UNIVERSITA' DEGLI STUDI DI PADOVA

DIPARTIMENTO DI SCIENZE ECONOMICHE ED AZIENDALI
"M. FANNO"

CORSO DI LAUREA IN
BUSINESS ADMINISTRATION

PROVA FINALE

TRANSFER PRICING REGULATION IN CHINA

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ANNO ACCADEMICO 2020 –2021

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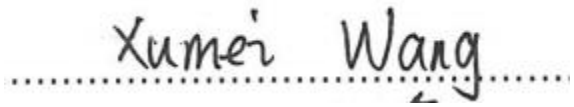

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Abstract

This thesis first briefly expounds the relevant theories and basic knowledge of transfer pricing, and then discusses how multinational enterprises carry out tax planning, including its motivation, principles and characteristics. Multinational companies generally use the way of "high in and low out" or "low in and high out" to avoid the tax burden of tangible assets. And they avoid the tax burden of intangible assets by adjusting the price of technology, patent and trademark. Then, this thesis elaborates on the two aspects of intangible assets and tangible assets.

After that, through the analysis of the current situation of China's transfer pricing and the comparison with the relevant laws and regulations of developed countries in Europe and the United States, we find the differences between China's transfer pricing rules and those of developed countries in Europe and the United States, which are manifested in the following aspects: the scope of intangible assets is not clear enough, the tax management of cost sharing agreement is not standardized enough and the advance pricing system is not perfect enough. Finally, in order to solve the above three problems, this thesis puts forward some ideas by drawing lessons from the rules of European and American countries and.

Key words: taxation regulations, tax avoidance, price transfer

I. Introduction

With the development of economic integration, the free flow of capital, the further elimination of trade barriers, the leap-forward development of telecommunications and technology, and the further development and cross-regional utilization of intangible assets, multinational enterprises have changed from the previous nationalization. The business has evolved to the current highly integrated global business model of the supply chain, which has promoted the continuous growth of international investment and the prosperity of international trade. Economic globalization becomes the mainstream of world economic development, and multinational companies are becoming the leading core force of the world economy increasingly. Conversely, some discordant phenomena are happening all over the world: multinational companies often avoid taxation by transfer pricing strategies, squeezing out competitors and transfer profits, and signing a series of internal agreements to reduce risks. Assets are transferred to regions/countries with relatively more favorable taxation policies in order to pay lower income taxes, which make social welfare losses to the relevant countries.

In China, under the policy of Reform and Opening, China are connecting more and more closely with the world economy. On the one hand, There are many development advantages in China, such as relatively loose investment environment, low labor costs, a series of preferential tax policies and a huge consumer market which attract a large amount of foreign investment. According to relevant statistics, as of December 2019, there are currently 1,001,635 foreign-invested enterprises, and the accumulated actual use of foreign capital reached US$229.47 billion. [1]And about 490 of the world's top 500 companies invest in China, accounting for about 98% of the total number.[2]

On the other hand, as a developing country, China is a relative late-comer in the transfer pricing arena.While the Chinese tax Authority, the State Administration of Taxation has been adept at leveraging the international tax experience of other countries, China began to establish her own unique transfer pricing system from the 1980s.[3]

Although China's economic prosperity and national employment are improved by these foreign-funded enterprises, who bring advanced technology and management experience to China. However, behind these positive effects is lots of multinational companies taking advantage of the differences in the taxation systems of various countries and loopholes in foreign tax laws,transferring profits,and avoid paying tax.

[1] China Foreign Investment Statistical Bulletin (2019)- https://swt.fujian.gov.cn/zjswt/jgzn/jgcs/wzglc/tjsj/202011/P020201123555794829525.pdf
[2] XINHUANET(2019) - http://www.xinhuanet.com/fortune/2019-08/21/c_1124903506.htm
[3] The development of transfer pricing in China (2014) - Michelle Markham and Yixin Liao

Since international tax avoidance has a significant impact on international economic exchanges and the taxation interests of relevant countries, how to effectively prevent the occurrence of international tax avoidance is an important topic in the taxation activities of various countries. The current tax avoidance of multinational companies not only involves the purchase and sale of goods and the provision of labor services, but also involves various types of transactions such as financing and transfer of intangible assets. Therefore, this thesis hopes that through the study of China's transfer pricing rules, analysis and reference to western advanced experience and successful practices, exploring the transfer pricing intentions and tax planning methods of multinational companies, it will be able to have a deeply understanding of China's transfer pricing regulations, so as to further promote the effective development of China's anti-tax avoidance work.

