

# 32nd Annual Asia Pacific Tax Conference

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# The consequences of real transparency:

Reporting, documentation and reconsidering your Asian structures in light of BEPS

Chair: Peter Tan, Singapore

Rafic Barrage, USA

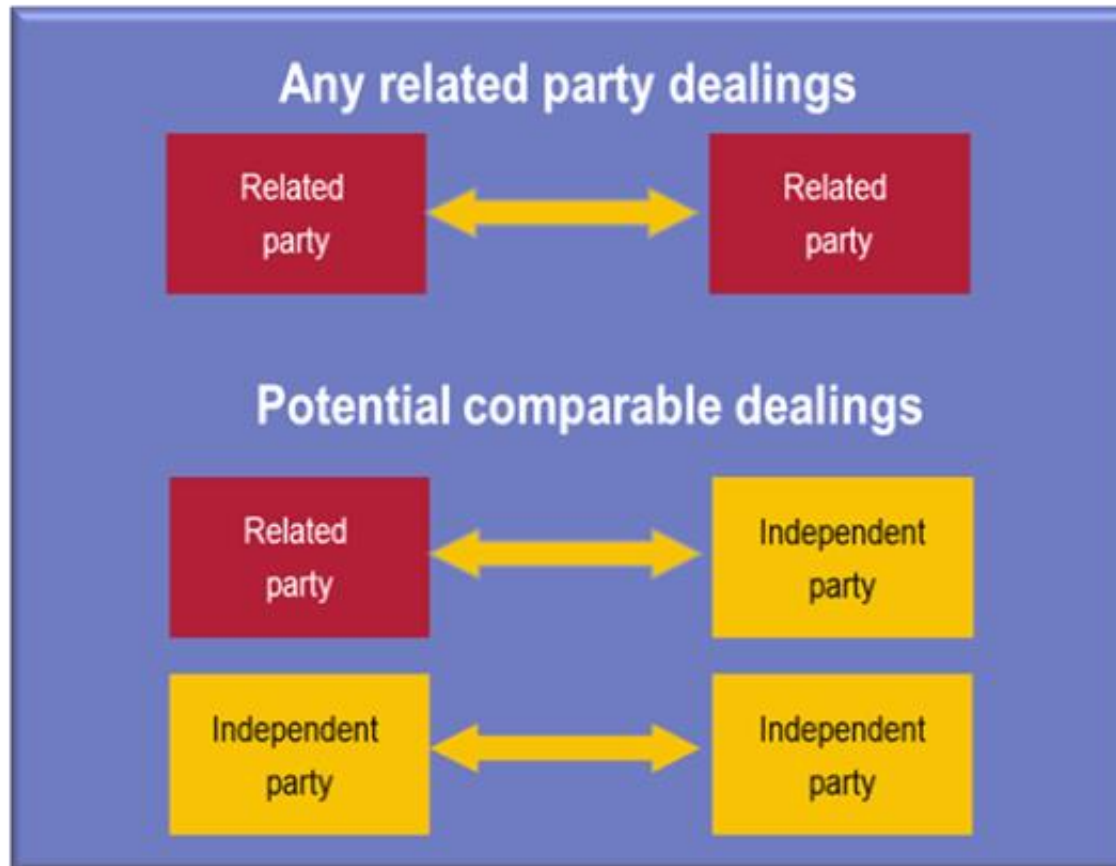
Pierre Chan, Hong Kong

Yukiko Komori, Japan

Liu Ning, Shanghai

Michael Nixon, Singapore

# Related party phobia?



# Transparency?





# Greater Transparency

1. Addressing tax challenges of the digital economy
2. Neutralising the effects of hybrid mismatch arrangements
3. Designing effective CFC rules
4. Limiting interest deductions and other financial payments
5. Countering harmful tax practices, taking into account transparency and substance
6. Preventing granting of treaty benefits in inappropriate circumstances
7. Preventing the artificial avoidance of PE status
- 8
- 9     Aligning TP outcomes with value creation
- 10
11. Measuring and monitoring BEPS
12. Mandatory disclosure rules
13. Transfer pricing documentation and CbCR
14. Making dispute resolution mechanisms more effective
15. Develop multi-lateral instruments to modify bilateral tax treaties

# Reconsidering your Asian structures in light of BEPS?

- Digital economy
- Hybrid arrangements
- Interest deduction limitation
- Issues surrounding PE status
- Queries regarding where value sits
- What will CbCR reveal?





