

This is an unofficial English translation of Public Notice on Matters Regarding Refining the Filing of Related Party Transactions and Administration of Contemporaneous Transfer Pricing Documentation (Public Notice of the State Administration of Taxation [2016] 42). In the case the unofficial English translation conflicts with the content in the original Public Notice in Chinese, the Public Notice in Chinese shall prevail.

Public Notice on Matters Regarding Refining the Filing of Related Party Transactions and Administration of Contemporaneous Transfer Pricing Documentation

Public Notice of the State Administration of Taxation [2016] 42

To refine the filing of related party transactions and the administration of contemporaneous transfer pricing documentation (hereinafter referred to as the “contemporaneous documentation”), the Public Notice is hereby issued in accordance with the relevant provisions of “Enterprise Income Tax Law of the People’s Republic of China” (hereinafter referred to as the “Enterprise Income Tax Law”) and its implementation regulations, and “The Tax Collection and Administration Law of the People’s Republic of China” (hereinafter referred to as the “Tax Collection and Administration Law”) and its implementation regulations.

1. A tax resident enterprise that pays Enterprise Income Tax according to its financial records and a non-tax resident enterprise that has an establishment or a place of business in China and settles Corporate Income Tax based on its actual accounts shall, at the time of submitting its annual Enterprise Income Tax return, report related party transactions based on its dealings with related parties, and file the “People’s Republic of China Enterprise Annual Reporting Forms for Related-Party Transactions (2016 version)”.
2. Any of the following relationships of an enterprise (one party) with other enterprises, organisations or individuals (the other party) shall constitute a “related party relationship” as stipulated in this Public Notice :
 - (i) One party directly or indirectly owns 25% or more shares of the other party; or a common third party directly or indirectly owns 25% or more of shares of both parties.

Where one party indirectly holds the other party’s shares through an intermediate party, so long as it owns 25% or more shares of the intermediate party, the percentage of the other party’s shares held by it is equal to the percentage of the other party’s shares held by the intermediate party.

Where two or more natural persons, who are spouses, related by lineal consanguinity, siblings, or in other custodianship/family maintenance relationships, hold the shares of a same enterprise, the percentage of shares held by them shall be aggregated in the calculation to determine related party relationship.

- (ii) One party owns shares of the other party, or a common third party owns shares of both parties, even though the percentage of shares held in either situation is less than the percentage as specified in item (i), the total debt between both parties accounts for 50% or more of either party's total paid-in capital, or 10% or more of one party's total debt is guaranteed by the other party (except for loans or guarantees from or between independent financial institutions).

Ratio of total debt to paid-in capital = annual weighted average debt / annual weighted average paid-in capital, where:

Annual weighted average debt = $\sum_{i=1}^n$ (book value of debt (i) x corresponding number of days outstanding / 365;

Annual weighted average paid-in capital = $\sum_{i=1}^n$ (book value of paid-in capital (i) x corresponding number of days invested) / 365.

- (iii) One party owns shares of the other party, or a common third party owns shares of both parties, even though the percentage of shares held in either situation is less than the percentage as specified in item (i), the business operations of one party depend on the proprietary rights, such as patents, non-patented technological know-how, trademarks, copyrights, etc., provided by the other party.
- (iv) One party owns shares of the other party, or a common third party owns shares of both parties, even though the percentage of shares held in either situation is less than the percentage as specified in item (i), the business activities, such as purchases, sales, receipt of services, provision of services, etc., of one party are controlled by the other party.

The aforementioned "controlled" refers to the case where one party has the right to make decisions on the other party's financial and operational policies and can therefore derive benefits from the other party's operations.

- (v) More than half of the directors or senior management (including secretaries of the board of directors of listed companies, managers, deputy managers, financial controllers and other personnel specified in the company's articles of association) of one party are appointed or assigned by the other party, or simultaneously serve as directors or senior management of the other party; or more than half of the directors or senior management of both parties are appointed or assigned by a common third party.

(vi) Two natural persons who are spouses, related by lineal consanguinity, siblings, or in other custodianship/family maintenance relationships have one of the relationships as specified in items (i) to (v) with one party and the other party respectively.

(vii) Two parties substantially have common interests in other ways.

Except for item (ii) in this Article, the aforementioned related party relationship should be recognized for the period during which it exists, in the event it changes during the filing year.

3. Any shareholding by the State or association through assignment of directors or senior management by the state-owned assets management authorities, and therefore qualified as the relationship as specified in Items (i) to (v) of Article 2, will not be deemed to constitute a “related party relationship” as specified in this Public Notice.

