing scrutiny is expected to increase in the coming years and the tax authorities will probably aim at mining and oil industries, and also focus on challenging comparability adjustments. In this sense, audit risk has been high.

## APA opportunity

The tax reform enacted in 2003 established APA regulations. APAs may be granted for a four-year term and they can be renewed, and can only be requested on a unilateral basis. Currently there are no precedents set for APAs or respective requests.


# Croatia

## Taxing authority and tax law

Tax authority: Ministry of Finance

Tax law:

- The Corporate Income Tax Act (the "CIT Act")
- The Corporate Income Tax Bylaw (the "CIT Bylaw")

## Relevant regulations and rulings

Article 13 of the CIT Act and Article 40 of the CIT Bylaw prescribe arm's length pricing as the basic principle to be followed, define the methods allowed and documentation required to support prices between related parties.

In general, arm's length pricing is required only for cross-border transactions between related parties. However, in line with the Amendments to the CIT Act that are in force as of 1 July 2010, the obligation to comply with transfer pricing rules is extended to transactions between domestic entities if one of the entities is either in a tax loss position or in a special tax status (paying tax at lower rate or is exempt from paying corporate income tax). Note that this is in line with the (non-binding) official opinion of the Tax Authorities issued prior to the amendments of the legislation were introduced i.e. this is applied for the periods before 1 July 2010. At present, neither the CIT Act nor the CIT Bylaw provide extensive guidance or instruction to taxpayers with regard to meeting the transfer pricing requirements.

## OECD guidelines treatment

Although Croatia is not an OECD member country, the provisions of relevant Croatian tax legislation are generally based on the OECD Transfer Pricing Guidelines. Furthermore, the Ministry of Finance issued instructions for the tax officials performing transfer pricing audits. The instructions are also based on the OECD Transfer Pricing Guidelines.

## Priorities/pricing methods

The Croatian CIT regulations do not provide detailed rules on how to arrive at the market price that should be applied in related-party transactions. However, the CIT Act prescribes the methods that a taxpayer can use to determine the market price: Resale Minus, Comparable Uncontrolled Price ("CUP"), Cost Plus, Profit Split and Transactional Net Margin Method. The relevant legislation states that the CUP method has priority over the other methods.

## Transfer pricing penalties

Fines up to HRK200,000 (approximately EUR 28,000) for a company and up to HRK 20,000 (approximately EUR 2,800) for the responsible individual within the company, per offence, may be imposed in respect of any underestimation of the corporate income tax liability. Penalty interest would also be calculated from the date when the tax was due until the date when the tax is paid.

## Penalty relief

There are no specific provisions concerning penalty relief.

# Croatia (continued)

## Documentation requirements

According to the CIT Bylaw, a taxpayer should perform (and provide documentary evidence of) the following activities in the process of proving that market prices have been applied in transactions with any related parties:

- List of related parties and specification of transactions with them
- Identification of the transfer pricing method applied (description of the method chosen for determining the transfer prices and a statement justifying the reasons for choosing the particular method)
- Comparable search – description of data, methods and analysis used for determination of transfer prices. Specification of assumptions and evaluations used in the process of determining transfer prices (in line with the principle of unbiased transactions), with reference to comparability, functional analysis and risk analysis
- Documentation of all calculations based on the selected method (such documentation should enable a comparison with the prices applied by other comparable taxpayers)
- Update of the transfer pricing documentation to reflect adjustments made due to changes in relevant facts and circumstances
- Prepare other documentation substantiating the analysis and determination of transfer prices

The taxpayer must maintain data and information concerning related parties and the business transaction conducted between them.

## Documentation deadlines

There is no specific deadline for the preparation of the transfer pricing documentation prescribed by the legislation. The law requires the transfer pricing documentation to be available and to be provided to the tax authorities upon their request in a tax audit. The documentation should be available in the Croatian language.

## Statute of limitations on transfer pricing assessments

The general statute of limitation for determination of tax liabilities and rights in a particular tax period expires at the end of the third year following the year in which a tax return should have been filed (e.g., as the 2010 corporate tax return has to be filed by 30 April 2011, filings for 2010 become statute-barred on 1 January 2015). However, the general statute of limitations may be prolonged and recommences after each intervention by the tax authority with respect to a tax return which has been filed. The absolute statute of limitations expires after six years. Therefore, filings for 2010 become statute-barred absolutely on 1 January 2018.

## Return disclosures/related-party disclosures

No specific disclosures are required in the annual tax return.

However, Croatian tax authorities regularly request information on transfer pricing methods used after the CIT return has been filed.

## Audit risk/transfer pricing scrutiny

In past few years the tax authorities have increased the frequency of transfer pricing audits. As they still have limited experience in transfer pricing, there are many disputes, as well as requirements for supporting explanations with respect to related party charges and additional documentation. However, there is a noticeable trend towards increased awareness of transfer pricing problems among the tax authorities' officials.

The tax authorities are in particular focused on examining documentation on service fees charged by related parties. Tax inspectors tend to challenge service costs based on the argument that the available documentation is insufficient to prove the benefit arising to the Croatian company from the respective services. They also challenge the appropriateness of the prices applied in such transactions.

Generally, the transfer pricing audit risk can be considered high.

## APA opportunity

Currently there is no legal basis for APAs in Croatia.


# Czech Republic

## Taxing authority and tax law

Tax authority: Ministry of Finance (MF)

Tax law: The Income Tax Act §23(7) – arm's length principle, and §38nc – APA scope and procedures

## Relevant regulations and rulings

Directive D-258 discusses the application of international standards in the taxation of transactions between associated companies (i.e., transfer prices). D-258 confirms the applicability of the OECD TP Guidelines for both international and domestic transactions (with certain exceptions).

Directive D-292 outlines requirements concerning §38nc of the Income Tax Act. D-292 comments on the principles of binding assessments, which correspond to the preliminary price agreement principles within the meaning of the OECD guidelines.

Directive D-293 outlines requirements on the expected scope of documentation of a TP method agreed between related persons. D-293 comments on the scope and nature of TP documentation in accordance with the European Union (EU) TP Documentation requirements created by the EU Joint TP Forum.

Directives D-258, 292 and 293 are not legally binding but are usually followed in practice by the tax authority.

## OECD guidelines treatment

Based on Directive D-293 (not legally binding), the OECD guidelines as well as the Code of Conduct on TP Documentation for Associated Enterprises in the EU are generally accepted in the Czech Republic. This directive also mentions that TP documentation prepared in accordance with the Code of Conduct "should be sufficient" for substantiating the method of calculation of the arm's length price.

## Priorities/pricing methods

The MF follows the OECD TP Guidelines. Use of profit-based methods is possible where substantiated.

## Transfer pricing penalties

There are no specific TP penalties. Generally, upon a successful challenge of TP by the tax authority, a penalty of 20% of the unpaid tax or 1% of the decreased tax loss will be applied. Thereafter, interest is assessed at 14% above the "repo rate" (or repurchase agreement rate) of the Czech National Bank (for five years at maximum).

## Penalty relief

There is no specific penalty relief regime in place. It is at the discretion of the MF to decrease penalties; however, this is limited to specific situations.

## Documentation requirements

There are no specific statutory requirements in place. It is crucial for the taxpayer to have supporting documentation in case the transactions are audited by the tax authority, as the burden of proof remains with the taxpayer. The tax authority has great discretion in deciding what level and nature of documentation is sufficient. During the tax audit, the authority may request any documentation that reasonably substantiates the actual character and substance of the transaction, its benefits for taxpayers, the appropriateness of the level of fees and the TP method selected. The analysis of a controlled transaction and the identification of comparables could be useful. Therefore, a high level of formal evidence may be necessary to support various aspects of the transaction. Deadlines for submitting the required documentation may be 15 or 30 days after the request is delivered to the taxpayer.

# Czech Republic (continued)

## Documentation requirements (continued)

D-293 describes the documentation that is expected and may be required by the tax authority. Nevertheless, as the directive is not legally binding, there is no legal requirement to prepare documentation.

D-292 sets out documentation that should serve as the initial basis for filing the application for issuance of a binding assessment. The submitted documentation should contain information on the group, information on the company, information on the business relationship, information on other circumstances affecting the business relationship and information on the TP method.

## Documentation deadlines

There is no specific deadline to prepare documentation, since no specific statutory documentation requirement exists.

In the event of a TP challenge, the taxpayer must file information before the statutory deadline for tax proceedings. This is generally within 15 days of the receipt of a request by the tax authority. This time limit may be extended at the discretion of the tax authority if a request is made by the taxpayer.

## Statute of limitations on transfer pricing assessments

The general statute of limitations applies. Effective since 1 January 2011, the limit set by the Tax Code is three years from the end of the period for filing of the return of the taxable period in question i.e. in which the tax liability arose. However, if the tax authority undertakes an act directed at the assessment of tax, then the three-year time limit begins again. The limit will also be prolonged if the supplementary tax return for the respective period is filed (should the taxpayer file an additional return in the 12 months prior expiration of current limit, the limit is extended by one year) or if a tax loss carry forward may be utilized in the particular period. Tax may not be assessed, however, later than 10 years or 17 years if tax losses were incurred (15 years in case of tax losses incurred in 2004 and onwards).

## Return disclosures/related-party disclosures

Effective from 1 January 2001, the executives of a controlled entity are required to complete a memorandum with respect to relations and transactions with companies in the group. This does not apply if a controlling agreement is concluded. Note that this is based on commercial legislation rather than tax legislation, and the memorandum has no direct tax impact or tax aspects. Taxpayers must provide documentation of transactions with related parties in the corporate income tax return.

## Audit risk/transfer pricing scrutiny

The risk of TP issues being reviewed under an audit is high. The tax authority has adopted a global approach. Audit subjects are selected based on complex criteria and TP is only one aspect among many others. Intangibles, royalties and service fees are seen as the most likely TP audit issues. Although no specific country is targeted for TP audits, transactions with tax haven countries are closely scrutinized. The tax authority intends to increase scrutiny of TP. According to press statements of MF's representatives, the tax authorities should particularly focus on TP and fully dedicated specialists forming specialized sections have already initiated this increased scrutiny.

## APA opportunity

APA regulations were established under §38nc of the Income Tax Act, which became effective on 1 January 2006. Upon the tax entity's request, the tax administrator decides whether a taxpayer has chosen a TP method that would result in a transfer price determination on an arm's length basis. The binding assessment can only be issued for transactions effective in a particular tax period or that will be effective in the future. It is impossible to apply for a binding assessment of business relationships that have already affected the tax liability. D-292 details the procedure for issuing binding assessments and the necessary particulars for the application. Generally, the tax administrator should issue the decision within six months assuming all documentation and information are provided, but this deadline is not legally binding.


# Denmark

## Taxing authority and tax law

Tax authority: Ministry of Taxation (MT)

Tax law:

- Section 2 of the Tax Assessment Act
- Sections 3B, 14(3) and 17(3) of the Tax Control Act
- Sections 26 and 27 of the Tax Administration Act

## Relevant regulations and rulings

Regulation number 42 of 24 January 2006 pertains to the documentation of the pricing of intercompany transactions and guidelines for preparation of written documentation. The regulation sets forth the minimum requirements and guidelines for tax assessment and for disclosing information. The regulation is referred to as the Executive Order on Transfer Pricing Documentation.

## OECD guidelines treatment

The MT will, for the purpose of its assessment, apply the principles of the OECD Transfer Pricing Guidelines.

## Priorities/pricing methods

The MT accepts CUP, Resale Price, Cost Plus, Profit Split and TNMM. In selection of the method, the taxpayer should take into consideration the aspects regarding the application of methods stated in the OECD Transfer Pricing Guidelines.

## Transfer pricing penalties

Fines were introduced for income years commencing on or after 2 April 2006, if the transfer pricing documentation requirements are not observed either intentionally (deliberate omission) or due to gross negligence or if incorrect and misleading information on the exemption rule for small and medium-sized companies is given. The amount of the penalty is twice the costs saved for not having prepared the transfer pricing documentation in the first place. The penalty may be reduced by 50% if the documentation required is produced subsequently.

If, in addition, the income is increased because the arm's length criterion has not been satisfied, the minimum fine will be increased by an amount equal to 10% of the income increase.

In case of income adjustments, a 5.1% (6.1% for 2009, 6.3% for 2008, 5.8% for 2007, 5.3% for 2006, 5.4% for 2005 and 5.7% for 2004) nondeductible surcharge on all adjustments of prior years' corporate taxes payable will be levied. Furthermore, a non-deductible interest of 0.5% (0.6% for income year 2007-2009, 0.5% for the income years 2005-2006 and 0.6% for the income year 2004) for each month since the due date for the corporate tax payable for the income year in question is applicable.

## Penalty relief

If the taxpayer prepares the lacking or insufficient documentation and ensures that the documentation meets the requirements, the fine (except that which is related to the increase of taxable income) will be reduced to half of the original amount.

# Denmark (continued)

## Documentation requirements

The documentation must be available upon request from the tax authority within 60 days' notice. The earliest such a request can be made is the date of filing for a company's tax return. The transfer pricing documentation requirements affect both domestic and foreign intercompany transactions. In certain circumstances the transfer pricing documentation requirements are reduced for small and medium sized companies (companies are classified according to thresholds measured at group level), as well as for entities subject to tonnage tax.

The documentation requirements were tightened as of 2006. According to the Executive Order on Transfer Pricing Documentation, the documentation should include:

- A description of the group, including the legal group structure, the history of the group, including a description of restructurings, operational structure and primary business activities, as well as a description of the industry in which it operates
- A description of the Danish entity, its intercompany transactions and the other entities involved (primary business activities and three years' key financials for all entities involved)
- A description of each intercompany transaction including:
  - Parties, types of products/services/assets transferred and the volumes involved
  - An analysis of functions and risks undertaken and assets employed by the entities involved
  - Contractual terms
  - Economic conditions
  - And
  - Business strategies
- Comparability analysis by intercompany transaction, including:
  - Information about the transfer pricing policy and method applied, and how the transfer pricing principles are implemented in practice (e.g., whether year-end adjustments are made)
  - An analysis of how the transfer prices satisfy the arm's length principle
- A list of any written intercompany agreements entered into by the Danish entity and a copy of any written agreements in place with foreign tax authorities regarding transfer prices

According to the tightened documentation requirements, a taxpayer must, within 60 to 90 days' notice, provide external comparable searches as part of the arm's length analysis upon request from the tax authority.

As of August 2009 additional documentation guidelines are applicable to the valuation of companies/businesses, shares and intangible assets/IP in a related party context.

## Documentation deadlines

The deadline for preparing documentation is the same as the deadline for filing the tax return. Documentation must be provided upon request. 60 days' notice is given.

## Statute of limitations on transfer pricing assessments

The statute of limitations for a transfer pricing assessment is 1 May in the sixth year after the end of the calendar year following the income year.

# Denmark (continued)

## Return disclosures/related-party disclosures

Form 05.021 (05.022 - English version) discloses information on all controlled transactions and whether the company is qualified for reduced documentation requirements.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being reviewed under an audit is high. Three dedicated transfer pricing audit centers across Denmark are operated by the tax authorities with the single purpose of carrying out transfer pricing audits. We see an increasingly intense focus on transfer pricing which is emphasized in the well publicized plan of action on taxation of MNEs released by MT in July 2010. From a transfer pricing perspective the plan of action focuses on MNEs which are operating at breakeven or are loss making.

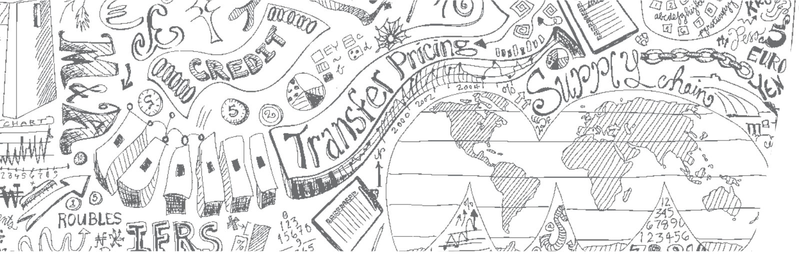
The transfer of business/intangibles out of Denmark is also a key target for MT and audit risk associated with these transactions is high. In line with this focus the August 2009 MT guidelines were published on the valuation methods applicable to and documentation of companies/businesses, shares and intangible assets/IP in a related party context.

Most normal tax audits now include and are being initiated with requests related to transfer pricing. Intensified cooperation between the Nordic tax authorities has led to a higher level of information sharing and a significant increase in the number of coordinated cross-Nordic audits.

## APA opportunity

The Danish legislation provides for unilateral APAs only. There is no APA regime in place, but the MT has entered into a limited number of bilateral APAs. For instance, MT has entered into the first bilateral APA between China and a European country.

We expect this area will develop significantly within the next few years.




# Ecuador

## Taxing authority and tax law

Tax authority: Internal Revenue Service (Servicio de Rentas Internas or SRI)

Tax law: Internal Tax Regime Organic Law (Ley Orgánica de Régimen Tributario Interno or LORTI) and its Regulation

## Relevant regulations and rulings

In the First Title, Chapter I, First Section, the first unnumbered Article after the Article 4 of the Internal Tax Regime Organic Law defined related parties.

The First Title, Chapter IV, Second Section, in the first unnumbered Article after the Article 15 of the Internal Tax Regime Organic Law, established the transfer pricing regime.

In the same section mentioned above, the fifth unnumbered Article after the Article 15, established and exception of the transfer pricing regime application when a taxpayer comply with this conditions: tax payable greater than the 3% of their taxable income, do not perform transactions with tax heavens, do not have contracts with the Government for the exploration and exploitation of none renewable resources.

Article 90 of the Internal Tax Regime Organic Law, established the utilization of secret comparables for the review of the application of the Arm's Length principle.

Article 87 of the Tax Regulation (Reglamento para la Aplicación del Régimen Tributarios Interno) established the median calculation and arm's length standard.

In addition the Tax Regulation established the concept of sub-capitalization, which requires the amount of the external debt not be greater than 300% of the equity in order to consider interest payments abroad as deductible expenses.

The SRI Resolution NAC-DGER2008-0464 established the transfer pricing exhibit and transfer pricing integral report content requirements.

## OECD guidelines treatment

The SRI considers the 1995 edition of the OECD guidelines as a technical reference for analyzing intercompany transactions. However the Internal Tax Regime Organic Law has supremacy over the OECD guidelines.

Ecuador follows a hierarchy of transfer pricing methods. Local regulations establish that only the six methods established in the OECD Guidelines are applicable. The CPM and full profit split method are considered the last resort methods by the SRI.

## Priorities/pricing methods

The SRI accepts the CUP, Resale, Cost Plus, Profit Split, Residual Profit Split, and Transactional Net Margin Method. There is a hierarchy of methods. Indeed, the SRI has made the application of the CUP method mandatory. If the CUP method cannot be applied, the Resale or the Cost Plus methods must be implemented. If none of these methods can be executed due to the complexity of the transactions under analysis, the SRI accepts the other analyses frameworks mentioned above as valid ones, leaving the Transactional Net Margin Method as the method of last resort. The direct implication is that all method rejections must be thoughtfully documented.

There are specific CUP method applications. More specifically, for exports and imports of tangible goods between related and independent parties where there is an international price in transparent markets, the market price is used, unless there is evidence to the contrary. In addition, there is another application for companies that operate through international intermediaries, who are not the final consignees or producers of the goods. Such goods include all products with well-known prices in transparent markets. In these cases, the price to be applied is the price in those markets on the day the goods are loaded for shipment or the agreed-upon price if higher. This method may not apply if the local exporter or importer is able to prove the substance of the operations of the consignee abroad and that this intermediary party has not more than 20% of its operations with related parties.

# Ecuador (continued)

## Transfer pricing penalties

Ecuador has a specific transfer pricing penalty regime. There are processes in place to ensure the consistent application of transfer pricing penalties in the jurisdiction.

Penalties up to US$ 15,000 could be applied if deadlines are not met or where inaccuracies are detected. Interest could be applicable on unpaid adjustments as part of the income tax.

## Penalty relief

No penalty relief regime has been provided.

## Documentation requirements

The SRI requires a Transfer Pricing Annex report to be filed, detailing:

- All transactions with foreign related-parties
- The methods applied in analyzing each transaction
- Calculated adjustments for each transaction using software provided by the tax administration

This declaration must be filed by companies with accumulated transactions with related parties exceeding US$ 3m in the reported fiscal year or companies with accumulated transactions with related parties between US$ 1m and US$ 3m in the reported fiscal year, which amount represents up to 50% of the total revenues.

Additionally, the Transfer Pricing Integral Report must be presented to the SRI by companies with accumulated transactions with related parties exceeding US$ 5m in the reported fiscal year. This Report must substantiate the analyses made of all transactions reported in the Annex. Both documents must be filed up to two months after the income tax return deadline.

Nevertheless, the SRI may require, at any time, the Transfer Pricing Annex and/or the Integral Report even though the company does not reach the threshold, or in the case of intercompany transactions between domestic related companies.

Transfer Pricing Integral Report Requirements:

- Full functional analysis of the multinational group and the local party
- Risk analysis of the local company and assets detail
- Intercompany transactions detail and functional description
- Market analysis including global and local descriptions and a demand analysis for both levels
- Economic analysis including:
  - Detailed and quantified information for each type of operation held with foreign related parties
  - Detailed reasoning for acceptance or rejection of a method
  - Profit level indicator selection process
  - Comparable companies detail
  - Applied adjustments explanation
  - Reason for rejection of searched comparable companies
  - Accepted comparable companies activities description and financial statements
  - Analysis description and conclusion

## Documentation deadlines

Adjustments and intercompany transaction figures must be included on an Income Tax Return form (due in April).

The Transfer Pricing Annex and Integral Report must be filed two months after filing the tax return. That is, from 10 June to 28 June depending on the ninth digit of the company Tax ID Number.

# Ecuador (continued)

## Statute of limitations on transfer pricing assessments

The statute of limitations is three years from the date of the income tax return filing and six years if overall tax compliance was not accomplished.

The obligation to prepare and present the Transfer Pricing Annex starts when related parties' transactions exceed US$ 3m or when related-parties' transactions between US$ 1m and US$ 3m represents up to 50% of the total revenues.

The Integral Report must be delivered in addition to the Annex only when those transactions exceed US$ 5m.

## Return disclosures/related-party disclosures

No specific related-party information, aside from the documentation required by transfer pricing regulations, is required. However, these regulations also require the following additional parties to be treated as related:

- Tax-haven located companies
- Parties buying or selling more than 50% of the products sold or bought by the local company
- Parties on which the local company has at least a threshold of 25% ownership

Resolution NAC-DGER2008-0182 established a list of tax havens or low tax rate jurisdictions as well as the contents and the mandatory filing of a transfer pricing study.

The Article 1 of the Resolution NAC-DGERCGC09-00704, exclude Uruguay from the list of counties considered as a tax haven by the SRI.

## Audit risk/transfer pricing scrutiny

Ecuador Transfer pricing risks of audit could be assessed as high. Recent audit activity included a specific focus on transfer pricing. For the first semester of 2010, the SRI has performed 44 intensive reviewing processes.

In recent years, the number of ongoing litigation and undergoing domestic appeals cases (preceding court action) has increased. Tax havens are frequently involved in disputes.

The sale of tangible goods (representing 80% of the current case load) and intra-group services (approximately 20% of the current case load) are currently the focus of the Directorate of Taxes for transfer pricing review.

A transfer pricing audit is instigated by a central decision-making body. Various considerations are taken into account in determining which taxpayers to audit, including (ranked in order of importance):

- The outcome of a risk assessment by the SRI
- The nature of related-party transactions undertaken by the taxpayer
- The outcome of customs
- Previous tax audits of the taxpayer
- The profitability of the local taxpayer

A high risk of audits could be assessed for oil, agriculture, pharmaceutical, construction and fishing industries and the activities related with them. Several auditor teams are acting simultaneously on about 40 relevant companies at a time.

## APA opportunity

Ecuador has no formal APA program. The local law outlines the possibility of APA procedures and prescribes that regulations will be issued by the tax administration on the application process of APA. However, the relevant regulations have not been issued. Therefore, no taxpayers have started consultation for an APA.

Generally, the procedures require taxpayers to satisfy inquiries relating to the previous two taxable years from the tax administration, after which taxpayers may propose, through consultation with the tax administration, applicable prices for the APA Term. The APA Term includes the year preceding the APA application, the year of the APA application and the two tax years following the application and the SRI has two years to resolve the proposal.


# Egypt

## Taxing authority and tax law

Tax authority: Egyptian Tax Authority

Tax law: Income Tax Law No. 91 of 2005

## Relevant regulations and rulings

According to Article no. 30 of the income tax law "If the associate persons set conditions in their commercial or financial dealings different from the conditions taking place between non-associate persons, which are liable to reduce the tax base or transfer its burden from a taxable person to another tax-exempted or non-taxable person, the Administration may determine the taxable profit on basis of the neutral price."

The head of the Administration may conclude agreements with associate persons on one or more methods for determining the neutral price in the Administration's dealings.

## OECD guidelines treatment

Pursuant to the executive regulations of the income tax law, in case none of the three methods referred to in the law are possible to apply, any one of the methods mentioned in the form of the OECD, or any other method suitable for the taxpayer may be followed.

## Priorities/pricing methods

According to Article no. 39 of the executive regulations of the Income Tax Law, the fair market price prescribed in Article no. 30 of the law shall be determined according to the following methods:

- Comparative uncontrolled price method
- Cost plus method
- Re-sale price method

According to Article no. 40 of the executive regulations the preferred method for determining the neutral price shall be the comparative uncontrolled price method. In case the data necessary for applying this method are unavailable, any of the two other methods prescribed in the previous article may apply.

## Transfer pricing penalties

According to the income tax law, if the tax amount the taxpayers include in the tax return is less than the amount of the finally estimated tax, they shall be liable for a penalty based on the following:

- 5% of the tax payable on the non-included amount, if such amount is between 10% and 20% of the legally-payable tax
- 15% of the tax payable on the non-included amount, if such amount is between 20% and 50% of the legally-payable tax
- 80% of the tax payable on the non-included amount, if such amount is more than 50% of the legally-payable tax

## Penalty relief

The tax authority has not issued any instructions or guidelines regarding penalty relief.

# Egypt (continued)

## Documentation requirements

Taxpayers are advised to follow a four-step process through which they develop the reasoning and documentation needed to support the evaluation of their transfer prices.

TP documentation requirements correspond to the four-step approach as follows:

**(1) Identifying the intra-group transactions and understanding the nature of such transactions, providing documentation related to:**

- The group of associated enterprises as a whole
- The nature of the industry/market in which the taxpayer operates
- The taxpayer's business policies and strategies
- The controlled transactions under review
- The comparables

**(2) Selecting the most appropriate transfer pricing method(s), providing documentation:**

- Identifying the pricing method(s) used
- Presenting the analysis conducted to evaluate the reliability of data used

**(3) Applying the selected pricing method, providing documentation:**

- That is generally produced regardless of the pricing method used
- Related to the pricing method applied

**(4) Determining the arm's-length amount and introducing a review process to reflect any future changes, by documenting:**

- The established arm's-length amount
- The actions undertaken to monitor changes
- The evaluation of the impact of such changes (if any) on the validity of the arm's-length amount
- The adjustments made to account for such an impact in order to obtain a reliable arm's-length amount

## Documentation deadlines

To date, the tax authority has not issued any instructions related to TP documentation deadlines.

## Statute of limitations on transfer pricing assessments

According to the income tax law, the statute of limitations is five years.

## Return disclosures/related-party disclosures

According to the corporate tax return format, taxpayers are obliged to declare the following:

- Name of the related party/parties along with the group structure
- The nature of the relationship
- Type of the related parties' transactions, if any
- The value of the transactions
- The method used to determine the FMP and the reasons for selecting this method
- The country of origin for tangible and intangible goods
- The country of the supplier

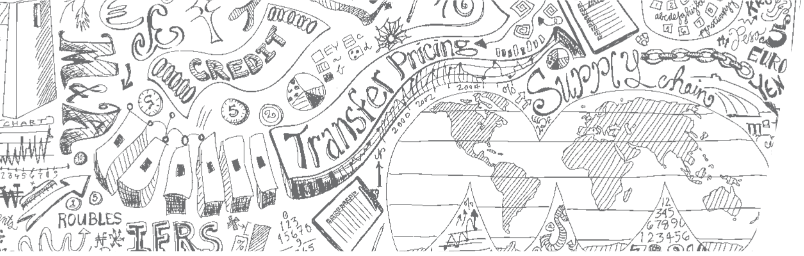
# Egypt (continued)

## Audit risk/transfer pricing scrutiny

No TP assessment has taken place as of this date. To the best of our knowledge the tax authority will demand that the taxpayer file a TP study starting in financial year 2010 along with the corporate tax return.

## APA opportunity

The head of the Administration may conclude agreements with associate persons using one or more methods for determining the neutral price in the Administration's dealings.




# Estonia

## Taxing authority and tax law

Tax authority: The Tax and Customs Board

Tax law:

- Estonian Income Tax Act Article 50 sections 4 – 6
- Article 53 section 46
- Article 14 section 7
- Article 50 section 7 - documentation requirements

Current Estonian transfer pricing legislation is effective as of 1 January 2007. Based on the amendments to the Income Tax Act, which are applicable as of 2011 (and not as of 2010 as initially anticipated), the definition of related parties shall be broadened, thus expanding the list of persons who must conclude transactions at arm's length to persons who have a common economic interest or a prevalent influence over another person.

Furthermore, persons formally not related based on the current Income Tax Act, but who in spite of the formal unrelated status undertake transactions that decrease the taxable income in Estonia, are considered from 2011 as related entities and should undertake transactions at arm's length.

## Relevant regulations and rulings

The Ministry of Finance issued a transfer pricing regulation on 10 November 2006 (No. 53), which came into force on 1 January 2007. The regulation sets out in more detail the principles for determining arm's length prices, and it also establishes documentation requirements. There have been a few court rulings and an increasing number of tax proceedings on transfer pricing issues in Estonia.

## OECD guidelines treatment

The tax authorities follow the OECD Transfer Pricing Guidelines. Nevertheless, the domestic legislation is the prevailing law.

## Priorities/pricing methods

The Tax and Customs Board accepts the CUP, Resale Price, Cost Plus, Profit Split, Transactional Net Margin methods or, if necessary, any other suitable method. The methods are not hierarchical and are all treated as equal. However, if available, internal and Estonian domestic data is preferred for determining arm's length prices.

## Transfer pricing penalties

If the required documentation or the relevant tax return is not submitted in time, the fine may be as high as EUR 3,200. In case of intentional submission of wrong information on the tax return that results in less tax paid, a criminal penalty may be imposed and the fine may be as high as EUR 15m. If tax is assessed, interest from the tax amount at the rate of 0.06% per day will be imposed retroactively as of the date when the tax was supposed to be paid.

## Penalty relief

There is no penalty relief if a taxpayer has the necessary documentation, but the transfer pricing is determined to be non-arm's length and there is an income tax adjustment. However, imposing a fine is probably more an exception than a rule. Interest for the delay of the tax fine payment is always enforced.

# Estonia (continued)

### Documentation requirements

All entities must be able to prove that transactions with related parties take place at arm´s length. Yet, an additional documentation requirement is imposed in the following cases if at least one of the preconditions is met:

- Resident credit institution, financial institution, insurance agency and listed company
- If one party of the transaction is a resident of a low tax rate territory
- Resident legal person or non-resident who has a permanent establishment in Estonia
  - who has more than 250 employees with related parties or
  - whose turnover, including related-parties, in the previous financial year was at least €50m or
  - whose consolidated net assets were at least €43m

Categories of documentation required:

- Company analysis
- Industry analysis
- Functional analysis
- Economic analysis

### Documentation deadlines

There is no deadline for preparing transfer pricing documentation. However, taxpayers are obliged to submit the documentation within 60 days upon the request of the tax authority.

### Statute of limitations on transfer pricing assessments

The statute of limitations period for making an assessment of tax is three years. In the event of intentional failure to pay or withhold an amount of tax, the limitation period for making an assessment of tax is six years. A limitation period starts from the due date of submission of the tax return, which was not submitted or which contained information that caused an amount of tax to be calculated incorrectly.

### Return disclosures/related-party disclosures

An annual report including a description of transactions with related parties is required to be filed within six months from the end of the relevant financial year. If the taxpayer has the obligation to prepare transfer pricing documentation, a respective analysis must be carried out per financial year.

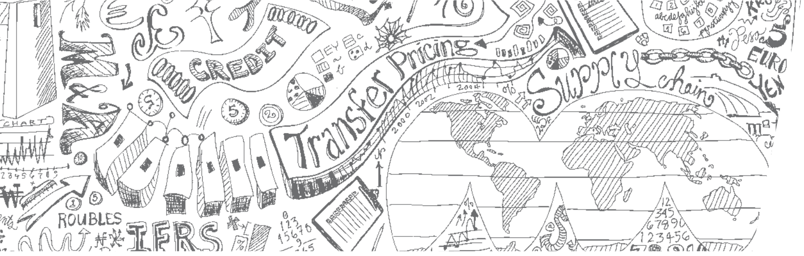
The documentation does not have to be filed with the tax return.

### Audit risk/transfer pricing scrutiny

The taxpayers in Estonia run a high risk that transfer prices will be scrutinized during a tax audit. However, today the overall transfer pricing tax risk for Estonian taxpayers can be evaluated as medium.

### APA opportunity

Currently, the Estonian tax laws do not provide any opportunity to conclude APAs. Yet, the transfer pricing methodology and the general approach for determining transfer prices can be verified with the authorities within the scope of a binding ruling request.




# Finland

## Taxing authority and tax law

Tax authority: Finnish Tax Administration

Tax law: Finnish Fiscal Assessment Act §§14 a-c, 31, 32, 75 and 89

## Relevant regulations and rulings

Government Proposal and Tax Administration's Guidelines of 19 October 2007

## OECD guidelines treatment

The Finnish regulations and tax practice in general follow the OECD Transfer Pricing Guidelines and the approaches presented in the OECD Discussion Draft on Business Restructurings.

Regarding the business restructurings, the Finnish Tax Administration's Guidelines state that the business restructurings should be examined as a whole from a transfer pricing perspective. However, the guidelines state that the specific circumstances and effects of the restructuring on the material functions of parties should be taken into account and the arm's length principle has to be utilized. Nevertheless, the guidelines are general in nature and do not specifically state how the tax authorities should consider individual cases.

There is no established case law on business restructurings in Finland. However, there have been some advance rulings relating mainly to the transfer and valuation of intangibles.

## Priorities/pricing methods

Taxpayers may choose any OECD transfer pricing method as long as the chosen method results in an arm's length pricing for the intra-group transaction. In its selection of the method, a taxpayer should take into consideration the aspects regarding the application of methods stated in the OECD Transfer Pricing Guidelines.

## Transfer pricing penalties

A tax penalty of up to €25,000 can be imposed for a failure to comply with the transfer pricing documentation requirements, even if the pricing of intra-group transactions has been at arm's length. In addition, the possible adjustment of taxable income may result in a separate tax penalty of up to 30% of the adjusted amount of income as well as penalty interest.

## Penalty relief

Penalties can be reduced or removed if the taxpayer presents supplementary transfer pricing documentation that supports the arm's length nature of the intra-group transactions. The determination of penalties will be made on a case-by-case basis.

## Documentation requirements

Transfer pricing legislation came into effect on 1 January 2007. The provisions contained in the law apply to financial periods beginning on 1 January 2007 or later.

The transfer pricing documentation aims to prove that the prices used in cross-border intra-group transactions are acceptable from the perspective of the tax authority. According to the law, the documentation obligation applies to the following entities:

- Group companies if the group employs at least 250 employees, regardless of the amount of turnover or assets
- Group companies if the group employs less than 250 employees and if the company's turnover exceeds EUR 50m and their assets are worth more than EUR 43m
- The Finnish branches of a foreign company if the above conditions are met by this company
- Companies which are not small- and medium-size enterprises, as defined by criteria (related to, for example, a company's independence) contained in the European Commission's Recommendation on the definition of micro, small- and medium-sized enterprises (2003/361/EC)

# Finland (continued)

## Documentation requirements (continued)

When calculating the amount of employees, turnover or assets of an enterprise or a branch owned by a foreign company, information regarding the foreign owners is also taken into account in pro rata.

Group companies are required to prove the arm's length nature of cross-border intra-group transactions by preparing transfer pricing documentation. According to the law, the documentation should contain the following information:

- A description of the business
- A description of associated enterprises
- Information on transactions between associated enterprises
- Functional analysis regarding transactions between associated enterprises
- A comparability analysis, including available information on comparables
- A description of the transfer pricing method and its application

Less extensive documentation is required if the total amount of transactions between two parties during a fiscal year does not exceed EUR 500,000.

## Documentation deadlines

A taxpayer has to submit the transfer pricing documentation for a specific fiscal year within 60 days upon a request of the tax authorities, but not earlier than six months after the end of the financial period. The additional clarifications concerning the documentation have to be submitted within 90 days of a request by the tax authorities.

## Statute of limitations on transfer pricing assessments

The time limit for the adjustment of income due to the failure to apply arm's length principles to the pricing of a transaction is five years from the beginning of the following year during which the taxation was finalized.

## Return disclosures/related-party disclosures

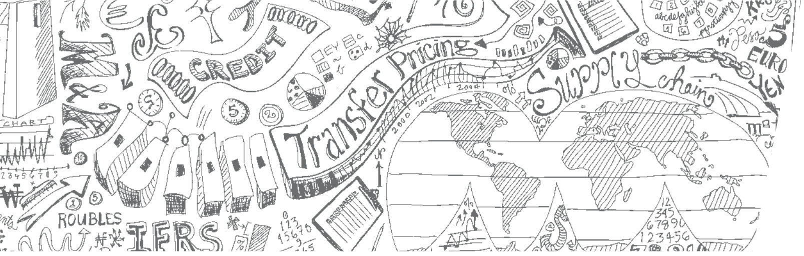
Based on Paragraph 26.4 of the Taxation Procedure Act, if the other party of the transaction is a non-resident, and if the tax authorities cannot obtain adequate information on the transaction by using an appropriate international treaty, the taxpayer is responsible for presenting such information.

## Audit risk/transfer pricing scrutiny

The tax authority is being very active and the risk for transfer pricing audit is high. All kinds of intra-group transactions have been under scrutiny in tax audits.

## APA opportunity

Advance rulings are available in Finland. There is no legislation for APAs; however, the tax authorities have indicated their willingness to utilize them.




# France

## Taxing authority and tax law

Tax authority: Generally referred to as the French Tax Authorities (FTA), or Direction Générale des Finances Publiques (DGFiP), or Direction Générale des Impôts (DGI)

Tax law, main technical provisions:

- French Tax Code (FTC) Articles 57 and 238A
- French Procedural Tax Code (FPTC) Articles L 10, L 13AA, L 13AB, L 13B, L 80B and L 188A
- Case law about application of the theory of Abnormal Act of Management
- Thin capitalization rules are also covered by Articles 212 and 39-1 of the FTC

## Relevant regulations and rulings

Administrative doctrine pertaining mainly to Articles 57 and 238A of the FTC, and Articles L 13B and L 80B of the FPTC.

Administrative guidelines are expected to be published in relation to the application of the new documentation requirement provided by Articles L 13AA and L 13AB FPTC.

## OECD guidelines treatment

The French Tax Authorities consider the French transfer pricing regulations to be consistent with the OECD Guidelines.

There is no specific French transfer pricing-related regulation pertaining to business restructuring or attribution of profits to permanent establishments, and the FTA did not comment so far the new guidelines released by the OECD (Transfer Pricing and Business Restructuring Guidelines of 22 July 2010).

