TRANSFER PRICING: BEYOND DOCUMENTATION

WHY YOUR TP POLICY SHOULD ALIGN WITH YOUR OPERATIONS

TP INSIGHTS

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The Problem: The Documentation Trap

Many multinational enterprises (MNEs) spend time and effort crafting detailed transfer pricing documentation (TPD). While this is necessary, there is a critical issue - the Documentation Trap. If TP policies do not align with actual transactions, affected entities are exposed to substantial risk during an audit.

Tax authorities, including the Zambia Revenue Authority (ZRA), do not evaluate transfer pricing based solely on the documentation; financial data, contracts, and operational documentation are analysed to verify compliance. Should there be a mismatch between policy and practice, potential repercussions include:

- **Tax adjustments** that increase your liability
- **Heavy penalties** for non-compliance
- **Increased audit scrutiny,** leading to further investigations.

Given the increase in scrutiny and with ZRA ramping up its audit activities, companies must ensure that TPD is not only comprehensive but also accurate and reflective of existing positions and practices.

The Risk: Policy Mismatches

So, what are the most common misalignment issues?

- **Functional Profile vs Actual Operations** - The TPD describes a functional profile which differs from the actual operations.
- **Pricing Policy Discrepancies** - The TPD details a pricing policy which is not consistently followed in practice.
- **Contracts vs Actual Practice** - Agreements set out specific terms (e.g., exclusivity, volume commitments), but real-world transactions follow a different pattern.
- **Unsubstantiated Cost Allocations** - Shared service costs aren’t allocated based on economic substance often with missing or inappropriate allocation keys.

Why Alignment Matters?

- **Compliance Beyond Paper:** Tax authorities focus on economic reality, not just documentation. If financials, contracts, and actual business activities don’t align with your TP policy, expect scrutiny.
- **Economic Substance is Key**: Your business functions, assets, and risks should support your transfer pricing methodology—on paper and in practice.
- **Avoiding Costly Adjustments:** A mismatch between TP policies and real transactions can lead to tax adjustments, disputes, and penalties.

How to Ensure Alignment?

- **Regular TP Policy Reviews** - Does your policy still reflect your business model?
- **Functional & Risk Analysis** - Are key roles and risks properly allocated?
- **Transaction Testing** - Do actual intra-group transactions align with policy benchmarks?

Final Thought: Be Audit-Ready

Transfer pricing compliance isn’t just about having documentation—it’s about ensuring your transactions tell the same story as your policies. If you’re not sure whether your policies align with reality, it’s time for a review.

Are you confident your TP documentation aligns with your actual transactions?

Let’s discuss!

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