

Background Paper

Working Draft

Chapter 9

Documentation

[This paper is based on a paper prepared by Members of the UN Tax Committee's Subcommittee on Practical Transfer Pricing Issues, but includes Secretariat drafting and suggestions not yet considered by them – the Secretariat takes responsibility for any relevant errors and omissions.]

I. Introduction

Adequate documentation will make it easier for tax authorities to review a taxpayer's transfer pricing analysis and thereby contribute to avoiding a dispute or timely resolution of any transfer pricing disputes that may arise. Adequate documentation is characterised by (i) the sufficiency of the details demonstrating the taxpayers' compliance with the arm's length principle, as well as (ii) the timely manner in which such details are prepared and submitted to tax authorities upon their request.

A taxpayer should make reasonable efforts to undertake an adequate transfer pricing analysis to ascertain the arm's length pricing, as well as to show clearly that such analysis has been actually conducted. Activities undertaken to prepare and maintain appropriate documents with a view to conforming to the arm's length principle can be referred to as the "arm's length documentation".

This Chapter first introduces some existing international guidelines on transfer pricing documentation, which will be helpful in browsing general issues on transfer pricing documentation. It is then followed by a more in-depth discussion on several topical issues frequently raised in the process of TP documentation, with the goal of providing practical guidance on such issues. An annex to this Chapter will set forth selected countries' legislation examples on TP documentation and a Sample TP Study.

II. International Guidelines on Transfer Pricing Documentation

1. OECD Transfer Pricing Guidelines (2010)

The OECD's guidance on documentation is well summarized in the following paragraphs of the 1995 (and now 2010) versions OECD Transfer Pricing Guidelines:¹

¹ As noted elsewhere in this Manual, the Commentary to Article 9 of the UN Model recommended acceptance of the 1995 Guidelines in applying the "arm's length principle enshrined in Article 9. The 2010 Guidelines reproduce the 1995 Guidelines on the documentation issues.

- vi) Tax administrations should try to **rely on exchange of information provisions** of tax treaties to the extent possible, especially in relation to information not readily available to the taxpayer.

Of course it is recognised that most non-OECD

iii)

	<p>whose transactions directly or indirectly affect the pricing of the related party dealings</p> <ul style="list-style-type: none"> • A description of taxpayer's worldwide organizational structure (including an organization chart) covering all associated enterprises engaged in transactions potentially relevant to determining an arm's length price for the documented transactions
<p>Nature of the business/industry and market conditions</p>	<ul style="list-style-type: none"> • An outline of the business including a relevant recent history of the taxpayer, the industries operated in, the general economic and legal issues affecting the business and industry, and the taxpayer's business lines • The corporate business plans to the extent they give an insight into the nature and purpose of the relevant transactions between the associated enterprises • A description of internal procedures and controls in place at the time of the related party dealings • Analysis of the economic and legal factors that affect the pricing of taxpayer's property and services • A description of the structure, intensity and dynamics of the relevant competitive environment(s) • A description of intangible property potentially relevant to the pricing of the taxpayer's property or services in the controlled transactions • Copies of annual reports and financial statements for the year to which the Package relates and the prior five years • Information as to the functions performed, assets employed and risks assumed relevant to the transactions • An explanation of capital relationships (e.g., balance and source of debt and equity funding) relevant to the transactions
<p>Controlled transactions</p>	<ul style="list-style-type: none"> • A description of the controlled transactions that identifies the property or services to which the transaction relates and any intangible rights or property attached thereto, the participants, the scope, timing, frequency of, type, and value of the controlled transactions (including all relevant related party dealings in relevant geographic markets), as well as the currency of the

	<p>transactions, and the terms and conditions of the transactions and their relationship to the terms and conditions of each other transaction entered into between the participants</p> <ul style="list-style-type: none"> • Identification of internal data relating to the controlled transactions • Copies of all relevant inter-company agreements
<p>Assumptions, strategies, policies</p>	<ul style="list-style-type: none"> • Relevant information regarding business strategies and special circumstances at issue, for example, set-off transactions, market share strategies, distribution channel selection and management strategies that influenced the determination of transfer prices • If the taxpayer pursues a market share strategy, documentation demonstrating that appropriate analysis was done prior to implementing the strategy, that the strategy is pursued only for a reasonable period, and that the costs borne by each associated enterprise are proportionate to projected benefits to such enterprise • Assumptions and information regarding factors that influenced the setting of prices or the establishment of any pricing policies for the taxpayer and the related party group as a whole

