

It's soon time to prepare and submit transfer pricing files – let's focus on calculating amount of controlled transaction 1/36/24



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Since the current Latvian transfer pricing (TP) rules came into force back in 2018, companies are used to preparing and submitting a TP file in the second half of the current year. For most taxpayers, the financial year is the calendar year, which in conjunction with the TP rules means a TP file for the previous financial year must be submitted by 31 December of the current year.

Now is the right time to remember how the controlled transaction amount (CTA) should be calculated, so the taxpayer can make sure he meets the relevant requirements for preparing and/or submitting a TP file. It's crucial to calculate the CTA correctly, as this amount determines whether the taxpayer is liable to prepare a TP file, what form is required and whether he is also liable to submit the file to the State Revenue Service (SRS) within 12 months after the end of the financial year.

After the new TP rules came into force, the SRS has issued several guidelines and instructions on how to calculate the CTA depending on the type and substance of controlled transactions. Yet we still see cases where the CTA is computed incorrectly. For example, it does not include certain controlled transactions or is computed as the difference between revenue (for supplies of goods and services) and expenses (for acquisitions of goods and services). This is not the right approach and can expose the taxpayer to major TP risks arising from failure to duly prepare and submit a TP file because the CTA calculation is not correct.

What is the CTA and how do we calculate it?

Let's step back and strengthen our understanding of what constitutes a controlled transaction. In the most common and straightforward situation, this is a transaction between two related companies based in different tax jurisdictions. For example, a sale of goods between two group members, one of which is based in Latvia and the other in Estonia, qualifies as a controlled transaction. However, a similar transaction between group members in Latvia is a related-party transaction that does not count as a controlled transaction under section 15.2(2) of the Taxes and Duties Act. Both transactions are essentially related-party transactions, but only controlled transactions – those with a non-resident related party – are considered when computing the CTA, which determines the requirements for preparing and submitting a TP file.

Any transaction with a non-resident related party is essentially a controlled transaction, and this should be taken into account when determining the total CTA for the financial year. CTA calculations vary according to the type of transaction. All controlled transactions can be split into two major categories:

- Financial transactions (a loan, a credit line or a cash pool transaction)
- Other transactions (e.g. purchases and sales of goods, supplies and acquisitions of services, cost recharges, issuing a guarantee)

It's a good idea to separate financing transactions – they have their own specific CTA calculation procedures. We will not deal with them here, though, as we recently posted a separate article on this significant topic where we explained in detail how to determine the CTA in financing transactions.

In addition to transactions with non-residents, the CTA calculation for TP documentation purposes should also include transactions between the taxpayer and related individuals, entities or persons registered in tax havens, as well as transactions between related residents within a single supply chain. These business partners are described in section 15.2(2) of the Taxes and Duties Act.

Below we offer a general example of the CTA calculation for a company entering into controlled transactions (other than financing) in the financial year:

$$\text{CTA} = \text{total goods purchased} + \text{total goods sold} + \text{value of services acquired} + \text{value of services supplied} + \text{cost recharges (cost allocations)}$$

This calculation reflects typical controlled transactions that companies make in the course of business. We should also evaluate financing transactions (if any). And the CTA calculation should include some less popular controlled transactions, such as sales/acquisitions of shares (at arm's length) and issuing a guarantee, regardless of their economic substance or form.

CTA thresholds for preparing and submitting a TP file

As mentioned, it's crucial to calculate the CTA correctly, as it's used to determine whether the taxpayer should prepare only or prepare and submit a TP file to the SRS and in what form. The table below summarises information on the requirements for preparing and submitting a TP file:

Form of TP file	CTA ¹	Obligation to prepare and/or submit it to the SRS
Local file	EUR 250,000 < CTA < EUR 5,000,000	Must be prepared within 12 months after the end of the financial year and submitted within one month after receiving an SRS request
	CTA > EUR 5,000,000	Must be prepared and submitted within 12 months after the end of the financial year
	Revenue < EUR 50,000,000 and EUR 5,000,000 < CTA < EUR 15,000,000	Must be prepared within 12 months after the end of the financial year and submitted within one month after receiving an SRS request
Master file	CTA > EUR 15,000,000	Must be prepared and submitted within 12 months after the end of the financial year
	Revenue > EUR 50,000,000 and EUR 5,000,000 < CTA < EUR 15,000,000	

We ask all taxpayers entering into controlled transactions to carefully compute the CTA in order to identify relevant TP documentation requirements and be able to duly prepare the prescribed form of TP file, or to make sure the taxpayer is not subject to this obligation for the current financial year.

We also encourage you to contact us if you need support in computing the CTA for any non-standard or unusual related-party transactions, to carry out an objective TP analysis and verify the need to include those in your CTA calculation.

¹ The CTA in transactions that a resident company or permanent establishment makes with a related foreign company, a related individual, or an entity or individual based in a tax haven