

Transfer Pricing in China

[CHN ¶5-100] Annual information returns

Within four months after the end of the tax year, an associated enterprise must submit an “Annual Declaration to the State Administration of Taxation of the People’s Republic of China on Business Transactions between Foreign Investment Enterprises and Foreign Enterprises with Their Associated Enterprises” to the in-charge tax bureau. If the enterprise conducted business transactions with two or more than two related parties, separate declarations must be submitted.

The Declaration Forms comprise Form A and Form B. Form A applies to enterprises where the types and substance of the business transactions were uniform and unitary. It requires the taxpayer to declare information such as:

- enterprise name;
- address;
- total capital;
- main business; and
- head of the enterprise.

The enterprise is required to provide details of its related party transactions, such as:

- type;
- content;
- date;
- quantity;
- model;
- fee standard; and
- amount.

Form B applies to enterprises where the business transactions were varied and different. It requires the taxpayer to provide information similar to Form A, and also to fill out the details of the related party transactions, classified by sales, financing, service, transfer of the property, or the provision of the right to use the property.

Furthermore, Form B requires the information to be verified. The increase (decrease) in the amount of related party transactions over that of the previous years should also be provided. The requirements of Form B are more stringent.

If the enterprise cannot submit the Declaration within the time schedule due to special circumstances, an application for the extension should be submitted to the competent tax authorities within the prescribed time limit. Upon the approval by the tax authorities, the deadline may be extended for a maximum of 30 days.

Even though it seems that the requirement for reporting related party and related party transactions may not be stringent, the laws give tax authorities much discretionary power in requesting information from taxpayers. During a transfer pricing investigation, the tax authorities may ask the enterprises to provide relevant information.

On the surface, the taxpayer’s reporting responsibility is not heavy. However, once the audit procedures have started, the taxpayer is required to provide many reports to the tax authorities in a short time. Taxpayers that are not prepared for this may end up in a chaotic situation. If the deadline for filing the reports is not met, the taxpayer is likely to be subject to fines and penalties.

[CHN ¶6-100] Requirements for documentation

When the competent tax authorities have put a case on file and have started investigating the business transactions between an enterprise and its related parties, the tax authorities have the power to ask the enterprise to provide relevant materials regarding its business transactions with related parties, such as the pricing and expenses.

When making such requests, the tax authority should issue, in written form, a “Notice on Providing Specific Information on Business Transactions with Related Parties”. In this notice, the tax authority will list in detail, the specific information related to the related party transactions, such as the type, content, scope, period covered, quantity, amount, etc. It will mainly comprise the following information:

- 1. Discussion of each type of related-party transaction. The information that should be provided includes: purchases, sales, financing, loans, service provided, the transfer of tangible and intangible properties, and the provision of the right to use tangible and intangible properties;
- 2. Detailed functional analysis and supply chain analysis, such as the quantity, place, form, trademark, method of payment, discussion of the transfer pricing method (TPM) selected and the reasons for its selection to determine the components of the price factor in a transaction. The TP regulations does not mention whether it was necessary for the enterprise to give a description of the alternative methods that were considered and rejected. In practice, such a description is usually provided.

In the past, the taxpayer could just provide the components of the pricing factors, which was much simpler. Now, the taxpayers are under a heavier burden of proof to provide more information and documentation materials, eg the transfer pricing method.

- 3. The application of the TPM to the controlled transactions at issue, the basis for the receipt (payment) of expenses, and demonstration that the taxpayer’s related-party transactions were conducted at arm’s length, with references to comparable firms used to benchmark the taxpayer’s transfer prices.

After receiving the request for information from the tax authorities, the enterprise should provide such information in a timely, complete, truthful and accurate manner within the time prescribed by the notice (for a maximum of 60 days).

If such information cannot be provided in time due to special circumstances, a written application for the extension may be submitted to the in-charge tax bureau. After the approval is obtained, an extension may be granted for a maximum of 30 days. The in-charge tax bureau should reply to such request for extension within five days after the receipt of the request from the enterprise. If the tax bureau does not reply or does not reply within the time limit, it should be deemed as an approval for the extension.