Experience in business restructuring shows that tax auditors often consider that a decrease in profit is an indicator that an intangible has de facto been transferred and should be taxed. In addition, specific care should also be paid to closure costs in light of the transfer pricing profile undertaken by the group entities at hand. French tax inspectors are also paying more attention to financial transactions (e.g., loans, guarantees).

## Priorities/pricing methods

The tax authorities accept the CUP, Resale Price Method, Cost Plus Method, Profit Split and TNMM; yet tax inspectors usually prefer the TNMM.

## Transfer pricing penalties

Penalties specific to failure in complying with the TP documentation requirement apply in addition to fiscal penalties generally applied as a consequence of a transfer pricing reassessment. Indeed, transfer pricing reassessments from the FTA trigger an adjustment of the taxable profit for Corporate Income Tax purposes (and other taxes if depending on the case at hand).

**Penalties specific to the transfer pricing documentation requirement:**

Specific transfer pricing penalties are applicable in situations where the taxpayer failed to answer the tax authorities' request for documentation, either on the basis of Article L 13B FPTC (which relates to General TP documentation requirements), or on the basis of Articles L 13AA and L 13AB FPTC (which relate to newly published Special TP documentation requirements):

- Failure in providing complete information in the framework of Article L 13B FPTC

  (i) may result in a reassessment of the company's taxable profit based on information the tax authorities possess, and

  (ii) will result in the application of EUR 10,000 penalties for each year audited
- Failure in providing sufficient transfer pricing documentation under the framework of Articles L 13AA and L 13AB FPTC will trigger penalties amounting from €10,000 up to 5% of the transfer pricing reassessment potentially notified afterwards, depending on the "seriousness of the breach." Such penalties are due per fiscal year audited.

# France (continued)

## Transfer pricing penalties (continued)

**Penalties generally applied as a result of a transfer pricing reassessment, regardless of compliance with TP documentation requirements:**

- After a transfer pricing reassessment is made, the additional profit is usually analyzed as deemed dividends, therefore, a withholding tax on deemed distribution is usually required (when a double tax treaty applies, the withholding tax depends on the relevant tax treaty provisions.[1] In the absence of specific tax treaty, the withholding tax rate is generally 25%, and increased to 50% when the foreign entity is based in a "non-cooperative" jurisdiction).
- In case the transfer is qualified into a deemed dividend, the FTA also usually applies a 10% penalty for absence of declaration of the withholding tax. Such penalty is applied regardless of the good faith of the taxpayer.
- Late payment interests are applied in case of tax reassessments made on the ground of Article 57 of the FTC. The ordinary late payment interest rate is 0.40% per month (i.e., 4.8% per year).
- Supplementary penalties are applicable if the taxpayer committed a willful offence (40%) or acted fraudulently (80%)

In addition, the adjustment may result in a reassessment of other taxes and contributions such as business taxes and employee profit-sharing regimes.

## Penalty relief

During a tax audit and before the tax authorities send the notice of reassessment, taxpayers, under the framework of Article L 62 FPTC, are allowed to correct their errors or omissions in consideration of a reduced late payment interest rate (3.36% per year) that is equal to 70% of the ordinary late payment interest rate. In this respect, taxpayers must file a complementary tax return and pay the corresponding additional taxes at the same time.

## Documentation requirements

### General TP documentation requirements (Article L 13B FPTC)

The FTA may require information pertaining to transfer pricing in the course of an audit (based on Articles L 13 B and L 10 FPTC). The nature of the required information, and the short deadline under which a taxpayer may have to provide it, lead to a de facto documentation requirement covering any French-based company. The following documents are usually expected:

- Business and organizational structure overview
- Functional analysis, contracts, legal and management account information
- Method selected and economic analysis (including as need be, identification of competitors and comparables, usually French when the tested party is French)
- Description of the tax regime applied to the subsidiaries of the audited French company

### Special TP Documentation Requirement newly published (Articles L 13AA and L 13AB FPTC)

Pursuant to Article L 13AA FPTC, and as from fiscal years opened from 1 January 2010, companies that satisfy any of the criteria listed below, must provide upon the tax inspector's request (hence in the context of a tax audit) their transfer pricing documentation:

- Have total net sales (before taxes), or total gross assets, equal to or greater than EUR 400 million
- Hold, directly or indirectly, at the closing date of the fiscal year, more than 50% of the capital or voting rights in a legal person having such turnover or gross assets
- Are, on the closing date of the fiscal year, more than 50% held, directly or indirectly, by such a legal person
- Are included in a group benefiting – subject to a ruling – from the worldwide tax consolidation regime, every French company being included in the regime
- Belong to a French tax consolidated group that includes at least a legal person that meets one or more of the aforementioned criteria

[1] See the Dividends or the Other Income clauses.

# France (continued)

## Documentation requirements (continued)

If the documentation is not immediately provided to the FTA, it should be delivered within 30-days from the FTA's request. In case of absence of documentation, or if the taxpayer fails to provide an exhaustive and comprehensive documentation within 30 days of a formal notice from the FTA, a penalty up to 5% of the transfer pricing reassessment would be applied with a minimum of EUR 10,000 per fiscal year under audit. An extra deadline to complete the documentation could however be granted by the FTA, yet administrative guidelines in this regard were not yet published to date.

The contents of the transfer pricing documentation to be made available to the FTA upon tax audit are twofold:

1. General information concerning the related enterprises (economic, legal, financial background of the group):
    - General description of the activity carried out, including changes that occurred during the audited period compared to previous years;
    - General description of the legal and operational structures (with identification of the entities involved in controlled transactions);
    - General description of the functions carried out and risks borne by the related entities to the extent that they impact the audited company
    - List of the main intangible assets held in relation to the audited company
    - General description of the transfer pricing policy of the group
2. Specific information pertaining to the audited company:
    - General description of the activity carried out including changes that occurred during the audited period compared to previous years
    - General description of the transactions carried out with related enterprises including amount and nature of the flows including royalties
    - List of the cost-sharing agreements, copy of transfer pricing rulings
    - Presentation of the methods used to determine the transfer prices (including an analysis of the functions, risks and assets and with an explanation on the choice of applied methods)
    - Where necessary, an analysis of the comparables used (including characteristics of the goods and services, functional analysis, contract clauses, economic situation and specific strategies of the companies used as comparables)

Pursuant to Article L 13AB FPTC, all French companies involved in transactions with companies located in non-cooperative jurisdictions (as defined by the Article 238-0 A FTC) have to provide, in addition to the documentation described in article L 13AA FPTC, a complementary documentation including all documents normally required by the FTA from companies subject to Corporate Income Tax, and such requirement notably includes French-accounting-compliant balance sheet and P&L of the foreign company.

French taxpayers that do not meet the conditions set out in Articles L 13AA and L 13AB FPTC nevertheless remain bound by the General TP documentation requirements set out in Article L 13B FPTC and the general information sharing rule set out in Article L 10 FPTC.

## Documentation deadlines

### General TP Documentation Requirement (Article L 13B FPTC)

Upon the FTA's request, documentation must be submitted within 60 days, though it may be possible to obtain a 30-day extension in exceptional circumstances. Exceeding such deadline will trigger penalties as mentioned previously.

### Special TP Documentation Requirement newly published (Articles L 13AA and L 13AB FPTC)

Upon the FTA's request, documentation must be submitted immediately upon first request made by the tax inspector in the course of an audit. If not, the FTA will send a formal claim for the documentation that will provide for a 30-day deadline after which penalties for documentation failure will apply as previously mentioned.

# France (continued)

## Statute of limitations on transfer pricing assessments

The statute of limitations for transfer pricing adjustments is the same as for all French corporate tax assessments: generally three years following the year for which the tax is due (it might be longer under certain circumstances e.g., permanent establishment qualifications, losses carried forward).

In cases where a mutual agreement procedure to avoid double taxation (on the ground of a tax treaty or the European Arbitration Convention) is initiated further to a tax reassessment, tax collection can be suspended during the entire mutual agreement process and is postponed until the competent authorities reach an agreement (Article L 189 A FPTC).

## Return disclosures/related-party disclosures

In the event of a specific request from the tax authorities at the time of an audit (on the basis of either Articles L 13AA and L 13AB FTPC, or Article L 13B FPTC), there is an obligation to disclose the nature of the relations involving the taxpayer with related parties (i.e., the links of dependence between the French audited entity and the related parties). These legal provisions also provide for an obligation to disclose the activities of the related parties.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being scrutinized during a tax audit is high. The number of tax audits in transfer pricing is considerably increasing, and the FTA are becoming more extensive and accurate in their queries since they now also use economic references in addition to legal grounds.

**Transfer pricing issues that receive the greatest scrutiny are:**

- Business restructuring (e.g., transfer of intangibles, indemnity) or a sudden decrease into the operating margin likely to hide a change in the TP policy applied
- Product sale prices (under or over estimated prices), especially but not only, in case of losses
- Management fees
- Agents and commissionaire operations (e.g., conversion of a distributor into an agent)
- Permanent establishment
- Closure/conversion costs
- Intangibles and economic ownership (including questions about royalties)
- Benchmarking exercises

There are rather few court decisions in France going into detailed TP issues. One of the main questions relates to the burden of proof, which is usually said to be lying on the tax inspectors.

# France (continued)

## APA opportunity

Bilateral and, under certain circumstances, unilateral APAs, are available (Article L 80 B 7° of the FPTC). This section was provided by the Finance Amendment Act for 2004 and has come into force since 1 January 2005. It incorporates existing procedures as described by the French administrative guideline #4 A-8-99 dated 7 September 1999. A specific procedure also exists for certain activities (e.g., headquarter profile).

On 28 November 2006, the tax authorities released a new administrative guideline (#4 A-13-06), adding a simplified APA procedure for small and medium enterprises, and presenting an online guide pertaining to transfer pricing methods.

The process requires that, in theory, the submission has to be performed at the latest 6 months before the beginning of the first fiscal year covered. It has also to be noted that there is no roll-back possibility.

## Mutual Agreement Procedures

Besides and following a tax reassessment, taxpayers can request the introduction of a mutual agreement procedure (on the ground of tax treaty or the European Arbitration Convention) in order to avoid double taxation resulting from the reassessment. On 23 February 2006, the FTA published administrative guidelines (#14 F-1-06) specifying the scope and the conditions to be met for the introduction of such procedure.

Regarding the Specific TP documentation requirements set out in Articles L 13AA and L 13AB, soon to-be-published administrative guidelines should define whether the penalties applied for documentation failure would not prevent taxpayers from being able to apply for a mutual agreement procedure.


# Germany

## Taxing authority and tax law

Tax authority: German taxes are administered either by the German Federal Central Tax Office (Bundeszentralamt für Steuern) or by German state tax authorities

Tax law: German tax law is found in tax acts, executive order laws, double taxation treaties and supra-national norms

## Relevant regulations and rulings

The German tax law assesses intercompany transactions by following the arm's length principle (§1 Foreign Tax Act). The German interpretation of the arm's length principle generally follows the definition in Article 9 of the OECD Model Tax Convention. However, a practically relevant exception, §1 Sentence 2 Foreign Tax Act, stipulates that for the interpretation of the arm's length principle it is assumed that both parties involved in an intercompany transaction have full knowledge about all and the same facts and circumstances (information transparency).

Detailed transfer pricing regulations concerning the cross-border transfer of functions were incorporated into §1 Foreign Tax Act since 1 January 2008. An Executive Order Law providing details on how the new transfer pricing provisions relate to business restructurings and function transfers is effective from 2008 onwards.

In October 2010 new Administration Principles were released that include 81 pages of clarifications concerning the application of §1(3) of the Foreign Tax Act and the Executive Order Law on Transfer of Business Functions. The Administration Principles detail, for example, exemption rules due to which a business restructuring and function transfer does not lead to a taxable valuation of a so called "transfer package." Such cases are, amongst others, cases where the receiving entity of a function exclusively performs the transferred function for the transferring entity and receives a cost-based remuneration (i.e., based on the cost plus method or a cost based TNMM), in accordance with the arm's length principle. In such cases, it is assumed that the transfer package did not include any significant intangible property and other advantages that were transferred and, thus, a valuation of the transfer package is not required. This exception from examination of the transfer package basically affects the transfer of routine functions whose execution is connected with low risks which, as a consequence, are usually remunerated on the basis of the cost-plus method.

Other relevant provisions for transfer pricing issues in German tax law are:

- Section 8 (3) German Corporate Income Tax Act (hidden profit distribution)
- Section 4 (1) German Income Tax Act with Directive R40 of the German Corporate Tax Directives (hidden capital injection)
- Sections 90 (3), 162(3) and 162(4) German General Tax Code and the Executive Order Law to §90(3) German General Tax Code

To help interpret the above outlined provisions, the German tax authority issued a circular on the *Principles Governing the Examination of Income Allocation between Multinational Enterprises* in 1983, known as the Administration Principles. The Administration Principles do not constitute binding law for taxpayers or the courts but are binding for the tax authority and, thus, serve as an indication to taxpayers as to how the tax authority will treat specific intercompany transactions between related parties. The purpose of the Administration Principles can be interpreted as to provide a directive concerning the tax audit treatment of transfer pricing cases and to ensure the uniform application of rules and methods by the tax authorities.

In addition to the Administration Principles, administration circulars concerning income allocation with regard to cross-border secondments of personnel, costs contribution arrangements, permanent establishments and procedures have been published since December 1999.

## OECD guidelines treatment

The tax authority considers its transfer pricing laws and regulations to be consistent with OECD guidelines. The OECD guidelines provide support for domestic use but do not constitute binding law in Germany; however, German transfer pricing regulations and practices differ with regard to certain issues (e.g., the application of transactional profit methods and documentation requirements, and the treatment of shifts of functions).

# Germany (continued)

## Priorities/pricing methods

Under the arm's length principle, it is assumed that the taxpayers have acted in a manner comparable to unrelated parties. This assumes that all material information about the transaction (complete information about the counterparty) is available and that the parties acted as prudent and diligent business managers.

Under the new law (effective 1 January 2008), the application of transfer pricing methods is dependent on the availability and quality of third-party comparable data. Three different situations are distinguished: full comparability of the data, limited comparability of the data and non-availability of third-party comparable data.

When full comparability of third-party data exists, the new law stipulates the priority of the traditional transaction methods: CUP, Resale Price and Cost Plus. Any price within the full range of full comparable third-party data meets the arm's length principle.

If limited comparability exists, Germany allows all OECD methods, i.e., the aforementioned traditional methods and the transactional profit methods TNMM and (residual) profit-split. In case of limited comparability, third party comparable data must be adjusted (i.e., by statistical procedures).

If no comparable data exists, the law stipulates that taxpayers have to conduct the hypothetical arm's length comparison to derive arm's length transfer prices. Accordingly, in compliance with the so-called prudent and diligent business manager principle, and based on the functional analysis and internal projections, the taxpayer has to establish an area of "hypothetical" arm's length prices. The area of negotiation is defined by the minimum price of a hypothetical seller and by the maximum price of a hypothetical purchaser. The taxpayer must prove the value with the highest probability within the area of negotiation, otherwise the mean value is assumed to be the arm's length transfer price for the transaction under review.

## Transfer pricing penalties

If a taxpayer does not comply with its duty to document its transfer pricing to the extent outlined in §90(3) German General Tax Code, a refutable presumption applies according to which the income of the German company under review has been reduced by means of inappropriate transfer prices, which forms the basis of a transfer pricing adjustment by the tax authority.

Tax authorities may apply §162(3) of the German General Tax Code if the taxpayer submits no or only insufficient documentation or if exceptional transactions have not been recorded contemporaneously. In all three cases, the tax authority is authorized to estimate the income, provided that the taxpayer cannot rebut the presumption. This holds also true if a taxpayer does not disclose relevant data only available at foreign related parties.

The legislation takes into consideration that an appropriate single transfer price does not exist and that comparable third-party prices may vary within price ranges. However, it explicitly entitles the tax authority to make use of the full price range estimating the income, in case of insufficient documentation, to the detriment of the taxpayer.

If the taxpayer fails to submit transfer pricing documentation or if the documentation is unusable or insufficient, or if the documentation for extraordinary business transactions is not prepared contemporaneously, a surcharge of 5%-10% on the income adjustment will be applied, with a minimum surcharge of €5,000. For late filing, the taxpayer faces a penalty up to €1m (minimum penalty of €100 per day of delay). Penalties are imposed after the closing of a tax audit. The aforementioned penalties constitute non-tax deductible expenses.

Under the law effective 1 January 2008, in the event that the taxpayer's transfer price falls outside the full range (in case of full comparability of third-party data) or the interquartile range (in case of limited comparability of third-party data) of arm's length prices, the transfer price is adjusted to the median of the range.

Interest is assessed on tax payments (6% per annum, which is non-deductible for tax purposes).

There are also penalties for tax evasion.

# Germany (continued)

## Penalty relief

The taxpayer is required by law to present utilizable documentation to the tax authority. Accordingly, no penalty relief applies.

## Documentation requirements

Section 90 of the German General Tax Code contains transfer pricing documentation requirements. For the documentation of transfer pricing issues, an Executive Order Law (effective 30 June 2003) prescribes general requirements and the documentation required in special circumstances. A circular (Administration Principles - Procedures) dated 12 April 2005 provides the tax authority's interpretation of the requirements set out in the General Tax Code and in the Executive Order Law.

**General documentation requirements are:**

- General information: shareholder relationships, organizational and operative group structure and operations
- Description of intercompany transactions: manner and extent of transactions, intercompany contracts and a list of important intangibles
- Functions and risks analysis: description of functions and risks the taxpayer bears within the intercompany transaction, contractual terms, business strategies and value chain
- Transfer pricing analysis: selection of the transfer pricing method, appropriateness of the method selected, calculation of the transfer price, list of comparables and documentation of adjustment calculations

**Special documentation requirements:**

The taxpayer has to document special circumstances which are used to substantiate the arm's length nature of the price determined, including: special business strategies, business restructurings, cost contribution agreements, overview of APAs and mutual agreement procedures, information on transfer price adjustments, causes for losses from intercompany transactions, as well as countermeasures (if losses occur in more than three consecutive financial years).

## Documentation deadlines

Contemporaneous documentation requirements exist only for exceptional business transactions. For extraordinary business transactions (e.g., legal restructuring within the group), the documentation must be contemporaneous (i.e., prepared within six months of the end of the business year in which the transaction has occurred). However, the preparation of contemporaneous documentation is strongly recommended for all cross-border transactions.

Documentation must be submitted within 60 days upon receipt of the tax authority's request. In the case of extraordinary business transactions (e.g., transfer of functions), documentation must be submitted within 30 days of the tax authority's request. In general, the request is made in the course of a tax audit.

## Statute of limitations on transfer pricing assessments

There are no special time limit provisions applicable if intercompany transactions are involved. The general regime of the statute of limitations applies in accordance with the General Tax Code. Accordingly, each case has to undergo careful consideration to determine the specific statute of limitations. Most taxes are levied by way of assessment. Assessments can only be made within the statutorily prescribed assessment period, which is subject to the statute of limitations for assessments. The assessment period for taxes (§169 General Tax Code) is four years. For customs duties, it is shorter, and in case of grossly negligent evasion of taxes or tax fraud, it is much longer (10 years in the case of tax fraud). These periods commence at the end of the calendar year in which the tax liability arose. The assessment period, however, does not start prior to the end of the calendar year in which the taxpayer has submitted the tax return (but also does not start later than three years after the year the tax liability has arisen). There are a number of statutory exceptions to the statute of limitations for assessments (e.g., it should be kept in mind that the limitation period is interrupted when a tax audit begins).

Section 175a General Tax Code stipulates that tax assessments can be amended due to the result of a MAP/EU arbitration procedure up to one year after the effective date of such agreement irrespective of whether the aforementioned statutes of limitations have expired before.

# Germany (continued)

## Return disclosures/related-party disclosures

There are no specific disclosure requirements.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being scrutinized during a tax audit is high and continuously rising. Due to the documentation requirements, and in the light of the new stricter law effective 1 January 2008, it is expected that transfer pricing issues attract significantly more attention in tax audits than in the past. It is expected that transactions qualifying as exceptional business transactions under the documentation provisions, such as the transfer of functions and risks, particularly attract the tax auditors' attention. Further, many tax audits increasingly focus on (brand) royalty charges and management services cost allocations into Germany.

## APA opportunity

APAs are generally available. The German Ministry of Finance issued an APA circular on 5 October 2006 which defines the APA procedures and provides guidance with regard to the negotiation of APAs. Additionally, the Annual Tax Act 2007 introduced fees for APAs. The administrative competence for APAs is centralized in the Federal Central Tax Office. The APA process typically takes from one-and-a-half years to several years from application to conclusion. An agreement reached between two competent authorities will be made conditional in two regards: the taxpayer must consent to the intergovernmental agreement, and must waive its right to appeal against tax assessments to the extent that they are in line with the contents of the APA.


# Greece

## Taxing authority and tax law

Tax authorities: The Ministry of Development and the Ministry of Finance

Two separate sets of law and authorities regulate the Transfer Pricing Documentation requirements. The Ministry of Development has introduced Transfer Pricing Documentation Rules by Law 3728/18-12-2008 and the Ministerial Decision A2- 8092/31-12-2008, applicable for the fiscal years 2008 and onwards. Within the aforementioned legislative framework, the Ministry of Development is the auditing authority of the TP rules, while in case of identification of TP infringements the case is referred to the supervising tax authorities for the application of the relevant provisions of the tax legislation and the imposition of the relevant tax sanctions.

## Relevant regulations and rulings

In addition, Transfer Pricing Documentation rules were introduced also by Ministry of Finance (L.3775/2009, applying for fiscal years 2010 and onwards). No Ministerial Decision has been issued yet to this end.

## OECD guidelines treatment

The aforementioned legislative framework confirms the applicability of the OECD Transfer Pricing Guidelines.

The Ministry of Development and the Ministry of Finance, the two Greek supervising authorities of intra-group transactions, recognize the OECD guidelines and consider their transfer pricing laws and decisions to be consistent with OECD guidelines. However, due to the limited time period since the Greek TP Law was approved by the Greek Parliament and applied in the Greek market, the tax audit treatment of transfer pricing cases cannot be ascertained, nor is it known whether the tax authorities will follow the uniform application of rules and methods.

## Priorities/pricing methods

The tax authorities follow the OECD Transfer Pricing Guidelines. All three of the traditional transactional methods (CUP, Resale Price and Cost Plus) can be applied while the use of profit-based methods is possible where substantiated. In particular, other (non-traditional) transfer pricing methods such as the TNMM and the Transactional Profit Split Method can be used only in the cases where the use of the above traditional transfer pricing methods are considered ineffective, provided that a detailed justification is included in the documentation files.

## Transfer pricing penalties

In accordance with the Ministry of Development TP Documentation Rules, a penalty equal to 10% of the value of the transactions for which no file has been submitted to the auditing authorities or for which the lists of intra-group transactions have not been submitted timely is imposed. The Ministry of Finance also imposes a penalty equal to 20% of the value of the transactions (with the possibility of reducing it to one-third), in case no file is submitted to the tax authorities or the submitted data are insufficient. Either the case is initially examined by the Ministry of Development or the Ministry of Finance, if an infringement of the arm's length principle is assessed from the audit report, the supervising tax authorities impose the relevant tax sanctions, i.e., any price difference (over-or under-invoiced amount) deemed to be an accrued profit for the respective enterprise will be included in its actual profits and be taxed accordingly. Additionally, a penalty equal to 20% of the price difference assessed will be imposed, regardless of any other penalties applicable for inaccurate tax return filings. In addition, if the case is examined by the Ministry of Development, a fine of €5,000 and penal sanctions are triggered.

# Greece (continued)

## Penalty relief

The Ministry of Development provides that the decision of the Head of the Market Supervision Authority is given to the company under audit within 30 days of its issuance. The above decision may be challenged by means of recourse to the Ministry of Development within five working days of its receipt by the audited company. The Minister of Development should decide within 10 working days of the filing of the recourse. In case of rejection of the recourse by the Minister, the audited company is entitled to appeal against the negative decision by filing recourse to the competent Administrative First Instance Court within 60 days of its formal notification of the company. The recourse to the Administrative Court is legally acceptable provided that 20% of the fines and penalties assessed to the company is paid.

The Ministry of Finance provides that the penalty equal to 20% of the value of the transactions for the non-submission of file may be reduced to one third.

## Documentation requirements

For the purposes of assessing the compliance of the liable companies with the arm's length principle, the following documentation files should be available upon request of the supervising authorities of either the Ministry of Development or the Ministry of Finance within 30 days, from the notification of such request.

With respect to groups of companies with a Greek parent company, the Master Documentation File should include the following information:

**Group-related information:**

- The organizational, legal and operational structure of the Group, including any permanent establishments and interests in partnerships, as well as general background information of the Group's industry and the financial data relating to it
- General description of the Group activity, the business strategy, including changes of the business strategy as compared to the previous financial year
- General description and implementation of the Intra-Group transfer pricing policy, if applicable.
- General presentation of transactions concluded between the Greek parent company and its affiliated companies (Greek or foreign), as well as of the transactions among the affiliated companies, if one of these is Greek, namely:
  - Nature of transactions (e.g., sale of goods, provision of services, financial transactions)
  - Invoices' flows
  - Amounts of transaction flows

The description of the affiliated companies or of their permanent establishments that enter into the above transactions shall include:

- The scope of their activities, the years of operations, the annual turnover, the number of employed personnel, etc.
- General description of functions and risks undertaken by the affiliated companies, including the changes incurred to this end as compared to the previous year.

In addition, a general description of the tangible assets used by the Group for the purposes of carrying out the above functions:

- The ownership of intangibles (e.g., patents, trademarks, brand names, know-how) and royalties paid or received.
- List of any Advance Pricing Agreements concluded by the Group companies with foreign tax authorities.

**Company-related information:**

- A detailed presentation of the transactions with associated companies for which the obligation documentation exists:
  - Nature of transactions (sale of goods, provision of services and financial transactions)
  - Invoice flows
  - Amounts of transaction flows

# Greece (continued)

## Documentation requirements (continued)

- Comparative analysis:
  - Characteristics of goods and services
  - Functional analysis (e.g., functions, risks, used fixed assets)
  - Contractual terms
  - Economic circumstances
  - Specific business strategies
- Description of the transfer pricing method implemented from among those specified in the OECD Transfer Pricing Guidelines as well as reasoning on the selection criteria thereof
- Relevant information on internal and/or external comparables, if available
- Description of other data or circumstances that are deemed to be relevant

With respect to groups of companies with a foreign parent company as well as foreign companies operating with any type and legal form in Greece, the Greek Documentation File should include the same information as listed above for Greek parent companies, with the following exceptions:

**Group-related information for companies with a foreign parent should include:**

- A general presentation of transactions concluded between the Greek company (or the Greek branch) and the affiliated companies (Greek or foreign), namely:
  - Nature of transactions (e.g., sale of goods, provision of services, financial transactions)
  - Invoices' flows
  - Amounts of transaction flows

**Company-related information for companies with a foreign parent should include:**

Description of the affiliated companies or of their permanent establishments that enter into those transactions or agreements:

- Description of the transfer pricing method implemented from among those specified in the OECD Transfer Pricing Guidelines as well as reasoning on the selection criteria thereof
- Relevant information on internal and/or external comparables, if available
- Description of other data or circumstances that are deemed to be relevant

## Documentation deadlines

The liable companies should submit annually to the Ministry of Development, within four months and 15 days of their fiscal year-end, a list with the details of their intra-group transactions, including especially the number and the value thereof.

The above-mentioned documentation files should be made available upon request from the supervising authorities of the Ministry of Development and within 30 days from the notification of such request.

In the context of a tax audit performed by the Ministry of Finance, the documentation data in accordance with the law of the Ministry of Finance should be made available to the tax authorities within reasonable time of no less than 30 days.

## Statute of limitations on transfer pricing assessments

Documentation files must be kept by the liable companies for a period equal to the prescription period of the State's right to impose tax (statute of limitations), as the latter is specified by the provisions of tax legislation.

# Greece (continued)

## Return disclosures/related-party disclosures

The liable companies disclose their intra-group transactions through the submission of a list to the Ministry of Development, annually. In particular, the list should be filed within four months and 15 days from their fiscal year-end (as stated above in "Documentation deadlines").

## Audit risk/transfer pricing scrutiny

Transfer pricing audits are expected to become more frequent and intensive. It is likely that the tax authorities will try to increase revenue through the imposition of penalties on companies that are not complying with transfer pricing requirements.

## APA opportunity

Currently, the use of APAs is not permitted. It is expected that the introduction of APAs will be discussed in the near future. However, a unilateral APA procedure has been introduced that addresses intra-group service centers operating for the exclusive benefit of affiliates abroad. Under this proposal, after filing an application with the tax authorities, the entities may be taxed on a cost plus basis, using an agreed markup, for a period of up to five years.


# Hungary

## Taxing authority and tax law

Tax authority: The Hungarian Tax and Financial Control Office

Tax law:

- Act LXXXI of 1996 on Corporate Income Tax (CIT) and Dividend Tax (Act on CIT)
  - Section 4.23 - definition of related party for CIT purposes
  - Section 18 - correction of prices applied between related parties
  - Section 31(2) - reference to the OECD TP Guidelines
- Act XCII of 2003 on Tax Procedure (Act on Tax Procedure)
  - Section 1.8 - definition of fair market price
  - Section 23(4)(b) - reporting related parties to the tax authority
  - Sections 132/A and 132/B - provisions on the Hungarian APA
  - Section 178.17 - definition of related party
- Section 259.13 within Act CXXVII of 2007 on Value Added Tax (Act on VAT) defines a non-independent party for VAT purposes
- Section 3.69 within Act CXVII of 1995 on Personal Income Tax (PIT) defines independent party for PIT purposes
- Ministry of Finance Decree 38 of 2006 on the administrative procedure for obtaining an APA
- Ministry of Finance Decree 22 of 2009 on the fulfillment of transfer pricing documentation obligations effective from 1 January 2010 and to be first applied to tax liabilities for 2010[1]

## Relevant regulations and rulings

- 37/2004 Guideline issued by the tax authority on the fulfillment of the transfer pricing documentation requirement
- 55/2006 Guideline issued by the tax authority on the application of the Transactional Net Margin Method
- 77/2007 Guideline issued by the tax authority on the preparation of consolidated transfer pricing documentation
- 139/2007 Guideline issued by the tax authority on the application of transfer pricing methods in practice
- 17/2008 and 48/2007 Guidelines issued by the tax authority on the preparation of simplified transfer pricing documentation and default penalties
- 13/2008 Guideline issued by the tax authority regarding when related party relations should be determined
- 16/2010 Guideline issued by the tax authority on changes to the definition of related parties from 2010
- 21/2010 Guideline issued by the tax authority on the adjustment related party items in connection with the assumption of loan and waiver of receivables
- 41/2010 Guideline issued by the tax authority on the adjustment of the prices for in-kind contributions

## OECD guidelines treatment

The Act on CIT contains specific reference to the OECD guidelines. Recent tax authority practice is that if the Hungarian tax laws do not include regulations on specific issues, the OECD guidelines may be used as primary reference.

[1]Containing the new provisions with regard to the EU Masterfile concept.

# Hungary (continued)

## Priorities/pricing methods

The OECD guidelines changed in July 2010. The Act on CIT has implemented these guidelines effective as of 1 January 2011. Accordingly, the three traditional methods (the CUP method, the resale price method and the cost plus method) and the profit-based methods recommended by the OECD, i.e., the transactional net margin and the profit split method are now practically equivalent. In addition, other methods can also be chosen, but only subsequent to the rejection of the five major methods.

## Transfer pricing penalties

A penalty of 50% of the unpaid tax may be imposed, as well as a late payment interest charge at double the prime rate of the National Bank of Hungary, in line with general rules. A default penalty up to HUF2m (approximately EUR 7,300) may be levied for not fulfilling, or not properly fulfilling, the content and formal documentation requirements. The HUF2m default penalty is applicable on each set of documentation and on each year under tax audit.

## Penalty relief

No penalty relief is applicable.

## Documentation requirements

The Act on CIT states that companies that do not qualify as small companies (small companies are defined as employing fewer than 50 persons and having less than €10m in total turnover on a consolidated basis) must document the methods they used to determine the fair market prices, as well as the facts and circumstances supporting them. The detailed documentation obligation must be applied for all agreements in effect and where there was a supply in the tax year. The details of the documentation obligation are regulated by the Ministry of Finance Decree 22 of 2009. Foreign entities (usually foreign taxpayers engaged in business activities through a Hungarian permanent establishment) are also subject to the documentation obligation. However, according to the relevant transfer pricing regulation, there is an option to prepare simplified documentation if the value of the transactions does not exceed HUF50m.

The Hungarian transfer pricing documentation requirements are consistent with the OECD Transfer Pricing Guidelines. The following list outlines the compulsory elements of the Hungarian transfer pricing documentation:

- Name, registered seat (official location) and tax number (or company registration number and the name and seat of the registering authority) of the related party
- Content of the agreement with the related party, which includes:
  - Subject of the agreement
  - Signing date (amendment date) of the agreement
  - Period during which the agreement is effective
  - Characteristics of the service provided and/or goods sold (functional analysis)
  - Method and terms of the fulfillment of the agreement
- Analysis of the market (industry analysis)
- The method applied for establishing the arm's length price
- Reasons for selecting the method applied
- Description of comparable services and goods transactions
- Factors affecting the arm's length price, margin or profit and the extent of any necessary adjustments

# Hungary (continued)

## Documentation requirements (continued)

- The arm's length price or margin
- Information on pricing agreements and court procedures
- Preparation date of the documentation

According to the Ministry of Finance Decree 22 of 2009, a taxpayer can choose to prepare a separate or a joint documentation. By introducing the joint transfer pricing documentation option, the Decree essentially adopted the regulations regarding the Masterfile concept as included in the EU's Code of Conduct on transfer pricing documentation. The joint documentation consists of two parts: common documentation containing standard information on the members of the group within the EU (i.e., Masterfile) and specific documentation describing the agreements concluded between the Hungarian taxpayer and its related parties. Taxpayers must declare to the tax authority (on the CIT return) which type of transfer pricing documentation they would like to prepare (either single or joint documentation).

The common document has to be prepared with respect to the member states of the European Union and should also include the controlled transactions carried out between third-country companies and EU group companies.

**The obligatory elements of the common documentation are the following:**

- A general description of the business and the business strategy of the enterprise including the changes from the previous year
- A general description of the organization, the legal and operational structure of the group (including an organizational chart, a list of the group members, and a description of the parent company's participation in the operation of its subsidiaries)
- A list of the related parties carrying out controlled transactions with group members within the EU
- A general description of controlled transactions (list of the significant controlled transactions, e.g., sale of tangible fixed assets, provision of services, development of intangible assets and provision of financial services including the values of these transactions)
- A general description of the functions and risk, and the changes in these compared to the previous year
- Information on the ownership of intangible assets and on royalties paid and received
- A description of the group's transfer pricing policy or transfer pricing system
- Cost contribution agreements and APAs relating to the determination of the arm's length price and court decisions on the arm's length price
- Date of preparation and modification of the documentation

**The specific document must include the following information:**

- Name, registered seat (official location) and tax number (or company registration number and the name and seat of the registering authority) of the related party
- Description of the business enterprise and the strategy of the business enterprise including the changes compared to the previous year
- Subject of the agreement, description of the transactions, value of the transactions, signing date (amendment date) of the agreement, period during which the agreement is effective
- Comparable search (characteristics of the service provided and/or goods sold, functional analysis, contractual conditions, economic circumstances)
- Description of the comparable data
- Transfer pricing policy of the group
- Preparation date and modification date of the documentation

For 2009 and onwards, the documentation can also be prepared in a foreign language. However, at the tax authority's request, the taxpayer has to prepare a Hungarian translation.

# Hungary (continued)

### Documentation deadlines

The transfer pricing documentation for contracts effective in a given tax year has to be prepared by the deadline for filing the annual corporate income tax return (within 150 days of the year-end).

### Statute of limitations on transfer pricing assessments

General rules apply. The statute of limitations lapses on the last day of the fifth calendar year calculated from the tax year in which taxes should have been declared, reported or paid in the absence of a tax return or reporting. However, within the frame of the Arbitration Convention, there is a possibility to request a tax base adjustment even after the statute of limitation has expired.

### Return disclosures/related-party disclosures

Within 15 days of concluding its first contract with a related party, the taxpayer must report the name, registered seat and tax number of the contracting party to the tax authority.

In the CIT return, the tax base should be adjusted if the price used in the related-party transaction differs from the fair market price. In their year-end corporate tax returns taxpayers must declare which type of transfer pricing documentation they have selected to prepare.

According to Hungarian transfer pricing regulations, the taxpayer is not required to file the transfer pricing documentation with the tax authority; however, the taxpayer needs to present the documentation during a tax audit.

The Financial Statements of companies include certain compulsory disclosures on related-party transactions.

### Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being scrutinized during a tax authority audit is steadily growing. Since the decree on the documentation obligation came into force the tax authority checks the existence of the documentation. Based on our experience, the tax authority usually inspects whether the content and formal requirements are fulfilled in the documentation. Since the beginning of 2007, the tax authority has started to train transfer pricing specialists. The tax authority's knowledge of the application of transfer pricing methods is expected to increase during the tax audits.

Overall, the risk of a transfer pricing audit can be set at medium. The tax authority focuses on reviewing the transfer pricing documentation in the framework of almost every tax audit. As a result, significant default penalties are levied if the transfer pricing documentation is missing or incomplete. Recently, there has been a tendency that the tax authority challenges not only the formal criteria of the transfer pricing documents but also the transfer prices themselves.

The tax authority focuses on transactions carried out by loss-making and/or large taxpayers especially where the taxpayer came to an unusual conclusion regarding the transfer prices or:

- If the pricing method is unusual
- Where the transactions themselves can be regarded as unusual or unique

Based on our experience, the tax authority makes an effort to challenge transfer prices in almost all of the instances listed above.

### APA opportunity

On 1 January 2007, a formal APA regime was introduced in Hungary. Unilateral, bilateral and multilateral APAs are available according to the new provision. APAs requested for future transactions can be used for three to five years and they can be extended for a further three years. The application fees for APAs range from HUF500,000 (approximately €1,825) to HUF10m (approximately €36,500) depending on the type of APA and the transaction value. The tax authority is responsible for the establishment of APAs and dealing with other transfer pricing-related issues.


# India

## Taxing authority and tax law

Tax authority: Central Board of Direct Taxes (CBDT), Income Tax Department

Tax law: Sections 92-92F, 144C, 271, 271AA, 271BA and 271G of the Income Tax Act, 1961

## Relevant regulations and rulings

Rules 10A to 10E of the Income Tax Rules, 1962

## OECD guidelines treatment

The Indian legislation is broadly based on the OECD guidelines. In conformity with the OECD guidelines, the legislation prescribes the same five methods to compute the arm's length price. Further, the tax authorities generally recognize the OECD guidelines and refer to them for guidance to the extent they are not inconsistent with the domestic law.

## Priorities/pricing methods

The Indian legislation prescribes the following methods: CUP, Resale Price, Cost Plus, Profit Split and Transactional Net Margin Method. The legislation also grants the power to the CBDT to prescribe any other method; however, no other method has been prescribed by the CBDT to date. No hierarchy of methods exists. The most appropriate method should be applied.

