

Transactions between associated enterprises coming into the transfer pricing net

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The transfer pricing (TP) provisions, contained in section 31 of the Income Tax Act (ITA) of South Africa, are applicable to “affected transactions”. Affected transactions are regarded as being cross border transactions between “connected persons” where any term or condition to that transaction differs from that which would have existed had those persons been independent and dealing at arm’s length.

Connected persons in relation to a company includes any shareholder that holds at least 20% of its shareholding where no other company holds a majority or any majority shareholder (i.e., shareholding of at least 50%) or where a company holds at least a 50% shareholding in the other company.

In certain circumstance, 2 companies under common control may not be connected persons as defined in terms of current legislation therefore the transactions between such companies would not be regarded as being affected transactions.

Accordingly, the TP provisions, technically speaking, do not apply to these transactions. However, there is a view that SARS may still attempt to apply the doctrine of “substance over form” to argue that these transactions should still be conducted at arm’s length as the OECD regulations on Transfer Pricing do include transactions between common control companies (referred to by the OECD as “associated enterprises”). This is supported by the fact that South Africa generally does follow the recommendations of the OECD particularly in the area of taxation.

The 2019 Taxation Laws Amendment Act made an amendment to the definition of “affected transaction” to include transactions between “associated enterprises” as described in Article 9(1) of the OECD’s Model Tax Convention (MTC). The MTC is the basis on which most of the South African tax treaties have been drafted. The

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expansion of the affected transaction definition to associated enterprises effectively expands the TP provisions to transactions between companies that are under common control/management.

This amendment was initially intended to commence on 1 January 2021 but in terms of the 2020 Taxation Laws Amendment Act this amendment has been postponed to years of assessment commencing 1 January 2023.

The TP regulations in South Africa require a mandatory comprehensive TP policy (local file and master file) to be submitted to SARS annually where the affected transactions for the year of assessment exceed R100 million.

It is our recommendation that where affected transactions are below this threshold but still significant that a mini/micro TP policy be maintained to ensure that should a query from SARS arise that one is able to support the basis of the transactions being conducted at arm's length. Whilst the TP provisions do not require a comprehensive TP policy to be maintained in such circumstances, it must be ensured that all transactions that fall within the ambit of section 31 comply therewith and can be suitably evidenced.

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