Simplifying transfer pricing record keeping

We conduct transfer pricing reviews as part of broader risk reviews of businesses under our compliance program. Documenting your transfer pricing:

- is important for demonstrating your compliance with Australia’s transfer pricing rules
- can be costly, particularly for smaller businesses.
- We have developed some simplified transfer pricing record keeping options so that certain eligible businesses can opt to minimise some of their record-keeping and compliance costs.

This information explains:

- transfer pricing record-keeping options
  - small business taxpayers
  - distributors
  - intra-group services
  - low level loans
  - specific criteria that need to be met for a business to opt in
  - disclosing within the international dealing schedule the selection and application of an option
  - providing evidence of the applicability of the eligibility criteria to your circumstances if you are using any of the simplified record-keeping options
  - that relevant dealings will not be subject to a review once an option is selected and disclosed
  - that options will be available for a three-year period.

Background

- Last modified: 06 Mar 2015
- QC 43562

Transfer pricing rules aim to ensure that the amount brought to tax in Australia from cross-border dealings between entities is consistent with that of an independent entity dealing wholly independently with others and is determined through the application of the arm’s length principle.

For income tax years starting on or after 29 June 2013, new transfer pricing rules apply to international related party dealings (IRPD) including Subdivision 284-E of Schedule 1 to the TAA 1953 containing rules about transfer pricing documentation. Documenting your transfer pricing for IRPD, assists you to demonstrate that your transfer pricing treatment was consistent with the arm’s length principle at that time.

While the 284-E requirements do not mandate the preparation or keeping of documentation, the consequence of not meeting the requirements is that in determining the administrative penalty for any transfer pricing benefit and tax shortfall there is a presumption that you have an undocumented transfer pricing treatment which is not reasonably arguable and a higher base penalty amount will apply.

Documenting your transfer pricing in a way that meets all of the requirements of Subdivision 284-E may impose an administrative burden on you that is disproportionate to your risk of not complying with the transfer pricing rules. By disclosing your eligibility and selection of a simplified record-keeping option, the costs and certainty concerns associated with documenting your transfer pricing treatment can be mitigated.

If you or the character, type, value and quantity of your affected transactions meet the stipulated criteria for one or more of the options, you may choose to disclose you have...

applied the options for simplifying your transfer pricing record keeping for the relevant dealing or dealings. Having demonstrated the applicability of the options through meeting the specified eligibility criteria, you will be considered as likely posing a low risk of not complying with the transfer pricing rules. The record-keeping requirements for you under these circumstances would relate to the general requirements (s.262A of the *Income Tax Assessment Act* 1936), together with evidence of the applicability of the relevant eligibility criteria.

In selecting an option you need to inform us of your selection through a disclosure on your International Dealings Schedule. If you are eligible, we will not allocate compliance resources or take other compliance action to examine your transfer pricing records the subject of the disclosed option. We accept that you take your self-assessment obligations to prepare and retain adequate records seriously, and acknowledge that your choice to apply and disclose a simplified option demonstrates your willingness to comply. The selection of an option does not limit or waive the operation of the law but demonstrates that you have self-assessed your compliance with the transfer pricing rules.

These options will be introduced for an initial period of three years, over which time their use will be carefully monitored by us. We will also undertake a review of the results of adopting these simplified approaches.

### Small taxpayers

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#### Eligibility criteria

If you meet the following criteria you are eligible to apply the small taxpayers’ simplified record-keeping option to your international related party dealings. The criteria are:

- your turnover for the year is between $0 and $25 million for the [Australian economic group](#)

and you

- have not derived [sustained losses](#)
- do not have related-party dealings with entities in the [specified countries](#)
- have not undergone a [restructure](#) within the year
- do not have related-party dealings involving royalties, licence fees, or research and development arrangements
- do not have [specified service related-party dealings](#) (either as expenses or as income) greater than 15% of your turnover
- are not a distributor (if you are, refer to the [distributors](#) section to determine if you are eligible)
- have assessed your compliance with the transfer pricing rules.

This option does not apply to:

- international related-party financial transactions (for example, loans and guarantees) and associated charges
- international related-party dealings of a capital nature.