4. Related party transactions mainly include:

(i) Transfer of the right to use or ownership of tangible assets. Tangible assets include merchandise, products, buildings, transportation vehicles, machinery and equipment, tools, apparatus, etc.

(ii) Transfer of financial assets. Financial assets include accounts receivables, notes receivables, other receivables, equity investments, debt investments, derivative financial instruments, etc.

(iii) Transfer of the right to use or ownership of intangibles. Intangibles include patents, non-patented technological know-how, trade secrets, trademarks, brand names, customer lists, sales channels, franchise rights, government licenses, copyrights, etc.

(iv) Financing. Financing includes all types of long-term and short-term loans (including group’s cash pool), guarantees, all types of interest-bearing advance payments and deferred receivables or payables, etc.

(v) Services. Services include market survey, marketing planning, agency, design, consulting, administrative services, technical services, contract research and development, maintenance services, legal services, financial services, audit, recruitment, training, centralised procurement, etc.

5. Tax resident enterprises that fall into any of the following categories shall file the Country-by-Country Report at the time of submitting their “Annual Related Party Transactions Reporting Forms”:

(i) The resident enterprise is the ultimate holding company of a multinational enterprise’s (hereafter referred to as the “MNE”) group having total consolidated group revenue of more than 5.5 billion RMB during the fiscal year immediately preceding the reporting fiscal year as reflected in its consolidated financial statements for such preceding fiscal year.

Ultimate holding company is the enterprise that can consolidate the financial statements of all constituent entities that belong to its MNE group and cannot be included in the consolidated financial statements of another enterprise.

Constituent entities shall include:

- a. Any entity that is included in the consolidated financial statements of the MNE group.
 - b. Any entity that would be included in the consolidated financial statements of the MNE group if equity interest in such entity were traded on a public securities exchange.
 - c. Any entity that is excluded from the consolidated financial statements of the MNE group solely on size or materiality grounds.
 - d. Any permanent establishment that prepares a separate financial statement.
- (ii) The resident enterprise that has been appointed by the MNE group to file the Country-by-Country Report.

The Country-by-Country Report is to disclose information relating to the global income, taxes and business activities of all constituent entities of the MNE group to which the ultimate holding company belongs on a country-by-country basis.

6. For a MNE group whose ultimate holding company is a resident enterprise in PRC, if its information is related to national security, it can be exempted from filing the Country-by-Country Report in whole or in part in accordance with the applicable laws and regulations.
7. Tax administrations may exchange the Country-by-Country Report in accordance with tax treaties, agreements or arrangements that PRC has entered into.
8. For an enterprise that is not required to file the Country-by-Country Report under the provisions of Article 5 of this Public Notice, tax administrations can request the enterprise to provide the Country-by-Country Report during a special tax investigation if the MNE to which the enterprise belongs is required to prepare the Country-by-Country Report in accordance with the relevant regulations of another country and one of the following conditions is met:
 - (i) The MNE has not filed the Country-by-Country Report to any other countries.
 - (ii) Although the MNE has filed the Country-by-Country Report to another country, there is no mechanism in place to exchange Country-by-Country Report between China and that country.
 - (iii) Although the MNE has filed the Country-by-Country Report to another country, and there is a mechanism in place to exchange the Country-by-Country Report between China and that country, the Country-by-Country Report has not been successfully exchanged to China.

9. Enterprises that encounter actual difficulties in filing the “Annual Reporting Forms for Related Party Transactions” on time as required may apply for an extension of time in accordance with relevant provisions of the Tax Collection and Administration Law and its implementation regulations.
10. Enterprises shall, in accordance with Article 114 of the implementation regulations of the Enterprise Income Tax Law, prepare contemporaneous documentation with respect to their related party transactions for each tax year and submit the documentation upon the tax administration’s request.

Contemporaneous documentation may include master file, local file and special issue file.

11. Any enterprise that meets one of the following criteria shall prepare a master file :
 - (i) The enterprise that has conducted cross-border related party transactions during the tax year concerned, and the MNE group to which the ultimate holding company that consolidates the enterprise belongs, has prepared a master file.
 - (ii) The annual total amount of the enterprise’s related party transactions exceeds 1 billion RMB.
12. The master file is to provide an overview of the global business operations of the MNE group to which the ultimate holding company belongs, and shall include the following information:

- (i) Organisational structure

Chart illustrating the global organisational structure and ownership structure of the MNE group, and the geographical locations of all constituent entities. A constituent entity refers to any operating entity of the MNE group, including corporations, partnerships and permanent establishments, etc.

