December 2012: Ukraine

Related-party transactions, green tariff, tax rates.

- Parliament withdrew the draft law on transfer pricing.
- Application of the ‘green tariff’ will begin 1 April 2013.
- All companies must amend their registered documents according to the new economic activity classifications by the end of 2012.
- Rates for certain taxes are to increase.
- Excise tax is imposed on sales of securities and derivatives.
- Tax authorities clarified the procedure for application of penalties to unified taxpayers.

December 2012: Serbia

Definitions and rules that apply for transfer pricing purposes have been revised, generally to reflect provisions contained in the OECD transfer pricing guidelines.

The revised definitions are included in a law passed by the Serbian Parliament on 15 December 2012, and the law was published in the official gazette (no. 119/2012, dated 17 December 2012). The following provides an overview of the revised transfer pricing definitions.

Related party
A related party is considered to be a private individual or a legal entity that directly or indirectly holds at least 25% of shares or a stake (thereby enabling control over the taxpayer) or that holds at least 25% of voting rights in the taxpayer’s managing bodies (ie, significant control over decision making). Parties related to the taxpayer may also include every non-resident entity from a jurisdiction with a preferential tax system.

Thin capitalisation
Besides banks, the debt to equity ratio of 10:1 also applies to financial leasing companies.

Transfer pricing documentation
The taxpayer is required to submit documentation of transactions with related parties at prices that would have been realized on the open market, had they not involved a related party (ie, the arm’s length principle), when a uniform approach can be applied to a large number of individual transactions or a separate approach, in the case of complex transactions.

If the transfer price differs from the arm’s length price, the taxpayer is required to declare in the tax base:

- The amount of the positive difference between the arm’s length income and the transfer price income
- The amount of the positive difference between the transfer price transaction costs and arm’s length transaction costs

If the arm’s length price is specified as a range, and the value of the transfer price is within such range, it is deemed that there is no difference between the two prices.

If the value of the transfer price is outside of such range, the arm’s length price is equal to the median value of the specified range.

The taxpayer is also required to declare separately in the tax balance any interest on deposits, loans and borrowings involving related-party
transactions (up to the level specified by thin capitalization rules).

The Minister of Finance can specify instance for which it is possible to reduce amounts that are declared in the tax base, when such reduction can be used only in cases involving the application of double taxation avoidance treaties.

Arm’s length pricing methods
In addition to the comparable uncontrolled price method, the cost-plus method (increased for gross margin) and the resale price method (in accordance with the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations), the following additional methods for determining the arm’s length price have been introduced:

- Transactional net margin method
- Profit split method
- Any other method, if shown that any of the above methods cannot be applied

In determining the price, the method used is the method that corresponds best to the particulars of the case when the use of several methods is permitted.

Only the effects of the difference between the transfer price and the market price are declared in the tax balance as an increase in the tax base.

The Minister of Finance and Economy is to provide guidance that will specify separately the contents of required transfer pricing documents, relying on the OECD guidelines.

In the event of incomplete or partially complete documentation, the Serbian tax authority will issue a warning to the taxpayer with instructions to provide the requisite documentation within a period that cannot be shorter than 30 days or longer than 90 days, as of the date of issue of such warning.

Arm’s length interest rate
The Finance Minister can specify arm’s length interest rates on deposits, loans and borrowings between related parties. Instead of such interest rates, the taxpayer is entitled to apply arm’s length transfer pricing methods to all loans and borrowing involving related parties.

December 2012: BIAC
FATCA – the Foreign Account Tax Compliance Act – presents business with unique challenges and an opportunity to find global solutions to a single country’s broadly applicable tax legislation. The Business and Industry Advisory Committee (‘BIAC’) to the Organisation for Economic Co-Operation and Development is leading the business effort to engage with governments in a mutually beneficial dialogue. The OECD is playing a key role in facilitating these discussions.

Keith Lawson, Chair of the FATCA Business Advisory Group organized by the Business and Industry Advisory Committee to the OECD writes in the December edition of World Commerce Review.