# CbC Report Template

G114021

## List of all the constituent Entities of the MNE group included in each aggregation per tax jurisdiction

Name of the MNE group:

Fiscal year concerned:

Tax Jurisdiction	Constituent Entities resident in the Tax Jurisdiction	Tax Jurisdiction of organization or incorporation if different from Tax Jurisdiction of Residence	Main business activity(ies)												
			Research and Development	Holding or Managing intellectual property	Purchasing or Procurement	Manufacturing or Production	Sales, Marketing or Distribution	Administrative, Management or Support Services	Provision of Services to unrelated parties	Internal Group Finance	Regulated Financial Services	Insurance	Holding shares or other equity instruments	Dormant	Other <sup>1</sup>



# CbC Report Template

G114031

## **Additional Information**

Name of the MNE group:

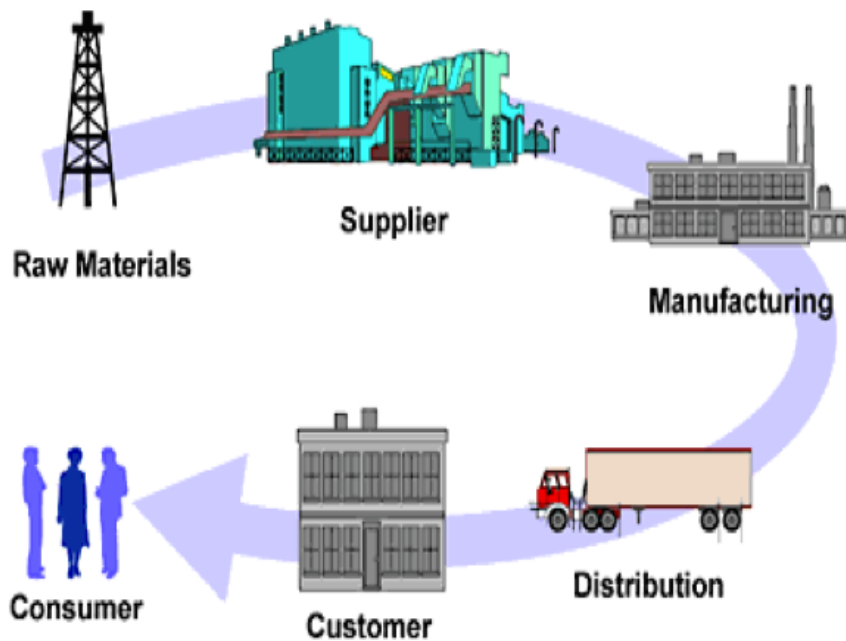
Fiscal year concerned:

Please include any further brief information or explanation you consider necessary or that would facilitate the understanding of the compulsory information provided in the country-by-country report.

# Transparency

- Exchange of Information under tax treaties
- MCMAA and MCAA
- BEPS Action 13 (CbCR)

# Reconsidering your Asian structures in light of BEPS?



# Reconsidering your Asian structures in light of BEPS?

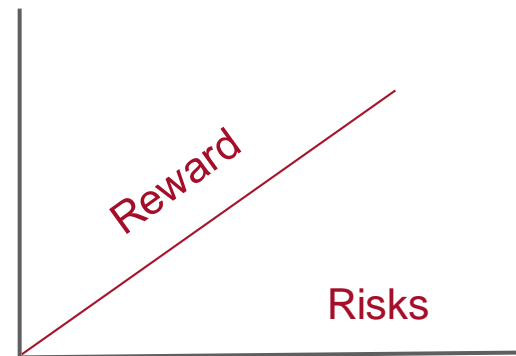
- Supply chain structures involve delivery of goods to the customers who demand the goods
- Supply chain management is about doing that efficiently and cost effectively
- This will be organised based on factors such as production costs, logistics costs and availability of resources
- Proximity to customers and logistics connectivity are also important