#### Examples

**Example: Small taxpayers – meeting the criteria**

Australco is a subsidiary of Kenspire, a UK company. For the 2015 financial year, Australco has a turnover of $17 million and a taxable income of $1.1 million and there were no restructures. Australco is the only member of the Australian economic group. It has paid Kenspire $2 million for administrative support and has no other international related-party dealings.

Australco meets the eligibility criteria for the small taxpayers’ record-keeping option and can elect to apply it to its purchases from Kenspire.

**Example: Small taxpayers – not meeting the criteria**

Australco is a subsidiary of Kenspire, a UK company. For the 2015 financial year, Australco has a turnover of $17 million and a taxable income of $1.1 million and there were no restructures. Australco is the only member of the Australian economic group. It has paid Kenspire $3 million for marketing and media strategies and has also paid $1 million royalties to Manx, a company registered in the Isle of Man and a subsidiary of Kenspire.

Australco neither meets the specified countries nor the specific international related party dealings criteria. All criteria need to be met to be eligible therefore Australco cannot use the small taxpayers’ simplified record-keeping option.

### Distributors

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#### Eligibility criteria

If you meet the following criteria you are eligible to apply the distributors’ simplified record-keeping option to your international related-party dealings. The criteria are:

- you are a distributor with turnover between $0 and $50 million for the [Australian economic group](#)
and you
- have not derived sustained losses
- do not have related-party dealings with entities in specified countries
- have not undergone a restructure within the year
- do not have related-party dealings involving royalties, licence fees or research and development arrangements
- do not have a profit-before-tax ratio of less than 3%
- have assessed your compliance with the transfer pricing rules.

This option does not apply to:
- international related-party financial transactions (for example, loans and guarantees) and associated charges
- international related-party dealings of a capital nature.

Examples

Example: Distributors – meeting the criteria
Gusco is a wholesale business and an Australian subsidiary of Falkenhagen, a German company. For the 2015 financial year, Gusco has a turnover of $47 million and a taxable income of $2.6 million with a 6% weighted average profit before tax ratio. It has purchased stock from Falkenhagen of $38 million and has no other related-party dealings. There were no restructures and Gusco is the only member of the Australian economic group.

Gusco meets the eligibility criteria for the distributors’ record-keeping option and can elect to apply it to its purchases from Falkenhagen.

Example: Distributors – not meeting the criteria
Kelco is an Australian subsidiary of Britai, a UK company. For the 2015 financial year, Kelco has a turnover of $49 million and a taxable income of $1.1 million with a 2.6% weighted average profit before tax ratio. It has purchased stock from Britai of $38 million and has also paid $1 million royalties to Jerri, a company registered in Jersey and a subsidiary of Britai. There were no restructures and Kelco is the only member of the Australian economic group.

Kelco neither meets the specified countries nor the specific related-party dealings nor the profit-before-tax ratio criteria. All criteria need to be met to be eligible, therefore Kelco cannot use the distributors’ simplified record-keeping option.

Intra-group services

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Eligibility criteria

If you meet the following criteria you are eligible to apply the intra-group services’ simplified record-keeping option to your appropriate international service related-party dealings. The criteria are:

- you have international related-party service dealings of either:
  - $1 million or less – the de minimis rule
  - greater than $1 million, but for services you
    - receive, the total amount charged to you must not be more than 15% of the total expenses of the Australian economic group
    - provide, the total amount derived by you must not be more than 15% of the total revenue of the Australian economic group.

And you:

- have not derived sustained losses
- do not have related-party dealings with entities in specified countries
- have not undergone a restructure within the year
- do not have specified service related-party dealings
- have a mark-up on costs of the relevant services of either
  - 7.5% or less for services you receive
  - 7.5% or more for services you provide

This option does not apply to:

- other international related-party dealings
- international related-party financial transactions (for example, loans and guarantees) and associated charges
- international related-party dealings of a capital nature.
Examples

Example: Intra-group services – meeting the de minimis rule
Victas is a subsidiary of Nevadaplus, an American company, and in the 2015 year paid $850,000 for management and administration services and $20 million for stock purchases. Victas was charged on a 7.1% mark-up for the management and administration services it received. In the 2015 year it had total expenses of $42 million and a taxable income of $11 million. Victas had no other related-party dealings and there were no restructures during that time. Victas is the only member of the Australian economic group.

