GARRIGUES

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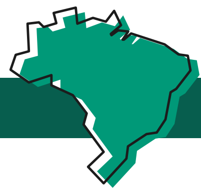
Transfer pricing: here's what the rules in Latin America look like

Latin America has been implementing in its tax law provisions for combatting base erosion by any other type of company that has a presence in various countries in the region.

One of the tax authorities' most important tools for preventing the avoidance or evasion of obligations by taxpayers are transfer pricing rules, taken directly from the Transfer Pricing Guidelines for Multinationals and Tax Administrations (TPG) drawn up by the Organization for Economic Cooperation and Development (OECD). These guidelines have been used as a basis for including transfer pricing rules or regimes in local laws. Except for specific provisions on filing dates or document requirements, the transfer pricing rules in Latin America mirror the OECD's guidelines and are quite similar among the various Latin American countries.

Moreover, the region's tax authorities, specifically those in Brazil, Chile, Colombia, Mexico and Peru, countries where Garrigues has a direct presence, have been introducing the recommendations that have come out of the OECD's Base Erosion Profit Shifting (BEPS) project, aimed at combating base erosion and profit shifting worldwide.

Here is a country-by-country analysis.



Brazil

1. What are the existing transfer pricing rules?

Imports and exports of goods, services and rights with related parties in other countries and with non-related parties located in tax havens or in jurisdictions with privileged tax regimes are subject to the Brazilian transfer pricing rules.

The aim of these rules is to control the prices charged in those transactions to ensure that they are performed on an arm's-length basis. For imports the rules restrict deduction of the cost or expense concerned. And for exports, they set out minimum taxable revenues for the purposes of Brazilian corporate income tax and the social contribution on net income (CSLL after its initials, subject to the same rules as Brazilian corporate income tax).

Though they take their cue from the OECD rules and the arm's length principle, Brazilian transfer pricing rules are very different from the international rules, because they do not consider the economic or business elements of transactions, instead they have a more restricted scope than that adopted by the OECD (because they do not take in royalty payments, licensing for technology transfer and brand use, or other intangibles) and are based on mathematical formulas that produce predetermined fixed margins for calculating the parameter price to be compared with the price charged in transactions subject to control. Another important point is the need for support documents for the parameter prices, because it is not allowed to verify those prices based on public or private databases..

2. Are any transfer pricing amendments planned in the near future?

Brazil formally applied to become an OECD member in 2017, and the proposal is being considered by the Organization´s Ministerial Committee. In view of Brazil's potential admission as OECD member, at a ceremony held in Brasilia in March 2018 led by the National Confederation of Industries (CNI) and the federal government, a joint working project on transfer pricing was launched in which Brazil and the OECD will analyze over 15 months the divergences between Brazilian legislation and the OECD approach to assess the options for bringing Brazilian legislation closer to the OECD transfer pricing standard. To date, no change to the Brazilian legislation has occurred as a result.

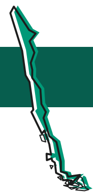
3. What are the key dates or time limits to remember?

Brazilian taxpayers have until December 31 every year to complete their transfer pricing calculations, because in that month any adjustments required to transactions subject to transfer pricing control must be added to the base for corporate income tax and the social contribution on net income.

Then taxpayers have until July 31 the following year to file their returns for corporate income tax and the social contribution on net income electronically with the Brazilian Tax Agency. This return shows their calculations in relation to transactions subject to transfer pricing control and contains the country-by-country report where the Brazilian company is responsible for filing that report.

Additionally, once that return has been filed, taxpayers are required to file, in the event of a tax audit, the support documents for the parameter prices and for the prices charged, which often have to be translated into Portuguese by a certified Brazilian Portuguese translator.

Chile



1. What are the existing transfer pricing rules?

A. Scope

The Income Tax Law (LIR) allows the Chilean Inland Revenue Service (SII) to challenge the prices, values or returns determined (or to calculate them if none have been determined), in the following cases:

i) Cross-border transactions, which taxpayers domiciled, resident or established in Chile carry out with related parties in other countries.

ii) Business or company restructurings or reorganizations where, as a result of these transactions, income-generating assets or activities have been transferred from Chile to other countries under any type of act or contract or without an act or contract.

