

Advantages and disadvantages of centralised and decentralised transfer pricing documentation (2)

2/50/24



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To pick up where we left off about preparing transfer pricing (TP) documentation, this article explores the advantages and disadvantages of a decentralised approach.

Decentralised TP documentation

A decentralised approach means that each subsidiary within a multinational enterprise group takes responsibility for preparing TP documentation. Each company uses local expertise and consultants to prepare its own TP file appropriate for its transactions and requirements.

Decentralised TP documentation has several advantages.

Local expertise

Local company representatives better understand the local market conditions, requirements and practices, which can serve as the basis for preparing TP documentation that is accurate and meets local requirements. Local companies can work with consultants in the particular country who specialise in TP matters and can help mitigate risks associated with TP documentation.

Responsiveness

Local teams are able to rapidly adapt the TP documentation to local requirements or recent practices, ensuring relevance and compliance. If any changes have been made to the company's structure and to the facts and circumstances of its related-party transactions, then each company preparing the documentation is able to promptly reflect such changes in its TP file.

Responsibility

Decentralised TP documentation could increase the engagement and responsibility of local company representatives, as they are personally responsible for developing the TP file according to local requirements and the company's actual operations.

Active engagement of the local company

Actively engaging in the analysis of controlled transactions helps the local company implement the group's TP methodology better and more accurately. Local staff gain a deeper understanding of how related-party transactions are analysed and TP methods applied, which helps prepare the TP file more efficiently and accurately.

Decentralised TP documentation has some disadvantages too.

Consistency

It could be difficult to secure consistency across all group companies, as each team might have a different approach and interpretation of TP requirements. This lack of consistency can make it difficult for group companies to defend their TP practices on a tax audit if the tax authorities mutually cooperate and compare the available information.

Costs

Each company needs to allocate resources for preparing TP documentation, which could be a costly and time-consuming exercise. These costs include not only direct costs incurred in preparing the documentation but also indirect costs such as staff time and effort being diverted away from other important tasks. If each company hires its own consultants, then extra costs could be incurred because consulting services can be expensive and the group might not have access to bulk discounts that would be available in the case of a centralised approach.

Key takeaways

The centralised and the decentralised approach to preparing TP documentation have their advantages and disadvantages. The choice depends on a variety of factors, including the size and structure of the group, the complexity of transactions, and the diversity of TP requirements in markets the group operates in. A hybrid approach that combines elements of centralised and decentralised TP documentation can often provide a balanced solution based on the strengths of each approach and minimising their weaknesses. At the end of the day, the goal is to ensure the TP documentation is accurate, compliant with local requirements and defensible, thus minimising the risk of disputes with tax authorities.