ARM LENGTH PRICE TO RELATED AND CONNECTED PERSON

Transfer Pricing – Analysis and Way Forward

By CA Atul Kumar Gupta, FCA, FCMA, LLB

Thought leader

Tax impact on Cost Sheet need to rework for revised Pricing, Margins.

- ✓ Tax Cost
- ✓ Expenses not allowed as deductions
- ✓ Arm Length Price Cost
- ✓ Tax Losses not adjusted

Business remodeling

- ✓ Tax Group/Participative Exemptions
- ✓ Business Restructuring decision
- ✓ Acquisition and Mergers Decisions
- ✓ Permanent Establishment
- ✓ Agreements review for Arm Length
- ✓ Free Zone Vs Main Land
- ✓ Source Based Activity
- ✓ Related Party Eco-System

Infrastructure

- ✓ Accounting Manual
- ✓ Accounting Software Integration
- ✓ Handling Expenses Vouchers
- ✓ Record Keeping/Registers
- ✓ MIS for Audit/Scrutiny
- ✓ Cost Centre Development/Tax Group
- ✓ Stock Verification
- ✓ Third Party Confirmation

Tax Compliances

- ✓ Withholding Tax
- ✓ Tax Credits
- ✓ Exempted Units
- ✓ Audit
- ✓ Registration, Returns

HR Related Aspect

- ✓ Team Building
- ✓ Capacity Building

RATIONALE

- Providing a statutory framework for computation of reasonable, fair & equitable profits and tax.
- Protect the right of a country to collect its due share of tax in respect of transactions between related entities.
- Preventing MNEs from shifting profits to low tax jurisdictions by manipulating prices of intra-group transactions
- "Where in an international transaction or specified domestic transaction, two or more associated enterprises enter into a mutual agreement or arrangement for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises, the cost or expense allocated or apportioned to, or, as the case may be, contributed by, any such enterprise shall be determined having regard to the arm's length price of such benefit, service or facility, as the case may be."

MEANING OF INTERNATIONAL TRANSACTION

"a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and

shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises."

Takeaways:

- Transaction to be between Associated Enterprises (AEs)
- Transactions to have a bearing on profits, income, losses & Assets

WHAT MAY BE TRANSACTION……?

the expression "transaction" may possibly include—

(a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

(b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

WHAT MAY BE TRANSACTION……?

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

(d) provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

(e) a transaction of business restructuring or re-organisation, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

WHAT IS INTANGIBLE PROPERTY ?

the expression "intangible property" may include—

(a) marketing related intangible assets, such as, trademarks, trade names, brand names, logos;

(b) technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;

(c) artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;

(d) data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;

(e) engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schema-tics, blueprints, proprietary documentation;

(f) customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

WHAT IS INTANGIBLE PROPERTY ?

(g) contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;

(h) human capital related intangible assets, such as, trained and organised work force, employment agreements, union contracts;

(i) location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

(j) goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;

(k) methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;

(l) any other similar item that derives its value from its intellectual content rather than its physical attributes.

ARM'S LENGTH PRINCIPLE-ARTICLE 34

1. In determining Taxable Income, transactions and arrangements between Related Parties must meet the arm's length standard as specified in Clauses 2, 3, 4 and 5 of this Article and any conditions that may be prescribed in a decision issued by the Authority.
2. A transaction or arrangement between Related Parties meets the arm's length standard if the results of the transaction or arrangement are consistent with the results that would have been realized if Persons who were not Related Parties had engaged in a similar transaction or arrangement under similar circumstances.
3. The arm's length result of a transaction or arrangement between Related Parties must be determined by applying one or a combination of the following transfer pricing methods:

   a) The comparable uncontrolled price method.

   b) The resale price method.

   c) The cost-plus method.

   d) The transactional net margin method.

   e) The transactional profit split method

ARTICLE 35 – RELATED PARTIES AND CONTROL

1. For the purposes of this Decree-Law, “Related Parties” means any of the following:

   a) Two or more natural persons who are related within the fourth degree of kinship or affiliation, including by way of adoption or guardianship.

   b) A natural person and a juridical person where:

      1. the natural person or one or more Related Parties of the natural person are shareholders in the juridical person, and the natural person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in the juridical person; or

      2. the natural person, alone or together with its Related Parties, directly or indirectly Controls the juridical person.

ARTICLE 35 – RELATED PARTIES AND CONTROL

c) Two or more juridical persons where:

1. one juridical person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in the other juridical person;

2. one juridical person, alone or together with its Related Parties, directly or indirectly Controls the other juridical person; or

3. any Person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in or Controls such two or more juridical persons;

d) A Person and its Permanent Establishment or Foreign Permanent Establishment. e) Two or more

Persons that are partners in the same Unincorporated Partnership.

ARTICLE 35 – RELATED PARTIES AND CONTROL

f) A Person who is the trustee, founder, settlor or beneficiary of a trust or foundation,

and its Related Parties.

2. For the purposes of this Decree-Law, "Control" means the ability of a Person, whether in their own right or by agreement or otherwise to influence another Person, including:

a) The ability to exercise 50% (fifty percent) or more of the voting rights of another Person.

b) The ability to determine the composition of 50% (fifty percent) or more of the Board of directors of another Person.