The new rule provides a more lenient treatment for taxpayers who may find it difficult to provide all the materials within 60 days. However, given the complexity of the documentation, an extension of 30 days may still be not enough. As such, the taxpayer might need to have contemporaneous documentation.

If the enterprise failed to provide information on pricing and fee standard within the prescribed time limit (including the extension), the tax authority will invoke Art 62 of the *Law of the People’s Republic of China Concerning the Administration of Tax Collection* and impose a penalty of under RMB2,000. If circumstances are serious, a fine between RMB2,000 and RMB10,000 would be imposed.

If the enterprise provided false information, or refused to provide relevant information, the tax authority is empowered to inflict a penalty of under RMB10,000. If the circumstances are serious, the fine would be between RMB10,000 and RMB50,000.

Tax Planning & Compliance in Thailand

[THA ¶15-300] Transfer pricing and the Customs Act

Transfer pricing is not just concerned with direct tax. Indirect taxes, value-added tax, specific business tax and customs duties may also generate transfer pricing problems and issues.

Under the *Customs Act (No. 17) B.E. 2543 (2000)*, the word “customs price”, or “price” of any goods, means:

- • in the case of exportation, the cash wholesale price for the sale of goods, of the same category and type, without suffering any loss at the time and place of exportation, and without any deduction or reduction whatsoever; or
- • in the case of importation, the price of goods, with the aim of collecting the duty, according to any of the following prices. The customs price will be determined by applying the prices in the following order:

- (a) selling/buying price of imported goods;
- (b) selling/buying price of identical goods;
- (c) selling/buying price of similar goods;
- (d) deductible price;
- (e) computable price;
- (f) reversible price.

In cases where the declared price of imported goods is evidently low, or is unlikely to be the true value, and if, after the customs price has been fixed, the price is still evidently low or is unlikely to be the true value of such goods, the Director-General of the Customs Department has the power to re-fix the customs price of the said goods.

Based on the above provisions, it can be seen that the Customs Department has the power to determine and fix the customs price for imported goods for the purposes of imposing Customs Duty. Also, Customs law defines the situations where the relationship, between the parties involved, is regarded as a relationship that can affect the fixing of a “customs price”. These situations are:

- • A person is a director, or a member of the executive staff, of the business of another person.
- • A person is a partner of another person involved in a joint business operation.
- • A person is the employer or an employee of another person.
- • A person is an owner, a controller or a holder of shares with right to vote in the business of another person, and holds at least 5% of the voting shares, either directly or indirectly.
- • A person controls another person, either directly or indirectly.
- • A third person controls the two persons, either directly or indirectly.
- • The two persons jointly control a third person, either directly or indirectly.
- • A person is a family member of another person.

It is important not to mix-up this Customs’ procedure with the transfer pricing provisions contained in the *Thai Revenue Code* as their purpose is not the same. Basically, the Customs Department will intervene where the import prices are understated, because customs’ duty is being avoided. The Revenue Department will challenge overstated import prices by disallowing any excess price of the goods over the fair market value as an expense.

Law:

sec. 3 and sec. 5 of the *Customs Act (No. 17)*; Art. 3 of the *Ministerial Regulation No. 132 (B.E. 2543 (2000))* issued under the *Customs Act B.E. 2469 (1926)*; and *Customs Act (No. 17) B.E. 2543 (2000)*.

Tax Planning & Compliance in Korea

[KOR ¶15-100] Introduction to transfer pricing in Korea

Multinational enterprises tend to manipulate international transaction prices among related companies by reverting incomes to their affiliated companies operating in countries with relatively low tax rates in order to increase their income and minimise their overall tax burden. Rules on transfer pricing come into play in a situation where a domestic corporation or a domestic place of business of a foreign corporation (“resident”) enters into a cross-border transaction with its related foreign company in which the resident pays or receives a price much higher or lower than the arm’s length price. In such case, the taxable income is unreasonably transferred to the related foreign party. The tax authorities have the power to re-calculate a resident’s income by way of assessing the difference between the arm’s length price and the actual transaction price, and the power to include the difference as taxable income or exclude the difference from deductible expenses.