December 2012: Czech Republic
The General Financial Directorate (Generální finanční ředitelství (GFŘ)) posted on its website GFŘ Instruction No. D-10 concerning low value
adding services provided between related parties/associated enterprises. The GFŘ instruction is effective 1 January 2013.

According to the GFŘ, the aims of the instruction are:

- To provide for uniform application of the transfer pricing rules in evaluating services with a low value adding factor
- To reduce administrative demands on taxpayers when supporting the correctness of transfer prices set for these services
- Low value adding services

Low value adding services are those that do not comprise the principal business of the entities, that involve routine functions, and that do not constitute a substantial cost or revenue for the parties involved.

Under the GFŘ instruction, these services must not exceed 10% of the provider’s turnover, or 20% of the recipient’s operating expenses and, at the same time, are not to exceed CZK 50 million. These include, for instance, services of an administrative, technical, financial, consulting or commercial nature which serve the group of enterprises to support their main business activity.

**December 2012: Sweden**

The Administrative Court of Appeal found that the Swedish tax agency had failed to satisfy its burden of proof in not showing that the agreed-to rate of interest on a loan from a foreign parent company to a Swedish subsidiary was not at arm’s length.

This is the second court decision in recent years concerning arm’s length interest on intercompany loans. In June 2010, the Supreme Administrative Court rendered its judgment in a case in which both lender and borrower were members of the same group of companies, finding that this relationship would influence a determination of what is the arm’s length rate of interest.

In that case, the court found that the credit risk was lower than would have been the situation if the parties had been unrelated. As a consequence, the interest paid on the shareholder loans was not fully deductible.

**Interest on loan from foreign parent company to Swedish subsidiary**

In the instant case, originally two loans were the subject of the dispute:

- One between a Swedish subsidiary and its foreign parent company
- The other between the subsidiary and a minority shareholder in the subsidiary

The Swedish tax agency asserted that the 2010 decision applied in this case for purposes of determining arm’s length interest rates in cross-border situations, and that the arm’s length interest rate was 8% for both loans.

The lower court agreed with the Swedish tax agency’s posi-
tion concerning the shareholder loan, but found that the tax agency had not met its burden of proof regarding the loan from the minority shareholder.

The company appealed, and the Swedish Administrative Court of Appeal concluded that the Swedish tax agency had failed to meet its burden of proof and that there were no grounds for a tax adjustment.

**December 2012: Ukraine**

The Parliament of Ukraine ‘registered’ a draft law containing new transfer pricing rules, and then posted the draft law on its website.

Among the changes concerning the transfer pricing rules of Ukraine are measures providing:

- Lists of controlled transactions (ie, transactions between related parties, or with respect to low-tax jurisdictions)
- Transfer pricing methods and their application
- Rules for determining the arm’s length price/range
- Transfer pricing documentation requirements

**December 2012: Canada**

The Canada Revenue Agency (CRA) updated its administrative positions on referrals to its Transfer Pricing Review Committee and its use of the OECD Guidelines when performing transfer pricing audits.

These positions are now reflected in two new transfer pricing memoranda (TPM) published at the end of October 2012:

- TPM-13, Referrals to the Transfer Pricing Review Committee
- TPM-14, 2010 Update of the OECD Transfer Pricing Guidelines
- TPM-13 - Referrals to the Transfer Pricing Review Committee
- The CRA’s Transfer Pricing Review Committee (TPRC) must approve the application of transfer pricing penalties and reassessments based on Canada’s “recharacterization” provisions.

TPM-13, which replaces TPM-07 (August 2005), discusses the specific referral procedures that taxpayers and the CRA must follow when either potential recharacterization or penalties may apply.

- Recharacterizations - a recharacterization assessment arises when the CRA finds that a related-party transaction would not have been undertaken by parties dealing at arm’s length. The CRA’s assessment is based on its view of the way arm’s length parties would have structured the commercial arrangement. These assessments must be approved by the TPRC.