Cost contribution arrangements (CCA)³

- A copy of the CCA agreement that is contemporaneous with its formation (and any revision) and any other agreements relating to the application of the CCA between the CCA participants
- A list of the arrangement's participants, and any other associated enterprises that will benefit from the CCA
- The extent of the use of CCA property by associated enterprises which are not CCA participants, including the amounts of consideration paid or payable by these non-participants for use of the CCA property
-

intended to be developed

- A description of each participant's interest in the results of the CCA activities
- The duration of the arrangement
- Procedures for and consequences of a participant entering or withdrawing from the agreement (i.e., buy-in and buy-out payments) and for the modification or termination of the agreement
- The total amount of contributions incurred pursuant to the

	<ul style="list-style-type: none">• Extension of the analysis over a number of years with reasons for the years chosen, where relevant
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information and (ii) a country-specific file of standardized information for each EU member country in which the taxpayer has related-party transactions.

Centralizing and standardizing documentation for centralized MNE groups is very likely to reduce their compliance burdens. The Code itself does not itself require contemporaneous documentation but, in practice, files should be prepared contemporaneously if a national law mandates contemporaneous documentation.

An EU Member State may decide not to require TP documentation at all or to require a shorter version of the EU transfer pricing documentation, i.e. require fewer items in the master file or the country specific documentation. However, a Member State should not require *more* items in the master file or the country specific documentation.

The Code also provides that translation to other languages would only be provided upon request and translation should not be required unless necessary in the circumstances. The Code seems particularly to deter countries from seeking translation of the Master File. The code also provides that EU member countries should not reject comparables found in pan-European databases automatically. Therefore, the use of non-domestic comparables by itself should not subject the taxpayer to penalties for non-compliance.

The “Master file” provides a “blue print” of the company and its transfer pricing system that would be relevant for all EU Member States concerned. The Master file should contain

III. Practical Guidance on Documentation Rules and Procedures

1. Burden of proof

In most countries, the tax administration bears the burden of proof with respect to tax assessments unless a tax law specifically provides otherwise. It means that, in general situations, taxpayers need not prove the correctness of their transfer pricing or transactional margin unless the tax administration challenges taxpayers with concrete and clear grounds for such challenges.

However, if one country has a set of specific documentation rules in its tax law or regulations, it is generally understood that the burden of proof for the transfer price at which a taxpayer transfers good or services with his/her related parties falls on the taxpayer unless the taxpayer is believed to have fulfilled the obligations imposed by such documentation rules. Even where the burden of proof rests on the tax administration, the tax administration might still require the taxpayer to provide documentation about its transfer pricing, because without adequate documentation, the tax administration cannot assess the case properly. In fact, where the taxpayer does not provide adequate documentation, there may be a shifting of burden of proof in some countries in the manner of a rebu

- Prepare information at the time of the transactions, to be submitted at the time of the filing;
- Prepare information at the time of the transactions, to be submitted upon request in case of an audit;
- Prepare information at the time of the filing;
- Prepare information only if requested upon audit; or
- No documentation requirement.

As paragraphs 3.69-3.71 of the 2010 OECD TP Guidelines state, taxpayers, in some cases, establish transfer pricing documentation to demonstrate that they have made reasonable efforts to comply with the arm's length principle at the time their intra-group transactions were undertaken (hereinafter "the arm's length price-setting" approach), based on information that was reasonably available to them at that point. Such information includes not only information on comparable transactions from previous years, but also information on economic and market changes that may have occurred between those previous years and the year of the controlled transaction. In other instances, taxpayers might test the actual outcome of their controlled transactions to demonstrate that the conditions of these transactions were consistent with the arm's length principle (hereinafter "the arm's length outcome-testing" approach). Such test typically takes place as part of the process for establishing the tax return at the end of a tax year.

A country that wishes to establish a TP documentation rule, especially so-called "contemporaneous documentation requirements" in its TP regime, should take into account that there exist the two pricing approaches mentioned in the previous paragraph and that, when a taxpayer opts for the arm's length *outcome*-testing approach, data for external comparables are often not readily available by the year-end or by the due date of the tax return filing.

Perhaps for this reason, and because the tax authorities will not be seeking such documentation at the time of the transfer pricing, the OECD TP Guidelines do not require contemporaneous *presentation* of documentation to the tax authorities, or that they be fully ready to present to the documents at that time (Paragraph 5.4). The document storage

The basis for this is that at the time of filing, no particular transaction has been identified for transfer pricing review and that all that is needed at that stage is enough information to know if a further examination is needed of particular taxpayers.