Chapter Ⅱ Related theories of transfer pricing - This chapter deals with the description of the concept of transfer pricing, analyzes the motivation of transfer pricing on the basis of two theories, studies the influence of China on the transfer pricing behavior of multinational companies, and lays the foundation for the next few chapters.

Chapter ⅢChina's transfer pricing and taxation strategies - Most scholars concentrate on studying China's anti-tax avoidance rules from the perspective of the government. This thesis is innovative in looking at transfer pricing from two different perspectives: the Chinese government and multinational companies. These two antagonistic and interlinked relationships lead readers to a more comprehensive and three-dimensional understanding of the starting point and method of setting transfer pricing regulations.

Chapter Ⅳ China's transfer pricing and anti-tax avoidance - It is the core chapter of this thesis. It first studies two kinds of Government restrictions on transfer pricing, and then summarizes the adjustment rules of transfer pricing. Next, through the classification of assets, namely tangible assets and intangible assets, the different rules corresponding to different assets are studied respectively. What's more, this chapter compares the transfer pricing regulation systems between the West and the East as well, hoping to gain experience from it. Finally, it summarize the status quo of China's transfer pricing rules and the issues that need to be improved.

Chapter Ⅴ Conclusion - It summarizes the content of the full text, in particular the characteristics of China's transfer pricing, and puts forward suggestions for the improvement of China's transfer pricing rules.

II. Related theories of transfer pricing

2.1 Overview of transfer pricing

A multinational company (MNC) is a corporate organization that owns or controls the production of goods or services in at least one country other than its home country.[4] And the term related-party transaction refers to a deal or arrangement made between two parties who are joined by a preexisting business relationship or common interest. Companies often seek business deals with parties with whom they are familiar or have a common interest. [5]

Therefore, transfer pricing refers to the transfer of tangible property (such as commodities, vehicles, machinery and equipment, factories, land, etc.) and intangible property (such as commodities, patents, know-how, etc.), financing funds and provision of labor services between affiliated companies. This kind of pricing method is determined through transfer pricing called the transfer price.[6] Although it is a neutral concept originally, but the term transfer pricing is used derogatively, that is, transfer pricing is a pricing method that is different from normal market transaction prices between multinational affiliates in order to realize the overall interests of affiliates and the collection of remuneration or the allocation of expenses, and transfer the income of one member company to another member company in order to achieve the purpose of tax avoidance.

Simply, the definition of "transfer pricing" refers to the price set between related companies when selling goods, providing services and transferring intangible assets.Of course, the transfer price issue can occur within one country or between countries.

Transfer pricing is the result of intra-company transactions. Due to the incomplete market, companies that conduct transactions through the external market incur greater transaction costs or even invalid costs. In order to reduce these costs and expenses, and minimize the overall tax burden of the company and other related costs, companies prefer to use internal transactions, which build the "internalization" of market transactions, thereby promoting the development of transfer pricing continuously.

Some multinational companies usually use transfer pricing to maximize after-tax profits based on the differences in taxation between countries and the tax preferences of different countries. The main manifestation is "high import and low export", that is, the prices of imported materials, imported equipment, and loan interest rates are higher than the international market prices, while the prices of export products are lower than the international market. Through this operation, the company has formed a loss on the book and

[4] Multinational corporation - https://en.wikipedia.org/wiki/Multinational_corporation
[5] Related-Party Transaction(2020) - https://www.investopedia.com/terms/r/related-partytransaction.asp
[6] 《Model Agreement Concerning the Avoidance of Double Taxation》 - OECD

transferred its profits to countries or regions with low tax burdens. Multinational companies not only get more profits, but also reduce a lot of exchange rate risks. A survey conducted by Ernst & Young Accounting in 2001 showed that transfer pricing has been regarded by multinational companies and tax authorities as the most important international tax issue at present and in the future. 61% of the parent companies of multinational companies regard transfer pricing as the most important international tax issue in the following next two years, and up to 94% of subsidiaries believe that transfer pricing is the most direct international tax issue.[7] In general, the tax avoidance transfer pricing of multinational companies to achieve the goal of maximizing profits has become the mainstream of international transfer pricing.

