



Schedule 25A instructions 2011

For use by companies, trusts, partnerships and funds to assist with completion of 2011 tax returns. NAT 2639-6.2011

28 September 2012

Includes where to show foreign branch non-assessable, non-exempt income and lists new exemption and country codes for foreign locations.

About these instructions

Schedule 25A instructions 2011 will help you complete Schedule 25A 2011 (NAT 1125).

These instructions include information about:

- related-party international dealings
- permanent establishments
- foreign branch non-assessable non-exempt income
- country codes for foreign locations
- pricing methods.

A worked example at **appendix 5** shows how a hypothetical Australian resident company would complete the schedule.

When we refer to 'you', 'your business' or 'taxpayer' in these instructions, we are referring either to you as a business entity (for example, a company, trust, partnership or superannuation fund) that conducts a business, or to you as the tax agent or public officer responsible for completing the schedule.

This publication is not a guide to income tax law. Please get help from the Australian Taxation Office (ATO) or a recognised tax adviser if you feel that this publication does not fully cover your circumstances.

Publications and services

To find out how to get a publication referred to in these instructions and for information about our other services, see [More information](#).

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Introduction

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These instructions will help you complete **Schedule 25A 2011**.

If you answered yes on your partnership, trust, company or fund tax return to a question that asked if the aggregate amount of your transactions or dealings with international related parties was more

than \$1 million, complete section **A** of *Schedule 25A 2011* and lodge it with the appropriate tax return. The aggregate amount of the dealings is the total amount of all dealings, whether on revenue or capital account, and includes the balance of any loans or borrowings outstanding with international related parties.

If you answered yes on your partnership, trust, company or fund tax return to a question about your overseas branch operations, an interest in a foreign company or a foreign trust, complete all questions in section **B** of *Schedule 25A 2011* and lodge it with the appropriate tax return.

If you answered yes to both questions, complete sections **A** and **B** and lodge *Schedule 25A 2011* with the appropriate tax return.

Answer the items in *Schedule 25A 2011*, including yes or no items, that apply to your particular circumstances. If an item or part of an item does not apply, leave it blank.

Please note: if you are a financial services provider you may need to complete the *International dealings schedule - financial services 2011* instead of *Schedule 25A 2011*.

The *International dealings schedule -- financial services 2011* must be completed by all entities who are:

- a foreign bank
- a foreign bank branch
- general or life insurance entity, or
- financial service providers (except superannuation funds) who reported an annual turnover of \$250 million or more on their current year's income tax return.

For more information, refer to *International dealings schedule - financial services instructions*.

Related-party international dealings

Section **A** of *Schedule 25A 2011* refers to related-party international dealings.

Complete section **A** if you answered yes to any of the following:

- item **23** of the *Company tax return 2011* (NAT 0656)

- **W** item **29** of the Partnership tax return 2011 (NAT 0659)
- **W** item **29** of the Trust tax return 2011 (NAT 0660)
- **B** item **17** of the Fund income tax return 2011 (NAT 71287).

The ATO issues public rulings setting out its policies on taxation aspects of related-party international dealings. Those public rulings are:

- *Taxation Ruling TR 94/14 - Income tax: application of Division 13 of Part III (international profit shifting) - some basic concepts underlying the operation of Division 13 and some circumstances in which section 136AD will be applied*
- *Taxation Ruling TR 97/20 - Income tax: arm's length transfer pricing methodologies for international dealings*
- *Taxation Ruling TR 98/11 - Income tax: documentation and practical issues associated with setting and reviewing transfer pricing in international dealings*
- *Taxation Ruling TR 1999/1 - Income tax: international transfer pricing for intra-group services*
- *Taxation Ruling TR 2004/1 - Income tax: international transfer pricing - cost contribution arrangements.*

We recommend that taxpayers with related-party international dealings be familiar with these rulings. There are also a number of publications about international transfer pricing. Go to www.ato.gov.au and enter 'international transfer pricing' in the 'Search for' box at the top of the page.

Also see the Organisation for Economic Co-operation and Development (OECD) Transfer pricing guidelines for multinational enterprises and tax administrations - 1995.

Definitions of some terms used in *Schedule 25A 2011* are in appendix 2.

Permanent establishments

Permanent establishment is defined in subsection 6(1) of the Income Tax Assessment Act 1936 (ITAA 1936). It includes:

- business operations carried on by an Australian resident entity at or through a fixed place of business in another country, and
- business operations carried on by a foreign resident entity at or through a fixed place of business in Australia.

For more information refer to *Taxation Ruling TR 2002/5 Income tax: Permanent establishment - What is 'a place at or through which [a] person carries on any business' in the definition of permanent establishment in subsection 6(1) of the Income Tax Assessment Act 1936?*

Although branch operations are not an 'entity' or 'party' separate from the taxpayer who undertakes those operations, determining the taxable profits of branch operations involves attributing income and expenditure of the taxpayer on a separate entity basis. In the case of income and expenditure of the taxpayer which is not wholly or directly earned from, or incurred in, its branch operations, income or expenses may be attributed to its branch operations on the basis of internally recorded 'dealings' on the proviso that those records reflect the functions and assets of the business operations carried on at or through the permanent establishment and represent the best estimate of branch profits that can be made in the circumstances. Refer to *Taxation Ruling TR 2001/11 Income tax: international transfer pricing-operation of Australia's permanent establishment attribution rules* and *Taxation Ruling TR 2005/11 Income tax: branch funding for multinational banks* for more information.

The information collected at items **1** and **2** of this schedule includes what you have internally recorded as dealings between you and your branch operations, or income/gains you have returned or the expenses/losses you have claimed in respect of those internally recorded dealings.

Examples

Examples, including suggested answers, for items **2** to **6** of *Schedule 25A 2011* are provided at appendix 5.

Interests in foreign companies or foreign trusts

Section **B** of *Schedule 25A 2011* refers to offshore branch operations of Australian companies, controlled foreign companies (CFCs) and

controlled foreign trusts (CFTs), and must be completed in all cases where the answer is yes to any of the following:

- item **24** of the Company tax return 2011
- **S** item **22** of the Partnership tax return 2011
- **S** item **22** of the Trust tax return 2011
- **C** item **17** of the Fund income tax return 2011

If you need to complete section **B**, you must answer item **11** and items **13** to **17**. Leave other items blank if they do not apply.

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Section A of Schedule 25A 2011

Item 1



Item 2



Item 2a Tangible property



Item 2b Royalties, rent and intangible property



Item 2c Services



Item 2d Other



Item 2e Loans - Interest bearing



Item 2f Loans - Interest free



Item 3a



Item 3b



Item 4



Item 4a



Item 4b



Item 5 Column A



Item 5 Column B



Item 6



Item 6a



Item 6b



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Item 1

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Item **1** asks for details and total values of the three main business activities carried out with international related parties, and the three principal foreign locations for each. If you had fewer than three different, relevant kinds of business activities with international related parties, or dealings in fewer than three locations, list those that you had.

Item **1** also collects information about your internally recorded 'dealings' with your branch operations that records your attribution of your income and expenditure to the branch operations. Refer to the section titled **Permanent establishments** in the Introduction to these instructions for more information.

Accordingly, for the purpose of item 1, also treat the reference to a 'party' as though it extended to:

- offshore branch operations carried on by an Australian resident - treat such operations as though they were instead a separate 'party' located in the branch country; and

- Australian branch operations carried on by a non-resident - treat such operations as though they were instead a separate 'party' located in Australia.

The industry codes to be used in this question are those listed in the Business industry codes 2011 (NAT 1827).

The appropriate code is the code best describing the international business activities giving rise to or underlying the international dealings. It will not necessarily be the same as the code describing your general business activity or the kind of transaction between the parties.

Where your business is divided into divisions or business segments which can be categorised under one of the industry codes, this may also be an appropriate basis for responding to this item.

You are not expected to conduct a detailed financial analysis to answer item **1**. A reasonable estimate is sufficient.

