Argentina provides new transfer pricing rules

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In brief

The Argentine Government, on December 27, 2018 enacted the regulatory decree (RD) to the reformed income tax law (ITL), effective for fiscal years starting from January 1, 2018.

With respect to transfer pricing, the RD provides regulations on the following topics:

- More details on the information requirement related to import and/or export of goods carried out through international intermediaries (intermediary substance test).
- Further guidance on the methodology for the valuation of exports of commodities carried out through international intermediaries.
- Upgrade to an RD status of the list of assumptions of situations that are deemed to constitute ‘economic relationship’ for documentation purposes, and additional guidance regarding jurisdictions that are considered of low or nil taxation (tax havens).
- Changes to transfer pricing documentation requirements broadly consistent with OECD Action 13 of the BEPS initiative, including materiality thresholds for the transactions.
- Introduction of further guidance regarding comparability analysis, risk assessment of the transactions, and transfer pricing methods consideration.
- Additional clarifications on the interest expense deduction limitation.
- Permanent establishment (PE): clarifications on the dependent agent status.

See PwC Tax Insight issued January 31, 2018, for a description of the main transfer pricing implications of the modifications introduced in the legislation by the comprehensive tax reform passed by the Argentine Congress on December 27, 2017.

In detail

International intermediaries – substance test

The RD introduces guidance regarding the information that taxpayers must provide to the tax authorities in case of imports and/or exports of goods carried out by Argentine taxpayers involving international intermediaries (triangulated transactions).

The law provides that such documentation requirement will be applicable when either:
(a) the international intermediary is a related party of the Argentine taxpayer, or

(b) the foreign importer/exporter is a related party of the Argentine taxpayer.

According to the RD, taxpayers can prove that the conditions stated by the law are not met — and thus they are not required to provide further information on the intermediary — by providing evidence and documentation such as the intermediary’s bylaws, or annual report of the intermediary’s group.

If either condition (a) or (b) is met, a functional analysis of the international intermediary must be performed to demonstrate that the remuneration obtained by it is consistent with the functions, assets, and risks involved in the transactions.

The functional analysis must evaluate and document (a) that the intermediary has a real presence in its territory of residence and has a commercial facility where its business is managed, and that it complies with the legal requirements of incorporation, filing of financial statements, tax returns, and general rules in its place of establishment; (b) that the remuneration of the intermediary is consistent with its involvement in the transactions and, when the intermediary is a related party, the Argentine taxpayer must keep information on the purchase and sale price and expenses associated with the transactions; and (c) the intermediation model, the functions performed, assets involved, and risks assumed by the intermediary must be identified.

The information to be considered for the analysis of the intermediary must be that of the last fiscal year of the intermediary that ended before the fiscal year-end of the local entity.

Observation: Section 21.19 of the RD is a potential focus of conflict and disputes between Argentine taxpayers and Tax Authorities (AFIP).

Regardless of the entrepreneurial nature of the international intermediary, this Section states that if the international intermediary’s remuneration is higher than the one that would have been agreed upon by independent parties — in accordance with the assets, functions, and risks of the intermediary — the excess in the remuneration/income amount will be considered as higher income of Argentine source that is attributable to the local taxpayer. Further guidance on this is expected to be provided in AFIP’s regulations.

In case the actual transaction differed significantly from the described functions or agreements in place, or if the transaction was set up for tax purposes only, AFIP are allowed to re-characterize the transaction and even ignore the existence of the intermediary in the transaction.

Exports of commodities — registration of agreements

The RD introduces further guidance regarding the transfer pricing rules for the valuation of the exports of commodities carried out through an international intermediary.

Taxpayers must document the price setting mechanism — particularly the components of the price when it is formulae pricing — and quotation must be the closing quotation or the max/min range, when available.

According to the new rules, in addition to complying with the ‘substance test’ described above, the taxpayer must register electronically with the AFIP the agreements related to such export transactions. The information to be disclosed in the registry includes: (1) date of the agreement/sale; (2) information of the exporter (name, address, tax ID, etc.); (3) information of the foreign importer (name, address, country of residence, tax ID, etc.); (4) existence of relationship between the exporter, importer, or intermediary, or if they are located in a low or nil tax jurisdiction; (5) type of shipment (bulk, bagged, etc.); (6) type of product, quality, volume of sale, and transportation; (7) price and condition of sale, including the price-fixing methodology; (8) price and condition of sale considered as a market reference; (9) adjustment applied to the quoted price, providing details; (10) official price (if available); (11) agreed period for the shipment of the goods; and (12) country or region of destination of goods.

For those transactions that do not fulfil the registration requirements, or if registered but taxpayers are not able to support with documentation, the price of the goods exported at the time of shipment will be considered for tax purposes, including the correspondent comparability adjustments that may apply.

AFIP will publish prices or indexes based on market information, which taxpayers may use as minimum values for the export transactions for certain goods. Observation: Further regulations on this topic are needed.

Assumption to define ‘related parties’ and guidance on low or nil tax jurisdictions

The RD now includes the list of assumptions — formerly included in General Resolution 1122/01 issued by AFIP — that would deem two entities to be ‘related parties,’ making the transactions between them subject to transfer pricing rules. These assumptions include not only
shareholding, but also economic and/or functional influence to establish relationship.

**Observation:** Even though upgraded to an RD status, these assumptions should be rebuttable, since the ITL does not state that they are non-rebuttable assumptions. Former jurisprudence would be in line with this position.

