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WTS Transfer Pricing Newsletter

Editorial

Dear Reader,

It is our pleasure to present to you the second edition of our WTS Transfer Pricing Newsletter for 2020.

In this latest edition of the WTS Transfer Pricing Newsletter, our colleagues from 13 countries provided an update on recently introduced legislations and cases. Additionally, developments in the field of transfer pricing, due to the economic and social impact of the ongoing COVID-19 pandemic are presented.

Europe

Our **French** colleagues explain what needs to be considered from a transfer pricing perspective in these times of COVID-19, especially with regard to documentation requirements, the use of benchmarking studies and the deductibility of interest expenses.

The tax consequences of the **German** draft law on intercompany financing are compared and discussed both in a purely domestic as well as a cross-border scenario.

Hungary provided its taxpayers a four-month extension of their transfer pricing documentation and furthermore accepts a re-evaluation of the profit-loss model, due to the impact of COVID-19.

In **Italy,** a new Legislative Decree came into force to ensure a more effective EU transfer pricing dispute resolution mechanism.

In an example, our colleagues from the **Netherlands** describe the field of tension in which the OECD regulations and Dutch tax laws on the deductibility of intra-company financing are currently moving.

Ukraine recently introduced new proportional adjustment rules, which could lead to a reduced risk of double taxation triggered by one-sided TP adjustments.

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Further Countries

Our colleagues from **Argentina** provide an overview of the new transfer pricing regulations by summarising the six main aspects of GR4717.

Despite the modernised Income Tax Law and Tax Code, which has been published at the beginning of this year, **Chile** expects further practical and regulatory modifications due to the ongoing COVID-19 pandemic.

The contribution from **Nigeria** sheds light on the first transfer pricing decision of the Nigerian tax appeals tribunal and provides a brief outlook on what taxpayers should consider in view of their transfer pricing.

Pakistan shifted the focus of its Tax Authorities towards transfer pricing issues by introducing regulatory amendments concerning TP audits.

Since the beginning of 2020, reduced limitations on **Taiwan's** "one-time transfer pricing adjustment" became effective, which helps enterprises to achieve an arm's-length result even in times of unexpected market conditions.

Thailand extended the deadline for the 2019 tax return until 31 August 2020 and recently signed the "Multilateral Convention on Mutual Administrative Assistance in Tax Matters" on 3 June 2020, which will likely lead to stricter documentation requirements.

Vietnam enhances its focus on transfer pricing by introducing the new "Law on Tax Administrations" and thereby changing existing regulations on the deduction of loan interest costs - alongside other TP-related innovations.

If you have any questions regarding any aspects of this newsletter, our Global Transfer Pricing experts will be happy to answer them.

Yours sincerely,

WTS Global Transfer Pricing Team

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France

Impact of the crisis on transfer prices

Postponement of the annual filing of the transfer pricing policy

Companies exceeding given turnover thresholds, or belonging to the same multinational enterprise ("MNE"), must electronically apply a special file that consists of a simplified and recapitulative version of the standard transfer pricing ("TP") documentation (Master file ("MF") and Local file ("LF")).

In principle, this tax return filing must be sent to the French tax authorities within 6 months after the filing of the corporate income tax ("CIT") return.

However, to take into account the postponement of the deadline for filing the tax return for companies facing difficulties due to the health crisis, the French tax authorities have specified that this filing may exceptionally be filed at the latest 31 December 2020 (for the financial year ending 31 December 2019).

COVID-19: amendments to 2020 Master and Local Files

The economic impact of the health crisis involves fairly significant changes in the implementation of the transfer pricing policies of MNEs. The documentation must be adapted accordingly to justify these changes in the event of a tax audit.

Consolidated profits could decrease in 2020 and in the coming years for some industries, and such a decrease could also be observed in the independent companies' results that are used as a comparable to test the arm's length nature of intra-group transactions.

So as to determine the remuneration to be allocated to intra-group entities, and in application of the transactional net margin method, groups carry out research of independent comparable companies (benchmark studies) in order to determine the arm's length margin ranges. However, this research is necessarily based on the use of historical financial data since there is a time lag between the time the accounts are approved and the availability of this information. As a matter of fact, the tested party will measure the controlled transactions made in the financial years ("FYs") affected by COVID-19, comparing with results of selected comparables, but scored in the pre-COVID-19 periods. Such objective discrepancy gives rise to the question as to whether or not the traditional comparability practices are still applicable for 2020.

It is a matter of fact that MNEs will need treasury to re-load their activities. In the framework of Base Erosion and Profit Shifting ("BEPS") Action 4, France introduced limits to the deductions of interest. Interest accrued by a French corporation in relation with borrowings from its direct shareholders may be deducted only if the interest rate does not exceed the average interest rate on loans with an initial duration of more than two years granted by banks to French companies or a higher rate if it can be demonstrated that this rate would be at arm's length. The figure as at 20 May 2020 is 1.31%.

Effective 1 January 2019, in line with the implementation of the ATAD 1 rules, interest deduction is further limited.

With effect from 1 January 2019, interest deduction is generally limited to EUR 3 million or 30% of adjusted taxable profits. Where a company is thin-capitalised (i.e. the company has a

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debt-to-equity ratio exceeding 1.5/1), these limits are reduced to EUR 1 million or 10% of adjusted taxable profits (article 212 bis of the CGI).