In the first column, at **A**, **F** and **K** write the industry code that describes the three main business activities giving rise to, or underlying the dealings carried out with international related parties. List these codes in descending order of total dollar value.

In the second column, at **B**, **G** and **L** write the value of the activities with international related parties for each of the industry codes. The value of the activities is the total for all locations in connection with the underlying business for each industry code. If part of the value of the activities is attributable to loans, this amount should not be included in the total value for each industry code.

In the third, fourth and fifth columns, write the foreign location code (from appendix 1) for the three foreign locations principally involved in the activities with international related parties for each industry code. If there are fewer than three locations for an industry code, list only those that apply. List the location codes in descending order of dollar value.

Example 1

An Australian manufacturing and holding company has three subsidiaries, located in Thailand, Singapore and Indonesia. The following international business activities occurred during the year:

- The Thai subsidiary manufactured household appliances that were purchased by the Australian parent company for wholesale distribution. The value of these purchases was \$50,000.
- The Singapore subsidiary manufactured electrical components for distribution in Australia and South-East Asia. During the year, the Australian parent company purchased finished components for resale. The parent company also carried out product design projects on behalf of this subsidiary. The value of the products purchased was \$900,000, and the value of the design work carried out by the Australian parent company was \$40,000.
- Dealings that the Australian parent company had with the Indonesian subsidiary consisted only of a loan to that subsidiary and the receipt of interest on the loan. The value of the loan was \$250,000 and \$25,000 interest was received. The loan was to enable the Indonesian subsidiary to undertake market research in Indonesia.

Select the code for the Australian parent company's underlying international businesses as follows:

- Thailand (location code THA): household appliance wholesaling, that is, purchase of finished goods from its subsidiary for wholesale distribution (industry code 34940)
- Singapore (location code SGP):
 - product design services (industry code 69230)
 - purchase of finished goods from its subsidiary for resale (industry code 34940)
- Indonesia (location code IDN): the business activity giving rise to, or underlying, the loan was market research and the most appropriate industry code is market research service (industry code 69500).

The Australian parent company completes item **1** as follows:

A	34940	B	950,000	C	SGP	D	THA	E
F	69230	G	40,000	H	SGP	I		J

K	69500	L	25,000	M	IDN	N		C
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The company writes the interest amount at **L**. The loan is not included in the total value for this industry code.

As there is no other market research activity with international related parties, the interest is the only amount written at this label.

Example 2

An Australian parent company has subsidiaries in New Zealand (location code NZL), Thailand (location code THA) and the United States of America (location code USA).

The company has three identifiable divisions:

- chemical products manufacturing (industry code 18990). The related-party dealings by this division total \$120,000 across all three locations
- agricultural chemicals wholesaling (industry code 33230). The related-party dealings by this division total \$200,000 across all three locations
- mining and oilfield services (industry code 10900). The related-party dealings by this division total \$700,000 across all three locations.

International transactions between the Australian parent company and its foreign subsidiaries can be reasonably attributed to each division's business activities.

Use codes from the [Business industry codes 2011](#) at **A**, **F** and **K** and the appropriate location codes from [appendix 1](#).

A	10900	B	700,000	C	NZL	D	THA	E
F	33230	G	200,000	H	USA	I	NZL	J
K	18990	L	120,000	M	THA	N	NZL	C

Example 3

An Australian company carries out a food manufacturing business (industry code 11990) through its offshore branch operations carried on in New Zealand (location code NZL).

The company conducts market research in relation to food and confectionery (industry code 69500). The company conducts this market research partly in the course of its operations carried on at or through its New Zealand branch operations; however the costs of the market research are not wholly incurred by the company in the course of those New Zealand operations.

The Australian company has internally recorded the attribution of its expenditure incurred in the market research to its New Zealand branch operations. Specifically, the Australian company records that \$2,400,000 of its total expenditure (of \$10,000,000) incurred in the income year in conducting the market research is incurred by the Australian company in the course of its New Zealand branch operations.

The company completes item 1 as follows:

A	69500	B	2,400,000	C	NZL	D		E
F		G		H		I		J
K		L		M		N		O

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Item 2

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The terms **related-party international dealings** and **international related parties** used in these instructions are defined in [appendix 2](#).

Item 2 also collects information about use of your property, services, funds or any other benefit in your offshore branch operations where your attribution of your income or expenses in relation to the property, services, funds or other benefit is internally recorded as a 'dealing' with your branch operations. Refer to the section titled **Permanent establishments** in the Introduction of these instructions for more information.

Accordingly, for the purpose of item **2**, also treat the reference to a 'party' as though it extended to:

- offshore branch operations carried on by an Australian resident - treat such operations as though they were instead a separate 'party' located in the branch country; and
- Australian branch operations carried on by a non-resident - treat such operations as though they were instead a separate 'party' located in Australia.

Include only dealings between international related parties, and not dealings between you and Australian resident entities. For example, if you received management fees from a foreign subsidiary but incurred costs in Australia to earn those fees, show only the management fees received from the foreign subsidiary.

Show only the gross amounts in columns A and B at this item, in whole dollars. Where, for example, a related-party international dealing involved payments by an Australian taxpayer to an international related party and also receipts from an international related party, show the payments at column A and the receipts at column B. An exception to this general approach applies in the case of certain derivative instruments. See **Item 2dOther** for more information.

For revenue transactions, unless otherwise specified, include those amounts that you have returned as assessable income or claimed as allowable deductions for the dealing.

For capital transactions, include the amount of the price or proceeds of the transaction including for any deemed acquisition or disposal for income tax purposes.

If you are an Australian resident, include at item **2e** the amount of any of your borrowed funds used, but not wholly or directly used, in your offshore branch operations that you have internally recorded as a 'loan' with your branch operations in accordance with:

- if you are an authorised deposit-taking institution (ADI) within the meaning of section 995-1 of the *Income Tax Assessment Act 1997* (ITAA 1997) - **Taxation Ruling TR 2005/11** *Income tax: branch funding for multinational banks*, or
- if you are not an ADI - paragraphs 3.41 to 3.44 of **Taxation Ruling TR 2001/11** *Income tax: international transfer pricing - operation of Australia's permanent establishment attribution rules*.

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Item 2a Tangible property

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At **A (Stock in trade and raw materials)** show your gross purchases or expenditure for trading stock and raw materials obtained from international related-party dealings.

At **B (Stock in trade and raw materials)** show your gross sales or revenue from trading stock and raw materials provided to international related parties.

These amounts will typically be included in trading account items, and will include partially finished goods.

At items **C** and **D (all other tangible property)**, write the amount of your gross purchases or expenditure and your gross sales or revenue respectively, in respect of all tangible property other than:

- trading stock and raw materials - you must instead show these amounts at item **2a**
- loan funds - you must instead show these amounts at items **2d, 2e** and **2f** as applicable.

Include at item **C** the gross acquisition cost of ordinary shares or preference shares acquired from any international related party.

Include at item **D** the gross issue or disposal proceeds from the issue or disposal of ordinary shares or preference shares to any international related party.

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Item 2b Royalties, rent and intangible property

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Royalties are defined in subsection 6(1) of the *Income Tax Assessment Act 1936* (ITAA 1936). At **E** show gross expenditure for royalties payable to international related parties. At **F** show gross revenue from royalties derived from international related parties.

Rent other than royalties includes gross expenditure and revenue for the use of, or the right to use, property, both tangible and intangible, not included as royalties. At **G** show gross rent payable to international related parties. At **H** show gross rent derived from international related parties.

At **I** and **J** include gross purchases/expenditure and gross sales/revenue, respectively, for **all other intangible property** not in the nature of royalties or rent.

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Item 2c Services

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At item **2c** you must show values for the provision of services to or from international related parties.

An inclusive definition of 'services' is provided at section 136AA(1) of the ITAA 1936.