TPM-13 generally revises the communication process between the auditor and the TPRC to determine and assess a recharacterization proposal. TPM-13 clarifies that, if the initial referral to the TPRC is approved, the auditor must then carry out an in-depth examination to determine whether the facts support recharacterization.

- Transfer pricing penalties - the CRA may assess transfer pricing penalties on an adjustment to income or capital that exceeds the lesser of $5 million or 10% of the taxpayer’s gross revenue. If the TPRC finds that
the taxpayer did not make reasonable efforts to determine and use arm’s length transfer prices for a given transaction, a transfer pricing penalty is assessed at 10% of the adjustment to income or capital.

The CRA generally provides a draft of its penalty referral report to the taxpayer at the proposal letter stage, so that the taxpayer can make its own representations to the TPRC.

TPM-13 now clarifies that the CRA auditor will submit the taxpayer's representations, along with the penalty referral report, to the TPRC.

December 2012: Mexico

Miscellaneous Rule I.3.8.3 (published in the Mexican official gazette in November 2012) includes a provision that Mexican taxpayers are not required to comply with the obligation of preparing a transfer pricing documentation report supporting the arm's length nature of domestic intercompany transactions to the extent that their annual gross receipts the previous tax year did not exceed MX $13 million or, in the case of taxpayers providing professional services, their gross receipts did not exceed MX $3 million.

Tax agreements
Mexico has signed income tax treaties/agreements with Samoa, Belize, Costa Rica, and Bahrain.

Transfer pricing documentation
New rules allow taxpayers to opt out of the transfer pricing documentation requirement if the transactions are conducted at arm’s length prices between related parties and residents of Mexico whose income for the preceding year does not exceed 13 million pesos (approximately US $1.01 million) and for taxpayers providing professional services whose income for the preceding year does not exceed 3 million pesos.

December 2012: Mexico

The fourth amendment to the tax law for 2012 includes a list of new tax treaties or agreements, measures concerning transfer pricing documentation rules, and other measures. The amendment (Cuarta Resolución de Modificaciones a la Resolución Miscelánea Fiscal para 2012) was published on 12 November 2012 in the official gazette (Diario Oficial de la Federación).

December 2012: Ireland

Guidelines for monitoring compliance with transfer pricing law. According to the guidelines (26 November 2012), the primary mechanism for monitoring Ireland’s transfer pricing regime will be the Transfer Pricing Compliance Review (TPCR) program. In general:

- A TPCR is a self-review conducted by a company or group of compliance with the Irish transfer pricing law.
- The review’s goal is to determine whether the arm’s length principle has been correctly applied in
relation to relevant trading transactions between associated persons.

- Companies will be notified by letter from Revenue if they have been selected for a TPCR.
- The initial focus of the TPCR program will be certain cases selected across a range of large companies.
- Any company notified that it has been selected for a TPCR will have three months to provide Revenue with a copy of a report that addresses each of a number of issues.

Irish Revenue announced that in situations when a transfer pricing report or study already exists in order to satisfy transfer pricing obligations in another country, that report or study will suffice for the TPCR provided it addresses the issues to be reported to Revenue.

Irish Revenue also listed conditions that a company must satisfy if it wishes to rely on the grandfathering provision to exclude transactions, the terms of which were agreed before 1 July 2010, from the scope of the Irish transfer pricing rules.

### November 2012: Indonesia

Potential changes to transfer pricing regulations. Officials from the Directorate General of Taxation informally presented proposals for future changes to the transfer pricing regulations. These would include:

- An expanded definition of ‘related party’
- Increases to the thresholds of controlled transaction amounts subject to the transfer pricing regulations
- Amendments relating to the domestic related-party transaction requirements
- Separate vs. combined transactions approaches – i.e. the arm’s length principle would apply on a transaction-by-transaction basis except when transactions are so closely linked or continuous that they cannot be evaluated adequately on a separate basis
- New segment financial information requirements
- Measures for determining the arm’s length nature of intellectual property transfers
- New contract manufacturer and commodity exporter focus
- The ‘most appropriate method’ approach, with the CUP method always preferable whenever possible

No significant changes are expected in relation to the documentation requirements.