# Reconsidering your Asian structures in light of BEPS?

- Why are supply chain structures being scrutinised by tax administrations?
- What issues do tax administrations have – the profitability of each link in the supply chain or only the link in their country?
- What are the tax administrations doing?
- Which countries are most aggressive?
- What can taxpayers do?
- Do supply chain structures have a future?

# Reconsidering your Asian structures in light of BEPS?

- What tools do the tax administrations have?
  - BEPS Actions 1 – 15
  - Unilateral actions
  - Identifying where value really sits for profit attribution
  - Permanent establishment issues



# Reconsidering your Asian structures in light of BEPS?

## – Actions 8-10, Aligning Transfer Pricing Outcomes with Value Creation:

"The guidance ensures that:

- actual business transactions undertaken by associated enterprises are identified, and transfer pricing is not based on contractual arrangements that do not reflect economic reality
- contractual allocations of risk are respected only when they are supported by actual decision-making
- capital without functionality will generate no more than a risk-free return, assuring that no premium returns will be allocated to cash boxes without relevant substance
- tax administrations may disregard transactions when the exceptional circumstances of commercial irrationality apply."

# Reconsidering your Asian structures in light of BEPS?

Overarching Goal: make profits follow "value creation"

- Contractual risk allocation without decision making and control over the risk?
- Ability to support risk taking role?
- New PE rules, CFC-type rules, and profit splits will affect residual
- Nowhere income structures highly disfavored
- Certain functions have special significance, including DEMPE (**Development, Enhancement, Maintenance, Protection, Exploitation**)





# Reconsidering your Asian structures in light of BEPS?

## Action 13 - Transfer Pricing Documentation and Country-by-Country Reporting

*"...requirement that MNEs provide all relevant governments with needed information on their global allocation of income, economic activity and taxes paid among countries according to a common template."*