Identify the nature of any services to or from international related parties and group them into the type of services listed at item **2c**. At **K**, **M**, **O** and **Q** write the total gross purchases/expenditure for each type of service. At **L**, **N**, **P** and **R** write the total gross sales/revenue for each type of service.

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Item 2d Other

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At item **2d** you must show values for the listed kinds of expenditure and revenue for your dealings with international related parties not specifically included at other labels in item **F2**.

At **A** include gross expenditure in the nature of interest or discounts. At **B** include gross revenue in the nature of interest or discounts.

At **C** include gross expenditure relating to insurance, such as premiums, and at **D** include any gross revenue from insurance dealings, including settlements.

At **E** and **F** show the amount of your expenditure and revenue respectively, for derivatives and any other kind of financial transactions, other than a loan, with international related parties.

For this purpose a **financial transaction other than a loan** will include guarantees and repurchase agreements.

For this purpose a **derivative** is a contractual right that derives its value from the value of something else, such as a debt security, equity, commodity or a specific index. The most common derivative instruments are forwards, futures, options and notional principal contracts such as swaps and credit derivatives. Unlike traditional debt and equity securities, these instruments do not involve a return on an initial investment.

For many derivative contracts such as notional principal contracts (for example, interest rate swaps), the parties to the contract will often only be liable for amount calculated on a net basis. In these kinds of contracts, only the liability or receivable calculated on this net basis should be included at **E** or **F** respectively.

In other kinds of derivative contracts, only one party becomes liable under the contract (for example, certain forward agreements or option premiums). In these kinds of contracts, the gross amount of the liability incurred, or receivable payable, under the contract should be recorded at **E** or **F** respectively.

Mark-to-market accounting may be used for determining the amounts in respect of derivatives where it is used by the taxpayer for financial accounting purposes.

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Item 2e Loans – Interest bearing

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Item **2e** identifies the gross amounts of loans and advances between international related parties for which an interest component is being charged.

The loans and advances to be shown here include all amounts borrowed between a taxpayer and the related parties.

The terms **loans** and **advances** are intended to be applied broadly in accordance with commercial and accounting practices (a rigorous application of the debt-equity test is not necessary).

Where you have **borrowed** amounts or **received** advances from an international related party or parties, add all the opening balances of these loans or advances and write the sum at **G**. Add all the closing balances for these loans and enter this amount at **H**.

Where you have **loaned** or **advanced** amounts to international related parties, add the opening balances of these loans and enter that total at **I**. Add the closing balances of the loans or advances and enter the total at **J**.

Example 4

An Australian company has several affiliates, which are related parties, in foreign countries. At the start of the income year, the company's balance sheet showed \$182,678 owing to the affiliates by the company and \$53,250 owing by the affiliates to the company.

At the end of the income year, \$86,782 was owed to the affiliates by the company, and \$245,354 was owed by the affiliates to the company. Item 2e would be completed as follows:

Opening Balance	Closing Balance
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G	182,678	H	86,782
I	53,250	J	245,354

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Item 2f Loans – Interest free

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Item **2f** identifies the gross amounts of loans and advances between international related parties for which no interest component is being charged.

The loans and advances to be shown here include all amounts borrowed between a taxpayer and the related parties. The terms **loans** and **advances** are intended to be applied broadly, and to include quasi-equity loans in which no amount of interest was paid or accrued during the year.

The terms are not intended to include trade debtors and creditors who fall within ordinary commercial dealings. However, where trade debtors or creditors that are international related parties are allowed or give terms significantly more generous than those allowed to, or given by, comparable arm's length parties, those terms may constitute interest-free loans or advances. In completing this item, have regard to the terms of trade that are arm's length in your own particular circumstances.

Where you have **borrowed** amounts or **received** advances from an international related party or parties, add all the opening balances of these loans or advances and write the sum at **K**. Add all the closing balances for these loans and enter the total at **L**.

Where you have **loaned** or **advanced** amounts to international related parties, similarly add the opening balances of these loans and enter

that total at **M**. Add the closing balances of the loans or advances and enter this at **N**.

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Item 3a

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This item asks whether any non-monetary consideration has been given or received in any dealings with related international parties.

These dealings may include providing services, transferring property (both tangible and intangible) or any similar dealings.

The nature of the dealing in which the non-monetary consideration is provided may be a barter, swap, bonus or discount, or any type of similar agreement.

Non-monetary consideration will generally include any consideration other than:

- monetary payment
- payment by cheque
- telegraphic and bank-to-bank transfer of funds
- inter-company loan account charges.

In particular, debt-for-equity swaps and non-monetary settlements of inter-company loan accounts will be taken to be non-monetary consideration.

Example 5

A taxpayer purchased trading stock for \$20 million from an international related party.

The taxpayer would print **Y** for yes at **B** if, rather than paying for the trading stock with a \$20 million telegraphic funds transfer to the related party's loan account, the decision was made to settle the debt by any of the following:

- forgiving royalties that would otherwise be payable by the international related party
- transferring title in a fixed asset
- agreeing to a discount on specified future transactions.
- However, where individual debts between two parties are aggregated or netted and the net balance settled monetarily, this will not be considered to be non-monetary consideration.

As mentioned earlier, for the purposes of *Schedule 25A 2011*, a permanent establishment is to be treated as a separate party from its head office or other related parties. Consequently, where non-monetary consideration passes between a permanent establishment and its head office in return for the provision of services or other transactions listed on *Schedule 25A 2011*, print **Y** for yes at **B** item **3a**.

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Item 3b

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This item asks whether you have made any provision of services, transfer of assets (both tangible and intangible) or any similar dealings with any related international party, for which you received no consideration.

Example 6

An Australian parent company manufactures trading stock that it sells to a foreign subsidiary for resale. The Australian parent develops a new product, which requires considerable training of the foreign subsidiary's staff in order to on-sell the new product.

The Australian parent provides this training, but does not charge the subsidiary. The Australian company should print **Y** for yes at **C**.

Similarly, the answer yes at **C** would also be required where an Australian company owned a trademark that it allowed an international related party to use without payment.

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Item 4

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This item requires estimations of the percentages of the total dollar value of the related-party international dealings for which you have written documentation to support:

- the characterisation of the international dealings in the context of your business, as described in step 1 of [Taxation Ruling TR 98/11 - Income tax: documentation and practical issues associated with setting and reviewing transfer pricing in international dealings](#)
- the selection of the most appropriate arm's length pricing methods for those dealings, as described in step 2 of Taxation Ruling TR 98/11, and
- the application of the most appropriate arm's length pricing methods to those dealings, as described in step 3 of Taxation Ruling TR 98/11.

The total related-party dealings to be included in this calculation are those dealings for which you showed amounts at items **2a** to **2d**, excluding any of your internally recorded 'dealings' with your branch operations recording your attribution of your income and expenditure to the branch operations: refer to the section titled **Permanent establishments** in the Introduction to these instructions for more information.

Do not include related-party dealings identified in items **2e** or **2f**.

The concept of 'the most appropriate method' is discussed in [Taxation Ruling TR 97/20 Income tax: arm's length transfer pricing methodologies for international dealings](#), at paragraphs 3.5 to 3.9.

Contemporaneous documentation

Documentation is contemporaneous if:

- it is existing or brought into existence either

- at the time you are developing or implementing any arrangement that might raise transfer pricing issues, or
 - when you are reviewing these arrangements prior to or at the time of the preparation of tax returns, and
- the documentation records information relevant to transfer pricing decisions.

The documentation may be in the form of books, records, studies, budgets, plans and projections, analyses, conclusions and other material that record the information. It may be in electronic or written form.

The initial analysis of your international dealings against the arm's length principle will have been carried out and documented at the time of engaging in the dealings. To review those international dealings before you prepare your tax returns is prudent business practice.

Where you have not used arm's length consideration in the ordinary course of your related-party international dealings, review prices before preparing the tax return, and make any adjustments for taxation purposes. Keep all your documentation in relation to this.