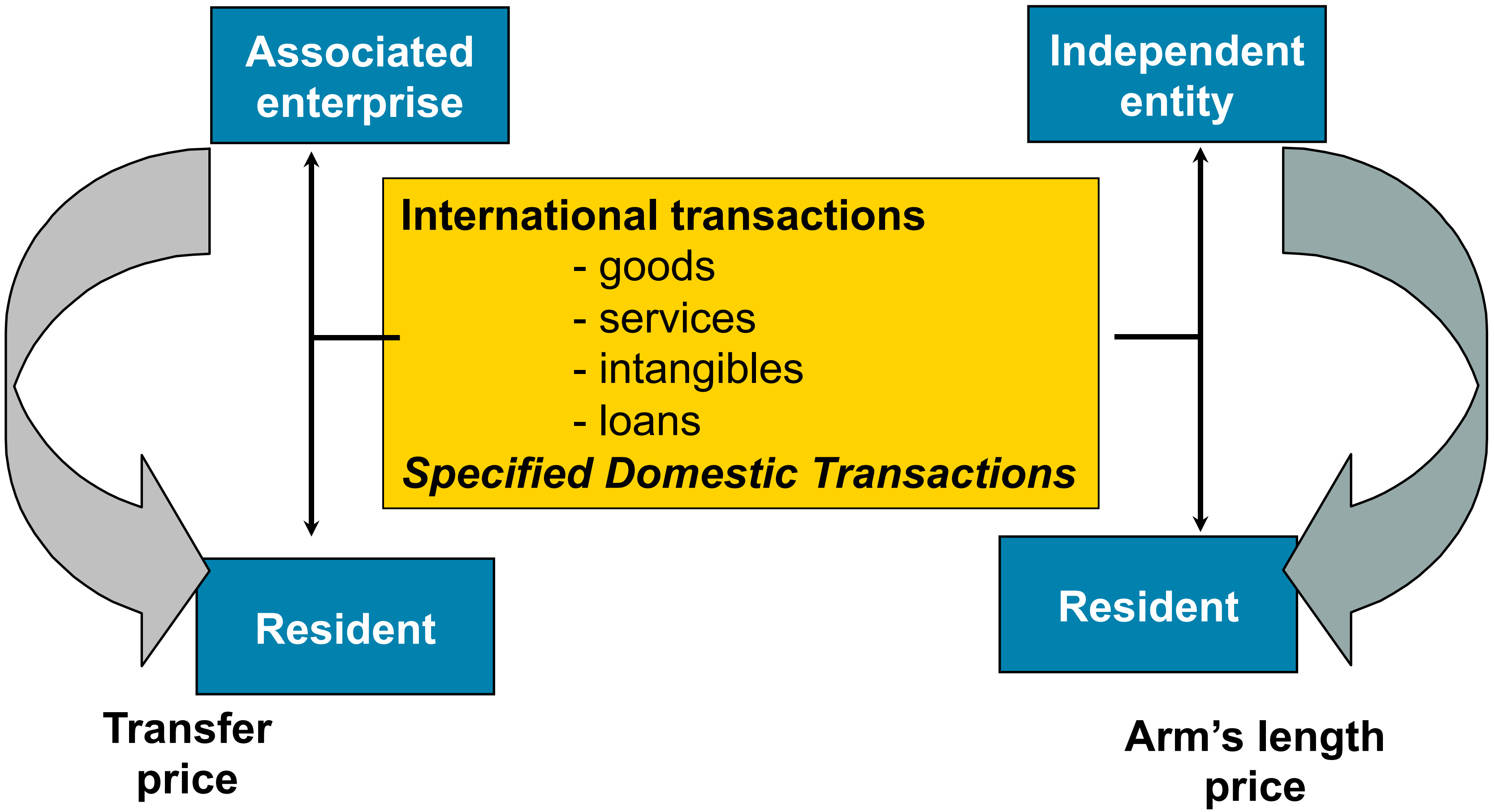
c) The ability to receive 50% (fifty percent) or more of the profits of another Person. d) The ability to determine, or exercise significant influence over, the conduct of the Business and affairs of another Person.

