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## INSIGHT: Advance Pricing Arrangement Series—Asia Pacific



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In the years following issuance of the Organization for Economic Cooperation and Development (OECD) action plan against base erosion and profit shifting (BEPS), KPMG has seen a significant increase in transfer pricing controversy and expects this trend to continue. Among the contributing factors are: the increase in the exchange of information between tax authorities, the growth in the number and qualification of tax auditors, tax authority aggressiveness, tax authorities' use of technology to identify transfer pricing risks and inconsistencies, developing tax laws and regulations, and public pressure on governments to increase revenues generated from corporate income taxes. As a result, more and more Advance Pricing Arrangement (APA) applications are being submitted across the Asia Pacific region.

This article focuses on the APA programs in Australia, China, Japan, New Zealand, Singapore, and Vietnam.

### HISTORICAL OVERVIEW

#### Australia

Australia was one of the first countries to adopt APAs, dating back to the early 1990s, and has continued to offer APAs as a mechanism to prevent tax disputes and gain certainty on transfer pricing. The Australian Taxation Office (ATO) has competent authority and APA teams that sit separately from case teams and are responsible for ensuring APAs are undertaken

objectively—recognizing the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD Guidelines).

The ATO has unilateral, bilateral, and multilateral APA programs that can be utilized by companies and branches to resolve issues and tackle complexity in transaction pricing. Bilateral and multilateral APAs are entered into in accordance with Australia's tax treaties while unilateral APAs fall under the ATO's general powers of administration. Often APAs have been used as a way to resolve disputes but, more recently, they are focused on the go-forward position after the back-period controversy issues have been resolved—for example, APAs that are agreed to after a mutual agreement procedure (MAP) resolution to an audit.

Recently, the APA program in Australia has gone through some changes in terms of process. The first major impact of this has been a desire on the part of the ATO to identify and tackle issues upfront in a rigorous early engagement process prior to formal acceptance into the APA program, such that subsequent APA steps operate smoothly. The second major impact is around transparency, in that the ATO requires an understanding of the upstream value chain, including location and tax profile of other group entities that are part of the flow of goods and services into and out of Australia. These changes were adopted by the ATO to better position the APA program in a post-BEPS world.

#### China

China's APA history can be traced back to the late 1990s, where the program was introduced on a trial basis. The Chinese APA program was then formally introduced in 2002 through the introduction of Article 53 of *The Implementation Rules of the Tax Collection and Administration Law of the People's Republic of China No. 362*.

It was not until the end of 2004 that China promulgated a further regulation which provides details of the APA program such as the application requirements, procedures (e.g. negotiation and conclusion procedures), and the follow-up execution and monitoring of the concluded APA. The details and procedures were further improved upon in 2009 and 2016.

The current APA administration requirements are laid out in the *Public Notice on Matters Regarding Enhancing the Administration of Advance Pricing Arrangements [2016] No. 64* (Announcement 64) where it sets out six stages in the Chinese APA process: (1) pre-filing meetings, (2) intention, (3) analysis and appraisal, (4) formal application, (5) negotiation and signing, and (6) supervision of implementation.

China concluded its first unilateral APA in 1998, and the first bilateral APA with Japan in 2005.

### Japan

The Japanese tax authority (“National Tax Agency” or “NTA”) lays claim to the invention of the APA program back in 1987, which was one year before the U.S. Internal Revenue Service launched its APA program. The program was initially called the “Pre-confirmation System,” but it was renamed to APA or “Advance Pricing Arrangement” after the IRS named its similar program as APA or “Advance Pricing Agreement.”

Although the program initially began as a unilateral procedure, the NTA currently encourages taxpayers to file bilateral rather than unilateral APAs. As a consequence, most APAs filed and concluded in Japan are bilateral.