Also, interest deduction limitation rules have been deemed to be unsustainable in macro crisis periods. COVID-19 is going to hit MNE also below the earnings before interest and tax ("EBIT") line, indeed:

- Enterprises scoring operating losses or small operating profits can bear lower interest expenses. Such limitation is in contradiction with the companies' need for additional liquidity to reload their operations.
- Increasing debts and equities eroded by losses will affect the debt equity ratios generating additional not-deductible interest in those countries with D/E deduction rules.
- Downsizing of turnover, margin and profits as well as an increase of D/E ratios could determine a worsening of the credit rating, and an additional interest burden as well as the application of the default conditions in main financing agreements.

Action must be taken now!

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Germany

Suggested draft law on IC financing: typification of the arm's length principle also applicable to domestic transactions? – A comparison of tax consequences in cross-border and domestic cases

On 11 December 2019, the German Draft Ministerial Bill on the implementation of the Anti-Tax Avoidance Directive ("ATAD", together the "Draft Ministerial Bill") was released, suggesting national regulations on cross-border IC financing transactions as part of a new § 1a of the Foreign Tax Act ("FTA", together § 1a FTA-DRAFT), with a treaty override.

§ 1a FTA-DRAFT states amongst other things that if it cannot be shown that (i) the principal payments for the entire duration of the financing relationship could have been repaid from the beginning and (ii) the financing is economically necessary and used for the purpose of the company; or if the interest rate payable by the German taxpayer for a cross-border financing relationship with a related party exceeds the interest rate at which the multinational enterprise group could be financed by third parties, then the interest expense shall be deemed to be non-deductible at the level of the IC borrower.

§ 1 FTA allows for an adjustment of income for business relations with foreign entities. At the time of the publishing of the Draft Ministerial Bill, there was no consensus at an international level on how IC financing transactions should be treated. According to the explanatory memorandum, there had been no clear guidance on the interpretation of Article 9 (1) Organisation of Economic Cooperation and Development ("OECD") Model Convention in the respective double taxation agreements for financial transactions. Specifically, the final OECD Guidance on Financial Transactions was only published in February 2020. Due to this presumed lack of guidance, the explanatory memorandum to § 1a FTA-DRAFT outlines that § 1a FTA-DRAFT contains clear instructions that apply regardless of a double taxation agreement in order to secure and make the German tax claim clear, thereby essentially introducing a treaty override.

While § 1a FTA-DRAFT aims to introduce a correction measure for instances where the German taxpayer's income was reduced by cross-border IC financing relations, the explanatory memorandum to § 1a FTA notes that the arm's length comparison for purely domestic financial relations does not differ from the one contained in § 1a FTA. In other words, the principles laid down in § 1a FTA may also be applicable for domestic cases.

The tax consequences, however, are different for purely domestic and cross-border cases as detailed in the following. For simplification purposes, it was assumed that the lender is the shareholder of the IC borrower.

In the **domestic case,** the interest expenses on the level of the German borrower qualify as a hidden profit distribution and, thus, increase the taxable income. On the level of the German lender, however, the corresponding interest income qualifies as dividend income for tax purposes, which is 95% tax-exempt. Hence, apart from the remaining 5%, a double taxation can be avoided by the corresponding adjustment on the level of the lender. Nonetheless, cash taxes may be involved, depending on the profit situation of the involved entities. Potential withholding tax on the dividend can be fully credited. In the case of a fiscal unity between lender and borrower, no adverse tax effects would occur at all.

In the **cross-border case,** the tax consequences are more severe. The interest expenses qualify as a hidden profit distribution which increases the borrower's domestic taxable income. This generally triggers German withholding tax, unless the distribution can be taken from the borrower's tax equity account or is covered by an exemption certificate. Such withholding tax may not (or only partially) be creditable or refundable. The explanatory note to § 1a FTA-DRAFT outlines that there should generally be an international unified understanding on the pricing of IC financial transactions, and apparently presupposes that such common approach would be in line with § 1a FTA-DRAFT. While the OECD Guidance on Financial Transactions, which was released in February 2020, in theory represents a consensus document among the OECD members on the pricing of financial transactions, the fact that it does constitute a consensus document inevitably allows taxpayers a certain scope of interpretation for an individually based arm's length assessment. This stands in contrast to § 1a FTA-DRAFT which provides for a typification of the arm's length principle in line with the view of the German Federal Ministry of Finance. Therefore, due to a missing corresponding correction in the country of the foreign lender, negating interest expense at the level of the German borrower as suggested in § 1a FTA-DRAFT might lead to double taxation on the level of the foreign lender in cross-border cases, which can generally only be eliminated by a mutual agreement procedure.

IC financing transactions and their arm's length nature are a frequently discussed topic in tax audits. The new Chapter X of the OECD Guidelines provides taxpayers with a set guidance. The suggested changes to German law in § 1a FTA-DRAFT are in several aspects similar to the OECD guidance. That said, they impose a certain typification of the arm's length principle for financial transactions, which might lead to instances of double taxation in cross-border cases. This typification might also be applicable to domestic transactions. Tax consequences, if any, are usually less severe in domestic than in cross-border cases. It remains to be seen how the German legislator will react with updated and final law changes on IC financial transactions.

