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Japan tax newsletter

Ernst & Young Tax Co.

Updates to Japanese Transfer Pricing Regulations 2019-2020

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Executive summary

Introduction

Over the last year and a half, the Japanese government has issued a series of revisions to the laws and regulations regarding transfer pricing. In March 2019, the Japanese government passed its 2019 Tax Reform Proposals into law, revising the primary and secondary legislation on transfer pricing (“the revised legislation”)[1]. In June 2019, the administrative guidance on transfer pricing was also updated (“the revised guidance”), providing further interpretation and explanation of the new legislation[2]. On 28 June 2020, the National Tax Agency ("NTA") released their commentary on the Special Taxation Measures Law Circular (“the STMLC commentary”)[3], providing additional explanations and the rationale for the changes made. In the same month, the NTA updated the guidance entitled “Documents recognized as necessary for the calculation of the arm’s length price (Local file guidance)” (“the local file guidance”)[4].

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[1] Primary legislation is issued by the Diet after being proposed by the ruling party, and in relation to transfer pricing is found in Special Taxation Measures Law (STML) Article 66-4. Secondary legislation is issued by the Cabinet or certain ministries, and in relation to transfer pricing is found in Special Taxation Measures Law Enforcement Regulations (STMLER), Article 39-12 and Special Taxation Measures Law Enforcement Order (STMLEO) Article 22-10.

[2] Administrative guidance is issued by the Commissioner of the NTA, and instructs the NTA and other bodies on the interpretation of the law. It consists of the Special Taxation Measures Law Circular (STMLC), the Commissioner’s Directive on the Operation of Transfer Pricing (Administrative Guidelines), and the Reference Case Studies on the Application of Transfer Pricing Taxation (Reference Case Studies).

[3] Commentary on the STMLC is released periodically by the NTA. These are not binding on any authority, but provide useful information on how tax authorities are likely to interpret certain passages of legislation, and the background to the enactment of such laws.

[4] The updated local file guidance is supplementary guidance to aid taxpayers unsure of what to include in a local file. It is available online at https://www.nta.go.jp/publication/pamph/pdf/takokuseki_00.pdf. The documents listed here are illustrative but not exhaustive, so the taxpayer should be ready to prepare additional items.

EY

Building a better working world

Many of the revisions are intended to bring Japan's transfer pricing legislation further into alignment with the OECD guidelines. The revisions relate to:

1. The definition of intangible assets
2. The introduction of the discounted cash flow ("DCF") method as a transfer pricing method
3. Retrospective price adjustments by the tax authorities related to hard-to-value intangible assets ("HTVIs")
4. Guidance on the use of the interquartile range ("IQR")
5. An extension of the statute of limitations for transfer pricing

The revisions are applicable to a corporation's fiscal years beginning on or after 1 April 2020. The revisions have a number of implications for companies' transfer pricing policies and approaches to transfer pricing documentation.

Purpose and implications of the revisions

We understand that the main purpose of these revisions is to align Japanese transfer pricing regulations with the latest OECD guidance on intangibles, rather than to implement a disguised "exit tax" whose primary motive is to increase tax revenue.

The revisions give taxpayers more certainty if they want to restructure and move intangibles outside of Japan, as there is now a clear framework for valuation and guidance on how to avoid those intangibles being revalued.

The revisions also clarify that valuation should be covered under transfer pricing legislation, which could help taxpayers to access Mutually Agreed Procedures ("MAP") if there is disagreement on the valuation of intangible assets between tax authorities.