### New Zealand

APAs are available to taxpayers in New Zealand, and the Inland Revenue is keen to see a greater number of taxpayers seeking APAs. The Inland Revenue has established its APA program under a broad framework using informal procedures and has stated it will not issue formal APA guidelines. The Inland Revenue considers that its flexible approach to APAs minimizes the possibility of the process becoming too bureaucratic and enhances the efficiency of its APA program.

The Inland Revenue concluded its first bilateral APA in 2001 with Australia. Since then, the Inland Revenue has concluded several other bilateral APAs with Belgium, Canada, Japan, Korea, Switzerland, and the U.S. The department is also party to multilateral APAs.

### Singapore

Over the past decade, Singapore has gradually developed its transfer pricing regime in all relevant areas, including its APA program. The Inland Revenue Authority of Singapore (IRAS) is aware that many taxpayers in Singapore transact with group companies that are subject to higher domestic tax rates and may face scrutiny by local tax authorities. As such, Singapore has estab-

lished a wide network of double taxation avoidance agreements (DTAAs), which provide Singapore taxpayers with the opportunity to proactively obtain upfront certainty on their transfer pricing arrangements via APAs.

The program is administered by the Tax Policy & International Tax Division within IRAS, which manages all competent authority matters for Singapore.

### Vietnam

The APA regulations were introduced in Vietnam in 2013 under Circular 201/2013/TT-BTC issued by the Ministry of Finance (MOF), which became effective from Feb. 5, 2014. However, following the new Tax Administration Law which will be effective from July 1, 2020, the MOF is going to issue a new APA Circular to provide clearer guidance on application procedures and responsibilities of competent authorities. In addition, the local transfer pricing regulations are also applicable in the preparation of the APA application dossiers.

## CURRENT STATISTICS

### Australia

According to the latest data available from the ATO’s website, 268 APA cases were completed during the most recent eight-year period spanning from June 30, 2012, to June 30, 2019. The number of completed APAs were almost evenly split between bilateral APAs (136 cases) and unilateral APAs (132 cases) with only one multilateral APA case being finalized (in the 2017-2018 income year).

Further, 148 out of 268 finalized APA cases (approximately 55%) represented requests for the renewal of existing APAs while the remaining 120 (approximately 45%) represented new APA cases.

The average time to conclude a unilateral APA has increased considerably during recent years. While unilateral APAs that were concluded during the income year 2013-2014 took around 11 months on average to conclude, unilateral APAs that were concluded during the income year 2018-2019 took around 23 months to conclude. The time to conclude bilateral APA cases has varied quite a bit with the average time to complete increasing from around 30 months in income year 2011-2012, to around 16 months in 2013-2014, to around 35 months in income year 2017-2018, and then back to around 32 months in 2018-2019. The only multilateral APA that was completed during the 2012 to 2018 period took around 61 months to complete from the date of submission.

Although the ATO has APAs with many trading partners, the largest concentration is with Japan. It is expected that APAs with Asian countries will grow as the region continues to develop, and trade flows with Australia continue to grow.



## China

According to the 2018 statistics published by the Chinese State Taxation Administration (STA), the STA has, since the formalization of the program in 2005, concluded and signed a total of 156 unilateral and bilateral APAs. The total of 156 unilateral and bilateral APAs are broken down as follows:

Year	Unilateral APAs	Bilateral APAs	Total
2005	13	1	14
2006	10	0	10
2007	7	3	10
2008	6	1	7
2009	5	7	12
2010	4	4	8
2011	8	4	12
(Renewals in 2011)	(4)	(0)	(4)
2012	3	9	12
(Renewals in 2012)	(1)	(6)	(7)
2013	11	8	19
(Renewals in 2013)	(0)	(4)	(4)
2014	3	6	9
(Renewals in 2014)	(1)	(0)	(1)
2015	6	6	12
(Renewals in 2015)	(0)	(2)	(2)
2016	8	6	14
(Renewals in 2016)	(0)	(2)	(2)
2017	3	5	8
(Renewals in 2017)	(0)	(3)	(3)
2018	2	7	9
(Renewals in 2018)	(1)	(1)	(2)
<b>Total</b>	<b>89</b>	<b>67</b>	<b>156</b>

Of the total APAs concluded between 2005 and 2018, an overwhelming majority of the APAs (approximately 85%) involved the manufacturing industry. This generally reflects the type of investment China historically received from inbound multinational enterprises, but as China's economy diversifies, it is expected that more APAs will be concluded involving other industries.

