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Transfer pricing

Make your frontline defense against transfer pricing audits cohesive, consistent, and cost-efficient

What is transfer pricing?

Transfer pricing ensures that taxpayers clearly reflect income attributable to controlled transactions (i.e. transactions between related parties) and prevents avoidance of taxes with respect to those transactions.

Transfer pricing rules place a controlled taxpayer on tax parity with an uncontrolled taxpayer by determining the true taxable income of the controlled taxpayer. In the Turkish transfer pricing landscape, Corporate Tax Law Article 13 on Disguised Income Distribution Through Transfer Pricing lays out the details of the principal regulations governing transfer pricing. The Turkish regulations are generally consistent with OECD Guidelines and other transfer pricing regulations around the world.

A controlled transaction meets the "arm’s length standard" if the results of the transaction are consistent with the results that would have been realized if uncontrolled taxpayers had engaged in the same transaction under the same circumstances.

Methodology

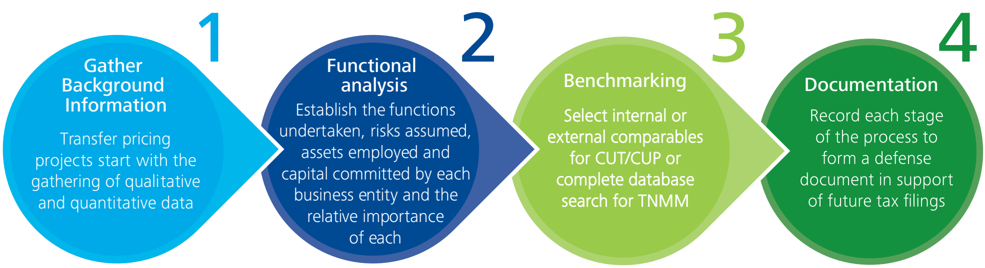
Several different methods are available for evaluating whether transactions between or among members of the controlled group satisfy the arm's length standard:

- **Comparable uncontrolled price method** offers a direct comparison between an intra-group transfer price and the price charged for the same or similar property or services transferred between third parties
- **Resale price method** takes the price at which a product is resold to an independent entity after being initially purchased from an associated entity, and reduces this price by an appropriate gross margin, the "resale price margin"
- **Cost plus method** adds an appropriate mark-up to the costs incurred by the supplier of property or services in a controlled transaction for property transferred or services provided to a related purchaser
- **Transactional net margin method** examines the operating profit from controlled transactions as a percentage of a base such as sales, costs, or assets
- **Profit split method** allocates operating profits or losses from controlled transactions in proportion to the relative contributions made by each party in creating the combined profits or losses
- Other methods

Although the methodology is complex and laid out in quite detail in regulations:

- Judgment calls are frequently needed; and
- Its practice requires prowess in a wide array of backgrounds such as economics, statistics, tax law, accounting, etc.

Managing the process



Documentation requirements

Documentation obligations in Turkey are twofold:

1) "Form Relating to Transfer Pricing, Controlled Foreign Companies, and Thin Capitalization"; and
2) Annual Documentation Report.

Taxpayers are required by law to maintain annual documentation with the Turkish Revenue Authority which is to be submitted to officials upon request.

The documentation must be completed by the deadline in order to be deemed "contemporaneous":

- Turkish and non-Turkish tax jurisdictions may have different deadlines for contemporaneous documentation; and
- In Turkey, documentation must be completed by the time taxes are filed.

If TP documentation is not completed before filing taxes:

- TP adjustments may require amendment and re-filing of tax returns;
- Re-files may raise red flags with the Turkish Revenue Administration; and
- Possible asymmetries in upwards vs. downwards adjustments may lead to suboptimal outcomes.

Turkish TP Environment

Does taxpayer have related transactions?

Yes

No

No need for transfer pricing documentation

Is taxpayer registered to LTP* tax office?

Yes

Scope of TP report:
- domestic related transactions
- cross-border related transactions

No

Scope of TP report:
- cross-border related transactions

* LTP: Large Tax Payers

Risk management

What needs to be done to avoid TP-related penalties and income adjustments?

- Must have a sound and locally & globally consistent TP policy;
- Must make sure that the TP policies are actually implemented; and
- Must have proper documentation in place.

TP compliance efforts may fail if not careful with implementation – in the end actual conduct is looked at and not the intention.

Globally inconsistent TP policies may have significant tax consequences.

It is a good idea to have intercompany agreements in place: e.g. for HQ services, distributorship, technical assistance, etc.

- Make TP policies more transparent; and
- Lay out the distribution of functions & risks clearly.

CAUTION

Past

- Flexible ad hoc defenses
- Adversarial approach to tax office

Present

- Show documentation up front
- Stiff enforcement and penalties
- Conflicts over methodology

How we may assist you

We provide a wide-array of tailor-made solutions for specific transfer pricing issues you may face. The enumeration below provides a partial list of our services:

- Transfer pricing documentation services for Turkish tax compliance purposes
- Global masterfile localization services for Turkish tax compliance purposes
- Transfer pricing planning studies to ensure compliance on a go-forward basis
- Transfer pricing risk analyses to identify past and/or future risks
- Headquarter cost allocation service studies
- Audit defense support for transfer pricing disputes
- Support with advance pricing agreement (APA) petitions and negotiations

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Dr. Toros is a Partner in the transfer pricing service line in Deloitte's Istanbul office. Prior to joining the Turkish transfer pricing practice, he has worked as a transfer pricing specialist in the Dallas and Washington, D.C. National offices of Deloitte Tax LLP in the U.S.A. for over 7 years. Dr. Toros' work has involved special emphasis on intellectual property migration and global documentation projects.

For more information

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