The guidelines note that it would be quite burdensome if detailed documentation were required at this stage on all cross-border transactions between associated enterprises, and by all enterprises engaging in such transactions. Therefore, it would be unreasonable to require the taxpayer to submit documents with the tax return specifically demonstrating the appropriateness of all transfer price determinations.

In practice, most countries *either* do not require the submission of transfer pricing related information at all *or* require only a minimum level of information at the tax return filing stage. The **PATA Documentation Package** noted above indirectly encourages contemporaneous

France has issued guidance for SMEs, with the effect that the mandatory TP documentation requirements in the legislative proposal will only apply to large enterprises. Thus, SMEs should only undertake TP documentation upon a specific request of the French tax authorities (FTA) in the course of a tax audit. In principle, such requests may occur only under

- Entities within the coverage period of an APA; or
- Entities with less than 50% foreign invested shares that only have transactions with domestic related parties.

Korea

The method used and the reason for adopting that particular one for an arm’s length principle determination must be disclosed to the tax authorities by a taxpayer in a report submitted along with the annual tax return. This is not the case, however, if the total value of cross-border transactions of goods and that of cross-border transactions of services of the taxpayer for the taxable year concerned is Korean Won (KRW⁸) 5 billion or less and KRW 500 million or less, respectively. The above obligation is also exempt for the taxpayer whose inter-company transaction volume per an overseas related party is KRW 1 billion or less for goods and KRW 100 million or less for services.

In summary, some countries have particular legislative provisions that allow exemptions from the obligation for TP documentation or submission of documents to tax authorities at the time of filing tax returns. However, some countries allow similar exceptions by an administrative measure notwithstanding the lack of any specific legislation granting such exceptions. In some countries, exemptions or mitigation of TP documentation obligation are targeted to SMEs directly. However, a number of countries operate such exemption or mitigation regime mainly targeting taxpayers whose turnover is less than 1 billion USD (or 1 billion EUR) or less.

commonly understood language in the Member States concerned and that translations of the master file be made available only if strictly necessary and upon specific request.

According to a country survey,⁹ most countries require taxpayers to present TP documentation in their own languages and require translation if the TP documentation was prepared in a different language. However, some countries such as France, Germany, Netherlands and Korea allow present TP documentation in a language other than their own languages as least on an exceptional basis. It is particularly common in practice to allow documentation to be provided in English.

The recent Egyptian TP guidelines¹⁰ provide that if documents are provided other than in Arabic, the taxpayer may be required to bear the cost of an official translation.

[It would be useful to have more developing country examples here – Secretariat Note]

[Perhaps there should be a distinct heading on whether copies need to (i) be provided in electronic form, and whether (ii) they should be required to be as readily searchable as the electronic copies held by the enterprise, i.e. in readable pdf form rather than scanned without optical character recognition, although the level of detail in (ii) may be unnecessary – Secretariat Note]

[On a related point, one of the characteristics of TP documentation is its size and complexity – perhaps some guidance can be given on general document handling, tracking, evidential, searching and access issues for large TP “files” – i.e. document management for large and complex files.- Secretariat Note]

6. Information to be included in the TP documentation

In preparing TP documentation, MNEs must decide the type and scope of documentation and information that should be provided to tax authorities to meet various documentation requirements and avoid any tax adjustments and penalties, while at the same time minimizing added burdens and potential tax exposure in the event of a tax controversy.

documentation required depends on the specific facts and circumstances of each case and the TP regime applicable in a country. Neverthe

Where a taxpayer concludes that no comparable data exists or that the cost of locating the comparable data would be disproportionately high relative to the amount at issue, reasons for such conclusion should be duly explained together with supporting documentation. Special circumstances would include details concerning any intentional set-off transactions that have an effect on determining the arm's length price. In such a case, documentation may be necessary to help describe the relevant facts, the qualitative, th

description of how the value of contributions is determined and how accounting principles are applied consistently to all participants.