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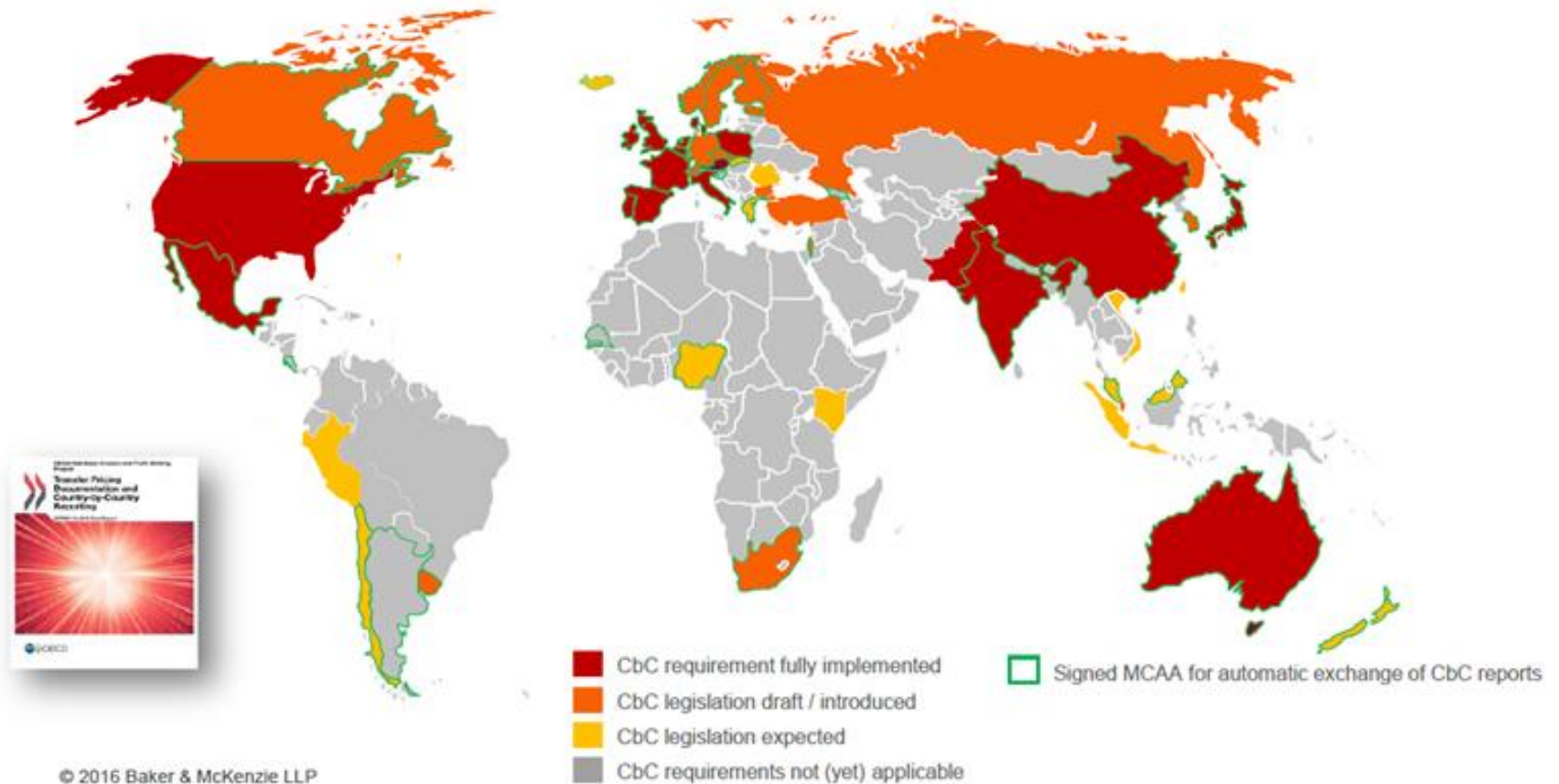
- Goal is for coherence and transparency
- with Master file, Local file and CbCR template
- Many countries have announced implementation for 2016

# What is Value: People, Capital, Risk

- People: CbC reporting will show people headcount and functions vs profits
- Capital
  - Legal ownership is only a starting point
  - Compensation may comprise "any share of the total return derived from exploitation of the intangibles."
- Risk
  - Control and financial capacity to assume risk is emphasized
  - Entitlement to unanticipated profits requires that an entity assume the risks which relate to them and perform the relevant functions



# Status of CBCR Implementation



# China

# Bulletin 42: New Transfer Pricing Documentation Requirements

## Bulletin 42: TP Documentation

Related Party Transaction Disclosure Forms	Contemporaneous Documentation		
22 forms including CbC Report	Master File	Local File	Special Documentation