Adequacy of documentation

The ATO does not expect taxpayers to prepare or obtain documents beyond the minimum needed to make a reasonable assessment of whether they have complied with the arm's length principle in setting prices or consideration.

However, the documentation that is created in the ordinary course of the taxpayer's business and used by it to establish the prices for its international related-party dealings - for example, invoices and orders - will not generally be regarded as contemporaneous documentation in relation to the arm's length nature of the dealings. This is because the documents do not produce any evidence or provide any basis for comparison for determining whether prices are established at arm's length.

It is not possible to provide a general checklist of documentation that would be adequate or desirable. The ATO realises that it is necessary to strike an acceptable balance between the need to keep compliance

costs to a minimum and the legitimate concern of the ATO in ensuring the proper amount of Australian tax is paid.

The amount and type of documentation that should be created or obtained over and above that created in the ordinary course of business will depend on the facts and circumstances of each case.

The issue is a practical one having regard to what a prudent business person would do in the same circumstances, and taxpayers need to exercise commercial judgment in assessing their own compliance with the arm's length principle.

Arm's length pricing methods

The arm's length principle is the statutory test for pricing related-party international dealings. The principle is incorporated into the associated enterprise articles in each of Australia's double tax agreements.

No particular method to establish the arm's length pricing, or order in which methods should be applied, is prescribed in the double tax agreements or related legislation, and taxpayers have the greatest scope to use methods appropriate to their circumstances.

Taxation Ruling TR 97/20 sets out:

- the methods acceptable to the ATO
- when these methods are considered acceptable
- our views on the concepts involved, and the issues that arise, in applying the methods.

We strongly recommend that all taxpayers with international related-party dealings read this ruling.

Further information is in [Taxation Ruling TR 94/14](#) *Income tax: application of Division 13 of Part III (international profit shifting) - some basic concepts underlying the operation of Division 13 and some circumstances in which section 136AD will be applied*, paragraphs 86 and 343, and also in the OECD's report *Transfer pricing guidelines for multinational enterprises and tax administrations - 1995*.

A brief overview of some methods is at [item 5 column A](#). However, for detailed information about the different methods, see the references above.

Permanent establishments

Refer to the section titled **Permanent establishments** in the Introduction to these instructions.

Capital dealings

Where the dealings between related parties are capital in nature, the methods discussed at item 5 column A may not be appropriate.

Some alternative suggestions are given at item 6b, and these may be appropriate under certain circumstances. However, no specific methods are recommended.

For the purpose of answering items **4a** and **4b**, include capital dealings where written documentation is held to support the choice of method for the processes involved in steps 1, 2 and 3 of Taxation Ruling TR 98/11, and a bona fide belief is held that the resulting transfer pricing is arm's length.

Choice of method to determine arm's length pricing

The characterisation of the dealings and the selection and application of the appropriate method are three steps in a four-step process for establishing arm's length transfer prices between associated enterprises. The fourth step is to provide processes for review and adjustment, if necessary, to the chosen method.

The four steps, briefly, are:

1. understanding the cross-border dealings in the context of the taxpayer's business, that is, characterisation of the dealings
2. selecting the most appropriate method or methods
3. applying that method
4. establishing review and adjustment processes.

The first two steps may be complex processes and you may need to refer to specific details provided in Taxation Ruling TR 98/11.

The ATO considers that the prudent taxpayer will document:

- the processes of characterisation and selection

- the reasons for the final choice of method
- the reasons other methods were considered and rejected.

As mentioned earlier, the ATO requires that adequate documentation be kept. However, the complexity of the dealings will indicate the extent to which analysis and supporting documentation is required.

Application of pricing methods

The application of the chosen method will usually require two separate processes:

1. an assessment of comparability
2. the collection of supplementary data.

The first process will include:

- searching for comparable transactions or enterprises
- identifying sources of information used in the search
- adopting transactions or enterprises as being comparable
- rejecting other transactions or enterprises as not being comparable
- providing reasons and amounts where an independent transaction has been adjusted to make it comparable with the dealings under examination
- applying the pricing method, and any checking method (such as sampling) to ensure the validity of the chosen method and resultant arm's length price.

The second process will include:

- collecting data on profit projections
- creating or acquiring records to supplement the analysis of comparability and function
- collecting data to calculate financial performance ratios, as part of applying the chosen pricing methods.

You must prepare and retain relevant documentation about these processes.

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Item 4a

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Use one of the following numeric codes to state the percentage of the total of the dollar values you wrote at items **2a** to **2d** (after excluding any amounts for your internally recorded 'dealings' with your branch operations) for which you have written documentation supporting your processes in steps 1 and 2 (characterisation and selection) of chapter 5 of Taxation Ruling TR 98/11. Print the code at **F**.

Percentage of dollar value of related-party dealings - items 2a to 2d only

Percentage	Code
0%	1
1% to less than 25%	2
25% to less than 50%	3
50% to less than 75%	4
75% to less than 100%	5
100%	6

You may calculate the percentage on the basis of a reasonable estimate.

A statistical sample may be an appropriate method of calculating the relevant percentage, provided the sample selection and mathematical considerations are consistent with generally accepted statistical methods.

Keep your working papers if you have used a sampling process to make this estimate.

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Item 4b

28 September 2012

Write the code shown in item **4a** which reflects the percentage of the total of dollar values used for item **4a** for which you have written documentation supporting your processes in step 3 of chapter 5 of Taxation Ruling TR 98/11. Print the code at **G**.

As in the instructions for item **4a**, you may calculate the percentage on the basis of a reasonable estimate. Keep your working papers that relate to item **4b**.

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Item 5 Column A

28 September 2012

In column A list the four principal methods that you used in establishing or reviewing the appropriate arm's length pricing or consideration in your related-party international dealings that are **revenue** in nature, and for which you have included amounts at items **2a** to **2d**. Related-party dealings of a **capital** nature are addressed in item **6**.

Not all the methods are generally considered to provide an arm's length outcome, but may be arm's length in some cases.

If you did not use any methods, leave item **5** blank. If you used fewer than four, list only those used.

Record the four methods at **H** to **N** in descending order of total dollar value, using the appropriate code from the following table:

Pricing method	Code
Comparable uncontrolled price (CUP) method	1
Resale price method	2
Cost-plus method	3
Profit split method	4
Transactional net margin method	5
Marginal costing	6
Cost-contribution arrangement	7
Apportionment of costs	8
Apportionment of income	9
Fixed mark-up applied to cost	10
Fixed percentage of resale price	11
Other methods	12

The above methods are explained in detail in Taxation Ruling TR 97/20 and [Taxation Ruling TR 1999/1](#) *Income tax: international transfer pricing for intra-group services*, and it is strongly recommended that taxpayers with related-party dealings read these rulings before completing item **5**. The rulings generally accept the principles in the OECD report *Transfer pricing guidelines for multinational enterprises and tax administrations - 1995*. However, any differences are clearly indicated.

A brief summary of each of the methods in the above table is provided in [appendix 4](#). The list is not intended to be exhaustive, nor will each method be acceptable under all circumstances.

As in item **4**, in order to establish appropriate arm's length pricing under a particular method, a sampling of the dealings may be sufficient if carried out according to accepted statistical practice. Note that where total dollar value of related-party dealings is to be

calculated, these dealings should not be 'netted off' other than in the case of certain derivative instruments (see [Item 2d Other](#) for further details). That is, do not set off incomings and outgoings against each other to result in a lesser amount. Instead, add the amounts, both income derived and expenses incurred, to obtain the sum total of all such dealings.

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Item 5 Column B

28 September 2012

In column B at **I** to **O** indicate, against each method identified in column A, the total dollar value of related-party dealings to which you applied that method. Express them as a percentage of the sum of all the related-party dealings for which you used methods to establish arm's length pricing.

