

# Transfer Pricing e-Alert

5 SEPTEMBER 2019

## Expert Witnesses In Transfer Pricing Disputes

*Chevron Australia Holdings Pty Ltd v Commissioner of Taxation* [2015] FCA 1092 was an Australian transfer pricing dispute which involved more than 20 witnesses and experts ranging from corporate banking, rating agencies and academia to oil and gas industry and transfer pricing specialists.

Briefly, the case concerns the assessment raised against Chevron Australia Holdings Pty Ltd (**CAHPL**) in relation to interest payments to its US-domiciled subsidiary, Chevron Texaco Funding Corporation (**CFC**). Both CAHPL and CFC have a common parent company, Chevron Corporation (**CVX**).

CFC had raised USD2.5 billion at rates of interest at or below USD LIBOR (approximately 1% to 2%) from the commercial paper market. CFC obtained a guarantee from CVX for the funds raised. Via a Credit Facility Agreement, CFC provided an inter-company loan to CAHPL for the AUD equivalent of USD2.5 billion on an unsecured basis. CAHPL then paid interests to CFC at an interest rate of AUD LIBOR plus 4.14%.

## Australian Court's Decision In *Chevron Australia Holdings*

Transfer pricing assessments were raised against CAHPL on the basis that the interest rates paid to CFC were in excess of an arm's length rate. The Federal Court held that CAHPL had not shown that the interest paid under the Credit Facility Agreement was equal to or less than arm's length. Hence, CAHPL had failed to prove that the assessments were excessive. The absence of loan covenants and security in the Credit Facility Agreement was a significant factor in the findings of the court. Reference is made to the following paragraph of the Federal Court's judgment:

"...CAHPL did not give security or operational and financial covenants, which would have affected that part of the consideration which was the interest rate: the interest rate was higher in the absence of those promises or covenants. **If the property had been acquired under an agree-**

### Contact persons:



**Datuk D. P. Naban**  
Senior Partner  
Tax, SST & Customs Practice  
T: +603 6208 5858  
E: dpn@lh-ag.com



**S. Saravana Kumar**  
Partner  
Tax, SST & Customs Practice  
T: +603 6208 5813  
E: sks@lh-ag.com

**CHAMPIONING  
TAXPAYERS**

We represent taxpayers. Be it tax litigation, advisory or structuring,  
we focus on clarity, certainty and solutions.  
Make us your confidante today.

## Transfer Pricing e-Alert

ment between independent parties dealing at arm's length with each other, I find that the borrower would have given such security and operational and financial covenants and the interest rate, as a consequence, would have been lower. The limited scope of the consideration given or agreed to be given by CAHPL resulted in the consideration which CAHPL did give, the promise to pay the interest rate, exceeding the arm's length consideration in respect of the acquisition. It follows, on that basis, that the applicant has not shown that the arm's length consideration assessed by the respondent Commissioner was excessive."

The Federal Court referred to expert reports submitted by CAHPL which provided evidence of the evaluation process undertaken by commercial lenders in assessing credit and in pricing loans. In reviewing the expert reports, the court observed:

"CAHPL put its positive case primarily by reference to the expert reports of Mr Gross and Mr Martin.

"As to Mr Gross, it will be recalled that the question he was asked was whether the interest rate in the Credit Facility Agreement exceeded the consideration that might reasonably have been expected to have been given by CAHPL to an independent third party for the provision of the Credit Facility. His conclusion was that the correct pricing of the Credit Facility provided by CFC to CAHPL was 500 basis points over 1 month AUD LIBOR BBA. Therefore the interest rate in the Credit Facility Agreement, in his opinion, did not exceed the consideration that might reasonably have been expected to have been given by CAHPL to an independent third party for the provision of the Credit Facility.

#### Our sub-specialisation includes:

<b>INCOME TAX</b>	<b>SALES &amp; SERVICE TAX</b>	<b>TRADE FACILITATION &amp; INCENTIVES</b>
• Tax Litigation & Dispute Resolution Proceedings	• SST Litigation	
• Tax Advisory & Planning	• SST Legal Advisory	<b>REAL PROPERTY GAINS TAX</b>
• Tax Audit & Investigation	• SST Audit & Investigation	
• Transfer Pricing & Thin Capitalisation	• Anti-Profitfiltering	<b>PETROLEUM INCOME TAX</b>
<b>INTERNATIONAL TAX</b>	<b>CUSTOMS DUTY, EXCISE DUTY, SAFEGUARD DUTY &amp; ANTI-DUMPING DUTY</b>	<b>SALES &amp; SERVICES TAX</b>
(Including Cross-border Transaction Tax & Withholding Tax)		
		<b>STAMP DUTY</b>
		...