APAs involving the transfer of the right to use, or ownership of, tangible assets account for the largest portion of transactions covered by China's APA program, i.e., 65% of the total from 2005 to 2018; followed by APAs involving services at 20%; and APAs involving transfer of the right to use or ownership of intangibles at 15%. None of the APAs concluded involve financing or transfer of financial assets.

During the period between 2005 and 2018, China concluded a total of 44 bilateral APAs with Asian countries, the majority of which are with Japan and South Korea, 16 with European countries, and seven with North American countries.

There are many factors that may determine the speed and time taken to conclude an APA, such as the type of the requested APA, the complexity of the transactions involved, the quality of the documents provided by taxpayers, etc. A majority of the unilateral APAs (approximately 93%) and bilateral APAs (approximately 60%) signed between 2005 and 2018 were concluded within two years of application.

## Japan

According to the most recent data released by the NTA, 163 bilateral APAs were filed in the fiscal year ended (FYE) June 2019, while 146 bilateral APAs were concluded in the same FYE. The bilateral APAs resolved in FYE 2019 took an average of 34.5 months to be concluded (slightly more than those concluded in FYE 2018 with an average of 30.7 months). The bilateral cases filed in FYE 2019 remained stable from the previous FYE (166 bilateral APAs filed in FYE 2018), but the cases settled increased from the previous FYE (122 bilateral APAs concluded in FYE 2018). The same report also indicates that the NTA had 200 bilateral APAs under review, suspended or being negotiated with the APAC countries, while the NTA had 134 with the North American countries and 70 with European countries in FYE 2019.

## New Zealand

According to the public Inland Revenue Department website, as of June 30, 2019, 205 APAs were concluded.

New Zealand does not break the figures into the number of unilateral or bilateral APAs. Most of the bilateral APA work has been with Australia. New Zealand has also completed bilateral APAs with Belgium, Canada, Japan, Korea, Switzerland, and the U.S.

## Singapore

IRAS regularly publishes APA (and MAP) statistics such as the inventory of APA cases and average time for completion. Over the past five years, the inventory has remained constant at around 40 APA cases. More than 60 APAs have been completed since 2014 and out of these, more than 60% were completed within two years. IRAS does not publish the counter jurisdictions for the APAs, but based on our experience most of the APAs have been with Japan and Korea, two of Singapore's major trading partners.

## Vietnam

Since the beginning of the APA program in 2014, 10 different multinational corporate groups applied for APAs, for a total of 24 companies in Vietnam. The majority of the cases are in the initial stages (i.e. pre-filing consultation or official application). There are some cases that are in the negotiation stage with the Vietnamese competent authority, i.e. the General Department of Taxation (GDT). So far only one case has completed the negotiation with the GDT, however, this case is still under the review of the Ministry of Finance and the Government.

## RECENT DEVELOPMENTS

### Australia

Due to growing worldwide attention to international tax and transfer pricing matters, multinational groups with total business income of AU\$250 million (\$162 million) or more continue to show an interest in considering whether to pursue an APA in Australia. As per the recent statistics available from the ATO, there are over 200 APAs in place or under request, and of this around 75% are for larger companies.

To address the continuing demand for APAs and for the purpose of introducing efficiency and minimizing the duplication of effort, since July 2018 the ATO has started to coordinate its APA program with its streamlined assurance review program (commonly referred to as the Top 1000 Tax Performance program). A Top 1000 review looks broadly at tax governance and holistically at all major tax risks for multinational groups with total business income of more than AUD 250 million.