Annex 1: Examples of Country Rules on Documentation

1. Korea¹¹

A. Reporting of the method of determining an arm's length price to the tax authorities

- A taxpayer should select the most reasonable method of determining an arm's length price in accordance with the criteria provided in the legislation and report the selected method and the reason for the selection to the district tax office at the time of filing a tax return.
- When filing the tax return, the taxpayer entering into an international transaction with a related party overseas should submit to the district tax office a detailed statement of the international transaction specified in the Ministerial decree (Form No.8) together with the simplified profit and loss statements or financial statements of the overseas related party.
-

10. Ownership relations among the related parties;
11. Forms or items not submitted to the district tax office in filing tax return;
12. Other data necessary for computing an arm's length price.

- The above data must be prepared and submitted in Korean. However, they can be prepared and submitted in English if tax authorities permit it.
- A taxpayer who is requested to submit information should submit such information within 60 days of the date the request is received. However, if the taxpayer files an

2. Business organizational chart (illustrating related parties to which TP may be applicable)
 3. Documents illustrating the process by which the applied TP method was selected:
 - i. Economic analysis and projections that served as the basis for selecting the particular TP method;
 - ii. Documents describing the details of adjustments made in determining the arm's length price range using comparables' data;
 - iii. Alternative TP methods and the reasons for which those were not selected;
 - iv. Relevant documents concerning the time period from the end of the taxable period until the filing of the tax returns.
- Criteria applied in determining the above mentioned "reasonableness" are as follows
1. With the end of the concerned taxable period as the basis, whether the collected data on the comparables are adequately representative. Particularly, it should be examined whether an omission of data of a certain comparable led to an outcome advantageous to the taxpayer;
 2. Whether the selection and application of the concerned TP method is supported by systematic analysis of the collected data.
 3. If a certain TP method was agreed upon through an APA process in a prior taxable year or was selected by the tax authorities during an audit, whether there are reasonable grounds for applying or not applying the

2. India

A. Documentation to be Maintained

- Sec. 92D of the Finance Act read with Rule 10D(1) of the Income Tax (IT) Rules lays down thirteen different types of information / documents that a person, entering into international transactions with associated enterprise(s), is required to maintain. Broadly, these information / documents can be classified as:
 - Enterprise-wise documents;
 - Transaction-specific documents; and
 - Computation related documents.

B. Enterprise-wise documents

- These documents describe the enterprise, the relationship with other associated enterprises, nature of business carried out, etc. This information is largely descriptive [Clauses (a) to (c) of Rule 10D(1) of the IT Rules]. An illustrative list of information / documents to be maintained under this classification is provided below.
 - Ownership / shareholding pattern of the taxpayer;
 - Business profile of the multinational group;
 - Details of associated enterprise(s) with whom international transactions are entered into;
 - Business of the taxpayer and the associated enterprise(s); and
 - Broad industry profile in which the taxpayer operates.
- The above documentation would provide the tax authorities with the preliminary information of the taxpayer's group profile, function in the group and the industry in which it operates. The broad industry profile, if well documented, will provide the tax authorities with an overview of the demand and the business drivers within the industry as well as the taxpayer's position in the industry. The documentation can also provide an overview of the taxpayer's growth objectives, given the evaluation of the industry sector and the competitive dynamics within industry in which the taxpayer operates.

C. Transaction-specific documents

- These documents explain each international transaction in detail e.g. the nature and terms of contracts, description of the functions performed, assets employed and risks assumed by each party to the transaction, economic and market analyses, etc. [Clauses (d) to (h) of

Rule 10D(1) of the IT Rules]. An illustrative list of information/ documents to be maintained under this classification is provided below.

- Details of each international transaction e.g. name of the associated enterprise,

- These documents detail the methods considered, actual working assumptions, adjustments made to the transfer prices and any other relevant information / data relied for determining the ALP [**Clauses (i) to (m) of Rule 10D(1) of the IT Rules**].
- An illustrative list of information / documents to be maintained under this classification is provided below.
 - Nature of each international transaction and the rationale for selecting the most appropriate method for each international transaction. The taxpayer is required to substantiate the selection by proper documentation and the manner in which the method was applied to each international transaction;
 - Actual working / computation of the arm length's price i.e. recording the calculations i.e. comparability analysis performed to determine whether or not uncontrolled transactions are comparable to the international transactions with reasons for adjustments made to make the comparability analysis more reliable.
 - Critical factors and assumptions influencing the determination of the ALP;
 - Adjustments made (along with reasons) to the taxpayer's transfer prices so as to align it with ALPs; and
 - Any other information relevant for the determination of the ALP

-One of the aspects of documentation is to capture the group policies and the pricing methodology of the international transaction. For instance, pricing methodology could be either on cost plus mark-up basis, percentage on sales basis, bilateral negotiations basis, etc to appropriately substantiate the arms length nature of the transaction.

