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# Global Tax Alert

News from Transfer Pricing

## Botswana issues transfer pricing regulations

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### Executive summary

On 12 July 2019, Botswana's Minister of Finance and Economic Development gazetted transfer pricing regulations (the Regulations). The Regulations follow the transfer pricing (TP) legislation that was gazetted at the end of 2018.<sup>1</sup> The Regulations are effective from 1 July 2019 and are based on the Organisation for Economic Cooperation and Development (OECD) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD TPG).

This Alert summarizes the key provisions of the Regulations.

### Detailed discussion

#### Scope of the Regulations

Under the Regulations, taxpayers have an obligation to prepare and provide transfer pricing documentation. This documentation is intended to allow the tax administration to assess the arm's-length nature of intra-group transactions.

#### Taxpayers subject to this new requirement

The regulations provide that this obligation is applicable for all direct or indirect transactions with "connected persons." The legislator has not specified in the Regulations, how this relationship is assessed. The assumption is that

“connected persons” shall have the meaning assigned to it in the principal act. For domestic transactions, the regulations have been limited only to transactions relating to an International Financial Services Center (IFSC) company.

### Documentation requirements

The documentation content requirements are relatively broad, and are in line with the elements recommended by the OECD TPG. In summary, the local file documentation should contain, inter alia, the following:

- a) Specific information about transactions that a taxpayer carries out with related companies
- b) Information on all related companies’ activities including agreements
- c) The overall transfer pricing policy of the group

### Documentation language

All transfer pricing documentation sent to the tax administration is to be drafted in Setswana or English.

### Submission of the documentation

The local file should be filed together with the tax return on the prescribed return-filing date. The detailed group information (Master File), however, will be required from only those taxpayers whose transactions with connected persons exceed BWP5 million. The Master File will be filed on notification from the tax authority and the due date will be stated in the notice. For failure to submit the required documentation, a penalty not exceeding BWP500,000 will be charged.

### Format of the documentation

The Regulations provide no guidance regarding the format in which the documentation should be filed i.e., manual or electronic.

### Required TP analysis

In addition to providing general guidelines on TP analysis as recommended by the OECD TPG, the Regulations specifically provide for the following:

#### A) TP methods

For the purposes of determining the arm’s-length price, only five methods have been approved. These and their corresponding financial indicators are shown in the table below.

TP method	Financial indicator
<b>Traditional methods</b>	
i. Comparable Uncontrolled Profit (CUP) method	Price
ii. Cost Plus method (CPM)	Mark up on costs
iii. Resale price method (RPM)	Resale margin
<b>Transaction methods</b>	
iv. Transaction Net Margin method (TNMM)	Net profit margin
v. Transaction Profit Split method (PSM)	Operating profit/loss split

The Regulations provide that where possible, the CUP is to be the default TP method. Where both the traditional and the transactional methods can be equally applied, the traditional methods are to be used. Furthermore, the taxpayer has been allowed to use any other method outside the approved methods provided the Commissioner General (CG) is satisfied that the TP method used is consistent with the Regulations and none of the five approved methods can be reasonably applied.

#### B) Comparability analysis

A provision has been made for taxpayers to use the following comparables:

- i) Internal - where one party to the controlled transaction is a party to the uncontrolled transaction
- ii) External - where both parties are not party to the uncontrolled transaction

However, the CG is not allowed to use secret comparables when challenging a transaction. Likewise, taxpayers have been obligated to use comparables which are easily accessible to the CG which may either be in the same geographical area or any other geographical area as approved by CG.

#### C) Specific arm’s-length pricing considerations for services (based on OECD TPG)

The regulations specifically provide that a charge for a service between connected persons shall be consistent with the arm’s-length principle (ALP) where:

- i) The service should actually be rendered
- ii) The service should provide an economic benefit to the recipient of the service

- iii) The charge for the service should be what an independent party is willing to pay
- iv) The amount aligns to what independent parties would have agreed upon

A charge for shareholders' services provided due to ownership interest are deemed to be inconsistent with the ALP.

#### **D) ALP consideration for license, sale or transfer of intangible property (IP)**

A further specific provision has been made in respect of transactions involving IP which requires an analysis of the following:

- ▶ The functions performed by both transferor and transferee
- ▶ The price an independent transferee would be willing to pay as well as the value
- ▶ Usefulness of the IP to the transferee

#### **Relevance of the OECD TPG**

Botswana joined the OECD Base Erosion and Profit Shifting Inclusive Framework in June 2017. It is with this background and commitment to the project that a specific provision has also been made in the regulations for the relevance of the OECD TPG as a source of interpretation of the regulations.

#### **Next steps**

The new TP documentation requirements introduce a significant new compliance obligation in Botswana. Taxpayers that are involved in cross-border transactions with related parties will need to review the new rules and take necessary steps to ensure they are able to comply with the new requirements. Botswana companies in multinational groups with transactions exceeding BWP5 million will also need to review their filing and notification requirements in Botswana and the countries in which other group members are resident.

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#### **Endnote**

1. The Regulations were gazetted through Statutory Instrument No. 80 of 2019.

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