



ROOK CONSULTANTS LIMITED

“Providers of tax, accounting & business advisory services”

Rook Consultants' August 2014 Newsletter

The Tanzanian Transfer Pricing Regulations

1. Background

Welcome to our August 2014 newsletter. This month's newsletter focuses on the Tanzanian Income Tax (Transfer Pricing) Regulations, 2014 (“TP Regulations”) and the resultant regulations contained therein.

Transfer pricing refers to prices charged in transactions between related parties. These transactions can be in the form of tangible goods, services, intercompany financing and intellectual property. Entities are generally said to be related if they have common direct/indirect control, ownership and management. Transfer pricing is an area of interest for most revenue authorities, worldwide, due to the possibility of manipulating pricing arrangements between related parties to “cheat” revenue authorities of their “fair” share of tax revenue.

Until recently, majority of the African countries simply relied on anti-avoidance provisions in their tax laws and requirement for related parties to conduct their dealings at arm's length. There were no specific guidelines on how entities with related parties were to apply the arm's length principle. Over the past five years, there has been a considerable focus on transfer pricing in Africa. As more African countries opened up their economy to Foreign Direct Investment (“FDI”), there has been a marked increase in intra-group transactions of MNEs. Tax administrations in Africa increasingly felt that their tax base was being eroded and have sought to protect it with the introduction of TP regulations. This has to be seen from the light of the recent global financial crisis which prompted revenue authorities across the world to aggressively protect their respective tax base.

2. The Income Tax (Transfer Pricing) Regulations, 2014

The Tanzania Transfer Pricing Regulations (“the TP Regulations”) were publicly released in May 2014. The relevant instrument is Government Notice No 27 (“The Income Tax (Transfer Pricing) Regulations, 2014”) published on and effective from 7 February 2014.

Scope

The Regulations apply not only to cross border transactions but also to domestic transactions between associates. These transactions between associates are referred in the TP Regulations as controlled transactions. Section 3 of the Tanzania Income Tax Act, 2004 (“ITA”) defines associate in relation to an entity to mean a relationship between two persons whereby: -

- One person, whether directly or through one or more interposed entities, controls or may benefit from 50 per cent or more of the rights to income or capital or voting power of the other, either alone or with associated entities; or
- Both entities are associates of a third person; or

- In any case not covered above, the relationship between the two entities is such that one may reasonably be expected to act, other than as employee, in accordance with the intentions of the other.

Arm's Length Principle

Tanzanian entities entering into controlled transactions are required to comply with the arm's length principle ("ALP"). The ALP is a principle whereby commercial or financial transactions between associates is carried out under comparable terms to similar transactions taking place between independent entities. The TP Regulations allow the Commissioner to make adjustments if he has reason to believe that a transaction has not been undertaken at arm's length.

Transfer Pricing Methods

Entities in Tanzania can adopt either of the following methods shall apply the following methods in determining the arm's length price of a controlled transaction:

- Comparable Uncontrolled Price Method ("CUP");
- Resale Price Method ("RPM");
- Cost Plus Method ("CPM");
- Profit Split Method ("PSM");
- Transactional Net Margin Method ("TNMM"); and
- Any other method as may be prescribed by the Commissioner from time to time.

The TP Regulations however impose a hierarchy in that the traditional transaction methods should be given priority over the transactional profit method when determining the most appropriate method to apply to the controlled transactions. The traditional transaction method comprises of the CUP, RPM and CPM methods while the transactional profit method consists of the PSM and TNMM.

Transfer Pricing Documentation

Tanzanian entities falling under the ambit of the TP Regulations are required to prepare contemporaneous documentation to support the arm's length nature of their controlled transactions. The TP Regulations set out the list of information that should be included in the taxpayer's transfer pricing documentation. The documentation for a year of income is expected to be in place prior to the due date for filing the income tax return for that particular year. Although the transfer pricing documentation is not required to be submitted with the tax return, it should be provided to the Commissioner within 30 days if requested.

Advance Pricing Arrangements ("APAs")

The TP regulations provide a reprieve to taxpayers by allowing them to enter into APAs with Tanzania Revenue Authority ("TRA"). Such an APA would lay down a set of criteria for determining whether the taxpayer has complied with the ALP for certain future controlled transactions undertaken by the taxpayer over a fixed period of time (not exceeding five years but may be reviewed). This is however at the Commissioner's discretion.

Intragroup Services

The following services are be disregarded as per the TP Regulations:

- shareholder or custodial services;
- duplicative services;
- services that provide incidental or passive association benefits; and
- on call services.

Penalties for Non-compliance

A person who fails to comply with the transfer pricing regulations is liable on conviction to **imprisonment for a term not exceeding six months** or to a **fine not less than 50 million Tanzanian shillings or both**.

In addition to this, any person who fails to maintain an appropriate Transfer Pricing documentation is liable on conviction to **a penalty equal to 100% of the underpayment of tax**.

3. Conclusion

While the promulgation of the Tanzanian TP Regulations is highly welcome, it is imperative that these Regulations are followed up by guidance on how to address a multiplicity of transfer pricing issues faced by taxpayers.

Given the heavy penalties imposed for non-compliance, we highly recommend that taxpayers who fall under the ambit of the Tanzanian TP Regulations regularly review related party transactions, prepare an up to date and robust transfer pricing policies that are properly documented to support the arm's length nature of their dealings with their associates.

If you are unsure about your transfer pricing compliance, we recommend you contact us on this matter. In this regard, Rook Consultants Limited (“Rook”) can help you in a number of areas including but not limited to:

- Assessment of transfer pricing risks;
- Developing transfer pricing documentation (local, regional and global);
- Handling TRA TP audits and queries;
- Negotiating APAs with TRA;
- Ad hoc TP advisory work including carrying out due diligence exercises, setting up tax efficient structures, drawing up agreements between related parties, setting up shared services centres, amongst others;

- Carrying out debt pricing exercises; and
- Carrying out training for staff involved in transfer pricing matters.

4. About Rook Consultants Limited:

Rook offers a broad range of **tax, accounting** and **business support services** including but not limited to the following:

- Accounting and book keeping services;
- Tax services;
- Payroll services;
- Staff recruitment & out-sourcing;
- Customized/in-house and general training programmes;
- Company secretarial services; and
- Other business support services.

Rook aims at providing high quality and professional services akin to those offered by the Big4 accounting firms while offering a more client-focused, dedicated, flexible and personalized services.

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