ARM'S LENGTH PRICE

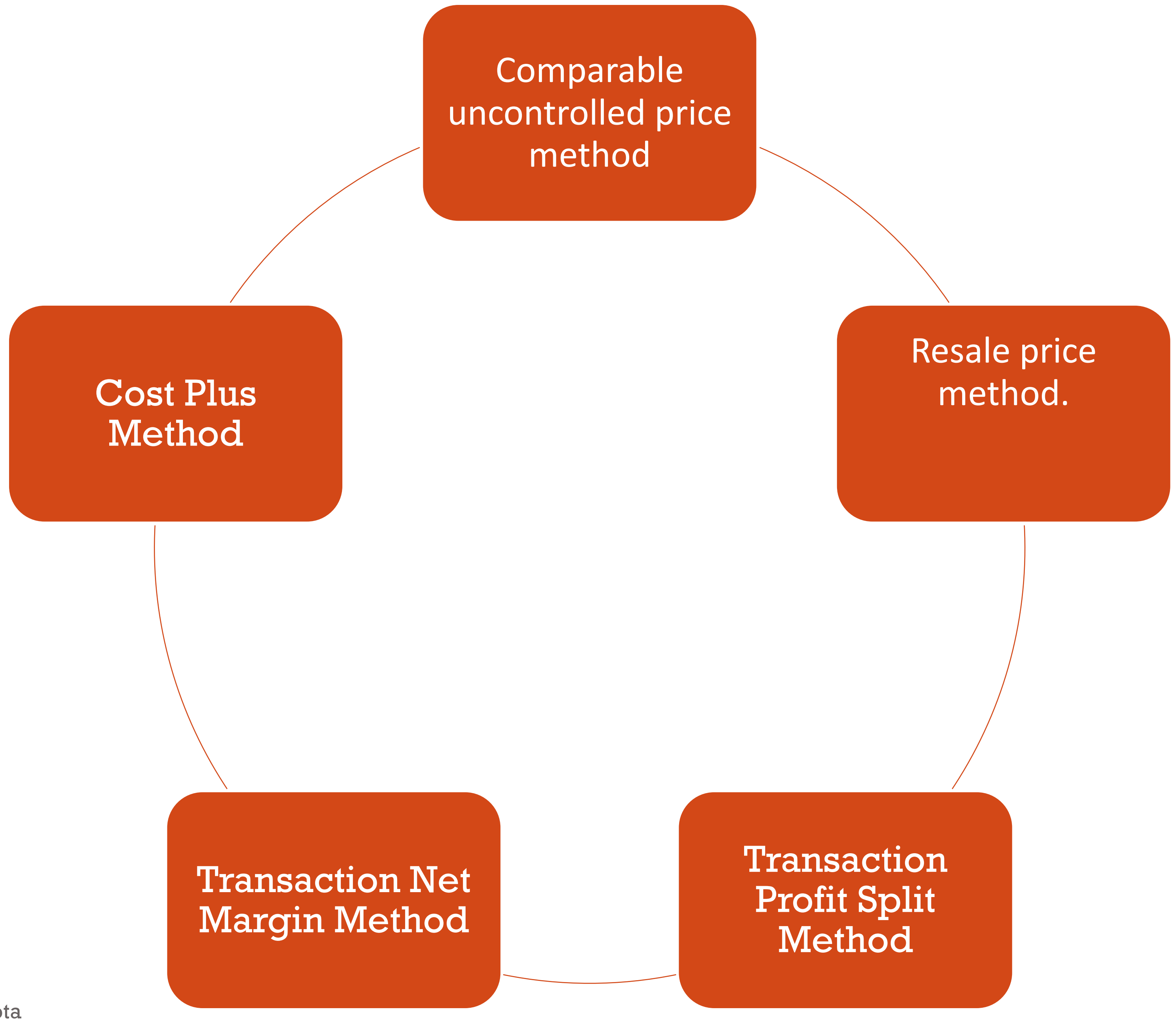
- **Meaning of Arm's length price (ALP) (Financial Definition)**

  The price at which a willing buyer and a willing unrelated seller would freely agree to transact or a trade between related parties that is conducted as if they were unrelated, so that there is no conflict of interest in the transaction.

