

Transfer Pricing Country Profile
(to be posted on the OECD Internet site www.oecd.org/taxation)

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1. Reference to the Arm's Length Principle

Since 1998, with the enactment of Law N° 25.063 (with effect for the operations arranged from 31/12/98), the Income Tax Law, among others, was amended and new features regarding transfer pricing were introduced by adding an updated normative body to the text of the Law in accordance with the position that, on this issue, had been adopted by many other countries, having to emphasize that, Argentine legislation to a great extent is in line with the rules and principles of the OECD.

Later, through the enactment of the Law N° 25.239, published in the Official Gazette on December 31st, 1999, the Income Tax Law was subsequently amended, carrying out adjustments to transfer pricing rules, being this amendment later regulated by the Decree N° 1037/2000.

Thus, article 14 of the Income Tax Law makes express reference to the arm's length principle, according to which the transactions between domestic companies (or PEs situated in Argentina) and foreign related persons will be considered as transactions between independent parties if they are undertaken at arm's length. When those transactions are not conducted under arm's length conditions the results can be adjusted according to the provisions of article 15.

Besides, when, among others, article 15 of the Income Tax Law was amended, anti-tax-havens provisions became more rigid, as far as transfer pricing is concerned.

In that sense, the legal text sets (without possibility of opposing proof to the contrary and whether or not related parties are involved) that transactions entered into by local taxpayers with persons or entities incorporated or domiciled in low-tax jurisdictions are considered not to be carried out at arm's length. It will be necessary to apply the transfer pricing methodology in order to justify the value of the operations arranged under those conditions.

Finally, with the enactment of the Law N° 25.784 published in the Official Gazette on 22-10-03, modifications to the transfer pricing regime were made, related to the treatment of independent parties' transactions of import and export of goods. Prior to the amendment, these transactions were subject to the methodology of transfer prices in certain cases.

The abovementioned law introduced a new methodology of determination of transfer prices for operations of export of goods with international well-known market price, issue that will be developed in item 4.

2. Reference to the OECD Transfer Pricing Guidelines (if any)

Argentina, in its tax legislation, does not make any reference with regard to the OECD Transfer Pricing Guidelines. Nevertheless, it is worth noting that in the Regulatory Decree of the Income Tax Law, the five factors of comparability are added, with a similar scope to those mentioned in the Guidelines.

3. Definition of related parties

The Income Tax Law establishes that a company, trust or permanent establishment located or incorporated in the Republic of Argentina and a person, entity or permanent establishment incorporated or located abroad, are considered associated parties if they are directly or indirectly managed or controlled by the same person (individual or company) because of their participation in the capital, their degree of credit balance, their functional influences or of any other nature, -whether contractual or not- have the power to decide, to guide or to define the activity or activities of the above mentioned companies, establishments or other type of entity.

On the other hand, the Tax Administration has drawn up guidelines to define the existence of associated parties. In such sense, transactions will be regarded as between associated enterprises when at least one of the following circumstances -among others- is verified:

- a) A person has the totality or majority of the capital of another person.
- b) In respect of two or more persons alternatively:
 1. The same person owns the total or majority part of the capital of both persons;
 2. The same person has total or majority share in the capital of one or more persons and significant influence on the others;
 3. The same person simultaneously has significant influence on them;
- c) A person has the necessary votes to form the social will or to prevail in the Shareholders' or Partner's meeting of another one.
- d) Two or more persons have directors, high level employees or managers in common.
- e) A person has the capacity to act as exclusive agent, distributor or dealer for the purchase and sale of goods, services and rights, of another one.
- f) A person provides the technological property or technical knowledge that constitutes the base of the activities of another person, on which the later manages its business. Evidently, it must be a technology without which its activity could not be developed, that is to say, in principle it refers to a technology which is essential for the exercise of the relevant activity.
- g) A person participates with another one in associations without legal existence as legal persons, such as condominiums, temporary joint ventures, groups of business collaboration, non- corporate groups or groups of any other type, through which it exerts significant influence when determining prices.
- h) A person agrees with another person contractual clauses in preferential terms with respect to those granted to third parties in similar circumstances, such as discounts by negotiated volumes, financing of the operations, delivery on consignment, among others.
- i) A person participates significantly in the establishment of business policies, such as, supply of raw materials, production and commercialization, of another one.
- j) A person develops an activity relevant only in relation to another person, or its existence is justified solely in relation to another person, giving rise to relations such as "only supplier" or "only client", among others.

- k) A person provides in substantial form the funds necessary for the development of commercial activities to another person, by means of the concession of loans or the granting of guarantees of any type, in the cases of financing provided by a third party.
- l) A person undertakes the losses or expenses of another person.
- m) The directors, high level employees or managers of a person receive instructions or act in interest of another person.
- n) Under special agreements, circumstances or situations the direction or administration is granted to a person with minority participation in the capital stock.

