

China's State Taxation Administration publishes its 2020 APA Annual Report

December 14, 2021

In brief

The State Taxation Administration (STA) published the “China Advance Pricing Arrangement Annual Report (2020)” ([2020 Annual Report](#)) on October 29. The 2020 Annual Report contains statistical data and analysis of the advance pricing arrangement (APA) cases from 2005 to 2020.

In 2020, the STA continued its efforts to enhance its capability to advance APA cases despite the impact of the COVID-19 pandemic. During the year, China signed 15 unilateral APAs (including four renewals) and 14 bilateral APAs (including six renewals), both reaching new highs after 2019 in recent years.

The STA recently has undertaken a number of measures to promote APAs to help enterprises achieve tax certainty in transfer pricing in China. In this regard, the STA issued the Public Notice on Matters Regarding the Application of Simplified Procedures of Unilateral Advance Pricing Arrangements (STA Public Notice [2021] No.24 (“Public Notice 24”) in July 2021 and the 2020 Annual Report also introduces the simplified APA procedures.

Action item: China tax authorities are exploring innovative approaches to promote APAs, including the introduction of simplified unilateral APA programs and the use of flexible mutual agreement procedures, aiming to strengthen the taxation services provided to enterprises. It is foreseeable that the number of APAs signed, especially the number of China unilateral APAs, will further increase. We suggest that multinational companies (MNCs) explore the feasibility of the APA program, together with other dispute resolution mechanisms, to manage their transfer pricing risks during the period of COVID-19 pandemic and worldwide trade uncertainty.

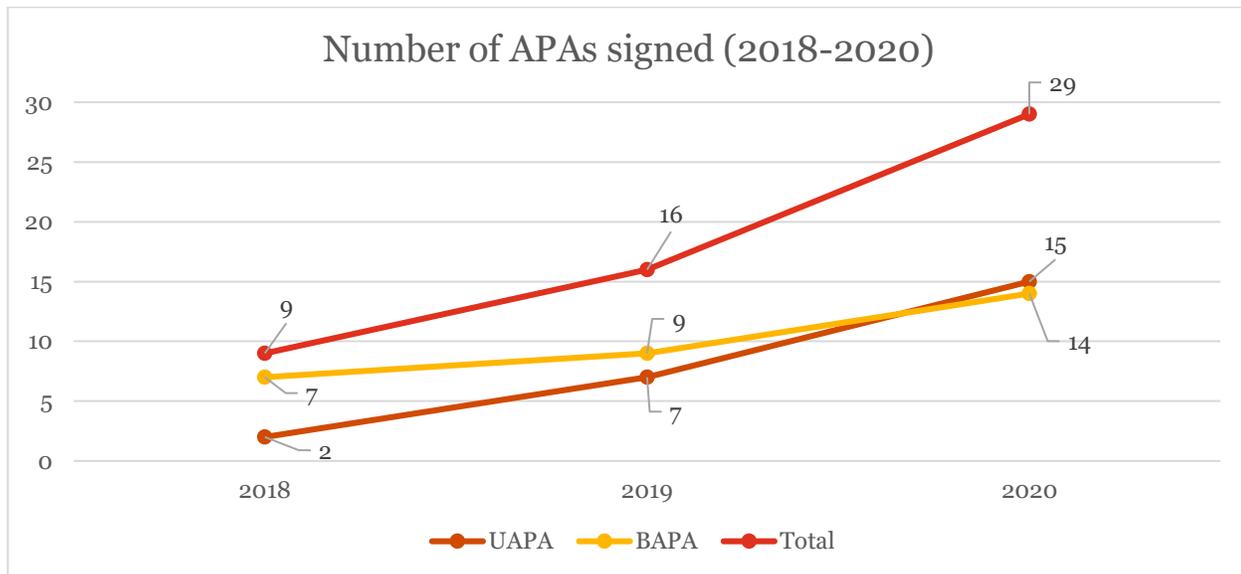
In detail

The STA has been releasing an APA annual report since 2009. The 2020 Annual Report is the 12th APA annual report released by the STA to describe the latest mechanisms, procedures, statistics, and implementation of the APA program in China.

APAs by year and by phase

During 2005 to 2020, China signed 116 unilateral APAs and 90 bilateral APAs with other jurisdictions, accounting for 56% and 44% of the total number of signed APAs in China, respectively.