B. Related entities

For the transfer pricing rules to apply, the parties to the transaction, reorganization or restructuring concerned must be in any of the related-party scenarios set out in the Income Tax Law, according to which, those parties are deemed to be related in the following cases:

i) Where one of them participates directly or indirectly in the management, control, capital, profits or revenues of the other, or

ii) Where the same person or persons participate directly or indirectly in the management, control, capital, profits or revenues of both parties, all of them being deemed related to each other, or

iii) In cases involving an agency, branch or any other form of permanent establishment, with respect to their parent company, and with other permanent establishments of the same parent company, with related parties of the parent company and their permanent establishments.

iv) Where the transactions are carried out with parties resident, domiciled, established or formed in a country, territory or jurisdiction classed as a preferential tax regime for the purposes of the Income Tax Law, unless that country or territory signs with Chile an agreement allowing the exchange of relevant information for the purposes of applying tax provisions, and that agreement is in force.

v) In relation to individuals, where the relationship between them is one of spouses or one of consanguinity or affinity up to and including the fourth degree.

vi) Lastly, a relationship is deemed to exist between the participants where one party carries out one or more transactions with a third party which itself carries out, directly or indirectly, with a party related to that party, one or more transactions that are similar or identical to those it performs with the first-mentioned party, regardless of the capacities in which that third party and the parties act in those transactions.

C. Settlement of differences

For the purposes of applying the transfer rules, the Chilean Inland Revenue Service must issue a notice to the taxpayer concerned asking it to produce all the background information needed to verify that its transactions with related parties were performed at arm's length prices or values or by reference to arm's length returns.

In this regard, the Income Tax Law itself determines the pricing methods for the transactions that may be used to determine those prices, values or returns, and states that the taxpayer itself is responsible for employing the most suitable method, by reference to the characteristics and circumstances in each particular case.

For these purposes, a transfer pricing study may be attached giving an account of how the prices, values or returns for their transactions with related parties were determined. A transfer pricing study is not a mandatory requirement, however, nor does it exclude other types of proof to evidence that the transactions were performed at arm's length values.

D. Taxes and Fines

Where as a result of the adjustments to prices, values or returns, the Chilean Inland Revenue Service determines a difference, a single tax is charged equal to 40% of the value of the difference so determined. In addition to the 40% single tax, a fine equal to 5% of the amount of the difference is charged, unless the taxpayer has properly and timely complied with its obligation to submit the background information requested by the Chilean Inland Revenue Service during the audit.

Subject to certain requirements, taxpayers are allowed to correct prices, values or returns for transactions carried out with related parties, based on transfer pricing adjustments made by other jurisdictions with which it has an international double taxation agreement that does not prohibit that type of adjustment. Where an adjustment results in a tax difference payable to the taxpayer, the excess taxes paid are refunded after being readjusted for inflation.

E. Advance Agreements

Any taxpayers performing transactions with related parties may propose to the Chilean Inland Revenue Service an advance agreement for determining the arm´s length price, value or return for those transactions.

If the advance agreement is accepted, it applies for transactions carried out by the applicant in the business year it was requested and in the following three business years, with an option to extend or renew it.

While the advance agreement is in force, the Chilean Inland Revenue Service is not allowed to settle tax differences arising from the transfer prices for the transactions covered by the agreement, if the prices values or returns have been determined or reported by the taxpayer consistently with its terms.

2. Are any transfer pricing amendments planned in the near future?

The tax modernization bill, presented by the president of Chile in 2018 and currently being discussed in parliament, contains a special provision on international reorganizations. Under that provision, if certain requirements are satisfied, the Chilean Inland Revenue Service could be prohibited from assessing transactions, which would make it easier to complete tax neutral international reorganization processes.

3. What are the key dates or time limits to remember?

Until the last business day in June every year, the taxpayers listed below must file Sworn Return No 1907, for transactions with related parties carried out in the previous business year:

(i) Taxpayers which are in the medium-sized enterprise or large enterprise segments, and have performed transactions with related parties that do not have their domicile or residence in Chile.