Indicate this percentage by using the appropriate code from the following table

Percentage of dollar value of related-party dealings that are revenue in nature - items 2a to 2d only

Percentage	Code
0%	1
1% to less than 25%	2
25% to less than 50%	3
50% to less than 75%	4
75% to less than 100%	5

100%	6
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The amount referred to above as the total dollar value of related-party dealings is, as in the calculation of the value of dealings in column A, the sum total of such dealings, both income derived and expenses incurred. Do not offset these amounts against each other.

The percentage required may be calculated on the basis of a reasonable estimate.

A statistical sampling is an acceptable method, provided the method follows accepted statistical practice. Keep any working papers relating to this process.

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Item 6

28 September 2012

This question is concerned with any dealings of a capital nature that have occurred between you and an international related party. These capital dealings include those for which you wrote amounts at items **2a** to **2d** (excluding dealings in trading stock in the ordinary course of business).

If you print **N** for no at item **6a**, disregard items **6b** and **6c** and go to item 7.

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Item 6a

28 September 2012

At this item you need to write either **Y** for yes or **N** for no. You should write yes if you have acquired an interest in an asset as a result of

dealings of a non-revenue (capital) nature with international related parties, or if you have had dealings with an international related party that would be classified as a capital gains tax (CGT) event within the meaning of Part 3-1 of the ITAA 1997. This will not include dealings in trading stock held in the ordinary course of business.

The terms 'acquired', 'CGT event', 'disposal' and 'asset' have the same meaning as they have in Part 3-1 of the ITAA 1997.

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Item 6b

28 September 2012

If you have acquired capital assets from, or have disposed of capital assets to, international related parties, write at **Q** the codes, taken from the table below, for the four principal methods you used for pricing those acquisitions or disposal. Write the codes in descending order of total dollar value, starting at the left-hand side.

If you used fewer than four methods leave the remaining spaces blank.

Pricing method	Code
Nil consideration	1
Cost price	2
Written-down value	3
Discounted cash flow	4
Director's valuation	5
Independent valuation	6
Quoted market price	7
Other methods	8

Cost price refers to the price the seller originally paid for the asset, including ancillary costs such as freight or handling.

Written-down value refers to a pricing method based on either the taxation 'adjustable value' or accounting residual value after depreciation has been allowed.

Discounted cashflow is a pricing method where the price of an asset is based on the discounted cash flow at the time of acquisition or disposal.

Director's valuation refers to a pricing method that is based on the directors' opinion of an asset's value, and not on any of the other methods listed in codes 1 to 8.

Independent valuation is a pricing method by which a suitably qualified person, acting at arm's length to both the buyer and seller, assesses the value of an asset.

Quoted market price refers to a price quoted on a public listed market, such as a public stock exchange, or commodities market.

Other methods means any other pricing method that is not mentioned in item 6.

The above pricing methods may not provide an arm's length price under all circumstances. The above examples are not an exhaustive list.

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Item 6c

28 September 2012

At **R** item **6c** write the code from the table below which is the percentage of your related-party international dealings that are capital in nature.

Total value of international related-party acquisitions and disposals of capital assets as a percentage of the total value of your international related-party dealings (items 2a to 2d only)

Percentage	Code
0%	1
1% to less than 25%	2
25% to less than 50%	3
50% to less than 75%	4
75% to less than 100%	5
100%	6

As in the instructions for **item 4**, you may calculate the percentage on the basis of a reasonable estimate, for example, a sampling technique based on accepted statistical methods. Keep your working papers that relate to item **6c**.

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Item 7

28 September 2012

In this item show whether any non-resident has participated in the capital, management or control of the company in this year.

'Participating in the capital' means having an equity interest of 10% or greater in the company. At **S** write **Y** if your answer is yes or **N** if your answer is no.

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Item 8

28 September 2012

In this item show the number of international related parties with which you had dealings during the year. 'International related parties' are parties whose international dealings can be subject to Division 13 of the ITAA 1936. An expanded definition is in [appendix 2](#).

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Section B of Schedule 25A 2011

28 September 2012

Section B of *Schedule 25A 2011* refers to overseas branch operations of Australian companies, controlled foreign companies (CFCs), and controlled foreign trusts (CFTs), and is to be completed in all cases where the answer is yes to any of the following:

- item **24** of the Company tax return 2011
- **S** item **22** of the Partnership tax return 2011
- **S** item **22** of the Trust tax return 2011
- **C** item **17** of the Fund income tax return 2011

If you need to complete section B, you must complete items **11** and **13** to **17**. If any other items in section B do not apply, you may leave the labels in those items blank.

For the purposes of section **B**:

- 'listed countries' are countries listed in Part 1 of Schedule 10 of the *Income Tax Regulations 1936* (ITR 1936)
- 'section 404 countries' are countries listed in Part 2 of Schedule 10 of the ITR 1936
- an 'unlisted country' is a country that is not shown in Schedule 10 of the ITR 1936.

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Item 9

28 September 2012

At this item, you must show the number of CFCs and CFTs in which your entity had either a direct or indirect interest at the start and end of the accounting period. There are separate labels to disclose this for listed countries, section 404 countries and unlisted country CFCs and CFTs.

A listed country trust estate is defined in section 102AAE of the ITAA 1936. The terms 'direct control interest' and 'indirect control interest' in a CFC and CFT have the same meaning as in Division 3 of Part X of the ITAA 1936.

Labels A, B and C

Write the total number of listed country, section 404 country and unlisted country CFCs and CFTs you had at the start of the entity's accounting period at each corresponding label.

Labels D, E and F

Write the total number of listed country, section 404 country and unlisted country CFCs and CFTs you had at the end of the entity's accounting period at each corresponding label.

If the number of CFCs and CFTs is less than 10, write **0** (zero) as the first digit. If the number of CFCs and CFTs is more than 99, write **99**. If the number of CFCs and CFTs is zero, leave the relevant label blank.

Example 7

If an entity had five listed country CFCs at the start of the year and nil at the end of the year, and no unlisted country CFCs at either the year's start or end, write **05** at **A**. Leave all other labels at item **9** blank.

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Item 10

28 September 2012

Write at the corresponding label the total amount of your attributable income included in your assessable income under each of sections 456, 457 or 459A of the ITAA 1936. Use whole dollars. Leave labels blank if they do not apply.

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Item 11

28 September 2012

At this item you must show the amount of your foreign income that is non-assessable non-exempt income under each of sections 23AH, 23AI, 23AJ and 23AK of the ITAA 1936.

Write at **O** to **V**, at the corresponding label, the total amount in whole dollars of your income separately derived from listed countries, section 404 countries or unlisted countries that is non-assessable non-exempt income under sections 23AH, 23AI or 23AJ.

Write at **W** the amount of your income that is non-assessable non-exempt income under section 23AK.

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Item 12

28 September 2012

This item concerns the reduction in a capital gain or capital loss where Subdivision 768-G of the ITAA 1997 applies. If a company held a voting interest of at least 10% in a foreign company and held that interest for a continuous period of at least 12 months in the two years before the specified CGT event, it may be entitled to use this measure. If this measure applies, the relevant item(s) at **12a** or **12b** must be completed.

Write at item **12a** the amount of any reduction in your capital gain in accordance with Subdivision 768-G.

At item **12b** write the amount of any capital loss reduced in accordance with Subdivision 768-G that may be utilised or carried forward.

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Item 13

28 September 2012

At this item show whether, during the year of income, accumulated profits, accumulated losses, paid-up capital or other assets or reserves have been transferred from any of your unlisted country CFCs or CFTs to a related entity in a listed country.

For the purpose of this item, transfer includes sale, acquisition, gift, deed of assignment, declaration of trust or otherwise, with or without consideration (monetary or non-monetary).

Examples of the type of transfers covered include:

- disposing of an asset to a related entity in a listed country, other than trading stock disposed of in the normal course of business
- waiving a debt owed by a related entity in a listed country
- making a loan to a related entity in a listed country
- acquiring a share, a right to acquire a share, or an option to acquire a share in a related entity in a listed country
- making a payment in respect of a call on a share in a related entity in a listed country.