## Transfer pricing penalties

- For inadequate documentation, the taxpayer is fined 2% of the transaction value
- For not furnishing sufficient information or documents requested by the tax officer, the taxpayer is fined 2% of the transaction value
- If due diligence efforts to determine the arm's length price have not been made by the taxpayer, then 100% to 300% of incremental tax on transfer pricing adjustments may be levied by the tax officer
- For not furnishing an Accountant's Certificate (Form 3CEB) along with the return of income, the taxpayer is fined approximately INR100,000 (approximately US$2,200)

## Penalty relief

Penalties may be avoided if the taxpayer can demonstrate that it exercised good faith and due diligence in determining the arm's length price. This is also demonstrated through proper documentation and timely submission of documentation to the tax authorities during assessment proceedings.

## Documentation requirements

A detailed list of mandatory documents are listed in Rule 10D(1). The categories of documentation required are:

- Ownership structure
- Profile of the multinational group
- Business description
- The nature and terms (including prices) of international transactions
- Description of functions performed, risks assumed and assets employed
- Record of any financial estimates
- Record of uncontrolled transaction with third parties and a comparability evaluation
- Description of methods considered
- Reasons for rejection of alternative methods

# India (continued)

## Documentation requirements (continued)

- Details of transfer pricing adjustments
- Any other information or data relating to the associated enterprise which may be relevant for determination of the arm's length price

A list of additional optional documents is provided in Rule 10D(3). The taxpayer is required to obtain and furnish an Accountant's Certificate (Form 3CEB) regarding adequacy of documentation maintained.

## Documentation deadlines

The information and documentation specified should, as far as possible, be contemporaneous and exist by the specified date of the filing of the income tax return, which is 30 September following the end of the financial year.

Although an Accountant's Report must be submitted along with the tax return, the taxpayer is not required to furnish the transfer pricing documentation with the Accountant's Report at the time of filing the tax return. Transfer pricing documentation must be submitted to the tax officer within 30 days of the notice during assessment proceedings.

## Statute of limitations on transfer pricing assessments

Tax assessments (where a matter has been referred to the transfer pricing officer) are to be completed within 45 months of the end of the financial year (1 April to 31 March). However, if the tax authorities determine that income has escaped assessment, an assessment may be re-opened within seven years of the end of the financial year.

## Return disclosures/related-party disclosures

Under Section 92E, an Accountant's Report is required to be provided along with the tax return. The accountant certifies whether proper documentation is maintained by the taxpayer.

In accordance with Indian Accounting Standard 18, the company is required to disclose related-party transactions in its financial statements.

## Audit risk/transfer pricing scrutiny

Internal guidelines have been issued by the tax authorities, pursuant to which companies with related-party transactions in excess of US$1m are being scrutinized. In most cases, the tax authorities does not seem to have adopted a centralized or coordinated approach to audits, with officers in different locations taking divergent positions on similar taxpayer fact patterns. Substantial documentation is being requested in the course of audit proceedings.

The information technology, business process outsourcing, banking and pharmaceutical sectors have received particular attention. Additionally, the tax authorities are increasingly scrutinizing intra-group services received and royalty payments made by Indian taxpayers.

The tax authorities have sought an updated analysis using data that may not be available to the taxpayer at the time of the preparation of contemporaneous documentation. Furthermore, officers have insisted on unbundling transactions in cases where the taxpayer has adopted an aggregate or combined approach to its transfer pricing documentation. During recent audits, the approach adopted by the taxpayer in the selection of comparable data has received considerable attention from the tax authorities.

The Government has introduced an alternate dispute resolution process, by which the taxpayer, at his option, can approach a dispute resolution panel in case a transfer pricing adjustment is proposed by the tax officer. The panel should dispose of the matter within nine months, which shall be binding on the tax officer. This process is expected to significantly expedite the first level of the litigation process in India, which usually takes a much longer time.

## APA opportunity

APAs are not available yet, but the Indian Government has proposed to introduce APA provisions as part of the new Direct Tax Code to be implemented from 1 April 2012 onwards.


# Indonesia

## Taxing authority and tax law

Tax authority: Directorate General of Tax (DGT)

Tax law: Article 18 of the Indonesian Income Tax Law

## Relevant regulations and rulings

The new income tax law implemented on 1 January 2009 contains transfer pricing provisions in Article 18 which require that all inter-company transactions be conducted at arm's length. Its implementing regulation (i.e., PER-43/PJ/2010 or "PER-43") was issued on 6 September 2010. The regulation mandates the preparation of transfer pricing documentations as well as the guidelines to establish the arm's length nature of the transactions. In particular, it requires taxpayers to:

- Conduct a comparability analysis and determine comparable transactions
- Identify the appropriate transfer pricing method
- Apply the arm's length principles based on the results of the comparability analysis and appropriate transfer pricing methods on the transaction between a taxpayer and the parties having special relationship
- Document the steps taken in determining the fair price or fair profit in accordance with the provisions of the prevailing tax regulations

## OECD guidelines treatment

Indonesia is not a member of the OECD, but PER-43 reconfirms the basic transfer pricing concepts and principles of the OECD TP Guidelines.

## Priorities/pricing methods

Selection of transfer pricing method is to be carried out in a hierarchy of priority, starting from Comparable Uncontrolled Price (CUP) followed by Resale Price (RP) or Cost Plus (CP), and then by Profit Split (PS) or Transactional Net Margin Method (TNMM).

## Transfer pricing penalties

There is a penalty of 2% per month up to 48% on any tax underpayment arising from adjustments of income and costs corresponding to related party transactions as a result of the tax audit process.

Inappropriate disclosure of information relating to related party transactions by a taxpayer in corporate income tax return may be construed as an act of fraud that could lead to an administrative penalty of up to 400% of tax underpayment.

## Penalty relief

There is currently no penalty relief regime in place.

## Documentation requirements

Under PER-43, transfer pricing documentation is mandatory. Within 90 days following the close of the fiscal year and simultaneous with the submission of the corporate tax return, taxpayers are required to disclose information used to establish the fairness of its price or profit in related party transactions. The information required must include:

- Detailed description of the tested party, such as structure of group's business, ownership structure, organizational structure, operational aspects of business activities, list of competitors, and description of business environment
- Pricing policies and/or cost allocation policies

# Indonesia (continued)

## Documentation requirements (continued)

- Results of comparable analysis on characteristics of products being traded, results of functional analysis, economic conditions, provisions of the contracts/ agreements, and business strategy
- Selected comparable transactions
- Application of the transfer pricing methods selected by the taxpayer

## Documentation deadlines

Under PER-43, there is no specific deadline to submit the transfer pricing documentation. However, in a tax audit, any document requested by tax auditor must be provided within a month from the date of request. Further, under PER-43, all documentations to support the arm's length nature of the related party transactions, including a transfer pricing study, must be maintained within 10 years from the relevant fiscal year.

## Statute of limitations on transfer pricing assessments

There is no separate statute of limitations under PER-43. However, under the tax laws, the Indonesian tax authority is allowed to conduct a tax audit which includes assessing the arm's length nature of related party transactions, within five years from the relevant fiscal year.

## Return disclosures/related-party disclosures

Disclosure of related party transactions in the tax return has been required since 1 January 2002. Domestic and international related party transactions are required to be disclosed. The information that must be disclosed includes the type of transaction, the value of the transaction, the transfer price and the method used to determine the transfer price. However, beginning 2009, the disclosure requirements have increased and in addition to the information previously requested, confirmation of the information that have been considered by the taxpayer to establish the arm's length nature of the related party transactions will also need to be disclosed (refer to section "Documentation requirements").

## Audit risk/transfer pricing scrutiny

There is no specialized investigation unit in the Indonesian tax authority and most transfer pricing queries arise during regular tax audits. In 2010, a special group of transfer pricing auditors is being formed within the tax authority.

Enterprises with significant inter-company transactions have high risks of transfer pricing audit. The number of transfer pricing adjustments increased significantly since fiscal year 2009, especially in cases where Indonesian entities have suffered losses, or where the export prices to related entities differs from the local sales price. The Indonesian tax authority's efforts have traditionally concentrated on intangibles and services (e.g., management fees, royalties, service fees and interest), but recent experience shows an increasing interest in the transfer pricing of tangible goods.

In practice, taxpayers that exhibit the following characteristics are more at risk of being subject to a transfer pricing audit:

- A large number of related-party transactions
- Losses for more than three consecutive years
- An increase in gross revenue or receipts but no change in net profit
- Erratic profit and loss historiesAssociated parties in tax havens
- Lower net profit in comparison to the industry average or other similar enterprises. Since October 2009, the DGT issued a series of Circular Letters which provide benchmarking ratios for various industries. Under these circular letters, those taxpayers whose profits fall below the range of profit ratios are exposed to transfer pricing audit risks.

# Indonesia (continued)

## Audit risk/transfer pricing scrutiny (continued)

In March 2009, the tax authority issued letter No. S-153/PJ.4/2010, which provides guidelines for tax officers applying the arm's length principle in the context of a tax audit. In general, the main issues that have to be examined in an audit of the related party transactions are:

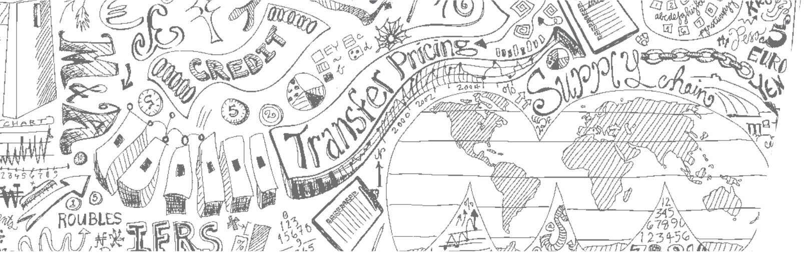
- The status of special relationship since the recalculation of income or deduction can only be made on related party transactions
- The selection of the independent transactions that are comparable
- The selection of the examined/ audited party and the tested transaction
- The comparability of conditions between those of the related party transaction and the comparable independent transaction
- The selection of profit level indicator for benchmarking
- The selection and application of transfer pricing method to apply the arm's length principle

Under PER-43, any transfer pricing adjustment made by the tax authority can result in a correlative adjustment on the income or costs of the local counterpart of the transaction.

## APA and MAP opportunity

Under PER-43, an Advance Pricing Agreement (APA) is applicable to mitigate future transfer pricing dispute with the tax authority. The APA can be in form of an agreement between the tax authority and the respective taxpayers, or between the Indonesian tax authority and the authority of another country.

In addition, PER-43 has also indicated that a Mutual Agreement Procedure (MAP) is applicable in accordance with the provision of an applicable tax treaty. The procedure for applying for MAP is further regulated under PER-48/PJ/2010.




# Ireland

## Taxing authority and tax law

Tax authority: The Irish Revenue Commissioners

Tax law: Part 35A Taxes Consolidation Act ("TCA") 1997

## Relevant regulations and rulings

Section 835C TCA 1997 sets out the main transfer pricing rules.

The regulations apply to any arrangement between associated enterprises involving goods, services, money or intangible assets, but only where those transactions meet the definition of being an Irish trading (Case I/II) transaction for one or both of the parties. The regulations apply to both domestic and cross border transactions. The regulations apply where Irish trading receipts are understated or trading expenses are overstated.

There are exemptions from these rules for small and medium enterprises where a company has fewer than 250 employees and either turnover of less than €50m or assets of less than €43m. This is an annual test.

Section 835F TCA 1997 imposes an obligation on companies to have available such records as may reasonably be required for the purposes of determining whether the trading income of the company has been computed in accordance with the requirements of section 835C. Transfer pricing documentation is fundamental to validating and explaining the pricing of the intra-group transactions, and if requested, has to readily establish to revenue's satisfaction that the transfer prices are consistent with the arm's length requirements of Section 835C TCA 1997.

## OECD guidelines treatment

The regulations adopt the OECD Transfer Pricing Guidelines wholesale into the domestic legislation. The tax authority's application of the rules in relation to documentation will accept both the 'EU Transfer Pricing Documentation' guidance and Chapter V of the OECD Transfer Pricing Guidelines (the OECD rules only apply insofar as they relate to trading transactions).

## Priorities/pricing methods

The arm's-length principle asserts that intra-group transfer prices should be equivalent to those that would be charged between independent persons dealing at arm's length in otherwise similar circumstances. Ireland accepts this principle as set out in Article 9 of the OECD Model Tax Convention and also in the "Associated Enterprises" article in Ireland's Double Taxation Treaties. To establish an arm's length price, the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations will be adopted.

Transfer prices should be reviewed at regular intervals to determine that pricing remains arm's length.

## Transfer pricing penalties

There is no separate statutory regime for transfer pricing penalties. However, normal penalties which apply to the Irish self-assessment regime may apply.

## Penalty relief

No penalty relief regime has been provided to date.

# Ireland (continued)

## Documentation requirements

The documentation must be sufficient to demonstrate a company's compliance with the transfer pricing rules. The actual documentation required will be dictated by the facts and circumstances of the transactions. The cost of producing the documentation should be commensurate with the risk involved. It would be expected that complex and high-value transactions would generally require more detailed documentation than simple high-volume transactions.

The transfer pricing documentation may be kept in the form of the company's own choosing, which the company is not required to prepare itself. The documentation does not need to be prepared or kept in the state but must be in the language of the state.

The documentation is required to contain the following:

- The associated persons that are party to the transaction
- The nature and terms of the transaction
- The terms of relevant transactions with both third parties and associates
- The method or methods by which the pricing of the transactions was arrived at, including any comparables analysis and any functional analysis undertaken
- The application of the transfer pricing method
- Any budgets, forecasts or other relevant papers relied on in arriving at an arm's-length result

Documentation should be reviewed at relevant intervals to determine whether the pricing remains at arm's length. The tax authority has stated that it will be guided by Chapter V of the OECD Transfer Pricing Guidelines and by EU Transfer Pricing Documentation guidance in applying the documentation requirement.

## Documentation deadlines

Documentation must be available for transactions that take place in accounting periods beginning on or after 1 January 2011. It is leading practice that the documentation be prepared at the time the terms of the transaction are agreed upon. It is considered leading practice that the documentation should exist by the time the tax return for the period must be made so that the company is in a position to make a correct and complete tax return, which is due to be filed nine months after the end of an accounting period.

The documentation requirements do not apply to a transaction, the terms of which were agreed upon before 1 July 2010, if:

- The terms of the agreement clearly envisage the transaction
- Application of these terms delivers the price of the transaction
- An agreement to enter into a further agreement would not meet these conditions

## Statute of limitations on transfer pricing assessments

The statute of limitations is currently four years after the end of the tax year or the accounting period in which the return is made.

## Return disclosures/related-party disclosures

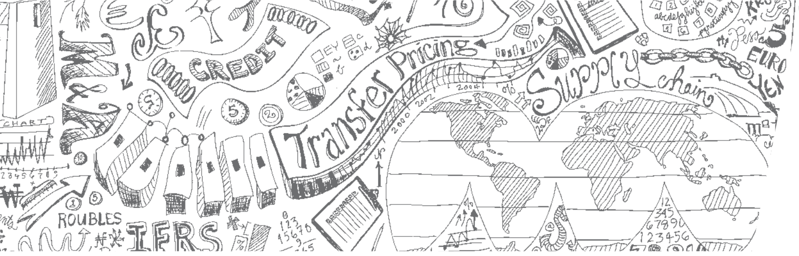
There are no requirements on return disclosures or related-party disclosures.

## Audit risk/transfer pricing scrutiny

Compliance with the transfer pricing requirements will be subject to audit. The new provisions reserve such auditing to officers authorized for that purpose by the tax authority. This ensures that the audits concerned will be undertaken by officers who appreciate, and are equipped to deal with, the complexities involved in applying the arm's-length principle.

## APA opportunity

No official APA programs or requirements are in place, but the tax authority has entered into APAs in the past.




# Israel

## Taxing authority and tax law

Tax authority: Israeli Tax Authority (ITA)

Tax law: Income Tax Ordinance §85A and Income Tax Regulations (Determination of Market Terms), 2006

## Relevant regulations and rulings

The ITA Income Tax Regulations (Determination of Market Terms) were drafted pursuant to §85A of the Israeli Income Tax Ordinance. Final regulations were adopted in November 2006. The Israeli Transfer Pricing (ITP) Regulations apply to all international intercompany transactions. The Regulations apply to all transactions carried out subsequent to their validation on 29 November 2006. The ITP Regulations are based upon a combination of the OECD Transfer Pricing Guidelines and the US Transfer Pricing Regulations.

Taxpayers are required to comply with the proper timing for the submission of documentation (i.e., 60 days from official demand of a tax inspector), which shifts the burden of proof to the tax authority if the prices do not appear to be at arm's length.

As a transitional provision, for tax years 2007 to 2008, a transfer pricing study documented prior to the publication of the ITP Regulations will be accepted for a period of two years upon their publication provided that the documentation was conducted based on the OECD guidelines or guidelines published by its members (e.g., the US).

The ITP requires that, commencing with tax year 2007, Israeli annual tax returns include a form (Form 1385), specific to transfer pricing, that delineates the intercompany transactions, details of the other party and its residency, the price of the transactions and signatures on declarations that the international intercompany transaction is at arm's length. According to the tax authority such declaration must be supported by benchmark analysis

## OECD guidelines treatment

The ITA considers its transfer pricing rules and regulations to be fully consistent with the OECD guidelines and the US Treasury Regulations under §1.482. For domestic use, the OECD guidelines do not provide support and would not be directly relevant to the application of any pricing methods. However, an arm's length study documented prior to the publication of the ITA Regulations will be accepted for a period of two years as of the Regulations' publication provided that the documentation was conducted based on the OECD guidelines or guidelines published by its members.

## Priorities/pricing methods

To determine whether an international transaction is at arm's length terms, the ITP Regulations require the taxpayer to apply one of the following methods in the following hierarchy:

- CUP or Comparable Uncontrolled Transaction (CUT)
- Comparable profitability
    - Cost Plus or Resale Price method
    - CPM or TNMM
    - Profit Split Method
- Other methods

An international transaction is at arm's length if through the application of an approved method, the result falls within a defined interquartile range. As an exception, the entire range of values will apply when the transfer pricing method applicable is a CUP or CUT, and no adjustments were performed. If the international transaction is outside the range of comparable transactions, the median should be applied as the transaction's price.

# Israel (continued)

## Priorities/pricing methods (continued)

Additionally, the ITP Regulations stipulate the use of several profit level indicators (PLIs) depending on the particular industry and environment. For example, when appropriate, the following PLIs may apply:

- A cost-plus mark-up may be applied to a company's direct costs
- A gross profit margin may be applied
  - The operating profit or loss applicable for comparable transactions
  - The profit or loss derived as a proportion of the firm's assets, liabilities or capital
- Other measures considered appropriate under the circumstances

## Transfer pricing penalties

The ITA has not currently specified any penalties with regards to its transfer pricing regulations. However, general tax penalties applied by the ITA, with regards to a tax deficit, will also apply on transfer pricing adjustments.

## Penalty relief

No penalty relief regime applicable.

## Documentation requirements

A taxpayer is required to file a transfer pricing report with the Tax Assessing Officer, at the Tax Assessing Officer's request, within 60 days from the application date. Documentation is required to include the following data:

- Details of the taxpayer, including group structure, the parties to the international transaction, their residency and any special relations between the taxpayer and the other transaction parties
- The contractual terms, including specifications of the asset, the service granted, the price paid, the loan and credit terms and related guarantees
- The taxpayer's area of activity and any relevant developments
- The economic environment in which the taxpayer operates and the related risks
- Details of all transactions entered into by the taxpayer with a related party
- An economic analysis

The taxpayer is also required to attach additional documents that corroborate the data submitted, such as transaction contracts and any other contracts between the related parties and tax returns filed with foreign tax authorities.

## Documentation deadlines

A taxpayer is required to file a transfer pricing report with the Tax Assessing Officer, at the Tax Assessing Officer's request, within 60 days of the application date.

Form 1385 should be attached to the annual tax return. The ITA has published Tax Circular 3/2008 where they stressed their opinion that this form must be backed with a benchmark analysis. Under this interpretation the deadline equals the timetable of the tax return.

## Statute of limitations on transfer pricing assessments

The Israeli Income Tax Ordinance has general rules for auditing a tax return. As such, the statute of limitations is usually three years (or four if the commissionaire extends the time period) beginning at the end of the fiscal year tax return was filed.

# Israel (continued)

## Return disclosures/related-party disclosures

Commencing with the fiscal year ending 2007, taxpayers must attach to the annual tax returns a specific transfer pricing form (Form 1385), in which the following should be disclosed:

- a short description of the intercompany transaction details of the other party and its residency
- the prices of the transactions
- signatures on declarations that the international transactions were at arm's length

## Audit risk/transfer pricing scrutiny

Medium Risk: The risk of transfer pricing scrutiny during a tax audit has increased exponentially following the issuance of the ITP Regulations and Form 1385. Transfer pricing will now be monitored with greater regularity and with increased ITA experience. In order to cope with the changing transfer pricing climate in Israel, the ITA has established a new division to enforce and regulate the ITP Regulations.

There is a growing emphasis on transactions involved with intangible assets and on July 2010 the ITA published an internal opinion instructing the assessing officers how to deal with post acquisition integration and IP migration following such restructuring.

## APA opportunity

Section 85A of the Israeli Income Tax Ordinance, which governs the ITP Regulations, stipulates in article 85A(d) the condition under which an APA may be conducted and delineates the scope of an APA. The process starts with a detailed application filed by the taxpayer that includes all the relevant details. Under the APA process, the ITP must respond within 120 days (though the time can be extended up to 180 days) otherwise the application will be approved automatically, and the intercompany policy will be deemed as providing reasonable arm's length prices.


# Italy

## Taxing authority and tax law

Tax authority: Amministrazione Finanziaria (Administration of Finance and Revenue Authority)

Tax law: Embedded within the Presidential Decree No. 917 of 22 December 1986, where transfer pricing is regulated in Article 110 (7) and Articles 9 (3)-(4)

## Relevant regulations and rulings

Law Decree no. 78 of 31 May 2010 introduced, for the first time, a specific transfer pricing documentation provision in the Italian tax law. Article 26 outlines that if the taxpayer provides tax authorities with proper transfer pricing documentation during a tax assessment, no tax penalties (currently varying from 100% to 200% of the additional taxes) will be applied on possible tax adjustments brought by the tax authorities if they determine the intercompany transactions are not in compliance with the arm's length. On 29 September 2010 the Commissionaire of the Italian Revenue Agency released a "provvedimento" (operational instructions) to implement the provisions endorsed in Article 1 (2-ter) of Legislative Decree No. 471, which was enacted on 18 December 1997. On 15 December 2010, Circular Letter 58/E has been released to interpret the new rules. The new documentation discipline still presents some open points.

The Instructions basically implement the EU Code of Conduct on transfer pricing by also following the OECD approach but provide for very specific requirements that multinationals should comply with in assembling their transfer pricing file. Compliance with the Instructions will protect taxpayers from tax penalties on adjustments arising from transfer pricing audits. Current provisions provide for very high penalties ranging from 100% to 200% of any additional taxes. Among the most significant implications of the new requirements are:

- The need to assess the type of entity which exists in Italy in order to determine the type of documentation to be prepared in order to avoid penalties (holding, sub-holding, subsidiary, permanent establishment)
- The requirement to advise the Revenue Authority of the existence of current transfer pricing documentation for the current tax year with the filing of the tax return
- To advise the Revenue Authority of the existence of transfer pricing documentation for open tax years before 29 December 2010 (communication)
- Notwithstanding a "Master-file approach," to have country specific documentation prepared
- The need to take steps to protect the taxpayer from a challenge by tax inspectors that the documentation prepared may be viewed as either incomplete or untrue, which could negate penalty protection

Notice to the Revenue Authority, indicating that transfer pricing documentation exists for FY2010 (and subsequent FYs), must be filed each year together with the annual tax return. For previous fiscal years subject to tax audits, a communication must be provided by the taxpayer within 28 December 2010. Late notices will only be deemed effective as long as filed prior to the beginning of any tax inspection.

Strategic risk management decisions need to be made by each taxpayer, possibly in coordination with central management.

It is not clear whether and to what extent previous Circular Letter Nos. 32/9/2267 of 22 September 1980 and 42/12/1587 of 12 December 1981 are still valid, at least as internal administrative guidelines.

According to the Italian Supreme Court (Corte di Cassazione) Decision No. 22023 of 13 October 2006 burden of proof rests on the tax authority for transfer pricing issues. According to the Supreme Court, and following the 1995 OECD guidelines, in the jurisdictions where the burden of proof is on the tax authority, the taxpayer is not obliged to give evidence that the transfer prices comply with the arm's length principle unless the tax authority has already proved (prima facie) that the taxpayer has not complied with the arm's length principle. It has to be seen how such an approach may be impacted by the new documentation discipline.

# Italy (continued)

## OECD guidelines treatment

The Italian transfer pricing rules are mainly provided by the tax law provisions within Presidential Decree No. 917/86 in conjunction with the above-mentioned Article 26 Law decree 78/2010, converted into Law 122 of 30 July 2010.

The Italian representatives actively participated in the OECD discussion on business restructuring as well as in the approval of the final TP guidelines release in July 2010. So far the only case law on cross-border business restructurings Ernst & Young is aware of is Ruling No. 124, dated 7 November 2006, in which the Revenue Agency deemed as occurred a sort of transfer of business concern (not specified if going concern or single assets) abroad in the case of a British insurance company which, after having operated on the Italian market for a certain number of years through a permanent establishment, subsequently provided directly its services to the Italian customers, by appointment of a fiscal representative in Italy (free supply of services).

## Priorities/pricing methods

Transactional-based methods, such as CUP, Resale Price and Cost Plus, are preferred over profits-based methods. Under the new transfer pricing documentation rules taxpayers are expected to perform every year an industry, group and company analysis with a detailed functional and risk analysis, including an indication of potential changes in the functions performed, assets used and risks assumed compared to the previous tax year will have to be provided for, with specific reference to changes if occurred in the context of a business restructuring.

The selection of the transfer pricing method entails a description of the selected transfer pricing method and of the underlying reasons determining its consistency with the arm's length. This should also cover the outcome of the comparability analysis that has determined the selection of the transfer pricing method deemed to be the most appropriate to the circumstances of the case. Should a transactional profit method be selected when a traditional transactional method could be applied in an equally reliable manner, it should be explained why the latter had been excluded. The same explanation applies in case of a selection of a method other than the CUP method, in the event the latter could potentially be chosen.

As to the criteria for the application of the selected transfer pricing method, an accurate description of the procedure followed by the taxpayer for the selection of comparable transactions will have to be provided and, if needed, a clear description of the underlying reasons for identifying a specific arms' length range.

The acceptability of possible Pan-European benchmarks is not expressly mentioned and is one of the open points.

## Transfer pricing penalties

If and when the above mentioned new TP Documentation regime is (deemed) not applicable, general penalties for underpayment apply (Legislative Decree No. 471). In particular, in a case where the tax return has been filed, standard administrative penalties apply in the amount equal to a minimum of 100% up to a maximum of 200% of the additional tax or the minor tax credit assessed by Italian tax authorities. This penalty applies with reference to single taxes when:

- The taxable income declared is lower than the one assessed
- The taxes declared are lower than those due, or
- The tax credit declared is greater than the one due to the taxpayer

The same penalties apply where undue tax allowances or deductions from the taxable income have been declared in the tax return. Interests on taxes or additional taxes due also apply. Because of the relatively high amount of potential tax revenue in a transfer pricing audit, tax officers almost "automatically" refer assessments to public prosecutors to explore possible criminal tax law ramifications, as permitted under Legislative Decree No. 74 of 10 March 2000. Some mitigation is provided by Article 7, whereby taxpayers are supposed to disclose their transfer pricing policy in their financial statement. Hopefully the new transfer pricing documentation would not only help on administrative penalties but also in demonstrating indirectly the good faith of taxpayers in case of possible tax criminal challenge.

# Italy (continued)

### Penalty relief

In addition to the above, Circular Letter 58/E dated 15 December 2010 provides further details on how to deal with the new rules in terms of Master-file versus domestic documentation's contents (depending on taxpayers' status), specific discipline for small-medium-size companies, conditions under which the transfer pricing documentation can be deemed effective, etc. Although some open points still exist, it is clear that taxpayers are expected to act transparently and in good faith. If not, not only the bona fide concept is in danger but taxpayers take the risk of harsher penalties. Some specific instructions are provided for tax assessments already occurred before the new provisions, as well as for tax assessments activities started between 28 December 2010 and 30 June 2011 *(regime transitorio).*

### Documentation requirements

Documentation must be drafted on a yearly basis with respect to the transactions carried out by the taxpayer falling into the scope of paragraph 7 of Article 110 of Presidential Decree No. 917 and it must be available in each of the taxable periods subject to audit according to the ordinary provisions.

The filing of the Documentation does not bind the tax authorities to the application of Article 1, paragraph 2-ter of the Legislative Decree No. 471, when:

- Notwithstanding the compliance with the formal structure referred to in Articles 2.1. and 2.2., the documentation delivered in the course of an audit is not complete and consistent with the provisions endorsed by the current decision
  Or
- The information provided for in the delivered documentation is inconsistent. Omissions or partial inaccuracies that do not hamper either the activity carried out by the auditors, or the accuracy of the outcome of such analysis, does not impede the application of Article 1, paragraph 2-ter of the Legislative Decree No. 471.

### Documentation deadlines

For future fiscal years taxpayers shall communicate to the Italian Revenue Agency the availability of proper documentation in the yearly income tax return.

In general, the submission of documentation to the tax authorities must be executed within and not beyond 10 days upon request. In case, during an audit or any other assessment activity, supplementary information is needed, the said supplementary information must be provided either within seven days upon request or in a longer time period depending on the complexity of the transactions under analysis, to the extent that the above period is consistent with the time of the audit. Once these terms are elapsed, the tax authorities are not bound by the application of Article 1 paragraph 2-ter of the Legislative Decree No. 471.

### Statute of limitations on transfer pricing assessments

There is no specific statute of limitations on an assessment for transfer pricing. In principle, the general statute of limitations period for tax purposes applies. Therefore, tax assessments must be notified to the taxpayer by 31 December of the fourth year following the year for which the tax return has been filed. If the tax return has been omitted or is treated as null and void, the assessable period for the relevant year is extended by one additional year. Furthermore, for companies that do not benefit from the 2002/2003 Italian Tax Amnesty, the assessable period is extended by two additional years.

In case of a potential tax criminal law ramification tax officers may invoke a specific law that in principle allows the doubling of the five years standard statute of limitations.

## Return disclosures/related-party disclosures

Italian companies must officially communicate (in documents, correspondence, register of companies) whether they are managed and controlled by another company and the name of the related company (Article 2497-bis of the Italian Civil Code). Financial statements should include essential data of the managing or controlling company's financial statement and relations with related parties (Articles 2424, 2427, 2428 and 2497-bis of the Italian Civil Code). Costs and expenses vis-à-vis parties located in black listed countries are also expected to be reported and monitored under a specific discipline with a burden of proof shifted on taxpayers.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing scrutiny during a tax audit is high. In fact, transfer pricing receives the greatest scrutiny. Italian tax authorities usually challenge the price of intercompany transactions that do not comply with the arm's length principle or that result in a mismatch between the characterization of entities and their remuneration. There appears to be a tendency toward challenging transfer pricing in combination with issues related to tax havens, deemed permanent establishments, business restructuring and abuse of law.

Italy is particularly active in challenging taxpayers on deemed permanent establishments. Following the Italian Supreme Court's "Philip Morris" case, additional case law is developing in this respect.

In addition, there is generally greater tax audit activity and particular attention paid to large taxpayers, where the Italian tax authorities are devoting greater resources in intelligence and monitoring activities on multinationals. Likewise, the Circular Letter No. 6/E issued by Central Revenue Agency on 25 January 2008 provides operating guidelines to tax authorities in relation to the prevention and combat of tax avoidance, and among the most delicate and crucial areas to be assessed, it mentions intercompany transactions and transfer prices according to the provisions of Article 110 (7) of the Presidential Decree No. 917. Legislative Decree No. 185 issued on 29 November 2008 introduced the category of "large" taxpayers stating that "in relation to the corporate income tax and VAT returns of relevant size companies, the Central Revenue activate substantial controls by the year following the one of the filing," where "relevant size companies are the ones which achieve a (yearly) turnover not lower than EUR 300m. Such threshold will be reduced to EUR 100m by 31 December 2011."

In addition, the Italian Supreme Court is developing a broad concept of "abuse of law," deemed to be inspired by the Italian Constitution Law, that is trying to introduce a general anti-avoidance principle potentially applicable to all the operations that appear to be carried out for tax reasons only, without a clear underlying business purposes.

## APA opportunity

With Article 8 of Legislative Decree No. 269, enacted 24 November 2003, the Italian government introduced a unilateral ruling system mainly relating to transfer pricing, dividends and royalties. The law has been enacted with the "*Provvedimento del Direttore dell'Agenzia delle Entrate*," dated 23 July 2004. This document provides a number of practical guidelines to apply and conduct the ruling program.

On 21 April 2010 the Central Directorate for Tax Assessment released the first Italian International Standard Ruling Report. This provides a number of statistical details that may be useful for taxpayers interested to explore an APA negotiation, including pre-filing. For taxpayers incline to support their transfer pricing policy under the new Italian transfer pricing documentation regime, the APA opportunity may become even more attractive.

Since Italy provides a variety of tax rulings, the interactions between the APA and the other tax rulings should be evaluated on a case-by-case basis.


# Japan

## Taxing authority and tax law

Tax authority: National Tax Agency (NTA)

Tax law:

- Special Taxation Measures Law (STML) Article 66-4 – Special Provisions for Taxation of Transactions with Foreign Related Persons
- STML Article 68-88 – Special Taxation Measures of Transactions between Consolidated Corporations and Foreign Related Persons

## Relevant regulations and rulings

- STML-Enforcement Order 39-12
- STML Enforcement Regulations Article 22-10
- STML-Circulars 66-4-(1)-1 to 66-4-(8)-2
- Commissioner's Directive on the Establishment of Instructions for the Administration of Transfer Pricing Matters (Administrative Guidelines)
- Commissioner's Directive on the Establishment of Instructions for the Administration of Transfer Pricing Matters for Consolidated Corporations (Administrative Guidelines for Consolidated Corporations)
- Commissioner's Directive on Mutual Agreement Procedures

## OECD guidelines treatment

The NTA refers to the OECD guidelines for direction, and the Japanese transfer pricing Administrative Guidelines contain the following statement: *"In light of the importance of a common understanding regarding transfer pricing by each country's tax authorities for the resolution of international double taxation that arises due to taxation pursuant to the transfer pricing tax system, appropriate administration shall be carried out by referring to the OECD Transfer Pricing Guidelines to the extent necessary in examinations and in reviews of requests for APA's."Administrative Guidelines,* Para. 1-2(3)

However, under audit tax examiners often point out that Japan is not bound by the OECD guidelines and that they will follow their interpretation of Japanese tax laws and regulations even where there may be a disagreement over whether their approach is consistent with the OECD guidelines. On the other hand, the most recent US–Japan tax treaty explanation refers extensively to the OECD guidelines and suggests greater harmonization in the future.

## Priorities/pricing methods

In general, transaction-based methods are preferred over profit-based methods. The tax authorities require that the CUP, Resale Price, and Cost Plus methods be used whenever possible, only allowing the use of other methods (e.g., Profit Split and Transactional Net Margin Method) after the first three have been discounted. The TNMM is available for fiscal years starting on or after 1 April 2004. Note that there are some cases in which the Residual Profit Split Method, which is accepted by the Japanese tax authorities as one type of the Profit Split Method mentioned above, is applied.

## Transfer pricing penalties

Transfer pricing assessments are subject to the same penalties that apply to general corporate tax assessments. There are two types of penalties:

- Underpayment penalty tax - computed as either 10% of the additional assessed taxes (up to JPY500,000) or 15% of the additional tax, depending on the amount of underpayment
- Delinquency tax (interest) - begins from 4% per year plus the official discount rate and increases after a certain period to 14.6% per year

There is no separate penalty for failure to prepare and maintain transfer pricing documentation.

# Japan (continued)

## Penalty relief

There are no specific provisions for reductions in underpayment penalties.

However, the 2007 tax reforms allowed for the provision of a grace period for the payment of assessed taxes – including penalty taxes – for taxpayers submitting an application for mutual agreement procedures. The taxpayer must submit a separate application to be entitled to the grace period, which is defined as the period starting on the initial payment due date of assessed taxes and ending on the day one month after the day following the day on which the "correction" based on the mutual agreement has been made (or the day on which a notification was issued that an agreement could not be reached). Any delinquency taxes accrued during the grace period will be exempted. However, under STML Article 66-4-2(2) (which grants a postponement of tax payment), the tax authority requires the taxpayer to provide security equivalent to the amount of the tax payment (i.e., collateral). This new transfer pricing rule will be applicable for applications for a grace period made on or after 1 April 2007.

## Documentation requirements

The 2010 tax reform effective 1 April of this year clarified expectations around documentation, by amending the STML to state that "documents stated in the ministerial ordinance…should be provided without delay" when requested in the course of an examination. The ministerial ordinance in question (STML Enforcement Regulations Art. 22-10) was in turn amended to include a detailed list of documents to be submitted. The previous version of the STML had required that "documents or accounting books" be rendered, without specifying what types of documents and books were required. The substance of the new list in the ministerial ordinance is largely identical to a list previously disclosed in the Administrative Guidelines (an advisory document), but the promotion to the ministerial ordinance, coupled with the citation in the STML, gives this list the force of regulation.

The list of documents is now formally linked to existing language in the STML providing that failure to provide appropriate materials in a timely manner upon request can trigger the tax examiner's authority to collect transactional data from comparable firms to use as "secret comparables" for the taxpayer. That is, the comparables are not disclosed to the taxpayer because the transactional data of the companies are confidential. Alternatively, an examiner can resort to "presumptive taxation", presuming an arm's length price with reference to profit ratios of other corporations in the industry which carry out similar activities.

## Documentation deadlines

The taxpayer is required to provide the tax authority with documentation (i.e., information and records) relevant to the establishment of the arm's length price in a timely manner upon request. There is no exact deadline specified.

## Statute of limitations on transfer pricing assessments

The statute of limitations on transfer pricing assessments is six years from the deadline for filing tax returns for a fiscal year (STML Article 66-4(16)).

A corporation must maintain corporate tax records for seven years from the fiscal year end (Corporation Tax Law Art. 126 and 150-2; Corporation Tax Law Enforcement Regulation, Article 59 and 67).

## Return disclosures/related-party disclosures

The taxpayer must file Schedule 17-4 (previously Schedule 17-3), Detailed Statement Concerning Foreign Affiliated Persons and Related Party Transactions for fiscal years beginning on or after 1 April 2003. Schedule 17-4 requires that taxpayers disclose the transfer pricing methods applied in calculating the arm's length prices of the foreign related-party transactions. This requirement implies that taxpayers are expected to identify the appropriate transfer pricing methods for their related-party transactions and be able to demonstrate the appropriateness of those methods. Therefore, this rule can be interpreted as a de facto transfer pricing documentation requirement as taxpayers are expected to maintain documents in support of any tax return disclosure.