E. Contemporaneous documentation

- Rule 10D(4) of the IT Rules require that the information and documents maintained by an taxpayer to demonstrate that the transaction price meets with the arm's length principle should be contemporaneous to the extent possible and should exist latest by the due date for filing the return of income.
- A question that arises is what is meant by contemporaneous documentation. The Oxford Dictionary defines the term 'contemporaneous' as '*Existing or occurring in the same period of time*'. Possibly, the contemporaneous documentation can be the one that -
 - exists or brought into existence at the time (by the due date for filing the return of income) the taxpayer is developing or implementing any arrangement that might raise transfer pricing issues; and

- records all relevant information that was necessary for the management to make transfer pricing decisions. The documentation may be electronic or in written form, which includes books, records, contracts, studies, periodic activity reports, budgets, plans, projections, analysis, conclusion and other material.
- Further, contemporaneous documentation maintained could have the following characteristics:
 - Completeness;
 - Accuracy i.e. true and proper information; and
 - Timeliness - information is maintained as and when the international transactions take place. This may not always be possible to comply with, e.g., when subsequent benchmarking under the TNMM alone would show whether or not the international transactions have been carried out at prices which have yielded an arm's length margin.
- Transfer pricing documentation is generated at various stages. For example, there could

be minutes of meeting / telephone calls, detailed description of the benefits received demonstrated by way of correspondences, memoranda, manuals, etc. Further, a certificate from an independent accountant of the service providing entity may be obtained certifying the method of allocation of costs and authenticity of the cost apportioned to each entity. It may also be beneficial to document that the services could not have been rendered internally (by the service recipient) or by third parties.

Annex 2: Sample TP Study - International Chamber of Commerce (2008)



Sample Documentation Package

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Executive Summary

1. Introduction

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 5
 Author: *John Doe* Annex 6

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 7
 Author: *John Doe* Annex 8

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 9
 Author: *John Doe* Annex 10

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 11
 Author: *John Doe* Annex 12

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 13
 Author: *John Doe* Annex 14

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 15
 Author: *John Doe* Annex 16

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 17
 Author: *John Doe* Annex 18

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 19
 Author: *John Doe* Annex 20

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 21
 Author: *John Doe* Annex 22

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 23
 Author: *John Doe* Annex 24

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 25
 Author: *John Doe* Annex 26

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 27
 Author: *John Doe* Annex 28

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 29
 Author: *John Doe* Annex 30

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 31
 Author: *John Doe* Annex 32

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 33
 Author: *John Doe* Annex 34

