
Update on the Japanese Transfer Pricing Documentation Requirements

December 2017

In brief

In March 2016 the Japanese Cabinet approved the 2016 tax reform proposals, which included revisions to the transfer pricing documentation requirements for taxpayers. These can be reviewed in our January 2016 newsletter, at this link:

<http://www.pwc.com/jp/en/taxnews-transfer-pricing/assets/tpnews-2016-01-en.pdf>

The revisions to the legislation were based on the recommendations contained in the “Transfer Pricing Documentation and Country-by-Country Reporting, 2015 Final Report” (“Action 13 Report”) published as part of the Base Erosion and Profit Shifting (“BEPS”) Project.

Since the implementation of the tax reform proposals into the Act on Special Measures Concerning Taxation (“ASMT”), the tax authorities have issued further guidance on the amendments to the legislation. In June 2016, the National Tax Authority issued an Outline of the Revision of the Transfer Pricing Documentation (“NTA Outline”), clarifying the entities required to submit the documentation, the types of documentation required to be submitted and the reportable items. The English translation of the NTA Outline is available at this link:

http://www.nta.go.jp/shiraberu/ippanjoho/pamph/pdf/h28iten-kakaku_en.pdf

This newsletter summarizes the details of the implementation of the Action 13 Report that have become available since our newsletter of January 2016, as highlighted in the NTA Outline, in other information published by the NTA since March 2016 or in inquiries made to the NTA’s helpdesk.

In detail

1. Definition of Terminology

Under the revised legislation, Japanese subsidiaries and branches that are Constituent Entities of a specified multinational enterprise (“MNE”) are required to prepare a Notification for Ultimate Parent Entity (“NUPE”) form, Country-by-Country Report (“CbCR”) and Master File.

The NTA Outline defines the terminology above that is used in the legislation, such as “Constituent Entity” and “Specified MNE”. According to the NTA Outline, a Constituent Entity is a company within an enterprise group whose property and profit/loss information is reported in a group’s consolidated financial statements under applicable standards, or would be included in the same manner if the parent company of the corporate group were listed. Further, a Specified MNE Group is

described as a MNE group with total gross revenue of JPY 100 billion or more in the preceding fiscal year.

Accordingly, the legislation in relation to the NUPE, CbCR and Master File is applicable to taxpayers that belong to an MNE with consolidated group revenue of JPY 100 billion or more (in the preceding year). For the CbCR however, this threshold will be adjusted to the threshold stipulated by the jurisdiction of the ultimate parent entity, as contemplated by the OECD's Action 13 implementation guidelines. In contrast, the threshold for filing of the NUPE and Master File is fixed at JPY 100 billion for all taxpayers.

2. New Transfer Pricing Documentation Requirements

Based on the NTA Outline, there are four tiers of documentation that are required to be prepared under the new rules. The CbCR, Master File and Local File were previously discussed in the tax reform proposals and in our January 2016 newsletter, however, the NTA Outline also includes a requirement for taxpayers to prepare a NUPE form.

Each of these documents is discussed in further detail below.

(1) Notification for Ultimate Parent Entity

Effective for fiscal years beginning on or after April 1, 2016, Japanese subsidiaries and branches that meet the threshold specified in section 1 above will need to prepare and submit the NUPE form. The NUPE form is in Japanese and must be submitted by the close of the ultimate parent entity's fiscal year via the e-tax system. The reportable items in the NUPE include basic information on the ultimate parent entity, such as the location of the head/principle office, the corporate number and name of representative.

(2) Country-by-Country Report

As confirmed in our January 2016 newsletter, the list of information to be included in the CbCR mirrors the reportable items under the BEPS Action 13 Report. The CbCR will also be filed through the e-tax system for Japanese taxpayers required to do so, within one year following the close of the ultimate parent entity's fiscal year to which the report relates. Note that the Japanese tax authorities have given a one year exemption to this deadline for countries that have enacted legislation relating to CbCR, with whom Japan has a treaty in place, but where the Japanese government has not yet entered into an arrangement for the exchange of CbCR (e.g., the US).

(3) Master file

The contents of the Master File under the Japanese transfer pricing legislation closely aligns with the requirements under the BEPS Action 13. As with the NUPE and CbCR, the Master File must be submitted electronically via the e-tax system. The deadline for filing the Master File with the Japanese tax authority is within one year following the close of the ultimate parent entity's fiscal year to which the report relates (same as CbCR).

