

# TRANSFER PRICES. ROMANIA VS. NORTH AMERICA STATES

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*The role of multinationals in Romania has increased since 1 January 2007, due to the increased integration of national economies and technological progress, particularly in the area of communications. This type of growth presents complex taxation issues for both tax administrations and multinationals, themselves, since separate country rules for taxation cannot be viewed in isolation, but must be addressed in a broad international context. In order to apply the separate entity approach to intra-group transactions, individual group members must be taxed on the basis that they act at arm's length in their dealing with each other. In this context, transfer prices are significant for both taxpayers and tax administrations because they determine in large part the income and expenses, and therefore taxable profit of associated enterprises in different tax jurisdictions.*

*Multinational enterprise, associated company, transfer prices, arm's length transaction, tax jurisdiction*

## **What is transfer price?**

Transfer prices are the prices at which an enterprise transfers physical goods and intangible property or provides services to associated enterprises. By associated enterprises, we understand, that one of the enterprises participates directly or indirectly in the management, control or capital of the other or if the same persons participate directly or indirectly in the management, control or capital of both enterprises.

Transfer pricing issues originally arose in dealings between associated enterprises operating within the same jurisdiction, but with time and the growth of world economy and increased integration of national economies, this issue should be dealt at international level. And these international aspects are more difficult to deal with because they involve more than one jurisdiction and therefore any adjustment to the transfer price in one jurisdiction implies that a corresponding change in another jurisdiction is appropriate.

## **Transfer pricing in Romania vs. North America**

In order to achieve the balance between the interest of taxpayers and tax administrators in a way that is fair to all parties, it is necessary to consider all aspects of system that are relevant in a transfer pricing case. One such aspect is the allocation of the burden of proof. In most jurisdictions, the tax administration bears the burden of proof, which may require the tax administration to make a prima facie showing that the taxpayer's pricing is inconsistent with the arm's length principle. It should be noted, however, that even in such a case a tax administration might still reasonably oblige the taxpayer to produce its records to enable the tax administration to undertake its examination of the controlled transactions. In other jurisdictions the taxpayer may bear the burden of proof in some respects. Some OECD Member countries, in respect of Article 9 of the OECD Model Tax Convention, have been established burden of proof rules in transfer pricing cases which override any contrary domestic provisions. Other countries, however, consider that Article 9 does not establish burden of proof rules (paragraph 4 of the Commentary on Article 9 of the OECD Model Tax Convention). Regardless of which party bears the burden of proof, an assessment of the fairness of the allocation of the burden of proof would have to be made in view of the other features of the jurisdiction's tax system that have a bearing on the overall administration of transfer pricing rules, including the resolution of disputes. These features include penalties, examination practices, administrative appeals processes, rules regarding payment of interest with respect to tax assessments and refunds, whether proposed tax deficiencies must be paid before protesting an adjustment, the statute of limitations, and the extent to which rules are made known in advance.

This Article focuses on the main issues of principle that arise in the transfer pricing area in North America region and Romania.

From the analysis of the legal requirements in United States, Canada and Romania, we conclude that there are a few common issues to be discussed and harmonized, as follows:

- a) the name of local taxing authority and what are the main statutory provisions in effect in each country;
- b) the current transfer pricing and regulatory provisions in effect in each country;
- c) details of the various transfer pricing methods allowed, and the priority with which each method is regarded;
- d) the specific penalties that the governing Tax Authority will impose on a transfer pricing transaction if the tax payer is found not to be in compliance with the transfer pricing rules imposed by that country;
- e) certain conditions that the tax payer has to satisfy in order to obtain the reduction in transfer pricing documentation penalty;
- f) governing tax authority requirements that ask the taxpayers to prepare and maintain written documentation to confirm that the amounts charged in relating party transactions are consistent with the arms length standard;
- g) types of information required as part of taxpayers documentation requirement;
- h) the deadline to prepare transfer pricing documentation;
- i) the deadline for submitting transfer pricing documentation;
- j) statute of limitations on assessment for transfer pricing adjustments;
- k) when do any assessments based on transactions begin;
- l) disclosures required with respect to relating party transactions;
- m) the level of risk of transfer pricing issues being scrutinized during the audit by the governing tax authorities;
- n) if the state have the ability to enter into Tax Authority approved multilateral or unilateral advance pricing agreements between group companies;
- o) the length of such agreements.