- (ii) Description of MNE’s business(es)

- a. A description of the MNE’s business, including important value drivers of business profit.
- b. A description of the supply chain and main geographic markets for the group’s five largest products or service offerings by turnover plus any other products or services amounting to more than 5 percent of group turnover. The required description could take the form of a chart or a diagram.
- c. A list and brief description of important service arrangements between constituent entities of the group, other than research and development services, including a description of the capabilities of the principal locations providing important services and transfer pricing policies for allocating service costs and determining prices to be paid for intra-group services.

- d. A functional analysis describing the principal contributions to value creation by individual constituent entities within the group, i.e. key functions performed, important risks assumed, and important assets used.
- e. A description of business restructurings, industrial restructurings, transfers of functions, risks or assets occurring within the group during the fiscal year.
- f. A description of reorganizations occurring during the fiscal year within the group, i.e. Changes of legal form, debt restructuring, equity acquisition, asset acquisitions, merger and divestitures.

(iii) Intangibles

- a. A general description of the MNE's overall strategy for the development, ownership and exploitation of intangibles, including location of principal research and development facilities, location of research and development management, and their functions, risks, assets and personnel.
- b. A list of intangibles or groups of intangibles of the MNE group that are important for transfer pricing purposes and which entities own them.
- c. A list of important agreements entered between constituent entities and their related parties related to intangibles, including cost sharing agreements, principal research services agreements and licence agreements.
- d. A description of the groups' transfer pricing policies related to research and development and intangibles.
- e. A description of any important transfers of interests in intangibles among related parties during the fiscal year concerned, including the entities, countries, and compensations involved.

(iv) Financial activities

- a. A description of financing arrangements between related entities within the group and important financing arrangements with unrelated parties.
- b. The identification of any constituent entities of the MNE group that provides a central financing function for the group, including the country under whose laws the entity is organised and the place of effective management of such entities.
- c. A description of the MNE's general transfer pricing policies related to financing arrangements between related entities.

(v) Financial and tax positions

- a. The MNE's annual consolidated financial statements for the fiscal year concerned.

- b. A list of the MNE group's existing unilateral advance pricing agreements, bilateral advance pricing agreements and other tax rulings relating to the allocation of income among countries.
 - c. Name and location of the constituent entity that files the Country-by-Country Report for the MNE group.
13. Any enterprise that meets one of the following criteria during the fiscal year shall prepare a local file:
- (i) The annual related party transfer of ownership of tangible assets exceeds 200 million RMB (for toll manufacturing transaction, the amount is calculated using the import/export customs declaration prices).
 - (ii) The annual related party transfer of financial assets exceeds 100 million RMB.
 - (iii) The annual related party transfer of ownership of intangibles exceeds 100 million RMB.
 - (iv) The annual total amount of other related party transactions exceeds 40 million RMB.
14. Local file is to disclose detailed information on the enterprise's related party transactions, including the following:
- (i) Overview of the enterprise
 - a. Organisational structure, including the setup, scope of responsibility and number of employees of each functional department of the enterprise.
 - b. Management structure, including the parties to which each level of the management reports, and the locations in which such parties maintain their principal offices, etc.
 - c. Industry description, including an overview of the industry in which the enterprise operates and its development, other major economic and legal factors affecting the industry, such as industry policies, trade restrictions, as well as key competitors.
 - d. Business strategies, including the workflow, operational model and factors that contribute to value creation, etc., of each department and each operational stage of the enterprise.
 - e. Financial data, including turnover, costs, expenses and profits for the different types of business and product offerings of the enterprise.
 - f. A description of business restructurings or intangibles transfers in which the enterprise has been involved in or affected by and an explanation of those aspects of such transactions affect the enterprise.
 - (ii) Related party relationship

