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GLOBAL TRANSFER PRICING SERVICES

Global Transfer Pricing Review

El Salvador

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TAX



El Salvador



KPMG observation

In El Salvador, the Tax Code includes transfer pricing rules from fiscal year 2010. The rules require Salvadorian taxpayers to document the arm's length nature of the intra-group transactions conducted with domestic and foreign related parties or with companies resident in low tax jurisdictions. The regulations require the taxpayer to produce transfer pricing documentation.

Failure to comply with the arm's length principle enables the Salvadorian tax authority to perform adjustments required to reflect arm's length transactions and to apply corresponding penalties.

Basic information

Tax authority name

Ministerio de Hacienda de El Salvador
– Dirección General de Impuestos Internos.

Citation for transfer pricing rules

- Art. 62-A of the Tax Code – Determination of prices.
- Art. 124-A and Art. 147 e) of the Tax Code – Transfer Pricing Documentation Requirements.
- Art. 135 f) of the Tax Code – Obligations of the Certified Public Accountant (CPA).
- Art. 199-A of the Tax Code – Tax authority power to determine adjustment if the transactions are not conducted in accordance with the arm's length principle.
- Art. 199-B of the Tax Code – Definition of arm's length principle.
- Art. 199-C of the Tax Code – Definition of Related Party.
- Art. 199-D of the Tax Code – Comparability Analysis and Adjustments.

Orientation Guide DG-001/2012.

Effective date of transfer pricing rules

1 January 2010.

What is the relationship threshold for transfer pricing rules to apply between parties?

Related parties are defined as follows:

- when one person or company directs or controls the other, or holds, direct or indirectly, at least 25 percent of its capital stock or voting rights
- when five or fewer persons direct or control both persons, or possess, direct or indirectly, at least 25 percent of participation in the capital stock or voting rights of both persons
- when companies belong to the same unit or business group decision. Specifically, two companies are part of the same unit or business group decision if one of them is a member or participant of the other and it is related to it in any of the following situations:
 - holds a majority of voting rights
 - has the power to appoint or remove the majority of the members of the board of directors
 - can dispose, under agreements with other partners of the majority of the voting rights
 - has appointed only with its votes the majority of the members of the board of directors

- most members of the board of directors of the acquired company are members or managers of the board of directors of the other company.

When two companies are part of each unit or business group decision in a third company, all companies will be integrated into a decision unit or business group.

- it is also considered that a person possesses participation in the capital stock or voting rights, when the ownership direct or indirect belongs to the spouse or person connected by relationship in direct or collateral, by consanguinity to the fourth degree or by affinity to the second degree
- in a union of persons, company event or business cooperation contract or joint venture agreement, when any of the contractors or partners participates directly or indirectly in more than 25 percent of the profit of the contract activities resulting from the association
- a person resident in the country and an exclusive distributor or agency thereof residing abroad
- a distributor or exclusive agent domiciled in the country of an entity domiciled abroad

- a person domiciled in the country and its supplier abroad, when the resident in the country make purchases, and the volume thereof represents more than 50 percent
- a person domiciled in the country and its permanent establishment abroad
- a permanent establishment located in the country and its parent company located abroad, another permanent establishment of the same or a person associated with it
- taxpayers must also document the arm's length nature of the transactions carried out with entities domiciled, incorporated, or located in countries, states or territories with preferential tax regimes, low or no taxation jurisdictions, or tax havens. Entities in preferential tax regimes, low or no taxation jurisdictions, or tax havens are those that meet any of the following requirements:
 - entities that are not taxed abroad, those who compute income tax on income or net income or taxable, less than 80 percent of income tax that would be caused in El Salvador
 - those classified by the Organisation for Economic Co-operation and Development (OECD) and the Financial Action Task Force.

What is the statute of limitations on assessment of transfer pricing adjustments?

Three years from filing date of the tax return but transfer pricing documentation must be maintained for 10 years.

Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be prepared or submitted to the revenue authority on an annual basis (e.g. with the tax return)?

Yes. Taxpayers are required to provide specific information in the transfer pricing studies to be prepared by taxpayers resident in El Salvador

documenting the arm's length nature of the domestic and cross-border intra-group transactions. In addition, taxpayers must file the transfer pricing information return.

What types of transfer pricing information must be disclosed?

The transfer pricing information return requires disclosing the following information:

- taxpayer's information:
 - identification number
 - legal name
 - fiscal year (start and end date of the fiscal year).
- detail of the controlled transactions:
 - legal name of the related parties
 - tax identification number of the related party
 - specification if the company is domiciled or not in El Salvador
 - code of the country of residence of the related party
 - relationship code (reason why the taxpayer in El Salvador and the related party are considered to be related parties and why the intra-group transaction is being documented)
 - code of the transaction
 - amount of the transaction in US dollars (USD)
 - specification if the determination of the market value took into account the following comparability criteria: characteristics of the transactions, functional analysis, assets and risks, contractual terms, micro and macro economic situation, and business strategies
 - specifications if the transfer pricing adjustments included: payment term, freight and insurance
 - transfer pricing method used.

What are the consequences of failure to prepare or submit disclosures?