Victas meets the eligibility criteria for the intra-group services simplified record-keeping option and can elect to apply it to its management and administration services from Nevadaplus.

Example: Intra-group services – meeting the 15% of dealings rule
Victas is a subsidiary of Nevadaplus, an American company, and for the 2015 year paid Nevadaplus:

- $850,000 in management and administration services
- $970,000 for training services, and
- $20 million for stock purchases.

Victas was charged on a 7.1% mark-up for the services from Nevadaplus.

In the 2015 year Victas had total expenses of $42 million and a taxable income of $11M. It had no other related-party dealings nor did it undertake any restructures during that time. Victas is the only member of the Australian economic group.

Whilst Victas does not satisfy the de minimis rule (because total services are $1.82 million) the services are less than 15% of its total expenses (being 4.3%). As all the other eligibility criteria for the intra group services simplified record keeping option have been met Victas can elect to apply the option to its services from Nevadaplus.

Example: Intra-group services – not meeting the de minimis and 15% of dealings rules
Holdal is the only Australian subsidiary of Gottlund, a Swedish company, and for the 2014 year Holdal paid Gottlund:

- $8 million in management and administration services
- $1 million for training services, and
- $23M for stock purchases.

Holdal's payment included a 7.4% mark-up on the services from Gottlund. In the 2014 year, Holdal had total expenses of $50 million and a taxable income of $15 million. Holdal had no other related-party dealings and there were no restructures for the year. Holdal is the only member of the Australian economic group.

Holdal did not satisfy the de minimis rule (because it had total services of $9 million) and as the services are over 15% of total expenses (services being 18% of total expenses) it cannot elect to apply the intra-group services simplified record-keeping option.

Example: Intra group services– not meeting the de minimis rule
Richoil is the only Australian subsidiary of Bascon, a Canadian company, and for the 2015 year Richoil paid Bascon

- $6.2 million in management and administration services
- $1.7 million for research and development services
- $62 million for stock purchases.

Richoil was charged a 7.4% mark-up for its services from Bascon.

In 2015 year Richoil had total expenses of $80 million and a taxable income of $20 million. Richoil had no other related-party dealings nor were there any restructures. Richoil is the only member of the Australian economic group.

Richoil does not satisfy the de minimis rule (because its total services are $7.9 million) but the services are less than 15% of total expenses (services being 9.88% of total expenses) and may be able to apply the intra-group services record-keeping option.

However, Richoil does not meet the specific services related-party dealings criterion. All criteria need to be met to be eligible therefore Richoil cannot apply the intra-group services simplified record-keeping option.

Low-level loans

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Eligibility criteria

If you meet the following criteria you are eligible to apply the low-level loans’ simplified record-keeping option to your inbound, international related-party interest-bearing loans and associated expenses. The criteria are:

- you have a combined cross-border loan balance of $50 million or less for the Australian economic group at all times throughout the financial year

and

- you have not derived sustained losses
- you do not have related-party dealings with entities in specified countries
- you have not undergone a restructure within the year
- for your inbound loans:
  - your interest rate is no more than the Reserve Bank of Australia (RBA) indicator lending rate for ‘small business; variable; residential-secured; term’
  - the funds actually provided to you under the loan are Australian dollar funds and this is reflected in your loan agreements
  - your associated expenses are paid in Australian dollars
- you have assessed your compliance with the transfer pricing rules.

This option does not apply to:

- outbound related-party interest-bearing loans and associated charges
- other international related-party financial transactions (for example, guarantees) and associated charges
- other international related-party dealings
- international related-party dealings of a capital nature.