# Japan (continued)

## Return disclosures/related-party disclosures (continued)

Effective 30 April 2008, Schedule 17-4 requires taxpayers to disclose the following three additional information items:

- The number of employees of the foreign related party
- The amount of retained earnings of the foreign related party for the preceding year
- Any APA agreed between the taxpayer and the foreign Competent Authority

## Audit risk/transfer pricing scrutiny

The NTA and the major Regional Tax Bureaus together employ about 200 dedicated transfer pricing specialists to actively enforce Japan's transfer pricing rules. Audit risk is generally medium-high for large taxpayers with significant related-party transactions. The risk is increased for taxpayers who meet any of the following criteria:

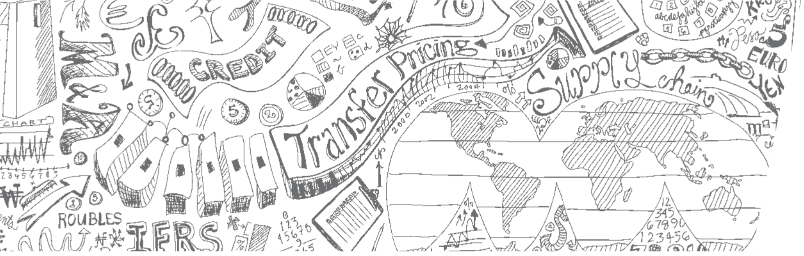
- In industries targeted by the NTA
- With low profits or losses in Japan
- High profits in foreign affiliates as disclosed on Schedule 17-4 (relative to profits reported in Japan)
- With fluctuating profitability
- Who have significant transactions with tax havens
- In industries with high margins. The NTA is likely to seek to apply comparables, including secret comparables available only to the NTA

## APA opportunity

Unilateral and bilateral APAs are available, though the NTA prefers bilateral. APA guidelines are included in the Administrative Guidelines.

The NTA has recently shown a willingness to accept profit-based methods, such as the TNMM.

The NTA amended the filing deadline for APA applications on 22 October 2008. Previous guidance required that the APA application be filed by the tax return filing deadline of the first year to be covered by the APA. The new NTA guidance sets the APA filing deadline as the day preceding the first day of the first fiscal year to be covered by the proposed APA.




# Kazakhstan

## Taxing authority and tax law

Tax and customs authorities are the authorized bodies to conduct control over transfer pricing. Tax authorities include Tax Committee of the Ministry of Finance of the Republic of Kazakhstan (TCMF) and territorial tax bodies. Customs authorities include Customs Control Committee of the Ministry of Finance (CCC), its territorial subdivisions, custom houses, customs points, checkpoints at the customs border of the Republic of Kazakhstan, and specialized customs offices.

The Law of the Republic of Kazakhstan No. 67-IV on Transfer Pricing, of 5 July 2008, regulates transfer pricing.

## Relevant regulations and rulings

The following subordinate legal acts regulate transfer pricing:

- Instruction on control over transfer pricing in international business transactions (pending approval of the Ministry of Finance)
- Rules for conducting of transactions monitoring (No. 62 of 12 February 2009)
- Rules for concluding agreements on application of transfer pricing (No. 63 of 12 February 2009)
- Rules on the procedure for cooperation of the authorized bodies in conducting control over transfer pricing issues (No. 129 of 26 March 2009)
- List of goods (work, services) international business transactions with which are subject to transactions monitoring (No. 293 of 12 March 2009)
- List of officially recongnized sources of information on market prices (No. 292 of 12 March 2009)

## OECD guidelines treatment

The OECD guidelines are not binding for Kazakhstan. Although the currently effective transfer pricing law has some common features with the OECD Transfer Pricing Guidelines, the principal difference with the guidelines is that the Kazakhstan transfer pricing legislation targets all international business transactions regardless of whether the parties are related or not.

## Priorities/pricing methods

The law allows for five pricing methods in the following priority: Comparable Uncontrollable Price, Cost Plus, Resale Price, Profit Split and Net Margin.

## Transfer pricing penalties

Special fines are envisaged for failure to comply with the documentation requirements established by the transfer pricing legislation (i.e., monitoring reporting and documentation supporting the transaction price). The maximum amount of fines is set at approximately US$3,300.

The fine for understatement of tax payment resulting from transfer pricing adjustment is up to 50% of the additionally accrued tax amount. In addition, interest for delayed payment of additionally assessed tax resulting from transfer pricing adjustments is two-and-a-half times the National Bank refinancing rate.

## Penalty relief

There is currently no penalty relief regime in place.

# Kazakhstan (continued)

## Documentation requirements

Different requirements are established for two categories of transactions:

- Transactions with goods (works, services) that are subject to monitoring
- All other transactions with goods subject to transfer pricing control

Participants involved in transactions subject to monitoring are obliged to prepare and submit transaction monitoring reports on an annual basis ("Monitoring reports") that should include information on the applied prices, the relationships of the parties, industries and market conditions, business strategy, transfer pricing methodology, functional and risks analysis, tangible and intangible assets, method, source of information used for determination of a market price and other information.

Transaction participants executing transactions with other goods that are subject to transfer pricing control should maintain documentation supporting the applied prices that is less detailed than the monitoring reports.

## Documentation deadlines

Monitoring reports must be submitted to the tax authorities no later than 15 April of the year following the reporting year. The filing deadline can be extended up to the extension period granted for filing a corporate income tax declaration.

The documentation supporting the applied transaction prices must be submitted within 90 days from the date of the competent authorities' request.

## Statute of limitations on transfer pricing assessments

There is no specific statute of limitations on transfer pricing assessments. The general statute of limitations period for the assessment of penalties for underpayments of tax, understatements of income or overstatements of expenses, is five years from the date of the relevant violation. Within the same statute of limitations, the taxpayer has the right to introduce amendments and additions to its tax reporting.

## Return disclosures/related-party disclosures

No related-party disclosure is required currently on tax declarations, although both National Accounting Standards and International Financial Reporting Standards require such disclosures in financial statements.

## Audit risk/transfer pricing scrutiny

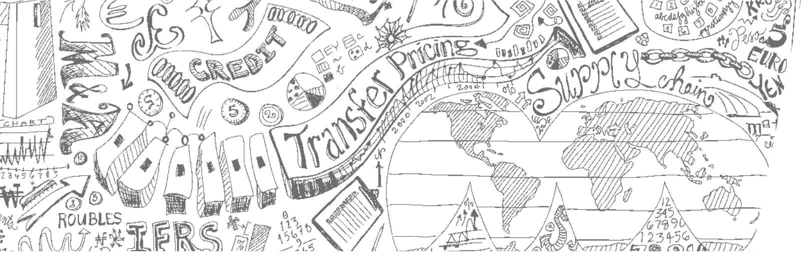
Transfer pricing audits can take place once per year. The risk of transfer pricing issues being scrutinized during an audit is high. The export of goods from Kazakhstan receives greater scrutiny. The review of the method, its use and the interpretation of information on market prices applied by the tax authorities often result in transfer pricing adjustments that are contested by taxpayers in many cases.

## APA opportunity

Transaction participants are allowed to conclude an agreement on application of transfer prices. The procedure for concluding such agreements is envisaged in the rules for concluding agreements on application of transfer pricing (No. 63 of 12 February 2009) that determine the following:

- List of documents required for concluding the agreement
- Procedure for consideration of the request by tax authorities
- Duration of the agreement (e.g., three years from the date of signing)
- Conditions for termination
- Other

The tax authorities reserve the right to unilaterally terminate an agreement if a participant violates its conditions.




# Kenya

## Taxing authority and tax law

- Tax authority: Kenya Revenue Authority (KRA)
- Tax law: Income Tax Act (Cap 470, Laws of Kenya) and the Income Tax (Transfer Pricing) Rules 2006 are the applicable regulations

## Relevant regulations and rulings

Section 18(3) of the Income Tax Act provides: "Where a non-resident person carries on business with a related resident person and the course of that business is so arranged that it produces to the resident person either no profits or less than the ordinary profits which might be expected to accrue from that business if there had been no such relationship, then the gains or profits of that resident person from that business shall be deemed to be the amount that might have been expected to accrue if the course of that business had been conducted by independent persons dealing at arm's length."

For the purposes of subsection (3), a person is related to another if:

- Either person participates directly or indirectly in the management, control or capital of the business of the other
- A third person participates directly or indirectly in the management, control or capital of the business or both
- An individual, who participates in the management, control or capital of the business of one, is associated by marriage consanguinity or affinity to an individual who participates in the management, control or capital of the business of the other

The Transfer Pricing guidelines apply to:

- Transactions between associated enterprises within a multinational company, where one enterprise is located in, and is subject to tax in Kenya, and the other is located outside Kenya
- Transactions between a permanent establishment and its head office or other related branches, in which case the permanent establishment shall be treated as a distinct and separate enterprise from its head office and related branches.

## OECD guidelines treatment

The Income Tax (Transfer Pricing) rules provide for the application of the OECD methods in determining the arm's length pricing.

## Priorities/pricing methods

Rule 4 of the aforesaid rules provides that a tax payer may choose to employ in determining the arm's length price from among the six methods as follows:

- Comparable Uncontrolled Price (CUP) method
- Resale price method
- Cost price method
- Profit split method
- Transactional net margin method
- Such other method as the commissioner for Domestic Taxes may prescribe

# Kenya (continued)

## Transfer pricing penalties

There are no specific TP penalties. However, the Commissioner for Domestic Taxes can conduct an audit and make adjustments in the taxable profit and demand tax where applicable. Any tax due and unpaid tax in a transfer pricing arrangement is deemed to be additional tax for purposes of Sections 72D, 94 and 95 of the Income Tax Act.

- Section 72D of the Income Tax Act provides that “ when any amount of tax remains unpaid after the due date, a penalty of 20% shall immediately become due and payable”
- Section 94 of the Income Tax Act provides that ‘late payment interest of two per cent per month or part thereof shall be charged on the amount, including the penalty remaining unpaid for more than one month after the due date until the full amount is recovered’.
- Section 95(1) provides that if, for a year of income, the difference between the amount of tax assessed on the total income of a person and the amount of the estimate of the tax chargeable contained in a provisional return of income made by that person in respect of that year is greater than ten per cent of that estimated tax, interest at the rate of two per cent per month shall be payable on the whole of the difference between the tax assessed and the tax estimated.

## Penalty relief

There is no specific penalty relief for Transfer pricing arrangements.

## Documentation requirements

The Commissioner for Domestic Taxes may, where necessary request a person to whom these rules apply for information, including books of accounts and other documents relating to transactions where the transfer pricing is applied. Such documents shall include information relating to:

- The selection of the transfer pricing method and the reasons for the selection
- The application of the method, including the calculations made and price adjustment factors considered
- The global organization structure of the enterprise
- The details of the transaction under consideration
- The assumptions, strategies and policies applied in selecting the method
- Other background information as may be necessary regarding the transaction

The books of accounts and other documents shall be prepared in or be translated into English language, at the time the transfer price is arrived at.

Where a person avers the application of arm’s length pricing, such person shall:

- Develop an appropriate transfer pricing policy
- Determine the arm’s length price as prescribed under the guidelines provided under these rules
- Avail documentation to evidence their analysis upon request by the commissioner

## Documentation deadlines

The deadline for preparing documentation is the same as the deadline for filing the tax return.

Documentation must be provided upon request.

# Kenya (continued)

### Statute of limitations on transfer pricing assessments

According to Section 56(3) of the Income Tax Act, the statute of limitations for TP assessments is seven years after the relevant year of income unless the Commissioner has reasonable cause to believe that fraud or gross or willful neglect has been committed in connection with, or in relation to, tax for a year of income.

### Return disclosures/related-party disclosures

According to the corporate tax return format, the tax payer is obliged to declare the following:

- Name of the related party/parties outside Kenya
- The address of the related parties

### Audit risk/transfer pricing scrutiny

Audit risk can be characterized as high. The KRA has commenced TP audits and is requesting for TP policies for scrutiny.

### APA opportunity

There are no specific APA rules.


# Latvia

## Taxing authority and tax law

Tax authority: The State Revenue Service

Tax law: The arm's length principle is established in the Law on Corporate Income Tax. Article 12 of the Law on Corporate Income Tax of Latvia determines that the taxable income of the taxpayer may be increased if related-party transactions are not arm's length.

## Relevant regulations and rulings

4 July 2006 Cabinet Regulations No. 556 set the transfer pricing methods applicable for determining arm's length prices in related-party transactions.

## OECD guidelines treatment

Latvian transfer pricing legislative acts contain a reference to the OECD Guidelines on the application of the transfer pricing methods. The State Revenue Service also generally accepts the OECD Guidelines principles regarding transfer pricing documentation structure.

## Priorities/pricing methods

Five methods are accepted – Comparable uncontrolled price method, Resale price method, Cost plus method, Profit split method and TNMM.

## Transfer pricing penalties

There is no separate penalty for not having transfer pricing documentation. In case the prices applied in transactions between related parties are not at arm's length, the taxable income of the taxpayer may be increased and a penalty in the amount of 30 to 50% and a late penalty charge (annual rate of 18%) on additionally payable corporate income tax may be applied.

## Penalty relief

There is currently no penalty relief available; however, the existence of transfer pricing documentation generally reduces transfer pricing risks.

## Documentation requirements

Latvian legislative acts do not provide specific requirements regarding preparation of transfer pricing documentation. However during tax audits taxpayer should be able to justify that prices applied in transactions between related parties are arm's length. Generally transfer pricing risks are lower if the documentation prepared is based on the OECD Guidelines.

## Documentation deadlines

There is no specific deadline for the preparation of the transfer pricing documentation but the relevant documentation could be required during the State Revenue Service tax audit. The tax audit may be started immediately after submitting the Corporate Income Tax Return (i.e., four to seven months after the end of financial year).

## Statute of limitations on transfer pricing assessments

Generally the State Revenue Service has rights to make a tax assessment for three years from the payment date of respective tax. This general rule is applicable also to transfer pricing tax assessments

# Latvia (continued)

## Return disclosures/related-party disclosures

Related-party transactions must be disclosed in Appendix 2 of the Corporate Income Tax Return. The taxpayer should disclose related parties involved in related-party transactions, type of transaction (e.g., purchase or sale of goods, services or fixed assets), volume of transactions and transfer pricing methods applied.

## Audit risk/transfer pricing scrutiny

Small and medium taxpayers in Latvia run a medium risk that transfer prices will be scrutinized during a tax audit. However, for large taxpayers the risk of transfer pricing scrutiny is high.

## APA opportunity

There are no specific APA rules.


# Lithuania

## Taxing authority and tax law

Tax authority: Ministry of Finance of the Republic of Lithuania and the State Tax Inspectorate.

Tax law: The arm's length principle is established in the Corporate Income Tax of Lithuania and its implementation rules introduced in 2004.

## Relevant regulations and rulings

- Article 40 of the Law on the Corporate Income Tax of Lithuania
- Order of the Minister of Finance No 1K- 123 as of 9 April 2004 on transfer pricing evaluation and documentation rules
- Order of the Head of the State Tax Inspectorate No VA-27 as of 22 March 2005, on the associated party transaction disclosure in the annual corporate income tax return

## OECD guidelines treatment

The use of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrators is explicitly advocated in the regulations and rulings applicable in Lithuania. Other OECD papers, such as regarding business restructurings and profit allocation to permanent establishments, are not explicitly implemented in the Lithuanian legislation, however, in practice they are frequently referred to for practical guidance.

## Priorities/pricing methods

Transaction-based methods are preferred over profit-based methods. Taxpayers are encouraged to use profit-based methods only if transaction-based methods are not sufficient. Taxpayers are not required to use more than one method; however, a combination of methods may be used in all cases providing support for the decision to apply any particular method.

## Transfer pricing penalties

There are no specific transfer pricing penalties. General tax penalties applicable in the case of the taxable income adjustments by the tax authority are equal to 10% to 50% of the tax additionally calculated. In addition, the penalty interest will apply.

There are no special penalties related to the non-provision of the transfer pricing documentation at the request of the tax authorities.

## Penalty relief

No penalty relief regime applicable.

## Documentation requirements

The transfer pricing documentation requirements are binding for resident and non-resident legal entities registered as corporate income taxpayers in Lithuania, whose revenues in Lithuania in the year before the transactions were conducted exceeded EUR 2.9m.

In addition, transfer pricing documentation requirements are applicable to the credit institutions such as banks and entities providing financial services (e.g., insurance companies), irrespective of their revenue size.

The transfer pricing documentation has to contain:

- Details of the transactions
- Terms and conditions of the transactions
- Participants in the transactions, including their legal and organizational structure
- Functions performed, property used or contributed and the risks assumed by the parties
- Data and methods considered and the analyses performed to determine the transfer prices
- All relevant assumptions, strategies and policies that influenced the determination of the methods applied

In general, the OECD guidelines' principles are to be followed.

# Lithuania (continued)

## Documentation deadlines

There are no specific requirements or schedules for the preparation of transfer pricing documentation. Taxpayers must submit the transfer pricing documentation within 30 days of the corresponding notice by the tax authorities.

## Statute of limitations on transfer pricing assessments

Transfer pricing assessments may occur during the five years before the year in which the assessment takes place.

## Return disclosures/related-party disclosures

An associated party disclosure annex to the annual corporate income tax return has to be submitted within nine months after the end of each tax period, in case the associated-party transactions of the taxpayer exceed in annual value approximately EUR 87,000. In the annex, taxpayers are required to inform the tax authorities whether any prescribed transfer pricing methods have been used in the transactions disclosed.

## Audit risk/transfer pricing scrutiny

Taxpayers in Lithuania run a high risk that transfer prices will be scrutinized during a tax audit.

## APA opportunity

Currently, the Lithuanian tax laws do not provide for an opportunity to conclude APAs.


# Luxembourg

## Taxing authority and tax law

Tax authority: The Luxembourg Tax Authorities

Tax law: Income Tax Law (ITL), General Tax Law

## Relevant regulations and rulings

The Luxembourg ITL contains two articles relating to transfer pricing: Article 56 ITL on Transfer of Business Profits and Article 164(3) ITL on Hidden Profit Distribution. Both articles encourage the general application of the arm's length criteria for transactions between related parties. The ITL does not, however, contain any other specific guidelines or regulations. Moreover, the Luxembourg tax authorities have not issued any specific guidelines or regulations.

## OECD guidelines treatment

OECD TP guidelines are not officially enacted in Luxembourg tax law. However, even though there is no official publication in this respect, the Luxembourg tax authorities usually refer to the OECD transfer pricing guidelines for assessing the arm's length character of inter-company transactions. Considering that OECD TP guidelines are not enacted into Luxembourg ITL, the arm's length nature of inter-company transactions may also be established with reference to other generally accepted TP guidelines or regulations.

## Priorities/pricing methods

There are no specific pricing methods mentioned in the ITL. All methods advocated by the OECD are acceptable under the current administrative practice, such as CUP, Resale Price, Cost Plus method, TNMM, and Profit Split. There are no priorities established between the different methods.

## Transfer pricing penalties

To the extent that the arm's length criteria is not respected, the tax authorities may reassess and/or adjust the taxable result but no penalties are foreseen in the tax law for the case that such adjustments are made.

## Penalty relief

Since there are no specific transfer penalties in the tax law, there are no specific provisions for reductions in penalties.

## Documentation requirements

Luxembourg general tax law includes general documentation requirements, but does not provide for specific transfer pricing documentation regulations. Thus, intercompany transactions should always be supported at least by appropriate agreements and other supporting legal documentation. The tax authorities may, however, request complementary information supporting the transfer prices applied on intercompany transactions at the time they are executed. Reference is generally made to OECD guidelines for adequate documentation.

Luxembourg is also adhering to the EU code of conduct on transfer pricing documentation for associated enterprise in the EU. As a consequence, contemporaneous TP documentation available at head-quarter level may also be used in Luxembourg to support the arm's length nature of intercompany transactions.

## Documentation deadlines

As a general rule, contemporaneous documentation should exist when transactions are carried out. That rule also applies in relation to transfer pricing documentation. As the tax law does not contain specific TP documentation regulations, Luxembourg tax law does neither include a deadline to produce TP documentation. The tax authorities may, however, request in the context of an audit that TP documentation is provided within a certain delay. Such delay may be as short as a couple of weeks, but might be extended upon request.

# Luxembourg (continued)

## Statute of limitations on transfer pricing assessments

There are no specific limitations on transfer pricing adjustments. The general rules apply. The statute of limitation is, in principle, five years starting from 1 January of the calendar year following the relevant tax year. In case of incomplete tax returns or no tax returns filed as well as in case of fraud, the statute of limitation is extended to 10 years. Moreover, once a Luxembourg company has been finally assessed for income and net wealth tax purposes for a particular year, the tax authorities may not reassess the relevant tax year unless they have obtained new information and the statutes of limitation is not yet applicable. As long as the tax authorities have issued a provisional tax assessment, the taxable base may still be adjusted after the issuance of the provisional assessment until the statutes of limitation is acquired.

## Return disclosures/related-party disclosures

There are no specific disclosures required when filing tax returns. It is, however, common practice that transactions with related parties are detailed by nature and a related party breakdown included the tax returns.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing being reviewed under an audit is medium.

## APA opportunity

Although no formal advance pricing agreement procedure exists in Luxembourg, the tax authorities may express an opinion on transfer prices used by taxpayers on a case-by-case basis. In that respect, advance clearance can be sought from the Luxembourg tax authorities on the intercompany transfer prices being applied.


# Malaysia

## Taxing authority and tax law

Tax authority: Inland Revenue Board (IRB)

Tax law:

General Anti-Avoidance Provision

- Section 140 of the Malaysian Income Tax Act, 1967: Power to disregard certain transactions if not deemed arm's length
- Section 138C of the Malaysian Income Tax Act, 1967: Advance Pricing Arrangement
- Section 140A of the Malaysian Income Tax Act, 1967: Power to substitute the price and disallowance of interest on certain transactions and

Transactions by Non-Residents

- Section 141 of the Malaysian Income Tax Act, 1967: Powers regarding certain transactions by non-residents

The IRB released the Malaysian Transfer Pricing Guidelines on 2 July 2003 which specify documentation requirements.

## OECD guidelines treatment

The Malaysian Transfer Pricing Guidelines are largely based on the governing standard for transfer pricing, which is the arm's length principle as established in the OECD guidelines. The IRB respects the general principles of the OECD guidelines.

## Priorities/pricing methods

The IRB accepts CUP, Resale Price, Cost Plus, Profit Split and TNMM. However, the Malaysian Transfer Pricing Guidelines state that the traditional methods are preferred over the profit methods and advise that the profit methods should only be used when the traditional methods cannot be reliably applied or cannot be applied at all.

## Transfer pricing penalties

There are no specific penalties for transfer pricing. However, the existing legislation and penalty structure under the Malaysian Income Tax Act, 1967, are applied. Penalties for transfer pricing adjustments can range from 100% to 300% of the undercharged tax. There are no transfer-pricing-specific documentation penalties.

## Penalty relief

A reduction in penalties can be negotiated based on quality of contemporaneous transfer pricing documentation.

## Documentation requirements

Contemporaneous documents pertaining to transfer pricing need not be submitted with the tax return form, but should be made available to the IRB upon request. All relevant documentation must be in, or translated into, Bahasa Malaysia (the national language) or English.

There is no disclosure required on a tax return to indicate that transfer pricing documentation has been prepared.

The IRB has set out a list of information and documentation to be prepared for transfer pricing purposes. This list is neither intended to be exhaustive nor meant to apply to all types of businesses. Instead, taxpayers are advised to maintain information and documentation that are applicable to their circumstances. The list includes:

- Company details
  - Ownership structure showing linkages between all entities within the Multinational Enterprise (MNE)
  - Company organization chart
  - Operational aspects of the business including details of functions performed

# Malaysia (continued)

- Transaction details
  - A summary of transactions with other entities in the same MNE, indicating the name and address of each entity in the MNE with whom international transactions have been entered into, and the type of transactions (e.g., purchase of raw material or fixed assets, sale of finished goods, borrowing of money)
  - A summary of transactions similar to the above that are conducted with independent parties or information derived from independent enterprises engaged in similar transactions or businesses
  - Economic conditions during the time of the transactions
  - Terms of the transactions, including where applicable contractual agreements with overseas associated parties with regard to technical assistance fees, management fees, marketing fees, recruitment fees or other services provided, royalties payable, purchase or rental of equipment or other assets, handling charges, loans, allocation of overhead expenses or any specific expenses (e.g., promotional or advertising) borne by the foreign entity or other forms of payment to overseas associates
  - Pricing policy over the past seven-year period
  - Breakdown of product manufacturing costs
  - Product price list
- Determination of arm's length price
  - The pricing method adopted, showing how the arm's length price is derived, and indicating why that method is chosen over other methods
  - Functional analysis taking into consideration all risks assumed and assets employed
  - If a comparability analysis results in a range of arm's length outcomes, then the furnishing of documents relating to all of the outcomes and the reasons for choosing that particular arm's length price from the range of outcomes must be given.

## Documentation deadlines

There is no documentation deadline. However, documentation should be prepared contemporaneously. As tax returns are due for filing to the IRB within seven months of the close of a company's financial year-end, it is advisable that transfer pricing documentation be prepared before the submission date of the return.

## Statute of limitations on transfer pricing assessments

There is a six-year statute of limitations for tax adjustments, and documentation must be kept for seven years. There is no statute of limitations in instances of fraud, willful default or negligence.

## Return disclosures/related-party disclosures

Disclosure of arm's length values is required in the tax return for the following transactions:

- Sales to related companies
- Purchases from related companies
- Other payments to related companies
- Lending to and borrowing from related companies
- Receipts from related companies

# Malaysia (continued)

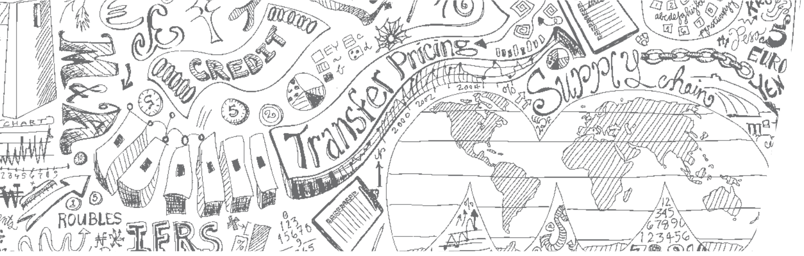
## Audit risk/transfer pricing scrutiny

The risk of transfer pricing scrutiny during an audit is high. Tax audits are carried out under a self-assessment regime. Every company is expected to be subject to a desk or field audit at least once every five years. With the release of the Malaysian Transfer Pricing Guidelines, greater scrutiny on transfer pricing has been observed in these field audits. Ernst & Young's experience is that every multinational corporation that was audited over the last 12 months was scrutinized on its transfer pricing policy. Since the beginning of 2005, the number of transfer pricing audits and investigation activity by the IRB increased significantly. There is a specific transfer pricing unit in the IRB to handle all transfer pricing audits.

This scrutiny is expected to increase significantly with the introduction of §140A of the Malaysian Income Tax Act, 1967: Power to substitute the price and disallowance of interest on certain transactions. This section effectively shifts the onus unto the taxpayer to prove arm's length pricing in acquisition or supply of property and services. Furthermore, this section also imposes thin capitalization rules, disallowing deductions for interest, finance charge and other consideration in respect of financial assistance between related persons.

## APA opportunity

The introduction of §138C in the Malaysian Income Tax Act, 1967 effectively formalizes the availability of unilateral and bilateral APAs in Malaysia. However, at this stage, formal guidelines on APAs are still in draft form, and the IRB has previously indicated that it will consider any terms and conditions which are the norm observed in the transfer pricing regimes in other jurisdictions. A specific transfer pricing unit in the IRB has been established to oversee the APA applications and negotiations.




# Mexico

## Taxing authority and tax law

Tax authority: The Central Administration of Transfer Pricing Audits of the Mexican Tax Administration Service (SAT) is in charge of enforcing transfer pricing rules, audits and the APA Program.

Tax law:

- Articles 86-XII, XIII and XV, 215, 216, 216-BIS and 217 of the Mexican Income Tax Law (MITL)
- Article 34-A of the Federal Fiscal Code (FFC)
- Article 216-BIS of the MITL provide special rules for maquiladoras

Additionally, questionnaires related to the tax review by the registered external auditor (external CPA) as part of the Financial Audit Report are published as Miscellaneous Tax Resolutions in the Federal Register (Diario Oficial de la Federación). Four of such questionnaires relate to inter-company transactions and require a great deal of detail.

## Relevant regulations and rulings

Tax regulations are issued by the Ministry of Finance and approved by Congress. The SAT publishes administrative rules on a regular basis, and few rules and regulations deal with transfer pricing issues.

## OECD guidelines treatment

The OECD guidelines can be relied upon for interpretation of the rules as long as they do not contradict the MITL or International Tax Treaties.

## Priorities/pricing methods

The transfer pricing methods in Mexico are the CUP, Resale Price, Cost Plus, Profit Split, Residual Profit Split and TNMM. Effective 2006, there is a best method rule and a hierarchy of methods. The CUP and other traditional transactional methods are preferred to profit-based methods. No alternative methods are acceptable.

## Transfer pricing penalties

No specific penalties are applied when taxpayers do not maintain contemporaneous transfer pricing documentation. However, the SAT has taken the position, confirmed by a tax court case, that failure to comply with the documentation requirements results in non-deductibility of the corresponding payments to non-resident related-parties. There are also penalties for failure or untimely filing of the transfer pricing information return. A penalty of US$4,100 to US$8,037 can be assessed if the information return on related-party transactions is not filed or is incomplete or incorrect.

If a transfer pricing adjustment is determined, and as a consequence unpaid contributions are established, a monetary sanction of 55% to 75% applies.

Also, if a transfer pricing adjustment reduces a net operating loss (NOL), the penalty ranges from 30% to 40% of the difference between the determined NOL and the NOL in the return. It is worth mentioning that both penalties described above will also need to be calculated based on surcharges and updates.

There are no penalties if self-correction of tax results is made before an audit and reduced penalties apply if self-correction is made during the audit but before the tax assessment. Waivers and abatements are possible under limited circumstances.

## Penalty relief

According to Art76 of the Federal Fiscal Code, if the taxpayer prepares and maintains annual transfer pricing documentation, a penalty relief between 27.5% and 37.5% of the tax omitted applies (50% of the corresponding penalty). Waivers and abatements are possible under limited circumstances such as financial hardship (during 2006). Penalties may be reduced after the audit has started by self-correction procedures.

# Mexico (continued)

## Documentation requirements

Contemporaneous transfer pricing documentation related to cross-border intercompany transactions must be maintained. Documentation must include the name, address and tax residency of the non-resident related persons with whom transactions are carried out, as well as evidence of direct and indirect participation between related-parties.

It is necessary to include in the documentation information on the functions, activities, assets used and risks assumed by the taxpayer involved in each transaction. It is also necessary to include information and documentation on comparable transactions or companies by type of transaction. Domestic intercompany transactions are also required to be documented by demonstrating that an accepted pricing methodology is being applied.

Taxpayers are required to identify non-resident related-party transactions clearly on their accounting records. Documentation must be readily available by due date of the tax return. The Multiple Annual Tax Return includes an appendix for the disclosure of information related to intercompany transactions with non-resident related-parties. Tax returns require the following information by type of transaction and by related-party:

- Names, countries and tax identification numbers of affiliates
- Types of transactions and corresponding amounts
- Transfer pricing methods
- Gross or operating margins earned on each transaction (only applicable under certain types of transactions)

## Documentation deadlines

A transfer pricing study must be in place at the time the company files its annual income tax return (by the end of March of the following year) and must be kept along with the company's accounting records for five years after the filing of the last tax return for each year.

The external auditor of each Mexican taxpayer is required to disclose the company's compliance with all tax obligations, including those related to transfer pricing. This disclosure is made through the Financial Audit Report (Dictamen Fiscal) that must be filed by certain companies by 30 June every year.

In order to issue the Financial Audit Report, the auditor must verify, among other things, that the company's transfer pricing documentation is in place for the fiscal year under analysis and that it complies with the requirements stated in the MITL and complete extensive questionnaires, four of which deal with inter-company transactions, as follows:

- Attachment 5: Segmented Profit and Loss Statement (not required for the Financial Audit Report for fiscal year 2008 but compulsory for fiscal year 2009)
- Attachment 34: Information regarding related-party transactions, such as:
  - Tax ID
  - Tax Name
  - Country of residence
  - Amount of the intercompany transaction
  - Transfer Pricing Methodology
  - Profit Level Indicator
  - Assessment regarding transfer pricing compliance

This information is required for all intercompany transactions (i.e., with foreign and local related-parties, per party and type of transaction). This questionnaire is intended to verify compliance with MITL not only to verify transfer pricing aspects, per se, but also deductibility transfer pricing requirements of all tax deductions.

# Mexico (continued)

## Documentation deadlines (continued)

- **Attachment 34.1: Questionnaire on Related-Party Transactions. This questionnaire includes the following sections:**
  - Advance Pricing Agreement (if applicable)
  - Transfer Pricing Documentation compliance and filing date of Informative Tax Return
  - Cost of Sales Segmentation
  - Related rules regarding Pro-rata charges
  - Information regarding financial derivative operations
  - Maquiladora rules compliance
- **Transfer Pricing Questionnaire related to the review conducted by the external auditor.** More than 90 questions regarding dealing with all aspects related to cross-border and domestic intercompany transactions.

Additionally, an information return on related-party transactions must be filed electronically along with the annual income tax return. Transfer pricing documentation must be readily available as part of the accounting records by 31 March. The SAT has taken the position that failure to comply with the documentation requirements results in non-deductibility of payments to non-resident related-parties.

## Statute of limitations on transfer pricing assessments

The statute of limitations on assessment in Mexico is five years. The term is affected by amended returns with respect to items changed, and it is suspended by audit. The SAT has two years to complete a transfer pricing audit.

## Return disclosures/related-party disclosures

Mexican taxpayers must submit a transfer pricing return to the SAT (Exhibit 9) which is due contemporaneously with the submission of the annual tax return. Information to be disclosed includes non-resident related-parties' tax address and tax identification number, transaction classifications, amounts, methods to be applied for analyses and profit or loss obtained. The information return must be filed by 31 March of each year.

## Audit risk/transfer pricing scrutiny

High audit risk focusing on business restructuring (limited risk structures, migration of intangible property and centralization of functions and risks in favorable tax jurisdictions), highly leveraged structures, cost-sharing agreements, and pro-rata based management fees.

## APA opportunity

Unilateral and bilateral APAs are available under Article 34-A of the Federal Fiscal Code and Mexico's tax treaties. Unilateral APAs can cover the fiscal year of the application, the three subsequent fiscal years and a one-year rollback.


# Netherlands

## Taxing authority and tax law

Tax authority: Dutch Tax Administration (Belastingdienst)

Tax law:

- Tax authority Articles 3.8 and 3.25 of the Dutch Income Tax Act 2001
- Articles 8 and 8b of the Dutch Corporate Income Tax Act 1969
- Effective 1 January 2002, Article 8b codifies the arm's length principle and introduces transfer pricing documentation requirements in the Netherlands that came into force

## Relevant regulations and rulings

Besides the articles in Dutch tax law as mentioned above, the Dutch Under-Minister of Finance issued several decrees in August 2004, which bring up to date existing decrees published in 2001, with adjustments and improvements in the rules for obtaining advance certainty. These 2004 decrees provide more clarity regarding how the fiscal rules within the APA/Advance Tax Ruling (ATR) practice should function. Furthermore, one decree clarifies how the tax authorities will treat certain issues regarding the application of the arm's length principle. The decrees provide the formal position of the tax authority, but do not legally bind the taxpayer.

The eight decrees published are:

- APA decree, IFZ2004/124M
- ATR decree, IFZ2004/125M
- Decree regarding financial service activities, IFZ2004/126M
- Questions and answers on the decree regarding service entities and grandfather regime ruling policy, IFZ2004/127M
- Decree on advance certainty and good faith versus treaty partners, DGB2004/1337M
- Decree on APAs, advance tax rulings (atrs), financial services entities, interposed holdings, contact point potential foreign investors, organization and competency rules, DGB2004/1338M
- Implementation decree regarding the Coordination Group Transfer Pricing, DGB2004/1339M
- Adjustments to the transfer pricing decree of 30 March 2001, application of the arm's length principle and the OECD guidelines, IFZ2004/680M

## OECD guidelines treatment

The tax authority in general follows the OECD guidelines. Further guidance regarding the interpretation and application of the arm's length principle is provided by the Dutch transfer pricing decrees (as published by the Under-Minister of Finance in the decree of 30 March 2001, updated with the decree of 21 August 2004). According to these decrees, the OECD guidelines leave room for interpretation or require clarification on several issues. The goal of these decrees is to provide insight into the position of the tax authority regarding these issues. The transfer pricing decree of August 2004 is an excellent source for transfer pricing guidance. It provides specific guidance on intra-group services and shareholder activities, support services, contract research, cost contribution arrangements, arm's length price determination when the value at the time of the transaction is uncertain and other topics. With respect to business restructuring no specific guidance has been issued to date but as already noted the tax authority in general follows the OECD guidance in this respect.

## Priorities/pricing methods

There is no "best method" rule. Taxpayers are in principle free to choose any OECD transfer pricing method as long as the method chosen results in arm's length pricing for the transaction. Taxpayers are not obligated to test all the methods, though they must substantiate the method chosen. The tax authority prefers traditional transaction methods over transactional profit methods.

# Netherlands (continued)

### Transfer pricing penalties

The lack of transfer pricing documentation will shift the burden of proof regarding the arm's length nature of the transfer prices used to the taxpayer.

During the parliamentary discussions regarding the introduction of the arm's length principle and transfer pricing documentation requirements (i.e., Article 8b) into the Dutch Corporate Income Tax Act, a question was raised regarding the Dutch policy in connection with the levying of administrative penalties in case of a transfer price adjustment. The Dutch Under-Minister of Finance declared that in case of transfer price adjustments the levy of an administrative penalty under the circumstance of an incorrect income tax return should be limited to cases in which it is plausible that the agreed transfer price is not regarded as arm's length as a result of a pure intentional act. Therefore, an administrative penalty will not be imposed even in the case of gross negligence or conditional intentional act according to this policy announcement.

In case of a pure intentional act as set forth above, the tax may be increased with a maximum penalty of 100% of the (additional) tax due, plus interest.

### Penalty relief

It is unlikely that there will be transfer pricing-related tax penalties if there is proper transfer pricing documentation available by the taxpayer and the documentation at hand adequately substantiates the arm's length nature of the intercompany transactions undertaken by the taxpayer.

### Documentation requirements

Taxpayers are obliged to prepare documentation that describes how the transfer prices have been established and which must be included in the accounting records. Furthermore, the documentation needs to include sufficient information that would enable the tax authority to evaluate the arm's length nature of the transfer prices applied between associated enterprises. The parliamentary explanations to Article 8b do not describe an exhaustive list of information that should be documented.

- The transfer pricing documentation could consist of the following elements:
- Information about the associated enterprises involved
- Information on the intercompany transactions between these associated enterprises
- A comparability analysis, describing the five comparability factors as set forth in Chapter I of the OECD guidelines
- A substantiation of the choice of the transfer pricing method applied
- A substantiation of the transfer price charged
- Other documents, such as management accounts, budgets and minutes of shareholder and board meetings

### Documentation deadlines

Documentation is generally expected to be available at the time when the taxpayer enters into a transaction. This has been communicated by the Dutch Ministry of Finance. However, if the transfer pricing documentation is not available upon the request of the tax authority, taxpayers are granted a minimum time frame of four weeks to prepare the documentation. This period may be extended to a maximum of three months depending on the complexity of the intercompany transactions in which the taxpayer is engaged.

# Netherlands (continued)

## Statute of limitations on transfer pricing assessments

The statute of limitations on transfer pricing assessments is the same as the statute of limitations on tax assessments (as covered by the General Tax Act). The statute of limitations for making an assessment is three years from the end of the fiscal year. If the tax inspector has granted an extension for filing the tax return, the assessment period is extended with the period of extension. An additional assessment must be made within a period of five years, starting from the end of the fiscal year (this period will also be extended with the possible period of the filing extension). With respect to foreign-source income, the period for making an additional assessment is 12 years. For the tax authority to be able to impose such an additional assessment, there needs to be a new fact which the tax authority did not know or could reasonably not have known upon the moment of imposing the initial tax assessment (unless the taxpayer did not act in good faith).

