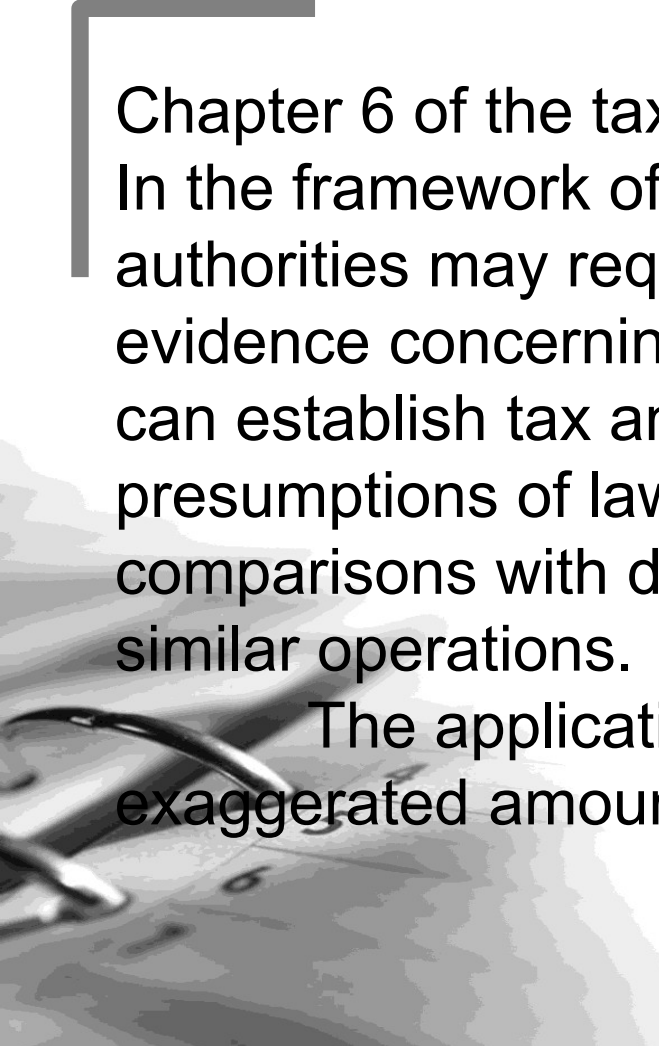


# Tax base erosion through transfer pricing The Tunisian experience

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# Legislative framework



Chapter 6 of the tax rights and procedures code:  
In the framework of the control or verification the tax authorities may request any information, clarification or evidence concerning the tax situation of the taxpayer. It can establish tax and correct statements based on presumptions of law or presumptions of fact comprising comparisons with data regarding income sources or similar operations.

The application of penalties for incomplete or exaggerated amounts on declared operations.



# Legislative framework

In the framework of agreements to avoid double taxation

Article 9 of the agreements to avoid double taxation provides that each State can calculate the tax base depending on what is the case for independent companies, since the article 9 granted each state the possibility to modify the reduced profits due to transactions between dependent companies.

Articles 11 and 12 also provide for the non application of preferential provisions on all excessive amounts paid compared to the amounts that can be paid in the framework of transactions between independent enterprises.

# Legislative framework

## **ARTICLE 48 septies of the personal income tax and corporate tax code**

When the tax authorities establish the existence of commercial or financial transactions between a company and other companies having a relationship of dependence, the determination of their value are governed by rules that differ from those governing independent enterprises, that is the reduced profit arising from the adoption of these rules shall be added to the results of that enterprise.

The provisions apply in cases where it is established that the price of transactions performed by the concerned company differs from the price of the transactions performed in respect of other customers or transaction prices charged by independent companies and exercising such activity or when it is determined that the charges were incurred in respect of unjustified operations and these operations or transactions resulted on a reduction in the payment of the tax due.

# The content of the procedure

The Tax Administration can adjust the profits which could have been reduced due to the adoption of the companies, which have relationships of dependence in the existence of commercial or financial transactions, to rules that differ from those governing independent enterprises in case of proofs that the reduction of profits led to a reduction of tax due.

# Terms of the application of the procedure

The application of the amendment provided for in article 51 of the Finance Bill 2010 is subject to two conditions:

First, the tax administration proves there is a relationship of dependence between the company that is concerned by the modification and the company which benefited from the transaction, and

Secondly, the tax administration proves the existence of transfer pricing between the companies which led to the reduction of tax due.

# Terms of the application of the procedure

Furthermore, article 51 of the Finance Bill 2010 has expanded the field of application of the above provisions to include foreign companies which are residents in countries with which Tunisia has not concluded yet an agreement on the avoidance of double taxation.



