

More to be disclosed about transfer pricing

The Indonesian Tax Office (ITO) has introduced a new disclosure form for corporate taxpayers, effective for financial years ending on or after 31 December 2009, which requires taxpayers to make detailed disclosures relating to transactions with related parties and the type of documentation held to support the arm's length nature of these transactions. The new disclosure form (Special Attachment 3-A) significantly expands the existing disclosures, which were limited to simple disclosures about a taxpayer's related-party transactions. Specifically, the new disclosures include:

- Business details of the related parties that the taxpayer transacted with;
- Details of the nature and value of the taxpayer's related-party transactions;
- Details of the pricing methodologies applied to set/review the price of the taxpayer's related-party transactions, and the rationale for the selection of these methodologies;
- Disclosures regarding what transfer pricing documentation the taxpayer has prepared to demonstrate that its related-party transactions adhere to the arm's length principle (documentation relating to business profile, functions and ownership structure; types of transactions and any similar transactions with independent parties; analysis of OECD comparability factors; and the application of the most appropriate transfer pricing method).

While the ITO is yet to release detailed guidance relating to the content of transfer pricing documentation, the new disclosure requirements in the corporate income tax return are in line with the analysis that would be performed under an approach consistent with the OECD's "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations".

This latest development in transfer pricing compliance reinforces the ITO's continued focus in this area - after introducing mandatory documentation rules in December 2007, formally adopting the OECD pricing methods as acceptable methods to accept or review transfer prices in the Indonesian taxation law and transfer pricing issues becoming a focus area in tax audits.

Taxpayers need to commence planning and preparing early if they want to make positive responses to the disclosures regarding transfer pricing, as a considerable amount of time and effort may be required to prepare documentation which satisfies the OECD standard and allows the taxpayer to respond positively to the disclosures. For the majority of taxpayers, the filing deadline for the first income tax return containing the new disclosure requirements will be 31 March 2010.

Our experience to date indicates that the ITO is moving towards a systematic targeting of taxpayers for transfer pricing focused audits - and not responding positively on the new disclosure form will likely increase a taxpayer's risk of audit. Preparation of documentation in line with the OECD Guidelines, that supports the arm's length nature of a taxpayer's transfer prices has proven to be an effective mechanism by which to manage and mitigate the risk of transfer pricing audits or assessments. We recommend that all taxpayers that need to complete this form review their transfer pricing documentation position and consider what additional documentation may be required as soon as possible.