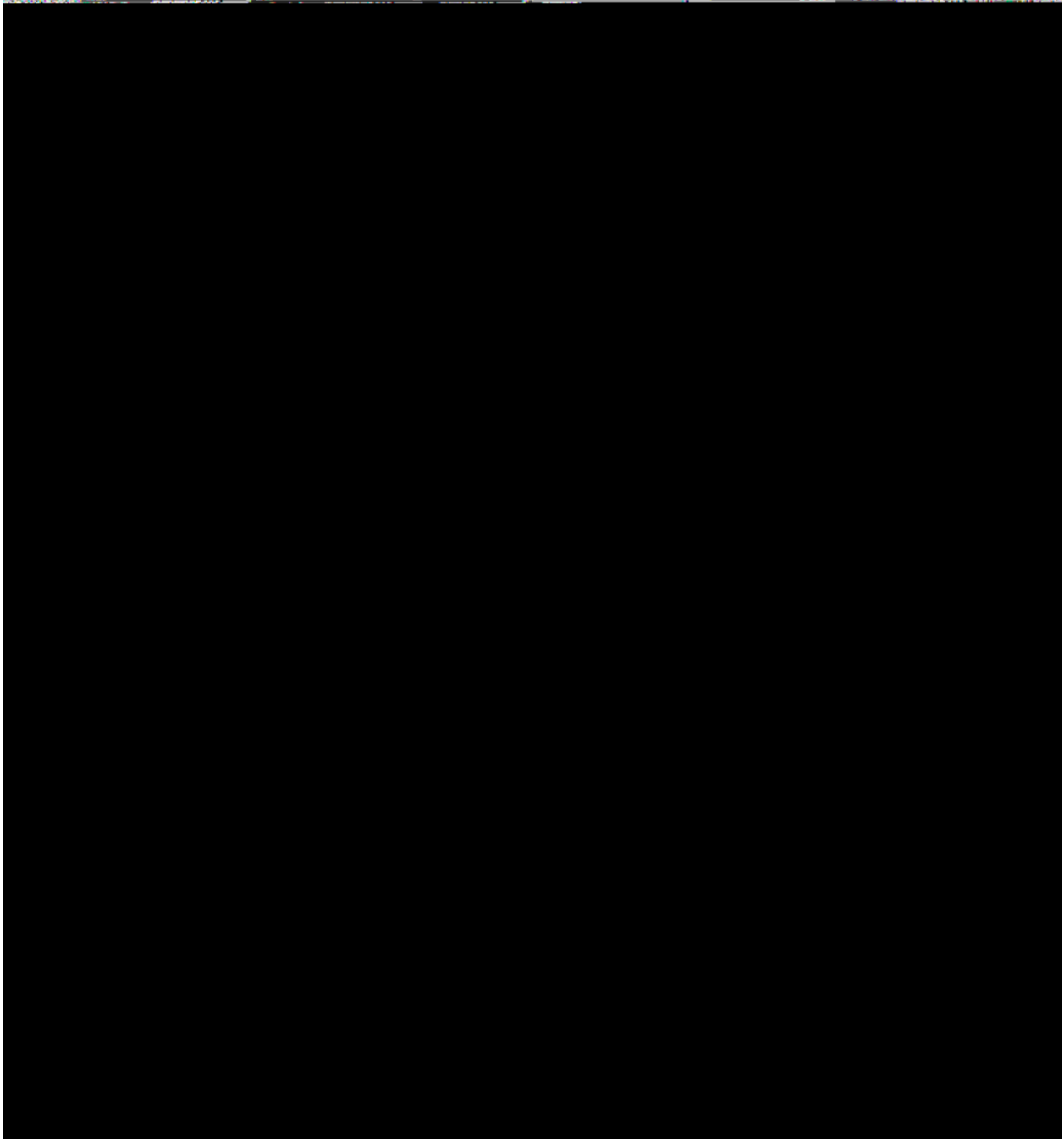
Title: *Chang's Impact on the Environment and the Role of the Government* Annex 35
 Author: *John Doe* Annex 36

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 37
 Author: *John Doe* Annex 38

Title: *Chang's Impact on the Environment and the Role of the Government* Annex 39
 Author: *John Doe* Annex 40

Division Requirements in 2012 and 2013 | OECD Transfer Pricing Guidelines

documentation in support of the related party subsidiaries (collectively the "Company"). This report compiles the transfer pricing documentation between Parent Company and its





1. Related Party Transactions

During 20XX, the Company had related party transactions of approximately XXX

(refer to Annex 4).

D) Functional Analysis.

to and functions is attached as Annex 5. In

A chart summarizing the Company's rd

where necessary, as well as the operations of the Company and its subsidiaries, the Company and its subsidiaries have been

attached as Annex 6.

E) Transfer Pricing

1. Background.

to prescribe specified methodologies for determining the amount of transfer of tangible property, intangible property, services, and

The OECD Guideline length terms for their control. In more cases

of the OECD Guidelines as a result of the OECD Guidelines.

be determined with the best method under the circumstances, provided that the method is the best method.

the profit split of the

provide that, in the vast majority of cases, the "transactional profit methods" (i.e.,

which method is the best method

paragraph 8 of the Transfer Pricing Report addresses

which method is the best method

paragraph 8 of the Transfer Pricing Report addresses

2. Transfer Pricing Method

The OECD Guidelines provide

The OECD Guidelines provide

the best method is the best method

the best method is the best method

the best method is the best method

the best method is the best method

the best method is the best method

the best method is the best method

¹ OECD Guidelines ¶ 1.68.
³ OECD Guidelines ¶¶ 2.49 and
⁴ OECD Guidelines ¶ 3.1.

...reasonableness of the transfer pricing associated with the intercompany transactions between and among the Company and its foreign affiliates and documents the reasons for a refusal to accept the proposed transfer pricing.