Other proposed measures would concern Mutual Agreement Procedure (MAP) revisions and Advance Pricing Agreement rules.

### November 2012: Australia

The Australian Assistant Treasurer released an exposure draft of legislation - Tax Laws Amendment (Cross-Border Transfer Pricing) Bill 2013: Modernisation of transfer pricing rules - proposing changes to Australia’s domestic transfer pricing rules.

The new rules, rather than focusing on an arm’s length price, look at cross-border ‘conditions.’ The rules would seek to provide that the amount brought to tax in Australia from those conditions would not be less than it would be if those conditions reflected the arm’s length contribution made by Australian operations through functions performed, assets used, and risks assumed.

The exposure draft arises out of the Treasury Consultation Paper Income Tax: cross border profit allocation: Review of transfer pricing rules (1 November 2011) that highlighted a range of issues with Australia’s
transfer pricing rules following judicial opinion in recent transfer pricing cases.

The exposure draft legislation also is shortly after the introduction of the new Subdivision 815-A of the *Income Tax Assessment Act 1997* (ITAA 1997), which became law on 8 September 2012 and introduced retroactive amendments to the law in relation to the transfer pricing rules that apply to treaty cases in income years commencing on or after 1 July 2004.

**November 2012: France**

The third draft legislation to amend the tax law (*Projet de loi de finances rectificative pour 2012*) was presented 14 November 2012 to the Assemblée nationale. The draft bill includes exit tax provisions that may have transfer pricing implications.

Also, draft legislative measures would expand the authority for tax-related searches and seizures conducted by the French tax authorities in matters involving cross-border transactions of multinational entities.

**Exit tax measure**

Article 16 of the draft bill clarifies the application of section 221 of the French tax law (*Code général des impôts* - CGI). CGI section 221 contains provisions concerning the tax consequences when a head office is moved from France to another country, upon termination of a business. In general, the interplay of CGI sections 221 and 201 requires the immediate determination of the amount of income tax that would payable on unrealized (latent) gains and on revenues not previously taxed. However, section 221 specifically excludes from such taxation the transfer of a head office from France to another EU member state (except if such transfer also includes the transfer of the head office’s underlying capital assets).

Section 16 of the draft bill would amend CGI section 221 to reflect two recent judgments of the Court of Justice of the European Union (CJEU). The CJEU held that Portuguese and Dutch law measures providing for the immediate taxation of unrealized (latent) gains on capital assets concurrent with the transfer of a head office from the country was not a ‘proportionate restriction’ on EU treaty principles.

Section 16 of the draft bill would provide for payment of tax on the unrealized (latent) gains over a period of five years following the transfer of the head office to another EU member state or member country of the European Economic Area (EEA) having an income tax treaty with France that contains a mutual assistance clause. If there were to be a subsequent sale or transfer of the assets outside of the EU or the EEA before the expiration of the five-year period, the balance of the amount of income tax related to the unrealized (latent) gains would be immediately payable.

The proposed legislation also would extend these rules to the transfer of a permanent establishment.

**Tax-related searches and seizures**

A proposed legislative provision reflects an increased focus on cross-border transactions of French subsidiaries of multinational companies. The French government proposed an amendment to article L 16 B of the French tax procedure code dealing with tax-related searches and seizures.

The draft legislative version of article L 16 B would authorize the French tax authorities to conduct a search-and-seizure operation and look for evidence of tax evasion wherever relevant documents may be stored including data on servers.
According to the draft legislative provision, the French tax authorities would be authorized to seize data supports (e.g., servers) without affording the taxpayer an opportunity to contest and refuse such seizures.

