Are you ready for FY2014/15 transfer pricing compliance?

The tax authorities, led by the Ministry of Finance and the General Department of Taxation, having been enforcing the transfer pricing regulations actively, including enquiring into transparency of taxpayers’ related party transactions and audits. Taxpayers are now required to provide more information about their related party dealings and their compliance with the arm’s length principle as defined in the transfer pricing regulations by maintaining contemporaneous transfer pricing documentation.

Form 03-7 for declaration of related party transactions

Pursuant to Circular 156/2013/TB-TCT issued by the Ministry of Finance on 6 November 2013, Form 03-7/TNDN ("Form 03-7") is applied for taxpayers’ disclosures of related party dealings for the tax period beginning 1 January 2014 onwards. The new Form 03-7 replaces Form GCN-01/QLT ("Form 01") issued under Circular 66/2010/TB-TCT providing transfer pricing regulations in Vietnam ("Circular 66"). Under Circular 66, taxpayers have obligations to declare the related party transactions correctly and sufficiently, failing which they may be subject to the local tax authority’s assessment or adjustment of transfer prices or profits for tax purposes. Generally, a transfer pricing assessment and adjustment will result in a higher amount of tax payable.

Form 03-7 (enclosed) requires taxpayers to:

- Self-assess the arm’s length value (commonly called ‘market value’) of their related party transactions and disclose the reassessed amounts based on market value in Column 4 (for revenue or income) or Column 8 (for expenses) of the form;
- Declare the differences between the accounting amounts and the reassessed amounts in Column 5 (for revenue or income) or Column 9 (for expenses) of the form;
- Declare an increase in profits due to the reassessment of transfer prices of the related party transactions in Column 11 of the form. The upward adjustment to the taxpayer’s accounting profit is reported in Form 03-7/TNDN, i.e. Item 1.5 (Code B6) of the annual tax return. There is no guidance in the forms in case the taxpayers’ reassessment of transfer prices results in a reduction of profits for tax in line with the arm’s length principle.

No specific guidance has been issued by the revenue authorities on the preparation of Form 03-7, especially how the reassessment of arm’s length value of the related party transactions should be made. Taxpayers are recommended to refer to the transfer pricing regulations (Circular 66) for general guidance on determination of arm’s length value of their related party transactions which contains the requirement of benchmarking for this purpose.

Like Form 01, Form 03-7 also requires taxpayers to disclose their transfer pricing method(s) for the different types of related party transactions involving tangible goods, services, intangibles and financial transactions, and the different types of related party relationship.
Transfer pricing documentation

In accordance with Circular 66, the taxpayers having related party transactions must maintain contemporaneous transfer pricing documentation as supporting evidence of the arm’s length nature of their related party transactions. Under laws, transfer pricing documentation must generally be in Vietnamese and submitted to the tax authority within 30 working days of the authority’s written request.

Tax payers’ failure to comply with the documentation requirement implies that they are exposed to the risk of the tax authorities’ reassessment of transfer prices or profits for tax purposes which can be accompanied by penalties and late payment interest charge (of 0.05% per day) under laws. Other than the mere amounts of tax for the years under adjustment, the adjustments may entail far reaching consequences in terms of the alternation of the taxpayers’ tax profile (e.g. determination of the first profit making year or tax loss carry forward) and even adverse publicity for the taxpayer companies.

Recommendation

Transfer pricing audits are often based on taxpayers’ information and the tax authorities’ risk assessment. Adjustments or non-adjustments of transfer prices or profits in related party transactions for tax purposes are basically based on financial data of the taxpayer companies and comparables in the benchmarking. Giving correct information and having the supporting benchmarking analysis are, therefore, of paramount importance for taxpayers to have the right outcome in the audits.

In their tax filing for the 2014 and future fiscal years, taxpayer companies having related party transactions should:

- Prepare Form 03-7 properly and submit the declaration timely to the local tax authority (i.e. within 90 days from the end of the fiscal year as applicable to the filing of corporate income tax returns); and
- Maintain a contemporaneous transfer pricing analysis to support their position taken in Form 03-7 on the self-assessment of transfer prices based on arm’s length or market values.

Under Circular 66, transfer pricing documentation must be available at the time of the transactions and updated during the course of the transactions. In international and local practice, the contemporaneity requirement generally means the transfer pricing documentation which normally contains benchmarking based on independent transaction or comparables’ data must be available before the tax filing. This is true in a sense that, for example, where the taxpayers consider that they complied with the arm’s length requirements in related party dealings and therefore report nil adjustments in the self-assessment of transfer prices or profits for tax in Form 03-7, their position needs to be substantiated by a contemporaneous transfer pricing analysis.