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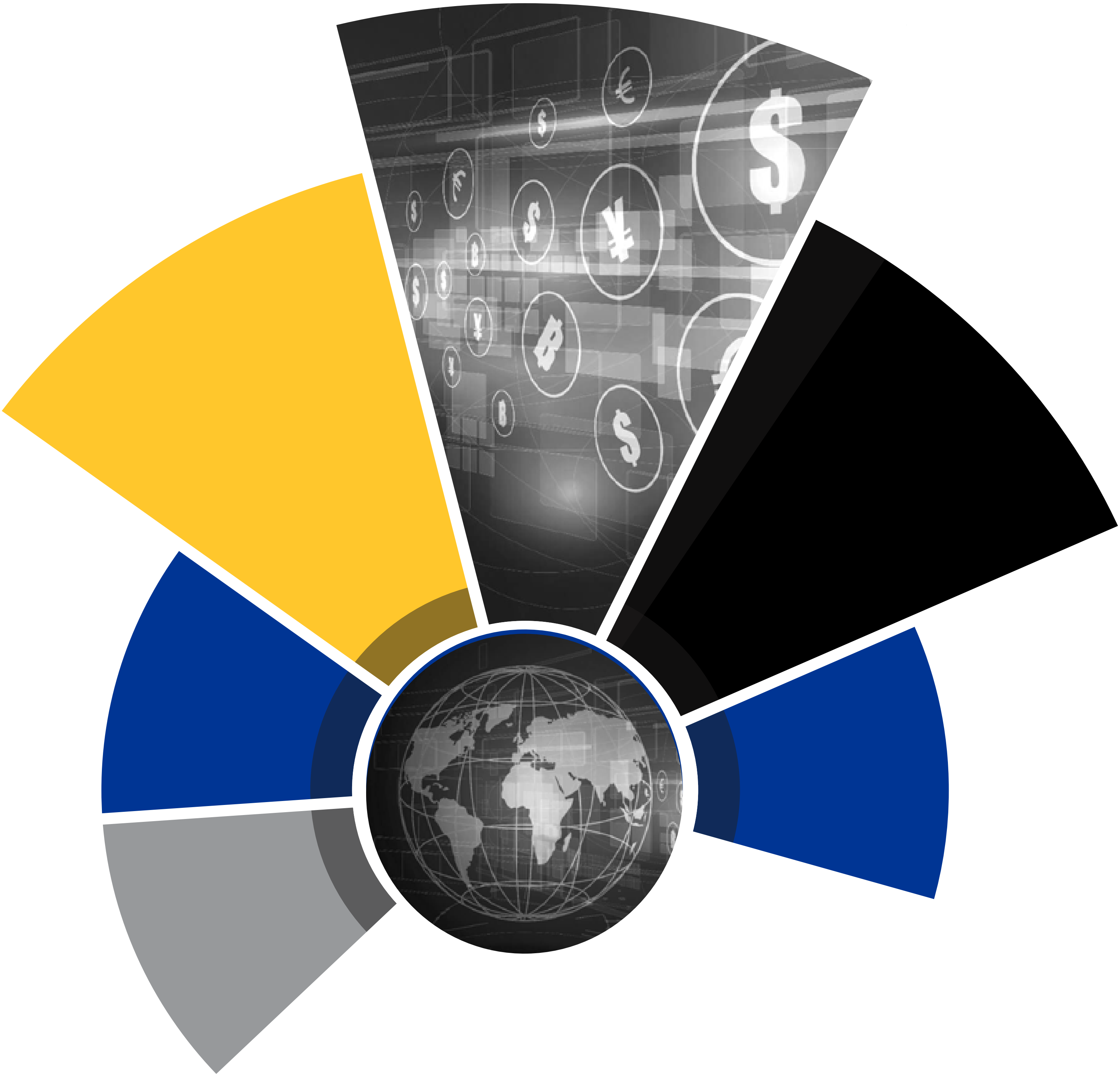

Are you at a Risk of Transfer Pricing?

TP Article # 2

A DECADE OF SERVICE

We have published an article on Introduction to Transfer pricing.
If you have missed out CLICK HERE **to read it.**

Transfer pricing (TP) is the practice of setting the price of goods and services for transactions between affiliated organizations for example, a manufacturer and a distributor owned by the same parent company. The effective management of transfer pricing allows global companies to achieve the best financial outcome possible.

The Organization for Economic Co-operation and Development (OECD) is responsible for regulating transfer pricing guidelines for multinational organizations. These guidelines, which are accepted by **nearly all tax authorities** including Tanzania, outlines the rules and regulations on transfer pricing to ensure accuracy and fairness. They specify that the price of a controlled transaction (one made internally between related companies) must follow what's known as the **arm's length principle**. This principle specifies that a company must charge a similar price for a controlled transaction as an uncontrolled transaction made by a third party. In other words, the transaction amount must be at a fair market price.

Businesses be it a multinational, conglomerate or a SME are exposed to Transfer pricing risks if they do transact with associated resident or non-resident entities

A number of these activities are indicators of the potential for incorrect transfer pricing, some of which are:

- Companies making losses over a number of years;
- Sustained losses by local entities, but (overall) profits at the group level;
- Sudden decrease in margins with no rationale;
- Failure to have a TP policy or a policy which does not cover all the related party transactions;
- TP policy which is not up to date and do not or no longer accurately reflect the operation and management of the business;
- Misstatements in the TP policy;
- Lack of formal agreement for services or finance provision with no recharge of costs;
- Non- existent or ambiguous intercompany agreements;
- Lack of credible benchmarking study;
- Debt levels, intra-group loans and guarantees that are "un-commercial";
- Trading debtor balances such as intercompany loans, long term debts which are interest free and non-moving; and
- Dormant companies with intercompany creditors and net assets/investments.

There are as well additional indicators which are considered as Red Flags by the Tax Authorities. The presence of these indicators does not, of itself, imply that the transfer pricing of the business is necessarily incorrect however they may trigger TP Audits:

- Companies paying large management fees or paying royalties or other charges for the use of intellectual property;
- Companies with innovative business structures;
- Significant group reorganizations involving business transfers overseas;
- Transactions with tax havens or shelters;
- Companies in a commercial relationship with a related party where non-tax factors provide incentive for manipulation; and
- Loss making companies in commercial relationship with a lower marginal rate taxpayer where the loss is as a result of payments to that entity.

Tips for Avoiding Common Transfer Pricing Pitfalls

- Comply with the Regulations;
- Create a thorough documentation. Ensure that the document is updated annually and where appropriate and prepare intercompany agreements to cover all material (especially recurring) intercompany transactions;
- Regularly assess your policy; and
- Always be audit ready.

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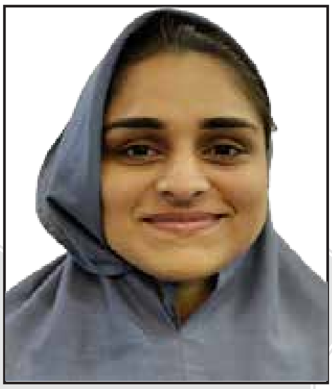

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