At **S**, **T**, **U** and **V** write either **Y** for yes or **N** for no in respect of each specified kind of transferred asset.

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Items 14 to 18

28 September 2012

Unless otherwise specified, the terms used in items **14** to **19** have the same meaning as they have in Divisions 6 and 6AAA of the ITAA 1936.

Item 14

At this item show whether, at any earlier time (including at a time before the commencement of the income year) property or services has been transferred or caused to be transferred by you or your entity to a non-resident trust estate.

'Transfer', 'property' and 'services' are defined in section 102AAB of the ITAA 1936. Sections 102AAJ and 102AAK of the ITAA 1936 provide guidance in relation to whether there was a transfer or a deemed transfer of property or services to a non-resident trust estate.

At **W** write either **Y** for yes or **N** for no.

Item 15

At this item show whether, at any time during the year of income, your entity was a beneficiary of a non-resident trust estate.

At **X** write **Y** for yes or **N** for no

Item 16

At this item show whether, at any time during the year of income, your entity had an interest in a non-resident trust estate, or was entitled to acquire an interest in a non-resident trust estate.

'Entitled to acquire' has the same meaning as set out in section 322 of Part X of the ITAA 1936.

At **Y** write **Y** for yes or **N** for no

Item 17

At this item show whether any of the non-resident trust estates for which you wrote yes at items **14**, **15** or **16** is a discretionary trust estate.

Discretionary trust estate is defined in section 102AAB of the ITAA 1936. I

At **Z** write **Y** for yes or **N** for no in answer to this question if you wrote **Y** at **W**, item **14**, at **X**, item **15** or at **Y**, item **16**.

Item 18

At this item show whether, at any time during the year of income, your entity was able to control a non-resident trust estate.

Control in relation to a trust estate is defined in section 102AAG of the ITAA 1936.

At **A** write **Y** for yes or **N** for no in answer to this question.

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Taxpayer's Declaration

28 September 2012

If the schedule is not lodged with the income tax return you are required to sign and date page 4 of the schedule.

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Appendices

28 September 2012

Appendix 1 Location names and codes



Appendix 2 Definitions



Appendix 3 Abbreviations



Appendix 4 Pricing methods



Appendix 5 worked example



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Appendix 1 Location names and codes

28 September 2012

The following table lists the location names and codes to be used in completing item **1**.

Country/Jurisdiction	Code
Afghanistan	AFG
land Islands	ALA

Albania	ALB
Algeria	DZA
American Samoa	ASM
Andorra	AND
Angola	AGO
Anguilla	AIA
Antarctica	ATA
Antigua and Barbuda	ATG
Argentina	ARG
Armenia	ARM
Aruba	ABW
Austria	AUT
Azerbaijan	AZE
Bahamas	BHS
Bahrain	BHR
Bangladesh	BGD
Barbados	BRB
Belarus	BLR
Belgium	BEL
Belize	BLZ
Benin	BEN

Bermuda	BMU
Bhutan	BTN
Bolivia	BOL
Bosnia and Herzegovina	BIH
Botswana	BWA
Bouvet Island	BVT
Brazil	BRA
British Indian Ocean Territory	IOT
British Virgin Islands	VGB
Brunei Darussalam	BRN
Bulgaria	BGR
Burkina Faso	BFA
Burundi	BDI
Cambodia	KHM
Cameroon	CMR
Canada	CAN
Cape Verde	CPV
Cayman Islands	CYM
Central African Republic	CAF
Chad	TCD
Chile	CHL

China	CHN
Christmas Island	CXR
Cocos (Keeling) Islands	CCK
Colombia	COL
Comoros	COM
Congo, Democratic Republic of (was Zaire)	COD
Congo, People's Republic of	COG
Cook Islands	COK
Costa Rica	CRI
Cote D'Ivoire (Ivory Coast)	CIV
Croatia (Hrvatska)	HRV
Cuba	CUB
Cyprus	CYP
Czech Republic	CZE
Denmark	DNK
Djibouti	DJI
Dominica	DMA
Dominican Republic	DOM
East Timor (Timor-Leste)	TLS
Ecuador	ECU
Egypt	EGY

El Salvador	SLV
Equatorial Guinea	GNQ
Eritrea	ERI
Estonia	EST
Ethiopia	ETH
Falkland Islands (Malvinas)	FLK
Faroe Islands	FRO
Fiji	FJI
Finland	FIN
France	FRA
French Guiana	GUF
French Polynesia	PYF
French Southern Territories	ATF
Gabon	GAB
Gambia	GMB
Georgia	GEO
Germany	DEU
Ghana	GHA
Gibraltar	GIB
Greece	GRC
Greenland	GRL

Grenada	GRD
Guadeloupe	GLP
Guam	GUM
Guatemala	GTM
Guernsey	GGY
Guinea	GIN
Guinea-Bissau	GNB
Guyana	GUY
Haiti	HTI
Heard and McDonald Islands	HMD
Holy See (Vatican City State)	VAT
Honduras	HND
Hong Kong	HKG
Hrvatska (Croatia)	HRV
Hungary	HUN
Iceland	ISL
India	IND
Indonesia	IDN
Iran	IRN
Iraq	IRQ
Ireland	IRL

Isle of Man, The	IMN
Israel	ISR
Italy	ITA
Ivory Coast (C te D'Ivoire)	CIV
Jamaica	JAM
Japan	JPN
Jersey	JEY
Jordan	JOR
Kazakhstan	KAZ
Kenya	KEN
Kiribati	KIR
Korea, Democratic People's Republic of (North Korea)	PRK
Korea, Republic of (South Korea)	KOR
Kuwait	KWT
Kyrgyzstan	KGZ
Laos	LAO
Latvia	LVA
Lebanon	LBN
Lesotho	LSO
Liberia	LBR
Libya	LBY

Liechtenstein	LIE
Lithuania	LTU
Luxembourg	LUX
Macau	MAC
Macedonia, The Former Yugoslav Republic of	MKD
Madagascar	MDG
Malawi	MWI
Malaysia	MYS
Maldives	MDV
Mali	MLI
Malta	MLT
Marshall Islands	MHL
Martinique	MTQ
Mauritania	MRT
Mauritius	MUS
Mayotte	MYT
Mexico	MEX
Micronesia, Federated States of	FSM
Moldova	MDA
Monaco	MCO
Mongolia	MNG

Montenegro	MNE
Montserrat	MSR
Morocco	MAR
Mozambique	MOZ
Myanmar (was Burma)	MMR
Namibia	NAM
Nauru	NRU
Nepal	NPL
Netherlands, The	NLD
Netherlands Antilles	ANT
New Caledonia	NCL
New Zealand	NZL
Nicaragua	NIC
Niger	NER
Nigeria	NGA
Niue	NIU
Norfolk Island	NFK
Northern Mariana Islands	MNP
North Korea	PRK
Norway	NOR
Oman	OMN

Pakistan	PAK
Palau	PLW
Palestinian Territory, Occupied	PSE
Panama	PAN
Papua New Guinea	PNG
Paraguay	PRY
Peru	PER
Philippines	PHL
Pitcairn Island	PCN
Poland	POL
Portugal	PRT
Puerto Rico	PRI
Qatar	QAT
R union	REU
Romania	ROU
Russian Federation	RUS
Rwanda	RWA
Saint Barth lemy	BLM
Saint Helena	SHN
Saint Kitts and Nevis	KNA
Saint Lucia	LCA

Saint Martin (French part)	MAF
Saint Pierre and Miquelon	SPM
Saint Vincent and The Grenadines	VCT
Samoa	WSM
San Marino	SMR
Sao Tome and Principe	STP
Saudi Arabia	SAU
Senegal	SEN
Serbia	SRB
Seychelles	SYC
Sierra Leone	SLE
Singapore	SGP
Slovakia (Slovak Republic)	SVK
Slovenia	SVN
Solomon Islands	SLB
Somalia	SOM
South Africa	ZAF
South Georgia and the South Sandwich Islands	SGS
South Korea	KOR
Spain	ESP
Sri Lanka	LKA