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Hungary

Recent Hungarian developments in transfer pricing with a focus on impacts of COVID-19

Introduction

As an answer to the COVID-19 crisis, Hungarian taxpayers received four months' extension for the filing deadline of the annual corporate income tax and return and thus for the preparation of the Transfer Pricing ("TP") documentation. It means that the new filing deadline for calendar-year taxpayers is 30 September instead of 31 May. Nevertheless, it is important to emphasise that if a company decides to file the corporate income tax return before 30 September, the TP documentation becomes due too.

Allocation of losses

With a few exceptions, global corporations suffered great economic losses due to the COVID-19 crisis, which could be challenging from a TP perspective as well. Most of the companies in Hungary that are part of a group have a low risk profile, which justifies a low but stable profit allocation. If TP analyses for the past years have been describing the previously mentioned low risk scenario, it will be hard to justify significant losses in these local entities.

However, there may be some viable approach to justify less favourable financials. The best way to support the loss split model by lower-risk entities is to use existing examples of third-party behaviour in similar situations. Even without existing comparable data (which is still limited), it seems to be reasonable to say that under such extraordinary circumstances, unrelated parties would renegotiate their existing agreements. The profit-loss model can be re-evaluated based on the new analysis called DEMPE (development, enhancement, maintenance, protection and exploitation) introduced by OECD for intangibles and risks.

Financial losses can occur for various reasons. Underpinning the allocation of losses as a result of commercial, financial or operational changes increases the chance that the tax authorities would accept intercompany pricing. In this context, the following may be considered:

- Commercial reason can be the reduced customer demand or the disruption in the supply chain;
- An example for financial changes may be the increased G&A-to-sales ratio that can support the allocation of losses. Low risk entities often undertake support functions and these fixed costs usually remain constant over a short term.
- As an answer to the unforeseeable event there may be changes in the company's operating structure like in management functions.

Furthermore, it is advisable to consider information about the country's previous response to the allocation of losses in similar situations, for instance after the economic recession of 2008.

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Other challenges in the transfer pricing documentation liability

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Based on past experience, Hungarian subsidiaries of a group may face difficulties in the preparation of the master file ("MF"), where the headquarters are in a different country and the filing of the MF is not a requirement in that specific country. This is especially true, where the Hungarian subsidiary has a marginal role and therefore the headquarters are not especially interested in sharing the necessary information. Even if the headquarters prepares and sends the master file to the subsidiary, additional queries may emerge if there is a difference in filing deadlines or in terms of obligatory content; or if a translation is needed if the MF is not prepared in one of the accepted languages, namely in Hungarian, English, German or French.

Italy

The New Italian Law on International tax disputes settlement

The Legislative Decree no. 49 of 10 June 2020 (the "Decree") implementing European Union ("EU") directive no. 2017/1852 on tax dispute resolution mechanisms in the EU has been published.

The Decree came into force on 25 June 2020 and introduces new rules relating to mutual agreement procedures ("MPAs") or other tax dispute resolution procedures between the Italian tax authority and the competent Authorities of the EU Member States deriving from the interpretation and the application of the tax treaties to avoid double taxation and the Convention no. 90/436 / EEC ("EU Convention") ***relating to the elimination of double taxation in the case of transfer pricing ("TP") adjustments.*** *However, the procedures to resolve general issues relating to the interpretation and application of the abovementioned treaties and Convention are excluded from the scope of the Decree.*

The provisions of the Decree apply to MAP applications filed from 1 July 2019 on controversial issues regarding fiscal year ("FY") starting 1 January 2018 and subsequent tax periods. They trace the EU Convention, extending the scope and providing for further remedies aimed at overcoming the critical issues encountered in Italy in the operation of the EU Convention, with particular regard to the access, duration and effective conclusion of the procedure (see in this respect also Organisation of Economic Cooperation and Development *("OECD") (2020), Making Dispute Resolution More Effective – MAP Peer Review Report, Italy (Stage 2): Inclusive Framework on BEPS: Action 14).*

In particular, the Legislative Decree introduces more detailed rules on international tax dispute settlements on the transfer pricing adjustments between EU States which are discussed here below.

Under the new rules, in the case of a disagreement between the States about the preventive assessment of admissibility for the purpose of the MAP application, there is the possibility to apply to a "Consultative Commission" and request its opinion about the eligibility; in this regard, it is also foreseen that the taxpayer is empowered to file an appeal by domestic courts even in the event of refusal of access to the MAP procedure and / or failure to establish the Consultative Commission. Before this new rule, the assessment of inadmissibility of the MAP application was not challengeable under Italian domestic law.

Furthermore, as far as the result obligation of the procedure is concerned, the taxpayer, in the case of a failure to reach the agreement by the competent authorities of the Member States involved, is granted the right to take action by requesting the establishment of a "Consultative Commission", therefore the crucial step towards the arbitration phase.

It should be stressed that, thanks to the new rules, the access to the MAP is also permitted in the case of tax dispute resolution by means of alternative procedures which lead to the definitive nature of the tax involved (except for the so-called *"ravvedimento operoso"* and *"conciliazione giudiziale"*).

