

# Uncertainty about transfer pricing rules in Africa a concern for foreign companies

Companies doing business in Africa face several uncertainties, including how tax authorities will handle transfer pricing (TP). It is vital that organisations prepare comprehensive documentation to demonstrate their application of the arm's length principle and the procedures followed.



"The lower the sophistication of tax authorities in a particular country, the higher the TP risk," says PwC South Africa's transfer pricing expert, Jeannè Havinga.

"Most countries in Africa do not have formal TP guidelines, although there are exceptions," she says. "The Organisation for Economic Cooperation and Development (OECD) provides the broadest and most measurable TP standards and African countries who do not have formal TP legislation or Guidelines do sometimes refer to them, but only if the application is in their favour! In some cases, we've found strange "interpretations" of the Guidelines and when the tax authorities are questioned about the application of the Guidelines, they choose to remind the taxpayer that they (the authority) are not an OECD member and are not required to adhere to the Guidelines. This uncertainty keeps many a financial director awake at night!"

## An easy, profitable target

TP is an easy and profitable target area for tax authorities. Although most African countries have no specific legislation in the area, they do have anti-avoidance regulations. These regulations piggy-back on the arm's length principle, which states that the amount charged by one related party to another for a given product or service must be the same as if the parties were not related.

Adding to the uncertainty is the fact that some countries have lengthy statutes of limitation on tax (e.g. TP) assessments. In Botswana, Kenya and Nigeria, the limitation is eight, seven and six years respectively.

Where countries have set TP penalties, these are always high. In Namibia, the penalty is 200% on underpaid tax and 20% per annum interest on unpaid tax.

## Anti-avoidance legislation

Further north, Egypt is about to publish its TP guidelines. While there are no specific penalties yet, the country does have general anti-avoidance rules around the arm's length principle.

Nigeria, Kenya and Tanzania's tax authorities have all sought to enforce TP or anti-avoidance legislation. Kenya and Tanzania both have TP regulations, while Nigeria's anti-avoidance rules are broad enough to cause much uncertainty for foreign companies doing business there.

In Ghana, where many foreign companies are involved in mining, there are formal TP as well as general anti-avoidance rules, and the statute of limitation on assessment for TP adjustment is six years.

"Even in Mauritius, a low tax jurisdiction, tax regulations requires that transactions between related parties must be at arm's length and there are cases where this has been enforced," says Havinga.

## Key focus

Key focus areas for most African tax authorities in terms of TP are management and technical fees, interest-free loans, decreased profits and royalties.

Most countries accept European comparables, as there is no African benchmarking database, but most tax authorities insist these comparable need be adjusted to make them comparable to an emerging market business. Nigeria and Uganda, however, do not accept European comparables at all.

"We expect to see several TP court cases throughout Africa over the next few years, which will give us a much better indication of the thinking of the tax authorities - court cases have the effect of clearing up some of the uncertainty," says Havinga.

"In the meantime, companies working in Africa must maintain adequate TP documentation to reduce their exposure to TP risk or else tax authorities may apply penalties in addition to TP assessments which are based on very limited information."

PwC South Africa has prepared a comprehensive African Transfer Pricing Dashboard that shows different TP practices throughout the continent.

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