# Bulletin 42: New Transfer Pricing Documentation Requirements

## Bulletin 42: TP Documentation

Related Party Transaction  
Disclosure Forms

Contemporaneous  
Documentation

22 forms  
including CbC Report

Master File

Local File

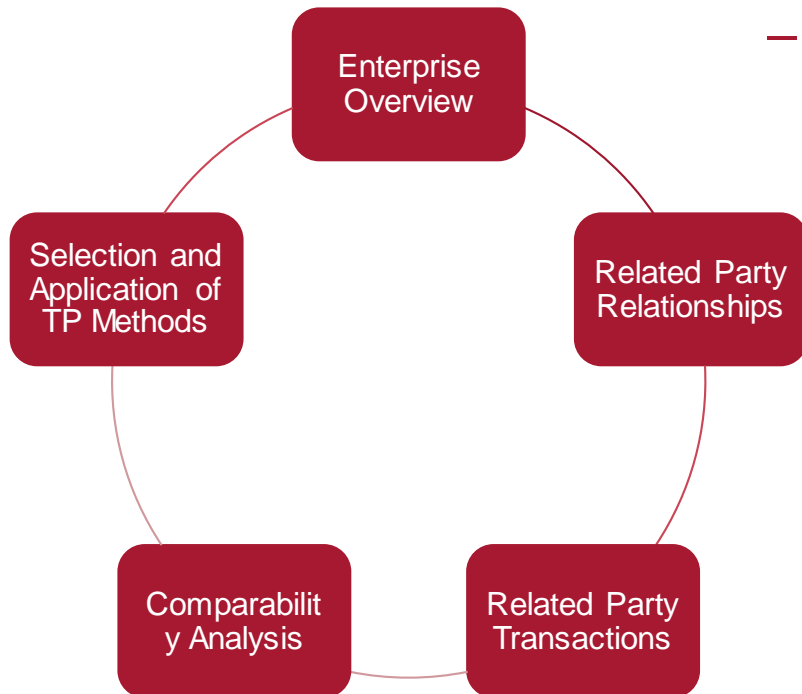
Special  
Documentation

# Master File



- An enterprise must prepare a master file within 12 months from when the fiscal year ends for the ultimate holding company if:
  - its total related-party transactions exceed RMB1 billion; or
  - it has cross-border related party transactions and the group has already prepared a master file.

# Local File



- An enterprise must prepare a local file by 30 June of the following year if:
  - its annual related-party transfers of tangible assets exceeds RMB200 million;
  - its annual related-party transfers of financial assets exceeds RMB100 million;
  - its annual related-party transfers of intangible assets exceeds RMB100 million; or
  - its annual other related-party transactions exceeds RMB40 million.