The access to the arbitration phase is now also granted in the case of pending domestic judgements, where, on the contrary, pursuant to art. 7, paragraph 3 of the EU Convention, the transition to the advisory commission is envisaged only if the taxpayer *"has left the deadline for submitting the appeal or has given up the appeal before a judgment has intervened".* The Decree provides for a strengthening mechanism for internal judgment' suspension which also automatically entails the suspension of tax collection. For more detail, the domestic judgement suspension can be requested at the time of the application to start the procedure, without waiting for the MAP admission by the competent Authorities, and it no longer requires a joint action of the parties, but a unilateral request by the taxpayer is permitted.

The current efforts of the Italian Legislator and Authorities, which focus on the implementation of more effective EU TP dispute resolution mechanisms, are undoubtedly welcomed. However, it seems necessary to include the associated enterprises rule (article 9(2)) through the "Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting", so as to grant a corresponding adjustment or access to MAPs with regard to the double taxation that may otherwise result from a primary TP adjustment.

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Netherlands

"To dip or not to dip, that is the question"

Suppose a Dutch MNE company **(BV)** borrows 1,000 from a bank (the **Bank Loan**) at a rate of 5% and BV's foreign parent (**Parent**) guarantees said Bank Loan (the **Guarantee**). Stand-alone, BV could have borrowed 700.

Parent's jurisdiction considers the Organisation of Economic Cooperation and Development ("OECD") Transfer Pricing ("TP") Guidelines ("OECD Guidelines") 'as law' (including the recent guidance on financial transactions). Following the OECD Guidelines,[1] the Parent delineates for tax purposes the Bank Loan into a part that relates to the BV's (a) stand-alone borrowing capacity of 700 (the **Stand-alone Part**) and (a) enhanced borrowing capacity following the Guarantee for 300 (the **Enhanced Part**). The Enhanced Part is deemed for tax purposes as a loan from the Bank to the Guarantor/Parent (**Deemed Loan 1)** and that "primary adjustment" is subsequently processed by the Parent as a "secondary transaction" in the form of a deemed equity contribution into BV (the **Deemed Contribution**). In its tax return, the Parent deducts 15 deemed interest expenses on the Deemed Loan 1.

1 OECD Guidelines par 10.161.

From a Dutch perspective, the Enhanced Part is also treated as the Deemed Loan 1. However, contrary to the OECD guidelines, Dutch tax law[2] allows the BV to process the "secondary transaction" in the form of a deemed loan from the Parent to the BV (**Deemed Loan 2**). In its tax return, the BV deducts 35 interest expenses on the Bank Loan and 15 deemed interest expenses on the Deemed Loan 2. However, the 15 deducted by the BV is not picked up at the level of the Parent as it is considered an exempt deemed dividend accruing on the Deemed Contribution into the BV.

As per the beginning of this year, one may question whether the BV's deduction of the deemed interest expenses on the Enhanced Part will be denied under the Dutch hybrid mismatch rules (i.e. ATAD II). ATAD II intends to neutralise tax benefits arising from differences between jurisdictions in the tax treatment of entities, financial instruments, permanent establishments or tax residency. Arguably, a different view on the processing of a "secondary transaction"[3] should not qualify as a 'hybrid mismatch'. Moreover, during Dutch parliamentary discussions on the implementation of ATAD II, it was mentioned that differences in tax outcomes that are solely attributable to differences in the application of transfer pricing rules are not considered to be a 'hybrid mismatch'. Instead, the Dutch government announced that undesired transfer pricing mismatches will be dealt with separately in the scope of a planned assessment of the wider application of the arm's length principle. But how about DAC6...?

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Ukraine

New proportionate TP adjustment rules introduced into Ukrainian tax law since May 2020

Ukrainian TP rules provided for a proportionate adjustment mechanism since 2013. It is defined as the right of a party in a controlled transaction to adjust its tax liabilities following a TP adjustment of the other party conducted to ensure that conditions of the transaction are at arm's length.

Yet, until recent changes, the procedure of such adjustment was not clear. Namely, the Tax Code only mentioned that the proportionate adjustment should be carried out following the procedure and on conditions set forth by the applicable Double Tax Treaty ("DTT").

Law 466-IX (in force since May 2020) introduced comprehensive changes into the Tax Code of Ukraine including the implementation of the Base Erosion and Profit Shifting ("BEPS") three-tier reporting standard. Introduction of the rules detailing the procedure of proportionate TP adjustment is one of such important changes.

The right to initiate proportionate adjustment is available to the taxpayer who receives from its counterparty in a controlled transaction the notification about accomplished TP adjustment of tax liabilities in the country of its residence. Such a right is available only in the event that Ukraine has concluded DTT with the country of the counterparty.

2 Dutch Decree, dated 22 April 2018, nr. 2018-6865, section 9.

3 According to the OECD Guidelines (in par. 4.68) a "secondary transaction" can take the form of "constructive dividends" (i.e. company benefitting shareholder), "constructive equity contributions" (i.e. shareholder benefitting company), or "constructive loans" (i.e. either).

Following such a notification, the taxpayer may apply to the tax authority informing about the intention to make a proportionate adjustment in the period or periods of the controlled transaction. The application should be accompanied with a calculation of the amount of adjustment for each period, other documents that formed the basis for the TP adjustment by the counterparty and also the TP documentation.