Sudan	SDN
Suriname	SUR
Svalbard and Jan Mayen Islands	SJM
Swaziland	SWZ
Sweden	SWE
Switzerland	CHE
Syria	SYR
Taiwan	TWN
Tajikistan	TJK
Tanzania	TZA
Thailand	THA
Timor-Leste (East Timor)	TLS
Togo	TGO
Tokelau	TKL
Tonga	TON
Trinidad and Tobago	TTO
Tunisia	TUN
Turkey	TUR
Turkmenistan	TKM
Turks and Caicos Islands	TCA
Tuvalu	TUV

Uganda	UGA
Ukraine	UKR
United Arab Emirates	ARE
United Kingdom	GBR
United States	USA
United States Minor Outlying Islands	UMI
United States Virgin Islands	VIR
Uruguay	URY
Uzbekistan	UZB
Vanuatu	VUT
Vatican City State (Holy See)	VAT
Venezuela	VEN
Vietnam	VNM
Wallis and Futuna Islands	WLF
Western Sahara	ESH
Yemen	YEM
Zambia	ZMB
Zimbabwe	ZWE

Appendix 2 Definitions

28 September 2012

Capital means an equity interest of 10% or greater.

International related parties means persons who are parties to international dealings that can be subject to Division 13 Part III of the ITAA 1936 or the associated enterprises article of a relevant double tax agreement. The term includes the following:

- any overseas entity or person who participates directly or indirectly in your management, control or capital
- any overseas entity or person in respect of which you participate directly or indirectly in the management, control or capital
- any overseas entity or person in respect of which persons who participate directly or indirectly in its management, control or capital are the same persons who participate directly or indirectly in your management, control or capital.

Participate(s) includes a right of participation, the exercise of which is contingent on an agreed event occurring.

Person has the same meaning as in subsection 6(1) of the ITAA 1936 and section 995-1 of the ITAA 1997.

Related-party international dealings means international transactions, agreements or arrangements between related parties. The term includes all transactions between an Australian resident and international related parties.

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Appendix 3 Abbreviations

28 September 2012

ADI	authorised deposit-taking institution
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CGT	capital gains tax
CFC	controlled foreign company
CFT	controlled foreign trust
CUP	comparable uncontrolled price
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
ITR 1936	<i>Income Tax Regulations 1936</i>
PE	permanent establishment
R&D	research and development

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Appendix 4 Pricing methods

28 September 2012

See Taxation Ruling TR 97/20 and Taxation Ruling TR 1999/1 for a more complete explanation of the operation and suitability of each of the methods mentioned below for particular circumstances.

The explanations below are only brief summaries of each method, and the list is not exhaustive. The methods may not be appropriate for determining an arm's length price under all circumstances. Other methods, which are not listed below, might also be appropriate.

It is not possible to identify all the circumstances under which the various methods will produce valid results, and the applicability of any particular method for any given transaction must be determined from all the facts and circumstances of the dealing.

Comparable uncontrolled price method - code 1

This method compares the price for property or services transferred in a controlled transaction (that is, with a related international party) to the price that is charged for comparable property or services in an uncontrolled transaction, under similar circumstances.

If you use this method but the comparable uncontrolled price (CUP) is adjusted to allow for particular circumstances of the controlled dealing, you should still record the adjusted price under this code.

Resale price method - code 2

This pricing method may be appropriate where an enterprise sells a product to a related party, who then re-sells that product to an independent third party.

The resale price is reduced by the arm's length resale price margin, and may then be regarded, after adjustments for other costs associated with the original purchase of the product, as an arm's length price of the original transfer of property between the related parties.

Cost-plus method - code 3

The cost-plus method begins with the costs incurred by the supplier of property or services in a controlled transaction for property transferred or services provided to a related purchaser. An appropriate arm's length cost-plus mark-up is then added to this cost, to make an appropriate profit in light of the functions performed, assets used, risks assumed and the market conditions. What is arrived at after adding the arm's length cost-plus mark-up to the above costs may be regarded as an arm's length price of the original controlled transaction.

This method is probably most useful if:

- semi-finished goods are sold between related parties
- related parties have concluded joint facility agreements or long-term buy-and-supply arrangements, or
- the controlled transaction is the provision of services.

If a fixed percentage mark-up is applied to the relevant cost base without any benchmarking of that percentage against comparable independent dealings, this will not be regarded as cost-plus method.

Profit split method - code 4

This is a method of determining the appropriate pricing for transactions by:

- identifying the combined profit or loss from the dealings between the related parties, and
- splitting that combined profit or loss between the related parties.

The split of profit or loss between the parties must be made on an economically valid basis that approximates the division of profits that would have been arrived at in an agreement made at arm's length.

Transactional net margin method - code 5

This pricing method is based on comparisons made at the net profit level between the taxpayer and independent parties, in relation to a comparable transaction or dealing.

Comparisons at the net profit level can be made on a single transaction or in relation to some aggregation of dealings between associated enterprises.

Marginal costing - code 6

Marginal costing is a method of pricing that applies only the variable production costs to the costs of a product. Marginal costing is often used by companies and multinational enterprise groups for internal cost accounting and management control purposes. However, its use in setting transfer prices on international dealings between associated enterprises for tax purposes is acceptable only if pricing on the basis of marginal costs represents an arm's length outcome for the transfer of goods or services into the particular market.

Cost-contribution arrangement - code 7

A cost-contribution arrangement is one where members of a multinational group act in concert for the benefit of each of the

participants to:

- produce or provide goods, intangible property or services, or
- acquire these jointly from a third party,

and agree to share the actual costs and risks undertaken.

Each participant bears a fair share of the costs, and is entitled to receive a fair share of rewards. The concept is akin to a joint venture or partnership.

To be consistent with the arm's length principle, the contributors must be satisfied that they can obtain an acceptable rate of return within a timeframe that takes into account their financial and business circumstances.

For more information refer to [Taxation Ruling TR 2004/1](#) *Income tax: international transfer pricing - cost contribution arrangements*.

Apportionment of costs - code 8

This pricing method apportions the costs associated with a controlled transaction among the associated enterprises. An answer must be found to all transfer pricing problems. However, cases may arise where neither comparable dealings nor data are available to apply to traditional, or profit-based, methods. In these instances, application of an indirect method such as apportionment of costs on the basis of a formula may be applicable.

Apportionment of income - code 9

This pricing method apportions the income associated with a controlled transaction among the associated enterprises.

As with the method for code **8**, this method may be applicable where there are neither comparable dealings nor data to apply the traditional, or profit-based, methods to the pricing problem.

Fixed percentage mark-up applied to costs - code 10

This pricing method determines the transfer price for a controlled transaction by applying a fixed percentage mark-up to a relevant cost

base, where the mark-up is not benchmarked against comparable independent dealings. The absence of benchmarking distinguishes this method from the cost-plus method discussed at code **3**.

Fixed percentage of resale price - code 11

This pricing method determines the transfer price for a controlled transaction as a fixed percentage of the resale price, where the fixed percentage chosen is not benchmarked against the gross margins earned in comparable independent dealings.

The absence of benchmarking distinguishes this method from the resale price method, code **2**.

Other methods - code 12

Any method used which is not included at codes **1** to **11**.

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Appendix 5 worked example

28 September 2012

The following example shows how the appropriate answers are determined for *Schedule 25A 2011* for a hypothetical situation involving an Australian resident company.

Example 9

An Australian company, XYZ Pty Ltd, has several wholly owned overseas subsidiaries.

Non-resident subsidiaries qualify as international related parties - see the definition in [appendix 2](#).

During the year ending 30 June 2011, XYZ Pty Ltd had dealings with subsidiaries. Some of these dealings were transacted at arm's length prices, ensured by implementing and following various arm's length pricing methods, while other dealings were not.