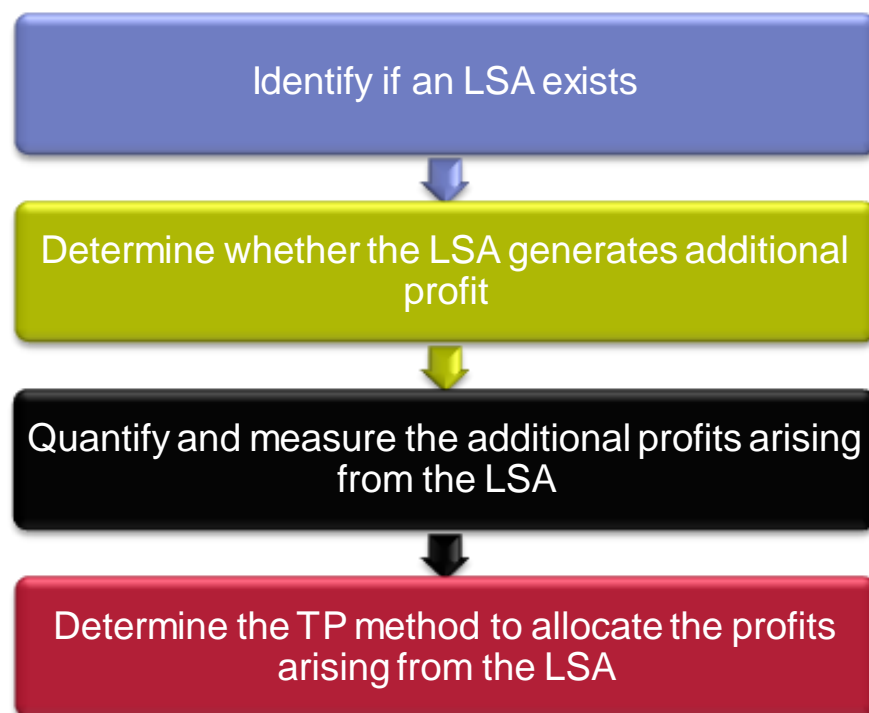


# Local File: Location Specific Advantages

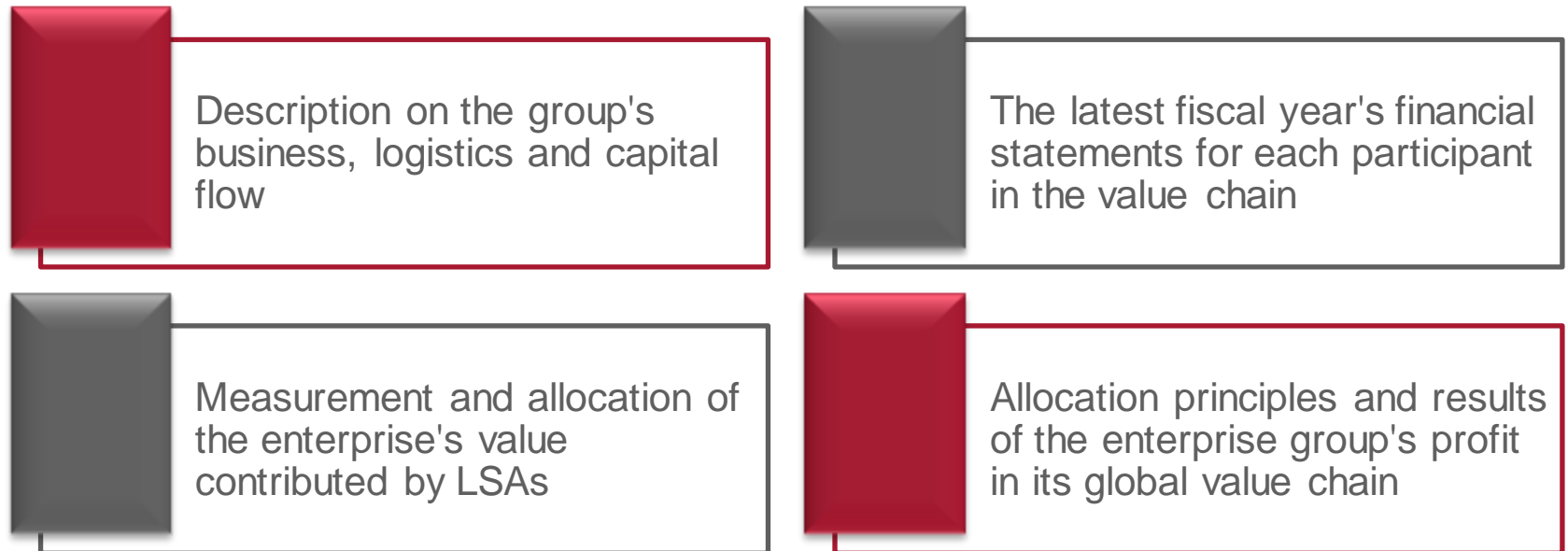
## Typical Examples of LSAs



## A four-step approach



# Local File: Value Chain Analysis



# Japan

# Japan TP Documentation (1)

A three-tiered approach was provided for in the domestic tax law based on the BEPS final report.

## 1. CbC Report:

- Reporting Entity: Ultimate Parent Entity of MNE group
- Excluded Entity: MNE group with consolidated revenues of **less than JPY 100 billion** in the prior year
- Items to be Reported: Same as items in Annex III to Chapter 5 of OECD Guidelines
- Notification: In principle, all Japanese taxpayer of the MNE groups must file the Japanese language form "Notification for Ultimate Parent Entity" **by the end day of the Ultimate Parent Entity's fiscal year**.
- Submission Method: CbC report **must be filed with the tax office via the E-Tax** (The national tax electronic declaration/payment system)
- Due Date of Filing: No later than 1 year after the last day of the fiscal year
- Language : English
- Timing of Application: Fiscal years of the Ultimate Parent Entity beginning on or after 1 April 2016
- Penalties: If a reporting entity fails to file the CbC report to the tax office by the deadline, **penalties will be imposed**.