November 2012: Russia

Transfer pricing adjustments before year-end. Taxpayers may need to take additional actions in 2012 to reduce their transfer pricing risks.

Profit-level indicator
Often, the chosen profit-level indicator and the actual profit at year-end can significantly differ from the ‘target’ or arm’s length profit-level-indicator range identified during the benchmarking study (that is, profit may be too high or too low).

Missing the target profit range could result in negative consequences for Russian companies and their related foreign counterparties, including these risks:

- Profit tax and value added tax (VAT) from a transfer pricing audit (if the Russian tax authorities consider the taxpayer’s revenues as being understated or the costs as overstated)
- Customs risks from adjustment of import prices (if the Russian customs authorities consider them to be overstated) and even a ‘slowdown’ or blocking of Customs’ clearance of goods
- Unrecoverable Russian VAT (resulting from some of the tools used to adjust profit to fit within the target profit-level-indicator range)
- Tax risks for foreign counterparties (resulting from non-compliance with the transfer pricing rules or with an advance price agreement (APA) of a foreign jurisdiction)
- Unavailability of correlative adjustments in situations of additional tax assessments

Methods for adjusting actual 2012 profits
If any of the above risks appear to apply for 2012, there may be a need to identify appropriate methods for adjusting actual 2012 profits, so as to:

- Bring the profit-level indicator into the target range under the chosen transfer pricing method
- Reduce collateral tax risks (as noted above)
- Be acceptable for the foreign counterparty from a tax and legal viewpoint
- Be feasible for implementation before closing the 2012 financial year

November 2012: France

Related-party’s use of domain name requires arm’s-length compensation. A French court held that the exclusive right to use an internet domain name entails the recognition of an intangible fixed asset, for which arm’s length compensation must be paid if used by a related party.

The Tribunal administrative de Montreuil - in a recently released decision - concluded that the French taxpayer must be regarded as having made an indirect transfer of profits abroad within the meaning of Article 57 of the French tax law because it held the exclusive right to use the internet domain name and made this right available to its Swiss parent company without receiving any compensation beyond the reimbursement of registration and renewal fees for the domain name. 9 February 2012, no. 1000897, eBay France TA Montreuil, 1st Chamber

Background
The taxpayer (eBay France) is a French company incorporated in 2000 and 99%-owned by a Swiss company (eBay International AG), itself a subsidiary of the eBay group.
The French entity provides marketing and sales support services for the benefit of the Swiss entity; it is also the registered owner of the internet domain name ‘ebay.fr’ since its acquisition and merger, in 2001, of the previous owner of that domain name, a French third party.

After that acquisition and merger, eBay France became the registered owner of the internet domain name, which eBay International AG has been using to conduct its business in France, and for which it has used the marketing and sales support services of eBay France.

On tax audit of fiscal years 2003 to 2005, the French tax administration:

- Considered that the right to use the internet domain name ‘ebay.fr’ was an intangible asset that eBay France had failed to recognize upon registration under its name
- Made a transfer pricing adjustment equal to 2% of the turnover realized by eBay International AG through ‘ebay.fr’ to reflect what the French tax administration considered to be arm’s length compensation for the registered owner of the domain name

The tax authorities’ assessment was challenged in court by eBay France.

Court’s decision
In its February 2012 judgment - recently made public - the Administrative Court of Montreuil, first chamber, established that the exclusive right to use an internet domain name is to be regarded as an asset because:

- It allows the domain name’s owner to generate regular income from it (either through direct use or by granting such right to another company).
- There are no apparent time limits to its use (because annual renewals to the domain name registration can be easily secured).

As a consequence, according to the court’s decision, eBay France must be regarded as having made an indirect transfer of profits abroad within the meaning of Article 57 of the French tax law because it holds the exclusive right to use the “ebay.fr” domain name and makes this right available to its Swiss parent company without receiving any compensation beyond the reimbursement of registration and renewal fees for the domain name.

The court noted that its June 2010 decision (Diligentia AB) has a limited value in the present case because the conditions in Diligentia deviated substantially from the facts of this case.