The tax authority has 30 workdays to consider the application and after this period adopts one of the following decisions:

- to confirm possibility of such proportionate adjustment;
- to disallow it in full or partially if it considers such adjustment to be unfounded or due to the absence of required documents. The tax authority must provide grounds for refusal;
- to initiate a TP audit of the taxpayer to study the grounds for the proportionate adjustment and to adopt one of the aforementioned decisions based on the results of such audit.

In the case that the tax authority fully or partially disallows proportionate adjustment, the taxpayer has the right to apply to the Ministry of Finance to initiate consideration of the case according to the Mutual Agreement Procedure ("MAP") according to applicable DTT.

In summary, since May 2020 Ukrainian taxpayers have the mechanism which may be followed to accomplish proportionate adjustment of its tax liabilities in the event of a TP adjustment of the counterparty in the transaction. In future it may prove to be an efficient tool for implementation of the group TP policy goals in transactions involving Ukrainian subsidiaries or to avoid double taxation triggered by one-sided TP adjustments.

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Argentina

"Argentine Transfer Pricing News - 2020 Second Trimester"

The milestone of the 2020 second trimester is certainly the enactment of the new transfer pricing regulations. On 15 May, the Argentine Revenue Service ("ARS") released the much-awaited general resolution 4717 ("GR 4717").

New Transfer Pricing Regs (GR 4717)

Here's a brief summary of the GR 4717 main aspects:

1. *Tested party:* GR 4717 provides that the tested party is the Argentine affiliate, as the general rule. However, it does allow testing all affiliated parties – even those residing outside Argentina – when the profit split method is applied.

2. *Business restructurings:* it regulates in detail the tax consequences of cross-border business restructurings within the affiliated group. The resident party is required to account an arm's length remuneration when it undertakes new risks or functions, or when it transfers a business line out of the country. In parallel, it is also required to account for an arm's length loss when the business restructuring results in the need to pay out an indemnification or a similar outlay. For benchmarking purposes, the new GR 4717 requires a consideration of the effects of civil and commercial laws, market standards and domestic case law, whenever applicable. Such economic analysis needs to be included in the annual transfer pricing ("TP")

study. Just to recap, the filing of such study is mandatory every year, as well as the need to file the Country by Country Reporting ("CbCR") (or to indicate the country where such filing is made by the Multinational Enterprise ("MNE") group) and the Master File ("MF").

3. *Definition of "intermediaries" subject to special audit:* They are defined as any foreign counterpart to the resident affiliated who does not take physical possession of the goods exported from Argentina. To prove substance of such intermediary, a detailed functional analysis is implemented by GR 4717, including the need to provide evidence as to the good standing of the intermediary in its jurisdiction of incorporation; submitting the intermediary's financial statements, as well as a certification of the margins obtained for such intermediation, which includes a detail of purchases, sales and associated costs. This type of evidence is difficult to obtain but needs to be kept filed by any resident MNE who purchases from or sells to related affiliates in the cross-border context. More cumbersomely, the new regs also require the provision of such evidence when the intermediary in not an affiliate, but it is part of a triangular transaction between related parties.

This evidence should be kept in files by the Argentine affiliate in the event of an ARS audit. Under special circumstances, if the margins obtained by the intermediary go beyond market standards, the ARS may allocate such excess to the Argentine exporter that deals with such intermediary. These issues are a complex topic of current debate, to ensure the evidence is kept while no collateral damage is triggered by the MNE group.

4. *Hydrocarbons Exports:* GR 4717 provides that such transactions could be benchmarked in view of a "marked product" (i.e. a product whose price is used for setting international prices of the underlying goods); if such standards are commonly used for pricing formulas between unrelated parties. It is not required that the exported goods match the reference values, provided this pricing methodology is proven to be consistent with the arm's length standard. For example, if the exported goods and the marked product are similar but not identical, a reliable comparability adjustment should be made.

5. *Cross-border services between related parties - Benefit Analysis:* the transfer pricing analysis should consider compliance with the ordinary and necessary tests; the parties' conduct (i.e. in compliance with the Organisation of Economic cooperation and Development's ("OECD's") "delineation of the actual transaction"); the contractual terms, as well as a benefit analysis (i.e. it should evidence that the profit or value obtained by the tested party outweighs the price paid for the service). The resolution does not allow deducting any service fee performed in the self-interest of the foreign affiliate or of any other affiliate; nor unrelated to the Argentine party's business. Cross-border services that are deemed duplicated may not be deducted too, a test that should be analysed in view of the arm's length standard, on a case-by-case basis.

6. *Associated transfer pricing compliance burdens:* these burdens are all fully amended, including cumbersome reporting and documentation rules concerning cross-border, unrelated-party transactions with commodities. Related party transactions are also burdensome regulated with new, detailed, transfer pricing studies and associated filing forms (F. 2668). A special Country by Country ("CbC") filing is required from any local party that is a member of an MNE group. In addition, the MF should be filed mandatorily, within twelve months after closing the financial statements of the Argentine affiliate.

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Chile

Revision of formal obligations: what to expect.

