



## Tax Newsletter

Timely news and information on national tax issues

### Transfer Pricing considerations in deducting intra-group services

Currently, there are many companies that make transactions for services between related parties. However, it is important that these companies have a clear understanding of the factors that must be considered for avoiding possible objections by the Tax Administration when deducting such services or for mitigating the risk of adjustments, fines, or penalties imposed by the Treasury Department (*Ministerio de Hacienda*) due to non-compliance with local transfer pricing regulations.

Based on the above, we can note that when we mention to intra-group services, this corresponds to any activity performed by a member of a business group (*service provider*) that generates a benefit for one or various members of this group, of which the

most common services are of an administrative, commercial, financial, or technical nature.

Furthermore, chapter VII of the updated guidelines published by the Organization for Economic Cooperation and Development (OECD) in January 2022<sup>1</sup> establishes that the main factors to consider with respect to intra-group services are documenting whether the service has in fact been provided, and whether this activity implies economic or commercial value for a group member that enhances or maintains its business position. In addition, this chapter refers to the determination of what the remuneration for these services should be in accordance with the arm's length principle. However, it is important to emphasize that the Salvadorian Tax Administration has additional factors that it considers in its oversight

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<sup>1</sup> [OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022 | READ online \(oecd-ilibrary.org\)](#)

processes for verifying the deductibility of the intra-group charges, which are:



- 1) **Materialization.** The materialization of the services is a decisive factor so that the services can be considered as intra-group services from the arm's length principle. This factor corresponds to having available the documentation that can prove that the services were actually provided. As evidence of the above, it is recommended that the taxpayer have contracts for the services received, invoices and receipts for payments made, schedules for the services, or any supporting documentation that demonstrates their existence.
- 2) **Usefulness and necessity of the service.** In order to determine the usefulness and necessity of the service, it is essential to be able to demonstrate that in comparable circumstances the taxpayer would have requested these services from an independent third party for the development of its business and would have been willing to pay for such services. Based on the above, the taxpayer must have the documentation that demonstrates the following factors:
  - Duplicate services: the taxpayer must be able to prove that it does not have personnel in its organization that perform the same functions that have been contracted. Furthermore, in the event that the taxpayer has a department that may generally perform similar functions (*human*

*resources, accounting, and marketing, among others*), the taxpayer should have a thorough detail of the functions performed by its personnel and the functions contracted, in order to have evidence that there is no duplicate functions.

- Shareholder activities: the taxpayer must be able to demonstrate that the functions performed do not correspond to activities exercised by a shareholder, which may include the providing of services to other group members, for example, services that would be provided by a coordinating center, detailed planning services for particular operations, costs related to the legal structure of the parent company, general shareholders' meetings, issuance of shares, stock exchange listing, costs related to the preparation of consolidated financial statements of the multinational group, or technical advice or assistance in day-to-day management.

In addition, to validate that the cost or expense is necessary for the business, the questions asked and information requested by the Tax Administration tend to be very detailed:

- Current organizational structure of the company, in order to verify the existing departments and internal functions performed by the taxpayer.
- Number, name, and position of permanent, temporary or outsourced employees that form part of each department, in order to verify whether there is any duplication of functions.
- Individualization of the payment made to related companies for each type of service received (not an overall charge,

but rather individualized by type of service).

- Indication of who within the organizational structure requested and authorized the service, by providing a copy of the requests and approvals.
- Indication of who or what department received the service, and what the result, benefit or added value was within the operations, in order to demonstrate the necessity for the corporate charge.
- Indication of who authorized the budget allocated to these charges, by providing a copy of this authorization.
- If there are other corporate charges received from related companies (e.g., royalties), there must be evidence that these are of a different nature and never could they be interpreted as duplicate charges.

**3) Appropriate documentation.** The taxpayer must have the documentation that permits verifying the transaction, contracts, reports, various tasks performed by the service provider, report on the calculation of the payment, cost allocation method, method for determining the total costs and expenses allocated to the calculation of the agreed upon fees, documentation of the risks assumed and assets involved in the providing of the service, determination of the level of specialization of the services received or provided, and documentation that supports the transaction (*exchange of letters, electronic mails, reports, work reports, detail of services and hours invested, and records of participation, among others*).