## Return disclosures/related-party disclosures

Dutch corporate income taxpayers are required to confirm in the corporate income tax return (by checking a separate box) whether they have been involved in related-party transactions during the fiscal year. The related-party transactions need to be specified in a separate appendix to the Dutch corporate income tax return.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being scrutinized during a tax authority audit is high and consequently the controversy risk is high as well. Transfer pricing is a key issue in any tax audit, and many companies are subject to separate transfer pricing audits. A functional analysis is incorporated into many of these audits and forms the basis of transfer pricing risk analyses of taxpayers. The tax authority has, among others, shown interest in performing head office audits (which include intra-group services and other activities performed by the head office) and characterizations in terms of alignment of functions and risks. Next to head office activities intangibles transactions are being evaluated, as well as business reorganizations. The tax authority has also focused, as a natural result of the risk analyses, on transactions with entities located in low effective tax rate countries.

## APA opportunity

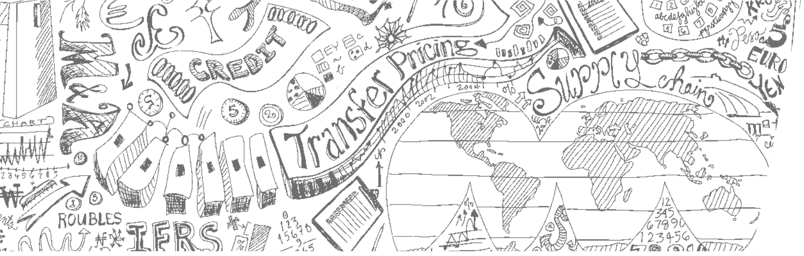
Unilateral, bilateral and multilateral APAs with rollback features are available. The APA process currently operates well in the Netherlands, despite earlier criticism regarding the uncertainty of obtaining APAs for financial service entities (see below). Pre-filing meetings with taxpayers to discuss the case before a formal APA request is made, support for small taxpayer APAs and case management plans have been introduced and processing time has been reduced.

Financial services entities consist of both financing (mere receipt and payment of intercompany interest) and licensing (mere receipt and payment of intercompany royalties) companies. For license companies, the first APA under the new regime was granted by the tax authority in 2005. For finance companies, the APA process had been functioning successfully for a number of years already by 2005.

A number of substantial improvements for Dutch financial services entities were introduced in 2005, which mainly relate to a reduction in the applicable transfer pricing documentation requirements.

### Mutual agreement procedure

On 29 September 2008 a decree (IFZ2008/ 248M) describing the Mutual Agreement Procedure (MAP) process under bilateral treaties and the EU arbitration convention has been published. The decree aligns the MAP process in the Netherlands with the OECD Memorandum on Effective Mutual Agreement Procedures (MEMAP) making the route to obtaining avoidance of double taxation more accessible and transparent for taxpayers. Key features of the new Decree are: formal introduction of an Accelerated Competent Authority Procedure (ACAP); endorsement of arbitration to resolve MAP cases; targeting a reduction of MAP related expenses; introducing transparency into the process by providing regular feedback and updates to the taxpayer; encouraging use of Article 9(2) of the *OECD Model Tax Convention*; commitment to tackle resolution of double taxation in cases "not provided for in the Convention" (Article 25(3) of the *OECD Model Tax Convention*) in addition to the more traditional double taxation cases.




# New Zealand

## Taxing authority and tax law

Tax authority: Inland Revenue Department (IRD)

Tax law:

- Sections YD 5, GB 2 and GC 6 to GC 14 of the Income Tax Act 2007
- Relevant double-tax agreements

## Relevant regulations and rulings

The final version of Transfer Pricing Guidelines issued in October 2000

## OECD guidelines treatment

The IRD fully endorses the positions set out in chapters one to eight of the OECD guidelines and proposes to follow those positions in administering New Zealand's transfer pricing rules. Consequently, New Zealand's guidelines should be read as supplementing the OECD guidelines, rather than superseding them. This applies for the domestic application of the New Zealand rules, as well as in relation to issues raised under New Zealand's double tax agreements. On business restructuring, IRD's approach seems to be largely in line with the recently published OECD paper. The IRD are cognizant of the fact that multinational enterprises undergo restructuring activities during the course of their existence and lifecycle. In addressing the restructuring issues, IRD will be seeking to ensure that there is a commercial case for effecting any restructure and that the economic substance aligns with the legal form of the arrangement. The IRD has released some high-level guidance in the form of the following ten questions that should be addressed by companies undertaking cross-border business restructures. These questions aim to help ascertain the commercial viability of the restructuring.

## Priorities/pricing methods

The IRD accepts the most reliable method chosen from CUP, Resale Price, Cost Plus, Profit Split and CPM (TNMM).

## Transfer pricing penalties

Penalties are imposed under §141A-K of the Tax Administration Act 1994: 20% penalty for not taking reasonable care, 20% penalty for an unacceptable tax position, 40% penalty for gross carelessness, 100% penalty for an abusive tax position and 150% penalty for an evasive or similar act.

## Penalty relief

Shortfall penalties may be reduced upon voluntary disclosure to the Commissioner of the details of the shortfall. If the disclosure occurs before notification of an investigation, the penalty may be reduced by 100% (only for lack of reasonable care or unacceptable tax position categories) or 75% for other shortfall penalties. If disclosure occurs after notification of an investigation, but before the investigation commences, the penalty may be reduced by 40%. Shortfall penalties may be reduced by a further 50% if a taxpayer has a past record of "good behavior."

## Documentation requirements

There are no explicit requirements in New Zealand's transfer pricing legislation (§§GC 6 to GC 14 of the Income Tax Act 2007) for any particular category of information to be included in transfer pricing documentation. Section GC 13 requires taxpayers to select and apply an appropriate transfer pricing method for tax return purposes. The New Zealand Transfer Pricing Guidelines indicate that a taxpayer's main purpose in preparing and maintaining documentation should be to place the taxpayer in the position where they can readily demonstrate to the IRD that a transfer pricing method has been used to determine whether the taxpayer's transfer prices are consistent with the arm's length principle in light of the facts and circumstances.

# New Zealand (continued)

## Documentation deadlines

There is no express legislative requirement for a taxpayer to document its transfer pricing policies and practices in New Zealand. However, the New Zealand Transfer Pricing Guidelines indicate that taxpayers who prepare and maintain transfer pricing documentation are more likely to ensure the burden of proof (that prices are not arm's length) remains with the Commissioner.

## Statute of limitations on transfer pricing assessments

The Commissioner's power to issue amended assessments is subject to a four-year time limit. A taxpayer has the ability to extend the applicable time bar by up to an additional six months by signing a waiver, which generally arises when a dispute is not resolved, and more time would allow completion of the dispute process by mutual agreement of both parties or where another case before the court is likely to resolve the issue in current dispute.

## Return disclosures/related-party disclosures

A company's income tax return requires disclosure of:

- Payments to non-residents such as dividends, interest, management fees, "know-how" payments, royalties or contract payments made
- Whether the company is controlled or owned by non-residents
- Whether the company holds an interest in a controlled foreign company ("CFC")

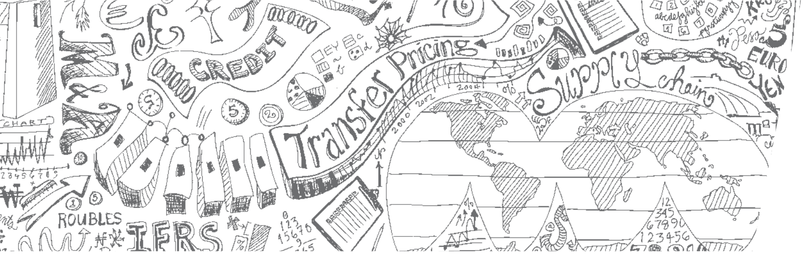
More detailed disclosure of various financial information and other data is now required for interests held in CFCs.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing scrutiny during a tax audit is high. Risk Assessment Review questionnaires relating to transfer pricing and thin capitalization are typically issued to companies during general income tax audits or risk reviews and as part of the IRD's specific transfer pricing review process. The IRD also uses questionnaires in respect of interest, guarantee fees and royalties. In addition, there is a separate transfer pricing questionnaire for branches.

## APA opportunity

Section 91E of the Tax Administration Act 1994 allows a unilateral APA to be issued in the form of a binding ruling. Bilateral or multilateral APAs may be entered into pursuant to New Zealand's double tax agreements under the mutual agreement procedure provisions. The IRD has not established any formal guidelines for APAs, as each case is considered to be different, depending on a taxpayer's specific facts and circumstances. The IRD has suggested pre-application conferences to make the APA application process less time consuming.




# Norway

## Taxing authority and tax law

Tax authority: The Norwegian Tax Authority (NTA)

Tax law: The arm's length principle is stated in the Taxation Act (1999) §13-1, and the transfer pricing filing and documentation requirements are stated in the Tax Administration Act (1980) §4-12

## Relevant regulations and rulings

In June 2007, the Norwegian Parliament adopted new transfer pricing regulations (Tax Administration Act §4-12). The requirements became effective as of January 2008. The transfer pricing requirements consist of two specific parts: filing and documentation requirements.

The Ministry of Finance also published guidelines to the Norwegian Documentation requirements in 2007. These guidelines outline specific requirements to include in the Norwegian Documentation.

## OECD guidelines treatment

The NTA has a long history of following the OECD Transfer Pricing Guidelines (OECD TPG). The Norwegian regulations follow OECD principles, and documentation prepared in line with the OECD TPG will generally meet the Norwegian requirements.

The Taxation Act §13-1 gives the OECD TPG a strong and formal status under Norwegian tax law. However, OECD TPG chapter IV (Administrative Approaches to Avoiding and Resolving Transfer Pricing Disputes) and chapter V (Documentation) are not included. The status of the OECD TPG is limited to that of guidance, and they do not constitute binding rules.

We have also seen that the principles outlined in OECD TPG chapter IX on the Transfer Pricing Aspects of Business Restructurings are being applied by the NTA. Recent tax audits and court cases have shown that the principles described in the OECD TPG chapter IX are applied in practice.

## Priorities/pricing methods

The OECD pricing methods are accepted by the NTA. The traditional transaction methods (CUP, RPM and Cost Plus) are generally preferred to the transactional profit methods (TNMM and Profit Split). There seems to be increasing support for the applicability of the profit methods under certain circumstances.

There is no specified priority under Norwegian tax law. As stated by the Norwegian Supreme Court, the Taxation Act §13-1 allows for the use of several transfer pricing methods, including methods not described by the OECD TPG, provided those methods will provide arm's length results.

## Transfer pricing penalties

Transfer pricing penalties (surtax) is 30% of the tax adjustments, provided that the tax authority concludes that incomplete or incorrect information has been provided by the tax payer. If complete and correct information has been provided, no penalty will be imposed. In case of gross negligence, a surtax of up to 60% may be levied. However, the normal surtax rate is 30%. Additionally, a non-deductible interest charge will apply per year.

Failure to comply with the filing requirement (described below) will carry the same penalties and risk as failure to complete the annual tax return. The same is applicable if the documentation is not submitted by the deadline.

## Penalty relief

A 30% penalty is normal; however, the risk of a penalty being imposed may be reduced if proper documentation has been prepared.

Disclosure in the tax return may in principle relieve penalties, as the tax authority will then have been informed and may further investigate the transfer pricing case. The application of penalties is, however, becoming increasingly common.

# Norway (continued)

## Documentation requirements

The transfer pricing requirements consist of two specific parts: filing and documentation requirements.

The filing requirement is an attachment to the annual tax return (RF-1123), which includes a listing of all intercompany transactions. The form will serve as a basis for the NTA when targeting transfer pricing tax audits. The filing requirements are applicable for all transactions reported in the tax return.

In addition, covered taxpayers are obliged to prepare transfer pricing documentation that describes how the transfer prices have been established between associated enterprises. The documentation needs to include sufficient information that would enable the NTA to evaluate the arm's length nature of the transfer prices applied between associated enterprises. Both cross-border and domestic transactions are covered. Specific requirements worth mentioning are:

- Key Financial figures on all transaction parties to the Norwegian Entity
- Description of how the transfer price on a transaction is computed
- The level of detail required will depend on the complexity of the transaction and in particular, if the transaction is of high value, intangibles are involved, and/or there may be a tax motivation for pricing the transaction on non-arm's length conditions

## Documentation deadlines

The transfer pricing documentation must be submitted within 45 days after a request by the NTA. All documentation must be retained for 10 years. The tax authority assumes that documentation is made on a contemporaneous basis, and will accordingly, not allow for extensions.

## Statute of limitations on transfer pricing assessments

The general statute of limitations for tax assessments in Norway states that issues regarding the tax return cannot be raised more than 10 years after the end of the income year. Transfer pricing documentation must therefore be retained and stored for at least 10 years.

The deadline is three years for changes of the tax return based on the tax authority's discretionary assessments, or the interpretation of the tax legislation, if the tax return filed is correct and complete.

The statute of limitations is two years if any tax adjustment is against the taxpayer, provided the taxpayer has not given incorrect or incomplete information to the tax authority.

## Return disclosures/related-party disclosures

The filing requirement is an attachment to the annual tax return (RF-1123), which includes a listing of all intercompany transactions. The form will serve as a basis for the NTA when targeting transfer pricing tax audits. The filing requirements are applicable for all transactions reported in the tax return.

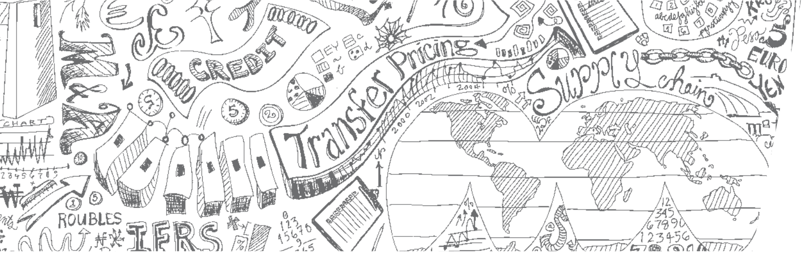
## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being reviewed during an audit is high. The tax authority has a strong focus on intercompany transactions and has established an in-house transfer pricing network where the major tax offices, including the Directorate of Taxes, are members. The introduction of the 2007 transfer pricing documentation and filing requirements exemplifies the increased transfer pricing focus. The NTA has launched a transfer pricing audit campaign against Tax Effective Supply Chain Management (TESCM) conversions, and the first cases have been brought to court. Situations especially targeted by the tax authority are limited risk distributors or commissionaires with low margins and those that have recently experienced reduction in margins.

In addition, the transfer pricing of intangible property and finance-related transfer pricing (loans, etc.) is expected to be a focus area for the NTA going forward.

## APA opportunity

APAs on transfer pricing assessments are currently unavailable. There is one exemption for the transfer pricing on the sale of gas under the Petroleum Taxation Act.




# Panama

## Taxing authority and tax law

Tax authority: Tax Administration of Panama (Dirección General de Ingresos, or "DGI")

Tax law: Law 33 enacted in 2010 established the Transfer Pricing provisions in the Tax Code (Chapter IX of Title I of the Fourth Book); Articles 762-A to 762-K

## Relevant regulations and rulings

Regulations are pending to be enacted by the tax authority regarding penalties and general guidelines, including the guidelines that would provide the contents of the transfer pricing return.

According to Article 762-D of the Tax Code, transfer pricing provisions apply only to intercompany transactions conducted by a Panamanian taxpayer with related parties resident in countries with which Panama has signed treaties to avoid double taxation.

Law No. 33 would become applicable for the period commencing after the tax treaties enter into force.

## OECD guidelines treatment

The OECD guidelines can be relied upon for interpretation of the rules as long as they do not contradict the Panamanian Tax Code or international tax treaties.

## Priorities/pricing methods

The transfer pricing methods in Panama are: the CUP, Resale Price, Cost Plus, Profit Split, Residual Profit Split and TNMM. The selection of the method should be based on the characteristics of the transaction under analysis, the circumstances of the case and the one that best respects the arm's length principle.

## Transfer pricing penalties

Transfer pricing penalties are pending to be determined by the tax authority. However, it is expected that penalties will be issued following what other countries in the Latin American region apply.

## Penalty relief

No penalty relief regime in place.

## Documentation requirements

Contemporaneous transfer pricing documentation related to cross-border intercompany transactions must be kept and maintained. Documentation must include the complete identification details of the taxpayer and of the non-resident related parties with whom transactions are carried out; a detailed description of the nature, characteristics and amount of all the intercompany transactions of the taxpayer including the transfer pricing method employed. It is also necessary to include the method selection process and the specification of the price or margin, or range of prices or margins applied by the taxpayer in its intercompany transactions. Also, the documentation must be prepared considering the complexity and volume of the transactions and should include the information that the taxpayer had used to determine the evaluation of the intercompany transactions consisting of information about the multinational group the taxpayer belongs to and of the taxpayer itself.

The information of the multinational group contained in the documentation should include:

- A general description of the organizational, legal and operating structure of the group, with any relevant relating changes, as well as the identification of the related parties to whom the taxpayer conducts intercompany transactions
- The transfer pricing policy of the multinational group, if any

# Panama (continued)

## Documentation deadlines

Documentation must be readily available by due date of the tax return and must be kept along with the company's accounting records. If requested by the tax authority, documentation should be provided within 45 days from the notification.

Taxpayers should file annually an information return on the transactions conducted with related parties residents in the countries with which Panama entered treaties to avoid double taxation, which shall be filed at the most six months after the closing date of the fiscal year, in the terms the tax authority approves in the regulations yet to be prepared.

Law No. 33 would become applicable for the period commencing after the tax treaties enter into force.

## Statute of limitations on transfer pricing assessments

The statute of limitations on assessments is three years. The term is affected by amended returns.

## Return disclosures/related-party disclosures

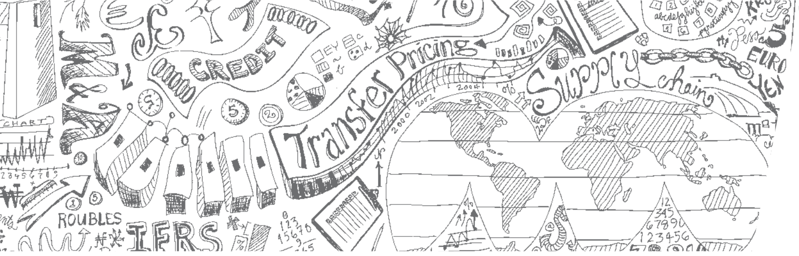
An information return on the transactions conducted with related parties residents in the countries with which Panama entered treaties to avoid double taxation should be filed annually. The terms are pending to be approved by the tax authority.

## Audit risk/transfer pricing scrutiny

The tax authority has not yet initiated any tax audits regarding transfer pricing issues due to the fact that the transfer pricing regulations are new in the country. At the moment, the tax authority is working on the creation of the Transfer Pricing Unit within the tax authority and 2011 will be the first year of application of the transfer pricing rules.

## APA opportunity

APA programs are not specifically addressed.




# Peru

## Taxing authority and tax law

Tax authority: Superintendencia Nacional de Administración Tributaria (SUNAT)

Tax law: Article 32, Items 4 and 32-A of the Peruvian Income Tax Law (PITL)

## Relevant regulations and rulings

Transfer pricing regulations were in force as of 1 January 2001 (Article 32 of PITL). Subsequently, Legislative Decree 945 and Legislative Decree 953 introduced transfer pricing amendments into the PITL and tax code, which were in force as of fiscal year 2004. The regulations are detailed in Article 24 and Chapter XIX (Articles 108 to 119) of the Peruvian Income Tax Regulations.

The transfer pricing rules will be applicable solely when the valuation agreed by the parties determines an income tax lower than the one it would have been calculated if the market value would have been considered. To this effect, the Regulations consider that a lower income tax is also determined when: i) the deferral of income is detected, or ii) the calculation of higher tax losses than the ones that would have corresponded.

In addition, the transfer pricing rules apply both to cross-border and domestic transactions between related parties. Moreover, all transactions with tax haven residents are considered to be with related parties. Thus, they are subject to the transfer pricing regulations.

In the case of domestic transactions, the transfer pricing rules must be considered not only for income tax purposes but also for VAT and excise tax.

## OECD guidelines treatment

The PITL refers to the OECD guidelines as a source of interpretation for transfer pricing analysis as long as they do not contradict the PITL.

## Priorities/pricing methods

Peruvian law implicitly adopts a best-method rule. Under Peruvian legislation, the transfer pricing methods identified are CUP, Resale Price, Cost Plus, Profit Split, the Residual Profit Split and Transactional Net Margin Method.

## Transfer pricing penalties

Non-compliance with the obligation to present a transfer pricing technical study, or documentation and information supporting the calculation of the prices agreed on in transactions with related parties, is penalized with a fine of 0.6% of the company's net income of the year before that under scrutiny. The penalty cannot be less than 10% of a Tax Unit, nor more than 25 Tax Units (one Tax Unit is equivalent to approximately US$1,300).

Likewise, non-compliance with the obligation to file the transfer pricing return according to the dates established by SUNAT is subject to a fine of 0.6% of the company's net income of the year before that under scrutiny. The penalty cannot be less than 10% of a Tax Unit nor more than 25 Tax Units.

The adjustments to annual taxable income resulting from the tax authority's application of the transfer pricing provisions will be subject to additional penalties that may be up to 50% of the resulting tax deficiency (income misstatement penalties).

## Penalty relief

The penalty reductions that a taxpayer can be subject to for not complying with the obligations of having a transfer pricing technical study or presenting the transfer pricing informative return are the following:

- 80% penalty reduction if the taxpayer rectifies the infraction and pays the corresponding fine within the time established by SUNAT
- 50% penalty reduction if the taxpayer rectifies the infraction but does not pay the corresponding fine within the time established by the SUNAT
- 100% penalty reduction if the taxpayer files the transfer pricing informative return after the due date but before it is detected and compelled to do so by SUNAT

# Peru (continued)

## Documentation requirements

Since 2006, taxpayers are compelled to keep a transfer pricing study if they fall within the scope of the transfer pricing rules contained in Article 32-A of the PITL and if they meet any of the following conditions:

- The company's income exceeds PEN6m and the amount of its intercompany transactions exceeds PEN1m.
- The company has been engaged in transactions from, to or through a low-tax jurisdiction.

## Documentation deadlines

There is no deadline to present the transfer pricing study to the tax authority. Nevertheless, as provided in Resolution N°167-2006-SUNAT, the tax authority can request a transfer pricing study from taxpayers once the fiscal year is closed.

According to the tax regulations published in 2010, the deadline for filing the transfer pricing return for the fiscal year 2010 onward is in June of the year that follows the year of the corresponding transfer pricing return.

## Statute of limitations on transfer pricing assessments

According to Articles 87-7 and 43 of the Peruvian Tax Code, the statute of limitations on income tax assessments is four years after 1 January of the year that follows the year the annual income tax return is due (generally, 31 March) and six years for returns that were never filed.

## Return disclosures/related-party disclosures

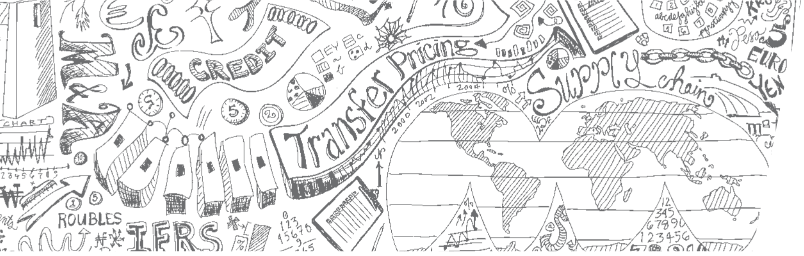
The main aspects to be disclosed in the transfer pricing information return are the amount of the transactions, the transfer pricing method selected, the related party with which the transactions were made and the amount of the adjustments, among others.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being reviewed during a tax audit is moderate. The Peruvian Tax Administration has already initiated tax audits regarding transfer pricing issues. Nevertheless, not many taxpayers are being audited. It is expected that SUNAT will increase its audit reviews in the years to come.

## APA opportunity

APAs are available for cross-border transactions only.




# Philippines

## Taxing authority and tax law

Tax authority: The Bureau of Internal Revenue (BIR)

Tax law: Under Section 50 of the National Internal Revenue Code of 1997, as amended, the Commissioner of Internal Revenue has the power to allocate income and expenses between or among related parties/taxpayers or make transfer pricing adjustments to reflect the true taxable income of taxpayers.

## Relevant regulations and rulings

Revenue Memorandum Circular (RMC) No. 26-08 formally adopted the OECD Transfer Pricing Guidelines as the interim transfer pricing guidelines in the Philippines. The RMC specifically states that the BIR, as a matter of policy, subscribes to the OECD Transfer Pricing Guidelines, and until the draft regulations are issued, any and all concerns on transfer pricing shall be resolved in accordance with said Guidelines.

In July 2009, the BIR issued Revenue Memorandum Order (RMO) No. 23-2009 mandating the National Investigation Division (NID) of the BIR to audit, among others, interrelated companies and conglomerates, including their officers and related individual taxpayers, to ensure that such taxpayers are clearly reflecting income and expenses that are attributable to controlled and inter-related transactions. The RMO further states that various schemes being employed by conglomerates and group of companies to reduce the amount of taxes shall be identified, such as (but not limited to) the use of tax-exempt entities or those with special tax privileges, inter-related company loans and advances, cost sharing, and the supply of goods and services. In the conduct of audit, particular attention shall be given to transfer pricing issues which should be considered in the audit findings of the taxpayers.

This was followed by RMO No. 36-2010 issued in March 2010 which prescribed the rules and procedures governing the conduct of special investigation and enforcement activities of interrelated companies, conglomerates, their affiliates and subsidiaries for taxable year 2009. The RMO amends RMO No. 23-2009 and now directs the Large Taxpayers Service and the Enforcement Service to identify the conglomerates consisting of interrelated companies (parent company, affiliates and subsidiaries) that will be subject for audit under the program. The investigation shall cover all internal revenue taxes for taxable year 2009 and has to be completed no later than six months from the issuance of the letter of authority (LA).

## OECD guidelines treatment

The BIR not only adheres to the OECD TP Guidelines but has in fact formally adopted the OCED TP Guidelines as the interim transfer pricing guidelines in the Philippines through RMC No. 26-08 (see above).

## Priorities/pricing methods

The methods to determine the arm's length price under the OECD TP Guidelines such as CUP, Resale Price, Cost Plus, Profit Split and TNMM are accepted in the Philippines.

## Transfer pricing penalties

There are no specific rules prescribing for penalties for failure to properly document intercompany transactions. In case of a deficiency assessment due to a transfer pricing adjustment, the general penalties apply such as the 25% surcharge (50% in fraud cases) and 20% interest per annum.

## Penalty relief

There is currently no penalty relief regime in place.

# Philippines (continued)

## Documentation requirements

There are no rules formally requiring specific documentation for related party transactions but since the Philippines has formally adopted the OECD TP Guidelines, there is an implied requirement to have documentation in place that is consistent with the guidelines on documentation under the OECD TP Guidelines.

Under the draft transfer pricing regulations, however, the following information are required or expected by the BIR from a taxpayer to support their intercompany pricing policies:

- General information on the group, such as:
  - Worldwide organizational structure showing the location and ownership linkages among related parties
  - Group's line of business, industry dynamics, market, regulatory and economic conditions in which the group operates
  - Group's business models and strategies (past, present and future);
  - Principal business activities and functions of each party in the group; business relationships among related parties; consolidated financial statements of the group for the last three years, including the year the controlled transactions occurred
- Information on each related-party in the Philippines (Philippine entity), such as:
  - General information, such as company registration number, address, etc.
  - Entity's line of business, industry dynamics, market, regulatory and economic conditions in which the entity operates
  - Entity's business models and strategies (past, present and future)
  - Entity's functions, risks and assets employed
  - Financial Statements, including detailed profit and loss statements for the last three years, including the year when the controlled transaction occurred
- Details on transactions between the Philippine entity and all related parties, such as:
  - Detailed information on all transactions with related parties
  - Contracts or agreements (if any) to show the terms of the transactions
  - Segmented financial accounts with respect to the transactions, including explanations on the assumptions (if any) used to derive the segmented information for the last 3 years, including the year when the controlled transactions occurred
- Transfer pricing analysis, which shall include:
  - Choice of the tested party and the reasons supporting the choice
  - Details on comparables and the screening criteria for choosing comparables
  - Comparability analysis of the related party transactions and the comparables
  - Details of (and reasons for) the adjustments deemed necessary to be made to achieve comparability
  - Transfer pricing method chosen and explanation why the method is most appropriate
  - Determination of the arm's length price/ margin, showing the detailed computation and explanation of any assumption made
  - If an arm's length range is determined, furnish details/ reasons to support the determination and use of the range

    And
- Other useful information, such as a list of any known comparable companies having transactions similar to the controlled transactions

# Philippines (continued)

### Documentation deadlines

There is no requirement for contemporaneous submission of documentation when tax returns are filed. However, under the draft transfer pricing regulations, documentation must be submitted to the BIR within 45 days of the BIR request.

### Statute of limitations on transfer pricing assessments

The general prescriptive period applies which is three years after the last day prescribed by law for filing of the return, except in cases of fraud with intent to evade tax where the prescriptive period is 10 years from discovery of fraud.

### Return disclosures/related-party disclosures

Related-party disclosures are required only in the Notes to the Audited Financial Statements which is required to be filed with the BIR together with the Annual Income Tax Return.

### Audit risk/transfer pricing scrutiny

The risk of a TP audit is medium to high as the BIR has started conducting TP audits pursuant to the RMOs mentioned above.

### APA opportunity

There is currently no APA procedure in place.


# Poland

## Taxing authority and tax law

- Corporate Income Tax Act dated 15 February 1992 (CIT Act), Articles 9a, 11 and 19 §4 (Journal of Laws No. 21, item 86)
- Personal Income Tax Act dated 26 July 1991 (PIT Act) Articles 25, 25a and 30d (Journal of Laws No. 80, item 350)
- Tax Ordinance Act dated 29 August 1997, Articles 20a-20r (Journal of Laws No. 137, item 926)
- Ministry of Finance Decree of 16 May 2005, on the countries and territories applying harmful tax competition rules (Journal of Laws No. 94, item 791)
- Ministry of Finance Decree of 10 September 2009, on the method and procedure for assessing taxpayers' income by estimating the prices in transactions conducted by these taxpayers, and on the method and procedure for eliminating double taxation of taxpayers in case of related-parties' income adjustment ( Journal of Laws No. 160, item 1268)

## Relevant regulations and rulings

Article 11 of CIT Act and Article 25 of PIT Act introduce the arm's length principle, providing a definition of affiliation and criteria for the determination of the size of direct and indirect shares held in another entity. Documentation requirements can be found in Article 9a of the CIT Act and Article 25a of the PIT Act. Transfer pricing penalties are defined in Article 19 §4 of the CIT Act and Article 30d of the PIT Act.

Article 9a of the CIT Act and Article 25a of the PIT Act provide detailed information on transactions which are subject to documentation requirements, including value limits and categories of such transactions.

According to Articles 9a of the CIT Act and 25a of the PIT Act, the documentation requirements also encompass transactions in which payment is made directly or indirectly to an entity in a territory or country considered to be a tax haven. The list of these territories and countries is presented in the Ministry of Finance Decree of 16 May 2005, on the countries and territories applying harmful tax competition rules. The Decree was issued separately for personal and corporate taxation purposes.

As of 1 January 2007, documentation requirements apply also to permanent establishments (based in Poland) of foreign companies.

The pricing methods recognized by the tax authorities are described in the Ministry of Finance Decree of 10 September 2009. This Decree replaces the one dated October 1997 where the major changes concern redefinition of selected TP methods (more precise description) and introduction of the corresponding adjustment procedure (based on the OECD guidelines, Arbitration Convention and Code of Conduct for Arbitration Convention and the revised Polish corporate income tax act, i.e. as of 1 January 2009). Provisions of the Decree apply also to Polish permanent establishments of the foreign companies and foreign permanent establishments of the Polish taxpayers.

The APA regulations are specified in Articles 20a-20r of the Tax Ordinance Act. Introduction of APAs has brought with it special reporting requirements. According to the Ministry of Finance Decree of 31 May 2006, taxpayers who have agreed to an APA must submit together with their annual CIT return a progress report on the implementation of the method stipulated in the APA decision. APA may also be concluded by permanent establishments of foreign companies in Poland as well as permanent establishments of Polish taxpayers, based abroad.

## OECD guidelines treatment

The Polish transfer pricing regulations do not refer to the OECD guidelines directly. Reference to the OECD guidelines is made with respect to the topic of tax havens. According to Article 9a §6 of the CIT Act (Article 25a §6 of the PIT Act), the list of countries recognized as tax havens is issued with regard to settlements made by the OECD. At the same time, the transfer pricing methods presented in the Polish rules are based on the OECD approach. There are no specific rules regarding the business restructuring issues in the Polish transfer pricing law. The OECD business restructuring report should, however, be an indication for the tax authorities when verifying the restructuring cases in Poland.

# Poland (continued)

## Priorities/pricing methods

Generally, the transfer pricing methods accepted by the tax authorities are based on the OECD guidelines. These methods are: CUP, Resale Price, Cost Plus, Profit Split and TNMM. The traditional methods are preferred. When the transfer price is determined by the tax authorities, the application of CUP method is verified in the first instance.

If a taxpayer has determined the arm's length value of a transaction by applying one of the three accepted traditional methods (CUP, Resale Price and Profit Split), and there is no doubt about the objectivity in choosing the method, the method is also binding on the tax authorities.

## Transfer pricing penalties

Taxpayers face a 50% penalty tax rate for income assessed by the tax authorities (instead of the standard tax rates).

## Penalty relief

The penalty rate can be reduced to the normal tax rate only if the taxpayer provides the required documentation in due time as specified by the tax authorities (7 days on request).

## Documentation requirements

Taxpayers carrying out transactions with related-parties and permanent establishments of foreign companies functioning in Poland, as defined in the Polish CIT and PIT Acts, are obliged to prepare tax documentation. Requirements for such transactions apply where the total transaction amount in a tax year exceeds the following limits:

- EUR 100,000 if the transaction value does not exceed 20% of the share capital
- EUR 30,000 if the transaction refers to services or intangibles
- EUR 50,000 for other types of transaction between related entities

Taxpayers carrying out transactions in which payments are made directly or indirectly to an entity in a territory or country recognized as a tax haven are obliged to prepare tax documentation for such transactions when the total transaction amounts in a tax year exceed EUR 20,000.

As there is no required specific form for transfer pricing documentation, the CIT and PIT regulations instead determine the extent of the documentation. The statutory transfer pricing documentation should cover at least the following elements:

- Functions performed by the parties to the transaction (with the consideration of assets employed and risks borne)
- Expected transactional costs and the method and payment due dates
- Method and manner of calculating profits and the transaction value
- Business strategy, if it influenced the transaction value
- Other factors influencing the transaction value
- Expected benefits from intangible performances or services -this element applies only to the purchase of intangibles or services

These elements are mandatory, so if the documentation prepared does not meet one of these requirements, such documentation may be disregarded by the tax authorities.

In addition, the statutory Polish transfer pricing documentation should be prepared and if requested, provided to the tax authorities in Polish.

## Documentation deadlines

There is no deadline for preparing the transfer pricing documentation; however, taxpayers are obliged to submit the documentation within seven days of the tax authorities' request.

# Poland (continued)

## Statute of limitations on transfer pricing assessments

There are no special time limit provisions applicable to intercompany transactions. The general regime of the statute of limitations applies in accordance with the Tax Ordinance Act. According to Article 70, §1 of the Tax Ordinance Act, the assessment period for tax is five years from assessment to the end of the calendar year in which the tax fell due.

## Return disclosures/related-party disclosures

Information about related-party transactions is one of the elements of the annual income tax return. The taxpayer is required to indicate in the return whether it was obliged to prepare transfer pricing documentation or not.

Taxpayers who have concluded APAs must enclose, with their annual tax returns, a special report on the implementation of the transaction method chosen. The form of this report is given in the Ministry of Finance Decree of 31 May 2006.

*Definition of related-parties*

Polish regulations recognize related entities in the following situations:

- The domestic entity participates directly or indirectly in managing or controlling the foreign entity or has a share in its capital
- The foreign entity participates directly or indirectly in managing or controlling a domestic entity or has a share in its capital
- The same legal and natural persons participate directly or indirectly at the same time in managing or controlling a domestic entity and foreign entity or have shares in their capital
- The domestic entity participates directly or indirectly in the managing or controlling of another domestic entity or has a share in its capital
- The same legal and natural persons participate at the same time directly or indirectly in managing or controlling domestic entities or have shares in their capital

Capital relations exist if one of the entities or contracting parties holds in the capital of the other entity, directly or indirectly, at least a 5% share. Domestic entities are also considered related for tax purposes by virtue of family, property or employment relations between them or between their management, supervision or control personnel, or if the same person carries out management, supervision or control functions in both these entities.

If the parties to a transaction, due to their relationship, agree or impose terms and conditions which differ from those that would be agreed to by unrelated parties, and as a result of these terms and conditions a domestic entity does not report income from the transaction or reports income that is lower than would be expected if the connection did not exist, the tax authorities may assess additional income and determine the tax due on such income for the domestic entity.

The above rules also apply to the allocation of taxable profit to the permanent establishment of a foreign entity in Poland and to Polish taxpayers carrying out transactions with their permanent establishments abroad.

Domestic entities transacting with foreign related-parties are allowed to adjust their income if the foreign tax authorities question the transactional prices as not meeting the arm's length principle and, consequently, additional income for the foreign entity is assessed and the tax due on such income is determined (the so-called "corresponding adjustment "). Prerequisites of making the adjustment must however be justified and accepted by the tax authorities.

Adjustments to the domestic entities' income will be allowed as long as the agreement on the avoidance of double taxation between Poland and the country (i.e., country of the domestic entity's related-party) will provide for the opportunity to do so. An application regarding such adjustments should be filed within three years since receiving the decision on assessing the additional income of the contracting party.

In addition, regulations relating to income adjustment apply also to permanent establishment.

Analogous elimination of double taxation is not allowed by Polish regulations in case of domestic related transactions.

# Poland (continued)

## Audit risk/transfer pricing scrutiny

The number of transfer pricing audits has steadily increased and the risk is growing. The risk of scrutiny and a very detailed approach of the tax authorities during transfer pricing audit and consequently a tax assessment are high. While the acceptance of OECD guidelines and international practices has increased, the local approach tends to prevail during audits. Local benchmarks are preferred over pan-European ones. The pricing information from cross-controls in the industry is used for benchmarking. Internal third-party transactions are used as a comparison for application of the CUP method, which is preferred by the tax authorities. Moreover, the tax authorities have increased cooperation in the exchange of information with other countries.

The compliance regime is still rigorous in Poland. The court rulings focus mainly on legal rather than economic issues. The most frequently audited types of transactions are limited risk structures such as limited risk distributors or contract manufacturers, immaterial services (including cost-sharing arrangements) and loans.

## APA opportunity

The APA regulations came into force on 1 January 2006. The APA procedures are described in Articles 20a-20r of the Tax Ordinance Act.