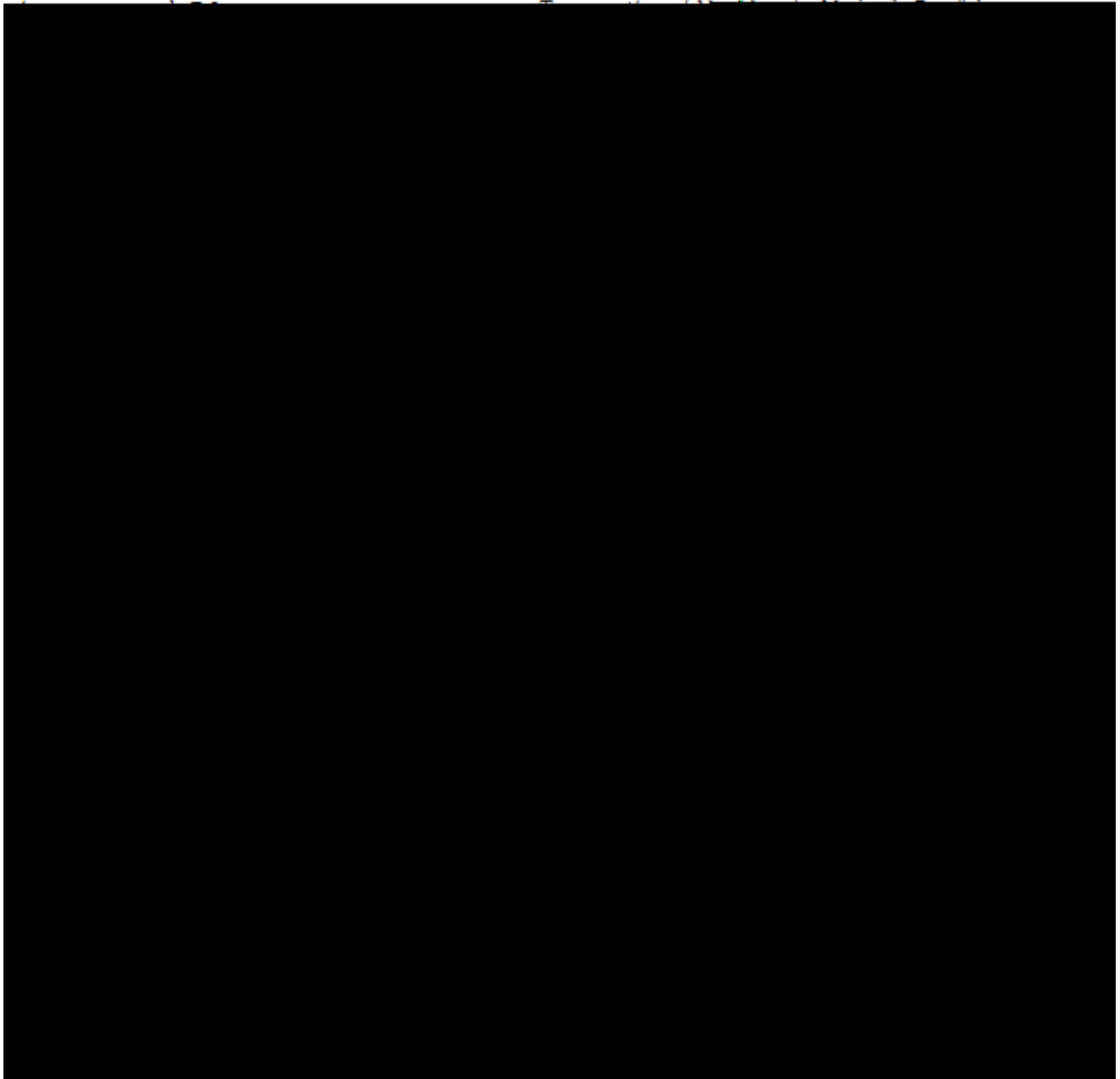


Reasons for Rejection	Method
... Add brief explanation for rejection.	Cost Plus Method
... Add brief explanation for rejection.	Transactional Net Mar
... Add brief explanation for rejection.	Direct Cost

the CUP method involves a direct comparison of related party prices with arm's length prices. Since the prices are CUP, they are not subject to the same level of scrutiny as arm's length prices. The CUP method is not subject to the same level of scrutiny as arm's length prices. Consequently, the CUP method was not selected as the best method for analyzing the related party transactions.

description similar to paragraph E.3.a.

Resale Price Method. Brief description similar to paragraph E.3.a.