The following dealings, shown in Australian dollars, occurred during the year and are grouped under the headings in item **2** of the schedule.

Stock in trade and raw materials

- Stock in trade was sold to subsidiaries for \$146,450. All sales were priced at bona fide arm's length prices, of which 50% were based on CUP and 50% based on the cost-plus method.
 - For the CUP dealings, the method for pricing was selected, applied and documented as discussed in the introduction to item 4
 - For the cost-plus dealings, the pricing method was selected and documented for all the dealings, but written documentation on the application of the method was kept for only one-quarter of all these dealings.

- Raw materials were purchased from subsidiaries for \$178,750. Of this total dollar amount, 60% was priced on comparative uncontrolled prices, and the remaining 40% was invoiced at a price XYZ Pty Ltd considered reasonable.

- For all CUP dealings, the method was selected, applied and documented as discussed in the introduction to item 4.

Other tangible property

- Shares in a listed company were sold to a subsidiary for \$23,345, being the quoted share price at the time. This method was selected, applied and documented as discussed in the introduction to item 4.

- Machinery was purchased by a subsidiary and transferred to XYZ Pty Ltd for \$18,850.

This was the actual price paid by the subsidiary, including handling charges. This method was also selected, applied and documented as discussed in the introduction to item 4.

Royalties

The subsidiaries used trademarks owned by XYZ Pty Ltd but did not pay royalties.

Other intangible property

XYZ Pty Ltd sold a trademark to a subsidiary. This was a 'once-only' occurrence and was invoiced at cost plus a nominal mark-up. The amount invoiced was \$17,800.

Management and marketing fees

XYZ Pty Ltd performed management services for its subsidiaries, and charged them cost plus 5%.

The amount invoiced was \$16,000.

For taxation purposes XYZ Pty Ltd selected, applied and documented a bona fide CUP of \$21,700.

This arm's length price was reflected in the taxable income by an adjustment at item **7 Reconciliation to taxable income or loss** on XYZ Pty Ltd's tax return.

- Training was provided for the sales staff of one subsidiary. No amount was invoiced for this service but, in exchange, the subsidiary completed a specific research project for XYZ Pty Ltd.

Technical and construction

XYZ Pty Ltd provided ongoing technical services regarding manufacturing processes to a subsidiary, and invoiced those services at rates equivalent to prices for similar services performed for arm's length customers. The process was not analysed in detail, neither was it documented.

- The amount invoiced was \$12,650.


Research and development

XYZ Pty Ltd maintained a research and development (R&D) division and incurred R&D expenditure on behalf of all subsidiaries and its own activities. Subsidiaries paid their own share of the total annual cost, and no mark-up was included in the invoiced price. The total amount was \$24,600.


Loans

On 29 June 2011, XYZ Pty Ltd approved the interest-bearing loan of \$450,000 to a subsidiary.

Answer to item 2

 Summary of the dealings

Working calculations for item 2

 Suggested answer to item 2

Answer to item 3a

Y for yes should be written at item **3a**. This is because XYZ Pty Ltd has provided management services to an international related party and consideration was settled by means of a swap or barter (in this case, staff training in return for the research project).

Answer to item 3b


Y for yes should be written at item **3b**. The subsidiaries used trademarks owned by XYZ Pty Ltd but did not pay royalties which is a dealing for which there was no consideration.

Answer to item 4a

The percentage of the related-party dealings for which written documentation is held to support the selection of arm's length pricing methods is calculated as follows.

The total dollar value of related-party dealings, for which an amount was included at items **2a** to **2d** is \$444,145.

The total dollar value of the dealings for which you hold documentation supporting selection and characterisation in accordance with steps 1 and 2 of chapter 5 of TR 98/11 is determined as follows:

 Answer to item 4a

The percentage is calculated as 71.5% (\$317,595 divided by \$444,145).


At **F** item **4a**, Code **4** is written.

Answer to item 4b

The percentage of the related-party dealings, for which you hold documentation to support the application of arm's length pricing

methods in accordance with step 3 of chapter 5 of TR 98/11, is calculated as follows:

- The total dollar value of related-party dealings is \$444,145, based on the amounts shown at items **2a** to **2d**.
- The total dollar value of the dealings for which the relevant supporting documentation is held is determined as follows:

 Answer to item 4b

The percentage is calculated as 59.1% being \$262,676 divided by \$444,145.

At **G** item **4b**, code **4** is written.

Answer to item 5

The amounts for dealings of a revenue nature are all the amounts in the **Answer to item 2** above after excluding the amounts for capital dealings (being the sale of shares to a subsidiary, the purchase of machinery by a subsidiary, and the sale of the trademark to a subsidiary).

The total amount for dealings of a revenue nature was \$384,150 ($\$444,145 - (\$23,345 + \$18,850 + \$17,800)$).

The total amount for dealings of a capital nature was \$59,995 ($\$23,345 + \$18,850 + \$17,800$).

The two arm's length pricing methods used for amounts included at items **2a** to **2d** were the CUP method, code 1, and the cost-plus method, code 3.

The method codes are in the table at [item 5](#) column A.

The codes for the percentages are in the table at [item 5](#) column B.

The percentage of the total amount for dealings of a revenue nature (\$384,150) representing use of each kind of method are calculated as follows:

CUP	\$202,175	52.6%
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(\$73,225 + \$107,250 + \$21,700)		
Cost plus	\$73,225	19.1%

The labels in item **5** are therefore completed as follows (with labels **L**, **M**, **N** and **O** left blank):

H	0	1		I	4
J	0	3		K	2

Answer to item 6

The amounts in the Answer to item 2 above which are for dealings of a capital nature are:	
• sale of shares	\$23,345
• purchase of machinery	\$18,850
• sale of a trademark	\$17,800
Total	\$59,995

Answer to item 6a

<p>The purchase of machinery, the sale of shares and the sale of the trademark will all be CGT events within the meaning of Division 104 of the ITAA 1997.</p> <p>At P item 6a write Y for yes.</p>
--

Answer to item 6b

At this item, write the codes for the four principal methods used for pricing these capital dealings. In this example only three methods were used:

- the quoted market price method for the share dealing - code **7**
- the cost price method for the machinery - code **2**, and
- other methods for the trademark - code **8**.

These codes are from the table at [item 6b](#)

The labels in item **6b** are therefore completed as follows:

Q	7	2	8	
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Answer to item 6c

In this item, write the codes for the percentage of the total of the amounts in the **Answer to item 2** above representing dealings of a capital nature .

This percentage is calculated as follows:

	$\frac{\$59,995}{\$444,145}$	=	13.5%
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The relevant codes are from the table at [item 6c](#)

Label **R** in item **6c** is therefore completed as follows:

R	2
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More information

28 September 2012

Publications referred to in these instructions



Publications



Phone



Other services



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Publications referred to in these instructions

28 September 2012

- *Business industry codes 2011* (NAT 1827)
- *Company tax return instructions 2011* (NAT 0669)
- *Income Tax Assessment Act 1936*
- *Income Tax Assessment Act 1997*
- *Income Tax Regulations 1936*
- *International dealings schedule - financial services 2011* (NAT 73345)
- *International dealings schedule - financial services instructions 2011*
- *Taxation Ruling TR 94/14 - Income tax: application of Division 13 of Part III (international profit shifting) - some basic concepts*

underlying the operation of Division 13 and some circumstances in which section 136AD will be applied

- *Taxation Ruling TR 97/20 - Income tax: arm's length transfer pricing methodologies for international dealings*
- *Taxation Ruling TR 98/11 - Income tax: documentation and practical issues associated with setting and reviewing transfer pricing in international dealings*
- *Taxation Ruling TR 1999/1 - Income tax: international transfer pricing for intra-group services*
- *Taxation Ruling TR 2001/11 - Income tax: international transfer pricing - operation of Australia's permanent establishment attribution rules*
- *Taxation Ruling TR 2004/1 - Income tax: international transfer pricing - cost contribution arrangements.*

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