2.2 Theoretical basis

Transfer pricing refers to the price at which intermediate products are traded between affiliated companies within the group. This affiliated transaction relationship includes not only the transactions between the parent company and the subsidiary, but also the transactions between subsidiaries. In the entire global production system, the intermediate product is a capital element. In that way, transfer pricing can be seen as a means for multinational groups to allocate capital elements in the this global system. The main goal of maximizing benefits and optimizing the allocation of resources is artificially formulated on a global scale, rather than depending on the cost of trading commodities or the supply-demand relationship in the international market. It is a flexibility and arbitrariness internal business decision and is not affected by market rules.

2.2.1 Internalization theory

The theoretical basis for multinational companies to implement transfer pricing is the internalization theory which explains the existence of the firm because it is the most efficient way of coordinating a set of activities rather than market exchange. The firm grows when it can absorb markets and it would do so until the costs to the firm of further growth exceed the benefits. [8]

The prototype of internalization can be traced back to the famous article "The Nature of the Enterprise" by Coase who realized that the internal market has advantages of low cost and high efficiency compared to the external market. When the various costs of transactions through the external market are far greater than the internal transaction costs of the enterprise, in view of the pursuit of enterprise profit maximization, the enterprise will establish an

[7] 《Thoughts on the Transfer Pricing Strategies of Multinational Enterprises in China》（2008）- The People's Government of Shanxi Province

[8] 《The Palgrave Encyclopedia of Strategic Management》（2018）- Mie Augier, David J. Teece

internal market so that the transaction can be carried out within the internal system of the enterprise to avoid the high cost of external transactions.

At the end of the 1970s, the British economist Barkley Carson and Canadian economist Lugman used the Coase Theorem to study the FDI behavior of multinational corporations and put forward related theories of internalization. For example, British scholar Barkley Carson used Coase's related theories and analyzed how companies obtain and retain monopoly advantage through internal transactions in his co-authored book "The Future of Multinational Corporations". In addition, Lugerman believes that internalization is the process of establishing an internal market within a company. In this process, the internal market of the enterprise replaces the external irregular market, the enterprise organization is regulated by the internal price or transfer price, and the internal market is made as efficient as the potential regular market.

Overall, the results of researching on internalization theory can be summarized as follows: The incompleteness of the market is not conducive for enterprises to realize the maximization of the profit, so they are willing to trade products in the internal market, because in that case, enterprises can coordinate and allocate internal resources reasonably. As we known, multinational groups expand their business scale through direct investment, replace external market mechanisms with internal management mechanisms, to improve the transaction efficiency of the entire group, save transaction costs, and achieve a higher degree of resource optimization effectively. The purpose of a company's foreign investment is to open up the market and expand control. It's not a simple transnational transfer of capital. The company's internal management mechanism replaces the external transaction market mechanism, which minimize transaction costs and maximize internal advantages.

2.2.2 Enterprise Organization Theory

Organizational theory consists of many approaches to organizational analysis. Organizations are defined as social units comprising people who are managed in such a way as to enable them to meet organizational needs, pursue collective goals, and adapt to a changing organizational environment.[9] Permat (1969) took the lead in proposing the EPG model of three types of multinational corporations: Ethnocentric, Polycentric and Geocentric. To begin with, the polycentric multinational company is a highly centralized organizational structure, which is mainly manifested in the centralized decision-making and unified command of the parent company, while the subsidiary company has little decision-making autonomy. Following this, the polycentric multinational company has a relatively decentralized organizational structure with less control by the parent company, and each

[9] Organizational theory - https://en.wikipedia.org/wiki/Organizational_theory

subsidiary has a decision-making autonomy. Finally, the geocentric multinational company regards the multinational company as a global organization, and the home country and its subsidiaries need to coordinate and cooperate all the time.