Find out more


Examples

Example: Low-level loan – meeting the criteria

Victas is an Australian subsidiary of Nevadaplus, an American company from which it borrowed A$10 million with the interest charged being A$350,000 per annum or 3.5% of the principal. For the 2015 financial year, Victas had a taxable income of $11 million, no other related-party dealings and there had been no restructures. Victas is the only member of the Australian economic group.

RBA published an indicator interest rate of 7.1%, which is the maximum rate to be eligible to use the low-level loans simplified record-keeping option.

Victas meets the eligibility criteria for this simplified record-keeping option and can elect to apply it to its interest-bearing loan and interest paid to Nevadaplus.

Example: Low-level loan – not meeting the criteria

Australco is an Australian subsidiary of Kenspire, a UK company from which it borrowed A$11 million with the interest charged being A$350,000 per annum or 8.5% of the principal. It also made an interest-free loan of $40 million to Choc, a Swiss entity. For the 2015 financial year, Australco has a taxable income of $2.6 million. Other than stock purchases of $38 million from Kenspire, Australco has no other related-party dealings. There has been no restructures and Australco is the only member of the Australian economic group.

RBA published an indicator interest rate of 7.1%, which is the maximum rate to be eligible to use the low-level loans simplified record-keeping option.

Australco neither meets the combined loan balance nor the interest rate criterion. All criteria need to be met to be eligible therefore Australco cannot use the low-level loans simplified record-keeping option.

Example: Low-level loan – not meeting the specified interest rate rule

Victas is an Australian subsidiary of Nevadaplus, an American company from which it borrowed A$10 million at an annual interest rate of BBSW + 5%. This equated to an interest payment of A$760,000 for the 2015 year or 7.6%. For the 2015 financial year, Victas had a taxable income of $11 million and no other related-party dealings. There has been no restructures and Victas is the only member of the Australian economic group.

RBA published an indicator interest rate of 7.1%, which is the maximum rate to be eligible to use the low-level loans simplified record-keeping option.

Given the effective interest rate paid in 2015 was higher than 7.1%, Victas does not meet the specified interest rate criterion. All criteria need to be met to be eligible, therefore Victas cannot apply the low-level loans simplified record-keeping option.
Compliance assurance

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Consistent with the ATO's intent to concentrate our efforts on international related-party dealings that pose the highest risk of not complying with the transfer pricing rules, we also understand that many of you who undertake these dealings want to comply and want to best evidence how you have complied by preparing and maintaining the right level of records to best explain your transfer pricing treatment.

We accept that you take yourself assessment obligations to prepare and retain adequate records seriously. Simplifying transfer pricing record keeping by providing options for you to apply to your relevant dealings where eligible does not limit or waive the operation of the law, but acknowledges that your choice to apply and disclose a simplified option demonstrates your willingness to comply and thereby mitigates your costs of compliance. The selection of an option confirms that you have assessed your compliance with the transfer pricing rules.

Should you self-assess as eligible for one or more of the simplification record-keeping options, we will not allocate compliance resources or take other compliance action to examine your transfer pricing records relevant to the option selected.

This assurance applies for three income years starting from 29 June 2013.

International dealings schedule

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You must complete and lodge an International Dealings Schedule (IDS) with your annual income tax return if you have more than $2 million of related-party dealings. Under self-assessment, you must disclose the value of those transactions and answer questions about the nature of the transactions, the pricing methodology selected and the level of dealings, and keep sufficient documentation.

If you are eligible to apply a simplified record-keeping option then at the relevant labels on the IDS you would include code 7 at the percentage of documentation label code. This confirms that you have assessed your situation as complying with the transfer pricing rules and advised us that a simplification option has been applied to your record keeping.

This code is not available for the 2014 year. If you are contacted and you have applied one of the options you will need to notify the compliance officer of your eligibility.

Definitions

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**Australian economic group**

For the purposes of the simplified record-keeping options for transfer pricing, an Australian economic group consists of an entity together with all the entities it is required by the Australian accounting standards to include in consolidated financial statements.

An entity can be a company, partnership, superannuation fund, or trust.

**Combined cross-border loan balance**

You include all interest-bearing and interest-free loan balances for amounts borrowed and loaned.