(4) Local file

The NTA Outline confirmed that the reportable items to be included in the Local File are essentially equivalent to the documents required to be presented or submitted under Article 22-10 of the ASMT Ministerial Order. There is, therefore, no fundamental change in terms of the type of information that was required to be prepared under the previous legislation.

3. Taxpayers Required to Submit Documentation

The NTA Outline provides an explanation of which entities are responsible for filing the NUPE form, CbCR Master File and Local File. A summary of the responsible entities is provided below as follows.

(1) Notification of Ultimate Parent Entity Form

In principle, all Japanese taxpayers that belong to a specified MNE should file the NUPE form. Thus, Japanese subsidiaries and branches, even those with a Japanese headquartered parent entity, are

required to submit the NUPE. Note that this rule applies, even if the Japanese taxpayer does not engage in any related party transactions (i.e., has no transactions subject to transfer pricing).

However, the NTA Outline provides that where there is more than one such entity in Japan, one of the entities can act as a representative and file the form on behalf of the other domestic group affiliates. This is a useful concession as it would help alleviate the administrative burden for taxpayers with multiple entities in Japan, and avoid unnecessary duplication of preparation of the documentation.

(2) Country-by-Country Report

For Japanese subsidiaries or branches with an ultimate parent entity located in a foreign country, the CbCR will be obtained through the automatic exchange of information. However, where Japan cannot obtain a copy of the CbCR from the country of residence of the ultimate parent entity (or surrogate parent entity, if applicable) the domestic entity will be required to submit the CbCR.

For both Japanese and foreign ultimate parent entities, the CbCR can be prepared in English. As with the NUPE, the CbCR is required even where the Japanese taxpayer does not engage in any related party transactions.

(3) Master File

Japanese subsidiaries and branches that meet the specified group revenue threshold are required to submit a Master File. As with the NUPE, if there are several entities that belong to the same MNE group, one of the entities can file the Master File on behalf of the others. Based on the NTA Outline, the Master File may be prepared in either English or Japanese.

As with the NUPE and CbCR, the Master File is required even where the Japanese taxpayer does not engage in any related party transactions.

(4) Contemporaneous Local File

Consistent with the previous legislation, all taxpayers engaged in transactions with foreign affiliates are required to prepare transfer pricing documentation going forward. However, under the revisions to the legislation, there is now a contemporaneous requirement to the preparation of the Local File.

In the past, the Japanese legislation was flexible as to when taxpayers should prepare documentation. Under the new rules, the Local File must be prepared by the time of filing the tax return, unless the taxpayer's transactions with its foreign related parties meets both conditions below:

- (i) The amount of transactions with a single foreign related party in the preceding year is less than JPY 5 billion; and
- (ii) The amount of intangible property transactions with foreign related parties in the preceding year is less than JPY 300 million.

The new legislation provides that submission of the Local File is within 45 days or less upon request from the Japanese tax authorities, although it should be noted that the tax authorities can choose any date within this designated period. Accordingly, in theory, a taxpayer may be required to produce a Local File within a shorter time frame, e.g., within one week.

For taxpayers that satisfy both conditions outlined above and are thus exempt from the contemporaneous requirement, those taxpayers will be still required to submit documentation within 60 days or less upon request from the Japanese tax authorities; again with the submission period being stipulated by the tax authorities.

4. Penalties

Although the NTA Outline does not specify whether there are any penalties for failure to submit the NUPE form by the specified deadline, it does outline the penalties for failure to submit the CbCR and Master File by the due dates. For both of these documents, the penalty for non-compliance is JPY

300,000 per document, which may be imposed on both the company and the company's representative.

As discussed in our previous newsletters of January 2016, there is no monetary penalty for failure to submit the Local File within the period designated by the tax examiners. However, the tax authorities can resort to using the presumptive method or use of secret comparables.

5. The takeaway

MNEs globally are focused on compliance with the requirements of the CbCR and Master File, and local notification rules, such as the Japan NUPE. As the above summary provides however, there are always local interpretations of how the Action 13 Report is to be implemented in each jurisdiction. It is therefore strongly recommended that MNEs check these local interpretations in each case, rather than assuming that they can rely on the OECD's proposal.

Moreover, taxpayers in Japan have historically paid less attention to preparation of the Local File than taxpayers in other countries, such as China or the US, where monetary penalties have applied to failure to complete transfer pricing documentation. Going forward however, we expect that the Japanese tax authorities' focus on documentation (in the form of Local Files) will be significantly increased, and it will therefore create difficulties in the audit process for taxpayers that have not completed and are not able to submit a Local File. We strongly urge all taxpayers to begin preparation of their Local File sooner rather than later, if they have not already done so.

Let's talk

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

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