China
Transfer Pricing Guide 2024

wts global

China

1. Legal Basis

Is there a legal requirement to prepare TP documentation?

Yes.

Since when does a TP documentation requirement exist in your country?

2009.

Adoption of the OECD or UN legislation in your country?

No. the State Administration of Taxation ("**SAT**") has referenced in their legislation both the OECD Guidelines and the UN Practical Manual on Transfer Pricing for Developing Jurisdictions.

Is your country a member of the OECD, Inclusive Framework, or other OECD groups (e.g. BEPS)?

No.

Are TP policies of multinational enterprises in principle accepted by the tax authorities, if they are in line with the OECD TP Guidelines?

China SAT has issued some of China's specific regulations on TP policies, referring to the OECD TP Guidelines. Minor differences may exist between the China regulations and MNE TP policies.

Which TP methods may be applied?

The five OECD TP methods (Comparable Uncontrolled Price (**"CUP"**); Resale Price method (**"RPM"**); Cost Plus method (**"CPM"**), Profit Split (**"PS"**); and Transaction Net Margin Method (**"TNMM"**)) are applied in China.

Practically, there are other methods like the asset appraisal method, which is generally applied to define a fair market value, and the CUP is used.

Is there a stated preference for any particular TP methods?

The most appropriate method should be used.

Have the documentation requirements of OECD BEPS Action 13 already been implemented (i.e. the LF, MF and CbCR concepts)?

Yes, BEPS Action 13 (requiring preparation of a LF, MF and CbCR) has been implemented.

Reference to documentation and statements of local-government or tax authorities regarding OECD BEPS implementation status

LF: Article 13 of SAT Announcement [2016] No. 42.
MF: article 11 of SAT Announcement [2016] No. 42. CbCR: article 5 of SAT Announcement [2016] No. 42.

Is there any statute of limitation period?

10 years.

Reference to relevant articles of law, legislative regulation or applicable administrative guidance that are in place for TP documentation in general.

In addition to those mentioned above, there are other regulations regarding TP, as follows:

- Chapter 6 of Corporate Income Tax and Implementation (special tax adjustment);
- SAT Announcement [2017] No. 6 (special tax adjustment);

- SAT Announcement [2016] No. 64 (APAs); and
- Chapter 7 (cost sharing agreement), chapter 8 (controlled foreign enterprise), chapter 9 (thin capitalisation), chapter 10 (general anti avoidance) of Guoshuifa [2009] No.2.

2. Master File (MF)

What is the (consolidated revenue) threshold requirement for the obligation to prepare a MF?

(I) Cross-border related party transactions have occurred in the year, and the ultimate holding enterprise which consolidates tested company's financial report already prepared the MF; or

(II) The total amount of the related party transactions in the year exceeds RMB 1 billion.

Euro Equivalent

EUR 128,730,000.

From which year does this obligation exist?

Following the year that the threshold is met (so that the MF is prepared for the year in which the threshold was met or exceeded).

Applies for fiscal years starting from 2016.

When does the MF need to be available?

The MFs shall be completed within 12 months from the end of accounting year of the ultimate holding enterprise of the whole business group. The MF shall be maintained on a contemporaneous basis.

When does it need to be submitted?

The MFs shall be submitted within 30 days upon request by the tax authority.

Does the MF have to be prepared in the relevant local language?

Yes. TP documentations should be prepared in Chinese.

Is documentation in English permissible?

No.

What are the possible consequences of not having the MF available?

Penalties?

Yes, different levels of fines, ranging from less than CNY 10,000 to CNY 50,000.

Imprisonment?

No.

Shifting of the burden of proof?

No.

Other?

No.

To what extent do the local rules differ from the OECD standard regarding the OECD content requirements for the MF as shown in the BEPS implementation overview chart?

Most consistent with OECD requirements. In addition, China requires the provision of the following items:

- Industry structure adjustment, and shifting of enterprise functions, risks or assets within the group, which occurred in the accounting year;
- The main functions, risks, assets and personnel of main R&D organisation;
- The bilateral pre agreed pricing arrangement entered into by each member entity in the enterprise group;
- Name of the enterprise submitting the nationality report and its location.

3. Local File (LF)

What is the threshold requirement for the obligation to prepare a LF?

