

China Tax Alert

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Signed BAPAs reach a record high, with applications from “going global” enterprises being prioritised

Executive Summary:

The <China Advance Pricing Agreement Annual Report (2023)> ("APA Report") highlights that from 2005 to 2023, the Chinese tax authorities have signed a total of 296 Advance Pricing Agreements (APAs). This includes 153 unilateral APAs and 143 bilateral APAs. In the year 2023 alone, they signed 36 APAs, out of which 9 were unilateral and 27 were bilateral. The number of signed APAs has steadily increased, with the number of bilateral ones reaching a record high in 2023. This trend demonstrates the active participation of Chinese tax authorities in international tax governance amid a climate of deepening international tax cooperation.

Background

On December 26, 2024, the State Taxation Administration ("STA") released the APA report in both Chinese and English. This is the 15th annual APA report released by the STA. The APA report systematically details the development history of the APA, the latest mechanisms, application procedures, statistical data, and implementation of APA in China, and contains the statistical data pertaining to the relevant period from 2005 to 2023.

Overview of the report

The number of signed APAs continued to increase, and the number of bilateral APAs reached a record high. In 2023, Chinese tax authorities signed 36 APAs, including 9 unilateral APAs and 27 bilateral APAs. Overall, the number of APAs signed was slightly higher than the number (34 cases) of the previous year, and the number of signed bilateral APAs reached a record high.

Bilateral APA applications continued to increase. Of the 27 bilateral APAs signed in 2023, 14 are new APAs and 13 are renewals. In 2023, there were a total of 60 bilateral APAs in the intention stage, increasing by 13 compared to that of 2022. This shows that in the current international and domestic tax environment, more cross-border taxpayers seek to obtain tax certainty through bilateral APAs.

High signing efficiency was maintained. In terms of the time required to conclude an APA, all 9 unilateral APAs signed in 2023 were concluded within 24 months. Among 27 bilateral APAs, 13 were concluded within 24 months, and 14 took more than 24 months to conclude. The completion of a bilateral APA depends on many factors, including but not limited to the quality of the enterprise's submission, the complexity of the case, the time of application submission and treaty partners' intention to push forward the APA.

Signed Bilateral APAs were mainly with Asian jurisdictions. Of the 143 bilateral APAs signed by Chinese tax authorities from 2005 to 2023, 99 were signed with other Asian countries (regions), accounting for about 70% of the total number of the signed bilateral APAs. Of the 27 bilateral APAs signed in 2023, 22 were concluded with other Asian countries (regions). It could hence be concluded that Asia is still the most concentrated region for STA to negotiate and sign bilateral APAs with.

The types of industries and related party transactions involved in APA were increasingly diversified. Of the 36 APA cases successfully signed in 2023, 28 involved the manufacturing industry, 6 involved the wholesale and retail industry, 1 involved the scientific research and technical services industry, and 1 involved other industries. From the perspective of the related party transaction types, there were 36 cases involving tangible asset transactions, 12 cases involving intangible assets transactions, 13 cases involving services transactions, and 1 case involving financing transactions. The types of industries and related party transactions involved in APA are increasingly diversified.

The transactional net margin method ("TNMM") was still the main transfer pricing method applied in APA. As of 2023, among the signed APAs, TNMM was the most frequently used method, being used 299 times and accounting for 83% of all the applied transfer pricing methods. Meanwhile, Chinese tax authorities have been exploring the use of other appropriate transfer pricing methods, especially in dealing with transactions where both transacted parties have made significant contributions to the value creation or location specific advantages such as market premium or cost savings have been present. Other transfer pricing methods have also been applied in the signed APA depending on the situations, where the cost-plus method ("CPM") has been used 21 times, the profit split method ("PSM") has been used 14 times, and the comparable uncontrolled price ("CUP") method has been used 10 times. Among the 36 APA cases successfully signed in 2023, TNMM was used 41 times, other methods were used 5 times, the CUP method was used twice, the resale price method ("RPM") was used once, and the PSM was used once.

KPMG observations

In the context of strengthening international tax and transfer pricing administration in various countries, more and more "bring in" and "going global" enterprises are applying for APAs to mitigate cross-border tax risks, obtain tax certainty, and effectively avoid or eliminate international double taxation. The speed of APA negotiation and signing has been increased and efficiency improved, providing guarantee for enterprises to deal with uncertainty.

- **To accelerate APA, enterprises need to pay attention to the quality of the submission.** By the end of 2023, China has 149 bilateral APAs in the intention or application stage, increasing by 4 compared with that of 2022. With the increase of APA inventory, to quickly promote the application and negotiation process, enterprises need to check the quality of the submitted documents, including whether the application documents are complete, whether the value chain analysis is clear, and whether the pricing principles and methods are reasonable. The APA report clearly states that if a submission that presents innovative application of transfer pricing methods or high-quality quantitative analysis for intangibles, cost savings or market premiums, it will merit the STA's prioritized attention. In addition, enterprises are suggested to actively communicate with the in-charge tax authorities and STA. For bilateral APAs, it is also suggested to strengthen communication with foreign tax authorities.
- **The APA application of China's "going global" enterprises are being prioritized.** Recently, some Chinese "going global" enterprises are facing transfer pricing challenges from tax authorities in Southeast Asia, Europe, and other regions. It is expected that more and more "going global" enterprises will be willing to resolve cross-border tax disputes by applying for APA in the future. China signed the first "going-global" bilateral APA with the United States in 2018 and the second one with New Zealand in 2020. At present, some "going global" enterprises are applying for APAs. The APA report clearly points out for the first time that the application of "going global" enterprises are being prioritized, which provides strong support for "going global" enterprises to protect their legitimate rights and interests and avoid double taxation through APA application.
- **Enterprises should evaluate the feasibility of APA renewal according to the actual situations.** With the increasing number of signed APAs, the renewal cases also showed an upward trend. Of the 27 bilateral APAs signed in 2023, nearly half (13 cases) are renewal cases. After the expiration of the APA, if there are no significant changes of the business environment, the operations, the types of related party transactions, the pricing methods, etc., the enterprises could obtain the tax certainty for a longer operating period through APA renewal procedure. It is worth noting that in practice, some enterprises have changes in their actual operations, and are hence difficult to implement the previous pricing mechanism. Those enterprises would then be advised to apply for new APAs.

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