Summary of next steps for taxpayers to consider

- The applicability of the DCF when selecting the transfer pricing method ("TPM") because Japan follows the best method approach when selecting TPM
- The possibility of transferring IP in or out of Japan as an alternative to licensing now that there is a clear method and guidance on the valuation of assets being transferred
- The need to perform robust valuations with detailed documentation to evidence valuation when transferring HTVIs
- Whether any existing intangible assets may be considered HTVIs under the updated guidance
- The execution of intercompany agreements in advance of any HTVI transfers
- Reviewing the pricing for transactions which rely on the full range to be considered arm's length and consider adjusting pricing to be within the interquartile range
- Reviewing reserve calculations and considering the need to update documentation retention policies to match the new statute of limitations

1. Definition of intangible assets subject to transfer pricing

Explanation

The definition of intangible assets for transfer pricing purposes has been revised in line with the definition used in Action 6.6 of the OECD Guidelines[5]. Under the revised legislation, an intangible asset is defined as any asset:

- which is not a tangible or financial asset; and
- whose lending, transfer, use or other similar action would be compensated in a transaction between independent parties in comparable circumstances[6]

Examples of intangible assets are given in the STMLC commentary[7], and include:

- Industrial property rights and other rights relating to technology, production methods using special technology or similar items
- Copyrights and related rights
- Mining rights, patent rights, utility model rights, trademarks and other fixed intangible assets
- Customer lists and sales networks
- Know-how and business secrets (this refers to proprietary information for the support or improvement of business activities which, unlike patents and trademarks, cannot be protected legally)
- Trade names and brands (trade names are often company names. Like brands, they are considered to have market penetration power, and are often registered as trademarks. Brands may be intangible assets such as trademarks, trade names, customer relationships, reputation or goodwill, or a combination of these)
- Rights established as a result of the licensing of an intangible asset or a transaction equivalent to a license transaction (a transaction equivalent to a license transaction is typically any right which, like a license, effectively recognizes the use of an intangible asset for a certain scope, in a certain period, in a specified geographic region)
- Contractual rights (excluding those listed above)
- Rights relating to government approvals and licenses

In line with the OECD guidelines, the updated list of intangible asset examples does not include group synergies, which are not considered capable of being transferred in return for consideration, or goodwill/going concern value, which does not necessarily arise in comparable transactions. Taxpayers should consider on a case-by-case basis whether group synergies or goodwill/going concern value need to be considered when selecting comparable transactions.

Next steps

- Taxpayers should review their value chain to ensure that all intangible assets under the new definition are appropriately documented in the Group's transfer pricing policy
- Items considered intangibles for accounting purposes may not include all intangibles under the transfer pricing definition, so the review should be conducted specifically for the purposes of transfer pricing

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[5] The definition given in the OECD Guidelines (2017) is as follows:

1. which is not a physical or financial asset;
2. which is capable of being owned or controlled for use in commercial activities; and
3. whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances.

[6] STMLEO, Article 39-12 paragraph 13

[7] STMLC Commentary, 66-4 (8)2

2. Introduction of the DCF method as a transfer pricing method

Explanation

The DCF method can be used to value foreign related party transactions involving intangible assets where it is not possible to utilize a method based on comparable transactions or the profit split method[8].

Under the revised guidance, the DCF method is considered less reliable than other transfer pricing methods because of its reliance on uncertain inputs such as sales forecasts. Taxpayers will need to carefully demonstrate why it is the best method available[9].

Considerations when valuing an intangible using the DCF method

DCF calculations are likely to be intensely scrutinized by the tax authorities. According to the revised guidance, the examiners will review the following aspects of the primary inputs into a DCF calculation:

Sales forecasts [10, 11]

- Whether forecasts are based on information which is reasonable and verifiable
- Whether forecasts are consistent with historical revenue figures.
- Whether growth rates applied to forecasts are consistent with both the future prospects of the business and market growth rates seen in similar businesses
- Whether projected sales forecasts have been appropriately risk-weighted when multiple forecasts are available (for example, where a "conservative" sales forecast and an "optimistic" sales forecast with higher numbers are available, it is likely to be appropriate to risk-weight the forecasts according to the likelihood of their outcome, rather than using only the most conservative sales forecasts in the DCF calculation)

Discount rate [12, 13, 14]

