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Transfer pricing: grouping of transactions in light of the new regulations

Tax Alert

Dear Readers,

On the basis of the new regulations on transfer pricing, which will come into force on January 2017, in order to determine the obligation to prepare transfer pricing documentation it is necessary to sum up the value of all the transactions made with a related entity. They cannot be grouped under one type, since this method can be applied only in relation to "other events". This is the result of the individual interpretation issued by the Director of the Tax Chamber in Katowice on 15 July 2016, file ref. No. IBPB-1-2/4510-430/16/JW.

As we have already informed you several times, on 1 January 2017 new regulations on transfer pricing come into force. Among other things, the method of determining the obligation of documenting transactions with related entities is subject to a change. The obligation to prepare the documentation will be applied to entities whose revenue or expenses according to their accounting books in the previous year exceeded the equivalent of EUR 2 million PLN. Moreover, in addition to the introduction of the revenue (cost) criterion, the amount of transaction thresholds will also be changed. Up to now, the level of thresholds for particular types of transactions was fixed, which meant that it was not dependent on the revenue obtained by a taxpayer in a given year (incurred expenses). From the beginning of the year, the obligation to prepare the documentation will apply to those transactions (or other events entered into the accounting books) that are significant for the business activity of the taxpayer. The concept of materiality has been explained in the newly added Section 1d to Article 9a of the Act of 15 February 1992 (Journal of Laws of 2014, item 851, as amended, hereinafter: "the CIT Act"), pursuant to which *the transactions or other events of one kind, in which the total value of which exceeds the equivalent of EUR 50,000 in a tax year are deemed as transactions or other events that have a significant impact on the amount of income (loss) of a taxpayer*. At the outset, it can be observed that this provision does not specify the method to determine the value of particular transactions in order to establish which of them shall be subject to the obligation of documenting.

A company being a part of a capital group motioned for the interpretation of the new provisions, estimating that its revenue in 2016 would exceed the value of EUR 2 million. The company will conduct transactions with related entities, consisting, among other things, in the acquisition of fixed assets, purchase of IT services, provision of fixed property lease services, etc. The company's question came down to whether for the purpose of assessing the materiality of the effect of transactions or other events on the amount of income, it is required to sum up the values of all transactions or other events made with a single related entity. In the company's opinion, classifying the transactions or other events as "of the same kind" each time should be preceded by their individual assessment made on the basis of objective criteria and taking into account business specifics.

For this purpose, the nature of a given transaction (another event) should be discussed, as well as the functions, involved assets, incurred risks and costs of each party involved in the transaction and the calculation mechanism of the price applied. On such a basis, the company stated that the transactions listed by them cannot be considered as transactions of one kind within the meaning of Article 9a Section 1d of the CIT Act, and thus, in order to determine the existing obligation of documenting their values, shall not be subject to being summed up.

However, the tax authority did not agree to the applicant's view, and explained that in light of the new provisions the transactions should not be grouped according to the criterion of one kind, as it is possible only in relation to "other events". In the justification, the tax authority referred to the use of alternatives in the regulations discussed and to the interpretation of the content of Article 9a Section 1 item 1 of the CIT Act in the wording in force since 1 January 2017. The legislator details in it transactions and other events separately, which, in the opinion of the tax authority, points out the different treatment of those operations in terms of their grouping.

The interpretation under discussion is clearly unfavourable for taxpayers, who will have more administrative duties starting from the new year. In the opinion of the tax authority, in light of the new regulations, in order to determine the obligation of documenting, the taxpayer shall be obliged to sum up all transactions with a related entity without dividing them into, e.g. commodity and intangible transactions, or purchase and sales transactions, as was previously the case. Consequently, the obligation of documenting will also concern transactions of little importance, which probably was not the legislature's objective. This is just the first individual interpretation concerning the new regulations. Other interpretations should be expected, as the provisions are formulated in a quite vague manner and allow for a great deal of free interpretation. We do hope that further interpretations will offer more positive consequences for taxpayers than those described in this Tax Alert.

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Should you wish to discuss the above mentioned amendments in detail, feel free to contact us:

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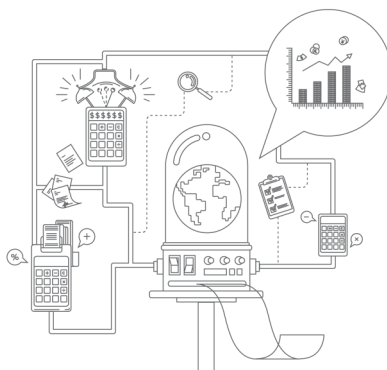
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