Enterprises whose amount of yearly related party transactions satisfy any one of the following criteria shall prepare LFs:

i. The amount of transfer of ownership of tangible assets (for processing of supplied materials, computed in accordance with the Customs declaration prices in the year) exceeds CNY 200 million;
ii. The amount of transfer of financial assets exceeds CNY 100 million;
iii. The amount of transfer of ownership of intangible assets exceeds CNY 100 million;
iv. The total amount of other related party transactions exceeds CNY 40 million; or
v. For enterprises with simple functions and limited risks and occurs continuous operating loss, even if it does not meet the threshold of LFs, the enterprise shall prepare the LF.

Euro Equivalent

EUR 12,873,000.

From which year does this obligation exist?

The LF is prepared for the year in which the threshold was met or exceeded. The LF shall be maintained on a contemporaneous basis.

When does the LF need to be available?

The LF shall be prepared before 30 June of the year following the year in which the related party transactions occur.

When does the LF need to be submitted?

The LF shall be submitted within 30 days upon request by the tax authorities.

Does the LF have to be prepared in the relevant local language?

Yes. TP documentation should be prepared in Chinese.

Or is documentation in English permissible?

No.

What are the possible consequences of not having the LF available?

Penalties?

Yes, there are different levels of fines, ranging from less than CNY 10,000 to CNY 50,000.

Imprisonment?

No.

Shifting of the burden of proof?

No.

Other?

Yes. For failure to submit TP Documentation to tax authorities (upon request) or for submitting false or incomplete information, a tax assessment (by way of a deemed profit rate) can also apply.

To what extent do local rules differ from the OECD standard regarding the OECD content requirements for the LF as shown in the 2017 OECD TP Guidelines?

Most consistent with OECD requirements. In addition, China requires to provide the following items:

- Value chain analysis;
- Foreign investment;
- Equity transfer by related parties;
- Factors that influence transaction pricing, including intangible assets involved in related party transactions and their impact, and special geographical factors such as cost savings, market premiums etc.;
- Pre agreed pricing arrangements entered into with the tax authorities of any country other than China and tax rulings made by the tax authorities of any country other than China, which are directly related to related party transactions of the enterprise; and
- Explanation of the contribution of the enterprise towards the group's overall profits or remaining profits.

4. Country-by-Country Reporting (CbCR)

What is the threshold requirement for the obligation to prepare Country-by-Country Reporting?

Resident enterprises which fall under any of the following, shall prepare a CbCR:

- The Ultimate Parent Entity (**"UPE"**) of the group, with revenue of CNY 5.5 billion or greater; and
- A Chinese subsidiary which is delegated by its UPE to submit the CbCR.

From which year does this CbCR obligation exist?

CbCR is prepared for the year in which the threshold was met or exceeded. It applies for fiscal years as of 2016.

Are Taxpayers required to notify of CbCR filing in your country?

Yes.

If yes, when and how do the tax authorities need to be notified?

The notification is to be filed together with the annual corporate income tax return (due 31 May), if a Chinese company meet the criteria for the CbCR filing. It is possible to apply for an extension.

For fiscal years starting in 2016. It should submit the CbCR simultaneously and notify the reporting entity.

If the reporting entity (ultimate parent or surrogate parent) is in your country, what is the CbCR submission deadline?

Before 31 May of the year following the year in which the entity has such obligation.

Are there any deviating submission deadlines for the secondary mechanism?

Yes.

OECD: CbCR filed no later than 12 months after the last day of the reporting fiscal year of the MNE group.

China: Before 31 May of the year following the year in which the entity has such obligation.

Does your country have a requirement that the financial figures of the group need to be aligned with?

No practical guidance issued to date.

Does your country have a requirement that the financial years of the group need to be aligned with?

No.

Where is the CbCR to be submitted?

CbCR should be submitted to the tax authority in charge, together with the annual CIT tax return.

How is the CbCR to be submitted, specifically, is there any prescribed standard?

The CbCR report is submitted in the annual CIT filing via the e-tax system.

What are the possible consequences of not having the CbCR available?

Penalties?

Yes, different levels of fines, ranging from less than CNY 10,000 to CNY 50,000.

Imprisonment?

No.

Shifting of the burden of proof?

No.

Other?

No.

To what extent do your local rules differ from the OECD standard regarding the content requirements for the CbCR as shown in the 2017 OECD TP Guidelines?

The threshold for CbCR is EUR 750 million according to OECD, whereas CNY 5.5 billion according to China's regulation.