No.	Issues in discussion	United States	Canada	Romania
1	Taxing Authority and Tax Law	Internal Revenue Service	Canada Customs and Revenue Agency (CCRA)	National Fiscal Administration Agency
2	Regulations and Rulings	Extensive transfer pricing regulations issued under various sections of Internal Revenue Code	Section 237 of the Income Tax Act, the OECD guidelines, IC 87-2R International Transfer Pricing	Fiscal Code Fiscal Procedure Code, article 42, 79 and 219 Ministry of Finance Order 222 as of 8.02.2008 OECD Guidelines
3	Priorities and Pricing Methods	Best method under the Transfer Pricing Regulations	Traditional methods are preferable to the transactional profit methods	The price comparison method, the cost-plus method, the resale price method, any other method recognized in the transfer prices guidelines issued by

No.	Issues in discussion	United States	Canada	Romania
				the Organization for Economic Cooperation and Development.
4	Transfer Pricing Penalties	20% and 40% penalty on underpayment of tax due to Transfer pricing adjustment	10 % penalty on total transfer pricing adjustments, plus non deductible interest	0,1% penalty per day for tax due to transfer pricing adjustment (if it is a profit)  A fixed penalty of 2000 – 3500 lei for physical persons and 12000 – 14000 lei for enterprises
5	Reduction Penalties	No penalties apply; there was reasonable cause and the taxpayer acted in good faith with respect to the transaction	The transfer pricing penalty is reduced under the following conditions: - adjustments are less than the lesser of \$5million or - 10% of taxpayers gross revenue	Not applicable
6	Documentation Requirements	Extensive and contemporaneous transfer pricing required	Contemporaneous documentation required	Transfer pricing file
7	Categories of Documentation Requires	Extensive and contemporaneous transfer pricing documentation required include: (i) complete description of the transfer pricing method selected; (ii) complete description of the alternative methods considered; (iii) complete description of the controlled/related party transactions, (iv) complete description of the comparables used and how comparability was evaluated	Statutory required information: - Details of the property/ service involved; - Terms and conditions of the transaction; - Participants of the transaction; - Functions performed, property used and the risks assumed by the parties; - Data and methods considered and the analysis performed to determine the transfer prices; - The assumptions strategies and policies that influenced the	Transfer pricing file includes: - group information, including structure of group, history and financial information, details of group activities, business strategy, changes from the previous year, the assumption used to choose the method to determine the transfer price; - taxpayer information, including a detail presentation of transaction with affiliates, comparative analysis, affiliates and

No.	Issues in discussion	United States	Canada	Romania
			determination of the method applied.	permanent establishment, methods considered to determine the transfer prices, other information.
8	Deadline to Prepare Documentation	By filing date of income tax return	Corporations – within 6 months of year end Partnerships – within 5 months of fiscal year	Within 3 months of a written request from National Fiscal Administration Agency, which can be extended only once, at the written request of taxpayer with a maximum of 3 months
9	Deadline to Submit Documentation	Within 30 days of a request from the internal Revenue Service	Within 3 months from the date of service of a written request from the CCRA	Within 3 months of a written request from National Fiscal Administration Agency, which can be extended only once, at the written request of taxpayer with a maximum of 3 months
10	Statute of Limitations on Transfer pricing	General statute of limitations rules apply	Individuals, trusts and Canadian controlled companies – 6 years from date of initial assessments Other corporations – 7 years	Not applicable
11	Assessments	Not applicable	Not applicable	Not applicable
12	Return Disclosure – Related Party Transactions	From 5471 and 5472 disclosure related party transactions. These forms are required to be filed with the filer's US Income tax return	Tax return disclosure of transactions with shareholders associated/related parties	Financial statements disclosure of transaction with shareholders associates or other related parties
13	Audit Risk/Transfer Pricing Scrutiny	High	High	High
14	Advance Pricing Agreements	Advance Pricing Agreement Program in effect. The APA Program covers unilateral, bilateral and multilateral APAs. Appropriate APA term is	Unilateral and bilateral/multilateral available but bilateral/multilateral preferred.	Advance pricing agreements can be unilateral, bilateral and multilateral. Appropriate APA term is determined

No.	Issues in discussion	United States	Canada	Romania
		determined on a case-by-case basis.		on a case-by-case basis (up to 12 months for a unilateral APA, up to 18 months for bilateral and multilateral APA)

***Analysis of Transfer Pricing Legal Requirements in United States, Canada and Romania***

As it could be seen, the Romanian legislation offers place for improvement, the transfer pricing being a challenging domain both for taxation and economic matters within the Romanian economy. Up to now, it has been identify only a few adjustments made by Fiscal Authorities. For example, the rent charged by a company having a shareholder relation of 5% with a Romanian company has been increased up to the amortization cost plus 30%.

**Conclusion**

In conclusion, countries need to reconcile their legitimate right to tax the profits of a taxpayer based upon income and expenses that can reasonably be considered to arise within their territory with the need to avoid the taxation of the same item of income by more than one tax jurisdiction. Such double or multiple taxation can create an impediment to cross-border transactions in goods and services and the movement of capital.

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