[www.lh-ag.com](http://www.lh-ag.com)

### Lee Hishammuddin Allen & Gledhill

Level 6, Menara 1 Dutamas  
Solaris Dutamas  
No. 1, Jalan Dutamas 1  
50480 Kuala Lumpur  
Malaysia  
Tel: +603 6208 5888  
Fax: +603 6201 0122  
Email: [tax@lh-ag.com](mailto:tax@lh-ag.com)

## Transfer Pricing e-Alert

“Further, I would be reluctant to place weight on an analysis, such as that of Mr Gross, where he accepted that there could not have been a single lender under an agreement between independent parties and no lender would lend absent financial covenants. **Mr Gross wrote:**

**‘In fact, such a lender would not make a five-year bullet loan without restrictive financial covenants. It would have been impossible to either syndicate a loan or use a high-grade or high yield bond without those covenants.’**

‘He also said that there were no loans or bonds in the market with such a lack of financial covenants.

“Mr Gross also agreed that an absence of restrictive or negative covenants meant that CAHPL, and **I would infer an independent borrower, could not have entered into the Credit Loan Facility.**

...

“I do not accept the applicant’s submission that a Term Loan B was an appropriate comparator for the hypothetical where, most significantly, the borrower would be an E&P company with a BB risk rating equivalent; there were no financial covenants for the borrowing; there were no restrictive covenants for the borrowing; and the borrower could repay the loan at any time such that the lender would have the risks but not the benefit for potentially a short period. It follows, in my opinion, that Mr Martin’s evidence that the Credit Facility could be priced as a Term Loan B **lacks a realistic foundation.**”

#### Our sub-specialisation includes:

##### INCOME TAX

- Tax Litigation & Dispute Resolution Proceedings
- Tax Advisory & Planning
- Tax Audit & Investigation
- Transfer Pricing & Thin Capitalisation

##### INTERNATIONAL TAX

(Including Cross-border Transaction Tax & Withholding Tax)

##### SALES & SERVICE TAX

- SST Litigation
- SST Legal Advisory
- SST Audit & Investigation
- Anti-Profitteering

##### CUSTOMS DUTY, EXCISE DUTY, SAFEGUARD DUTY & ANTI-DUMPING DUTY

##### TRADE FACILITATION & INCENTIVES

##### REAL PROPERTY GAINS TAX

##### PETROLEUM INCOME TAX

##### SALES & SERVICES TAX

##### STAMP DUTY

[www.lh-ag.com](http://www.lh-ag.com)

### Lee Hishammuddin Allen & Gledhill

Level 6, Menara 1 Dutamas  
Solaris Dutamas  
No. 1, Jalan Dutamas 1  
50480 Kuala Lumpur  
Malaysia  
Tel: +603 6208 5888  
Fax: +603 6201 0122  
Email: [tax@lh-ag.com](mailto:tax@lh-ag.com)

## Transfer Pricing e-Alert

The Federal Court also gave “no weight to the opinions of transfer pricing economists where those opinions appear not to be founded in the statutory language which the Court must apply”.

Hence, it can be seen that the expert evidence tendered by CAHPL (specifically on the absence of loan covenants and security) ironically played a crucial role in leading the learned judge to arrive at the conclusion that CAHPL had not shown that the interest paid was equal to or at arm’s length.

The Federal Court’s decision was upheld by the Full Federal Court (see [2017] FCAFC 62).

### Importance Of Expert Witness

The primary function of the expert witness is to assist the court in reaching its decision by providing independent expert/technical analysis and opinion on an issue(s), based on the information provided by those instructing him. The expert evidence should provide as much detail as is necessary to convince the judge that the expert’s opinions are well founded.

The importance of expert evidence in tax hearings was highlighted by the Supreme Court of India in *CIT v Bharti Cellular Ltd* (2011) 330 ITR 239, where the Indian tax authority was instructed to issue directions to all its officers that in cases involving the determination of taxability of cellular service providers/other technical service providers, the department need not proceed only by the contracts placed before the officers. With the emergence of India as one of the BRIC countries and with the technological advancements in this area, the department should appoint technical experts to assist it and the courts in understanding the factual basis of cases.

Like the Indian Income Tax Act 1961, our Income Tax Act 1967 does not contain specific provisions regarding the use of expert reports as expert evidence. However, the Evidence Act 1950 (**EA**) provides for expert opinions to be taken into consideration for the purpose of reaching a sound conclusion.