(ii) Taxpayers not classified in the foregoing segments which have performed transactions with parties domiciled, resident, established or formed in a territory or jurisdiction classed as a "preferential tax regime" for the purposes of the Income Tax Law, and

(iii) Taxpayers not falling in the segments mentioned in letter a), which have performed transactions with related parties not having their domicile or residence in Chile and those transactions involved sums higher than $500,000,000 (approximately USD 700,000).

Within the same filing period for Sworn Return no 1907, the parent or controlling companies of multinational enterprise groups that have their residence in Chile must file Sworn Return no 1937 on the country-by-country report.

There is a fine for failing to file these sworn returns, or filing returns that are incorrect, incomplete or out of time, amounting to up to 50 annual tax units (approximately USD 3,400), which cannot go above an upper limit equal to between 15% of the taxpayer's own capital or 5% of its effective capital.

Colombia

1. What are the existing transfer pricing rules?

The Colombian transfer pricing legislation states that any taxpayers carrying on transactions with related parties from other countries or located in Colombia's free trade zones and/or with economically related parties or independent third parties located in low tax or no tax jurisdictions, non-cooperative regimes and preferential regimes have to comply with transfer pricing reporting requirements for the taxable year.

The Colombian rules specifically require the following:

- The transfer pricing reporting requirements must be maintained annually (information return, local file, master file and country-by-country report). Specific revenue or wealth thresholds determine the obligation for a taxpayer to file these documents.
- The information return (DI) has to be filed by taxpayers satisfying the condition mentioned in the previous point and the return must include all transactions carried out with related parties in other countries and in free trade zones.
- Any taxpayers that carry out transactions with entities located in low tax or no tax jurisdictions, preferential regimes or non-cooperative jurisdictions (formerly, tax havens) do not have to meet the stipulated thresholds and have to file the information return (DI) on transactions with related parties or independent third parties located in these jurisdictions. Additionally, they have to submit the local file on transactions equal to or higher than USD114,233 (approximately) for fiscal year 2019.
- The local file has to be submitted for any transactions equal to or above USD 514,050 (approximately) in fiscal year 2019.
- The master file has to be submitted by any taxpayers that are required to submit the local file; and which also belong to a multinational group within the meaning of the local legislation (Decree 2120 of 2017).
- The country-by-country report has to be filed by any entities with tax residence in Colombia that have been appointed by their parent companies to act as substitute entity and that satisfy the requirements in the local legislation for doing so (Decree 2120 of 2017); which are based on BEPS Action 13.
- Any transactions involving commodities have to be analyzed using the uncontrolled comparable price method.
- The law provides the option to negotiate advance pricing agreements with the tax authorities.

2. Are any transfer pricing amendments planned in the near future?

In the past 10 years, Colombia has submitted three tax reforms, the most recent in 2018. A large part of the changes introduced in these reforms are directed at complying with the OECD's requirements for Colombia to complete its accession process to the organization, and at implementing the recommendations that have come out of the BEPS plan.

3. What are the key dates or time limits to remember?

The filing periods for the information return, local file, master file and the notification of the country-by-country report, for taxable year 2018 started (according to the last digit of the tax identification number) on July 9, and ends on July 22, 2019.

The periods for filing the country-by-country report for taxable year 2018, start (according to the last digit of the tax identification number) on December 10 and end on December 23, 2019.

The dates for the transfer pricing reporting requirements for taxable year 2019 will be published by the government before December 31, 2019; they are usually determined between July and September.

Mexico

1. What are the existing transfer pricing rules?

Mexico added the rules on economic related parties to its legislation in 1992, and the transfer pricing legislation they include arrived in 1994. Mexico is the only Central American country that is an active member of the OECD and it has one of the most advanced sets of international taxation laws, because of its proximity to the U.S. and Canadian markets.