The last time Chilean Transfer Pricing ("TP") regime was updated was in September 2019. In said opportunity, the modifications were aimed at aligning formal obligations such as the F1907 (transactions with related parties) and F1937 (CbCR). Later in February 2020, just before the COVID-19 outbreak worldwide, a modernised Income Tax Law and Tax Code (its art. 64 provides specific case examples for appraising and adjusting prices in transactions within an enterprise group in Chile) was finally published. Although minor changes in TP issues were introduced, they added pressure to taxpayers and to the Internal Revenue Service itself. But are these the implementations that we expect and need?

With the F1907, Chilean taxpayers are complying to disclose their related parties and operations performed during the previous fiscal year; and with the F1937, economic group information exchange standards are being met successfully.

We certainly expect practical modifications in accordance with the current and future post-COVID-19 scenario, for example:

- Benchmarking and TP analysis; we expect more details about discerning the effects of an economic crisis between companies, industries, or markets; the reduced probability of finding appropriate comparables that have experienced financial distress (e.g. bankruptcy or operating losses). Hence, in the F1907 it would be good to include the interquartile range of comparable companies and the suggested adjustments.
- Pricing financial transactions (cash pooling, related parties' loans, credit rating, guarantees); the economic downturn will lead Multinational Enterprises ("MNEs") to reassess their existing intercompany ("IC") financing agreements. We would expect from the Internal Revenue Service explicit guidelines to search the unit of criteria regarding adjustments in the agreed conditions: SBIF/CMF[1] information would be useful for TP purposes? Only a credit rating approach would lead to the best outcome when determining the arm's length interest rate?
- Allocation of legitimate losses and business restructurings (shutting down or scaling back their operations due to the pandemic); we would expect a solid guidance on the termination or substantial renegotiation of IC agreements (mainly intangibles and services).
- Submission of the TP study (local file ("LF")) following the regional trend. We would expect that serves to standardise criteria for documentation and audits.
- Standardisation of complementary analysis such as Benefit Test in the LF and/or F1907.

Clearly, the Chilean TP landscape has been broadening in recent years. It is worth mentioning that this has happened not only regarding cross-border transactions, but also for domestic transactions within the economic group. We hope that the present circumstances serve to include these elements and can provide greater certainty for the Internal Revenue Service and elements of defence for taxpayers with regard to audits.

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1 The banking regulator (SBIF) joined the Commission for the Financial Market (CMF) in 2019, as provided in the amendment to the Banking Law. The CMF is the government agency that oversees the entities and activities involved in the securities markets and insurance in Chile.

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Nigeria

Applicable TP Methods in Nigeria – Analysing prime plastichem Nigeria limited V federal inland revenue services

Introduction

Nigeria's Tax Appeal Tribunal ("TAT") recently adjudged its first Transfer Pricing ("TP") case, ***Prime Plastichem Nigeria Limited v. Federal Inland Revenue Service (Appeal No: TAT/LZ/CIT/015/2017).*** TAT had to determine the appropriate TP method and Profit level indicator ("PLI") best applied in the TP documentation for 2013 and 2014 of Prime Plastichem Nigeria Limited ("PPNL's"/Appellant). The Federal Inland Revenue Service ("FIRS"/Respondent) assessed PPNL's TP returns using the TNMM with a Gross Product Margin ("GPM") PLI for the 2013 and 2014 TP returns. TAT ruled in favour of the FIRS.

Examining TP methods in line with decision of the TAT

In the above case, the PPNL applied the CUP method in 2013 and then applied a different method in 2014 (Transnational Net Margin Method – "TNMM") with an earnings before interest and taxes ("EBIT"). A guiding precept for TP transactions as recommended by both the UN and OECD is that TP methods in transactions involving same parties (which was the case here) should maintain a uniformity except where there is a compelling reason to change the TP method.

In this case, the change to the TNMM questioned the validity of both methods applied in 2013 and 2014. This inconsistency is likely the trigger for the tax authority's assessment on the TP returns for PPNL in both years.

Furthermore, the FIRS adopted the GPM as the applicable PLI for the use of the TNMM method. This position is considered inconsistent with the relevant TP Guidelines. The GPM does not compare net profitability. It should be noted that the GPM is best suited when parties to a transaction are adopting the Resale Price Method ("RPM"). Thus, the FIRS erred in its use of the GPM as the appropriate PLI for the TNMM. Also of importance is why neither of the parties adopted the RPM which is suitable where the purchasing party involved is buying with intention to resell to third parties and, as in this case, PPNL was buying to resell to the Nigerian market.

The decision leaves a lot to be desired and requires an appeal.

Conclusion

The case reveals the need for taxpayers to ensure that the benchmarking study reveals which TP method is most suitable to be applied, bearing in mind the availability of reliable and sufficient information to support a choice.

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Pakistan

Transfer Pricing Audit

Pakistan has introduced amendments in the Income Tax Ordinance, 2001 – the "Tax Ordinance" for conducting transfer pricing audits of multinational enterprises ("MNEs"). These amendments have been made in section 230E of the Tax Ordinance through Finance Supplementary (Second Amendment) Ordinance, 2019 and Tax Laws Amendment Act, 2020, thus shifting the focus to examining Transfer Pricing ("TP") of MNEs – a historically overlooked area of the taxation sphere in Pakistan.