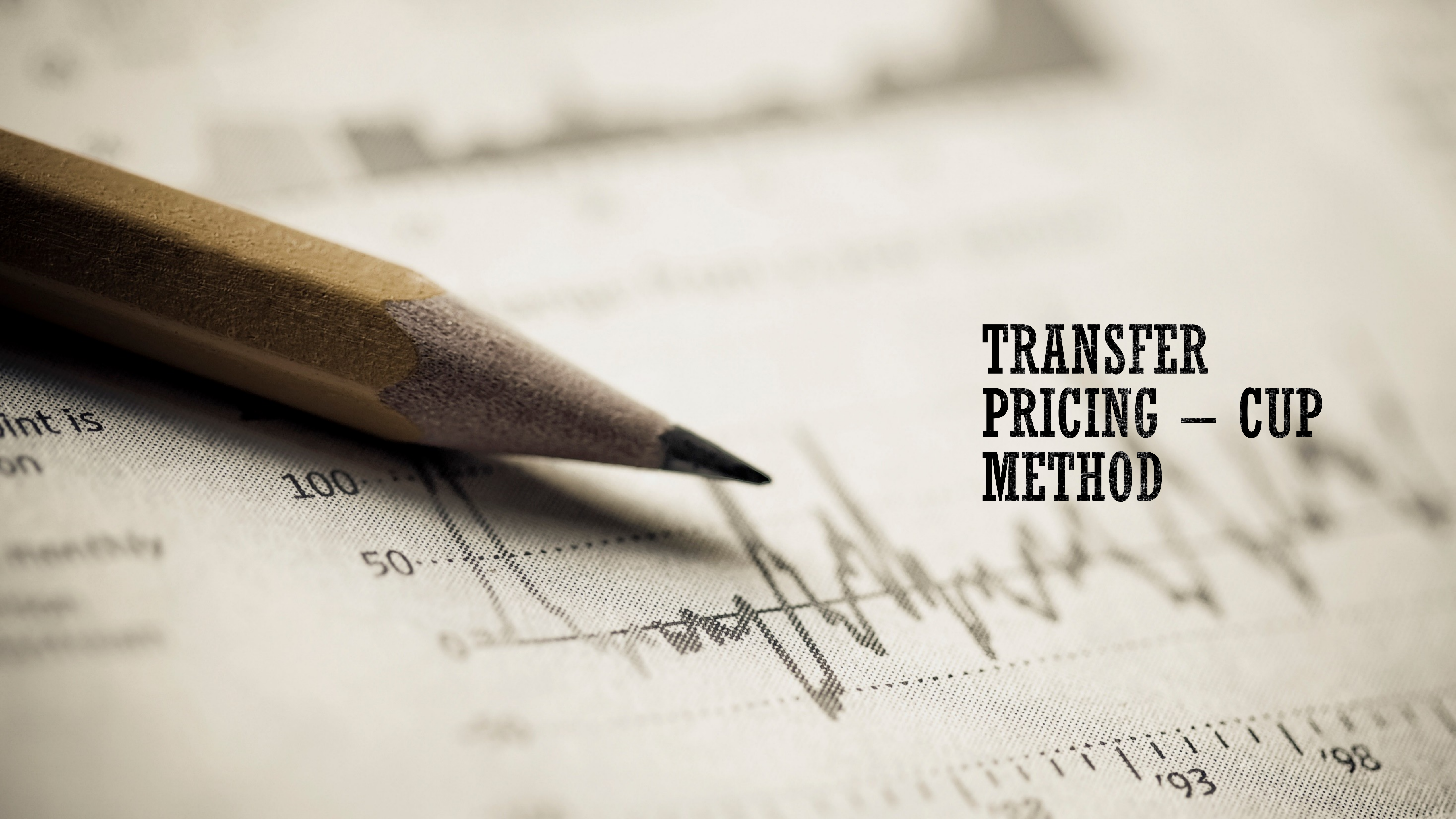
CONCEPT



Associated enterprise
Independent entity
International transactions
- goods
- services
- intangibles
- loans
Specified Domestic Transactions
Resident
Resident
Transfer price
Arm's length price


Comparable uncontrolled price method
Resale price method.
Transaction Profit Split Method
Transaction Net Margin Method
Cost Plus Method

TRANSFER PRICING – CUP METHOD



COMPARABLE UNCONTROLLED PRICE METHOD

- A comparable uncontrolled price method is used for comparing prices, price charged for property or services transferred in a controlled transaction to the price charged in a comparable uncontrolled transaction in comparable situations.

ADVANTAGES AND DISADVANTAGES

- Advantages
  - It is the most direct and reliable way to apply the arm's length principle under international taxation.
  - It is considered as most appropriate transfer pricing method for establishing the arm's length price for the transfer of commodities between associated enterprises.

- Disadvantages
  - It is difficult to find a similar transaction between independent enterprises
  - It may involve a significant cost to maintain information required to compare the data.

STEPS TO DETERMINE CUP METHOD

1. Identification of price charged or paid for property transferred or services provided under any comparable uncontrolled transactions.
2. The price is adjusted to account for differences, if any, between the international transaction and comparable uncontrolled transactions
3. Adjusted price arrived above taken to be as arm's length price

ILLUSTRATION:

10%. Tax	30% Tax	Calculations
Foreign	India	Price charged in uncontrolled transaction - $6000 Less: Adjustment (discount given to Y ltd for bulk purchase)- $400
Y Ltd	X Ltd	Arm's length Price - $5600
Sale $6000 outsider	Sale $4000	Price charged in controlled transaction - $4000 Difference to be added in X ltd's income- $1600

TRANSFER PRICING – RESALE PRICE METHOD

RESALE PRICE METHOD

- Definition-
- The resale price method (RPM) is a method which compares the gross margins (i.e. gross profit over sales) or difference between the price at which a product is purchased and the price at which it is on-sold to a third party.
- This method is applicable where the controlled party is a distributors and resellers.

ADVANTAGES AND DISADVANTAGES

- Advantages
- It is considered as most appropriate transfer pricing method where one enterprise produces and another enterprises only resells.
- It is useful where the reseller does not add substantially to the value of the product/ services.
- This method is based on market price. This means that it represents a method based on demand, thus making it more reliable in situations where there is a weak relationship between cost and sale prices.

Disadvantages

- It is difficult to collect gross margin data on a transaction by transaction basis.
- It may involve complexity when buyer adds significant value addition before reselling to customers.

STEPS TO DETERMINE RPM METHOD

1. Identification of resale price charged for goods sold to unrelated enterprises
2. Resale price is reduced by normal gross profit margin with reference to uncontrolled transaction.
3. Then, reduce expenses like custom duty which are in connection with purchase of the product/services.
4. Adjusted price arrived above taken to be as arm's length price

ILLUSTRATION

- A Ltd (Dubai) holds 60% equity shares of ABC Inc. (USA). A ltd purchased goods worth INR 20,00,000 from ABC Inc. and sold to unrelated person CC Ltd in India for INR 30,00,000. A ltd paid INR 3,50,000 as customs duty for import of goods from ABC Inc. Normal gross profit margin of A ltd in similar uncontrolled transaction is 25%. Calculate Arm's length price using resale price method.

ANSWER

Resale price of goods purchased from ABC Inc.	30,00,000
Less: normal gross profit margin @25%	(7,50,000)
Less: Expenses (customs duty)	(3,50,000)
Arm's length price	19,00,000
Increase in income of A ltd	1,00,000 (20,00,000- 19,00,000)

TRANSFER PRICING – COST PLUS METHOD

COST PLUS METHOD

- Definition-
- The Cost Plus Method ('CPM') determines an arm's-length price by adding an appropriate gross profit margin to an associated entity's costs of producing goods or services.
- CPM is applicable in the case of **manufacturers or service providers** engaged in supply of a property or provision of services to its related party.
- This method probably is most useful where **semi-finished goods** are sold between related parties.

