



Is the Company in China required to submit transfer pricing contemporaneous documentation before or by June 30, 2020?

A Talk with Client

We were recently asked by one of our clients: “We are a processing and trading enterprise established in China for more than 10 years. In 2019, the total of purchase and sale transaction with related parties is CNY0.3 billion; In addition, the overseas headquarter company provided the technology supporting service to us which is amounted to CNY40 millions. Do we need to prepare the transfer pricing contemporaneous documentation for 2019? The answer is “Yes”.

If an enterprise fulfills one of the following requirements, it is exempted from submitting transfer pricing contemporaneous documentation (“TP Documentation Exemption”):

- The annual amount of related purchase and sale is less than CNY200 million and the amount of other related transactions is less than CNY40 million. The above amounts do not include the amount of related party transactions involved in the implementation of cost sharing agreement or advance pricing arrangement within the year (*Note: The processing business with supplied*



materials is calculated based on annual import and export customs declaration price; the related financing funds are calculated based on the amount of interest collection and payment).

- Related party transactions belong to the scope involved in the implementation of Advance Pricing Arrangements (“APA”);
- The shares owned by its foreign related party are less than 50% and the enterprise only has related party transactions domestically.

Obviously, the client does not fulfill any requirement of listed above so transfer pricing documentation (local file) is a must for year 2019.

What’s TP and Frequently Asked Questions?

Transfer pricing is the rates or prices that are used when selling goods and services between a parent company and a subsidiary in different tax jurisdictions. It can manage profit and loss ratios within the whole group and shift the profits in a jurisdiction with low profit tax rate so as to achieve overall tax efficiencies in the group.

With global business operation is getting more and more complicated, governmental supervision environment become increasingly stringent. You have to stay compliance with the most up-to-date transfer pricing regulations. Here are some leading questions that you may think about potential transfer pricing



risks.

Q1: Upon the request by in-charge tax bureau, you shall provide a transfer pricing documentation within 30 days. What should you do?

A1: Normally speaking, local file and special issue file should be submitted before or by June 30 of the following year in case the Company's annual related party transaction amount exceeds the legislative threshold. However, the in-charge tax bureau may question the Company when they find that it receives a relatively small portion of the overall profits in the supply chain. In this case, we would recommend completing a new transfer pricing documentation. This is helpful to identify whether or not the profit rate falls within the arm's length range.

Q2: The parent company prepared the transfer pricing master file, whether or not it is applicable to the Company in China? Do you need to prepare a new one?

A2: Having the transfer pricing master file prepared for the parent company does not mean that the Company in China must prepare a local file accordingly unless the TP Documentation Exemption cannot be satisfied or upon the in-charge tax bureau's special request.

Q3: The Company in China has huge volumes of related party transactions with



overseas entities during the year. Is there a risk associated with such transactions?

A3: In order to secure the potential TP risk and validate those related party transactions are rational, the Company in China could engage an experienced firm to proceed a benchmarking study.

Q4: The in-charge tax bureau challenged on the transfer pricing method currently adopted by the Company in China. What should you do?

A4: You need to ask for an experienced firm since they will be more familiar on how to deal with these arguments. They could make an analysis base on the current one and indicate the potential transfer pricing issues in the process.

What's the Latest Updates on Transfer Pricing?

The recent update is about the OECD's final paper on the transfer pricing aspects of financial transaction has been announced in February 2020. It reflects a tax enforcement trend to financial transactions of not only non-financial institutions but financial institutions (i.e. banks and insurance companies). It requires to analyze the loan transaction of related parties, transfer pricing analysis of financial center, cash pooling and guarantees transaction from bilateral perspective.



For more information, contact:

Mrs. Eva Tian

Chung Rui Tax Group Co., Ltd.

E: eva.tian@crtax.com

T: +86 21 18621810863

Date: March 2020