Conclusion

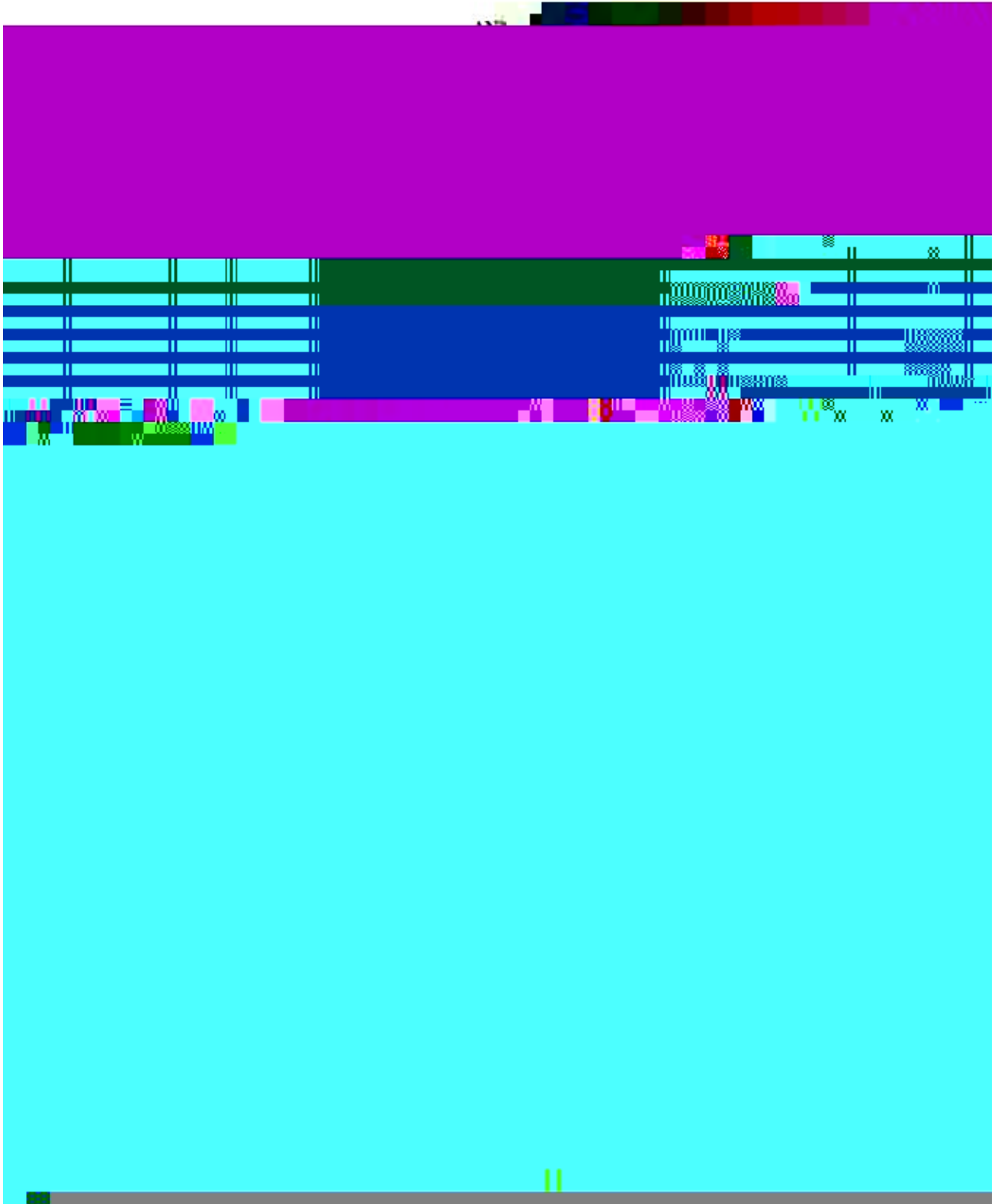
and documentation provided by the
sactions comply with the arm's length
principle under the OECD Guidelines and the

Based on the review of the financial informatio
Company, we conclude that all related party tr
principle under the OECD Guidelines and the

Transfer Pricing Requirements

Local Co

1. Transfer Pricing Policy	A. Local Country
2. Economic substance	B. Economic substance
3. Transfer Pricing Penalties	C. Transfer Pricing Penalties
4. Analysis and Conclusions	D. Analysis and Conclusions





ANNEX 5

Risk-Function Summary			
Risk-Function summary			
	Company 1	Company 2	Company 3
Name of Company	SCA	SGM	SUK
Country of Residence	Canada	Germany	



ANNEX 8

SAMPLE INC						
FOREIGN COUNTRY						
12/31/XX						
TYPE OF ENTITY	GLOBAL		DIST	DIST		