- Whether an appropriate method for calculating the discount rate has been used (in the Japanese guidance, the weighted average cost of capital (WACC) is specifically mentioned. The use of other discount factors should be clearly explained);
- Whether the WACC figure used is appropriate to the risk inherent in the business line which uses the intangible asset, rather than the company as a whole; and
- Whether business risk has been "double-counted", for example by being factored in to both the WACC and the forecast income figures.
- Whether the discount rate reflects the wide range of sources of business risk, including country risk and foreign exchange risk, for example

Forecast period [15]

- Whether the period for the sales forecasts accurately reflects the pace of technological change and thus expected economic life of the asset;
- Whether the sales forecast period reflects the legal term of ownership of the intangible; and
- Whether a terminal value has been included in cases where profits from the intangible are expected to arise in perpetuity

Tax amortization benefit [16]

- Whether the benefit which the buyer of an intangible obtains as a result of being able to amortize the asset in future years and reduce taxable income (tax amortization benefit or TAB) is reflected in the DCF calculation; and
- Whether the tax amortization benefit is congruent with the sales forecast (for example, an intangible should not be amortized if sales related to it are forecast in perpetuity)

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[8] (Special Taxation Measures Law Enforcement Regulations (STMLER), Article 39-12 paragraph 8 (vi))

[9] Administrative Guidelines, 4-3

[10] Administrative Guidelines, 4-13 (1) and (2)

[11] Reference Case Studies, Case 23

[12] Administrative Guidelines, 4-13 (3)

[13] STMLC, 66-4 (7)-2

[14] STMLC Commentary, 66-4 (7)-2

[15] Administrative Guidelines, 4-13 (4)

[16] Administrative Guidelines, 4-13 (5)

Documents required to support the DCF method and forecasts used [17]

For each business year for which profits are forecast in a DCF valuation, the taxpayer should prepare workpapers showing:

- The calculation of projected profit
- Reasons for using a terminal value, its validity and calculation method (if applicable)
- The appropriateness of assumptions used in the DCF calculation, such as growth rate and corporate tax rate
- The benchmarking study supporting an allocation of routine profit (if the taxpayer has calculated the routine profit accruing to one party using the Transactional Net Margin Method (TNMM)). See "Using the DCF method in practice" below for an example of this

The taxpayer should also prepare:

- Documents supporting the validity of the discount rate used, and showing how it was calculated
- Documents supporting the validity of the forecast period for which profit is expected

Financial forecasts should be supported with the following documents[18]:

- Third party evaluations confirming the reliability of business plans
- The rationale for using historical financial information as the basis of forecasts (if applicable), and the source and content of the information
- Documents explaining the purpose of the forecasts (e.g. management decisions, investment decisions, specifically for transfer pricing purposes), and to whom they were reported (shareholders meeting, the board of directors etc.)
- Any other supporting information such as industry and company reports prepared by specialists or research agencies

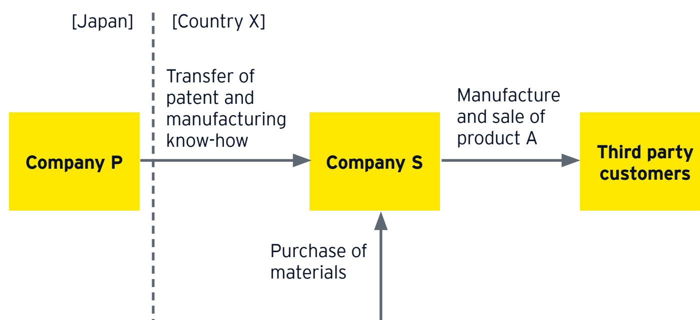
Methods similar to the DCF method

- The revised legislation also permits the use of "methods similar to the DCF method"
- The STMLC commentary states such similar methods would include[19]:
  - Cases where income is used rather than cash flows in the DCF calculation
  - Cases where negative cash flows arise in individual years of the multi-year DCF calculation

Using the DCF method in practice [20]

The NTA's Reference Case Studies show the DCF used in conjunction with other transfer pricing methods, giving guidance on how the NTA expects taxpayers to conduct the calculation. In the primary case study illustrating the application of the DCF method, Company P in Japan transfers a unique patent and associated manufacturing know-how ("the IP") related to Product A to its related party Company S, located in Country X. Company S procures raw materials domestically, and uses the IP to manufacture, promote and distribute Product A to third parties (see diagram below).