October 2012: India and the United Kingdom
Convention on avoidance of double taxation amended by India and UK. The pact will streamline the provisions on partnerships and dividends, besides enhancing the information flow between tax authorities of the two countries.

The pact relates to the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains.
Firms partnering with UK would benefit from the amendment. Further, the withholding taxes on the dividends would be 10% or 15% and would be equally applicable in the UK and India.

Post the amendment, the convention will provide tax stability to the residents of India and the UK and will facilitate economic cooperation between the two nations. It will also encourage the flow of investment, technology and services.

The pact incorporates the provisions for effective exchange of information between the tax authorities of the two countries in line with latest international standards, including exchange of banking information and supplying of information irrespective of domestic interest. It also provides for sharing of information to other agencies with the consent of the supplying state.

The pact further includes the anti-abuse (limitation of benefits) provisions to ensure that the benefits of the convention are not misused.

Further, both the countries would enter into memorandums of understanding (MoUs) to expedite exchange of information and assistance in collection of taxes.

October 2012: Nigeria

Proposed transfer pricing regulations to be effective 2013. Among the measures of the proposed transfer pricing regulations are:

- The definition of ‘connected taxable persons’ to include related persons, individuals, companies, partnerships, joint ventures, trusts, or associations
- Rules for applicable transactions (ie, controlled transactions or commercial and financial transactions between connected taxable persons)
- Requirements for companies in preparing their transfer pricing documentation, including the use of appropriate methods and that the documents are to be prepared before the due date for filing the income tax return

For certain taxpayers, the proposed transfer pricing regulations will present challenges if certain connected transactions are not proactively identified and addressed. For example, among such areas would be the following:

- Turnover based on cost-plus mark-up arrangements - which may be of particular concern in the oil services industry
- Deemed profit rate - possibly warranting a transfer pricing study for non-resident companies that previously filed their income tax returns on a deemed profit basis
- Interest-free and below-market interest rate loans - which will need to be at an arm’s length rate
- Shared services costs possibly warranting a study to determine the appropriate profit rate for the services provided
- Technical or management services arrangements and payments for intellectual properties - possibly requiring appropriate transfer pricing documents supporting the tax deductibility of such payments

October 2012: Canada

2012 federal budget tax measures are ‘substantively enacted’ for purposes of IFRS and Canadian GAAP. Bill C-45 includes business and international tax measures from the 2012 federal budget that:

- Restrict the ability of foreign-based multinational corporations to transfer, or ‘dump’, foreign affiliates into their Canadian subsidiaries, while preserving the ability of these subsidiaries to undertake legitimate expansions of their Canadian
businesses
  • Improve the integrity and fairness of the thin capitalization rules
  • Reduce the general Scientific Research and Experimental Development (SR&ED) investment tax credit rate to 15% (from 20%)
  • Reduce the prescribed proxy amount, which taxpayers use to claim SR&ED overhead expenditures, to 55% of the salaries and wages of employees who are engaged in SR&ED activities (from 65%)
  • Remove the profit element from arm’s length third-party contracts for the purpose of the calculation of SR&ED tax credits
  • Remove capital from the base of eligible expenditures for the purpose of the calculation of SR&ED tax incentives
  • Prevent the avoidance of corporate income tax through the use of partnerships to convert income gains into capital gains
  • Provide that transfer pricing secondary adjustments will be treated as dividends for Part XIII withholding tax purposes
  • Phase out the Atlantic investment tax credit for activities related to the oil and gas and mining sectors
  • Phase out the Corporate Mineral Exploration and Development Tax Credit
  • Provide that qualified property for the purposes of the Atlantic investment tax credit will include certain electricity generation equipment and clean energy generation equipment used primarily in an eligible activity
  • Expand the eligibility for the accelerated capital cost allowance for clean energy generation equipment to include a broader range of bio-energy equipment
  • Phase out the Overseas Employment Tax Credit