4. Transfer pricing methods

The legislation of Argentina contains provisions regarding the methods to be used in order to determine whether transactions between related parties satisfy the arm's length principle.

In fact, Article 15 of the Income Tax Law stipulates that the method(s) to be used are those that are most appropriate based on the type of transaction made.

In that regard, the said Article stipulates that the applicable methods are the comparable uncontrolled price, resale price between independent parties, cost plus, profit split, and transactional net margin methods, in the form -and among other methods- set forth in the regulations thereof.

In turn, the Tax Administration implemented this provision by issuing regulation indicating, on a general and theoretical basis, that the most appropriate method to determine whether transfer prices are consistent with normal market practices between independent parties shall be the one that best reflects the economic reality of transactions, and the regulation includes some of the factors to be considered for this purpose.

It indicates that the best method shall be the one that:

- Is most compatible with the business and commercial structure.
- Has the best information –as regards quality and quantity- for an appropriate justification and application.
- Provides for the most appropriate degree of comparability between related and unrelated transactions and the enterprises involved in such comparison.
- Requires the lowest level of adjustments to eliminate the differences between comparable facts and situations.

The methods adopted by the legislation in Argentina to verify transfer pricing are similar to those set forth in the OECD Transfer Pricing Guidelines. The statutory methods and definitions are as follows.

- a. Comparable uncontrolled price: the price that would have been agreed upon with or among independent parties in comparable transactions.
- b. Resale price: the price of acquisition of a good, provision of a service or consideration of any other transaction between related parties, which shall be determined by

multiplying the resale price or the price of the service or of the consideration of the relevant transaction set between independent parties in comparable transactions by the result of subtracting from the unit the percentage of gross profit that would have been agreed with or between independent parties in comparable transactions. For this purpose, the percentage of gross profit shall be obtained by relating the gross profit to net sales.

c. Cost plus: the one that results from multiplying the cost of goods, services or other transactions by the result of adding to the unit the percentage of gross profit applied with or between independent parties in comparable transactions. Such percentage shall be obtained by relating the gross profit to the cost of goods sold.

d. Profit split: the profit obtained in a transaction between related parties is allocated in the proportion by which it would have been allocated should the transaction have taken place between independent parties, according to the following procedure:

1. A global profit is determined, which results from adding the profits allocated to each related party involved in the transaction(s).

2. The global profit thus obtained shall be allocated to each related party in the proportion resulting from considering each party's assets, costs and expenses in relation with the transactions made between them.

e. Transactional net margin: the profit margin applicable to transactions between related parties, determined by establishing the profit that would have been obtained by any one of them in comparable uncontrolled transactions, or comparable transactions between independent parties. For the purposes of establishing the said margin, profitability factors may be considered, like return on assets, sales, costs, expenses or cash flow.

In addition, it is worth mentioning that Article 15, 6th paragraph referred to above also contains a rule about the new method for transfer pricing in the case of exports to related parties, involving grains, oil seeds, other products obtained from the land, hydrocarbons and derivatives thereof, and, in general, goods with public prices in transparent markets, in which an international broker, other than the actual recipient of the goods is involved. The best method to assess the Argentine-source income shall be the trading value of the good in the market on the date in which the goods are shipped –regardless of the means of transport-, without considering the price that would have been agreed upon with the international broker.

However, if the price agreed upon with the international broker were higher than the effective trading value at the above-mentioned date, the former will be considered as the actual value of the transaction.

The method described above shall not apply when the taxpayer effectively proves that the international broker meets all of the following requirements:

a) It must have an actual presence in the territory of residence, with a commercial establishment where the business is managed, and meet all the legal requirements in terms of incorporation, registration and filing of financial statements. Assets, risks and functions of the international broker must be in accordance with the volumes traded;

b) Its primary activity should not consist of obtaining passive income or brokering in the trading of goods from, or to, Argentina or with other members of the economically related group; and

c) Its international trade transactions with other members of the same group must not exceed thirty per cent (30%) of its total annual transactions.

The conclusion of the above is that the transfer pricing methodology contained in Article 15 of the Income Tax Law establishes no order of precedence for the use of the methods, with the exception of the case described in the sixth paragraph of the said article.

However, the taxpayer shall have to indicate the reasons why a given method has been chosen and prove that the mechanism chosen is the most appropriate for the transaction made.

5. Transfer pricing documentation requirements

As regards the information that the tax authority requires from taxpayers to prove that they have operated under the arm's length principle and which may be required by our Tax Administration according to its control and examination powers, it is worth mentioning the following:

1. No specific type of documentation has been defined. This is obviously due to the fact that, given the different situations that might be found in practice, it is not possible to standardize the documentary elements required. On the other hand, this makes it possible for taxpayers to use any piece of evidence, as long as it fully supports and justifies each aspect as required by the rules of the Tax Administration and is appropriate for the relevant situation.