Did your country sign the Multilateral Competent Authority Agreement on the Exchange of CbCR ("CbCR MCAA")?

Yes.

Did your country enter into other information exchange agreements, such as on a bilateral basis?

Yes.

Can a Taxpayer in your country fulfil his CbCR requirement by referring to the reporting entity in the same or another country?

No.

5. TP disclosure in tax return or TP specific returns

Is there a threshold for Related Party Transactions?

No.

Does a Taxpayer need to disclose information regarding TP documentation in his tax return?

Yes. Related Party Transaction Form delivered in the annual CIT filings indicates TPD prepared or not.

When a Taxpayer files a tax return for which he understands or should understand that the result reported in that tax return is too low due to incorrect TP, what could be the legal consequences?

The tax authorities have the right to determine the taxable amount of income and impose a penalty pursuant to the law.

What could be the consequences for the tax advisor/accountant/administrator drafting and filing the tax return of a client where that advisor/accountant/administrator understands or should understand that the result reported is too low due to incorrect TP?

No practical guidance so far.

Does a Taxpayer need to file TP specific returns?

Yes.

Please state the filing form number and name.

Related Party Transaction Form (22 forms).

What would be the filing deadline?

Before 31 May of the year following the year in which the related party transactions occur.

What would be the penalties for non-compliance?

Penalties (no more than CNY 10,000) should be imposed if the required tax return is not available.

6. Benchmarking

Is there any local guidance or requirement with regard to the preparation of a benchmark study?

Yes. Article 14(4) of SAT Announcement [2016] No. 42 regulates comparable analysis should include the following factors:

- Factors taken into consideration in comparability analysis, including the characteristics of transaction assets or services, functions, risks and assets of the transaction parties, contract clauses, economic environment, business strategies etc.;
- The relevant information on functions performed, risks borne, and assets used by comparable enterprises;
- Method for searching, information source, selection criteria and reason for comparable targets;

› Selected internal or external comparable uncontrolled transaction information, and financial information of comparable enterprises; and
› Adjustment of variance in comparable data and the reason.

Is there any stated preference for local benchmarks?

No clear rulings.

Are there any materiality thresholds that apply to the requirement to have a benchmark study available?

No.

7. Year-end, secondary, and corresponding adjustments

Are year-end/ secondary/ corresponding adjustments permissible?

There are no clear rulings about the year-end adjustment. China's customs rules and foreign exchange policies could cause issues in the implementation of the year-end adjustment.

Does the Taxpayer have to comply with any specific features or guidance?

No.

8. TP Audit and Dispute Resolution Mechanisms

What are currently the main TP areas of scrutiny by the tax authorities in your country?

Tax authorities usually focus on enterprises with the following risk characteristics:

i. Involves related party transactions with a large transaction amount or varied types of related party transactions;
ii. incurs long term losses, low profits or non-linear profits;
iii. profit is lower than the industry's level;
iv. the profit level does not match the functional risks borne, or the earnings shared do not match the costs shared;
v. carries out related party transactions with related parties located at low tax countries (regions);
vi. fails to declare related party transactions or prepare contemporaneous documentation under the provisions;
vii. the ratios of debt investments and equity investments accepted from the related parties exceed the stipulated standards;
viii. an enterprise controlled by a resident enterprise or by a resident enterprise and a Chinese resident which is established in a country (region) with an actual tax burden lower than 12.5% does not distribute profit or reduces profit distribution and such non-distribution or reduced distribution is not due to reasonable business needs; or
ix. implements other tax planning or arrangements that do not have a reasonable business objective.

Based on your experience, are joint or multilateral audits initiated and carried out?

Yes.

Does the Taxpayer have the option to apply for bilateral or multilateral APAs?

Yes.

Are there any restrictions?

An enterprise whose related party transactions exceed CNY 40 million for 3 consecutive years has the opportunity to apply for APA.

Under any of the following circumstances, the tax authorities may decline the APA application:

a) the tax authorities have implemented case investigation for special tax adjustment on the enterprise or other tax related case investigation, and it is yet to be closed;
b) the enterprise has not completed and submitted a report on annual related party transactions under the relevant provisions;
c) the enterprise has not prepared and given contemporaneous documentation under the relevant provisions; or
d) the tax authorities and the enterprise are unable to arrive at a consensus during the preparatory meeting phase.

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