



Tax & Legal - News Alert



October 2022

Change to the transfer pricing legislation – “associated enterprises”

In 2019, National Treasury proposed that the application of the South African transfer pricing rules be broadened by also including cross-border transactions etc that are carried on between “associated enterprises”. Following several postponements, the effective date for the proposed amendment was set for 1 January 2023 and the new rules will then apply in respect of years of assessment commencing on or after that date.

On 14 October 2022, SARS published a draft Interpretation Note to provide guidance in respect of the definition of the term “associated enterprise” ([link](#)).

Background

The term “associated enterprises” is defined in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, 2022. In terms of this definition, two enterprises are associated enterprises with respect to each other if one of the enterprises meets the conditions of Article 9, sub-paragraphs 1a) or 1b) of the OECD Model Tax Convention with respect to the other enterprise, which states that two enterprises are “associated enterprises”

“Where

- a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or*
- b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, ...”*

Observations

The term “associated enterprises” is very broad and requires further definition in terms of local law. In addition, the OECD Model Tax Convention is designed to assist countries entering into agreements for the avoidance of double taxation by giving examples and suggestions, which require specification in each individual case. The articles of the Model Tax Convention, including Article 9, which deals with potential double taxation arising from transfer pricing matters, are not intended to be universally applicable. Therefore, countries other than South Africa that also rely on the “associated enterprises” concept have defined this further in terms of their local law.

So what has really changed?

The introduction of the term “associated enterprises” substantially expands the coverage of section 31 and this suggests that section 31 now also covers the following types of transactions (but not limited to) :

- Transactions between indirectly related entities (see examples in interpretation note);
- Arrangements between Head Office and Branch;
- Global sourcing arrangements or preferred supplier/ customer agreements where prices of products/ services are influenced/ agreed by an associated enterprise;
- Economic dependency for business (sales or purchases);
- Transactions with associated enterprises that may hold or be held less than 20% if the circumstances suggest that either of the enterprises have the ability to exercise control or influence transfer prices; or
- Any other relationship of mutual interest between enterprises.

What to do

As a draft interpretation note has already been released it is to be expected that the proposed amendment to section 31 will be implemented as is. The Taxation Laws Amendment Bill, 2022, will be published in the coming days.

Taxpayers should review their cross-border transactions and ensure that not only those transactions with connected persons, but also those with associated enterprises are in line with the arm’s length principle and appropriately supported. This will include a review of agreements, an updated analysis of the potentially affected transactions amounts to ensure that Master File and/or Local File documentation is prepared and filed as required.

KPMG will be providing comments in respect of the draft interpretation note with a view to achieving clarity, certainty and consistency. If you have any comments/ suggestions and would like us to include these in our submission, please contact a member of our transfer pricing team.

If you require advice as to how this amendment to the South African transfer pricing rules may impact your business, please feel free to contact our team.



Natasha Vaidanis
Director
Head of International Tax &
Transfer Pricing
M: +27824581043
natasha.vaidanis@kpmg.co.za



Amit Chadha
Director
International Tax &
Transfer Pricing
M: +27791308540
amit.chadha@kpmg.co.za



Christian Wiesener
Associate Director
International Tax &
Transfer Pricing
M: +27827192012
christian.wiesener@kpmg.co.za



Lourika Goodburn
Associate Director
International Tax &
Transfer Pricing
M: +27636820029
lourika.goodburn@kpmg.co.za

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KPMG Tax & Legal

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