An APA concluded for a particular transaction is binding on the tax authorities with regard to the method selected by the taxpayer. APAs in Poland may apply to transactions that have not yet been executed or transactions that are in progress at the time the taxpayer submits an application for an APA. Under the Polish rules, three types of APAs are available:

- Unilateral Agreement: This type of APA is defined in the Tax Ordinance Act as an agreement on the method of setting transfer prices between:
  - Two domestic entities – those without foreign capital links
  - A domestic entity and its related foreign party
  - A domestic entity related to a foreign entity and another domestic entity related to the same foreign entity
- Bilateral Agreement: This is an agreement concerning cross-border transactions which can be given by the Polish Ministry of Finance upon the request of a domestic entity, but only after consultations and upon obtaining consent issued by the tax authorities of the related foreign entity
- Multilateral Agreement: If the agreement concerns a transaction concluded by a domestic entity with foreign entities from more than one country, in order to conclude such an agreement, the consents of all foreign entities' tax authorities are required

There are no transaction value limits to be covered by the APAs. In order to submit an application for an APA, the taxpayer must pay a fee which is usually 1% of the transaction value. However, the Tax Ordinance Act sets the following fee limits:

- Unilateral APA – fee cannot be lower than PLN5,000 and cannot exceed PLN50,000
- Unilateral APA concerning a foreign entity – fee cannot be lower than PLN20,000 and cannot exceed PLN100,000
- Bilateral or multilateral APA – fee cannot be lower than PLN50,000 and cannot exceed PLN200,000

The mandatory elements of an APA application are:

- The suggested method for determining prices and an indication of the pricing method recognized by the tax authorities
- A description of the manner of application of the suggested method, with an indication of the principles for price calculation, forecasts and analyses on which the calculation is based
- A description of the circumstances which may affect the prices
- The documents which may determine the transaction price (agreements, arrangements and other documents indicating the intentions of the parties to the transaction)

# Poland (continued)

## APA opportunity (continued)

The suggested length of the APA arrangement:

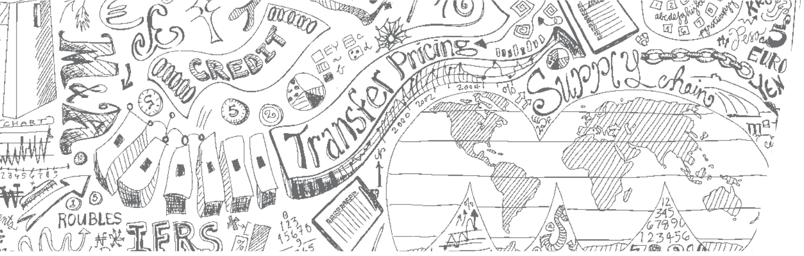
- A list of entities with whom the transaction will be concluded, including their agreement to submit to the tax authorities all documents and provide necessary explanations with regard to the relevant transaction
- The application must be submitted in the Polish language

The Tax Ordinance Act precisely defines the terms under which the APA procedure is to be completed:

- The unilateral APA must be issued without unnecessary delay within six months of the start of the APA application procedure
- The bilateral APA must be issued without unnecessary delay within 12 months of the start of the APA application procedure
- The multilateral APA must be issued without unnecessary delay within 18 months of the start of the APA application procedure

The APA is issued by the Ministry of Finance in the form of an administrative decision and the general administrative procedure resulting from the Tax Ordinance Act applies to the APA. In consequence, the above time limits for the APA procedure may be extended if necessary.

The period for which the APA may be concluded must be no longer than five years. The APA may be extended for another five years if the criteria applied in concluding the APA have not changed or the entity applies for an extension of the APA not later than six months before it expires. The decision is valid from the date of its delivery to all parties (including the Polish and foreign – if applicable - tax authorities).




# Portugal

## Taxing authority and tax law

Tax authority: Portuguese General Tax Directorate (“DGCI”)

Tax law: Article 63 of the Corporate Income Tax Code establishes the arm’s length principle

## Relevant regulations and rulings

Ministerial Order 1446-C/2001 of 21 December 2001 (Transfer Pricing Ministerial Order), issued by the Minister of Finance, implements Article 63 of the CIRC regarding the application of the transfer pricing methods, cost-sharing agreements, documentation requirements and the corresponding adjustments procedure.

A detailed APA procedure, setting out the APA submission requirements, APA process and fees was implemented by Ministerial Order 620-A/2008 of 16 July (which came into force on 17 July).

Furthermore, a general anti-avoidance provision applies to all simulated transactions and the rules embodied in the thin-capitalization, CFC and anti-tax haven regimes may be used in the general context of transfer pricing.

## OECD guidelines treatment

The Portuguese regulations and tax practice in general follow the OECD Transfer Pricing Guidelines.

Business restructurings were already specifically addressed in the Portuguese transfer pricing regulations as activities that must rely on the arm’s length principle, but the approaches stated in the new Chapter IX of the OECD Transfer Pricing Guidelines are likely to affect the transfer pricing audit activity.

The Masterfile concept foreseen in the Code of Conduct on transfer pricing documentation for associated enterprises in the European Union was not yet adopted in the Portuguese legislation, as the same addresses all the relevant topics contained therein, despite being more rigorous in terms of contents.

## Priorities/pricing methods

The transfer pricing methods described in the Portuguese legislation are based on the OECD Transfer Pricing Guidelines and, thus, do not introduce significant changes to the widely accepted methods recognized among transfer pricing administrators and practitioners. However, the Portuguese rules also state (paragraphs 1 and 2 of Article 4 of the Transfer Pricing Ministerial Order) that the most appropriate method should be applied to a controlled transaction or to a series of transactions in order to determine whether those transactions comply with the arm’s length principle.

This principle reflects a best method rule. This means that a taxpayer is expected to use the method or methods most suitable to each case, thus explaining not only the reason why a certain method is considered as the most appropriate to test whether the controlled transactions comply with the transfer pricing rules, but also why other methods are rejected.

Hence, the Portuguese tax authorities recognize both the transactional and profit-based methods in the OECD Transfer Pricing Guidelines and, theoretically, any method is acceptable provided that it can be justified and that the traditional transactional or profit-based methods are not applicable.

## Transfer pricing penalties

Transfer pricing adjustments are subject to the general tax penalty regime and, thus, are subject to withholding, late payment and bad-faith penalty provisions. Penalties for non-compliance with mandatory contemporaneous documentation rules may reach EUR 100,000 per year and per company. A late payment interest penalty is also applicable for transfer pricing adjustments at the rate of 4% per year.

Failure to comply with documentation requirements may result in a possible reversion of the burden of proof and the application of secret comparables.

It is expected that the transfer pricing rules will be extended by the publication of specific legislation on penalties for non-compliance with the documentation obligations in the near future.

# Portugal (continued)

## Penalty relief

The general tax penalty regime applies. The determination of penalties will be made on a case-by-case basis.

## Documentation requirements

The Portuguese transfer pricing rules require taxpayers with a turnover and other income in excess of €3m in the prior year to prepare contemporaneous documentation in Portuguese, which should provide evidence of market parity regarding the terms and conditions agreed, accepted and practiced in the agreements made with related parties, as well as the selection and utilization of the best method. The regulations divide the documentation between relevant, supporting documentation and that which is applicable to cost contribution arrangements and intra-group services.

The transfer pricing documentation should include:

- Related-party status, according to the definition presented in Article 63 of the Corporate Income Tax Code (a company subject to a substantially favorable tax regime or included in the Portuguese offshore blacklist is considered to be a related party, independent of other related-party criteria)
- Characterization of the taxpayer's activity and that of the related parties with which it engages in commercial and/or financial transactions
- Identification of all intercompany transactions, comprising the volume, terms and conditions of the transactions for the past three years, or for the period in which they occurred (if less)
- A functional analysis for each relevant transaction
- Technical studies focusing on essential areas of business
- A description of the method used and demonstration of how the prices were calculated
- Information about Portuguese comparables (geographical comparability requirement)
- The legal entity organization structure
- All intercompany contractual agreements and unrelated-party agreements

## Documentation deadlines

For companies adopting the calendar year for tax purposes, the documentation must be prepared by 15 July of the year following the one which it concerns or the 15th day of the seven month after the corresponding tax year-end for those not using the calendar year.

All Portugal-based companies have a statutory obligation to keep available and in good order their tax documentation file for the relevant year for a 10-year period. It must be kept at the Portuguese establishment or premises and should be prepared by the last working day of the six-month period following the tax year-end. However, the tax authorities may, and do, ask for documentation on transactions at any time after they take place.

## Statute of limitations on transfer pricing assessments

Assessment is possible during the four years after the end of the assessment year. The transfer pricing documentation must be kept by the taxpayer for 10 years.

# Portugal (continued)

## Return disclosures/related-party disclosures

The main disclosure requirements at this level are contained in annexes A, B, C and H (transfer pricing annexes) of the Annual Tax and Accounting Return ("IES/DA"), which include (on a yearly basis) the following information:

- Identity of the related entities
- Amount of transactions conducted with each of the related parties
- Confirmation that proper contemporaneous (annual) documentation in support of transfer prices adopted was timely prepared and is currently retained

The deadline for submission is the same as for the annual documentation. Taxpayers have to state in good faith in the annual declaration whether they have complied with the contemporaneous documentation requirements. Criminal ramifications may result in the case of misleading information.

## Audit risk/transfer pricing scrutiny

Since January 2004, entities resident in blacklisted offshore countries or territories are deemed related parties for transfer pricing purposes. Additionally, in 2007, the Portuguese tax authority began making positive adjustments to taxpayers' taxable profits as a result of tax audits. These adjustments are based on a benchmark computed with the financial information of an internal database called MGIT.

In respect to the comparables analysis performed by the tax authority, the following issues are relevant:

- Entities with a recurrent loss situation are excluded from the comparables final sample
- Comparables identification is not disclosed in the final sample
- A transaction is considered arm's length only if within the computed interquartile range
- Only the median of the interquartile range of the benchmark is considered when the tax adjustments are made

More recently special emphasis is being put on the quality of comparables, namely on royalty CUP analysis. Head-office interest charged to branches is the most recent area of scrutiny and adjustments. Cross-border restructuring is also an area of intense scrutiny.

## APA opportunity

An APA program was included in the Portuguese corporate income tax code in 2008. Taxpayers are now allowed to negotiate clearance for a period of three years regarding a transaction with transfer pricing implications.

We expect this area will develop significantly within the next few years.


# Romania

## Taxing authority and tax law

Tax authority: Ministry of Finance, National Agency for Fiscal Administration (ANAF)

Tax law:

- Law 571/2003 regarding the Fiscal Code as subsequently completed and amended
- Government Decision 44/2004 for the approval of the Norms for the application of Law 571/2003 regarding the Fiscal Code, as subsequently completed and amended

## Relevant regulations and rulings

ANAF Order 222/2008 on the content of the transfer pricing documentation file and rulings; Decision 529/2007, approving the procedure for the issuance of advance individual rulings and advance pricing agreements; Government Ordinance 92/2003 regarding the Fiscal Procedure Code, as subsequently completed and amended.

## OECD guidelines treatment

The Romanian Fiscal Code and the related Norms provide that the tax authority should also take into consideration the OECD guidelines when analyzing the prices applied in related-party transactions. In addition, the legislation on transfer pricing documentation requirements also refers to the EU Code of Conduct on transfer pricing documentation (C176/1 of 28 July 2006).

## Priorities/pricing methods

The transfer pricing methods provided by the OECD guidelines are accepted by the tax authority. The traditional methods (CUP, resale price and cost plus) are generally preferred to the transactional profit methods (TNMM and profit split).

More specifically, when it is possible to apply, CUP is the preferred traditional method for assessing the market value of related-party transactions.

## Transfer pricing penalties

Failure to provide the authorities with transfer pricing documentation upon request and within the required term is sanctioned with a fine of up to RON14,000 (approximately €3,200).

Additionally, failure to present the transfer pricing documentation file or presentation of an incomplete file could trigger an estimation of the transfer prices by the tax authority. Such estimation would be performed by simply using the arithmetic average of prices for any three transactions identified as similar by the authority. The resulting adjustments would trigger a profits-tax liability of 16% (the standard profits tax rate) and late payment interest and penalties according to the provisions of the legislation. Starting 1 October 2010, the late payment interest is 0.04% (note that the late payment interest was 0.1% per day of delay prior to 1 July 2010 and 0.05% after 1 July 2010). In addition, late payment penalties of 5% (for outstanding tax liabilities paid in a period of 30 to 90 days from the due date) or 15% (for outstanding tax liabilities not paid for more than 90 days) may also be imposed starting 1 July 2010.

## Penalty relief

No specific penalty relief provisions are currently in place under the Romanian transfer pricing legislation.

## Documentation requirements

Even though the documentation requirements were introduced in the Romanian regulations from 2006, the specific content of the transfer pricing documentation file was formally detailed by the tax authority only in February 2008.

Such requirements provide that Romanian entities having transactions with related parties should make available upon the request of the tax authority, and within a required term, a file comprising the transfer pricing documentation for such transactions. Taxpayers that entered into APAs for related-party transactions are not required to prepare and submit a transfer pricing documentation file for the periods and transactions covered by such APAs.

# Romania (continued)

## Documentation requirements (continued)

The transfer pricing documentation file should comprise information regarding the taxpayer, the group and the related-party transactions (including an analysis of functions performed and risks assumed by the related parties), as well as information on the transfer pricing methods used for determining the value of related-party transactions and a set of relevant statistical comparables.

## Documentation deadlines

The term for the provision of the transfer pricing documentation file is set by the tax authority depending on the complexity of transactions, and it can be for a period of up to three months from the date of tax authority's request (such term may be extended only once for a period equal to the initial period). The transfer pricing documentation may be requested by the tax authority during any tax audit (e.g., audits for VAT reimbursement requests), and there is no specific requirement to have the transfer pricing documentation submitted to the Romanian tax authority together with annual tax returns.

Separately, taxpayers that have an APA must submit annually to ANAF a report regarding observance of the APA terms and conditions. This report deadline is similar to that of the submission of annual financial statements, i.e., normally the end of May. Noncompliance leads to cancellation of the APA.

## Statute of limitations on transfer pricing assessments

No specific statute of limitations rules are provided for transfer pricing assessments; however, general rules for statute of limitations are applicable, i.e., the Romanian tax authority may normally review tax-related matters retroactively for five years (or 10 years in the case of fiscal evasion or fraud).

## Return disclosures/related-party disclosures

Generally, information on the related-party transactions undertaken by a Romanian entity is disclosed only upon the specific request of the Romanian tax authority. Also, for statutory accounting reporting purposes, Romanian companies are required to disclose the transactions undertaken with related parties.

- Separately from the above, the Romanian legislation provides for the following general disclosure requirements:
- Disclosure of transactions performed by Romanian entities with non-resident companies for which the Romanian company has an obligation to withhold taxes
- Disclosure or registration of contracts concluded by Romanian entities with non-resident companies and individuals performing in Romanian construction works, assembly, supervisory activities, advisory and technical assistance activities and any other similar activities which may trigger Romanian permanent establishment exposure
- Disclosure of long-term financing contracted by a Romanian entity with non-resident companies or individuals

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing scrutiny by the tax authority during a tax audit is characterized as medium to high.

## APA opportunity

Comprehensive APA procedures and requirements have been in effect in Romania since June 2007. An APA may be unilateral (involving only one tax administration) or bilateral or multilateral (involving two or more tax administrations).

By means of an APA, the ANAF will approve the specific transfer pricing method utilized by a multinational entity prior to the actual transaction. APAs are binding on the tax authority as long as their terms and conditions are observed by taxpayers.

The term for issuing an APA is 12 months for unilateral agreements and 18 months for bilateral or multilateral APAs. The fees payable to ANAF for issuance or amendment of an APA are:

- EUR 20,000/EUR 15,000 – in case of large taxpayers or for agreements on transactions with a consolidated value exceeding EUR 4m
- EUR 10,000/EUR 6,000 – in all other cases

As a general rule, APAs are issued for a period up to five years; however, this term may be extended in certain cases.


# Russia

## Taxing authority and tax law

Tax authority: The Federal Tax Service of the Russian Federation

Tax law: The Tax Code of the Russian Federation (the Tax Code)

## Relevant regulations and rulings

The transfer pricing rules are stipulated primarily in Articles 20 and 40 of the Russian Tax Code. A number of clarifications from the tax authority and extensive court practice exist; however, these sources are of a non-binding nature.

## OECD guidelines treatment

The tax authority does not recognize the OECD guidelines. However, to a certain extent, the Russian Tax Code's provisions follow these guidelines, insofar as three transfer pricing methods are stipulated (CUP, Resale Minus and Cost Plus), although it is noted that the application of the Resale Minus and the Cost Plus methods differ from the approach set out in the OECD guidelines.

Amendments to the TP law were approved by the Russian Parliament in the first reading on 19 February 2010. Two more readings are still required in order for the draft law to be approved by the president. If the amendments are introduced, the Russian transfer pricing rules will be brought much more in line with international practice, including explicit functional analysis requirements, transfer pricing documentation and reporting on transfer prices and policies when filing a tax return. However, certain differences will remain between the expected Russian rules and OECD practice. In relation to the treatment of restructuring the draft law does not introduce any new provisions.

The targeted introduction date of the proposed TP rules is 1 January 2011; however, given the recent postponement of the second parliamentary reading, the introduction might be delayed until mid 2011 or even 1 January 2012.

## Priorities/pricing methods

There are three methods mentioned in the Tax Code: CUP, Resale Minus and Cost Plus methods. In the Tax Code, the three methods are set out in a strict hierarchy. The Resale Minus method is used only if there is no information available about the prices used in identical or similar transactions by independent entities, and the Cost Plus method is applied only if both the CUP and the Resale Minus methods are inapplicable. The Resale Minus and Cost Plus methods are tested at the operating margin level, which in effect makes them similar to the OECD guidelines' TNMM method.

## Transfer pricing penalties

There are no specific transfer pricing penalties. In case of a tax assessment as a result of a transfer pricing adjustment, the tax authority will charge the tax itself and interest, which is calculated as 1/300 of the refinancing rates of the Russian Central Bank for each day while the tax was underpaid. The current refinancing rate is 7.75%.

The tax authority may also seek to charge a 20% penalty (40% in the case of a deliberate tax violation), and although the Tax Code does not provide the tax authority with the right to do so, it has been successful in imposing such penalties in a number of court cases.

Currently, transfer pricing documentation is not required. However, the above-mentioned proposed amendments stipulate the obligation to have such documentation for certain transactions (and corresponding fines for its absence). However, recent indications from the Ministry of Finance suggest that the introduction of explicit TP penalties will be delayed by two years after the introduction of the amended TP rules.

## Penalty relief

Penalties are not imposed if the taxpayer voluntarily pays the tax before the tax authority indicates the tax underpayment.

As noted above, there are no specific transfer pricing penalties in the Tax Code and the court practice has been of conflicting nature in this area. In some cases, there were penalties imposed by the tax authority for transfer pricing violations, but these were cancelled by the court (generally, based on the grounds that transfer pricing rules are of an estimative nature rather than a precise tax calculation). At the same time, there are at least three court cases at the level of the Federal Arbitration Court where the court upheld both the transfer pricing adjustment and the penalty imposed by the tax authority.

# Russia (continued)

## Documentation requirements

There are no specific documentation requirements under the current Russian transfer pricing rules.

## Documentation deadlines

As there are no specific documentation requirements currently, documentation deadlines are not applicable.

## Statute of limitations on transfer pricing assessments

The general rule is that the tax authority may audit the taxpayer for up to the three years before the year that the audit is conducted. For example, if the tax audit is performed in 2010, in addition to 2010, the tax authority can audit 2007, 2008 and 2009. In a case where it is proved that a taxpayer acted in "bad faith," including where a taxpayer actively prevented the tax audit procedures, the statute of limitations could be expanded.

## Return disclosures/related-party disclosures

There are no disclosure requirements at the present time. However, the expected amendments to the transfer pricing rules would require the disclosure of transactions with related parties and also other types of third-party transactions which would remain subject to TP control (e.g., transactions with parties located in low-tax jurisdictions and cross-border sale of oil and oil products, minerals).

## Audit risk/transfer pricing scrutiny

If the proposed amendments to the Russian transfer pricing rules are introduced and as the authorities become more experienced at implementing legislation which conforms more closely to OECD guidelines, it is likely that the level and effectiveness of transfer pricing scrutiny will increase from its historically relatively low level. For example, as of 2009, based on the available data, the tax authority only succeeded in approximately 15% of the transfer pricing tax court cases. Although taxpayers win the majority of transfer pricing cases, the tax authority continues to increase the number of cases they take to courts at the federal level year by year, and in 2008, more than 750 court cases, but in 2009 this figure decreased to 672 (the number of cases does not include cases at lower levels of the Russian court system) court cases included references to the transfer pricing rules. Out of those cases, it is estimated that approximately 20% were primarily focused on transfer pricing issues.

The risk of a transfer pricing audit in Russia would be estimated as medium.

## APA opportunity

APAs are not allowed under the current legislation, but it is included in the draft law. The APA program would be available from 1 January 2012 and at the initial stage it might be available only for "major taxpayers." Both unilateral and bilateral APAs are expected to be available.


# Singapore

## Taxing authority and tax law

Tax authority: Inland Revenue Authority of Singapore (IRAS)

Tax law: Section 34 D of the 2009 Singapore Income Tax act relates to transfer pricing and empowers the IRAS to make transfer pricing adjustments in cases where a Singapore taxpayer's transfer pricing practices are not consistent with the arm's length principle.

## Relevant regulations and rulings

The IRAS issued Transfer Pricing Guidelines on 23 February 2006 (Singapore Transfer Pricing Guidelines). Subsequent to the release of the Singapore Transfer Pricing Guidelines, the IRAS also published circulars/other guidelines on the following topics:

- Transfer pricing consultation process – relates to the IRAS' program to assess whether taxpayers are following the recommendations in the Singapore Transfer Pricing Guidelines (IRAS Circular – Singapore Transfer Pricing Consultation, published on 30 July 2008).
- Procedures for advance pricing agreements (APA Guidelines) – outlines timelines and format for information provided to the IRAS in connection with a taxpayer's request for an APA (IRAS Supplementary Circular – Supplementary Administrative Guidance on Advance Pricing Arrangements, published on 20 October 2008).
- Transfer pricing guidelines for related party loans and related party services (Singapore Loans and Services Guidelines) – further guidance on the application of the arm's length principle to related parties (IRAS Supplementary e-Tax Guide – Transfer Pricing Guidelines for Related Party Loans and Related Party Services, published on 23 February 2009).

## OECD guidelines treatment

The Singapore Transfer Pricing Guidelines and circulars/other guidelines are generally consistent with the OECD guidelines. The principles and transfer pricing methods set out in the OECD guidelines are acceptable in Singapore.

However, there are certain differences between the OECD Transfer Pricing Guidelines and the Singapore Loan and Services Guidelines. Specifically, services provided by a Singapore taxpayer in a cost pooling arrangement should not be the "principal activity" of the taxpayer. Services are considered the principal activity of the Singapore service provider if the costs relating to the provision of the service exceed 15% of the Singapore service provider's total expenses in a financial year. Further, cost pooling should only be used for "routine" services as defined by the Singapore Loans and Services Guidelines.

## Priorities/pricing methods

The IRAS does not have a specific preference for any of the five prescribed methods outlined in the OECD guidelines, with the exception of loan transactions where the IRAS indicates in the Singapore Loans and Services Guidelines that the comparable uncontrolled price method is the preferred method for substantiating the arm's length nature of interest charges. The transfer pricing method that produces the most reliable results should be selected and applied.

## Transfer pricing penalties

There are no specific penalties regarding transfer pricing adjustments. Under general tax provisions relating to understatements of income, the penalty range is from 100% to 400% of the tax underpaid. In practice, where a transfer pricing adjustment is made, the general penalty rates are applicable and penalties will most likely be applied if the taxpayer has no or insufficient transfer pricing documentation.

## Penalty relief

In general, tax penalties can be mitigated if there is reasonable cause for the understatement of income. Good-quality transfer pricing documentation is important in mitigating penalties.

# Singapore (continued)

## Documentation requirements

Singapore tax law and the Singapore Transfer Pricing Guidelines do not explicitly impose a formal requirement to prepare transfer pricing documentation. The IRAS expects taxpayers to assess their transfer pricing risk and prepare transfer pricing documentation commensurate with that risk. At a minimum, Singapore taxpayers should perform and document a transfer pricing risk assessment regarding their related party dealings. Based on the assessment, the taxpayer should determine whether more detailed transfer pricing documentation should be prepared.

A transfer pricing risk assessment should cover at least the following information:

- A description of the taxpayer's related-party transactions, including the amount of the transactions and their contractual terms
- A high-level functional analysis that describes the key contributors to the relevant transactions in terms of functions performed, assets developed, assets used and risks assumed
- An outline of the taxpayer's assessment of its tax risk

If a Singapore taxpayer has complex or large transactions, preparation of more detailed transfer pricing documentation may be necessary to substantiate compliance with the arm's length principle. More detailed transfer pricing documentation would usually include:

- Detailed factual information regarding the related-party transactions, including the functions performed, assets developed, assets used and risks assumed in relation to the transaction
- An analysis of the applicable industry in which the taxpayer operates
- Selection and application of one of the transfer pricing methods specified in the Singapore Transfer Pricing Guidelines
- An economic analysis that supports the use of the selected method using appropriate benchmarking data and analysis

## Documentation deadlines

There is no deadline for the preparation of documentation. However, when a taxpayer believes that it has potential transfer pricing risk, then transfer pricing documentation should be prepared contemporaneously. There is also no submission requirement or deadline. However, documentation should be made available if requested by the IRAS.

## Statute of limitations on transfer pricing assessments

The statute of limitations for transfer pricing adjustments is as follows:

- If the year of assessment is 2007 or a preceding year of assessment, the statute of limitations is six years from the end of the year of assessment to which the transfer pricing issue relates.
- If the year of assessment is 2008 or a subsequent year of assessment the statute of limitations is four years from the end of the year of assessment to which the transfer pricing issue relates.

Singapore corporate taxpayers are required to file tax returns by 30 November of the following year after the applicable financial year. For example, a Singapore corporate taxpayer that had a 31 December 2008 financial year end will be required to file its Singapore corporate tax return by 30 November 2009. The applicable year of assessment in this case is the 2009 year of assessment which corresponds to the financial year ended 31 December 2008.

## Return disclosures/related-party disclosures

No specified disclosures are required on Form C, Singapore income tax return.

# Singapore (continued)

## Audit risk/transfer pricing scrutiny

The recent passing of a specific statutory provision on transfer pricing and given the purpose of the Singapore Transfer Pricing Guidelines is to create an awareness of transfer pricing issues it is likely that over time there will be an increase in the number of tax audits that involve transfer pricing.

In July 2008 the IRAS issued a circular on transfer pricing consultation. The transfer pricing consultation process is intended to assess the level of taxpayers' compliance with the Singapore Transfer Pricing Guidelines and to identify potential areas where the IRAS can further facilitate and advise taxpayers on appropriate transfer pricing practices. The initial phase of the consultation process involves the issuance of a questionnaire regarding certain transfer pricing matters. These questionnaires are (and have been) issued to various taxpayers. Based on the answers to the questionnaire the IRAS will assess whether a field visit to the taxpayer's business operations and review of the taxpayer's transfer pricing documentation are necessary. Further steps may involve specific guidance from the IRAS to the taxpayer regarding compliance with the arm's length principle. To date there have been three rounds of the transfer pricing consultation process and it is likely there will be further in the future.

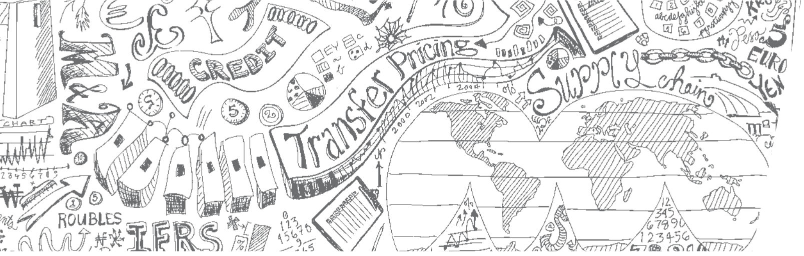
The Loans and Services Guidelines specify that cross border loans must be arm's length by 1 January 2011, so it is likely there will be a particular focus on cross border loans from 2011 onwards.

The risk of a transfer pricing audit is currently medium.

## APA opportunity

Unilateral, bilateral and multilateral APAs are available. However, for bilateral and multilateral APAs, there must be a double tax agreement between Singapore and the other involved country or countries. The Singapore Transfer Pricing Guidelines outline the procedures for applying for an APA. Further procedural guidance on the APA process has been provided in the IRAS circular "Supplementary Administrative Guidance on Advance Pricing Arrangements" issued in October 2008. The circular applies to APA requests made after 20 October 2008 and includes guidance on the following:

- Suggested timing for the overall APA process
- The circumstances where the IRAS may reject a taxpayer's APA request
- The nature of taxpayer resources and commitments that should be made when an APA is requested
- That "roll-backs" are limited to bilateral and multilateral APAs




# Slovak Republic

## Taxing authority and tax law

Tax authority: Slovak Tax Directorate, local tax authorities and Ministry of Finance

Tax law:

- Sections 2, 17 (5, 6, 7) and 18 of the Income Tax Act
- Act on International Assistance and cooperation by tax administrators

## Relevant regulations and rulings

The Slovak transfer pricing rules laid down in the Income Tax Act generally conform to the OECD guidelines. The OECD Transfer Pricing Guidelines were published in the Slovak Financial Newsletter but are not legally binding. Nevertheless, the tax authorities should follow them in practice.

The Slovak Income Tax Act has been amended with effect as of 1 January 2009. The amendment introduced an obligation of the taxpayer to prepare and keep transfer pricing documentation supporting the transfer pricing method used in transactions with foreign related parties. The required content of transfer pricing documentation is stipulated in Guidance No. MF/8288/2009-72 of the Slovak Ministry of Finance.

## OECD guidelines treatment

The tax authorities usually follow the provisions of the OECD guidelines. The acceptable methods listed in the Income Tax Act correspond with the methods stipulated by the OECD guidelines. However, the 2010 update to the OECD guidelines has not been reflected yet in the Slovak Income Tax Act.

## Priorities/pricing methods

The Slovak Income Tax Act prefers the methods based on the comparison of prices over methods based on the comparison of profits, combined methods or other alternative methods. The method used must respect the arm's length principle. The 2010 update to the OECD guidelines has not been reflected yet in the Slovak Income Tax Act.

## Transfer pricing penalties

No penalties specific to transfer pricing exist. The penalty rate for unpaid (or understated) tax liability is three times the basic interest rate of the European Central Bank (at the date of issue 3*1% = 3%). As of 1 January 2010, the penalty rate will be three times the basic interest rate of the European Central Bank or 10 % (whichever will be higher). This is not a per annum rate, but rather the penalty would be a multiple of this rate and the under-declared tax, irrespective of the time of tax underpayment. In addition, a penalty for the breach of non-monetary obligations (e.g., non-existing or insufficient supporting documentation) of an amount up to approx. EUR 33,200 can be imposed. On assessing the penalty for the breach of non-monetary obligations, the tax authorities have to take into account all the circumstances that led to the breach of non-monetary obligations (e.g. importance, duration and consequences of the breach).

## Penalty relief

There are no specific reductions in penalties. Generally, a penalty is reduced by half if the taxpayer submits a supplementary income tax return where the tax base is adjusted upwards. Upon a successful challenge of transfer prices by the tax authorities, no specific reduction in penalties is available.

# Slovak Republic (continued)

## Documentation requirements

The required content of transfer pricing documentation is stipulated in Guidance No. MF/8288/2009-72 of the Slovak Ministry of Finance. The intent of the Guidance is to conform with the EU Code of Conduct on transfer pricing documentation for associated enterprises in the European Union (No. 2006/C 176/01).

Transfer pricing documentation must be prepared for related-party transactions with an amount exceeding the level of materiality for accounting purposes (as defined by International Financial Reporting Standards). Documentation must be prepared separately for each transaction or homogenous group of transactions.

For taxpayers obliged to use International Financial Reporting Standards (banks, insurance companies, pension funds, companies exceeding a certain size), the Guidance prescribes the required contents of the transfer pricing documentation, which are generally in line with the master file approach set out by the EU Code of Conduct on Transfer Pricing Documentation. The documentation will consist of global (master file) and local documentation. The master file must contain information with regard to the whole group of related parties (overview of the industry, business strategies and general overview of functions, risks and assets of the members of the group). The local documentation will contain information regarding the Slovak taxpayer. Moreover, the approach to transfer pricing, methods used, and description of transactions with related parties should be covered by the documentation. The local documentation should also include analysis of the comparability of the transactions.

For other taxpayers, the Guidance does not stipulate the contents of the documentation. However, the transfer pricing documentation must prove that prices applied in related-party transactions conform to the arm's-length principle.

The language of the documentation should be Slovak, unless agreed. The tax authorities have unofficially stated that documentation presented in English, German or French should also be accepted.

It is not clear from the Guidance whether the documentation requirements will also apply for transactions performed or contracts concluded prior to 1 January 2009. However, the tax authorities already require taxpayers to have sufficient transfer pricing documentation prepared in the case of a tax audit. This stems from the provision of the Income Tax Act stipulating that the burden of proof rests with the taxpayer.

## Documentation deadlines

Transfer pricing documentation must be submitted wihin 60 days of a request by the tax authorities. The documentation does not have to be disclosed unless requested by the tax authorities.

## Statute of limitations on transfer pricing assessments

The statute of limitations in Slovakia in the case of applying a double tax treaty is 10 years from the end of the year in which the respective tax return is filed.

## Return disclosures/related-party disclosures

Transfer pricing documentation does not need to be enclosed with the tax return. The taxpayer should state (on a specific row of the tax return) the difference (if any) between the prices used in transactions with related parties and the prices at an arm's-length level that decreased the tax base. The tax base must be at increased by this difference at the same time.

The corporate income tax return includes a summary table where the amounts of various types of related-party sales and purchases must be stated (regardless of whether there are differences from arm's-length prices).

# Slovak Republic (continued)

## Audit risk/transfer pricing scrutiny

Overall, the likelihood that a company with significant related-party transactions will get a transfer pricing audit can be classified as medium.

The tax authorities have been historically relatively inactive in this area, with only few complex transfer pricing audits performed. However, following the amendment to the Income Tax Act applicable as of 1 January 2009, the tax authorities have intensified their activities in the area of transfer pricing and are increasingly focusing on the transfer pricing and related documentation when auditing companies that form part of a multinational group. Thus, we expect the level of risk to increase in the future.

## APA opportunity

According to Section 18(4) of the Slovak Income Tax Act, in cases of cross-border related-party transactions, the taxpayer may request the tax authorities to approve the selected transfer pricing method. If approved, the method should be applied for a maximum of five tax periods. The Income Tax Act, however, does not explicitly stipulate that the tax authorities may approve the particular price or margin percentage used. Therefore the use of advance pricing agreements in Slovakia is rather limited.


# Slovenia

## Taxing authority and tax law

Tax authority: Davčna uprava Republike Slovenije (DURS)

Tax law:

- Corporate Income Tax Act (Zakon o davku od dohodkov pravnih oseb)
- Regulation on Transfer Prices (Pravilnik o transfernih cenah)
- Regulation on the Acknowledged Interest Rate (Pravilnik o priznani obrestni meri)
- Tax Procedure Act (Zakon o davčnem postopku)

## Relevant regulations and rulings

Articles 16 and 17 of the Corporate Income Tax Act provide the definitions of related parties and general requirements they need to comply with. The latter are explained in more detail in the Regulation on Transfer Prices.

Article 18 of the Corporate Income Tax Act sets the basis for documentation requirements which are then elaborated in the Tax Procedure Act.

Article 19 of the Corporate Income Tax Act provides the general rules in relation to acknowledged interest rate on loans between related parties. The rules are defined in more detail in the Regulation on the Acknowledged Interest Rate. The acknowledged interest rate rules determine a safe harbor for loans between related parties.

## OECD guidelines treatment

As the Slovenian transfer pricing regulations follow the principles of the OECD Transfer Pricing Guidelines, the tax authority, where there is no guidance in Slovenian legislation, also consider them in their tax audits.

## Priorities/pricing methods

All five standard methods are acceptable, however the CUP and in the next stage also resale price method and cost plus method are preferred. If none of the specifically identified methods are suitable for determining the arm's length price, the taxpayer is permitted to adopt a suitable combination of such specified methods.

## Transfer pricing penalties

A taxpayer may be fined up to EUR 30,000 if the transfer pricing documentation is not submitted in the prescribed manner; additionally, the individual responsible for the preparation of the documentation on behalf of the taxpayer may also be fined up to EUR 4,000. In case of a tax adjustment, late payment interest and penalties for offences may be charged. If the additional tax exceeds EUR 5,000 the tax offence is qualified as a severe tax offence and fines in the amount of 45% of the additional tax may be levied.

## Penalty relief

If the tax authority is able to conclude that the taxable person has cooperated well during the tax audit, fines are usually not levied.

# Slovenia (continued)

## Documentation requirements

The Slovenian transfer pricing documentation requirements are based on the master file concept. Under this concept, as recommended by the European Community (EC) Council as well as the EU Joint Transfer Pricing Forum, the transfer pricing documentation should consist of a master file and a country-specific file. Disclosure of any related parties transaction amounts should be provided with the tax return when it is filed with the tax authority.

The local legislation sets the following documentation requirements:

### The Master File

The master file normally includes documentation common to the whole group. It may be prepared by the group's headquarters and should include a general description of the way business is conducted by the group companies. The file should include the following:

- a description of the taxable person
- a description of the global organizational structure of the group
- an explanation of the type of connections between the companies in the group
- an explanation of the method used in the determination of transfer prices
- a description of the business activities and business strategies ( including any general economic and other factors, an assessment of the competitive environment, etc.)

### Country specific documentation

As in the Master file, the local documentation should describe the company's course of business but on a local level. The country-specific documentation should normally include:

- a description of transactions between affiliated persons
- a functional analysis determining the main functions performed and risks undertaken by the tax payer and outlining which adjustments may need to be made in relation to comparable situations
- a description of any comparable search performed
- a description of business strategies
- a description of goods/services transferred/rendered
- a description of the method applied for establishing the arm's length price
- any other information that might be relevant from the transfer pricing perspective should also be included in the documentation

## Documentation deadlines

The documentation should be provided to the tax authority upon its request, usually made in the course of a tax inspection. Wherever any such documentation proves impossible to submit immediately, a deadline extension of up to 90 days (depending on the extent and complexity of the information) may be granted. If the master file is not kept in the Slovenian language, it must be translated, before submission, at the tax authority's request. An additional period of 60 days may also be granted for the translation of the Master file.

## Statute of limitations on transfer pricing assessments

The statute of limitation on transfer pricing assessments is five years. The transfer pricing documentation must be archived for a period of 10 years.

# Slovenia (continued)

**Return disclosures/related-party disclosures**

Related-party transactions are reported in the scope of the annual corporate income tax return.

**Audit risk/transfer pricing scrutiny**

High risk

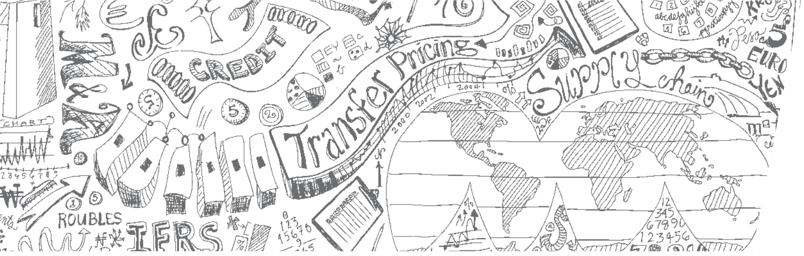
The tax authority mainly initiates a transfer pricing audit where a Slovenian taxable person is part of a multinational group. The following transactions are currently in the focus of the tax authority:

- Intra-group services
- Intangible goods (e.g. royalties and licensing)
- Financial transactions (e.g. loans and cash-pooling)

Additional risk factors are the profitability of the local taxpayer, business restructurings, the nature and volume of related-party transactions, transfer pricing issues identified in previous tax audits, information available from media.