Amendments in the Transfer Pricing Audit Regime

The recent amendments relate to the procedure for conducting TP audits by the Tax Authorities. The responsibility to conduct TP audits lies with the Directorate General of International Tax Operations ("DGITO") introduced in 2019. However, due to the absence of a clear procedure for carrying out TP audits, ambiguity surrounded the Tax Authorities and Taxpayers. According to recent amendments, TP audits will be conducted in accordance with section 177 of the Tax Ordinance – the existing audit provision for conducting an audit of the affairs of a taxpayer by calling records and other information is not limited to books of accounts. While TP audits will be governed by the section 177 framework, the following powers of the Commissioner Inland Revenue provided under section 177 shall not apply to audits:

- Power to amend the assessment under section 122 of the Tax Ordinance after issuance of Audit Report.
- Power to make the best judgement assessment under section 121 of the Tax Ordinance, in the event that no information is provided by the Taxpayer.
- Power to treat the return or revised return filed by the taxpayer as of no legal effect, if no information is provided during the audit procedures.

It has also been clarified that Commissioner Inland Revenue is empowered to determine the TP of the transactions at arm's length between the associates while conducting the Audit of the Income Tax affairs of the Taxpayer under section 177, section 214C (random ballot based audits) or during the proceedings for the amendments in assessment under section 122 of the Tax Ordinance. The Transfer Price audit is an independent Audit as compared to Audit of Income Tax affairs of the Taxpayer and refers to the audit for determination of Transfer Price at arm's length in the transactions between associates.

In conclusion, the following TP audit process has transpired from recent amendments:

- Federal Board of Revenue will notify the criteria for selection of taxpayers for TP audit in the Official Gazette.
- Directorate General of International Tax Operations will conduct the TP audit and issue Audit Report.
- Assessment proceedings on the basis of the Audit Report shall remain within the jurisdiction of Commissioner Inland Revenue having jurisdiction over the Taxpayer normally.

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Taiwan

One-time Transfer Pricing adjustment in Taiwan

To manage the Transfer Pricing ("TP") risk, MNEs would develop a global TP policy to determine how assets and risks are remunerated, via price or margin, among associated enterprises. In practice, however, many unexpected market conditions cause the actual transaction to deviate from the target results of the TP policy, where TP adjustments may therefore be required. To resolve the conflicts at an early stage, taxpayer-initiated adjustments are accepted by some countries for tax purposes.

Taiwan has a procedure which allows taxpayers to initiate TP adjustments, called the "One-Time TP Adjustment." On 15 November 2019, Taiwan's Ministry of Finance ("MOF") released a new tax ruling (Tai Tsai Shui No. 10804629000) which reduced limitations on one-off TP adjustments. Beginning in 2020, enterprises can make such adjustments before the year-end if four requirements are met:

1. Transaction terms and all price-relevant factors have been concluded in a prior bilateral agreement.
2. The adjusted accounts (A/R & A/P) have been recorded for financial accounting purposes.
3. The counterparty in the controlled transactions make corresponding adjustments at the same time.
4. All taxes associated with the one-time adjustments are paid.

Importation of tangible goods

For companies who have imported goods from related parties and would like to adopt the above procedure, the compliance requirements can be divided into three phases: 1) upon importation before the end of the FY ("FY"); 2) submitting the one-time TP adjustment application; and 3) customs value assessment and finalisation process.[1]

1. The first step is to indicate in the import declaration form, "Making a one-time adjustment for FY XXXX" and attaching a proforma invoice and customs value declaration form based on a tentative price at the time of importation. A deposit will be made to customs at this stage and then reconciled when the price is finalised.
2. The final step is to prepare an application for the assessment and finalisation of the customs value according to the Customs Act within one month after the end of the FY. The taxpayer will know whether they need to pay in addition to the deposit or ask for a refund from customs.

Other Types of Controlled Transactions

For other types of controlled transactions like import of service and export of goods or services, declaration letters of one-time TP adjustments and other supporting documents are required to be submitted to tax authorities for tax filing purposes.

1 Guidelines on assessing the one-time TP adjustment to determine the customs value (the "Guidelines") on 31 December 2019

Ongoing Documentation

The one-time TP adjustment provides enterprises a feasible mechanism to achieve an arm's-length result when unexpected market conditions (e.g. COVID-19) cause transaction results deviating from the target of their TP policies. Because supporting documents are required to adopt a one-time TP adjustment, it is crucial for the taxpayers to review their intercompany pricing for intercompany transactions contemporaneously. The COVID-19 crisis highlights the importance of thorough TP documentation. The creation of documentation is an ongoing process, so it is advisable for companies to start preparing their documentation ASAP.

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Thailand

Transfer Pricing Update

By joining the Inclusive Framework on Base Erosion and Profit Shifting on 2 June 2017, Thailand committed itself to the implementation of the BEPS minimum standards.

As a consequence, the Act Amending the Revenue Code on Transfer Pricing ("TP") was announced on 18 November 2018 and came into effect on 1 January 2019, requiring any company with annual revenue of over THB 200 million (~ USD 6.5 million) to submit a TP disclosure form together with its annual tax return and to prepare the underlying TP documentation.