- a. Information on related parties including the name, legal representatives, composition of senior management, address of actual operation of any related party (enterprise) that directly or indirectly own shares of the enterprise and with which the enterprise has entered into transactions, as well as the name, nationality and country of residence of any related party (individual).
 - b. Information on taxes of income tax nature to which the enterprise is subject, with details including types of the taxes, tax rates and applicable preferential tax treatments.
 - c. Information on changes in related party relationship of the enterprise during the fiscal year concerned.
- (iii) Related party transactions
- a. Overview of related party transactions
 - (1) A description of related party transactions with details, including copies of contracts or agreements relating to the related party transactions and their execution, characteristics of the underlying targets, and categories, parties involved, timing, transaction value, settlement currency, contractual terms and conditions, trading models of the related party transactions as well as an explanation of how they are similar to or different from that of unrelated party transactions.
 - (2) Transactional flow of the related party transactions, including the flows of information, goods and materials, and capitals, as well as an explanation of how they are similar to or different from that of unrelated party transactions.
 - (3) A description of functions and risks, including the functions performed, risks assumed and assets used by the enterprise and its related parties for each category of related party transactions.
 - (4) Key factors affecting the pricing of related party transactions, including intangibles involved in the transactions and their impact on pricing, as well as location specific factors such as cost savings and market premium etc. Analysis on location specific factors shall focus on aspects such as labour costs, environmental costs, market size, degree of market competition, consumer purchasing power, substitutability of goods or services, and regulatory controls, etc.
 - (5) Financial information on related party transactions, including the amount involved for each related party and each category of related party transactions; segmented data on turnover, costs, expenses and profits of related party transactions and unrelated party transactions; for items that could not be directly segmented and therefore have been allocated using appropriate allocation keys, information on how they are allocated and an explanation of how the allocation keys have been selected.

- b. Value chain analysis
 - (1) Flows of business, goods and materials, and capitals within the group, including design, development, manufacturing, marketing, sales, delivery, billing and payment, consumption, after-sale service, recycling, other processes related to goods, services or other relevant underlying targets of the related party transactions and all the parties involved.
 - (2) Annual financial statements of each of the aforementioned parties for the immediately preceding fiscal year.
 - (3) Measurement and attribution of value creation contributed by location specific factors.
 - (4) Allocation policies and actual allocation results of the group's profits in the global value chain.
- c. Outbound investment
 - (1) Information on outbound investment, including the locations, amounts, main businesses and strategic plans of the investment projects.
 - (2) An overview of outbound investment projects, including shareholding structure and organisational structure of the investment projects, employment of senior management involved in the investment projects, decision making process and the parties with final decision making authority about the investment projects.
 - (3) Data of outbound investment projects, including operational data.
- d. Related party equity transfer
 - (1) An overview of related party equity transfer, including background, parties involved, timing, pricing, payment method of the transfer, as well as other factors affecting the transfer.
 - (2) Information on the equity transferred, including information like the equity's geographic location, timing of the transfer, methodology of the transfer, cost of the transfer, income generated from the transfer, etc.
 - (3) Due diligence report or asset valuation report or any other information pertaining to the equity transfer.
- e. Related party services
 - (1) An overview of related party services, including service providers and recipients, nature of services, characteristics, method of service delivery, pricing policies and methods, form of payments, and benefits received by each party in relation to the services provided, etc.

- (2) Methodology for determining the service costs, service items, service amount, allocation keys, calculation process and results.
 - (3) Where the enterprise and its group are involved in transactions of the same or similar nature with an unrelated party, the enterprise shall describe in detail how the transactions are similar to or different from related party transactions in pricing policies and results.
 - f. Existing advance pricing agreements and other tax rulings to which the PRC is not a party and which are related to the enterprise's related party transactions.
- (iv) Comparability analysis
- a. Factors considered in the comparability analysis, including characteristics of the goods or services involved in the transactions, functions performed, risks assumed and assets used by each party involved, contractual terms, economic environment, business strategies, etc.
 - b. Information related to the functions performed, risks assumed, and assets used by the comparable companies.
 - c. Search process for comparables, data source, selection criteria and rationale for setting the criteria.
 - d. Information of selected internal or external comparable uncontrolled transactions and financial information of comparable companies.
 - e. Comparability adjustments and rationale for the adjustments.
- (v) Selection and application of transfer pricing method
- a. Selection of tested party and rationale for the selection.
 - b. Selection of transfer pricing method and rationale for the selection. Regardless of the transfer pricing method selected, description of the contribution of the enterprise to the group's overall profit or residual profit is required.
 - c. Assumptions and judgment made in the process of determining arm's length prices or profits.
 - d. Application of reasonable transfer pricing method and result from comparability analysis to determine the arm's length prices or profits.
 - e. Other information supporting the selection of transfer pricing method.
 - f. Analysis and conclusion of whether the transfer pricing for the related party transactions complies with the arm's length principle.
15. Special issue files include special issue file on cost sharing agreements and special issue file on thin capitalisation.

An enterprise that enters into or implements a cost sharing agreement (hereafter referred to as “CSA”) shall prepare a special issue file for the CSA.

An enterprise with a related party debt-to-equity ratio exceeding the threshold shall prepare a special issue file on thin capitalisation to demonstrate its conformity with the arm’s length principle.