It is therefore important to be familiar with the main components of the Mexican transfer pricing rules listed below:

- Rules on related parties provided in the Income Tax Law (LISR).
- The Income Tax Law provides that the taxpayers required to prepare and keep a transfer pricing study supporting that their transactions with related entities were carried out in compliance with the arm's length principle, are any who:
  1. Perform business activities and the revenues obtained in the year under analysis were in excess of MXN$ 13,000,000.
  2. Provide professional services and the revenues obtained in the year under analysis were in excess of MXN$ 3,000,000.
- Mexican *maquila* processing companies have their own set of transfer pricing rules in the Income Tax Law; which also contain the requirements determining a permanent establishment and rules on how to calculate the consideration for providing *maquila* services.
- Mexican taxpayers falling under the transfer pricing rules have to file:
  1. **Master file return (DIM),** local file return (DIL) and country-by-country report return (DPP). These contain the same information as that described in BEPS Action 13; the country-by-country report return, however, must be filed by taxpayers meeting special requirements. These last returns were included in the local legislation as a result of the OECD's BEPS plan and must be filed by December 31 in the year following the year under analysis.
  2. **Return on relevant transactions:** This return has to be filed by any taxpayers that carry out specific transactions included in the Federal Tax Code (CFF), within thirty days after they took place. Filing this return is a condition for any deduction related to transfer pricing adjustments.
  3. **Information return on tax situation:** This return must be filed with the return for the period and may have 2 attachments (15 and 16) in which taxpayers have to report if they have complied with their transfer pricing obligations, the amount and type of the transaction with their related parties, together with the transfer pricing method used.
- It is not mandatory to file the transfer pricing study with the tax authorities; although it does have to be prepared to support the filed information return and in the event of an audit by the tax authorities (SAT).
- Taxpayers are required to comply with the rules and file the mandatory transfer pricing documents if they:
  1. Perform transactions with economically related parties located in other countries; and
  2. Perform transactions with economically related parties (including local transactions).

Lastly, Mexico is notably one of the countries that has made the most progress with implementing the OECD recommendations that have come out of its BEPS project. To date it has already implemented in its local legislation the recommendations in BEPS Actions 2, 3, 4, 5, 6, 7, 12, 13 and 15.

2. Are any transfer pricing amendments planned in the near future?

For the 2020 tax law reform, a bill approved by the legislative branch of government already exists, which does away with the obligation to file the return on relevant transactions.

The bill also contemplates, however, the obligation to notify "reportable arrangements" to the tax authorities, which are set out on a list containing a wide variety of transactions carried out between related parties.

3. What are the key dates or time limits to remember?

Those mentioned above in relation to the obligations.

Peru

1. What are the existing transfer pricing rules?

In Peru, transfer pricing rules apply to transactions performed: (i) between taxpayers and their related parties; (ii) from, with or through countries or territories classed as "non-cooperative" or "low tax or no tax" jurisdictions; or (iii) with parties whose income, revenues or gains from those transactions are subject to a preferential tax regime.

The aim of those rules is for the income tax on a transaction or group of transactions to be determined on an arm's length basis, and to leave aside underpricing, overpricing, deferrals and simulations or sham transactions that could be detrimental for the taxman.

To determine whether a transaction was performed on an arm's length basis, the Income Tax Law defines a number of pricing methods. Although no method has priority over another, the most commonly used methods in Peru are the comparable uncontrolled price method and the net margin method.

Moreover, in the specific case of services provided between related parties, an inescapable condition for deduction of the expense and/or cost concerned is that the services must meet the "benefit test" (i.e. the service must provide economic or commercial value for the customer). And, for services with low added value (i.e. ancillary or support services), deduction of the expense concerned is determined by reference to the costs and expenses incurred by the provider of the service, and to the profit margin, which cannot exceed 5% of those costs and expenses.

In procedural terms, taxpayers subject to transfer pricing rules whose revenues exceed the thresholds provided in the Income Tax Law, its regulations and related provisions have to file with the National Customs and Taxes Authority – SUNAT the sworn information returns on the local file, master file and country-by-country report.

2. Are any transfer pricing amendments planned in the near future?

We are not currently aware of any forthcoming legislative reforms related to transfer pricing.

3. What are the key dates or time limits to remember?

It is important to underline that the periods for filing the information returns on the local file, master file and country-by-country report are determined according to the date schedule that will be approved for reporting and paying the taxes with monthly self-assessment returns for the periods of May (in the case of the local file) and September (in the case of the master file and country-by-country report).

In this regard, according to the last digit in their Single Taxpayer Number (RUC), any taxpayers who have performed transactions subject to transfer pricing rules (and meet the specific requirements for filing each information return), have to file, for the 2018 tax period: (i) the local file, in mid-June 2019; and (ii) the master file and country-by-country report in mid-October 2019.

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