Pacific Association of Tax Administrators (PATA) Transfer Pricing Documentation Package

I. Introduction

The PATA members, which include Australia, Canada, Japan and the United States, are providing principles under which taxpayers can create uniform transfer pricing documentation ("PATA Documentation Package") so that one set of documentation can meet their respective transfer pricing documentation provisions. Use of this PATA Documentation Package by taxpayers is voluntary and does not impose any legal requirements greater than those imposed under the local laws of a PATA member. In this regard, it should be noted that each PATA member has different legal systems, statutes, regulations and administrative approaches with respect to transfer pricing[i]. The PATA members, after reviewing their respective domestic laws regarding transfer pricing and documentation of controlled transactions[ii], agree that a multinational enterprise ("MNE") will satisfy each PATA member's documentation provisions by complying with all of the principles contained in this PATA Documentation Package, and will thus avoid the imposition of the PATA members' transfer pricing penalties[iii] with respect to the documented transactions among associated enterprises resident in PATA member jurisdictions. However, satisfaction of the principles of this PATA Documentation Package does not preclude PATA member tax administrations from making transfer pricing adjustments, and assessing any interest due on those adjustments.

This PATA Documentation Package responds to the potential difficulties that MNEs face in complying with the laws and administrative requirements of multiple tax jurisdictions. MNEs may face significant and potentially costly duplicative administrative requirements in order to meet the transfer pricing documentation standards of the different jurisdictions. By providing taxpayers with the option of applying this uniform documentation package, the PATA members intend to assist taxpayers to efficiently prepare and maintain useful transfer pricing documentation, and timely produce such documentation upon request to PATA member tax administrations while precluding any related transfer pricing penalties. It is considered that this documentation package is consistent with the general principles outlined in Chapter V of the Organisation for Economic Co-operation and Development Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ("OECD Guidelines").

II. The PATA Documentation Package

Taxpayers that choose to use the PATA Documentation Package in order to avoid the imposition of PATA member transfer pricing penalties with respect to a transaction need to satisfy three operative principles. First, MNEs need to make reasonable efforts, as determined by each PATA member tax administration, to establish transfer prices in compliance with the arm's length principle. Second, MNEs need to maintain contemporaneous documentation of their efforts to comply with the arm's length principle. Third, MNEs need to produce, in a timely manner, that documentation upon request by a PATA member tax administrator. These three operative principles are more fully explained below.

A. Efforts to comply with the arm's length principle in establishing transfer prices

The first principle is that taxpayers need to make reasonable efforts to establish their transfer pricing in accordance with the arm's length principle. Such efforts include, but are not limited to, analysis of controlled transactions, searches for comparable transactions between independent enterprises dealing at arm's length, and selection and application of transfer pricing methods that are reasonably concluded to produce arm's length results in accordance with applicable PATA member transfer pricing rules and the relevant treaty, consistent with the OECD Guidelines.

B. Contemporaneous documentation of efforts to comply with the arm's length principle

The second principle is that taxpayers need to reasonably and contemporaneously document their efforts to comply with the arm's length principle. Contemporaneous documentation helps taxpayers and tax administrations in the examination process by giving taxpayers notice of information needed to assess whether prices of controlled transactions comply with the arm's length principle. Such documentation also provides tax administrations with useful analysis of controlled transactions between associated enterprises and assists in minimizing controversies over potential transfer pricing issues. Documentation is contemporaneous if it is existing or brought into existence no later than the due date, under the relevant PATA member's rules, of a timely filed (taking into account extensions allowed by the PATA member) income tax return for the taxation year of the controlled transactions at issue (and includes relevant information through such date).

The attached schedule[iv] describes the documentation for purposes of satisfying the second operative principle of the PATA Documentation Package. An analysis under the arm's length principle is generally based on information about the associated enterprises involved in the controlled transactions, the transactions at issue, the relevant functions, assets and risks, and information derived from independent enterprises engaged in similar transactions or businesses. A taxpayer needs to prepare and maintain the documentation for transactions or arrangements between itself and an associated enterprise resident in another PATA member jurisdiction, as necessary to demonstrate compliance with the arm's length principle. Transfer pricing documentation prepared and maintained pursuant to this PATA Documentation Package needs to be adequate and of sufficient quality so as to evidence that the taxpayer reasonably concluded that it selected and applied a transfer pricing method that produced an arm's length result in accordance with applicable PATA member transfer pricing rules and the relevant treaty, consistent with the OECD Guidelines. In evaluating the quality of an MNE's documentation, each PATA member tax administration will take into account all the relevant facts and circumstances, which for example may include: the extent to which reliable data was reasonably available and analysed in a reasonable manner and the significance, importance and complexity of the taxpayer's transfer pricing issues.

Additional information not listed on the attached schedule may be requested by a PATA member tax administration as necessary to examine an MNE's conclusions as to the arm's length nature of its arrangements.

