Income Adjustments for Cross-Border Bilateral or Multilateral Advance Pricing Arrangements

In line with international tax trends, a new decree announced by the Ministry of Finance of Chinese Taipei grants flexibility for income adjustments for cross-border bilateral or multilateral advance pricing arrangements.

1. The Decree

On 24 June 2021, the Ministry of Finance (MoF) of Chinese Taipei issued a decree (Tai Tsai Ji No. 11024508100) that grants flexibility for income adjustments for cross-border bilateral or multilateral advance pricing arrangements (BAPAs). The decree stipulates that when the tax authorities of Chinese Taipei negotiate cross-border BAPAs with the competent authorities of its treaty partners, both authorities may determine the method for examining whether the controlled transactions fall within the arm’s length range. They can either adopt the results of the controlled transactions on a year-by-year basis or use the average results of the controlled transactions in the covered years as a whole. In cases in which the results of the controlled transactions do not fall within the arm’s length range, either an upward or a downward adjustment should be made to the income of the enterprise at an agreed point within the arm’s length range. Moreover, this adjustment can either be calculated and made separately to the income of the enterprise on a year-by-year basis or be aggregated as a sum and made on a one-time basis to the last year covered in the BAPA.

The decree grants flexibility to the tax authorities of Chinese Taipei to conclude BAPAs with the competent authorities of its treaty partners and provides more certainty with regard to the transfer pricing adjustment practice under BAPAs. It may safeguard taxpayers’ rights, provide more flexibility for taxpayers’ operations to comply with the agreed BAPA results, fulfill the core spirit of eliminating double taxation endorsed in income tax agreements and comply with the principles indicated in the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations published by the Organization for Economic Co-operation and Development.

The MoF illustrated this by means of an example: Company A is an enterprise resident in Chinese Taipei, and its affiliated enterprise, Company B, is an enterprise resident in Country B. Company A and Company B applied to the competent authorities of Chinese Taipei and Country B, respectively, for a BAPA that covers the controlled transactions for the years 2021-2025. In ordinary situations, the tax authorities of Chinese Taipei may negotiate with the competent authority of Country B and conclude terms, such as taking Company A as the tested party, using a comparable-profit method (the transactional net margin method) with the operating net profit margin as the profit-level indicator and setting the arm’s length range between 3% and 8%. According to the decree, the tax authorities of Chinese Taipei may additionally agree on the following matters:

- **The method for examining whether the results of the controlled transactions are in line with the BAPA**: Whether the operating net profit margin of Company A falls within the aforementioned arm’s length range (3% to 8%) could be determined either by checking the margin for each year from 2021 to 2025 or by checking the simple average of the margin for those 5 years.

- **The extent of adjustment when the results of the controlled transactions are not within the arm’s length range**: Either an upward or a downward adjustment should be made to Company A’s income at the point closest to the range (i.e. 3% or 8%) or at any other point within the range.

- **The methods of adjustment when the results of the controlled transactions are not within the arm’s length range**: The amount of the adjustments made to Company A’s income could either be calculated and made separately for each year from 2021 to 2025 or be aggregated and made on a one-time basis for the year 2025.

2. Conclusion

In conclusion, issues related to transfer pricing and the avoidance of double taxation are now among the most challenging topics for enterprises’ international tax management. Multinational enterprise groups may want to consider applying for BAPAs in order to avoid double taxation arising from transfer pricing, as both of the competent tax authorities involved can conclude arm’s length results with appropriate conditions for multinational enterprise groups’ controlled transactions within a given period. Accordingly, BAPAs may improve taxation certainty, prevent disputes, avoid double taxation on income and be used by multinational enterprise groups as vehicles for enhancing their overall tax management.

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