

Introduction

- ▶ *2009 Global Transfer Pricing Survey*
 - ▶ Latest in Ernst & Young's suite of Transfer Pricing Surveys
 - ▶ First global survey was in 1997
- ▶ Fifty jurisdictions covered
 - ▶ A decade ago there were less than 20
 - ▶ Where possible, input based on interviews with tax authority representatives
- ▶ Current economic factors clearly impacting the transfer pricing landscape
 - ▶ Substantial losses, compressed margins, volatile results
- ▶ Bailouts and stimulus – straining public finances around the globe
 - ▶ Tax authorities seeking to protect their tax base; need to pay for the stimulus somehow

China

“From a China perspective, our observations indicate that we have firmly moved into the enforcement phase – the rules are now in place and there are no ambiguities. Taxpayers should be under no illusions that the authorities are now committed to compliance and enforcement.”

- ▶ The regulatory/enforcement tools are in place
 - ▶ Tax authorities are looking at various ways to enforce - national audits, examination, self-assessment, industry surveys, etc.
- ▶ We are observing increased coordination between authorities at the provincial level
- ▶ China is evolving its coordination and cooperation with global tax authority peers

Resourcing

- ▶ Countries with new regimes and rulings tend to “gear up” quickly
- ▶ Some countries aiming to establish specialist TP cells
- ▶ Other jurisdictions, including China, are broadening resource capabilities, increasing resources and focusing on training to increase yields
- ▶ MAP/APA resources anticipated to grow, as increasing demand from taxpayers for certain puts strain on the systems
 - ▶ China has seen a surge in APA applications, but is resource constrained

Industry focus

- ▶ Roughly half of jurisdictions, including China, identified and targeted specific industries
- ▶ Traditional and long time targets
 - ▶ Automotive
 - ▶ Consumer products/retailing
 - ▶ Oil and gas
 - ▶ Pharmaceuticals
 - ▶ Financial services

Geographic focus

- ▶ Tax havens and blacklisted jurisdictions squarely in the sights of tax authorities
- ▶ Number of countries with formal blacklists (or grey/white lists increasing)
 - ▶ World watching tax developments from the Obama administration with interest
- ▶ China monitoring transactions with taint of treaty shopping
- ▶ Major trading partners also often a focus
 - ▶ Germany, Japan, the United States and United Kingdom often make the top five list
 - ▶ China, somewhat surprisingly, yet to make an appearance in same but this is expected to change as Chinese operations come under audit

Transactions under scrutiny

- ▶ Clear divide between jurisdictions in this regard
 - ▶ Those rich in natural resources focus on transfers of tangible goods
 - ▶ Others focus firmly on service transactions and those involving intangibles
 - ▶ Triangular transactions also a focus for some jurisdictions
 - ▶ Goods manufacturing in jurisdiction A, sold to an overseas entity but “re-imported” for sale locally in jurisdiction A
- ▶ China, as a global supply point, has typically focused on goods, but this is changing as the new rules have equal emphasis on royalties, services, and financing

Penalties

- ▶ Overall, anticipated that the use of penalties will increase
 - ▶ Consistent with the need to protect the base and increase revenues
- ▶ China's penalties are interest geared
 - ▶ Penalty regime is new
- ▶ China has moved into enforcement phase
 - ▶ Taxpayers should be under no illusions that the authorities are now committed to compliance and enforcement

Audit triggers

- ▶ Most consistently cited trigger: “a sudden reduction in taxable profits”
 - ▶ If this continues to be the case, given the current economic conditions it will be a busy time for those from tax authorities involved in transfer pricing reviews
- ▶ Around half of the jurisdictions mentioned evidence of business restructurings as a trigger for transfer pricing audits
- ▶ Indirect tax reviews are also playing an increasing role
- ▶ China explicitly lists audit triggers (Guoshuifa [2009] 2, Article 29)
 - ▶ Enterprises which have significant amount of related party transactions or have various types of related party transactions
 - ▶ Enterprises with recurring loss, marginal profit or fluctuating profit
 - ▶ Enterprises whose profit level is lower than the level of the industry
 - ▶ Enterprises whose profit level obviously does not match with the functions undertaken and risks assumed
 - ▶ Enterprises which have transactions with related party registered in the tax haven
 - ▶ Enterprises which fail to make declaration on the related party transactions or prepare contemporaneous documentation
 - ▶ Enterprises which obviously do not comply with the arm's length principle

Thank you

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