Low or nil tax jurisdictions are those countries or tax regimes that are determined to have a maximum corporate income tax rate lower than 60 percent of the Argentine corporate income tax rate (25%), considering all levels of government. The RD also defines a ‘special tax regime’ as those regulations or tax schemes that deviate from the general corporate income tax rate in the country, ending up with an effective tax rate lower than the general regime.

**Compliance: transfer pricing documentation and materiality threshold**

The RD introduced new transfer pricing documentation requirements, aligning the rules to Action 13 of the OECD’s BEPS initiative. The RD lists the content to be included in the Master File, the Local File, and the Country-by-Country Report. Further details on the information to be included and due dates are expected to be provided in a resolution to be issued by AFIP.

Master File and Local File obligations will not apply to those companies carrying out intercompany transactions that do not exceed the materiality threshold of ARS 3,000,000 (total amount of transactions) or ARS 300,000 (individual amount per transaction).

**Comparability analysis, risk assessment, and transfer pricing method consideration**

The RD introduces the documentation of the comparability analysis as mandatory, suggesting that taxpayers could, to this end, conduct a nine-step analysis similar to the OECD nine-step approach. Internal comparables have a higher degree of preference over external.

A risk assessment analysis for the transactions also is introduced, following an approach consistent with the OECD (six-step approach).

The analysis of the transactions must be performed on a stand-alone basis (i.e., each individual transaction having its own comparability analysis), allowing a combined analysis of different transactions when they are closely related.

For the analysis of the related transactions, information of the current tax period must be used for the tested party, while for the comparables it is possible to use more than one period, depending on the business and market conditions.

The RD also establishes that the transactions or business lines must be analyzed based on segmented financial information, following the financial statements of the taxpayer. If segmented financial information is not available in the financial statements, the results must be segmented following an approach that must be consistent year-on-year.

**Observation:** Additional AFIP guidance on this topic is needed.

Business strategies have been reintroduced as an acceptable comparability factor so long as the taxpayer documents it contemporaneously when the decision is made.

Regarding transfer pricing methods, the RD introduces specifically the residual profit split, indicating that taxpayers must inform in advance the use of this method to AFIP (further guidance needed in this respect). In addition, taxpayers are allowed to use ‘other methods’ if, due to the nature of the transactions — in particular for those transactions that involve the transfer of unique intangibles, financial assets with no public pricing, or unique assets that do not have comparables — the transfer pricing methods recognized by the RD could not be applied. Changes in the transfer pricing method from one year to the other must be duly justified.

Finally, the interquartile range was kept as the arm’s-length range when there are two or more comparables, but the adjustment is made now to the median (as opposed to the former point: median +/- 5%). In case of goods with public quotation, the arm’s-length range will be that between the maximum-minimum daily quote and the adjustment would be to the min-max average.

**Restriction on interest deduction**

As outlined in our prior Tax Insight, the tax reform introduced a BEPS-based rule capping the deduction on interest expense with local and foreign related parties to 30% of the taxpayer’s taxable income before interest, foreign exchange losses, and depreciation (EBITDA). An extension of the rule is that not only interest expenses must be taken into account for the ratio calculation, but also the foreign exchange losses generated by the financial intercompany debts.

The RD has clarified that the described 30% of the EBITDA limitation does not apply to interest subject to withholding tax, even when the provisions of a tax treaty (e.g., reduced rates or exemptions) apply. On the other hand, the foreign exchange losses generated by the financial debts not subject to withholding tax (e.g., the foreign
exchange losses generated by principal of loans) will be subject to the described deductibility restriction.

The limitation does not apply to situations in which it is demonstrated that the ratio of interest to EBITDA of the Argentine taxpayer is equal to or lower than the same ratio for its economic group — regarding debt with unrelated parties — for the same fiscal year. The RD has established that the ratio of the economic group will have to be supported through a special report to be issued by an independent public account. AFIP will rule the specific content of this report.

**Permanent establishment**

As outlined in our prior Tax Insight, the tax reform introduced a detailed definition of PE in the ITL, jointly with rules aiming at capturing profits generated by the PE. Further, the reform introduced a positive list of situations that give rise to a dependent agent status, where the local subject assumes risks that correspond to a foreign subject, or if it receives a remuneration independently of the outcome of the activities carried out, amid other assumptions.

Among other aspects, the RD has established that the mentioned situations that give rise to a dependent agent status are not deemed to constitute a PE, provided that the activities carried out by the subjects are of ‘ancillary or preparatory’ character.

**Observation:** The rule lacks guidance on criterion to characterize an activity as having a ‘preparatory or auxiliary character.’

Further, the RD has established that it will be considered that a dependent agent plays a significant role leading to the conclusion of a contract not only if the contract has been signed by that agent, but also if such contract has been signed by the enterprise without substantial modifications to the terms negotiated by the agent.

**Other aspects not regulated yet**

Other important aspects introduced by the tax reform in the Tax Procedural Law have not yet been regulated by the Argentine Executive. Such aspects include the Regime named ‘Determinaciones Conjuntas de Precios de Operaciones Internacionales’ (similar to an Advanced Pricing Arrangement (APA) program) and regulations that would make the Mutual Agreement Procedures (MAPs) effective.

**The takeaway**

The amendments introduced by the tax reform and regulated by the RD tend to align Argentine transfer pricing rules with international (OECD) standards, although some local deviation implications should be carefully analyzed.

Additional details to the regulations are expected with future resolutions to be enacted by AFIP, which will provide more specific and practical guidance.
Let’s talk

For a deeper discussion of how this issue might affect your business, please contact:

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