If you have branch operations, you include the amounts claimed or returned for internally recorded dealings as amounts borrowed or loaned, interest-bearing and interest-free. You do not net off the amounts borrowed or loaned but include both totals.

**Distributor**

You are a distributor if your main business activity – as you put on your tax return – has an ANZIC Wholesale Trade code.

Australian and New Zealand Standard Industrial Classification (ANZSIC), 2006 (Revision 1.0) Chapter 8 Division F – The Wholesale Trade Division includes units mainly engaged in the purchase and on-selling, the commission based buying, and/or the commission based selling of goods, without significant transformation, to businesses. Units are classified to the Wholesale Trade Division in the first instance if they buy finished goods and then on sell them (including on a commission basis) to businesses.

**International related-party dealings**

You have international related-party dealings if you have international commercial or financial dealings or relations between related parties, for example, an agreement with your foreign subsidiary.

**International related parties**

An international related party includes any of the following:

- any overseas entity or person who participates directly or indirectly in your management, control or capital
- any overseas entity or person in respect of which you participate directly indirectly in their management, control or capital
- any overseas entity or person in respect of which those who participate directly or indirectly in their management, control or capital are the same as those who participate directly or indirectly in your management, control or capital.
Loan

To be classified as a loan for the purposes of these options, the instrument must be a debt interest under Division 974 of the Income Tax Assessment Act 1997.

Profit-before-tax ratio

The profit-before-tax ratio is calculated by subtracting the sum of the total expenses labels from the sum of the total income labels on your income tax return.

For the purposes of using these options, the ratio is to be calculated as a weighted average of three consecutive years, including the year for which you are considering applying the option.

Restructure

A restructure event for the purposes of these options, consistent with the definition in TR 2011/1, refers to arrangements in which assets, functions or risks of a business are transferred between you and your international related parties or your branch operations. Such arrangements may include:

- reorganisation of your structure resulting in the disposal or acquisition of entities or the change of ownership of entities
- establishment, expansion, reduction, liquidation or relocation of business operations or business lines, resulting in the
  - acquisition or disposal of assets or liabilities (tangible or intangible)
  - transfer of functions or the significant modification of service arrangements between yourself and international related parties (for example, transfer of agency, distribution, finance, information technology, insurance, logistics, marketing, sales, shared services, shipping, trading, transport and treasury functions)
  - transfer of risks between yourself and international related parties
  - increase or decrease of rights or obligations
- a change in the nature of the business carried on through your branch operations (for example, you have commenced or ceased to use your property in your branch operations or to perform functions or services through your branch operations).

Specified countries

'Specified countries' are the tax jurisdictions listed in the table below.

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<th>Andorra</th>
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<th>Antigua &amp; Barbuda</th>
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<td>Saint Martin (Dutch Part)</td>
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Specified service related-party dealings

A specified service between related parties is any strategic activity that contributes significantly to the creation, enhancement or maintenance of value in the Australian economic group. These services include:

- development of various forms of intellectual property and know how
- financial trading and execution activities
- insurance activities
- investment and asset management activities
- research and development activities
- software development activities
- strategic sales, marketing and relationship management and related activities.

Sustained losses

Sustained losses

Sustained losses occur where you have incurred losses for three consecutive years, including the year for which you are considering applying the option. For the purposes of these options, a loss is calculated by subtracting the sum of the total expenses labels from the sum of the total income labels on your income tax return.

Turnover

For the purposes of these options, turnover is the total ordinary income you derive in the ordinary course of carrying on a business. It includes income sourced from sales, rent, dividends, interest, distributions etc. For example, a company would use the amount reported at the total income label on its tax return.

Our commitment to you

We are committed to providing you with accurate, consistent and clear information to help you understand your rights and entitlements and meet your obligations.

If you follow our information and it turns out to be incorrect, or it is misleading and you make a mistake as a result, we will take that into account when determining what action, if any, we should take.

Some of the information on this website applies to a specific financial year. This is clearly marked. Make sure you have the information for the right year before making decisions based on that information.

If you feel that our information does not fully cover your circumstances, or you are unsure how it applies to you, contact us or seek professional advice.

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