Coordination is achieved through aligning the timing of Top 1000 reviews with activities under the APA Program that have regard to the situation and circumstances that apply to each taxpayer, including the following pathways (if a company already has an APA in place, then the top 1000 review will exclude transactions covered under the APA):

Situation for Top 1000 company	Pathway ATO may seek
Approach ATO to enter into an APA	Align the timing of the Top 1000 review with the APA early engagement stage
Currently in APA negotiations	Align the timing of the Top 1000 review with the APA negotiations
End of the APA negotiation stage and contemplating signing the APA	Align the timing of the Top 1000 review with the first APA annual compliance report.

### China

The progress made in the last few years on the APA program is in line with the STA's commitment to preventing double taxation and providing certainty to taxpayers. There was a significant increase in STA resources for APA and MAP work in the last couple of years, which means that more Chinese and foreign multinational taxpayer APA/MAP arrangements are expected to be facilitated, going forward.

For example, the STA set up a third APA/MAP division in 2016, to assist divisions 1 and 2 which primarily handle MAP and APA cases. Previously, STA resources for these matters were stretched, due to the commitment of relevant personnel to BEPS meetings from 2013 to early 2016.

As a result of the above, we are aware that the STA's focus is gradually shifting towards accepting applications involving more complex transactions (such as transactions involving intangibles). Accepting more complex applications provides the STA the opportunity to explore the less frequently used but more complex transfer pricing methods such as the profit split method.

Additionally, in line with the globally agreed measures, the STA generally aims to complete the review

and negotiation process within 12 months for unilateral APAs and within 24 months for bilateral APAs. Bilateral APAs involve negotiations with relevant competent authorities and therefore more time is required to reach a consensus on them than that of unilateral APAs. The 24-month timeline to resolve bilateral APAs is in line with the timeline set out in the BEPS Action 14 report for the resolution of MAP cases.

### Japan

The Japanese APA guidelines were revised in 2018. Under the revised guidelines, the authorities may suspend the review procedure when filing is not officially accepted by the counterpart country. In addition, a taxpayer may be asked to withdraw from the process after three years from submission in Japan, when the filing is not accepted by the counterpart country.

The revised guidelines state that a taxpayer must provide information within 45 days upon request during the process. The authority also made it clear in the revised guidelines that filing a rollback does not technically stop the authority from carrying out tax audits.

### New Zealand

The Inland Revenue Department is encouraging taxpayers to seek unilateral and bilateral APAs. The tax authority believes it is better for taxpayers to obtain APAs than run the risk of potentially costly and time-consuming transfer pricing audits. APAs encourage upfront taxpayer compliance and early resolution of potential disputes. Its view is that given the subjective nature of transfer pricing, APAs are the best way for taxpayers to achieve certainty.

The department further states in its publications that although unilateral APAs are one-sided, should double taxation arise on transactions covered by a unilateral APA, it will enter into competent authority negotiations with the other jurisdiction on the basis of the unilateral APA position. Unilateral APAs are especially viable where the amounts at stake are small and/or where most of the transfer pricing risk lies in New Zealand.

Domestic legislation allows a unilateral APA to be issued in the form of a binding ruling, and bilateral/multilateral APAs may be entered into in accordance with New Zealand's double-tax treaties.

The Inland Revenue aims to complete bilateral APAs with Australia and all unilateral APAs within six months of the date of acceptance of a formal application. Negotiations with tax authorities beyond Australia generally take considerably longer to resolve. The Inland Revenue Department has concluded 180 APAs for the year ending June 30, 2018, and is currently negotiating a number of others.



## Singapore

India and Singapore have recently amended the DTAA to include Article 9(2) within the provisions of the DTAA. This amendment was effective from April 1, 2017 (i.e. FY 2017-18) and has opened the door for multinational enterprises to settle transfer pricing-related disputes by applying for a bilateral APA.

Given India's growing importance in the region and as a trading partner for Singapore, we have experienced an increasing interest in APAs by taxpayers with operations in India. We expect this trend to continue as the bilateral relationship between the two countries continues to grow.

