Key to your future

CAA

CHARTERED ACCOUNTANTS ACADEMY

NATIONAL LEADER IN TRAINING CHARTERED ACCOUNTANTS

Tax Avoidance – Income splitting & Transactions between associates

Learning Outcomes

- Understand the general principles on tax avoidance.
- Interpret the definition of associate, control and controlled transactions.
- Understand how the taxman can apply income splitting principles to address tax avoidance.
- Apply the principles of income splitting in determining a tax payers taxable income.
- Understand the transfer pricing requirements.
- Understand the purpose and use of transfer pricing methods
- Apply the principles on transfer pricing in determining a taxpayers taxable income.

Tax Avoidance generally: sect 98

Requirement:

Where a transaction has been entered into:

- *In a manner which does not normally apply for similar transactions; or*
- *Has created rights and obligations which would not normally be created between persons dealing at arms length.*

Tax avoidance generally

How then will the commissioner determine tax payable?

- May completely disregard the existence of such transaction or
- Determine the tax payable in such a way that there is no avoidance or reduction of tax liabilities.

Implication of this requirement

- The provision apply regardless of whether the parties to the transactions are related.

Income splitting- sect 98A

What is income splitting?

- Transfer of **income** or **property** to an **associate** and the **sole or main** reason for the transfer is to lower the tax payable on the incomes of the two parties.

What is an associate?

- Refer to sect 2A & page 67 in module 1

Income splitting- sect 98A

What happens if a transactions results in income splitting?

- The commissioner will tax the two parties as if the transaction which resulted in income splitting never occurred.

Example

Refer to page 68 in module 1.

Transactions between associates

Sect 98B & 35th schedule

Requirement – par 1

The taxable income for **controlled transactions** between **associates** shall be determined with reference to the **arm's length principle** in a **comparable** uncontrolled transaction **.**

From the above key questions to answer are:

- What is a controlled transaction?;
- How do we determine comparability;
- What is an associate?; and
- How do we determine arms length price?

Comparability – 35th sch par 3

An uncontrolled transaction is comparable to a controlled transaction:

- Where there are no material differences between the two transactions or
- Where there is such differences accurate comparability adjustments can be made.

Controlled transaction – 35th schedule par 1

Uncontrolled transactions means any transaction between **independent persons**.

Quiz: provide examples of controlled transactions.

Arms length principle – 35th sch par 4

The arms length principle shall be used to determine the transfer price to be used in calculating the taxable income for controlled transactions between associates.

Transfer pricing methods:

1. Comparable uncontrolled price – page 71 module 1;
2. Resale price – page 71 module 1;
3. Cost plus – page 72 module 1;
4. Transactional net margin – page 72 module 1; and
5. Transactional profit split method – page 73.

Transactions with non-residents

Provisions in 98B also to transactions with non-residents.

Questions