With the ever-increasing scale of multinational companies, the complexity of operations is increasing. Based on the principle of saving costs and expenses, and responding to the needs of the external market as soon as possible, centralized organizational structure is replaced by the decentralized organizational structure gradually. However, the operational management efficiency of the decentralized organizational structure is usually low. In this case, transfer pricing must be used to improve this drawback. In the case of increased agency costs and incomplete and asymmetry of information, the polycentric company needs to introduce a resource allocation management mechanism to allocate the overall profit of the multinational company and improve the efficiency of resource allocation by formulating transfer pricing for each subsidiary. It means the scale effect of multinational corporations provides the soil for the generation of transfer pricing. The transfer pricing mechanism meets the requirements of multinational corporations' resource allocation mechanism in terms of performance appraisal, pursuit of profit maximization, and tax burden minimization.

2.3 Motives of transfer pricing

There are differences in taxation systems, management methods, economic development levels and market conditions in various countries and regions, above mentioned factors stimulate multinational companies to develop transfer pricing strategies. So the main motivations for multinational companies to adopt transfer pricing strategies are as follows:

2.3.1 Tax avoidance

Tax reduction is a obvious motivation for multinational companies to adopt transfer pricing strategies, and this purpose is mainly achieved by adjusting the profits of subsidiaries located in countries and regions with different tax rates. These taxes are mainly divided into the following categories:

The first one is income tax. Because different regulations are adapted by different countries on taxation, such as taxation system, tax law and so on, so multinational companies take advantage of this regional difference to transfer profits between countries with different tax rates through transfer pricing, in order to achieve the purpose of reducing the income tax paid by enterprises.

For example, Company B in Country B is a wholly-owned subsidiary of Company A in Country A. The tax rate for company A in country A is 50%, and the tax rate in country B is 20%. A provides B with a batch of parts and components, which are processed by B and sold.

A reduces its taxable income and pays less income tax through low-priced supplies. And B has increased profits due to lower costs and paid more taxes in country B. However, because of the low tax rate in country B, the total tax burden of the entire company group has been reduced.

The second is tariffs, which means the internal transactions of multinational companies usually transcend national boundaries and occur in different countries. Frequent transactions will cause multinational companies to pay high tariffs. In view of this, multinational companies make price adjustments in their internal market by manipulating high prices to low prices and low prices to high prices. For example, take advantage of thin capitalization, or relevant regulations of the Customs Union to avoid taxation.

In 2018, China Customs imported a total of 14,088.1 billion yuan in goods imported by China Customs.[10] Although after joining the World Trade Organization in 2001, in order to fulfill the WTO's commitment to lower tariffs and taxes, the Chinese government lowered the tariff import tax rate several times in the past ten years. From the early stage of reform and opening up,the arithmetic average tariff rate of 42.5% fell to the current 9.8 %, the decline can be said to be the largest among all taxes. Compared with the average tariff rate of 2% in developed countries, China's tariff rate is still high. For multinational companies, this factor has also become one of the purposes of their implementation of transfer pricing. Since the effect of transfer pricing on tariffs and income taxes is exactly the opposite, foreign-funded enterprises need to weigh the size of the tax burden and choose the best.

The third is withholding tax. Multinational companies' foreign investments usually use capital operations and a large number of intangible assets are used for transactions. These are all within the scope of expected tax collection. The estimated tax is based on the gross profit of the enterprise, and the tax burden is heavier. Therefore, multinational companies use transfer pricing to reduce the company's book profits and reduce the payment of withholding taxes.

For example, company A in country A is the parent company of company B in country B, and B should pay a dividend of 1 million yuan to A from the profits of the year, and it should pay 200,000 yuan withholding tax. In order to avoid this withholding tax, B does not directly pay dividends to A, but sells a batch of 3 million yuan worth of accessories produced for A to A for only 2 million yuan replacing the payment of dividends with low-priced supplies .

[10] Table of total value of import and export commodities A: Annual table（2020）- http://www.customs.gov.cn/customs/302249/302274/302277/302276/2851238/index.html

2.3.2 Enhance corporate competitiveness

Occupying new markets and improving the competitiveness of subsidiaries in the country where they are located are also one of the main motivations for multinational companies to implement transfer pricing.