Figure 1: Transaction flow in NTA's DCF Reference Case Study



[17] Local file guidance, 2(4)

[18] Local file guidance, 2(5)

[19] STMLC Commentary, 66-4 (7)-1

[20] Reference Case Studies, Case 24

Within this case study the NTA first allocates profits to routine functions using the TNMM before proceeding to apply the DCF method. The calculation was as follows:

- Forecasts for Product A in Country X for 10 years were obtained from the business plan agreed at a directors meeting between Company P and Company S
- A benchmarking study was conducted to determine an arm's length return for companies performing manufacturing and distribution activities comparable to Company S using the TNMM
- The routine profits related to manufacturing and distribution and the forecast tax payments were deducted to arrive at the excess profit related to IP
- The forecast profits related to IP were discounted to present value using WACC as the discount rate
- The tax amortization benefit that Company S obtains from owning the IP is added on to calculate the arm's length value for the IP transfer
- The actual example calculation given by the NTA, and the assumptions underlying the calculation, are shown below

Figure 2: Sample DCF calculation in the NTA's Reference Case Studies

Initial DCF Calculation	Reference	Year									
		1	2	3	4	5	6	7	8	9	10
Sales	1	1000.00	1030.00	1060.90	1092.73	1125.51	1159.27	1194.05	1229.87	1266.77	1304.77
Operation profit	2	200.00	206.00	212.18	218.55	225.10	231.85	238.81	245.97	253.35	260.95
OM of comparable companies	3	7%	7%	7%	7%	7%	7%	7%	7%	7%	7%
Routine return based on TNMM	4 (1*3)	70.00	72.10	74.26	76.49	78.79	81.15	83.58	86.09	88.67	91.33
Residual pre-tax OP related to IP	5 (2-4)	130.00	133.90	137.92	142.05	146.32	150.71	155.23	159.88	164.68	169.62
Tax paid	6 (5*30%)	39.00	40.17	41.38	42.62	43.89	45.21	46.57	47.97	49.40	50.89
Residual post-tax OP related to IP	7 (5-6)	91.00	93.73	96.54	99.44	102.42	105.49	108.66	111.92	115.28	118.73
Discount factor (WACC 10%)	8	0.9535	0.8668	0.7880	0.7164	0.6512	0.5920	0.5382	0.4893	0.4448	0.4044
Present value of IP	9 (7*8)	86.77	81.24	76.07	71.23	66.70	62.46	58.48	54.76	51.27	48.01
Total present value of IP	10 (Σ9)	657									

Tax amortization benefit (TAB) calculation	Reference	Year				
		1	2	3	4	5
Amortization rate	11	20%	20%	20%	20%	20%
Effective tax rate	12	30%	30%	30%	30%	30%
Discount factor (WACC 10%)	13	0.9535	0.8668	0.7880	0.7164	0.6512
Present value effect of TAB	14 (11*12*13)	5.72%	5.20%	4.73%	4.30%	3.91%
Total present value effect of TAB	15 (Σ14)	23.85%				

