

SRS starts transfer pricing risk analysis under *Advise First!* principle (2/41/17)

As we know, the State Revenue Service (SRS) is responsible, among other things, for monitoring the correctness of computing and paying taxes, duties and other statutory charges. This article explores *Voluntary Transfer Pricing Risk Analysis*, a taxpayer consultation process the SRS has launched this year following the *Advise First!* principle. It is important to note that beginning the implementation of this principle is listed as an operational priority for 2017 in the SRS' public report for 2016. Implementing this principle is also envisaged in the SRS' operational and development strategy for 2017–2019.

The new SRS consultation process *Voluntary Transfer Pricing Risk Analysis*

In order to perform its tasks, i.e. to ensure that taxes and duties are calculated and collected in a complete, timely and fair manner, to avoid delays in increasing the efficiency and effectiveness of its core operational processes and to achieve a rational use of the allotted funds, the SRS focuses on planning tax control measures and selecting their targets.

Taxpayer control measures are selected by the SRS after evaluating the available information and identifying potential risk factors. Once the identified risks and the information available to the SRS have been assessed, taxpayers are selected for an appropriate tax control measure. The SRS conducts a variety of control measures on entities and individuals, from surveillance and inspection to data compliance checks, thematic reviews and tax audits.

To ensure compliance with the arm's length standard in transfer pricing, the SRS conducts two transfer pricing control measures that are well known to taxpayers: thematic reviews and audits.

This year, in line with international practice and the *Advise First!* principle, the SRS is invoking section 15.2 of the Taxes and Duties Act, which defines the taxpayer's obligation to provide information about transactions with related parties. Under this section the SRS has launched *Voluntary Transfer Pricing Risk Analysis*, a new consultation process related to checking multinational intragroup transactions.

As part of this analysis the SRS uses a set of criteria to select multinational enterprises – Latvian taxpayers who the SRS believes might have inherent transfer pricing risks. The SRS sends letters to those entities via the Electronic Declaration System and encourages them to provide information, within one month after receiving the request, about their transactions with related entities (persons) in particular periods.

After receiving the requested information from the entities, the SRS has undertaken to act as consultant before initiating any administrative procedure such as a transfer pricing audit. Those letters suggest that in the course of transfer pricing consultation the SRS pays attention to any errors made by the taxpayer and advises the taxpayer in order to better understand those errors, as well as offering a grace period to eliminate them without facing penalties.

Although the *Voluntary Transfer Pricing Risk Analysis* amounts to SRS' consulting services aimed at offering companies preventive assistance in eliminating tax risk, the SRS will resort to the penal system where an entity –

- refuses to cooperate with the SRS;
- fails to provide the information requested; or
- fails to take any steps the SRS has suggested for rectifying tax violations.

In such cases a statutory penalty can be imposed and there is a risk that the SRS will launch an advanced transfer pricing audit.

The chart for the *Voluntary Transfer Pricing Risk Analysis* consultation process



SRS control measures

In the first six months of 2017 the SRS conducted 5,427 tax control measures, of which in 773 cases the taxpayer was encouraged to rectify the discrepancies found during those measures. Some of those invitations might have been issued as part of *Voluntary Transfer Pricing Risk Analysis*.

For companies that are required to prepare information about transactions with related parties under section 15.2 of the Taxes and Duties Act because of exceeding the annual net revenue and transaction amount thresholds, we recommend preparing that information on a timely basis and assessing annually whether transactions with related entities (persons) meet the arm's length standard.