

Transfer pricing risks and opportunities



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We have witnessed a surge in investigations as tax authorities around the world increase their resources to tackle the issue. Due to unprecedented international co-operation, new onerous rules are being introduced to tackle perceived tax avoidance. Businesses need to be aware of the new risks and potential costs. Of particular importance is the fact that transfer pricing documentation submitted to the tax authority of one country will in many cases now be shared with other countries.

Risks....

There are many new transfer pricing laws which have been introduced which could impact your business. These include far reaching US tax reform changes, significant changes to compliance principles resulting from the OECD's Base Erosion Profit shifting (BEPS) project and anti-avoidance measures being considered by the EU. We are seeing transfer pricing investigations being instigated in many countries for the first time and a significant increase in the use of technology to aid risk assessing.

A key point to remember is that when you sign a tax return you are typically confirming that any transactions in that return comply with transfer pricing rules and that you have the correct documentation to support it. If you do not have an up to date local file and master file then it is unlikely that you are compliant and your return may be incorrect. This may have serious consequences including large tax liabilities, penalties, interest charges for earlier years and reputational damage for both you and the business.

...and opportunities

Tax cost management using transfer pricing remains alive and well and is likely to do so as long as countries use tax rates as a policy to attract investment. Indeed as many methods of tax planning become less attractive transfer pricing is becoming an increasingly popular method of tax cost management given that simply by implementing an effective compliance approach tax costs can often be reduced. What is important is that transfer pricing needs to be consistent with economic value creation and supported by appropriate documentation.

Who is affected?

Generally groups of companies that meet one or more of the following criteria:

- Operations in more than one country
- Transactions between group companies such as product sales, services, or financing
- Sales through a website
- Intangible property such as brands, patents, trademarks, knowhow, customer lists or client relationships
- Employees working or selling overseas

In some circumstances enterprises other than companies and also domestic transactions may be caught.

What should businesses be concerned about?

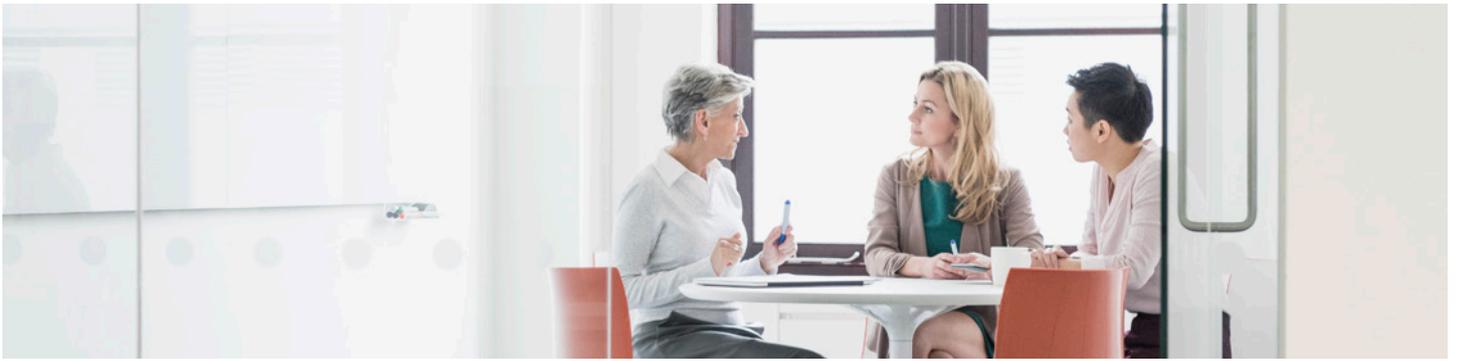
1. Are you sure that you are not paying too much tax in the countries in which you operate?
2. What do you know about new global transfer pricing rules and penalties for non-compliance?
3. Do you know about the new taxes on companies that sell or market through a website?
4. Would publication or leaking of group data pose a reputational or commercial risk to the business?
5. What is stopping you from selling goods or services into more countries?
6. What problems do you face with cross selling in the business?
7. When did you last update your intangible property tax strategy?
8. Are you aware of the opportunities and risks created by recent tax reform in countries including the US?
9. Is your transfer pricing being challenged?

What should businesses be doing?

An excellent starting point is for businesses to review their transfer pricing strategy and documentation. The new rules require profits to align with economic activity, and groups need to review their strategy for the pricing of transactions – or lack of it – between related parties. This typically means between group companies, but can include offices, permanent establishments and partnerships. Documentation then needs to be reviewed and updated to reflect the new rules.







Unlike in the past, this now means that many groups will no longer be able to rely solely on individual transfer pricing reports but instead will need a master file covering the whole group plus local files for each country. In some cases larger corporates may also have to file a country by country report. There are currently discussions as to whether such documents should be made public, and if this were to become law groups of companies would need to publish potentially confidential and sensitive financial, employment and tax details on their websites. **If your transfer pricing documentation has not been updated since 2016 it is unlikely to be compliant with the new rules.**

Do you have transactions between related parties?