If the taxpayers in El Salvador fail to comply with the requirement of

preparing the transfer pricing study, tax authorities will conduct appropriate analysis to determine the arm's length nature of the intra-group transactions and conduct the appropriate adjustments.

Transfer pricing study overview

Is preparation of a transfer pricing study required – i.e. can the taxpayer be penalized for mere failure to prepare a study?

Yes, the preparation of a transfer pricing report is required for all transactions for those taxpayers who carry out operations or transactions with related parties or parties domiciled, incorporated or located in countries, states or territories with preferential tax regimes, low or no taxation jurisdictions or tax havens. Taxpayers are also required to submit a transfer pricing information return disclosing specific information of cross-border and domestic intra-group transactions when such transactions (either individually or jointly) equals or exceeds USD571,429.

Other than complying with a requirement per the previous question, describe the benefits, if any, of preparing and maintaining a transfer pricing study?

Failure to prepare a transfer pricing documentation study will need to be disclosed in the annual tax opinion issued by a CPA. In addition, intra-group prices could be reviewed and determined by El Salvadorian tax authorities.

To satisfy the requirement and/or obtain the benefits, are there any requirements on when the transfer pricing study must be prepared and submitted?

The transfer pricing information return must be filed by 31 March while the transfer pricing documentation study must be ready 5 months after the end of the tax year.

When a transfer pricing study is prepared, should its content follow Chapter V of the OECD Guidelines?

Yes.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

Transfer pricing methods

Are transfer pricing methods outlined in Chapter II of the OECD Guidelines acceptable?

Yes. However, for the case of domestic, import and export transactions, the following methodologies will need to be considered (or disregarded) before applying OECD transfer pricing methods:

- **Market price in domestic operations:** The selling price of the goods or services of entities or establishments within the country unrelated to the tested party (third parties) that sell goods or render services with the same characteristics.
- **Market value in transferring goods or services abroad:** The price established by other entities (unrelated to the tested party) that sell the same products or render the same services from El Salvador to the same country abroad.
- **Import market price:** The price established for the same goods and services between third parties within the country in which the product or service is going to be acquired plus the freight charges if it the case.

Is there a priority among the acceptable methods?

Yes. Before applying the OECD transfer pricing methods, specific methods for domestic, import and export transactions will need to be used or disregarded.

If there is no priority of methods, is there a “best method” rule?

Not applicable.

Transfer pricing audit and penalties

When the tax authority requests a taxpayer’s transfer pricing documentation, how long does the taxpayer have to submit its documentation?

In practice, the taxpayer has 5 business days but can request a 20-day extension.

If an adjustment is proposed by the tax authority, are dispute resolution options available to the taxpayer outside of competent authority?

Yes, taxpayers can submit the resolution to an administrative area within the Ministry of Finance, in order to object to the procedures. Also, taxpayers may appeal to tax court.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

Yes. General tax penalties apply.

To what extent are transfer pricing penalties enforced?

Penalties are enforced in full by the Commissioner General and where a court process is preferred; the sanctions imposed by the court would subsist.

What defences are available with respect to penalties?

No experience yet.

What trends are being observed currently?

The transfer pricing rules are very recent and therefore there is no specific information about the target of audits. However, according to the law, the tax authority may estimate the taxable income if the prices or amounts of compensation do not comply with market value in accordance with the established methodology.

Special considerations

Are secret comparables used by tax authorities?

No.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

No.

Do tax authorities have requirements or preferences regarding databases for comparables?

No.

What level of interaction do tax authorities have with customs authorities?

Low.

Are management fees deductible?

Yes. However, taxpayers must support the fact that intra-group services have been rendered before a deduction is taken. That is, taxpayers must demonstrate that the services:

1. were actually rendered
2. provided a benefit to the taxpayer
3. were not duplicative services.

If no support can be provided, then the tax authority will consider them non-deductible.

Are management fees subject to withholding?

Yes. However, tax treaties may disallow withholding.

Are year-end transfer pricing adjustments permitted?

Yes. However, it is important that the year-end adjustments are accounted for before the end of the fiscal year to make sure tax and accounting figures are consistent. It is advisable to conduct periodic reviews in order to avoid significant year-end adjustments. Customs issues must also be taken into account.

Other unique attributes?

None.

Other recent developments

The first transfer pricing legislation was published in 2010 and the orientation guide or roadmap providing details on the production of documentation (i.e. No. DG-001/2012) was published in March 2012.

Tax treaty/double tax resolution

What is the extent of the double tax treaty network?

Minimal, only with Spain.

If extensive, is the competent authority effective in obtaining double tax relief?

Not applicable.

When may a taxpayer submit an adjustment to competent authority?

No formal rules.

May a taxpayer go to competent authority before paying tax?

No formal rules.

Advance pricing agreements

What advance pricing agreement (APA) options are available, if any?

No formal rules.

Is there a filing fee for APAs?

Not applicable.

Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

Not applicable.

Please provide some information on how successful the APA program is and whether there are any known difficulties?

Not applicable.

Language

In which language or languages can documentation be filed?

El Salvadorian tax authorities require all documentation to be in Spanish.

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