**APA opportunity**

The possibility of applying for APAs is not available in Slovenia.




# South Africa

## Taxing authority and tax law

Tax authority: Commissioner of the South African Revenue Services (SARS)

Tax law: Section 31 of the Income Tax Act 58 of 1962 (the Act) contains the main legislative provisions concerning transfer pricing.

Section 31 authorizes the tax authority to adjust the consideration for goods or services to an arm's length price for the purposes of computing the South African taxable income of a person.

For years of assessment commencing on or after 1 October 2011 the legislation has changed, allowing the tax authority to adjust any term or condition imposed in any part of a transactions, scheme or arrangement, thus widening the application of the section.

## Relevant regulations and rulings

There are no specific regulations or rulings; however, guidance on the application of §31 is contained in Practice Notes Number 2 (14 May 1996) and 7 (6 August 1999). The legislation currently prohibits the tax authority from issuing an advanced ruling on a transfer pricing matter.

## OECD guidelines treatment

Although South Africa is not a member of the OECD, the tax authority accepts the OECD guidelines and has largely based Practice Note 7 on these Guidelines. By the same token, the tax authority recognizes the five methods accepted by the OECD.

## Priorities/pricing methods

The tax authority accepts the methods prescribed by the OECD, i.e., CUP, RPM, Cost Plus, TNMM and Profit Split; and has indicated that it will subscribe to the OECD view on accepting a best method approach as long as this is substantiated. The tax authority may require that adjustments be made to foreign comparable company results used to benchmarking the results of the South African entity, to compensate for differences in risks assumed by entities operating in a different jurisdiction.

## Transfer pricing penalties

Any adjustments made by the tax authority under §31 are deemed to be dividends, and the Secondary Tax on Companies (STC) at a rate of 10% will be levied which is non-discretionary. There are no other specific penalties for transfer pricing, but general penalty rules are applicable, which could reach 200% of the additional tax resulting from an adjustment (in the event of default, omission, incorrect disclosure or misrepresentation).

## Penalty relief

Where taxpayers have made conscientious efforts to establish transfer prices that comply with the arm's length principle, and have prepared documentation to evidence such compliance, the tax authority is likely to take the view that the taxpayer's transfer pricing practices represent a lower tax risk. Accordingly, the preparation of sound and consistent transfer pricing practices may reduce the possibility of an audit and, therefore, reduce the likelihood of incurring penalties.

## Documentation requirements

Section 31 is discretionary therefore initially the burden rests with the tax authority (although this changes with effect from years commencing on or after 1 October 2011). Once the tax authority has arrived at a view, the taxpayer has the burden of proof to demonstrate that its prices are arm's length. Under the new legislation (effective 1 October 2011), this burden initially rests with the taxpayer. The best way to discharge the burden of proof is by developing a transfer pricing policy, determining the arm's length amount and voluntarily producing documentation to evidence the analysis undertaken. Having said this, the tax authority would expect taxpayers to have created, referred to and retained transfer pricing documentation in accordance with prudent business management principles (i.e., the principles that would govern the process of evaluating a business decision at a similar level of complexity and importance).

No specific documentation requirements exist however there is an inherent requirement in that the tax authority is of the view that by not preparing documentation, a company is not adequately monitoring the policies in place and cannot support that they result in an arm's length outcome.

# South Africa (continued)

**Documentation deadlines**

Transfer pricing documentation should be prepared not later than the date of submission of a tax return affected by the intercompany transactions. Tax returns are due 12 months after a company's financial year-end with no further extension.

**Statute of limitations on transfer pricing assessments**

The statute of limitations is three years from the date of assessment. Section 79 of the Act provides that an assessment will prescribe three years from the date of issue. However where the tax authority is of the view there was fraud, misrepresentation or non-disclosure of material facts, this will not apply.

**Return disclosures/related-party disclosures**

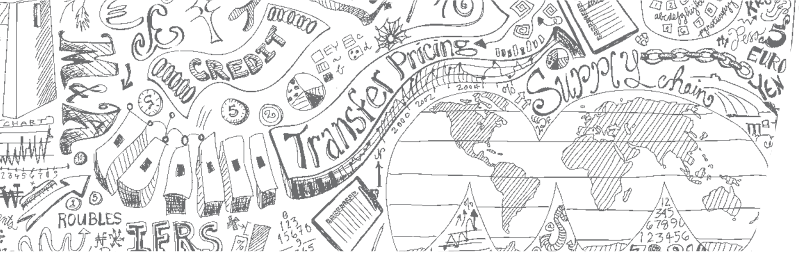
Very limited disclosure at present around whether related party transactions occurred, some limited questions on their nature, notably around lending arrangements and management services, a question on the existence of documentation and a question asking if the transactions occurred at arm's length.

**Audit risk/transfer pricing scrutiny**

The tax authority follows a risk matrix in assessing the level of transfer pricing risk. This follows two steps, an initial review of the information lodged with the tax return and possibly from a questionnaire issued, followed by a more thorough investigation into the documentation and results. If risk is found to exist they will then proceed into a desk and possibly a field audit. The last couple of years have seen some significant assessments being raised.

**APA opportunity**

Currently South Africa does not have an APA program although it is being considered. The legislation also currently prohibits the tax authority from providing an advanced ruling on a transfer pricing matter.




# South Korea

## Taxing authority and tax law

Tax authority: National Tax Service (NTS)

Tax law: The Law for Coordination of International Tax Affairs (LCITA)

## Relevant regulations and rulings

- Presidential Enforcement Decree (PED)
- The Ministerial Decree and Interpretations

## OECD guidelines treatment

The LCITA has priority over the OECD guidelines. The NTS recognizes the OECD guidelines, but the OECD guidelines have no legally binding effect. Hence, if a taxpayer's argument is based on the OECD guidelines only and not the LCITA, in practice, the NTS or regional tax offices may not accept it.

Due to the recent changes to the OECD guidelines, there are currently proposed changes to the LCITA which are pending legislation approval.

## Priorities/pricing methods

The South Korean transfer pricing regulations prescribe the following transfer pricing methods: CUP Method, Resale Price Method, Cost Plus Method, Profit Split Method, TNMM, and other reasonable methods. Among the aforementioned transfer pricing methods, the taxpayer is to select the most appropriate method based on the availability and reliability of data. According to the current language of the LCITA, the transaction-based methods (i.e., CUP Method, Resale Price Method and Cost Plus Method, with no internal priority amongst these three methods), have priority over the profit-based methods ( i.e., Profit Split Method and TNMM, with no internal priority between these two methods). There is currently pending legislation to replace this priority of transaction-based methods with a "best method" type rule. Other reasonable methods may be selected if none of the five specific methods can be applied.

## Transfer pricing penalties

There are two types of penalties associated with a transfer pricing adjustment: an underreporting penalty and an underpayment penalty.

- The underreporting penalty is approximately 10% of the additional taxes resulting from a transfer pricing adjustment.
- The underpayment penalty, which is an interest payment in nature, is calculated as 0.03% of the additional taxes on a transfer pricing adjustment per day (10.95% per annum) on the cumulative days. The counting of cumulative days of the underpayment starts from the day after the statutory tax filing due date, which comes three months after the fiscal year-end, and ends on the date that a payment for the tax assessment is made.

There is also a penalty of up to KRW30m for failure to provide the documentation requested by the NTS within the due date. There is pending legislation to increase the amount of this penalty to KRW100m, with the amount of the penalty to be based on the importance of the documentation requested. In general, the documents are to be submitted within 60 days of the date of request. However, the taxpayer may be granted a one-time extension for 60 days if the reasonable circumstances specified in the LCITA exist. See below for further details regarding contemporaneous TP documentation.

## Penalty relief

Under Article 13 of the LCITA, if the taxpayer has prepared and maintained contemporaneous TP documentation for the TP methods applied to the cross-border intercompany transactions reported in the corporate income tax return and such documentation supports the reasonableness of the TP methods reported, the penalty for underreporting will be waived in the case where a TP adjustment is made.

# South Korea (continued)

## Penalty relief (continued)

PED Article 23 of the LCITA provides guidelines on the contents of the contemporaneous TP documentation. In general, contemporaneous TP documentation should include information on the taxpayer's business (including functions performed and factors that can affect pricing for intercompany transactions with related parties), details on cross-border intercompany transactions, an explanation of the TP method selected and reasons for not selecting other TP methods prescribed in the regulations, and details on the comparable company or transaction data used. The guideline also stipulates that the comparable data used should be representative and should not have been chosen to favor the taxpayer's position (i.e., no "cherry-picking"). In the case where a taxpayer applies a TP method different from that agreed upon in an APA or selected by auditors in a tax audit, the taxpayer needs to justify the use of the different TP method.

Also, under the LCITA Article 13 and PED Article 23, the underreporting penalty is waived if the mutual agreement procedure (MAP) result confirms that a taxpayer is not guilty of negligence; i.e., a taxpayer must:

- Select and report the most appropriate transfer pricing method specified in the LCITA
- Actually apply the selected method
- Maintain supporting documentation

## Documentation requirements

At the time of filing the corporate income tax return, a taxpayer is required to submit certain transfer pricing reporting forms. Under the contemporaneous TP documentation rules, in order to receive the benefit of the relief from the underreporting penalty, taxpayers are required to prepare and maintain TP documentation by the due date of the filing of the annual corporate income tax returns. Such contemporaneous TP documentation must be submitted to the NTS within 30 days of the request. Documents are generally required to be submitted in Korean.

## Documentation deadlines

A taxpayer must submit documents and information within 60 days upon request of the NTS. A onetime 60-day extension may be granted if reasonable circumstances specified in the LCITA exist. Contemporaneous TP documentation should be submitted to the NTS within 30 days of the request. The tax authorities may also request that a taxpayer submit certain information, including a TP study, at the time of a tax audit. In that case, the taxpayer may be given a shorter notice to submit (e.g., a 10-day notice).

## Statute of limitations on transfer pricing assessments

The statute of limitations on transfer pricing adjustments is generally five years. It extends to 10 years in case of a fraud or other wrongful act and to 7 years if a taxpayer does not submit the tax filing on the due date.

## Return disclosures/related-party disclosures

The LCITA requires a taxpayer to submit the following transfer pricing reporting forms when filing the annual corporate income tax return:

- A form stating the transfer pricing method selected and the reason for the selection of the method for each intercompany transaction. There are different forms for different types of transactions, (e.g., tangible property transactions, intangible property transactions, service transactions, cost-sharing arrangements).
- A summary of cross-border intercompany transactions with foreign related parties.
- Summary income statements of foreign related parties having cross-border intercompany transactions with the South Korean entity.

# South Korea (continued)

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing issues being reviewed during a tax audit is high. The NTS, as a matter of policy, requests for transfer pricing documentation, and such requests can be made separately from a tax audit. The NTS closely monitors companies whose profitability suddenly drops or companies whose profits fluctuate substantially over a number of years, and they are likely to be subject to tax audits. Also, companies paying large royalties abroad or receiving large management service fee charges or cost allocations from overseas related parties will likely be subject to scrutiny by the NTS.

## APA opportunity

Unilateral, bilateral and multilateral APAs are available under the LCITA. In order to encourage the application of APAs, the NTS does not require an application fee, and documents submitted to the NTS with regard to an APA are to be held confidential in accordance with the LCITA. In addition, the APA officials of the NTS are making efforts to shorten the APA processing period. The NTS releases Annual Reports on APAs which include information such as statistics on the type of APAs being concluded, the countries that are counterparties to APAs, time taken to process APA cases, and other related information.


# Spain

## Taxing authority and tax law

Tax authority: State Agency of Tax Administration (AEAT) and General Directorate of Taxation (DGT)

Tax law: Spanish Consolidated Corporate Income Tax Law (CCITL) Article 16

## Relevant regulations and rulings

On 18 November 2008, by Royal Decree, the Spanish Government has approved and published regulations that specify transfer pricing documentation requirements (Royal Decree 1793/2008) applicable to persons or entities participating in related-party transactions.

Transfer pricing documentation requirements have been in effect in Spain since 2006 (following Law 36/2006, applicable to tax periods beginning as from 1 December 2006). This includes a shift of the burden of proof to the taxpayer, and penalty regime. However, the law did not include a detailed description of what the documentation should contain, except that the transfer pricing documentation had to reflect the arm's length principle and the arm's length test should be based on one of the methods specified in the law (i.e., CUP, Cost Plus, Resale Minus, TNMM and Profit Split). The new regulations provide more details regarding the information that should be included in the documentation. Spanish taxpayers engaged in related-party transactions are now required to prepare two sets of documentation:

- a "master file" related to the group as a whole, and
- a "local" file for each taxpayer containing specific information on the description, analysis and valuation of the controlled transactions

Regarding transfer pricing penalties, the Royal Decree-Law 6/2010 (approved on 9 April 2010) introduces amendments modifying the penalty quantities for companies that meet certain criteria. The Royal Decree 897/2010 (approved on 9 July 2010) and the Royal Decree-Law 13/2010 (approved on 3 December 2010) introduce certain amendments consisting on exemptions in Transfer Pricing documentation requirements.

## OECD guidelines treatment

Spanish Transfer Pricing legislation follows the OECD guidelines and those of the European Union Transfer Pricing Forum.

## Priorities/pricing methods

The law establishes that, in order to determine the market value, one of the following methods should be applied: CUP, Cost Plus or Resale Minus. These methods are on the same preferential level in the valuation method hierarchy.

When due to the complexity or to the information relating to the transactions, the above methods may not be applied properly, TNMM or Profit Split may be used.

## Transfer pricing penalties

Failure to comply with the documentation requirements specified in the new regulations may result in major penalties. These penalties can result from not having correct documentation and/or from not applying the arm's length principle (market value).

When the assessment does not produce a tax adjustment, the penalty will be EUR 1,500 per fact, or EUR 15,000 per group of facts omitted, inaccurate or false.

In the case of entities whose net sales do not exceed EUR 10m in the period but related-party transactions exceed EUR 100,000, the amount of the penalty will have as a maximum limit the lesser of the two following quantities:

- The 10% of the related-party transactions
- The 1% net sales

# Spain (continued)

## Transfer pricing penalties (continued)

When the tax authorities adjust the pricing of a transaction, the penalty may add up to 15% of the gross adjustment.

There will be no penalties where the obligation to document has been complied with, even if the tax authorities reassess the value of transactions.

In addition to the above, the new regulations also include the applicability of "secondary adjustments" (i.e., in those transactions where both values will have for the related parties the tax treatment that corresponds to the nature of the profit realized). The law makes a clarification for cases where the link is defined in light of the relationship between the shareholder and the entity, the difference shall (proportionally to the participation in the entity) be considered as:

- dividends whenever such difference is in favor of the shareholder, or
- contributions by the shareholder to the entity's equity whenever the difference is in favor of the entity

The above sanctions are compatible with aggravating circumstances such as resisting, obstructing, excusing or negating the tax authorities' actions.

## Penalty relief

Some reductions are applicable to penalties. Penalties should not apply with the fulfillment of the documentation requirements.

## Documentation requirements

The documentation requirements are in line with those of the EU Joint Transfer Pricing Forum (JTPF). Accordingly, two types of documentation must be maintained: one global document for the group (master file) and one document for each group entity (local file).

The documentation will cover domestic and international transactions. However, transactions within the same fiscal unit are exempted from the documentation requirements. The master file documentation requirements establish the necessity of:

- General description of the organizational, legal and operative group structure, and any change thereof
- Identification of the group entities that enter into related-party transactions to the extent that they affect the operations of the Spanish corporate taxpayer, directly or indirectly
- General description of the nature, amounts and flows of related-party transactions completed by corporate group entities, to the extent that they affect the operations of the Spanish corporate taxpayer, directly or indirectly
- General description of the functions performed and the risks assumed by the different group entities, to the extent that they affect the operations of the Spanish corporate taxpayer, directly or indirectly, including any changes since the last fiscal year
- List of intangibles (including patents, trade marks, commercial brands) owned by the group, to the extent that they affect the operations of the Spanish corporate taxpayer, directly or indirectly, as well as the considerations derived from the use of these intangibles
- Description of the group's transfer pricing policies, including the pricing methodology used to justify the group policy's compliance with the arm's length principle
- List of cost-sharing and services agreements between group entities relevant to the Spanish corporate taxpayer
- List of APAs and agreements entered into, as relevant to the Spanish corporate taxpayer, and
- Corporate group's Annual Report or equivalent

On the other hand, the local documentation requirements establish the necessity of:

- A detailed description of the taxpayer's business and business strategy, including changes in the business strategy compared to the previous tax year
- A description and explanation of the specific controlled transactions, including the transactions (tangible and intangible assets, services, financial, etc.), invoices and amounts of the transactions

# Spain (continued)

## Documentation requirements (continued)

- A comparability analysis, including:
  - Amounts of the transactions
  - Characteristics of property and services
  - Functional analysis (functions performed, assets used, risks assumed)
  - Contractual terms
  - Economic circumstances
  - Specific business circumstances
- An explanation about the selection and application of the transfer pricing methods, why the methods were selected and how they were applied
- Any other relevant information used by the taxpayer to value related-party transactions, as well as any agreement entered into with shareholders that may affect the transaction valuation

Further information could be required by the tax administration during a tax audit in regards to the related-party transactions.

There are some exemptions for documenting related-party transactions.

- Exemptions by volume:
  - For those corporate income tax taxpayers whose transactions carried out with the same related party do not exceed EUR 250,000 at market value (taking into account the total transactions carried out with the same related party)
  - Entities whose net sales do not exceed EUR 10m in the period and related-party transactions do not exceed EUR 100,000 (excluding tax havens)
- Exemptions by transaction characteristics:
  - Performed between entities within tax consolidation groups
  - Performed between Economic Interest Groupings or Temporary Business Alliances, and their shareholders
  - Carried out within the scope of an IPO
  - Carried out between Saving Banks integrated in a vehicle approved by the Bank of Spain

## Documentation deadlines

Documentation will have to be kept by companies once the corporate income tax return is filed.

## Statute of limitations on transfer pricing assessments

A general statute of limitations of four years applies. The term will be interrupted in case of a tax audit. If a new income tax return is filed with the tax authorities, the four-year period is suspended and a new one begins.

## Return disclosures/related-party disclosures

Specific disclosure rules exist for transactions with "tax havens," even with unrelated parties (as per a black list).

## Audit risk/transfer pricing scrutiny

High risk – the tax authorities have stated that Transfer Pricing audits will be a priority from 2009 on forward.

## APA opportunity

Taxpayers may request the tax authorities value related-party transactions before they are carried out. This request has to be filed with a proposal based on the arm's length principle. On the other hand, the tax authorities may also settle agreements with other tax authorities in order to determine the market value of the transactions jointly (i.e., bilateral APAs).

The new regulation has improved the previous regime on APAs by extending the valid term from a three-year period to a six-year period (e.g., the previous year, when the time limit for filing the tax return has not yet expired, the current year and the next four years).


# Sweden

## Taxing authority and tax law

Tax authority: Swedish Tax Agency

Tax law:

- Sections 14:19-20 of the Income Tax Act include the arm's length principle
- Sections 19:2a and b of the Law (2001:1227) on income tax returns and income statements include the documentation requirements regarding transfer prices

The Swedish Tax Agency is responsible for the correct and uniform implementation of the tax laws. It issues guidelines, recommendations and publishes its standpoints on specific issues to the local tax offices.

## Relevant regulations and rulings

Section 12:4 of the regulations (2001:1244) on income tax returns and income statements and the regulations (SKVFS 2007:1) regarding documentation of the pricing between associated enterprises. The tax authority also issues general taxation guidelines, which include information on transfer pricing.

## OECD guidelines treatment

The Swedish tax laws on transfer pricing refer to the OECD Transfer Pricing Guidelines, and they are applied by the courts and tax authorities.

Chapter IX of the OECD Transfer Pricing Guidelines (on Business Restructurings) is expected to significantly increase the Tax Agency's focus on restructuring but potentially also on existing structures, for example in relation to allocation of risk between related parties.

## Priorities/pricing methods

One of the methods described in OECD guidelines should be applied. Transaction-based methods are, all other things equal, preferred over profit-based methods.

## Transfer pricing penalties

There are no specific transfer pricing penalties. General penalty rules apply, with penalties ranging from 10% to 40% of the additional tax imposed. In transfer pricing cases, penalties at a rate of 40% are generally imposed.

## Penalty relief

Penalties are imposed on taxpayers for supplying the tax authority with inaccurate or insufficient information. In the preparatory work to the law that introduces transfer pricing documentation requirements, it is stated that if an income adjustment is made because the taxpayer's prices are not deemed to be at arm's length; the penalties might be reduced or eliminated if the taxpayer has prepared proper transfer pricing documentation.

## Documentation requirements

Multinational enterprises are required to document transactions with related companies as of 1 January 2007. The new legislation introduces formal transfer pricing documentation requirements in relation to cross-border transactions within multinational enterprises.

The documentation must include:

- A description of the company, organization and business operations
- Information regarding the characteristics and scope of the transactions
- A functional analysis

# Sweden (continued)

## Documentation requirements (continued)

- A description of the chosen pricing method
- A comparability analysis

The functional analysis should, in addition to identifying the functions performed, risks assumed and assets used, also describe which functions, risks and assets contribute to the company's ability to generate profit. Moreover, the importance of the comparability factors described in the OECD guidelines is highlighted.

Documentation prepared in accordance with the code of conduct regarding European Union Transfer Pricing Documentation (EU TPD) is deemed to comply with the Swedish documentation requirements. The documentation should be prepared in the Swedish, Danish, Norwegian or English language.

For transactions of limited value, it is possible to prepare simplified documentation. Transactions of limited value for fiscal year 2009 include the sale or purchase of goods amounting to approximately SEK27m or less per counterparty on a yearly basis, or other transactions amounting to approximately SEK5m or less per counterparty on a yearly basis. Simplified documentation is not possible for transactions involving the sale of intangible assets.

The simplified documentation should include the following:

- The group's legal and organizational structure and a description of the business operations
- The counterparty to the transaction and information on that entity's business operations
- Information on the intercompany transactions, including the type of transaction, amounts and value
- The method applied to the transaction to comply with the arm's length principle
- Information on comparable transactions, if utilized

## Documentation deadlines

The underlying analysis should, in principle, be prepared in connection with the transaction. The final documentation should be available upon request from the tax authority. Such a request is possible from the date that the income tax return is filed.

## Statute of limitations on transfer pricing assessments

A general statute of limitations applies, which is within five years from the year of assessment.

## Return disclosures/related-party disclosures

No specific disclosure requirements when filing the tax return currently exist. However, submiting the documentation when filing the tax return may eliminate risk of penalties.

## Audit risk/transfer pricing scrutiny

The risk that transfer price adjustments will be scrutinized during an audit is high. There has been a significantly increased focus from the tax authority on transfer pricing-related issues.

## APA opportunity

Formal APA procedures exist as of 1 January 2010.


# Switzerland

## Taxing authority and tax law

Tax authority:

- Cantonal Tax Authorities (tax assessments)
- Federal Tax Administration (SFTA; competent authority)

There are no specific references to transfer pricing in Swiss tax law. However, legal support for adjusting taxable profits of a taxpayer is derived from the arm's length principle in Article 58 of the Federal Direct Tax Act on a federal level as well as in Article 24 of the Federal Law on the Harmonization of the Cantonal and Communal Taxes on a cantonal level. In addition, there are various administrative directives referring to so-called "safe-harbor regulations" which allow for the setting of transfer pricing without any specific documentation (e.g., with regard to intercompany interest payments).

## Relevant regulations and rulings

There are no specific transfer pricing regulations.

## OECD guidelines treatment

The SFTA has instructed the cantonal tax administrations in its Circular Letter of 4 March 1997, to adhere to the OECD Transfer Pricing Guidelines for transfer pricing matters. There are no specific tax regulations on business restructurings in Switzerland.

## Priorities/pricing methods

The SFTA adheres to the OECD Transfer Pricing Guidelines and prefers the usage of the comparable uncontrolled price (CUP) method as well as the traditional transactional methods over profit-based methods. According to Circular Letter 4/2004, the profit margin for service companies must be determined in accordance with the arm's length principle (i.e., for each taxpayer individually on the basis of comparable uncontrolled transactions considering appropriate margin ranges). The Circular Letter also implicitly states that the cost plus method is the most appropriate method for service companies to price their services based on a functional and risk analysis. However, concerning the provision of financial and management services, the cost plus method shall only be accepted in exceptional cases.

The SFTA uses in principle a full cost approach including all direct and indirect costs. Generally, when the taxpayer can, based on appropriate documents and records, prove that the applied margin is too high, the SFTA may exceptionally allow for a lower margin.
The transactional profit split method is rarely used in Switzerland. In the financial and banking services sector (including in the area of investment and asset management), some Cantonal Tax Authorities tend to validate the applied transfer prices using transactional profit methods.

## Transfer pricing penalties

There are no specific transfer pricing penalties, but general penalty rules apply. However, penalties are only imposed in cases of fraud or negligence. Interest charges for late payment are due in case of adjustments.

## Penalty relief

There are no special provisions for reductions in penalties.

## Documentation requirements

There are no specific documentation requirements. However, if challenged by the SFTA, the taxpayer has to demonstrate that the transfer prices applied were based on sound economic and commercial reasoning on an arm's length basis. Although it can be concluded from the Federal Direct Tax Act that in principle, a taxpayer upon request of the Swiss tax administration, should prepare transfer pricing documentation, there is little guidance on the structure of such documentation. However, based on the references to the OECD Transfer Pricing Guidelines in the 1997 Circular Letter, an OECD-compliant documentation in one of the official languages of Switzerland is accepted by the SFTA. Due to the lack of sufficient independent comparable companies on the Swiss market, it is usually allowed to apply Western European comparables.

# Switzerland (continued)

### Documentation deadlines

There are currently no special provisions for documentation deadlines.

### Statute of limitations on transfer pricing assessments

The general rule provides for up to 10 years from the end of the tax year, if new facts or circumstances are discovered by the tax administration.

### Return disclosures/related-party disclosures

There are no formal related-party disclosure requirements. However, in the case of a tax audit or request from competent authorities, the taxpayer must provide the requested information to a reasonable extent.

### Audit risk/transfer pricing scrutiny

The risk that transfer pricing issues will be scrutinized during an audit is at a medium level, but transfer pricing is increasingly being addressed by the SFTA. Transfers of intangibles and transactions with related offshore companies, in particular in the financial industry, receive specific scrutiny.

### APA opportunity

There are no specific formal APA procedures. Nevertheless, the SFTA has already participated in several multilateral APAs. In practice, however, unilateral rulings are more common. APA procedures are carried out in accordance with the applicable rules for mutual agreement procedures. All Swiss signed double tax treaties usually contain a provision on the mutual agreement procedure, under which the SFTA can launch an APA process.


# Taiwan

## Taxing authority and tax law

Tax authority: National Tax Administration (NTA)

Tax law:

- Articles 43-1 of the Income Tax Law (ITL)
- Article 50 of the Financial Holding Company Law
- Article 42 of the Business Mergers and Acquisitions Law

## Relevant regulations and rulings

The Taiwan Transfer Pricing Examination Guidelines (TP guidelines) were put into effect on 30 December 2004.

## OECD guidelines treatment

The tax authority recognizes the OECD guidelines.

## Priorities/pricing methods

In accordance with the TP guidelines, the pricing methods are as follows: CUP, Resale Price, Cost Plus, Profit Split, Comparable Profit method (or TNMM) and other methods prescribed by the Ministry of Finance (MOF).

## Transfer pricing penalties

Pursuant to the TP guidelines, under certain circumstances, a maximum of 200% of the tax shortfall could be imposed if assessed by the tax authority.

## Penalty relief

There is currently no penalty relief regime in place.

## Documentation requirements

Except for immaterial related-party transactions, extensive contemporaneous documentation is required. According to the TP guidelines, upon filing of the annual income tax return, an enterprise must have the transfer pricing report and relevant documentation prepared.

In December 2005, the tax authority issued a safe harbor rule for transfer pricing reports in Tax Letter Ruling No. 09404587590. The ruling provides that an enterprise is not required to prepare a transfer pricing report (other supporting documents are allowed) if any of the following criteria is met:

- The total annual revenue (including operating and non-operating) of the enterprise does not exceed TWD100m
- The total annual revenue (including operating and non-operating) of the enterprise exceeds TWD100m but does not exceed TWD300m
  - The enterprise does not utilize tax credits for more than TWD1m or loss carry forwards for more than TWD4m to reduce the income tax or undistributed earnings surplus tax
  - An enterprise under the Financial Holding Company Law or Mergers and Acquisitions Law has no overseas related parties (whether a company or an individual), or an enterprise has no overseas affiliated companies
- The total annual controlled transactions amount is less than TWD100m

# Taiwan (continued)

## Documentation requirements (continued)

If the Taiwan enterprise meets the safe harbor threshold and does not prepare a transfer pricing report, the tax authority still may request "other supporting documents" as evidence of the arm's length nature of the intercompany transactions. One example of an "other supporting document" as stated under the ruling is the parent or headquarters' transfer pricing report, as long as it does not significantly vary from the concepts presented in the Taiwan TP guidelines.

In November 2008, the tax authority released a new letter ruling (No.09704555160) to further loosen the safe harbor criteria. The new rule is applicable for fiscal years ending in December 2008 and onwards. The ruling states that an enterprise is not required to prepare a transfer pricing report if any of the following three criteria are met:

- The total annual revenue (including operating and non-operating) of the enterprise does not exceed TWD300m
- The total annual revenue (including operating and non-operating) of the enterprise exceeds TWD300m but does not exceed TWD500m and
  - The enterprise does not utilize tax credits for more than TWD2m in a particular year or a loss carry forward for more than TWD8m for the preceding five tax years to reduce the income tax or undistributed earnings surplus tax
  - An enterprise under Financial Holding Company Law or Mergers and Acquisitions Law has no transactions with any overseas related parties (whether a company or an individual), or an enterprise has no transactions with overseas affiliated companies; or
- The total annual controlled transactions amount is less than TWD200m

The categories of documentation required are:

- Business overview
- Organizational structure
- Description of controlled transactions
- Transfer pricing report, including:
  - Industry and economic analysis
  - Functions and risks analysis
  - Application of the arm's length principle
  - Selection of comparables and related information
  - Comparability analysis
  - Transfer pricing methods selected by the enterprises
  - Transfer pricing methods selected by related parties under the same control
  - Result of comparables search under the best method of transfer pricing
- Report of affiliated enterprises under Article 369 of the Republic of China (ROC) Company Law
- Any other documents that have significant influence over pricing between the related parties

## Documentation deadlines

According to the TP guidelines, upon filing the annual income tax return, the taxpayer must have the transfer pricing report and relevant documents prepared. If the tax return meets the requirement for certification, the Tax CPA has to note on the return whether the enterprise has prepared a transfer pricing report in accordance with the TP guidelines. No attachment of the report to the return is required upon filing.

In accordance with the TP guidelines, upon audit, the enterprise has to provide the tax authority with the report within one month. With the approval of the tax authority, the submission could be extended for one month under special circumstances.

# Taiwan (continued)

## Statute of limitations on transfer pricing assessments

The statute of limitations is five years if the tax return was timely filed and seven years if not.

## Return disclosures/related-party disclosures

Beginning in 2004, a taxpayer must disclose related-party transactions and include the disclosure under the annual income tax return pursuant to the TP guidelines. The disclosure generally includes:

- The investing structure
- Identification of related parties
- The related-party transaction amounts by type
- The related-party transaction balances
- The related parties' financial information, including total revenues, gross margins, operating margins and net margins
- Whether the enterprise has prepared transfer pricing documentation for that fiscal year

The tax authority issued safe harbor rules for related-party transaction disclosures in Tax Letter Ruling No. 09404587580 for tax year 2005 and in Tax Letter Ruling No. 09604503530 for tax year 2006 and onwards. Both Rulings provide that an enterprise must disclose related-party transactions on its income tax return if the sum of its annual operating and non-operating revenue (total annual revenue amount) exceeds TWD30m and also meets one of the following:

- Has related parties outside the territory of the ROC (including the headquarters and branches)
- Utilizes tax credits for more than TWD500,000, or utilizes loss carry forwards for more than TWD2m to reduce the income tax or undistributed earnings surplus tax
- Exceeds total annual revenue of TWD300m

## Audit risk/transfer pricing scrutiny

On 2 August 2005, the MOF issued a Tax Letter Ruling No. 9404540920 that set forth the circumstances for a transfer pricing audit as follows:

- The gross profit ratio, operating profit ratio and net income before tax ratio are below the industry average
- The parent or headquarters reports profit on the global consolidation level, but the local affiliate reports loss or much less profit than the industry average
- An enterprise reports significant fluctuations of profit over the transaction year and the two years preceding
- An enterprise fails to disclose related-party transactions in accordance with the related-party transaction disclosure requirements
- An enterprise fails to determine whether its related-party transactions are within an arm's length range and fails to prepare documents in accordance with the TP guidelines
- An enterprise fails to charge related parties in accordance with the TP guidelines or charges an abnormal amount
- An enterprise fails to provide the transfer pricing report upon a tax audit
- The transfer pricing of the enterprise has been adjusted by the tax authority, in which case, the tax years preceding and subsequent to the year of a transfer pricing audit are likely to be selected for audit
- An enterprise has significant or frequent controlled transactions with related parties in tax havens or low tax jurisdictions
- An enterprise has significant or frequent controlled transactions with related parties entitled to tax incentives
- Any other transaction fails to meet the arm's length requirements in accordance with the TP guidelines

### Audit risk/transfer pricing scrutiny (continued)

In general, the level of audit risk is high. In the past year, there has been increased activity from Taiwan's tax authority especially with respect to requests to see documentation reports. These requests seem to be made irrespective of the revenue, the existence of cross border transactions or relative size of the company. In particular, companies conducting business through tax havens have attracted more scrutiny along with those making losses.

### APA opportunity

APAs are available under articles 23 through 32 of the TP guidelines. According to Tax Letter Ruling No. 9404540920, under an APA, a tax return is not subject to a transfer pricing audit except for the following circumstances:

- The enterprise fails to provide the tax authority with the annual report regarding the implementation of the APA
- The enterprise fails to keep the relevant documents in accordance with TP guidelines
- The enterprise fails to follow the provisions of the APA
- The enterprise conceals material facts, provides false information or conducts wrongful acts


# Thailand

## Taxing authority and tax law

Tax authority: Thai Revenue Department (TRD)

Tax Law: General TP-relevant provisions of the Thai tax code (dealing with exchanges at below-market price):

- Sections 65 bis (4) and (7); §70 ter; §65 ter (13), (14), (15) and (19); and §79/3 under the Thai Revenue Code
- Double Tax Agreements between Thailand and other countries
- Standard Accounting Nos. 37 and 47

Transfer pricing guideline: Departmental Instruction No. Paw. 113/2545

## Relevant regulations and rulings

On 16 May 2002, the TRD issued its guideline specifically addressing transfer pricing. The TP guideline, Departmental Instruction No. Paw. 113/2545, is written in the form of an internal departmental instruction which provides guidance to tax officials for tax audit purposes.

On 23 April 2010, the TRD issued the Bilateral Advanced Pricing Agreement (BAPA) guideline stipulating the guidelines on the BAPA process, including procedures for BAPA applications; level of information required; circumstances under which the TRD may discontinue a BAPA; and taxpayer compliance after a BAPA is concluded.

## OECD guidelines treatment

The TP guideline generally follows the model of the OECD guidelines, including allowing all methods allowed under the OECD guidelines. This includes supporting material beyond the scope of the OECD guidelines. The OECD guidelines are not binding on the TRD. The OECD guidelines may, however, be persuasive in areas not addressed by the Thai Transfer Pricing guideline.

## Priorities/pricing methods

The TRD accepts CUP, Resale Price and Cost Plus. Other commercially used methods are also acceptable, such as the OECD's Profit Split and TNMM.

## Transfer pricing penalties

There is no explicit penalty for TP assessments. Nor is there an explicit penalty for not having TP documentation.

However, for tax shortfalls in general, if a company is assessed by the TRD, a penalty of 100% or 200% of the tax shortfall and a 1.5% per month surcharge may be imposed. The 1.5% monthly surcharge is capped at 100% of the tax shortfall amount.

## Penalty relief

In the event of a transfer pricing adjustment, there is no formal penalty relief for having in place TP documentation.

Penalties may be reduced by half or waived if the taxpayer voluntarily files a return and accounts for the tax shortfall. Surcharges are a form of interest and cannot be reduced. Contemporaneous documents cannot be used to reduce the penalty for a transfer pricing shortfall. However, they are important for the defense of transfer pricing should a tax audit take place.

# Thailand (continued)

## Documentation requirements

The following extensive contemporaneous documentation is specified:

- The structure and relationships between business entities within the same group, including the structure and nature of business carried on by each entity
- Budgets, business plans and financial projections
- Taxpayers' business strategies and the reasons for adopting those strategies
- Sales and operating results and the nature of transactions between business entities within the same group
- Reasons for entering into international transactions with business entities in the same group
- Pricing policies, product profitability, relevant market information and profit sharing of each business entity
- Functions performed, assets utilized and risks assumed by the related business entities should all be considered
- Support for the particular method chosen
- Where other methods have been considered, details of those methods and the reasons for their rejection (contemporaneously documented)
- Evidence supporting the negotiation positions taken by the taxpayer in relation to the transactions with business entities in the same group and the basis for those negotiating positions
- Other relevant documentation (if any) supporting the transfer prices

## Documentation deadlines

The taxpayer is required to submit the transfer pricing documentation as and when requested by the TRD within the submission date stipulated in the requesting letter. However, the taxpayer may request for an extension of the submission if necessary. Such a request is required to be a written letter for submission to the TRD. In general, the extension granted from the TRD is up to one month after receiving the letter.

## Statute of limitations on transfer pricing assessments

Under Section 19 of the Thai tax code, the statute of limitations is two years from the date of filing the tax return. This period is extendible to five years if tax evasion or fraud is suspected.

## Return disclosures/related-party disclosures

No disclosure of the existence or non-existence of transfer pricing documentation is required to be submitted with a tax return. Nor does any documentation need to be filed with a tax return.

Under the Thai Federation of Accounting Professions and Securities and Exchange Commission of Thailand (SEC) regulations, the related party transactions of companies listed on the SEC must be disclosed in the company's financial statements and annual report. Non-listed companies are not required to disclose related-party transactions in their financial statements.

# Thailand (continued)

## Audit risk/transfer pricing scrutiny

Scrutiny of transfer pricing during a tax audit or inquiry in Thailand is common and the risk to the average multinational company is moderately- to slightly-high. The TRD expects taxpayers to cooperate in providing relevant transfer pricing support documentation. It is likely that failure to do so will lead to a tax audit.

