Transfer Pricing Country Summary
Zambia

June 2018

Legislation

Existence of Transfer Pricing Laws/Guidelines

The Zambian transfer pricing rules apply to related party transactions both domestically and cross-border.

The legislative basis for the Zambian transfer pricing rules is Section 97 (A-D) of the Income Tax Act (Chapter 323 of the laws of Zambia) ("Act"), read with the Income Tax (Transfer Pricing) Regulations of 2000, as amended by the Income Tax (Transfer Pricing) (Amendment) Regulations 2018, published on 6 April 2018.

The amended regulations ("Regulations"), incorporate many of the OECD's recommendations in respect of BEPS Actions 8-10, including the requirement to prepare transfer pricing documentation, rules governing the application of the arm's length principle, and a new safe harbor in relation to low value add intra-group services.

The Regulations are to be interpreted consistently with the OECD Guidelines and the United Nations Practical Manual on Transfer Pricing for Developing Countries. In the case of conflict between these documents and the Regulations however, the Regulations prevail.

On 14 December 2017, the OECD announced that Zambia has joined the inclusive framework on BEPS.

Definition of Related Party

The threshold for application of the transfer pricing regulation is 50% participation by a person/corporate entity, directly or indirectly in the management, control or capital of a second person/corporate body at a point in time.

Transfer Pricing Scrutiny

The level of scrutiny in respect of cross-border transactions generally, is high.

Transfer Pricing Penalties

Zambia does not have specific transfer pricing penalties. The penalties enshrined in the Act generally apply on transfer pricing cases as well.

Thus, persons guilty of tax offences against the Act are liable for an imprisonment term not exceeding 12 months; and or to a fine; except otherwise another penalty are prescribed by the Commissioner-General.

Generally, penalties ranging from 17.5% to 35% for incorrect return may be charged on understated income amount.

Furthermore, late payment of tax (on mineral as well) is penalized by a fine of 5% per month of the amount due, plus an interest assessed on the outstanding tax payable at the Bank of Zambia discount rate plus 2% surcharge. Fraudulent filing of tax returns is fined at a rate of 52.5% of the amount.

Advance Pricing Agreement (APA)

There is no provision for Advanced Pricing Agreements in the Act. However, a taxpayer may consult the tax authorities regarding the interpretation or application of any provisions in the Income Tax Act.

Safe Harbors

The Regulations provide for a safe harbor in respect of low value added services, of cost plus 5%, provided that the service charge is based on an appropriate cost allocation method.

Thin capitalization rules exist in relation to mining companies and limit interest deductions where such companies have a debt to equity ratio exceeding 3 to 1.

Documentation And Disclosure Requirements

Tax Return Disclosures

The corporate income tax return requires disclosure of whether the taxpayer entered into any related party transactions during the year. If this is answered in the affirmative, significant disclosure of the nature and value of the related party transactions is required.

Level of Documentation

In terms of the Regulations, a person participating in a controlled transaction is required to prepare, on an annual basis, contemporaneous documentation (defined as documentation which is generated when a person is developing or implementing a controlled transaction), which is to be provided to the revenue authority upon request.

The structure and content required for such contemporaneous documentation is based on the local file template in Annex II to Chapter V of the OECD Guidelines, with some additional specific requirements regarding budgets and financial estimates.

Record Keeping

In addition to the contemporaneous documentation, a person who engages in a controlled transaction is required to maintain certain information regarding the transaction, the associated person and the transfer pricing method used. The structure and content of such information largely follows the master file template in Annex I to Chapter V of the OECD Guidelines.

Language for Documentation

Documentation should be in English. Where a document required for purposes of the Regulations is not in English, the person required to submit it shall, at the person's own expense, produce a translation in English, prepared and certified by a translator before a Notary Public.

Small and Medium Sized Enterprises (SMEs)

The requirement to prepare contemporaneous documentation does not apply to a person whose annual turnover is less than 20 million Kwacha in any charge year, however this exemption does not apply to MNEs.

Deadline to Prepare Documentation

As discussed above, the contemporaneous documentation is to be made available upon request. No specific deadline exists, however in terms of the definition of "contemporaneous documentation" the documentation relates to the development and implementation of a controlled transaction and it is therefore advisable that such documentation be in place by the time a controlled transaction is implemented.

The record-keeping information is required to be prepared by the due date of the annual return submission, but is not required to be submitted with the return. Such information must, however, be submitted within thirty days from date of a written request by the Commissioner-General. Failure to provide such information is an offence, subject to the penalty provisions under the Income Tax Act.

Statute Of Limitations

The time limit for any deliberate or negligent filing of the tax return or furnishing of tax documentation as requested by the commissioner general is 6 years after the date of commission of the offence.

Transfer Pricing Methods

As aforementioned, the Zambian Revenue Authority has embraced the OECD Transfer Pricing international standards – the Arm's Length Principle. She also adopted the 5 OECD transfer pricing methods:

- the comparable uncontrolled price method;
- resale price method;
- cost plus method;
- transactional net margin method;
- transactional profit split method.

It is noted that the application of the CUP method in relation to the acquisition of new or used assets from non-connected persons resident outside Zambia, is subject to specific documentary requirements in relation to the supply chain, including invoices and delivery notes.

Other transfer pricing methods may be applied, in case it can be established that:

- none of the methods can be reasonably applied to determine arm's length conditions for the controlled transaction; and
- such other method yields a result consistent with that which would be achieved by independent persons engaging in comparable uncontrolled transactions under comparable circumstances.

The approval of the Commissioner-General is required in order to apply such non-standard transfer pricing methods.

Comparables

In practice, when an audit commences, the audited company is ordered to provide transfer pricing documentation. The Zambian Revenue Authorities in a bid to reassess the company's taxable income generally prefer the company under investigation provide comparables to substantiate her transfer price. She then assesses the comparables provided and thus determines its arm's length nature; and or negotiates with the controlled company accordingly.

An uncontrolled transaction is comparable to a controlled transaction within the meaning of Section 97A of the Act when:

- there are no significant differences between that uncontrolled transaction and a controlled transaction that could materially affect the financial indicator being examined under the appropriate transfer pricing method; or

- such differences exist, if a reasonably accurate adjustment is made to the relevant financial indicator of the controlled transaction un order to eliminate the effects of those differences on the comparison.

The Commissioner-General, in causing to be determined whether 2 or more transactions are comparable, shall consider the following factors to the extent that they are economically relevant to the facts and circumstances of the transactions:

- the characteristics of the property or services transferred or supplied;
- the functions undertaken by each person with respect to the transactions while taking into account assets used and risks assumed;
- the contractual terms of the transactions;
- the economic circumstances in which the transactions take place; and
- the business strategies pursued by the person and associated person in relation to those transactions.

Where the comparables include points that have a lesser degree of comparability, the interquartile range is to be used to enhance reliability. In the absence of persuasive evidence for the selection of a particular point in the range, the Commissioner-General may adjust to the mid-point.

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