ADVANTAGES AND DISADVANTAGES

- Advantages
- It is mostly applied to the routine manufacturing and sale of tangible goods
- It is easy to understand and apply because of simple calculations
- It covers all production and overhead costs

Disadvantages

- Prices considered are different than market prices
- More emphasis is given to cost components

STEPS TO DETERMINE COST PLUS METHOD

1. Determination of **direct and indirect costs of production** incurred by the enterprise in respect of property transferred or services provided to a related party
2. **(+) Gross profit mark-up earned in comparable uncontrolled transaction**
3. **(+) / (-) Adjustments** for differences which would materially affect the gross profit margins in open market.
4. Adjusted price arrived above taken to be as **arm's length price**

ILLUSTRATION

- ABC Ltd., Canada holds 35% shares in LMN Ltd., Dubai. LMN Ltd. develops software and does both onsite and offsite consultancy services for the customers.
- LMN Ltd. during the year billed ABC Ltd. Canada for 120 man-hours at the rate of US$ 1,800 per man hour. The total cost (direct and indirect) for executing this work amounted to US$ 2,25,000.
- However, LMN Ltd. billed XYZ Ltd., India at the rate of US$ 2,800 per man hour for the similar level of manpower and earned a **Gross Profit of 50% on its cost**. The transactions of LMN Ltd. with ABC Ltd. and XYZ Ltd. are comparable, subject to the following differences:
- As ABC Ltd. gives business in large volumes, LMN Ltd. offered to ABC Ltd., a quantity discount which may be valued **at 10% of normal gross profits.**
- Compute the Arm's Length Price along with income to be increased under the Cost Plus Method

SOLUTION:

Particulars	Amount (INR)
Gross Profit mark-up on cost in case of XYZ Ltd. [an unrelated party]	50%
Less: Adjustments Quantity discount to ABC Ltd. [Quantity discount is allowed to ABC Ltd. as it gives business in large volumes, but the same is not provided to XYZ Ltd. Therefore, it shall be adjusted] [10% of 50%, being gross profit]	(5%)
Arm's length gross profit mark up to cost	45%
Cost incurred by LMN Ltd. for executing ABC Ltd.'s work	2,25,000
Add: Adjusted gross profit (` 2,25,000 x 45%)	1,01,250
Arm's length billed value	3,26,250
Less: Actual Billed Income from ABC Ltd. (` 1800 x 120 man hours)	2,16,000
Total Income of LMN Ltd to be increased by	1,10,250

TRANSFER PRICING – PROFIT SPLIT METHOD & TNMM

PROFIT SPLIT METHOD

- Definition-
- The PSM determines arm‟s length profit based on combined profits derived by related parties
- Normally PSM is applicable where assessee executes an order in Joint Venture with its associated enterprise.
- [A joint venture is a short-term partnership between two or more business entities or individuals created for executing projects.]

ADVANTAGES AND DISADVANTAGES

- Advantages
- It is used to share profits for unique intangibles contributed through joint ventures
- It provides solution for integrated operations not offered by one-sided methods

Disadvantages

- It is difficult to measure the relevant revenues and costs to be split between the related parties
- This method often relies on less direct information or proxies in its application of the arm's length principle.

STEPS TO DETERMINE PROFIT SPLIT METHOD

1. Determination of total profit earned in Joint Venture
2. **Divide that proft between AEs in the ratio of manpower employed, functions performed, risk taken etc.**
3. Cost incurred by the assessee
4. **(+) share of profit of such enterprise derived in step 2**
5. **=Arm's length price.**

ILLUSTRATION

- MM Ltd incorporated in UK received order to develop a software for Nano Inc. US and consideration for same is $2,00,000. MM ltd executed such order in joint venture with BB ltd and Odi Ltd India based companies. Odi ltd holds 30% equity shares of BB ltd and 27% equity shares of MM Ltd. Consideraion of $ 2,00,000 is distributed amongst MM ltd, BB ltd and Odi ltd $1,00,000, $50,000 and $50,000 respectively.
- Cost incurred to develop the software is $1,60,000. Relative contributions by MM ltd, BB ltd and Odi ltd in FAR is 40:40:20.
- Cost incurred by BB ltd is $64,000. Calculate ALP for BB ltd.

SOLUTION:

Particulars	Amount ($)
Total profit from joint venture ($ 2,00,000 - $ 1,60,000)	40,000
Distribution of profit on relevant contribution ratio:	
MM ltd : $40,000 * 40%	$16,000
BB ltd : $40,000*40%	$16,000
Odi ltd : $40,000*20%	$8000
Calculation of ALP for **BB ltd**	
Cost incurred :	$64,000
Add: Profit	$16,000
Arm's length price	$80,000
Profit to be increased of BB ltd : $80000- $50,000	$30000

TRANSACTIONAL NET MARGIN METHOD-TNMM

- Definition-
- An arm's-length price is determined by comparing the net profit margin in relation to an appropriate base (example costs, sales, assets) of the tested party with the net profit margin in relation to the same base, of an uncontrolled party engaged in comparable transactions

ADVANTAGES AND DISADVANTAGES

- Advantages
- Minimum affect by transactional differences in the case with price on the net profit indicators.
- It is not necessary to state the books and records of all participants in the business activity on a common basis.