# Relationship of dependence

## Legal dependence

A company is considered as having relationship of dependence when:

A company is considered as being dependent to another company when the company exercises an authority in the other company directly or through intermediaries.

As well as for each company which has a capital in another company either it is important or has the majority of votes of shareholders, even if the headquarter of the company is located outside Tunisia.

Are also considered companies having relationship of dependence, the parent companies and subsidiaries as defined in the Code of Commercial enterprises and partner companies and common companies as defined in the accounting standards.

# Relationship of dependence

## De facto dependence

In case there is no proof of the legal dependence it is required to prove the existence of a physical dependence that can be contractual between the two companies.

Indeed the relationship of dependence can be contractual for a resident or a permanent establishment in Tunisia with a company established abroad with which it has a contract fixing the operations of purchases and sales that shall be followed by the first company and it shall also inform it of all operations.

The relationship of dependence could also be proven through correspondences between the two companies or periodic reports sent by the company exercising in Tunisia to the company established abroad.

## Existence of transfer pricing that led to a reduction in due tax

Furthermore the existence of a relationship of dependence between the companies, the administration must also prove that the operations which are subject to the modification do not fall under the normal management of the company and represent transfer pricing that led to a reduction in due tax.

# Cases of application of the procedure

Where there's modification of transfer of profits through the increase or reduction in the purchase or selling prices and in case the approved price of transaction by the concerned company differs depending on the customer with whom there is a relationship of dependence or not , or that the price differs from the one approved by other company exercising the same activity.

And it is considered a different price if the price is remarkably higher or less than the approved price with other customers or between two independent companies or the current market price of the same goods or services in the context of free competition.

# Cases of application of the procedure

It is also the case for a company concerned by the adjustment carries an unjustified or exaggerated burden compared to the service rendered i.e. royalties paid for the use or right to use property produced or developed by an enterprise which is situated abroad or offering privileges that are inadequate to the service rendered such as exaggerated wages, fees, commissions, transportation costs and advertisements. Or that the company carries the burden of services rendered for its account by a resident company in Tunisia or abroad with amounts exceeding those due to the recovery of the actual expenses.

# Cases of application of the procedure

Transfer of profits can be made by any other method:

- Attributing interest-free loans or with concessional terms (surplus ratio is less than the applicable rates in the context of free competition)
- Attributing unjustified commercial cuts or exceeding those granted to other companies.

It is worth mentioning that the modification is not applicable in case of failure to reach proof of transfer of profits through the above mentioned methods or by any other method which have led to a reduction in the payment of tax due.

# Practical example

A parent company active in the manufacturing industry sector owns more than 90% of the capital of the company established in a regional development area (benefits from a deduction of profits arising from exploitation).

Suppose that the parent company has achieved in a given year tax profits of 600,000 dinars taking into account the results of the sale process of raw materials for the benefit of the company established in the development and estimated at 200,000 dinars (20,000 units at a price of 10 dinars per unit).

Let's assume that the parent company has been subject to a tax audit for the same year and that the review process indicated that they sold raw materials for the benefit of others customers for the same material specifications that have been selling them for the benefit of the subsidiary company at a price of 25 dinars for the unit.

# Practical example

In this case and when we apply article 51 of the finance bill for the year 2010 and considering:

- The presence of relationship of dependence between the two companies,
- Selling price adopted by the parent company with its subsidiary company differs from the price billed to other customers ,
- The adoption of the parent company for a price less than the approved price led to a reduction in the taxable profit and thus converted a part of the profit margin for the benefit of its subsidiary and that this margin will be exempted from tax as it benefits from a deduction of profits arising from exploitation).



# Practical example

The profit of the parent company is modified and is integrated within the taxable profit for the concerned year which was transferred to its subsidiary, i.e. :  
300.000 Dinars :  $(20.000 \times (25d - 10d))$

According to this adjustment the fiscal profit equals:  
 $900.000 \text{ dinars} = 600.000d + 300.000d$

Fines for delayed payments are applicable according to the current law.

# Application Problems

The application of Article 48 Septies of the income tax and the corporate tax Code to problems at the level of application:

The procedure is applied and limited to companies with which it has relations of dependence and the tax administration needs to prove the existence of such relations between the company which benefited from the modification of prices and the company which benefited from the transfer of prices in order to be able to modify the transfer prices.

- When the tax administration proves that the transfer prices resulted in a reduction of the due tax it cannot modify the rates when the companies have no relationship of dependence.
- The introduction of Article 48 septies mentioned the income tax on natural persons and corporate tax Code led to a restriction in the application of the provisions contained by the income tax and the corporate tax exclusively and this led to the reduction of the area of intervention of the tax control services considering that Article 6 of the tax rights and procedures code is more comprehensive than article 48 septies which allows the tax control services to adjust all tax returns.