In 2020, the number of unilateral and bilateral APAs signed further increased, with a total of 29 APAs signed — a record high since China started APA statistics in 2005. These included 15 unilateral APAs (including four renewals), which is a significant increase compared with 2017 (three cases) and 2018 (two cases), and also a continuous increase compared with 12 cases in 2019. This reflects the increasing flexibility of China tax authorities toward accepting unilateral APAs. The remaining 14 are bilateral APAs (including six renewals), which also makes 2020 the year with the most signed cases.



In addition to the APA statistics by year, the 2020 Annual Report summarizes the number of unilateral APAs and bilateral APAs by phase. Compared with 2019, by the end of 2020 the total number of unilateral and bilateral APAs at the intent phase decreased by 11 cases, while total APAs at the application phase increased by four cases. As noted, 15 unilateral and 14 bilateral APAs were signed. Based on statistics, it can be inferred that the number of unilateral and bilateral APAs that were newly applied for but have not yet been signed in 2020 were four cases and 18 cases respectively.

Observation: This shows that bilateral APAs still are preferred by many MNCs under the growing uncertainty of global trade. Even though bilateral APA applications must be submitted to both competent tax authorities at the same time — which may complicate the application progress due to limited official resources and potential disagreement between the two competent tax authorities on certain issues — they can help MNCs in seeking to achieve tax certainty and effectively avoid or eliminate international double taxation.

Observation: At the same time, the release of Public Notice 24 broadens the application scenarios of unilateral APAs. We expect that the number of applications for unilateral APAs also will increase in the future.

APAs by time taken

According to statistics from the 2020 Annual Report, 89% of the unilateral APAs and 54% of the bilateral APAs were concluded within two years.

It is noteworthy that China's APA process has a special 'pre-analysis' practice. That is, in order to ensure the quality of APA applications, before the official acceptance of APA application, the China tax authorities already would have reviewed and evaluated a draft application submitted by the taxpayer during the pre-filing meeting and application intention stage. After an initial assessment that the proposed transfer pricing method in the application is in line with the arm's-length principle, the China tax authorities then will approve the taxpayer to submit the formal APA application.

Other statistics on China APAs

The 2020 Annual Report also summarizes other statistics related to China's APAs as of the end of 2020:

- **Transfer pricing method:** The transactional net margin method (TNMM) is the most commonly used method in APAs signed by China, being used a total of 199 times and accounting for 81% of all the applied transfer pricing methods.
- **Country/region:** Asia continues to be the region where China has signed the most bilateral APAs (59 cases), followed by Europe (19 cases) and Americas (11 cases). In 2020, a bilateral APA was newly signed with Oceanian countries (one case).
- **Transaction type covered:** Buy-and-sell transactions account for the largest portion of transactions covered by China's APA program. Of the concluded APAs, 58% are of this transaction type, followed by services (23%) and transfer of the right to use or ownership of intangibles (19%). With the development of China's service industry, the proportion of transactions involving services and intangibles in APAs also has increased on a yearly basis.
- **Industrial classification:** Most China APAs signed are for MNCs, accounting for 80% of the total.

Observations

Number of Signed APAs hits a record high

Although the COVID-19 pandemic inevitably has affected the work routine of tax authorities (including those that are relevant to the mutual agreement procedures (MAP) carried out by the STA and the competent tax authorities of other countries and regions), the APAs signed by China in 2020 still hit a record high.

While the pandemic made face-to-face negotiation almost impossible, we observed that the STA remained active and held online MAP negotiations with the tax authorities of many other countries and regions, e.g., Japan, South Korea, the United States, and Germany.

The increase in number of APAs signed in 2020 can be attributed to the working flexibility of the tax authorities and their determination to better serve taxpayers in times of economic uncertainty. It is foreseeable that virtual MAP negotiations will become the norm in the near term. At the same time, because online meetings are more flexible, it also is possible to hold multiple MAP negotiations within a year.

Number of renewal cases has increased significantly

In 2020, 10 APA renewals were signed, which is a significant increase compared with previous years (three cases in 2017, two cases in 2018, and two cases in 2019). This, to some extent, is the result of the settlement of the backlog of renewal cases from previous years. Meanwhile, this reflects that enterprises that have reached and signed APAs in earlier years still are actively seeking to reach agreement with tax authorities and obtain ongoing tax certainty.