Disadvantages

- A transaction net margin method is unlikely to be reliable if each party to a transaction makes unique and valuable contributions.
- The net profit indicator of a taxpayer can be influenced by some factors that would either not have an effect, or have a less substantial or direct effect, on price or gross margins between independent parties.

STEPS TO DETERMINE COST PLUS METHOD

1. Identify net profit margin realized by the enterprise from an international transaction with regard to an appropriate base
2. Identify net profit margin from a comparable **uncontrolled transaction** or a number of such transactions having regard to the same base
3. **Adjust for differences** that could affect net profit in the open market
4. Adjusted net profit used for establishing **Arm's Length Price**

ILLUSTRATION:

- X Limited has sold 20,000 units of **White bags** to its wholly owned subsidiary based outside Dubai for US$ 2,00,000. Net Profit Margin for such a transaction is 15%.
- X Limited sold 50,000 units of **black bags** to an unrelated enterprise for US$ 4,50,000. Net Profit Margin for such a transaction is 25%.
- For sale of more than 30,000 units X Limited provides a bulk discount of 1%.
- Also, Profit Margin on Black bags is 2% more as compared to White Bag.
- Therefore, adjusted Net Profit Margin for comparable uncontrolled transaction will be 24% (25%+1%-2%)

SOLUTION:

- Transaction value is US$ 2,00,000 and
- Net Profit Margin of International Transaction: 15%
- Cost of Goods sold: US$ 1,70,000 (2,00,000 * 85%)
- Net Profit Margin for computation of Arm's Length Price: 24%
- Arm's Length Price: US$ 2,23,684 (1,70,000*100/76)
- Difference of US$ 23,684 will be added to the income of X ltd.

ARM'S LENGTH PRINCIPLE-ARTICLE 34

4. The Taxable Person may apply any transfer pricing method other than the methods listed in Clause 3 of this Article where the Taxable Person can demonstrate that none of the above methods can be reasonably applied to determine an arm's length result and that any such other transfer pricing method used satisfies the condition of Clause 2 of this Article.
5. The choice and application of a transfer pricing method or combination of transfer pricing methods under Clause 3 or 4 of this Article must be made having regard to the most reliable transfer pricing method and taking into account following factors:

   a) The contractual terms of the transaction or arrangement.

   b) The characteristics of the transaction or arrangement.

   c) The economic circumstances in which the transaction or arrangement is conducted.

   d) The functions performed, assets employed, and risks assumed by the Related Parties entering into the transaction or arrangement.

   e) The business strategies employed by the Related Parties entering into the transaction or arrangement.

ARM'S LENGTH PRINCIPLE-ARTICLE 34

6. The Authority's examination as to whether income and expenditures resulting from the Taxable Person's relevant transactions or arrangements meet the arm's length standard shall be based on the transfer pricing method used by the Taxable Person in accordance with Clause 3 or 4 of this Article, provided such transfer pricing method is appropriate having regard to the factors mentioned in Clause 5 of this Article.
7. Application of the selected transfer pricing method or combination of transfer pricing methods in accordance with Clause 3 or 4 of this Article may result in an arm's length range of financial results or indicators acceptable for establishing the arm's length result of a transaction or arrangement between Related Parties, subject to any conditions specified in a decision issued by the Authority.
8. Where the result of the transaction or arrangement between Related Parties does not fall within the arm's length range, the Authority shall adjust the Taxable Income to achieve the arm's length result that best reflects the facts and circumstances of the transaction or arrangement.
9. Where the Authority makes an adjustment to the Taxable Income pursuant to Clause 8 of this Article, the Authority shall rely on information that can or will be made available to the Taxable Person.

ARM'S LENGTH PRINCIPLE-ARTICLE 34

10. Where the Authority or a Taxable Person adjusts the Taxable Income for a transaction or arrangement to meet the arm's length standard, the Authority shall make a corresponding adjustment to the Taxable Income of the Related Party that is party to the relevant transaction or arrangement.
11. Where a foreign competent authority makes an adjustment to a transaction or arrangement involving a Taxable Person to meet the arm's length standard, such Taxable Person can make an application to the Authority to make a corresponding adjustment to its Taxable Income.

ARTICLE 35 – RELATED PARTIES AND CONTROL

1. For the purposes of this Decree-Law, “Related Parties” means any of the following:

   a) Two or more natural persons who are related within the fourth degree of kinship or affiliation, including by way of adoption or guardianship.

   b) A natural person and a juridical person where:

      1. the natural person or one or more Related Parties of the natural person are shareholders in the juridical person, and the natural person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in the juridical person; or

      2. the natural person, alone or together with its Related Parties, directly or indirectly Controls the juridical person.

ARTICLE 35 – RELATED PARTIES AND CONTROL

c) Two or more juridical persons where:

1. one juridical person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in the other juridical person;

2. one juridical person, alone or together with its Related Parties, directly or indirectly Controls the other juridical person; or

3. any Person, alone or together with its Related Parties, directly or indirectly owns a 50% (fifty percent) or greater ownership interest in or Controls such two or more juridical persons;

d) A Person and its Permanent Establishment or Foreign Permanent Establishment. e) Two or more

Persons that are partners in the same Unincorporated Partnership.

ARTICLE 35 – RELATED PARTIES AND CONTROL

A Person who is the trustee, founder, settlor or beneficiary of a trust or foundation, and its Related Parties.