The usual due date is within 5 months after the fiscal year end (i.e. normally 31 May, unless the company uses a deviating Fiscal Year ("FY")), but the deadline for the 2019 tax return has been extended until 31 August 2020 to alleviate the impact of the COVID-19 pandemic.

Companies that reach the above-mentioned threshold of annual revenue of over THB 200 million and are thus required to submit a TP disclosure form should take note that Thailand signed the Multilateral Convention on Mutual Administrative Assistance in Tax Matters on 3 June 2020, becoming its 137th signatory.

Once ratified, Thailand must legislate, implement, and follow the automatic exchange of information requirements known as the Common Reporting Standard and Country-by Country-Reporting ("CbCR"), which requires the automatic exchange and reporting of certain taxpayer information to other countries' revenue departments.

Companies should therefore implement procedures to strictly comply with their tax obligations, including the preparation of a comprehensive transfer pricing documentation. As a member of the international community, Thailand will need to enforce all its obligations under multilateral treaties to avoid being blacklisted. In addition, the impact of the COVID-19 pandemic on the Thai tourism industry and economy as a whole will force the Thai authorities to increase their scrutiny on taxpayers to boost fiscal earnings.

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Vietnam

The impact of the new Law on Tax Administration on Transfer Pricing

The new Law on Tax Administration ("***LTA***"), effective from 1 July 2020, strengthens the tax enforcement in Vietnam. Regulations on Transfer Pricing ("***TP***") and the basic principles on viewing related-party transactions for the first time are included in a law. Previously, TP regulations were to be found in guiding documents linked to the laws, namely Decree 20, Circular 41. Some essential innovations in the LTA include:

- *The declaration of related-party transactions (TP declaration form)* are made a mandatory component of the Annual Tax finalisation. All enterprises must complete and file this form when filing the CIT finalisation.
- *The principles for declaring and determining taxable prices in related-party transactions (TP)* are reiterated, including independent transactions comparison, substance-of-operation rules, advance-pricing-agreement ("***APA***") regime. The new law clarifies that APAs must be approved by the Ministry of Finance prior to their application.
- *Incentives for small-sized taxpayers with low tax risks* are made through simplified procedures for declaration and the determination of related-parties transaction prices.

According to the draft of the new guiding decree following the LTA's implementation, Vietnam tax authorities will enhance the exchange of information with foreign tax authorities regarding related-party transactions in accordance with international tax agreements. The taxpayers´ obligation to provide information in that context will be reduced. Specifically, the tax authority will automatically exchange information in the event that the parent company of the taxpayer registered in a foreign country is required to submit a Country-by-Country Report ("***CbCR***") in that country of residence.

Change in deductible loan interest cost

On 24 June 2020, the Government has issued Decree No. 68/2020 amending and supplementing Article 8.3 of Decree 20 on the deductible loan interest cost. This took effect immediately and is applied retrospectively for the tax year 2019, in certain cases for the tax years 2017 and 2018 and onwards. The main amendments are:

- The cap on loan interest cost deduction is increased from 20% to 30% of the earnings before interest, tax, depreciation and amortisation ("***EBITDA***"). The taxpayer may carry forward the non-deductible interest expenses in excess of the 30% cap for a maximum of 5 years.
- Certain types of financing are now excluded from the cap, including official development assistance loans, various concessional loans made by the government, and loans made for implementing national programmes and state social benefit policies.
- For amending the Corporate Income Tax ("CIT") finalisation of the tax years 2017 and 2018, the taxpayer must submit the supplement 2017 and 2018 for CIT returns by 1 January 2021 to apply the new cap. The overpaid amount will be offset against the payable CIT in 2020 and carried forward up to 5 years from 2020.

The new LTA must be viewed in the context of the declared intention of the tax authorities to enforce tax compliance and increase tax revenue. Because not so few foreign invested companies are continuously declaring a loss but continue operations, they are in the focus of future tax audits. The tax audits in these cases will very likely focus on TP issues. It is highly recommended to conduct a TP health check within 2020.

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Glossary

APA	Advance Pricing Agreement
ARS	Argentine Revenue Service
ATAD	Anti-Tax Avoidance Directive
BEPS	Base Erosion and Profit Shifting
CbC	Country by Country
CbCR	Country by Country Reporting
CIT	Corporate Income Tax
CUP	Comparable Uncontrolled Price (Method)
DEMPE	Development, Enhanceme, Maintenance, Protection and Exploitation
DTT	Double Tax Treaty
EBIT	Earnings before Interest and Taxes
EBITDA	Earnings before interest, tax, depreciation and amortisation
EU	European Union
FTA	German Foreign Tax Act (AStG)
FY	Fiscal Year
GPM	Gross Profit Margin
IC	Intercompany
IP	Intellectual Property
LF	Local File
LTA	Vietnam Law on Tax Administration
MAP	Mutual Agreement Procedure
MF	Master File
MNE	Multinational Enterprise
OECD	Organization of Economic Cooperation and Development
OECD Guidelines	OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations
OECD MTC	Model Tax Convention on Income and on Capital
PE	Permanent Establishment
PLI	Profit Level Indicator
RPM	Resale Price Method
TAT	Tax Appeal Tribunal
TNMM	Transactional Net Margin Method
TP	Transfer Pricing
VAT	Value Added Tax

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