#### Our sub-specialisation includes:

##### INCOME TAX

- Tax Litigation & Dispute Resolution Proceedings
- Tax Advisory & Planning
- Tax Audit & Investigation
- Transfer Pricing & Thin Capitalisation

##### INTERNATIONAL TAX

(Including Cross-border Transaction Tax & Withholding Tax)

##### SALES & SERVICE TAX

- SST Litigation
- SST Legal Advisory
- SST Audit & Investigation
- Anti-Profitfiltering

##### CUSTOMS DUTY, EXCISE DUTY, SAFEGUARD DUTY & ANTI-DUMPING DUTY

##### TRADE FACILITATION & INCENTIVES

##### REAL PROPERTY GAINS TAX

##### PETROLEUM INCOME TAX

##### SALES & SERVICES TAX

##### STAMP DUTY

[www.lh-ag.com](http://www.lh-ag.com)

### Lee Hishammuddin Allen & Gledhill

Level 6, Menara 1 Dutamas  
Solaris Dutamas  
No. 1, Jalan Dutamas 1  
50480 Kuala Lumpur  
Malaysia  
Tel: +603 6208 5888  
Fax: +603 6201 0122  
Email: [tax@lh-ag.com](mailto:tax@lh-ag.com)

Specifically, Section 45 of the EA reads:

- (1) When the court has to form an opinion upon a point of foreign law or of science or art, or as to identity or genuineness of handwriting or finger impressions, the opinions upon that point of persons specially skilled in that foreign law, science or art, or in questions as to identity or genuineness of handwriting or finger impressions, are relevant facts.
- (2) Such persons are called experts.

## The Malaysian Experience

In transfer pricing cases, expert witnesses play an important role in showing the court that the taxpayer's pricing methodology is in compliance with the necessary regulations. In Malaysia, *MM Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (2013) MSTC 10-046 was the first transfer pricing case in which the taxpayer's transfer pricing reports and testimonies by expert witnesses were key to establishing that the taxpayer's pricing methodology was in accordance with the OECD Transfer Pricing Guidelines.

In reliance on the expert reports (transfer pricing study and benchmarking study) and oral testimonies of the taxpayer's transfer pricing expert witnesses, the Special Commissioners of Income Tax commented:

"On a balance of probabilities, we accept the Appellant's principal contention that it has not agreed to accept the Respondent's audit procedure in determining the price methodology in the transfer pricing exercise.

"We are justified to say so because we are satisfied that AW3 and AW7 had **explained in detail as to the basis in which they drafted their transfer pricing reports** and arrived at their conclusions.

...

"Now, despite the Respondent's contention that the 13 independent and local comparables did not perform similar business principal activity as a "shipping agent"; that their incomes did not arise out

#### Our sub-specialisation includes:

<b>INCOME TAX</b> <ul style="list-style-type: none"> <li>• Tax Litigation &amp; Dispute Resolution Proceedings</li> <li>• Tax Advisory &amp; Planning</li> <li>• Tax Audit &amp; Investigation</li> <li>• Transfer Pricing &amp; Thin Capitalisation</li> </ul>	<b>SALES &amp; SERVICE TAX</b> <ul style="list-style-type: none"> <li>• SST Litigation</li> <li>• SST Legal Advisory</li> <li>• SST Audit &amp; Investigation</li> <li>• Anti-Profitfiltering</li> </ul>	<b>TRADE FACILITATION &amp; INCENTIVES</b>
<b>INTERNATIONAL TAX</b> <small>(Including Cross-border Transaction Tax &amp; Withholding Tax)</small>	<b>CUSTOMS DUTY, EXCISE DUTY, SAFEGUARD DUTY &amp; ANTI-DUMPING DUTY</b>	<b>REAL PROPERTY GAINS TAX</b>
		<b>PETROLEUM INCOME TAX</b>
		<b>SALES &amp; SERVICES TAX</b>
		<b>STAMP DUTY</b>

[www.lh-ag.com](http://www.lh-ag.com)

## Lee Hishammuddin Allen & Gledhill

Level 6, Menara 1 Dutamas  
 Solaris Dutamas  
 No. 1, Jalan Dutamas 1  
 50480 Kuala Lumpur  
 Malaysia  
 Tel: +603 6208 5888  
 Fax: +603 6201 0122  
 Email: [tax@lh-ag.com](mailto:tax@lh-ag.com)

## Transfer Pricing e-Alert

of commission rates alone; that they performed at different operating profit margins, yet we repeat on a balance of probabilities, **we accept the Appellant's contention on the veracity of its transfer pricing reports** because:

- (a) the Appellant had not arbitrarily prepared the reports but based their drafting on the TNMM method which we find credible and acceptable, and in any event the Respondent had not disputed the TNMM method;
- (b) granted that the 13 comparables did not perform exactly similar functions like the Appellants yet we accept the fact that they performed generally similar functions as a "shipping agent". In our considered view the functions of "air freight forwarding agency" and "courier" etc can also be generally categorised as doing similar business as a "shipping agent" like the Appellant. This is especially so because we accept the Appellant's contention that there are no uncontrolled comparables in the market;
- (c) We agree that at no time when the Appellant's witnesses were under cross-examination did the Respondent's counsel suggest, much less put, the question that the transfer pricing reports are "afterthought".