2. For the purposes of this Decree-Law, “Control” means the ability of a Person, whether in their own right or by agreement or otherwise to influence another Person, including:

a) The ability to exercise 50% (fifty percent) or more of the voting rights of another Person.

b) The ability to determine the composition of 50% (fifty percent) or more of the Board of directors of another Person.

c) The ability to receive 50% (fifty percent) or more of the profits of another Person. d) The ability to determine, or exercise significant influence over, the conduct of the Business and affairs of another Person.

ARTICLE 36 – PAYMENTS TO CONNECTED PERSONS

1. Without prejudice to the provisions of Article 28 of this Decree-Law, a payment or benefit provided by a Taxable Person to its Connected Person shall be deductible only if and to the extent the payment or benefit corresponds with the Market Value of the service, benefit or otherwise provided by the Connected Person and is incurred wholly and exclusively for the purposes of the Taxable Person’s Business.

2. For the purposes of this Decree-Law, a Person shall be considered a Connected Person of a Taxable Person if that Person is:

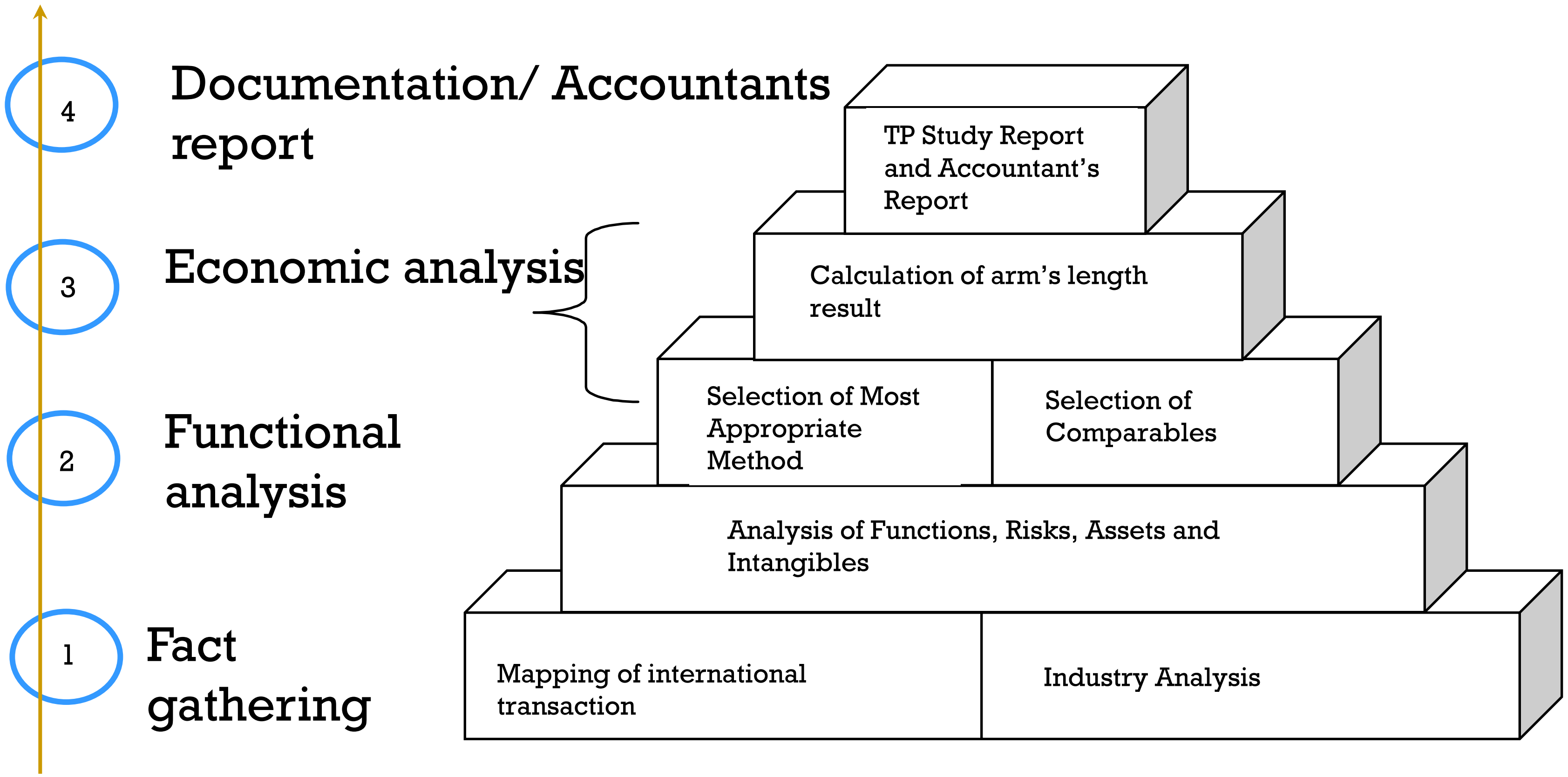
   a) An owner of the Taxable Person.

   b) A director or officer of the Taxable Person.

   c) A Related Party of any of the Persons referred to in paragraphs (a) and (b) of Clause 2 of this Article.