16. Special issue file on CSAs shall include the following information:

- (i) A copy of the CSA.
- (ii) Other agreements reached by the CSA participants to facilitate the implementation of the CSA.
- (iii) Use of outcomes of the CSA by non-participants, amount paid and form of payment, as well as the allocation method for sharing the payment among the participants.
- (iv) Information on any participants entering in or withdrawing from the CSA during the fiscal year concerned, including the names of the participants, their countries of residence and related party relationships, and the amount and form of payment for the buy-in or buy-out compensations.
- (v) Description of amendments to or termination of the CSA, including the reasons for the amendments or termination, and the treatment or allocation of the existing CSA outcomes.
- (vi) Total cost from the CSA and its breakdown during the fiscal year concerned.
- (vii) Cost sharing among the CSA participants during the fiscal year concerned, including the amount, form of payment and which parties the allocated costs are paid to; and the amount, form of payment, and which parties the balancing payments are paid to or received from.
- (viii) A comparison of expected benefits and actual benefits from the CSA, and the balancing adjustments made.
- (ix) Calculation of expected benefits, including the selection of parameters, calculation method and reasons for any changes to them.

17. Special issue file on thin capitalisation shall include the following information:

- (i) Analysis of the enterprise’s solvency and borrowing ability.
- (ii) Analysis of the borrowing ability and financing structure of the group to which the enterprise belong.
- (iii) A description of changes in equity investment of the enterprise, such as changes in registered capital, etc.
- (iv) Nature and purposes of the related party debt investment, and the market conditions at the time the debt investment was obtained.

- (v) Currency, amount, interest rate, term and financing terms of the related party debt investment.
 - (vi) Whether an unrelated party is capable and willing to accept the aforementioned financing terms, amount and interest rate.
 - (vii) Collaterals provided by the enterprise in order to obtain the debt investment and the relevant terms.
 - (viii) Details of the guarantor and the terms of guarantee.
 - (ix) Interest rates and financing terms of similar loans occurring during the same period of time.
 - (x) Terms of conversion of convertible bonds.
 - (xi) Other information that can demonstrate the enterprise's conformity with the arm's length principle.
18. Enterprises with effective advance pricing agreements in place may choose not to prepare local file and special issue file with respect to the related party transactions covered by such advance pricing agreements, and the amount of these related party transactions is excluded from the calculation of the thresholds stipulated in Articles 13 of this Public Notice.

Enterprises with only domestic related party transactions may choose not to prepare master file, local file and special issue file.

19. A master file shall be completed within 12 months of the fiscal year end of the ultimate holding company of the enterprise group; local file and special issue file shall be completed by 30 June of the year following the year during which the related party transactions occur. Contemporaneous documentation shall be submitted within 30 days after receiving a request from the tax administrations.
20. Enterprises that fail to submit contemporaneous documentation due to an event of force majeure shall submit the contemporaneous documentation within 30 days after the event of force majeure ceases to prevent the submission.
21. Contemporaneous documentation shall be prepared in Chinese. The source of information used should be specified.
22. Contemporaneous documentation shall be sealed with the enterprise's company chop, and signed and sealed by the legal representative or the representative authorised by the legal representative of the enterprise.
23. In the event of a merger or divestiture, the relevant contemporaneous documentation shall be kept by the surviving enterprise after the merger or divestiture.

24. Contemporaneous documentation shall be kept for 10 years from the completion date of the preparation as required by the tax administrations.
25. For enterprises that file related party transactions, submit contemporaneous documentation and other relevant information in accordance with relevant provisions, when additional tax is imposed by the tax administrations during the special tax investigation, an interest can be levied based on the People's Bank of China central base lending rates for the same period to which the tax payment is related, in accordance with the provisions under Article 122 of the implementation regulations of the Enterprise Income Tax Law.
26. This Public Notice also applies to transactions with related parties in Hong Kong, Macau and Taiwan.
27. This Public Notice shall become effective from 2016 and onwards. Chapter 2, Chapter 3, Article 74 and Article 89 of the "Implementation Measures of Special Tax Adjustments (Trial Version)" (Guo Shui Fa [2009] No.2), the "People's Republic of China Enterprise Annual Reporting Forms for Related-Party Transactions" (released with Guo Shui Fa [2008] No.114) shall be annulled as of the same date.

Appendix:

- (1) People's Republic of China Enterprise Annual Reporting Forms for Related-Party Transactions (2016 version)
- (2) Filing Instructions to "People's Republic of China Enterprise Annual Reporting Forms for Related-Party Transactions (2016 version)"

State Administration of Taxation
29 June 2016