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An Overview of Transfer Pricing in Latin America

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Historically, the United States ("US") has prevented multinational companies' ("MNC") transfer pricing attempts by adopting IRC §482[1] which authorizes the Internal Revenue Service ("IRS") to allocate gross income, deductions, and credits between related parties in a way to avoid the evasion of the US tax base as to clearly reflect the income earned by each taxpayer in each transaction. In this way, the US follows the internationally accepted "arm's length principle", which aims at treating all transactions as if they were all with unrelated parties for economic and tax purposes.

The main accepted methods provided by the US regulations for obtaining a arm's length price are the: Comparable Uncontrolled Price Method ("CUP"); Resale Price Method ("RPM"); Cost Plus Method ("CPM"); Comparable Profits Method ("CPPM"); and the Profit Split Method ("PSM"). These methodologies are the basis for the preparation and/or procurement of complex economic transfer pricing studies ("TP Study") by US MNCs to establish global transfer pricing policies for US tax purposes. A TP study must be supported by contemporaneous documentation and updated on a periodical basis. In addition, through a binding agreement between the IRS and the MNC, called an Advanced Pricing Agreement ("APA") procedure, the IRS ensures compliance and at the same time offers taxpayers some degree of certainty in the planning of their business activities by applying a pre-determined agreed upon transfer pricing methodology to specific transactions between the MNC and related parties.

Following the US footsteps most recently Latin American countries such as Argentina, Brazil, Colombia, Chile, Ecuador, Mexico, Peru and Venezuela have also created transfer pricing legislation to curtail MNCs to protect against the erosion of their respective tax bases. The transfer pricing rules adopted in all these above mentioned countries generally follow the Organization for Economic Cooperation and Development ("OECD") guidelines, which were first issued in 1979 (with the exception of Brazil).

As a result, a somewhat homogenous "playing field" can be found between the only OECD member country that is Mexico and the other Latin American countries that are non-OECD countries when dealing with transfer pricing issues. Thus, normally a MNC's TP Study prepared in the US can be used as a basis for the subsequent studies required in other OECD guideline compliant jurisdictions in Latin America (with the exception of Brazil).

However, the non-existent US Tax Treaty network (which only includes Mexico and Venezuela at this time) with Latin American countries does not allow any relief when the over-

[1]"In any case of two or more organizations, trades, or businesses(whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, the Secretary may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among such organizations, trades, or businesses, if he determines that such distribution, apportionment, or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades, or businesses. In the case of any transfer (or license) of intangible property (within the meaning of section 936(h)(3)(B)), the income with respect to such transfer or license shall be commensurate with the income attributable to the intangible".

lapping of transfer pricing rules may cause double taxation of a US MNC's income in non-Treaty Latin American countries. The Tax Treaties usually provide an opportunity for taxpayers burdened by simultaneous transfer pricing rules to force their tax authorities to agree on the terms of a secondary adjustment.

The definition of acceptable prices between related parties for US tax purposes is a highly technical discussion and relies heavily on in-depth economic analyses and valuations. Whenever the discussion is with or involves an OECD country or with a country that adopts the OECD transfer pricing guidelines and/or has a Tax Treaty with the US, the debate tends to revolve around known variables contained in the OECD guidelines documented (or to be documented) in some version of a TP Study.

On the surface, this seems so when dealing with Latin American countries, once again excluding Brazil. Below, we present a comparison chart of the main transfer pricing rules in the region:

As can be seen from the chart, most of the rules were enacted less than 10 (ten) years ago and even though they follow the OECD guidelines there are significant differences from country to country.

For the above reasons, it is strongly suggested that when dealing with cross-border transfer pricing issues in Latin America, US MNCs:

(i) Do not rely on their global TP Study;

(ii) Take into account the differences between the US and each country's transfer pricing systems (ie. methodology, arm's length ranges, documentation procedures, etc.); and

(iii) Implement tailor-made transfer pricing documentation procedures for each country based on applicable legislation.

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Country	Rules Enacted	OECD Compliant	APA	Special Penalties	Documentation	Authority Inspections	Commissionaires Agreements Permitted
Argentina	2000	Yes	No	Yes	Yes	High	Yes
Brazil	1997	No	Partial	Ordinary	No	High	Yes
Chile	2003	Yes	No	Yes	No	Low	Limited
Colombia	2004	Yes	Yes	Ordinary	Yes	Low	Yes
Ecuador	2005	Yes	Not yet	Not yet	Yes	Not yet	Yes
Mexico	1994/1997	Yes	Yes	Yes	Yes	High	Yes
Peru	2001	Yes	Yes	Yes	Yes	Low	Yes
Venezuela	2002	Yes	Yes	Yes	Yes	Low	No

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