Who does this affect?
Generally medium and large sized groups but also smaller business in certain countries.

The risk issues

Transfer pricing documentation is required to support the pricing of these transactions. BEPS has introduced a radical overhaul of documentation requirements. A master file and local file is required. The master file will cover the whole group at a strategic level and will be capable of being shared between all relevant tax authorities. This increases compliance risks considerably. The local file will include more detail regarding the related party transactions affecting that particular jurisdiction. It is crucial that evidence of arm's length pricing is compiled. Simply stating that the group complies with the arm's length principle places the business, auditors and advisors at significant risk of challenge.

The opportunities

Virtually any business with cross border transactions can potentially benefit from different tax rates or particular circumstances of their business. A relatively simple review will identify such opportunities.

Action

Review transfer pricing strategy and documentation now to check compliance status.

Do you have intragroup service transactions?

Who does this affect?
All groups with related party service transactions.

The issue

Intra-group service charges are seen as a leading cause of tax leakage by many tax authorities. New principles are being introduced for low value service charges whilst high value service charges require detailed transfer pricing analysis to justify the economic value provided by the service.

The opportunities

Many businesses fail to recharge services correctly thereby missing a relatively simple and entirely legitimate cost saving opportunity.

Action

Review all service fees to ensure the services provided are consistent with the service fee charged and new principles. Tax cost management is still possible providing that economic substance principles are recognised and adhered to.

Do you have intangible assets?

Who does this affect?
All groups with intangible assets whether or not they are shown on the balance sheet (e.g. trademarks, patents, licenses, goodwill, brands, know-how, client relationships).

The risk issues

Revised principles are being introduced regarding the allocation of profits from intangible assets. Registered ownership will be less important in allocating profit. Instead the creation of economic value and commercial substance should be rewarded appropriately. The valuation of intangibles being transferred between connected parties is also under the spotlight.

The opportunities

The changes in transfer pricing principles means that for many businesses this is the ideal time to review their strategy to ensure they are not overpaying tax.

Action

Review intangible asset ownership structures. Identify jurisdictions where control and development of intangible assets occur.

Do you have to prepare country by country reports?

Who does this affect?
Groups with cross border related party transactions and global turnover in excess of €750m. Smaller groups may still have to prepare a master file and local files.



The risk issues

A completely new compliance concept introduced with the aim of increasing transparency so as to enable tax authorities to identify risk. Groups need to submit specified financial and tax data to be shared across all countries in which they operate. The EU is seeking to implement legislation to force groups to publish this information on their websites. This may give rise to significant reputational and commercial risks in addition to tax exposures.

Action

You need to review information required by country-by-country reporting and the potential risks that arise as a result of the information being shared and potentially published.

Do you have debt transactions?

Who does this affect?

Medium and large sized businesses that pay interest on debt from independent lenders or related parties.

The risk issues

The OECD's BEPS recommendations are that tax relief on debt should be restricted. New rules are being introduced to enforce this approach. The restriction should be based on a fixed percentage of a company's EBITDA. This could cause significant increases in tax liabilities especially for highly geared businesses. The recommendations include third party as well as connected party debt. Interest rates and guarantees also need to comply with transfer pricing rules and be properly evidenced.

The opportunities

There are ways to mitigate the impact of these rules. Financing remains a key method for managing costs providing it aligns with commercial and transfer pricing principles.

Action

Review how the proposed changes will impact your business's ability to claim tax relief for interest. Restructuring may be appropriate. Amounts of debt and interest rates may need to be supported by evidence based documentation.

How can we help?

Our global transfer pricing specialists will work with you to provide clear, concise advice across the locations in which your business operates.

Our experience will enable you to gain insight into the strategies of tax authorities and benefit from practical advice as to the best options available to you. We have experts around the world and provide:

- Strategy advice
- Documentation including benchmarking
- Audit defence
- Advance agreements with tax authorities
- Valuation advice
- Supply chain advice

We have many years' experience including specialists with tax authority and Big 4 experience. We work cohesively to ensure that you receive advice from experts in tax, economics and business consulting.



About Moore Stephens

We help you thrive in a changing world.

We provide all the support and guidance you need to deal with new risks and opportunities. We ensure easy access to the right people, so decisions can be made quickly and confidently. A consistent team will partner with you to support your aspirations and contribute to your success.

You'll have access to a range of core services, including audit, accounting, tax, risk and systems assurance, corporate finance, restructuring and insolvency, wealth management and disputes analysis. As a Top 10 accounting and advisory network we support a broad range of individuals and entrepreneurs, large organisations and complex international businesses.

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Moore Stephens globally

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