# Japan TP Documentation (2)

## 2. Master file:

- Reporting Entity: A Japanese corporation (including a subsidiary of MNC group) or a foreign corporation having a PE in Japan
- Excluded Entity: MNE group with consolidated revenues of less than JPY 100 billion in the prior year
- Items to be Reported: Same as items in Annex I to Chapter 5 of OECD Guidelines
- Submission Method: Master file must be filed with the Tax Office via the E-Tax
- Due Date of Filing: No later than 1 year after the last day of the fiscal year
- Language : English or Japanese
- Timing of Application: Fiscal years of the Ultimate Parent Entity beginning on or after 1 April 2016
- Penalties: If a reporting entity fails to file the master file to the tax office by the deadline, penalties will be imposed.

# Japan TP Documentation (2)

## 2. Master file:

- Reporting Entity: A Japanese corporation (including a subsidiary of MNC group) or a foreign corporation having a PE in Japan
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- Items to be Reported: Same as items in Annex I to Chapter 5 of OECD Guidelines
- Submission Method: Master file must be filed with the Tax Office via the E-Tax
- Due Date of Filing: No later than 1 year after the last day of the fiscal year
- Language : English or Japanese
- Timing of Application: Fiscal years of the Ultimate Parent Entity beginning on or after 1 April 2016
- Penalties: If a reporting entity fails to file the master file to the tax office by the deadline, penalties will be imposed.

# Japan TP Documentation (3)

## 3. Local file:


- Reporting Entity: A Corporation that has transactions with foreign related parties
- Excluded Transactions: Transactions that meet both following conditions
  - I. Total transaction amount with that foreign related parties for the prior fiscal year is **less than JPY 5 billion**.
  - II. Total transaction amount for intangibles with that foreign related parties for the prior fiscal year is **less than JPY 300 million**.

A Japanese corporation that does not meet the prescribed thresholds for filing the local file is nonetheless required to provide support for its transfer prices to the Japanese tax authorities within 60 days, or possibly be subject to the same presumed transfer pricing methods.

- Items to be Reported: Documents necessary for calculating the arm's length price of transactions with foreign related parties (specified in the Law and Annex II of OECD Guidelines)
- Submission Method and Due Date of Filing : Local file must be submitted to the tax authorities within the 45 days of a request and **must be prepared by the reporting entity's tax return filing date**.
- Timing of Application: Fiscal years of the reporting entity beginning on or after 1 April 2017
- Presumptive assessment/ Secret comparable : If a reporting entity fails to file the local file, the tax authorities can make an assessment presumptively and can use secret comparables.

# Singapore



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- Singapore became a BEPS Associate in June 2016
  - The Inland Revenue Authority of Singapore issued the e-Tax Guidelines on CbC Reporting
  - Trend is towards more of transfer pricing consultations

What to do now

# Supply chain structures: Contractual Arrangements

- Appropriate analysis of intercompany transactions includes delineation of:
  - Contractual terms
  - Functions, assets, and risks
  - Characteristics of property and services
  - Economic circumstances
  - Business strategies
- Contractual terms only as a starting point where the combined view will "provide evidence of the actual conduct of the associated enterprises"

# Reconsidering your Asian structures in the light of BEPS

- What recourse do taxpayers have?
  - Forced to restructure their supply chain?
  - Practical difficulties to change global supply chain
  - Seek relief from competent authorities?

# What To Do Now?

- Review existing structure & supporting documentation
  - Substance and value creation
    - IP ownership and development – where are the key DEMPE functions occurring?
    - Risk management and control – does management function align with ultimate bearing of key risks?
    - Are risk profiles and entity characterization aligned?
- CbCR
  - What will it look like? Does it align with substance and value creation?
  - Do you have adequate supporting documentation?
- Master file and local file
  - Do the documented facts support the characterizations and profit allocation?
    - **D**evelopment
    - **E**nhancement
    - **M**aintenance
    - **P**rotection
    - **E**xploitation

# What To Do Now?

- Design/Implementation of new structure
  - Build a robust structure with consideration of future-state documentation and CbCR
  - Intercompany contracts should clearly define risk bearing, and align with actual economic activity
  - Location of Principal with view to recent EU state aid cases, as well as BEPS
  - Even greater need for business purpose and support – difficulties if structure is not aligned with actual economic activity

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