The transfer pricing rules are designed to prevent multinational enterprises from evading their tax obligations under Korean tax law by imposing tax on residents who enter into cross-border related party transactions. Moreover, if a related foreign party has control over a resident, and if the resident’s profit is classified as either a dividend income or interest on a loan paid to the resident under the transfer pricing rules, the tax authorities have the power to impose tax on the related foreign party with respect to such dividend income or the interest paid on the loan.

The *Law for Coordination of International Tax Affairs* provisions apply to cross-border related party transactions prior to other statutes. Article 52 of the *Corporate Tax Law* and regulations thereunder (so-called “domestic transfer pricing rules”),

for instance, shall not apply to cross-border related party transactions except for cases such as donation of assets, (excluding transfer of assets at a remarkably low price), waiver of debt, acquisition or in-kind capital contribution of non-income generating assets, and allocation between related parties of profits from capital increase or decrease, merger, spin-off or other capital transactions (Art 52 of the *Corporate Tax Law*; Art 3 of the *Law for Coordination of International Tax Affairs*; and Art 3-2 of the *Presidential Decree of the Law for Coordination of International Tax Affairs*).

The transfer pricing rule was first introduced in Korea in 1989 as part of the *Corporate Tax Law*. By enacting the *Law for Coordination of International Tax Affairs* (“LCITA”) in 1996, the government set up full-scale transfer pricing rules similar to the transfer pricing guidelines of the Organisation for Economic Co-operation and Development (“OECD”). Provisions on the advance pricing agreement (“APA”) became effective since 1997, which enable taxpayers to enter into an APA with the domestic tax authorities.

Law: Art 52 of the *Corporate Tax Law*; Art 3 of the *Law for Coordination of International Tax Affairs*; and Art 3-2 of the *Presidential Decree of the Law for Coordination of International Tax Affairs*.

Tax Planning & Compliance in Indonesia

[INS ¶15-200] Transfer pricing under the Indonesian Income Tax Law (“ITL”)

With regard to transfer pricing, the Indonesia tax authorities concentrate on transactions between parties sharing a so-called “special relationship”. In handling transactions among taxpayers who have a special relationship (“related parties”), the Indonesian taxation law adopts the substance-over-form rule. Although the tax authority adheres to a principle of substance over form in principle, in practice, attention is still very much focused on form.

Directorate General of Taxation (“DGT”) authority under the Indonesian Income Tax Law (“ITL”)

Under the ITL, the DGT is “authorised to re-determine the amount of income and/or deductions, or determine debt as equity, in accordance with fair and common business practice which is not influenced by a special relationship”.

Law: Art 18(3) of the *Indonesian Income Tax Law*.

Arm’s length transaction

The principle of establishing what is arm’s length is promulgated under the Transfer Pricing Directive, which broadly follows the Organisation for Economic Co-operation and Development (“OECD”) methodologies. The basic concept applied is the comparable uncontrolled price method. In the absence of any comparable pricing by parties that do not share a special relationship (“unrelated parties”), other methods such as cost-plus, sales-minus, other methods, ie profit split method and transactional net margin method may be used.

Law: Art 18(3) of the *Indonesian Income Tax Law*.

Special relationship

A “special relationship” is defined under Art 18 para. 4 of the ITL as follows:

- (a) a taxpayer possesses direct or indirect participation of 25% or more in another taxpayer, or where there is direct or indirect participation of at least 25% in each of the two taxpayers by another taxpayer;
- (b) a taxpayer has direct or indirect control over another taxpayer, or two or more taxpayers are under the same direct or indirect control; or
- (c) a direct or indirect family relationship within one degree exists by virtue of blood or marriage.

Law: Art 18(4) of the *Indonesian Income Tax Law*.