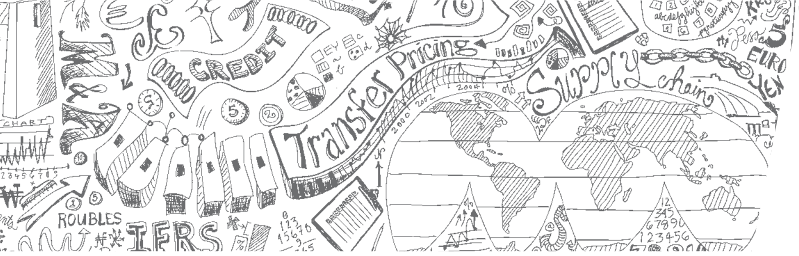
Generally, the TRD makes transfer pricing adjustments to the deductibility of expense items through its annual routine visits to taxpayers to review their business operations. During such checks, if officials find any transactions warranting further scrutiny (including deductibility of expenses arising from intercompany transactions), a further investigation will be conducted. In most cases, the taxpayer under investigation will be required to add back the expenses (to the extent deemed excessive) to taxable income and pay the additional tax arising. The final tax adjustments are then generally settled by way of negotiations.

Since 2006, there has been more aggressive enforcement by the TRD in all areas of tax, especially transfer pricing. The increased level of enforcement mainly arises from tax collection pressure on the TRD to compensate for customs duty and excise tax shortfalls.

## APA opportunity

Given that the formal BAPA guideline has been issued in April 2010, TRD actively encourages taxpayers to enter into an APA due to reasons such as allowing a greater degree of certainty in terms of future taxes to be paid, and eliminating double taxation pursuant to double tax treaties signed between Thailand and other jurisdictions.

Currently, TRD is active in negotiating APAs with Japan. Since the issuance of the Thai transfer pricing guideline and BAPA guideline in 2002 and 2010, respectively, there were four BAPAs concluded between Thailand and Japan to date. Currently, there are fifteen BAPAs that are in the process of being reviewed and negotiated.




# Turkey

## Taxing authority and tax law

Tax authority: Ministry of Finance

Tax law: Transfer pricing is regulated in Article 13 of Corporate Tax Code numbered 5520, published 21 June 2006

Article 13 of Corporate Tax Code states: "Income shall be considered to have been wholly or partially distributed in a disguised manner through transfer pricing, if the company engages in purchase of goods and services with related parties at prices or at amounts which they determine are not complying with the arm's length principle."

Transfer pricing provisions have been effective since January 2007.

## Relevant regulations and rulings

There is a cabinet decree published in December 2007, and two communiqués have been issued by the Ministry of Finance, namely "General Communiqué on Disguised Profit Distribution By Means of Transfer Pricing Serial No. 1 and 2." There is no ruling yet, however there is a recent court case which reveals for the first time the Tax Court's approach to the use of databases for transfer pricing documentation purposes. The Tax Court rejected the use of the Amadeus database for benchmark studies on the grounds the database does not contain any Turkish companies and provides information on the companies located throughout Europe. The court decision is specific to this particular event. However, it has raised questions about the use of the Amadeus database in transfer pricing documentation studies.

A large number of court cases exist on the subject of disguised profit distribution (legislation before transfer pricing). They are mostly conflicting and fail to establish a case law which would bind all the parties. Additionally, tax auditors recently started with their TP inspections for 2007 and following years, especially in the pharmaceutical sector. Since the inspections are at starting phase, the approach of the tax auditors and the courts are still uncertain.

## OECD guidelines treatment

In the preamble of the law, it is stated that the provisions of international regulations, especially the OECD Transfer Pricing Guidelines, are taken as a reference. However there is no particular reference to the OECD guidelines in the actual content of the regulations, including Article 13 of the Corporate Tax Code, the related decree and communiqués. In addition, there are two major differences from the OECD approach: the term "related party" is defined in a very broad manner, for example it includes all shareholders regardless of the level of interest and domestic related-party transactions are also covered by the new rules.

In general, the new transfer pricing rules place significant documentation and disclosure requirements on Turkish taxpayers, but it is difficult to estimate the level of assurance provided by fulfilling these requirements at the moment, as the intention of the new transfer pricing rules from the tax authority's point of view is to protect Turkey's tax base.

One of the obstacles in the way of a smooth transition in the application of the new transfer pricing rules is the lack of a reference for comparable searches and the difficulty in finding comparables, particularly in the Turkish domestic market. There is no database available for local benchmarking studies.

## Priorities/pricing methods

Taxpayers can use the following methods in order to prove that the prices applied in their transactions with related parties are arm's length: CUP, Resale Price and Cost Plus. If it is not possible to reach the arm's length price through one of these traditional methods, profit methods such as Profit Split, TNMM/CPM and other methods to be determined by the taxpayers can be selected. Taxpayers should select the most appropriate method according to the nature of their business, comparability factors and availability of relevant information. There is no priority among the traditional methods.

# Turkey (continued)

### Transfer pricing penalties

There are no specific transfer pricing penalties, but a disguised income distribution is assumed to exist if the transfer prices applied in related-party transactions do not meet the arm's length principle. If such a disguised distribution is assessed during a tax audit:

- For corporate income tax purposes, 20% corporate income tax is calculated again as if no disguised distribution were applied
- Dividend withholding tax of 15% is calculated over the net amount of the disguised distribution

Additionally, late payment interest and a tax loss penalty (which is the same as tax loss amount) is charged to the tax payer.

### Penalty relief

There are no special provisions for penalty relief. However, it is possible to come to a reconciliation regarding tax loss and tax penalty assessed. In such reconciliation the taxpayers may claim good faith.

### Documentation requirements

Taxpayers are required to submit a transfer pricing form related to transactions with related parties. This form should be submitted as a supplement attachment to the corporate tax return, which must be filed by the deadline of the 25th day of the fourth month following the fiscal year.

In addition to the transfer pricing form, certain taxpayers are required to file an "Annual Transfer Pricing Report." This requirement applies to:

- Corporate taxpayers who are registered with the "Grand Taxpayers Tax Office" prepare the report covering all domestic and foreign related-party transactions
- Corporate taxpayers having activities in Turkish Free Trade Zones prepare the report covering domestic transactions conducted with related parties
- Other taxpayers prepare the report for the purpose of disclosing transactions conducted with foreign related parties

This documentation report should include, company analysis, industry analysis, related parties, each transaction conducted with related parties with their values, functional analysis and economic analysis (selection of transfer pricing method, benchmarking studies and financial analysis).

The Report is required to be prepared by the 25th day of the fourth month following the fiscal year, which is the due date of the corporate income tax return. After this date taxpayers should present their documentation reports to the tax authority within 15 days of a request by the tax authority.

### Documentation deadlines

Stated in "Documentation requirements" section above

### Statute of limitations on transfer pricing assessments

There is no specific statute of limitations on transfer pricing assessments, but general rules for the statute of limitations are applicable, which is five years from accrual of the tax payment.

# Turkey (continued)

## Return disclosures/related-party disclosures

Taxpayers are required to disclose information on all related-party transactions in their transfer pricing forms. In addition, taxpayers are required to prepare an Annual Transfer Pricing Report which should include this information in detail.

The information will include the name or title of the local related party, taxpayer identification number, name of the foreign related-party and the country in which it resides. Other required disclosures include the sale and purchase of commodities both in the form of raw material and finished goods, the lease of any property, construction services, research and development, commission-based services, all related-party financial transactions, including lending and borrowing funds, marketable securities, insurance and other transactions and intra group services. Taxpayers also must disclose the transfer pricing methods applied in the related-party transactions.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing scrutiny during a tax audit is high. Tax inspectors generally focus on related-party transactions. With the abundance of related-party transactions, it is likely that tax inspectors will extend their tax audits. New transfer pricing rules have increased the awareness of transfer pricing applications in general. As a result of this in 2010 tax audits are mainly focused on intra-group charges such as management fees and cost allocations. Tax inspectors developed a different point of view and they look for whether specific services or projects are provided under the name of management fee or not (e.g., preparation of a procurement agreement, redesign of compensation policy or legal advisory for a court case). If the service charges are not documented with such specific services or projects provided particularly to the Turkish entity, then these charges are categorized as royalty, based on the claim that industrial or commercial experience is used, and subject to withholding tax.

Additionally tax auditors continue with their TP audits in pharmaceutical sector, for the active material prices imported from the group companies.

## APA opportunity

An APA is possible upon the demand of the taxpayer. In principle, the agreed-upon method would be binding through the period determined; however, it cannot exceed three years. APA applications will be allowed for Grand Taxpayers Tax Office corporate taxpayers as of 1 January 2008 for their foreign transactions. Other taxpayers will be able to apply for APAs as of 1 January 2009. To our knowledge, none of the companies operating in Turkey applied for an APA yet.


# United Kingdom

## Taxing authority and tax law

Tax authority: Her Majesty's Revenue and Customs ("HMRC") publishes its internal guidance on its website and this provides tax payer and their advisers with an insight into how HMRC applies the legislation. HMRC also publishes technical notes and Statements of Practice concerning a number specific transfer pricing related topics.

Tax law: The UK's domestic transfer pricing legislation is now consolidated and set out in Part 4 of the Taxation (International and Other Provisions) Act 2010 ("TIOPA 2010").

## Relevant regulations and rulings

The UK does not have a rulings process for transfer pricing outside of an Advance Pricing Agreement ("APA"). The legislation governing the unilateral APA process is set out in Part 5 of TIOPA 2010. A statement of practice governing the application of the statutory provisions for APAS was first published in 1999 and a revised statement is expected before the end of 2010. For APAs to be admitted to the program there needs to be sufficient doubt or difficulty in approaching compliance with the arm's length standard. Limited resources limit the UK to around 18-20 new admissions to the program each year although there is a stated intention to increase this number year on year. The UK also operates a thin cap agreement system which uses the APA legislation. These are known as Advance Thin Cap Agreements ("ATCAs"). Agreements in this regard are typically couched around covenants similar to that of third party lenders.

The UK operates a risk based approach to enquiries and in relation to compliance obligations. Most MNCs will have had a risk assessment in the UK and may approach HMRC for a discussion around the risks associated with their transfer pricing. This could result in a Low Risk rating which, although short of an APA and its contractual terms, would provide some comfort as to the meeting of their compliance obligations and the robustness of their intra-group pricing. Such discussions are encouraged by HMRC.

## OECD guidelines treatment

Section 164 TIOPA 2010 confirms that the UK's transfer pricing provisions are to be construed in alignment with Article 9 the OECD Model Tax Convention and its associated transfer pricing guidelines. For these purposes the transfer pricing guidelines mean all the documents published by the OECD at any time before 1 May 1998 "as part of their Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" and any other documents designated as such by Treasury order.

As at the date of drafting this entry, no Treasury orders have been made which means that the status of any updates made by the OECD since 1 May 1998, in particular the amendments published by the OECD in July 2010, under UK tax legislation is unclear. It is understood that HMRC are considering whether legislative changes are required.

Notwithstanding the above, HMRC actively participates in OECD Committees and generally tries to apply the most recent OECD pronouncements to the interpretation of double taxation agreements that are based on the OECD Model Convention.

## Priorities/pricing methods

The OECD Guidelines are followed in regards to pricing methods. HMRC generally prefers transaction methods over profit methods (such as with the TNMM). However, there is a recent move by the HMRC towards testing results against systems profits. This may also be mirroring OECD developments in this area.

Following a recent tax case, HMRC are believed to more routinely challenge the robustness of external CUP data (in particular in relation to IP licenses) unless there has been a testing of the relevant parties bargaining positions in coming to the license agreement.

## Transfer pricing penalties

For accounting periods ending on or after 1 April 2008, the provisions for neglect penalties are set out in Schedule 24 Finance Act 2007. These provisions are couched in terms of careless or deliberate inaccuracies rather than neglect. They are tax geared at up to 100% of the potential lost revenue figure. This is, however, now calculated without adjustment for the availability of loss reliefs and where the adjustment affects losses only; the lost revenue figure to which the penalty percentage is applied is calculated at 10% of the loss adjustment.

# United Kingdom (continued)

## Transfer pricing penalties (continued)

HMRC has recently published revised guidance setting out examples of negligence/carelessness which carry lower tax geared penalties (maximum penalty of 30%), and deliberate inaccuracies where the penalties will be higher (maximum penalty of 70%).

Examples of negligence and carelessness include:

- No attempt to price the transaction
- Shared service centre overseas, cost base, allocation key applied – turnover, modest mark up, but no consideration of benefits test for UK entity
- Policy, otherwise arm's length, not properly applied in practice

Examples of deliberate inaccuracies include:

- A clear internal Comparable Uncontrolled Price has been omitted with no reasonable technical analysis to support why it has been disregarded
- A cost plus return to a company that has in reality controlled the development of valuable intangibles (as not demonstrable as a sub-contractor to group members)
- Material factual inaccuracies in the functional analysis on which the pricing analysis has been based

## Penalty relief

The best protection against neglect penalties is a transfer pricing policy which fully documents and evidences due consideration of the application of the arm's length principle in the preparation of the relevant tax return.

## Documentation requirements

HMRC's internal guidance sets out what types of documents that it might expect to be kept. This guidance is stated as building upon that published by OECD. The UK Guidance divides documentation into primary accounting records, tax adjustment records and, most importantly, evidence. Documentation relating to evidence of compliance with the arm's length principle is to follow the OECD guidelines, and HMRC has set out some suggestions on what this should or may include, such as:

- An identification of the associated enterprises with whom the transaction is made
- A description of the nature of the business
- The contractual or other understandings between the parties
- A description of the method used to establish or test the arm's length result, with an explanation of why the method is chosen
- An explanation of commercial and management strategies, forecasts for the business or technological environment, competitive conditions and regulatory framework

HMRC applies a risk-based approach under which they would expect the level and depth of analysis to be dictated by the perceived risk of tax loss through manipulation of pricing. This typically allows a light touch approach to most UK to UK transactions.

## Documentation deadlines

Under the current guidance, the first two categories of documentation should be in existence when the accounts are prepared and the return submitted. In relation to documentary evidence of arm's length pricing, it is not needed in a form capable of production to HMRC until a request by HMRC has been made. The previous guidance published by the HMRC confirmed that all documentation should be in existence at the time the return is submitted. In practice, evidence confirming adherence to the arm's length principle should exist at the time of submission of the return if difficulties in its production are to be avoided.

# United Kingdom (continued)

### Statute of limitations on transfer pricing assessments

Discovery assessments can be raised six years after the company's accounting period ends, but this is extended to 21 years where the misstatement is due to fraudulent or negligent conduct by the taxpayer. With effect from 1 April 2010 these limits have changed to four years and 20 years respectively. Discovery assessments however require there to have been negligence on the part of the taxpayer (defined as carelessness in the preparation of returns from 2010).

The legislation applicable before 1999 operated in a different manner, and as a result, an investigation started now would not normally lead to transfer pricing adjustments for periods before 1999.

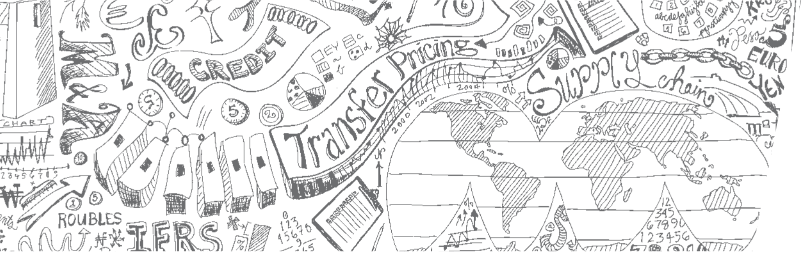
### Return disclosures/related-party disclosures

There are no return disclosure requirements except those required in statutory accounts and in annual reports filed in compliance with any current APAs. The absence of disclosure requirements will typically leave prior years open to discovery assessments.

### Audit risk/transfer pricing scrutiny

HMRC has developed a "Stage Gate" process for transfer pricing enquiries which is set out in the internal guidance published on its website. This process requires a transfer pricing specialist from with HMRC to be assigned where a case team identifies a transfer pricing issue that may necessitate an enquiry. The specialist helps the case team to prepare a risk assessment and a business case for submission to one of two panels set up for the purpose before any enquiry is commenced. The panels also review progress at regular intervals during the enquiry and sign off all settlement proposals.

HMRC considers that this process should lead to more targeted and focused enquiries on areas warranting specialist transfer pricing resources. The risk of audit is therefore high where there are red flags present in the accounts – changed business structure, losses, wildly fluctuating margins, high value-adding functions, etc.




# United States

## Taxing authority and tax law

Tax authority: Internal Revenue Service (IRS)

Tax law: Internal Revenue Code (IRC) §§482, 6038A, 6038C and 6662

## Relevant regulations and rulings

- Treasury Regulations (Treas. Regs.) §§1.482, 1.6662, 1.6038A, 1.6038C
- Revenue Procedure (Rev. Proc.) 2006-54, Rev. Proc. 99-32, and Rev. Proc. 2006-9
- Final regulations (TD 9088) on compensatory stock options under IRC §482, released on 26 August 2003, maintain that stock-based compensation must be taken into account in determining operating expenses for qualified cost-sharing arrangements (CSAs) under Treas. Reg. §1.482-7
- Audit checklist on CSAs issued in August 2005
- In April 2007, CSA buy-ins were designated by the IRS as a "Tier I" issue, and thus susceptible to intensified audit scrutiny
- A Coordinated Issue Paper was released on 27 September 2007 providing internal IRS guidance for examiners in developing CSA exam positions

The Department of Treasury and the IRS released temporary CSA regulations with an effective date of 5 January 2009 (TD 9441, 74 FR 340). These regulations revise the proposed regulations issued in 2005 and replace the existing CSA regulations from 1995. The temporary regulations provide the IRS with discretion to make periodic adjustments and formalize other new requirements for compliance.

New final, temporary, and proposed regulations related to services were issued on 31 July 2006. The new rules were effective 1 January 2007, and apply to tax years beginning after 31 December 2006. In conjunction with the new regulations, the IRS also issued Announcement 2006-50, which contained a proposed list of "specified covered services" that relate to a specific cost-based method. The new services regulations require stock-based compensation to be considered in total costs. On 20 December 2006, the IRS released Notice 2007-5 and Revenue Procedure 2007-13, which extended the effective date of the Services Cost Method until 1 January 2008 and added to the list of "covered services."

## OECD guidelines treatment

The IRS considers its transfer pricing laws and regulations to be wholly consistent with OECD guidelines. For domestic use, the OECD guidelines do not provide support, and would not be directly relevant, to the application of any pricing methods. However, if taxpayers pursue competent authority relief from double taxation or a bilateral APA, the OECD guidelines would be important and may be used to demonstrate compliance with international principles.

## Priorities/pricing methods

For tangible goods, the IRS accepts the CUP, Resale Price, Cost Plus, CPM, Profit Split, and unspecified methods. For intangible goods, the IRS accepts the Comparable Uncontrolled Transaction (CUT), CPM, Profit Split, and unspecified methods. The new services regulations provide for the following methods: Services Cost Method, Comparable Uncontrolled Services Price, Gross Services Margin, Cost of Services Plus, CPM, Profit Split, and unspecified methods.

The Coordinated Issue Paper related to CSAs advises IRS auditors that unspecified methods are appropriate for valuing buy-ins (such as the "income method" and the "acquisition price method"). The regulations provide a "best method rule" for determining the appropriate method to be applied by the taxpayer for each intercompany transaction.

## Transfer pricing penalties

Taxpayers may be liable for either a 20% or 40% penalty for underpayment of tax (IRC §6662), as a percentage of the underpayment, or the penalty may apply to a valuation misstatement. There is not a US penalty for failure to have documentation, but documentation may help to avoid a penalty.

# United States (continued)

## Penalty relief

Penalties may be avoided by adequate disclosure on IRS Form 8275 for disregarding rules or regulations and for a substantial understatement of income tax. Penalties for negligence and for a valuation misstatement are not avoided by disclosure. No penalties apply, however, if there was reasonable cause and the taxpayer acted in good faith with respect to the transaction. The regulations provide guidance for establishing reasonable cause and good faith, for example, by preparing documentation or by obtaining an APA.

## Documentation requirements

Transfer pricing documentation is not required by law. However, in practice, it is recommended that taxpayers maintain contemporaneous documentation in order to avoid penalties. Documentation must be provided to the IRS within 30 days of a request during an IRS examination. To be considered contemporaneous, the documents must be in existence when the return is filed, but their existence does not need to be disclosed with the tax return and they do not need to be provided with the return.

For penalty avoidance purposes, a taxpayer is considered to have satisfied the documentation requirement if it maintained sufficient documentation to establish that the taxpayer reasonably concluded that, given the available data and the applicable pricing methods, the method (and its application of that method) provided the most reliable measure of an arm's length result under the principles of the best method rule.

- A method determined as part of an APA is a consideration for whether the taxpayer's method was reasonable. The principal documents required by regulations are:
- An overview of the taxpayer's business and an analysis of legal and economic factors affecting pricing
- A description of the organizational structure
- Any documents explicitly required by regulations (e.g., CSA documents)
- A description of the pricing method and reasons why the method was selected (a best method analysis)
- A description of alternative methods and why they were not selected
- A description of controlled transactions and any internal data used to analyze them
- A description of comparables used, how comparability was evaluated and any adjustments
- An explanation of any economic analysis and any projections used to develop the pricing method
- Any material data discovered after the close of the tax year but before filing the tax return
- A general index of the principal and background documents and a description of the recordkeeping system

## Documentation deadlines

If documentation is prepared to help protect against penalties, then it must be in place by the filing date of the US tax return. Taxpayers must provide documentation to the IRS within 30 days of an examiner's request.

## Statute of limitations on transfer pricing assessments

A general statute of limitations applies, which is three years from the later of either the tax return due date or the date the return was actually filed. For substantial understatements of income, the statute is extended to six years. For fraud, there is no statute of limitations.

# United States (continued)

## Return disclosures/related-party disclosures

Taxpayers are required to file Forms 5471 and 5472 regarding transactions with related parties, and they may also need to file Form 8275 (regarding disclosure). Under new regulations issued in 2010, certain taxpayers will have to disclose their uncertain tax positions (UTPs) on Schedule UTP, and provide information such as the ranking of the positions by the sizes of their reserves, and concise descriptions of the tax positions. There is a phase in period so that by 2014, the UTP disclosures will be required by corporations with assets of US$ 10m or more.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing scrutiny during a tax audit is high. Transfer pricing is extensively regulated. The designation of CSAs and intellectual property transactions as a Tier I (high-risk transaction) issue for IRS auditors increases the risk for those transactions. This has been borne out in practice, where documentation is requested at the start of any international-issues audit.

## APA opportunity

The IRS has an APA Program Office dedicated to analyzing and negotiating unilateral APAs, as well as bilateral and multilateral APAs with competent authority, as provided in Rev. Proc. 2006-9. The revenue procedure has strict case management procedures, disclosure requirements, and detailed guidance for taxpayers and the IRS in submitting APA requests and processing the analyses. Competent authority guidance is provided in Rev. Proc. 2006-54, which complements the requirements of Rev. Proc. 2006-9.


# Uruguay

## Taxing authority and tax law

Tax authority: General Tax  Direction (Dirección Nacional Impositiva – DGI)

Tax law: Income Tax Law and Regulations

## Relevant regulations and rulings

Transfer pricing documentation requirements have been in effect in Uruguay since 1 July 2007 (following Law #18.803) but they were not regulated until 26 January 2009 with the publication of Decree # 56/009 with modifications made by Decree #392/009.

DGI issued on 1 December 2009 Resolution # 2.084/009 (with the modifications introduced by Resolution # 819/010 and #2.098/009) which defined concepts and established which requirements a transfer pricing report must follow.

## OECD guidelines treatment

Uruguay is not an OECD member and the OECD Transfer Pricing Guidelines are not mentioned in Uruguay's Income Tax Law and Regulations.

## Priorities/pricing methods

The Law establishes that in order to determine the market value, one of the following methods should be applied: Comparable Uncontrolled Price, Resale Price, Cost Plus, Profit Split and Transactional Net Margin Methods. For the application of the transfer pricing methods, the comparability analysis and justification for such prices may be indistinctly performed on the local or foreign party's situation. If the foreign party's situation is chosen, certified documented evidence will be required in the country of origin, issued by a firm of well known independent auditors, duly translated and authenticated.

Uruguayan Law does not prioritize methods. However, for transactions involving imports or exports of goods with well known prices in transparent markets, those prices must be used. If the transactions mentioned before are performed through international intermediaries who are not the final consignees of the goods, the applicable price is the price in the respective market. The price to be used is the one on the respective market on the day of the shipment or the price on the day of the contract if it was registered in the Mercantile Office. It is important that if the contract has been registered, it is mandatory to use the price of the day of the contract.

## Transfer pricing penalties

Since there are no special penalties for failure to file transfer pricing returns, general tax penalties are applicable. Penalties for not filing Form 3001 in due time are UYU260 (approximately US$13).

When there exists underpayment due to transfer pricing, the taxpayer is penalized with a tax omission fine that starts on 5% if it is paid before the fifth day after the deadline, 10% if it is paid between the five and 90 days after the deadline, and 20% if it is paid after 90 days past the deadline. In each case, corresponding surcharges are added.

If the company is accused of tax fraud the fine ranges from 100% to 1,500% of the unpaid tax. The penalty is determined by the DGI according to the circumstances of each case.

It is important to remark that if DGI requires a TP study and a company does not file it, DGI can suspend the certificate that shows that the taxpayer fulfilled his tax obligations. The immediate consequence of which bars the taxpayer from being able to import or obtain a bank loan.

## Penalty relief

There are no provisions for reductions in penalties.

# Uruguay (continued)

## Documentation requirements

Taxpayers who fall under one of the following categories are obliged to file a TP study and the TP annual return (Form 3001) with the tax authorities:

- The amount of the transactions subject to the TP rules is higher than 50 million units (approximately US$5m)
- Registered as Great Taxpayer
- Received a request for filing from the tax authorities

## Documentation deadlines

Four months after the fiscal year end the income tax return is due. In this filing, the company must disclose whether a TP adjustment is needed to have arm's length prices in its transactions with related parties and unrelated parties located in tax havens. Thus, the TP analysis should be performed by that time, even though the documentation is not due until later (nine months after fiscal year end).

Nine months after fiscal year end:

- TP annual return (Form 3001) including detailed information of all cross-border intercompany transactions (or those performed by the local company with entities located in tax havens)
- TP study (Regs. 2.084/009), to be filed together with Form 3001

## Statute of limitations on transfer pricing assessments

There are no specific limitations and the general regime applies. Assessments can be raised five years after the company's accounting period ends, but this is extended to 10 years where the difference is due to fraudulent or negligent conduct by the taxpayer.

## Return disclosures/related-party disclosures

Taxpayers are required to file:

- The TP study with key elements, such as the functions and activities of the company, risks and assets used, the methods used, the interquartile range, details of the comparables, etc.
- Annual tax return Form 3001

## Audit risk/transfer pricing scrutiny

September 2009 was the first time that taxpayers had to file a TP study so there is no background on TP audits yet.

## APA opportunity

APAs are not specifically addressed.


# Venezuela

## Taxing authority and tax law

Tax authority: Venezuelan Tax Administration (SENIAT)

Tax law:

- 2001 Master Tax Code: Chapter III, Articles 109 to 111, and 220 to 229
- 2001 Venezuelan Income Tax Law, Chapter III, Articles 112 to 170
- 2007 Income Tax Law Reform, Article 118 - inclusion of thin capitalization rules

## Relevant regulations and rulings

On February 2007, a partial reform of the Income Tax Law and rules in thin capitalization were published in the Official Gazette No.38.628. The thin capitalization rules apply, as of fiscal year 2008, to where a Venezuelan taxpayer or a Venezuelan Permanent Establishment has debt (controlled debt) to companies or individuals who are considered related according to Title VII, Chapter III, in the transfer pricing rules. The main inclusions are as follows:

- Taxpayer will have a limited possibility to deduct interest expenses resulting from related parties' loans when the average of its debts (with related and unrelated parties) exceeds the amount of the average of its equity for the respective fiscal year
- The extent of debt that exceeds the taxpayer's equity will be treated as equity for income tax purposes

## OECD guidelines treatment

The 1995 and its subsequence updates of the OECD guidelines are applicable as a supplement to these rules for everything else not considered in the Venezuelan Income Tax Law.

## Priorities/pricing methods

The acceptable methods are OECD methods: CUP, Resale Price, Cost Plus, Profit Split and TNMM. Priority is given to the CUP method.

## Transfer pricing penalties

By failing to apply the transfer pricing methods, the taxpayer faces fines from 300 to 500 Tax Units.[1] In addition, there will be a fine ranging from 25% to 200% of the omitted tax amount, and late payment interest may also be added to these amounts in the case of a transfer pricing assessment. Failing to issue the transfer pricing informative return (PT-99) will trigger a penalty of 10 to 50 Tax Units.

## Penalty relief

If a taxpayer complies with a transfer pricing method, this could be considered a mitigating circumstance in the determination of an assessment. This penalty relief is based on previous tax audit procedure and assessments, but there is not a legal provision to support it.

## Documentation requirements

Effective in 2002, taxpayers are required to prepare and maintain supporting and extensive contemporaneous documentation. The documentation requirements include functions, assets, risks, organizational structure, business descriptions, detailed information of all operations with related and non-related parties, audited financial statements, agreements and contracts, reasoned method selection, inventory valuation method (if applicable), analysis results and other relevant information.

[1] 2010 Tax Unit = BSF 65/unit.

# Venezuela (continued)

## Documentation deadlines

The taxpayer must prepare documentation by the filing date of the annual income tax return at the end of every fiscal year. In addition, the taxpayer must submit the documentation upon request by SENIAT during a transfer pricing audit. It is mandatory to file the transfer pricing informative return (PT-99) during the month of June for those taxpayers who have their fiscal year ending in December. In other cases, the filing deadline will be six months after the specific year's closing.

## Statute of limitations on transfer pricing assessments

The statute of limitations is four years from the date of filing the return and six years if the taxpayers failed to comply with the filing of any tax return, such as an income tax return, VAT returns or customs duties returns. PT-99 is not considered a tax return.

## Return disclosures/related-party disclosures

A controlled party's information return must be filed during the six months immediately following the closing of each tax year. The PT-99 form is available in the tax authority's website (www.seniat.gob.ve).

## Audit risk/transfer pricing scrutiny

SENIAT has been very active in transfer pricing audits lately. In the general tax audits has added transfer pricing as a relevant topic to be audited. Thus far, audits have been performed on taxpayers in the oil industry, pharmaceutical industry, service providers, consumer products industry, automotive and steel and iron producers.

SENIAT has issued several transfer pricing assessments to relevant multinational corporations in diverse industries, which have been publicly informed, and the assessed amounts ranged from US$ 5m to US$ 67m.

The audits have been organized by industry and the taxpayers are selected by:

- Having inconsistency between the transfer pricing report, income tax return and the transfer pricing informative return
- Using the TNMM
- Using non-updated financial information from comparable companies up to June of the fiscal year subject to study
- Having profit level indicators below the interquartile arm's length range
- Showing lower operating margins compared with operating margins from the previous year

The risk of transfer pricing scrutiny is high when a taxpayer performs financial operations directly or indirectly with related parties and when taxpayers have technical assistance or know how agreements with related parties abroad.

## APA opportunity

Unilateral and bilateral APAs are available to the extent that they are carried out with nations that have outstanding double taxation treaties (see Income Tax Law Articles 143 to 167, and Master Tax Code Chapter III, Articles 109 to 111, and Articles 220 to 229).


# Vietnam

## Taxing authority and tax law

Tax authority: General Department of Taxation (GDT)

Tax law:

- The Law on Tax Administration[1] contains an article (Article 37) on the arm's length principle that empowers tax authorities to adjust the value of purchases, sales, exchanges and accounting records of goods and services of taxpayers not in accordance with market prices. The arm's length principle is also included in Article 26 of Decree 85/2007[2] and Part B, Sec. XII, Clause 2.2 of Circular 60/2007.[3]
- Detailed transfer pricing regulations are included in Circular 117/2005/TT/BTC (Circular 117) dated 19 December 2005 of the Ministry of Finance and Circular 66/2010/TT/BCT (Circular 66) dated 22 April 2010 of the Ministry of Finance which provide Guidelines on the Calculation of Market Prices in Business Transactions between Related Parties. Circular 117 was replaced by Circular 66.

## Relevant regulations and rulings

See above Law, Decrees and Circulars. Circular 117 is still applicable to transactions which took place in financial years 2006-2009. Circular 66 governs related party transactions between related parties which take place from 2010 onwards.

Circular 66/TT-BTC sets forth formal and comprehensive guidelines on many significant issues with respect to the interpretation and application of the arm's length principle. The main elements of the Circular include the arm's length principle, definition of market prices, material differences, associated parties, acceptable transfer pricing methods, the "most appropriate method" rule, arm's length range, benchmarking principles, acceptable database, and annual declaration of related-party transactions and requirement of contemporaneous transfer pricing documentation.

HCM City Tax Department has recently issued the Official Letter 3304/TB-CT on 15 September 2010 requesting all enterprises in the territory, with related-party transactions, to prepare and submit mandatory TP Disclosure Forms based on Circular 117/2005/TT-BTC for the financial years 2006-2009 by 20 October 2010 at the latest, if not already filed. Failure to submit the information could trigger the selection of company for tax audit and if transfer pricing issues are detected, the company will subject to penalties under tax evasion provisions, including criminal proceedings. In addition, companies with related-party transactions are required to comply with the FY2010 requirements in a timely manner (i.e., submission of the mandatory TP Disclosure Form and maintenance of TP documentation by 31 March 2011 based on Circular 66).

Hanoi Tax Department issued Official Letter 17825/CT-KT1 on 29 September 2010 requesting a transmission and distribution company to submit transfer pricing disclosure form and contemporaneous transfer pricing documentation supporting the arm's length nature of its related party transactions and the most appropriateness of the selected transfer pricing method based on Circular 117/2005. The company is given only 30 days to provide the tax authority with such required form and documentation.

The Vung Tau Tax Department also issued Official Letter (6443/CT-TB) on 21 October 2010, requesting companies to submit their annual transfer pricing declaration forms for past years.

## OECD guidelines treatment

Circular 117 and Circular 66 are generally based on the OECD guidelines. How the GDT will apply the OECD guidelines in interpreting the principles under Circular 117 remains to be seen during the first few years of implementation of the Circulars. Transfer pricing documentations adhere to the OECD guidelines in applying the principles of Circular 117 and Circular 66.

## Priorities/pricing methods

Circular 117 and 66 permit the use of the following methods: CUP, Resale Price, Cost Plus, CPM (or TNMM) and Profit Split. Taxpayers must use the most appropriate method under the regulations. There is no hierarchy among the methods although an internal CUP appears to be preferred.

[1]This Law was enacted by National assembly on 29 November 2006 and effective from 2007.
[2]This Decree was issued by the Government on 7 June 2007, stipulating in detail the implementation of a number of Articles of the Tax Administration Law.
[3]This Circular was issued by the Ministry of Finance on 14 June 2007, providing guidelines for the implementation of Decree 85/2007.


Contents

# Vietnam (continued)

## Transfer pricing penalties

Adjustments in corporate income tax liabilities may be made by the tax authority in the following cases:

- Failure to disclose, or incomplete disclosure, of related-party transactions
- Failure to produce information, documents or source documents within 30 days of a request by the tax authority
- Intentional erroneous application of the provisions of the Circulars and failure to produce substantiation requirements within 90 days of the date of request by the tax authority

Administrative penalties ranging from VND500,000 to VND5m may be imposed for failure to comply with TP documentation and disclosure requirements, and an interest penalty of 0.05% of the outstanding tax due may also be imposed in case if there is a TP adjustment. Additional penalties of up to five times of the outstanding tax due may be imposed if there is a finding of tax evasion or fraud.

Vietnamese law allows for criminal proceedings against the taxpayer if a significant tax evasion is proved. According to the Vietnamese Criminal Law, if the evaded (underpaid) tax amount is VND100m (approximately US$5,200) or more, the taxpayer may be subject to tax penalties under criminal proceedings.

## Penalty relief

Penalties may be avoided by adequate disclosure on Form GCN-01/HTQT of the related-party transactions and the preparation and timely production of transfer pricing documentation.

## Documentation requirements

Contemporaneous documentation is required by law. Documentation must be provided to the tax authority within 30 days upon request. The documents must be in existence when the transaction occurs and must be updated during the performance of the transaction.
For penalty-avoidance purposes, a taxpayer is considered to have satisfied the documentation requirement if it maintained sufficient documentation to establish that the taxpayer reasonably concluded that, given the available data and the applicable pricing methods, the method (and its application of that method) provided the most reliable measure of an arm's-length result under the principles of the most appropriate method rule.

The principal information and documents required by the regulations are:

- Information on relations between affiliated parties and the taxpayer
- Information and updated reports on strategy for development, administration and control between affiliated parties
- The pricing policy for transactions in relation to each group of products in accordance with the general guidance of affiliated parties and the taxpayer
- Documents and reports on the process of development, business strategy, projects, production, business or investment plans
- Regulations and procedures for financial statements and internal control reports of the company and of affiliated parties to the transactions
- A diagram of transactions and documents describing transactions, including information on parties to transactions, order and procedures for payment and delivery of products
- Documents specifying properties and technical specifications of products, the breakdown of costs (or cost) of one product, selling price of products, total amount of products produced or traded and sold in the period (specifying such items on the basis of the related transaction and an independent transaction, if any) and the quantity of products
- Information, documents and source documents concerning the process of negotiation, signing, performance and liquidation of economic contracts and agreements related to transactions (usually including a description of products, place of transaction, form of transaction, value of transaction, terms of payment, payment documentation, period of performance, minutes of meetings or instructions of the management regarding the process of negotiation, signing and the performance of a transaction)

# Vietnam (continued)

## Documentation requirements (continued)

- Information, documents and source documents related to economic conditions of the market at the time of the related transactions affecting the method of calculation of a price for transactions (for example, changes in exchange rates and policies of the government affecting prices in transactions and financial incentives)
- The pricing policy for selling and purchasing products and the procedures for control and approval of prices
- Information, documents and source documents used to select the most appropriate method, including data used for comparative analysis and adjustment of significant differences
- Other information or documents used to select and apply the methods

## Documentation deadlines

The documentation must exist at the time of the transaction. Taxpayers must provide documentation to the tax authorities within 30 days of a request. If an enterprise has plausible reasons, a onetime 30-day extension could be applied.

## Statute of limitations on transfer pricing assessments

The general principles on statutes of limitations apply. There is no statute of limitations with respect to the recovery or re-collection of taxes. However, administrative penalties may be imposed only within two or five years from the date of commission to the date of discovery of the violation for tax procedures or tax evasion, respectively.

## Return disclosures/related-party disclosures

Taxpayers are required to file Form GCN-01/HTQT (under Circular 117) and Form GCN-01/QLT (under Circular 66) to disclose their transactions with related parties, the details of these transactions and the transfer pricing methods used to calculate the prices in these transactions. The disclosure form must be submitted with the corporate income tax return, which must be filed within 90 days of the end of the fiscal year.

## Audit risk/transfer pricing scrutiny

The risk of transfer pricing audit is rated as high, because TP regulatory enforcement and audit activities are currently becoming a priority on Vietnam tax authorities' 2010/2011 agenda. Currently the Vietnamese tax authorities are interested in tax and transfer pricing issues of taxpayers, particularly foreign investment enterprises that are found to be in one of the following situations and circumstances:

- Enterprises that are loss-making for several consecutive years and are expanding their business
- Enterprises with related-party service fees that are not adequately substantiated in terms of service received and supporting documentation
- Enterprises with a large volume of related-party transactions
- Enterprises enjoying preferential tax tratement, especially enterprises operating in industrial zones, export processing zones, or high-tech industrial zones
- Enterprises operating in the construction industry, the infrastructure construction business and the real estate business
- Banks
- Enterprises operating in marine service and transportation, especially international marine transportation
- Enterprises in the automobile industry

## APA opportunity

Circulars 117 and 66 do not provide for unilateral or bilateral APAs.

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EYG no. DL0357