In the recent transfer pricing case of *OSB v Ketua Pengarah Hasil Dalam Negeri* (yet to be reported), the independent transfer pricing reports provided by the taxpayer's transfer pricing consultant and testimony in court served as vital evidence in proving that the disputed transaction was at arm's length. As transfer pricing is not an exact science, taxpayers should actively review their transfer pricing policies and explore the appropriate steps that need to be implemented to comply with transfer pricing laws.

#### Our sub-specialisation includes:

<b>INCOME TAX</b> <ul style="list-style-type: none"> <li>• Tax Litigation &amp; Dispute Resolution Proceedings</li> <li>• Tax Advisory &amp; Planning</li> <li>• Tax Audit &amp; Investigation</li> <li>• Transfer Pricing &amp; Thin Capitalisation</li> </ul>	<b>SALES &amp; SERVICE TAX</b> <ul style="list-style-type: none"> <li>• SST Litigation</li> <li>• SST Legal Advisory</li> <li>• SST Audit &amp; Investigation</li> <li>• Anti-Profitteering</li> </ul>	<b>TRADE FACILITATION &amp; INCENTIVES</b>
<b>INTERNATIONAL TAX</b> <small>(Including Cross-border Transaction Tax &amp; Withholding Tax)</small>	<b>CUSTOMS DUTY, EXCISE DUTY, SAFEGUARD DUTY &amp; ANTI-DUMPING DUTY</b>	<b>REAL PROPERTY GAINS TAX</b>
		<b>PETROLEUM INCOME TAX</b>
		<b>SALES &amp; SERVICES TAX</b>
		<b>STAMP DUTY</b>

[www.lh-ag.com](http://www.lh-ag.com)

### Lee Hishammuddin Allen & Gledhill

Level 6, Menara 1 Dutamas  
 Solaris Dutamas  
 No. 1, Jalan Dutamas 1  
 50480 Kuala Lumpur  
 Malaysia  
 Tel: +603 6208 5888  
 Fax: +603 6201 0122  
 Email: [tax@lh-ag.com](mailto:tax@lh-ag.com)

# Transfer Pricing e-Alert

Taxpayers should ensure that all transfer pricing documentation are contemporaneously prepared and regular transfer pricing reports are obtained from transfer pricing consultants as these reports help to advance their case in the event of a dispute by the tax authority.

**Datuk D P Naban** and **S Saravana Kumar**, our partners from the Tax, SST & Customs Practice, successfully represented the taxpayers in the *MM* and *OSB* cases.

## Contact persons:

### Datuk D. P. Naban

Senior Partner  
Tax, SST & Customs Practice  
T: +603 6208 5858  
E: [dpn@lh-ag.com](mailto:dpn@lh-ag.com)

### S. Saravana Kumar

Partner  
Tax, SST & Customs Practice  
T: +603 6208 5813  
E: [sks@lh-ag.com](mailto:sks@lh-ag.com)

If you have any queries pertaining to transfer pricing disputes, please contact our tax partners at [tax@lh-ag.com](mailto:tax@lh-ag.com)

**Published by the Tax, SST & Customs Practice,  
Lee Hishammuddin Allen & Gledhill**

#### Our sub-specialisation includes:

##### INCOME TAX

- Tax Litigation & Dispute Resolution Proceedings
- Tax Advisory & Planning
- Tax Audit & Investigation
- Transfer Pricing & Thin Capitalisation

##### INTERNATIONAL TAX

(Including Cross-border Transaction Tax & Withholding Tax)

##### SALES & SERVICE TAX

- SST Litigation
- SST Legal Advisory
- SST Audit & Investigation
- Anti-Profitfiltering

##### CUSTOMS DUTY, EXCISE DUTY, SAFEGUARD DUTY & ANTI-DUMPING DUTY

##### TRADE FACILITATION & INCENTIVES

##### REAL PROPERTY GAINS TAX

##### PETROLEUM INCOME TAX

##### SALES & SERVICES TAX

##### STAMP DUTY

[www.lh-ag.com](http://www.lh-ag.com)

## Lee Hishammuddin Allen & Gledhill

Level 6, Menara 1 Dutamas  
Solaris Dutamas  
No. 1, Jalan Dutamas 1  
50480 Kuala Lumpur  
Malaysia  
Tel: +603 6208 5888  
Fax: +603 6201 0122  
Email: [tax@lh-ag.com](mailto:tax@lh-ag.com)