Total present value effect of IP including TAB	16 (10/(100%-15))	863

Assumptions used in the calculation

- Sales of Product A are forecast to be 1000 in year 1, and to grow at 3% per year
- The operating profit margin resulting from sales of Product A is forecast to be 20%
- A benchmarking study shows the return on the routine manufacturing and distribution functions conducted by Company S for comparable companies to be 7%
- The effective tax rate of Company S in Country X is 30%
- The only business line of Company S is the sale of Product A, and the whole company's WACC is 10%
- The company's sales accrue evenly throughout the year, so discount factors are calculated on the basis that all sales occur at the midpoint of the year. The same applies to the TAB
- The cost of the IP can be amortized over 5 years under the tax law of Country X

Other ways of applying the DCF method

- In addition to this case study illustrating the DCF using the TNMM, the Reference Case Studies recognize that the Contribution Profit Split Method could be used with a DCF calculation
- In this case the company would split the income forecast by the DCF method between related parties in accordance with an allocation key which reflects each party's contribution to the development of the intangible
- The Reference Case Studies also recognize that an entire business may be transferred, including substantial intangible assets. In this case, it may be appropriate to aggregate the non-intangible assets and intangible assets and value the entire business using the DCF method
- In this case, the value of goodwill should also be factored in to the DCF calculation

Next steps

License vs transfer of IP

- Where taxpayers have previously hesitated to transfer intangibles into or out of Japan due to lack of clarity within the legislation regarding the appropriate transfer pricing, the revised legislation and guidance provides a methodology for such transfers. Therefore, taxpayers should consider, with greater confidence, the transfer of intellectual property as opposed to licensing

Documentation

- Taxpayers should review and update their Local Files and TP Policy documents to include the DCF when determining the most appropriate method for transactions with Japan

3. Transfer pricing adjustments relating to transactions involving hard-to-value intangible assets (HTVI)

Explanation

Update to definition of HTVIs

HTVIs (called "specified intangible assets" in the Japanese legislation) are intangibles which meet all of the following conditions[21]:

- the intangible is unique and has significant value;
- revenue forecasts were used as the basis for the arm's length valuation of the intangible; and
- the revenue forecasts used to value the intangible were deemed to be highly uncertain

This is significant because the Japanese tax authorities may adjust the value of an HTVI transferred between related parties if the transfer value based on forecasts is estimated to be significantly different from a later valuation conducted on the basis of actual data. See the section "Potential HTVI price adjustments" below for further information on this.

Guidance on the conditions an HTVI must meet

The STMLC commentary offers further guidance on each of these three conditions which define an HTVI:

- The intangible is unique and has significant value.
  For this condition to be met, the STMLC commentary notes that two criteria must be satisfied:
  (1) The intangible is not comparable to any intangible asset which could be used by parties to comparable transactions, and
  (2) The intangible's use in business activities (in manufacturing, the provision of services, marketing, sales, management etc.) is expected to generate a greater economic benefit than if the intangible had not been used[22].
- Revenue forecasts were used as the basis for the arm's length valuation of the intangible
  - The STMLC commentary notes that this condition is deemed to have been met if the most appropriate transfer pricing method is one which uses forecast profits to calculate the arm's length price. This will apply even if revenue forecasts at the time of the transaction were not used in the calculation of the arm's length price because the company did not believe the intangible to have significant value[23]. Therefore, an asset can be deemed to be an HTVI by the tax authorities, even if the taxpayer did not believe the intangible to be an HTVI
- The revenue forecasts used to value the intangible were deemed to be highly uncertain

This will be determined based on all relevant factors, such as:

(1) The basis for calculation and purpose of forecasts used in the valuation[24]
  - The STMLC commentary notes that, for example, business plans prepared solely for the purpose of fulfilling transfer pricing requirements will be considered less reliable than business plans prepared for the board of directors to make decisions regarding the business and investment, and so is more likely to be considered highly uncertain[25]

[21] STMLEO, Article 39-12 Paragraph 14
[22] STMLC Commentary 66-4 (9)-1
[23] STMLC Commentary 66-4 (9)-2
[24] STMLC 66-4 (9)-3
[25] STMLC Commentary 66-4 (9)-3

(2) The length of forecast period [26]