According to the Public Notice 64 (Public Notice on Matters Regarding Refining the Administration of Advance Pricing Arrangements (Public Notice of the State Taxation Administration [2016] 64)), an enterprise shall file a renewal application to the tax authorities within 90 days prior to the expiration of the APA and submit an "APA renewal application" along with a report specifying the implementation status of the current APA. The renewal application shall document an explanation of whether there are any substantial changes to the facts in the existing APA and the operational environment.

For signed APAs, if the implementation period is affected by the COVID-19 pandemic, the STA provided relevant guidance in the "Questions and Answers on Anti-Tax Avoidance During the COVID-19" ("[Q&As](#)") issued on September 30, 2021.

According to the answers provided by the STA, if the enterprise does have a substantial change that affects the implementation of the APA due to the COVID-19 pandemic, it can provide a written report to the tax authority,

detailing the impact of the COVID-19 pandemic on the implementation of the APA, and provide the relevant supporting materials. The in-charge tax authority shall analyze and assess the extent of the impact of the substantial changes brought about by the COVID-19 pandemic on the APA. For unilateral APAs, the tax authority shall negotiate with the enterprise to revise or terminate the APAs; for bilateral (multilateral) APAs, the tax authority shall report to the STA through levels for coordination, and the STA shall negotiate with the competent tax authority of the other party of the tax arrangement.

The "Q&As" further clarify that if the impact of the COVID-19 pandemic results in a substantial change in the operating environment of a taxpayer that has an existing APA, and that change affects the key assumptions, the enterprise could communicate with the tax authority in a timely manner during the APA period. The enterprise shall provide supplementary analysis materials and solutions for continuous implementation of the APA, in order to seek understanding and cooperation with the tax authority and minimize the impact of the COVID-19 pandemic on APAs. This opinion seems in line with the relevant content of the "Guidance on the transfer pricing implications of the COVID-19 pandemic" issued by the Organisation for Economic Cooperation and Development on December 18, 2020.

Observation: Based on past tax practices in China, if the business of the enterprise continues to operate normally, the APA seems unlikely to be suspended or re-negotiated during the implementation period. Therefore, we do not anticipate that the Chinese tax authorities would carry out large-scale revisions or suspend the APAs during the covered period due to COVID-19. Once a consensus is reached, both tax authorities and enterprise are more likely to reflect the impact of the economic environment including the COVID-19 pandemic on the related-party transactions during the renewal phase.

The application of simplified procedures of unilateral APAs

On July 26, 2021, the STA issued Public Notice 24, which became effective from September 1, 2021, in order to "improve efficiency in providing tax certainty for taxpayers' cross-border investment and operations."

The simplified procedures are mainly embodied in the following two aspects: simplified procedures and faster processing, aimed at improving the application efficiency of unilateral APAs. For unilateral APAs, with regard to enterprises that have undergone special tax investigations or signed APAs previously, the Chinese tax authorities have accumulated extensive experience to provide better services to taxpayers.

With the issuance of Public Notice 24, more enterprises can apply for unilateral APAs under the simplified procedures. The public notice reflects the STA's commitment toward improving the level of taxation services and promoting the balanced development of tax management and services. Public Notice 24 also reflects the STA's commitment to ensuring taxpayers are aware of and able to exercise their rights, as well as their willingness to provide taxation services, despite limited resources, to highly cooperative and compliant enterprises.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

Transfer Pricing – China

Jeff Yuan, Shanghai
+86 (21) 2323 3495
jeff.yuan@cn.pwc.com

Spencer Chong, Shanghai
+86 (21) 2323 2580
spencer.chong@cn.pwc.com

Qisheng Yu, Beijing
+86 (10) 6533 3117
qisheng.yu@cn.pwc.com

Transfer Pricing Global and US Leaders

Horacio Peña, *New York*
Global Transfer Pricing Leader
+1 917 478 5817
horacio.pena@pwc.com

Paige Hill, *New York*
US Transfer Pricing Leader
+1 917 923 841
paige.hill@pwc.com

© 2021 PricewaterhouseCoopers LLP, a Delaware limited liability partnership. All rights reserved. PwC refers to the United States member firm, and may sometimes refer to the PwC network. Each member firm is a separate legal entity. Please see www.pwc.com/structure for further details.

This content is for general information purposes only, and should not be used as a substitute for consultation with professional advisors.