## Vietnam

Similar to other developing countries, the APA program in Vietnam is still in its infancy stage, i.e., the GDT APA working team is still expanding its resources and technical expertise. Currently, the APA program is undergoing a reorganization with the aim of increasing transparency and streamlining the APA process for both tax officials and taxpayers. Such developments have caused certain delays in the processing of APA applications. At this stage, the MOF and GDT have been deferring the APA program until the new APA Circular will be issued to provide clear guidance on procedures and responsibilities of competent authorities.

After the reorganization, however, we anticipate an influx of new APA applications, which the GDT would not be able to process all at once given their limited resources (i.e., resulting in a backlog of applications). Thus, the GDT will continue to process APA applications on a first-come basis. Therefore, we highly recommend that taxpayers lodge their APA applications, as soon as possible after the new APA Circular will be effective, to ensure their application will be prioritized for processing after the APA program resumes in full speed after the reorganization (i.e., avoid the application being in the backlog/bottleneck).

## KEY TAKEAWAYS

### Australia

Australia has an advanced APA program that is well resourced and has clearly defined upfront expectations around how the program will operate and the requirements the company is signing up for in terms of information and disclosures. However, entry into the APA program brings a range of expectations with it and these need to be considered carefully.

At the end of the day, complex transfer pricing just grows over time, so if you can get the APA process to work for you in Australia, the rewards are there.

### China

The latest developments in the STA, in particular with the availability of more resources for APA and MAP work, will likely see the STA providing greater support in facilitating more Chinese and foreign multinational taxpayers' APA/MAP arrangements in a more effective and expeditious manner going forward.

Taxpayers who are interested in applying for an APA in China should note that the APA applications are dealt with on a first-come, first-served basis. Therefore, taxpayers should make early preparations and get a head start if interested in an APA.

The quality of the submission package matters. The package should include all required documents for submission and the documents should contain clear explanation of transactions throughout the entire value chain. The STA will likely prioritize applications that present innovative application of transfer pricing methods or high-quality analysis for intangibles, cost savings, and/or market premium. Further, the proposed transfer pricing policy and methodology ought to be reasonable and justifiable.

Other factors that will be important for the STA to consider are: (1) whether the applicant is in a specific industry or located in a specific region that merits prioritized attention; and (2) for a bilateral APA request, whether the bilateral APA partner country (or region) has the intention to accept the case and pursue the bilateral APA.

## Japan

The Japanese APA guidelines were revised in 2018 to liberate the authorities from some of the burdens for them to carry out the program, given filings are continuously increasing. Although the Japanese authorities work rather efficiently to process the numerous new submissions that they receive every year, the taxpayers filing APAs sometimes had to wait several months before the process actually started.

It should be noted that the guidelines were revised also to prevent some of the multinational taxpayers from abusing the program. The Japanese authorities believe that some multinational taxpayers have abused the program for profit-shifting purposes. A taxpayer filing an APA should be able to clearly explain the background and purpose of its submission to avoid any misunderstandings by the tax authorities.

## New Zealand

Our experience with the Inland Revenue Department in relation to APAs has been positive. We believe this is attributable to the agency's informal approach to APAs and its pragmatic view on commercial realism.

## Singapore

Singapore's APA program is well-established, and IRAS has the capability and resources to administer them efficiently. It remains an important option for multinational companies to address potential transfer pricing issues upfront, and APAs are encouraged by IRAS which has a preference for bilateral APAs. Taxpayers considering this option should be aware that IRAS expects full cooperation on sharing of information and timeliness. This can be a challenge if the other tax authority works towards a different timeline and requires careful planning and alignment. We expect a growing number of APAs to be concluded going forward, in particular between Singapore and India.

## Vietnam

Taxpayers have to wait until the new APA Circular will be issued and the APA program will be resumed by

the competent authorities to lodge their APA applications. We expect that APAs will be concluded and signed by the competent authorities after issuance of the new APA Circular.

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