**4) Duly recorded.** The invoicing for intra-group services must be done through a direct or indirect method, which allows for demonstrating the cost allocation key, records of the information systems, and the detail of costs and expenses incurred for the services

provided, proper recording of the transaction in accounting, services supported by an identifiable and expected benefit, and documentation that reflects the calculations of the consideration agreed upon and the estimated costs and expenses.

**5) Appropriate tax withholding.** For the proper withholding of the corresponding tax, it is important that the taxpayer verify the domicile of the company with which it performed the transaction, both for related companies and independent third parties. The above has the purpose of verifying whether due to its domicile, the service provider is considered as a party domiciled in a state, country, or territory of low or zero taxation or a tax haven.

To facilitate the above, in September of each year the Tax Administration issues the "Tax Haven Guide." For the year 2022, the applicable guide is version "006.002/2021."<sup>2</sup> Based on the above, it is required that the taxpayer verify the domicile of the service provider and check whether such domicile is listed in the guide mentioned above, since this could result in a change in the Income Tax withholding rate, which depending on the transaction performed, could vary from 5% or 20% to a 25% withholding.

**6) Market value of the transaction.** The transaction performed between the related parties, or with an independent party that is domiciled, established, or located in a preferential tax regime, should be agreed upon at market value. Based on the above, the taxpayer should have all of the documentation (**transfer pricing study**) that permits verifying that the transaction is agreed upon in compliance with the arm's length principle, adhering to the

<sup>2</sup> [\(Microsoft Word - DGII Gu\355a Reg\355menes Fiscales Preferentes 2021 V CON FIRMAS REV DG V2\) \(transparenciafiscal.gob.sv\)](#)

methodologies of analysis detailed in the Tax Code and those established by the OECD.

### Final comments

Although many taxpayers are in compliance with some or most of the factors mentioned above, it is important to indicate that the factors described correspond to a step-by-step review process performed by the Tax Administration. Therefore, the taxpayer must comply with all of these factors, Otherwise, if the Tax Administration audits the taxpayer and the taxpayer has failed to comply with all of what was described above, there is a high probability that the Tax Administration will rule to consider the intra-group services agreed upon as non-deductible, and depending on which factor was not complied with, it could also result in a fine or penalty.

Therefore, it is essential that taxpayers give high importance to all of the factors described above when performing intra-group service transactions, regardless of whether the transactions are performed on a temporary or recurring basis, since being in compliance with these factors could mitigate the risk of objection to the deductibility of the expenses for Income Tax purposes, and thus avoid fines, significant adjustments, or penalties.



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# Tax Calendar

## September 2022

The updated 2022 tax calendar is now available on the Tax Administration's website, which includes public holidays and deadlines for all tax obligations.

S	M	T	W	T	F	S
				1	2	3
4	5	6	7	8	9	10
11	12	13	14	15	16	17
18	19	20	21	22	23	24
25	26	27	28	29	30	



Download the 2022  
Obligations Calendar

### September 14

#### VAT

Declaration and payment of the Tax on the Transfer of Movable Goods and the Rendering of Services (F-07).

#### Financial Income and Transactions

Monthly declaration of Payment on Account, and Tax Withheld on Income, Financial Transactions, and the Special Contribution for Citizen Security and Coexistence (F-14).

#### Specific and Ad Valorem Taxes

Declaration and payment of Specific Taxes, Ad Valorem Taxes and Special Contribution (F-06).

#### Other Obligations

- Report on donations (F-960)
- Report on Specific and Ad Valorem Taxes on Producers and

Importers of Alcoholic Beverages, Potable Ethyl Alcohol and Beer, Carbonated Beverages, Isotonic Beverages, Fortified Beverages or Energy Drinks, Juices, Nectars, Soft Drinks and Concentrated or Powder Mixtures for the Preparation of Drinks (F-955).

- Report on Specific and Ad Valorem Taxes on Producers and Importers of Firearms, Ammunitions, Explosives and Similar Items, Producers of Tobacco and Producers, Importers and those that clear fuels through customs (F-988).
- Monthly Report of Sales to Producers, Distributors or Retailers of Tobacco and Tobacco Products (F-956).
- Statement of Origin and Application of Funds (F-950).

### September 22

#### VAT

Monthly Report on Withholdings, Collections, or Payments on Account of VAT (F-930).

#### Printing Presses

Monthly Report on Documents Printed for Taxpayers Registered under the VAT (F-945).

### September 15

Public holiday celebrating  
Independence Day.

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