2. The documentation required is not limited to those documents included in the list provided, since the particular conditions of any given case might make the documents specifically listed insufficient or inapplicable, depending on the method used to adjust the prices of international transactions. For this reason, the list is intended as a minimum guide to help taxpayers prepare their body of documents.

3. The documentation should not only be contemporaneous but it should exist at the due date for filing informative returns. As from that moment, the documentation should be available to examiners and it should be kept until expiration of the statute of limitation period for the relevant tax.

To be accepted as evidence, the documentation should meet all the formal requirements under the current legislation, such as, for example, being in the Spanish language, duly translated by a certified translator, if applicable.

For these purposes, the data that the local taxpayer should document and which are necessary for the Tax Administration to review or apply some of the methods set forth in our legislation are:

a. Taxpayer data and information about their functions or activities (production, research and development, marketing, sale and distribution, shipment, inventory, installation, after-sale service, administration, accounting, legal, personnel, information technology, finance, etc.).

b. Complete information about the foreign related party and documentation, if any, indicating the nature of the relevant transaction.

This is important because this documentation about the foreign affiliates should exist even if no transaction has taken place between the parties. This means that although in this case it shall not be required to submit a transfer pricing informative return, the taxpayer shall be under the obligation to document the relationship that the parties may have. This information should be available for examinations that may be conducted by the tax authority.

c. In the case of multinational enterprises, in connection with which documentation is required indicating the activities conducted by each one of them, the transactions made between them and other aspects, it is necessary to note that the information and support documentation required concerns all the members of the group, even those with which no transactions have been made.

d. In addition, the following documentation is required:

- Transactions made with related parties, amounts and currency used.
- Consolidated financial statements, if applicable based on the pricing method used.
- Contracts and agreements executed.
- Information about the taxpayer's financial standing, about the enterprise's environment and the market in which it operates, commercial strategies, cost structure.

e. Information and documentation supporting the transfer pricing procedure followed.

6. Specific transfer pricing audit procedures and / or specific transfer pricing penalties

No specific transfer pricing audit procedures, in order to verify transfer prices, are provided for in Argentine legislation.

With respect to the penalties for the manipulation of transfer prices and in relation to documentation requirements, the Tax Procedure Law of Argentina contains some provisions in that sense.

Thus, only after the enactment of Law No. 25.795 –which was published in the Official Gazette on November 17, 2003 and which amended the Tax Procedure Law-, did the Argentine legislation incorporate specific rules for penalties to be imposed as a result of events on non-compliance with the rules governing international transactions, based on the practical experience our country had gained.

The penalty system is the following:

1. Automatic penalty –without serving prior notice- upon failure to file tax return by the corresponding deadline:

- Informative complementary return of import and export transactions between independents: \$ 1,500 (approximately U\$S 428) for individuals and \$ 9,000 (approximately U\$S 2,570) for corporations.

- Informative complementary return of transactions with foreign subjects –except for the above-: \$ 10,000 (approximately U\$S 2,850) for individuals and \$ 20,000 (approximately U\$S 5,710) for corporations.

2. Penalty for non-compliance with regulations establishing or requiring fulfilment of formal obligations to assess tax liabilities, and verify and examine compliance by the taxpayers.

- Penalty of \$ 150 (approximately U\$S 43) to \$ 2,500 (approximately U\$S 710).
- In the following cases, the penalty will range from \$ 150 (approximately U\$S 43) to \$ 45,000 (approximately U\$S 12,850):
 - o Resisting examination (repeated failure to respond to requests made by the tax authority).
 - o Failure to keep evidence of prices used in international transactions.
 - o Failure to provide data needed to control international transactions.
- 3. Failure to submit informative returns of international transactions or returns with information about the taxpayer itself or about third parties as requested by the tax authority.
 - Penalties: \$ 500 (approximately U\$S 143) to \$ 45,000 (approximately U\$S 12,850). These fines are in addition to those above and the amounts depend on taxpayer's status and seriousness of the breach.

4. Higher-income taxpayers.

When the taxpayer has an annual income of \$ 10,000,000 (approximately U\$S 2,857,000) or more, the penalty imposed upon failure to comply with the third request is 2 to 10 times the maximum amount established (\$ 45,000 or approximately U\$S 12,850), which shall be added to the rest.

5. Failure to pay the tax

- General: 50% to 100% of the tax that was not paid, withheld or collected.
- International transactions: 1 to 4 times the tax that was not paid or withheld.

7. Relevant regulations on Advance Pricing Arrangements

No legal provision allows taxpayers to enter into Advance Pricing Arrangements in Argentina.

8. Link to relevant Government Internet sites

Ministerio de Economía y Finanzas Públicas: www.mecon.gov.ar

Administración Federal de Ingresos Públicos: www.afip.gov.ar

9. Other relevant information