

Taiwan grants flexibility for income adjustments for cross-border bilateral or multilateral APAs

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In brief

In line with international tax trends, the Taiwan Ministry of Finance (MOF) on June 24 issued a Decree (Tai Tsai Ji No. 11024508100) which grants flexibility for income adjustments for cross-border bilateral or multilateral advance pricing arrangements (BAPAs). The new Decree stipulates that when the Taiwan tax authorities negotiate cross-border BAPAs with the competent authorities of the treaty partners, both authorities may determine the method of examining whether the controlled transactions fall within the arm's-length range. They can adopt the results of the controlled transactions either on a year-by-year basis or using the average results of the controlled transactions of the covered years as a whole.

If 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 the income of the enterprise at an agreed point within the arm's-length range. Moreover, this adjustment could be either calculated and made separately to the income of the enterprise on a year-by-year basis or aggregated as a sum and made one time to the last year covered in the BAPA.

This Decree grants flexibility for the Taiwan tax authorities to conclude BAPAs with the competent authorities of the treaty partners and provides more certainty to the transfer pricing adjustment practice under BAPAs. The Decree may retain 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 Organisation for Economic Co-operation and Development.

The MOF also illustrated with the following example. Company A is an enterprise in Taiwan, and its affiliated enterprise, Company B, is an enterprise in Country B. Company A and Company B applied for a BAPA to the competent authorities of Taiwan and Country B, respectively, which covers the controlled transactions for the years 2021 to 2025. In ordinary situations, the Taiwan tax authorities may negotiate with the competent authority of Country B and conclude the terms such as taking Company A as the tested party, using the comparable profit

method (transactional net margin method) with the operating net profit margin as the profit level indicator, and setting the arm's-length range from 3% to 8%.

According to this Decree, the Taiwan tax authorities may additionally agree on the following matters:

- **The method to examine whether the results of the controlled transactions are in line with the BAPA –** Whether the operating net profit margin of Company A falling within the aforementioned arm's-length range (3% to 8%) could be examined either by checking the margin for each year from 2021 to 2025, or by checking the simple average of the margin for those five 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 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 one-time to the year 2025.

The takeaway

Issues related to transfer pricing and double taxation avoidance are now among the most challenging topics for enterprises' international tax management. Enterprises may want to consider applying for BAPAs as a vehicle to enhance their overall tax management.

Let's talk

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