C. Timely production of documentation evidencing efforts to comply with the arm's length principle

The third general principle is that taxpayers need to timely produce the foregoing documentation upon request by a PATA member tax administration in order to benefit from the penalty protection afforded by this Package. Upon request by a PATA member tax administration, documentation needs to be provided to a tax administration in accordance with each PATA member's respective rules, if any, on timely production of documentation. A PATA member may request a PATA Documentation Package only to the extent it relates to transactions involving that jurisdiction, and as provided by each PATA member's domestic laws and relevant treaty. It is usually in a taxpayer's interest to provide this documentation to the tax administration early in a transfer pricing review or audit as it will assist in demonstrating whether its transfer pricing is appropriate for tax purposes. The confidentiality of the information submitted by taxpayers will be safeguarded in accordance with the usual treaty and domestic laws regarding disclosure.

TRANSFER PRICING DOCUMENTATION TO BE PROVIDED BY TAXPAYERS

To avoid the imposition of PATA member transfer pricing penalties, the taxpayer needs to maintain and upon request, produce in a timely manner, documentation of sufficient quality so as to accurately and completely describe the transfer pricing analysis conducted by the taxpayer and the efforts to comply with the arm's length principle. The list of documents below is considered to be exhaustive. That is, it includes all documents that the PATA tax administrations view as necessary in order to provide transfer pricing penalty relief under this package. However, it is recognized that in certain instances, some of the documents below would not be needed. For example, where a taxpayer is not involved in a Cost Contribution Arrangement or market share strategy, it follows that the documents relevant to such arrangement or strategy are not needed.

Organizational structure	▪ Identification of the participants in the related party dealings and their relationship (with a brief history of and any significant changes in the relationship), including associated enterprises whose transactions directly or indirectly affect the pricing of the related party dealings ▪ A description of taxpayer's worldwide organizational structure (including an organization chart) covering all associated enterprises engaged in transactions potentially relevant to determining an arm's length price for the documented transactions
Nature of the business/industry and market conditions	▪ An outline of the business including a relevant recent history of the taxpayer, the industries operated in, the general economic and legal issues affecting the business and industry, and the taxpayer's business lines ▪ The corporate business plans to the extent they give an insight into the nature and purpose of the relevant transactions between the associated enterprises ▪ A description of internal procedures and controls in place at the time of the related party dealings ▪ Analysis of the economic and legal factors that affect the pricing of taxpayer's property and services ▪ A description of the structure, intensity and dynamics of the relevant competitive environment(s) ▪ A description of intangible property potentially relevant to the pricing of the taxpayer's property or services in the controlled transactions ▪ Copies of annual reports and financial statements for the year to which the Package relates and the prior five years ▪ Information as to the functions performed, assets employed and risks assumed relevant to the transactions ▪ An explanation of capital relationships (e.g., balance and source of debt and equity funding) relevant to the transactions

Controlled transactions	▪ A description of the controlled transactions that identifies the property or services to which the transaction relates and any intangible rights or property attached thereto, the participants, the scope, timing, frequency of, type, and value of the controlled transactions (including all relevant related party dealings in relevant geographic markets), as well as the currency of the transactions, and the terms and conditions of the transactions and their relationship to the terms and conditions of each other transaction entered into between the participants ▪ Identification of internal data relating to the controlled transactions ▪ Copies of all relevant inter-company agreements
Assumptions, strategies, policies	▪ Relevant information regarding business strategies and special circumstances at issue, for example, set-off transactions, market share strategies, distribution channel selection and management strategies that influenced the determination of transfer prices ▪ If the taxpayer pursues a market share strategy, documentation demonstrating that appropriate analysis was done prior to implementing the strategy, that the strategy is pursued only for a reasonable period, and that the costs borne by each associated enterprise are proportionate to projected benefits to such enterprise ▪ Assumptions and information regarding factors that influenced the setting of prices or the establishment of any pricing policies for the taxpayer and the related party group as a whole
Cost contribution arrangements (CCA)[v]	▪ A copy of the CCA agreement that is contemporaneous with its formation (and any revision) and any other agreements relating to the application of the CCA between the CCA participants ▪ A list of the arrangement's participants, and any other associated enterprises that will benefit from the CCA ▪ The extent of the use of CCA property by associated enterprises which are not CCA participants, including the amounts of consideration paid or payable by these non-participants for use of the CCA property ▪ A description of the scope of the activities to be undertaken, including any intangible or class of intangibles in existence or intended to be developed ▪ A description of each participant's interest in the results of the CCA activities ▪ The duration of the arrangement ▪ Procedures for and consequences of a participant entering or withdrawing from the agreement (i.e., buy-in and buy-out payments) and for the modification or termination of the agreement ▪ The total amount of contributions incurred pursuant to the arrangement