DOCUMENTATION

The approach for TP documentation may be summarised in the following phases of work:



DOCUMENTATION

Entity related

- Profile of industry
- Profile of group
- Profile of Dubai entity(s)
- Profile of associated enterprises

Price related

- Transaction terms
- Functional analysis (functions, assets and risks)
- Economic analysis (method selection, comparable benchmarking)
- Forecasts, budgets, estimates

Transaction related

- Agreements
- Invoices
- Pricing related correspondence (letters, emails etc)

COMPLIANCE – A STEP BY STEP APPROACH

Stage 1

Pre-project planning

- Preparation of project plan

Stage 2

Functional analysis - Information gathering

- Interviews
- Questionnaires
- Discussions with Management
- Characterisation of each entity
- Agreement reviews

Stage 3

Comparable data

- Search strategy
- Access to local & global database
- Analysis of internal comparables
- Judicious identification of arm's length range

Stage 4

Analysis

- Understand existing costing mechanism
- Determination of billing methodology

Stage 5

Issuance of Transfer Pricing Documentation

- Consultation with management
- Finalization of Transfer pricing documentation

DOCUMENTATION FOR TP 97/2023 -27/4/23

- **Conditions for Maintaining Master File and Local File**
- A Taxable Person that meets either of the following conditions shall maintain both a master file and a local file in accordance with Clause (2) of Article (55) of the Corporate Tax Law in the relevant Tax Period:
- a) Where the Taxable Person, for any time during the relevant Tax Period, is a Constituent Company of a Multinational Enterprises Group as defined in the Cabinet Decision No. 44 of 2020 referred to above that has a total consolidated group Revenue of AED 3,150,000,000 (three billion one hundred and fifty million United Arab Emirates dirhams) or more in the relevant Tax Period.
- b) Where the Taxable Person's Revenue in the relevant Tax Period is AED 200,000,000 (two hundred million United Arab Emirates dirhams) or more.

DOCUMENTATION FOR TP

- 2. Subject to Clause (3) of this Article, the Taxable Person shall include transactions or arrangements with all of the following Related Parties and Connected Persons in the local file:
- a) A Non-Resident Person.
- b) An Exempt Person.
- c) A Resident Person that has made an election under Article (21) of the Corporate Tax Law and meets the conditions of such election.
- d) A Resident Person whose income is subject to a different Corporate Tax rate from that applicable to the income of the Taxable Person.

DOCUMENTATION FOR TP

- 3. The Taxable Person shall not include transactions or arrangements with the following Related Parties and Connected Persons in the local file:
- a) Resident Persons other than those specified in paragraphs (b), (c) and (d) of Clause (2) of this Article.
- b) A natural person, provided that the parties to the transaction or arrangement are acting as if they were independent of each other.
- c) A juridical person that is considered to be a Related Party or a Connected Person solely by virtue of being a partner in an Unincorporated Partnership, provided that the parties to the transaction or arrangement are acting as if they were independent of each other.
- d) A Permanent Establishment of a Non-Resident Person in the State whose income is subject to the same Corporate Tax rate as that applicable to the income of the Taxable Person.

DOCUMENTATION FOR TP

- 4. For the purpose of paragraphs (b) and (c) of Clause (3) of this Article, the parties engaged in the transaction or arrangement shall be considered acting as if they were independent of each other where both of the following conditions are met:
- a) The relevant transaction or arrangement is undertaken in the ordinary course of Business.
- b) These parties are not exclusively or almost exclusively transacting with each other.
- 5. For the purpose of paragraphs (b) and (c) of Clause (3) of this Article, where the activities of one Person in the transaction or arrangement are subject to detailed instruction or to comprehensive control of the other Person in the same transaction or arrangement, such Persons shall not be regarded as acting as if they were independent of each other.
- 6. For the purposes of Clauses (4) and (5) of this Article, the Authority shall take into account all relevant facts and circumstances to determine whether the Persons shall be regarded as acting as if they were independent of each other

DOCUMENTATION FOR TP

- **Article (3) -Transfer Pricing Documentation Guidelines**
- The Authority shall issue guidelines for the application of the provisions of this Decision and maintaining transfer pricing documentation.
- **Article (4) - Publication and Application of this Decision**
- This Decision shall be published and shall come into effect the day following the date of its publication.

ARTICLE 36 – PAYMENTS TO CONNECTED PERSONS

3. For the purposes of paragraph (a) of Clause 2 of this Article, an owner of the Taxable Person is any natural person who directly or indirectly owns an ownership interest in the Taxable Person or Controls such Taxable Person.

4. Where the Taxable Person is a partner in an Unincorporated Partnership, a Connected Person is any other partner in that same Unincorporated Partnership, and any Person that is a Related Party of that partner.

5. To determine that a payment or benefit provided by the Taxable Person corresponds with the Market Value of the service or otherwise provided by the Connected Person in

exchange, the relevant provisions of Article 34 of this Decree-Law shall apply as the context requires.

ARTICLE 36 – PAYMENTS TO CONNECTED PERSONS

6. Clause 1 of this Article shall not apply to any of the following:

   a) A Taxable Person whose shares are traded on a Recognised Stock Exchange.

   b) A Taxable Person that is subject to the regulatory oversight of a competent authority in the State.

   c) Any other Person as may be determined in a decision issued by the Cabinet at the suggestion of the Minister.

Thank You

CA Atul Kumar Gupta

Email: atulservicetax@gmail.com,

Mobile: 9810103611

Corporate Office:
C (Sushant Lok-I, Sector 43,
Gurgaon-1220002 (Haryana),
Phone: 9810103611, 0124-4277824

Email: info@azlindia.com Web: www.azlindia.com