

China Tax Alert

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China Activates More Country-by-Country Report Exchange Relationships, Outbound MNE's Compliance Burden Will Be Alleviated

Regulations discussed in this issue:

OECD BEPS Action 13 finalized in October 2015

Announcement on Matters Regarding Refining the Filing of Related Party Transactions and Administration of Contemporaneous Transfer Pricing Documentation ("Announcement 42")

Announcement on Administrative Measures of Special Tax Investigation and Adjustment and Mutual Agreement Procedures ("Announcement 6")

On November 9, 2018, OECD published the latest country-by-country (CBC) reporting implementation and activated exchange relationships. China has activated CbC report exchange relationships with 44 countries. The action is an expansion of China's current exchange relationship with the U.K., France, and Germany, and indicates China's commitment to fully participate in the OECD Base Erosion and Profit Shifting (BEPS) Action Plan, and to fulfil the minimum standards of the BEPS Action Plan. For Chinese outbound multinational enterprises (MNEs), the expanded CBC report exchange network means that more companies will not need to perform CBC report local filings. This will alleviate MNEs' burden for their global tax compliance management.

Background

The BEPS Action Plan initiated by the OECD and G20 countries in 2013 recognized that enhancing transparency for tax administrations and providing them with adequate information to assess high-level transfer pricing and tax risks is a crucial aspect of tackling BEPS issues.

The BEPS Action 13 provides a CBC report template for MNEs to report their annual business operating information by each tax jurisdiction in which they do business. The information includes revenue, profit, taxation, personnel, assets, etc. 47 jurisdictions that are members of the Inclusive Framework have introduced the CbC reporting obligation for fiscal years commencing in 2016. Currently, around 70 Inclusive Framework jurisdictions have introduced or taken actions to introduce the CbC reporting obligation.

The obligation to exchange CBC reports is one of the four BEPS minimum standards, which all members of the Inclusive Framework are required to fulfil. The implementation of CBC report exchanges between tax jurisdictions may be made based on the following three models:

- 1 Multilateral Convention on Administrative Assistance in Tax Matters (MCAA), including the Multilateral Competent Authority Agreement for Country by Country Reporting (CBC MCAA);
- 2 Bilateral tax conventions to prevent double taxation; and
- 3 Tax Information Exchange Agreements (TIEAs).

As of November 2018, there are over 1,900 bilateral exchange relationships activated with respect to jurisdictions committed to exchanging CbC reports, and the first automatic exchanges of CbC reports took place in June 2018. These include exchanges between the 74 signatories to the CbC MCAA, between EU Member States under EU Council Directive 2016/881/EU and between signatories to bilateral competent authority agreements for exchanges under Double Tax Conventions or TIEAs, including 40 bilateral agreements with the United States.

Since the Action 13 Report was released, jurisdictions have made great efforts to introduce the necessary domestic legislation, establish information exchange platforms and other administrative frameworks for the filing and exchange of CbC reports in accordance with the Action 13 minimum standards. Jurisdictions continue to negotiate arrangements for the exchange of CbC reports. The OECD publish regular updates to provide clarity for MNE Groups and tax administrations.

Currently China has activated CbC report exchange relationships with 44 countries, including Argentina, Australia, Austria, Belgium, Brazil, Bulgaria, Canada, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, India, Indonesia, Ireland, Italy, Japan, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Romania, Russia, Singapore, Slovak Republic, Slovenia, South Africa, South Korea, Spain, Sweden, Switzerland, and United Kingdom. Among the above countries, Cyprus and Romania are non-reciprocal jurisdictions, i.e. they have committed to send the CBC reports to China but will not receive CBC reports from China. China is expected to exchange CbC reports in 2019 for taxable years beginning on or after 1 January 2017.

KPMG Observations:

Currently, there are 53 countries that require the submission of CBC reports locally. The expanded CBC report exchange network between China and other tax jurisdictions means that more companies will not need to submit the CBC reports locally. This will alleviate Chinese outbound MNEs' burden for their global tax compliance management. Enterprises should pay close attention to further updates on the CbC report exchange arrangements, and formulate effective CbC report filing strategies.

In the meantime, the more extensive CBC report exchange network means that more information will be exchanged with foreign tax jurisdictions. Many countries including China have integrated the CBC report information into the tax risk monitoring and management system, and we expect that this would lead to more risk assessments in the future. MNEs must treat their CbC reporting obligations with the utmost diligence and care, to ensure that the CbC reporting is a true and fair representation of the groups' financial positions and operations, and rigorously examine any potential risks that could be highlighted by their CbC data.

For existing risks, MNEs should take actions to mitigate such risks, including providing further support in transfer pricing documentation and/or considering refinement of the global operating structures and global transfer pricing policies, such as improving substance in weak spots, winding down non-compliant structures, restructuring certain transactions to bring them into compliance, etc. MNEs should regulate their corporate governance and manage their global transfer pricing risks by establishing arm's length transfer pricing policies. MNEs should also reasonably allocate the functions, risks, assets and personnel in each country, and align tax outcomes with value creation. In tax jurisdictions where high transfer pricing risks exist, MNEs may also consider advance pricing agreements (APA) and other bilateral/multilateral instruments to mitigate their transfer pricing risks.





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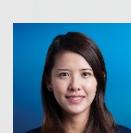
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