Cost contribution arrangements (continued)	▪ The contributions borne by each participant and the form and value of each participant's initial contributions (including research) with a description of how the value of initial and ongoing contributions is determined and how accounting principles are applied ▪ A description of the method used to determine each participant's share of the contributions including projections used to estimate benefits, any rationale and assumptions underlying the projections, and an explanation of why that method was selected ▪ The consistent accounting method used to determine the contributions and benefits (including the method used to translate foreign currencies), and to the extent that the method materially differs from accounting principles accepted in the relevant PATA member's country, an explanation of the material differences ▪ Identification of each participant's expected benefits to be derived from the CCA, the extent of the benefits expected, and the formula and projections used for allocating or sharing the expected benefits, and the rationale and assumptions underlying the expected benefits ▪ Where material differences arise between projected benefits and actual benefits realized, the assumptions made to project future benefits need to be amended for future years, and the revised assumptions documented ▪ Procedures governing balancing payments, e.g. where payments are required to reflect differences between projected benefits and actual benefits realized
Comparability, functional and risk analysis	▪ Description of the comparables including, for tangible property, its physical features, quality, availability; for services, the nature and extent of the services; and for intangible property, the form of the transaction, the type of intangible, the rights to use the intangible that are assigned, and the anticipated benefits from its use ▪ Documentation to support material factors that could affect prices or profits in arm's length dealings ▪ For the taxpayer and the comparable, identify the factors taken into account by the taxpayer to evaluate comparability, including the characteristics of the property or service transferred, the functions performed (and the significance of those functions in terms of their frequency, nature and value to the respective parties), the assets employed (taking into consideration their age, market value, location, etc.), the risks assumed (including risks such as market risk, financial risk, and credit risk), the terms and conditions of the contract, the business strategies pursued, the economic circumstances (for example, the geographic location, market size, competitive environment, availability of substitute goods and services, levels of supply and demand, nature

Comparability, functional and risk analysis (continued)	and extent of government regulations, and costs of production, etc.), and any other special circumstances ▪ Criteria used in the selection of comparables including database screens and economic considerations ▪ Identification of any internal comparables ▪ Adjustments (and reasons for those adjustments) made to the comparables ▪ Aggregation analysis (grouping of transactions for comparability) ▪ Supporting transfer pricing methodology or methodologies used, if any ▪ If a range is used, documentation supporting the establishment of the range ▪ Extension of the analysis over a number of years with reasons for the years chosen, where relevant
Selection of the transfer pricing method	▪ Description of the method selected and the reasons why it was selected, including, for example, economic analysis and projections relied upon ▪ Description of the data and methods considered and the analysis performed to determine the transfer pricing and an explanation of why alternate methods considered were not selected
Application of the transfer pricing method	▪ Documentation of assumptions and judgments made in the course of determining an arm's length outcome (refer to the comparability, functional and risk analysis section above) ▪ Documentation of all calculations made in applying the selected method, and of any adjustment factors, in respect of both the taxpayer and the comparable ▪ Appropriate updates of prior year documentation relied upon in the current year to reflect adjustments for any material changes in the relevant facts and circumstances
Background documents	▪ Documents that provide the foundation for or otherwise support or were referred to in developing the transfer pricing analysis
Index to documents	▪ General index of documents and a description of the record-keeping system used for cataloging and assessing those documents (required in the United States and encouraged, but not required, by other PATA members). The general index is not required to be prepared contemporaneously.

[i] For example, PATA member laws incorporate guidance on transfer pricing documentation consistent with Chapter V of the Organisation for Economic Co-operation and Development Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ("OECD Guidelines") in different manners, some by reference to the prudent business management principles under section 5.4 of the OECD Guidelines, others through an evaluation of whether documentation maintained is of sufficient quality to establish that a taxpayer reasonably concluded its transfer pricing is in accordance with the arm's length principle, others by both.

[ii] Changes to this Documentation Package may be necessary to reflect future changes to the transfer pricing documentation provisions of PATA members. Any such changes to the Documentation Package would be agreed by PATA members and made publicly available on or before the date on which the revised Documentation Package takes effect. If a PATA member determines that it must withdraw, either temporarily or indefinitely, from this agreement because a consensus on changes cannot be reached by the time required by the domestic provisions concerned, that PATA member will notify other PATA members of its withdrawal and issue a public notice thereof on or before the effective date of that withdrawal.

[iii] Australia, Canada and the United States have transfer pricing-related penalties that may be excused based on documentation that meets these PATA Documentation Package principles. The term transfer pricing penalties refers to the following penalties:

- For Australia, penalties under Division 284 of the *Taxation Administration Act 1953* for the 2000-2001 income year onwards and section 225 of the *Income Tax Assessment Act 1936* for the 1999-2000 income year and earlier years.
- For Canada, penalties under subsection 247(3) of the Income Tax Act
- For U.S., accuracy related penalties under I.R.C. § 6662 for underpayments of tax attributable to substantial valuation misstatements under I.R.C. §§ 6662(e)(1)(B)(i) and (ii), and gross valuation misstatements under I.R.C. § 6662(h)(2)(A).

[iv] The schedule is divided by documentation headings. The headings are intended to group the documentation into areas or categories of the transfer pricing analysis to which the specified documentation relates. The order of the headings is in no way representative of the importance to be assigned to a particular heading.

[v] The current Japanese and Australian tax law does not provide specific treatment for CCA.