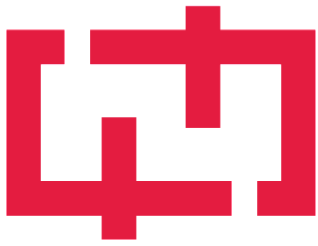


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Australian Taxation Transfer Pricing

The purpose of Australia's transfer pricing rules is to counter the underpayment of Australian tax by requiring businesses to price related party international transactions as if they were dealing with independent parties in order to ensure that the transaction is commercial.

Pricing for international dealings between related parties should reflect a fair return for the activities carried out in Australia, the Australian assets used (whether sold, lent or licensed), and the risks assumed in carrying out these activities. Where pricing is not in accordance with those conditions, the entity may be viewed as being involved in International Profit Shifting [IPS]

Methods of setting prices and reviewing the outcome of international transactions with related parties are recognised internationally using the arm's length principle, and Australia has adopted these in taxation rulings to help businesses understand what is expected of them. Essentially Australia is ensuring that there is also a proper matching process between the generation of income and the expenditure incurred in generating that income.

The Arm's Length Principle and Comparability

The arm's length principle uses the behaviour of independent parties as a basis to determine how income and expenses are allocated in international dealings between related parties. It involves comparing what a business has done and what a truly independent party would have done in the same or similar circumstances.

The internationally accepted arm's length methodologies are based on comparing the outcomes of related party dealings with the same or similar dealings of independent parties. The concept of comparability is central to the arm's length principle. As many factors may influence prices or margins, you need to closely examine the dealings you are comparing and the circumstances of the parties involved. The nature of this comparison with arm's length activity means that it is very difficult to achieve absolute precision and certainty. Accordingly the concept of materiality plays a big part in this assessment. The materiality depends on fully examining the facts and circumstances of each case and reflecting the reality that there is likely to be some element of uncertainty inherent in the judgments that have to be made.

Arm's Length Methodologies

There are several internationally accepted methodologies that business can use to comply with the arm's length principle. Australia does not have a preferred or particular method however the method adopted needs to be one which properly reflects the business' particular business case.