- The STMLC commentary notes that the longer-term forecasts become, the more unreliable they become, making long-term forecasts more likely to be considered highly uncertain[27]

(3) The availability of historic profitability data which supports the forecast figures [28]

- The STMLC commentary notes that forecasts for a new product will be considered less reliable than forecasts for a product already on the market for which past sales figures are available, and so are more likely to be considered highly uncertain[29]

(4) The future prospects of the business using the HTVI [30]

- The STMLC commentary that new businesses without assets similar to the one being transferred do not have experience of feasible growth rates for those assets, and therefore forecasts in this case are more likely to be considered highly uncertain[31]

(5) Any contractual provisions which stipulate price adjustments or conditional payments [32]

- The STMLC commentary notes that the presence of contractual terms stipulating price adjustments or conditional payments suggests that measures are already in place to respond to uncertainty, and therefore the valuation conducted at the time of the transaction will be considered less uncertain[33]

Possible indicators of HTVIs

The NTA also provides the following as indications that an intangible may be considered an HTVI[34]:

- The total amount of consideration paid for the intangible is fixed at the time of the transfer
- The intangible is still at the R&D stage
- The intangible is not expected to be used commercially for a certain period following the transaction
- The intangible is to be used in a new way for which there is no precedent

Potential HTVI price adjustments

In cases where the actual income arising from the HTVI over the five fiscal years from the first fiscal year in which the HTVI generates third-party revenue, is more than 20% above or below the original forecast income, the tax authorities may deem the arm's length price of the HTVI transaction to be the actual income generated, and levy tax on that basis[35]. This change gives the NTA the legal basis to challenge artificially low valuations of intangibles transferred from Japanese companies to entities outside Japan.

The STMLC commentary also notes that the profit forecast by the company from the intangible asset must be conducted on the basis of information as of the time the intangible asset transaction was conducted[36]. If this is not the case, the arm's length price can be recalculated on the basis of information as of the time of the intangible asset transaction, and the recalculated amount used to determine whether the 20% threshold has been reached.

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[26] STMLC 66-4 (9)-3

[27] STMLC Commentary 66-4 (9)-3

[28] STMLC 66-4 (9)-3

[29] STMLC Commentary 66-4 (9)-3

[30] STMLC 66-4 (9)-3

[31] STMLC Commentary 66-4 (9)-3

[32] STMLC 66-4 (9)-3

[33] STMLC Commentary 66-4 (9)-3

[34] Administrative Guidelines 4-15 (1)

[35] STML, Article 66-4 Paragraph 8 and STMLER, Article 39-12 Paragraph 16 Item (i) and (ii)

[36] STMLC Commentary, 66-4 (9)-2

Exemption from price adjustment for HTVIs

The HTVI transaction price will not be adjusted if both of the following sets of documents are submitted to the NTA upon request[37]:

- Documents that include details of the forecasts used to value the HTVI, which show the forecasts were based on reliable and verifiable evidence and using a reasonable method
- Documents that provide evidence that the difference between the forecast and actual income were caused by events which were extremely difficult to forecast, such as natural disasters or similar events [see next section for further details], or that the arm's length price was calculated appropriately taking into consideration the probability of the occurrence of such events at the time of the transaction

Definition of "similar events" to natural disasters

The STMLC commentary notes that "similar events" to natural disasters means events which, like natural disasters, clearly could not be predicted by the taxpayer at the time of the intangible asset transaction, but which were unavoidable and which had a significant direct impact on the value of the transaction[38]. Examples of similar events include:

- Significant changes in economic conditions as the result of a financial crisis
- Significant changes in the regulatory environment due to changes in legislation or government guidance
- Significant market changes, such as a dramatic change in market share for the business in which the intangible asset is used due to the collapse of a competitor

Taxpayers should note that exemption from adjustments to the valuation of intangibles only applies to transactions noted in the Schedule 17-4, which is appended to the tax return and records foreign related transactions during a corporation's business year[39]. Therefore it is essential that HTVI transactions are recorded in the Schedule 17-4 in the year of the transaction.

Next steps

- If intangibles are transferred, the taxpayer should consider whether the intangible meets the conditions of an HTVI, and document its conclusions, to reduce the risk of the tax authorities deeming an intangible to be an HTVI and assessing an adjustment to the price accordingly
- In order to reduce the chance of adjustments as a result of actual transaction value diverging by more than 20% from forecast transaction value, taxpayers should ensure that forecasts are properly documented, consistent with other transfer pricing documentation, and based on reliable and verifiable information that can be provided to tax authorities which shows that the forecasts were conducted as of the time of the transaction. It will be important to demonstrate to the NTA that the forecasts are from the business and not created purely for tax purposes
- If a company originally purchased HTVIs from a third party which it is then reselling to a related party, the valuations conducted at the time of the third party purchase may provide the basis for setting a transfer price; however, the valuation needs to be reviewed from a transfer pricing perspective in line with the new rules for the DCF method. Such information should be retained and used as the basis for valuation where reliable and relevant, along with consideration of its appropriateness for transfer pricing purposes
- Transfers of intangibles should also be supported by intercompany agreements which are signed and in place in advance of the transactions
- Given the potential for significant discrepancies between the forecast revenue from an asset and actual revenue, taxpayers may wish to consider a bilateral APA to provide protection from audit in both countries in relation to transactions involving significant HTVIs. Although an APA would not be available for a one-off sale of a HTVI, it could be used to cover the transaction (such as royalty or product transaction) after the sale of the HTVI. It could be possible to try and incorporate the sale of the HTVI into such an APA

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[37] STML Article 66-4 Paragraph 9

[38] STMLC Commentary 66-4 (9)-4

[39] STMLER Article 22-10 Paragraph 3

4. Interquartile Range

Explanation

The updated transfer pricing legislation provides guidance on the use of the interquartile range [40] (IQR). The IQR can be used if all of the following conditions are satisfied[41]:

- there are at least four comparable transactions;
- any adjustments for differences between the comparable transactions and tested transaction which can reliably be made have been made;
- there are remaining differences that are difficult to quantify, and the effect of those differences on comparability with the tested transaction is slight; and
- in cases where the IQR may be used and it has been appropriately applied, if the arm's length price falls within the IQR calculated, no transfer pricing adjustment will be made
- Both the IQR as calculated using Excel, or as calculated using the method approved by the IRS, are acceptable. However, consistency should be maintained across transactions.[42] In general, the IRS use this method in bilateral APAs[43]

Next steps

- Taxpayers still using the full range should revisit their transfer pricing policy and consider using the IQR or more carefully explaining why the full range is appropriate
- Taxpayers should review their intercompany transactions which use the IQR to test or set their transfer pricing to ensure that they meet the requirements outlined in the updated legislation and administrative guidance
- In particular, adjustments which have been made to comparable companies where the IQR has been used, and the adjustments considered difficult to make reliably, should be clearly documented

5. Changes to statute of limitations

Explanation

The statute of limitations for transfer pricing has been extended from six to seven years[44].

This extension may reflect the need for more time to evaluate DCF calculations based on how actual results compared with forecasts. In addition, it may reflect the tax authorities' need for more time to investigate transactions in industries where there may be a considerable time-lag between a transaction taking place and the realization of profits from that transaction.

Next steps

- Taxpayers should revisit their calculations of reserves where there is an uncertain tax position
- Taxpayers should also review their policies of retaining documents to ensure that the relevant information is stored for the full seven years potentially subject to adjustment

[40] STMLER Article 22-10 Paragraph 3

[41] Administrative Guidelines 4-4 and 4-5

[42] Reference Case Studies, Case 1

[43] Local file guidance, 2 (7)

[44] STML Article 66-4 Paragraphs 26 and 27

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