On the one hand, multinational companies usually use transfer low prices to provide raw materials, intermediate products and services to subsidiaries in the target market, so that the subsidiaries can lower their prices when they intend to occupy a new foreign market under their strategic goals. While the cost of producing the final product, occupying the market with a low price advantage. This purpose is mainly achieved by the subsidiary company's price advantage compared with other companies producing similar products in the country where it is located, and the subsidiary company's price advantage comes from the related transaction price set by the parent company through transfer pricing strategy. When a subsidiary of a multinational enterprise in a certain country is in poor operating conditions, the parent company provides raw materials, products or labor services to the subsidiary in the country at a lower price, thereby reducing the production cost of the subsidiary and realizing the products produced and sold by the subsidiary. And it makes the subsidiary's products have a great price advantage compared to the products of other companies that cannot obtain low-cost raw materials and labor services in the country. Price is an important factor which affects consumers' choice of goods, so price advantage can attract more consumers, thereby opening the market of subsidiary products in the country quickly, achieving rapid growth in the market share of subsidiary products in the country, and further realizing the overall competitiveness of subsidiaries is improved.

On the other hand, in order to support overseas subsidiaries that are in the early stages of entrepreneurship or encounter strong competitors, multinational companies will use transfer low prices, provide them with raw materials and parts, or only charge lower technology usage fees to reduce their Cost and enhance competitiveness. In addition, in order to enable overseas subsidiaries to establish a good corporate image in the host country, improve their credibility, and obtain convenient financing, good investment opportunities and preferential conditions in the host country, multinational companies will increase their book profits through transfer pricing.

2.3.3 Avoiding risks

Through transfer pricing, multinational companies can also avoid multiple risks such as exchange rate risk and financial risk.

The first is exchange rate risk and financial risk. For example, when the exchange rate of the country where the subsidiary is located rises or the parent company encounters a financial

crisis, multinational companies can quickly transfer funds back to the parent company through transfer pricing. The company's funds are changed to debts lent to subsidiaries through loans, and a certain amount of interest is charged to the subsidiaries at the same time. This way, on the one hand, it reduces the pressure of the parent company's financial status or successfully avoid the risks caused by the rise in the exchange rate of the country where the subsidiary is located.

The second is political and social risks. When political turmoil and political upheavals occur in the host country, multinational companies can use transfer prices to transfer materials and equipment that may be confiscated by the local government to foreign subsidiaries at low prices, or purchase other subsidiaries' goods at higher prices , In order to avoid possible losses to the company due to changes in the political situation of the host country, to achieve the purpose of transferring a large amount of funds from the host country, and to reduce or avoid as much as possible the losses caused to multinational companies due to political risks.

The third is policy risk. The use of transfer pricing can evade the price control of the host country and evade anti-dumping investigations and anti-monopoly investigations. Price control is the government's main regulatory measures to maintain market transaction order, safeguard the legitimate rights and interests of domestic producers and consumers, and protect domestic vulnerable industries. It is mainly implemented through anti-monopoly and anti-dumping investigations. In order to circumvent anti-dumping investigations and anti-monopoly investigations, companies generally apply different transfer pricing strategies to artificially increase or decrease the prices of import and export commodities to achieve the purpose of evading supervision. When the host country restricts the enterprises from selling in the host country's market at low dumping prices, it often adopts a low-price transfer strategy to greatly reduce the cost of the subsidiary's products with low raw and auxiliary material prices. When the host country restricts companies from selling products at monopolistic high prices, they can often use high-price transfer strategies to increase the book cost of the host country's products by charging additional service fees and management fees.

2.3.4 Preferential policies

In addition to the above motives, some transfer pricing methods can also help subsidiaries obtain policy preferences in their countries or regions. Most of the subsidiaries of multinational companies are established in the member states of the World Trade Organization, and these countries usually provide domestic companies with trade subsidies, tax rebates and other preferential policies in order to attract investment and promote trade growth. Multinational companies can increase the export prices of their subsidiaries' products

to enable their subsidiaries to obtain higher trade subsidies and policy preferences. At the same time, this can also remove the suspicion of dumping that the product prices are too low.

2.4 The impact of transfer pricing by multinational companies

On the one hand, multinational companies are striving to adapt to the changing tax and legal regulations in emerging markets, and to study how to improve tax efficiency. On the other hand, global tax regulators are considering the erosion of their national tax base based on transfer pricing, and they have also increased their concerns. Attention to and enforcement of transfer pricing behavior. This has directly led to the continuous emergence of tax disputes between global tax regulators and multinational companies, and the number has doubled compared with the results of the 2010 survey. Ernst & Young's survey report shows that 47,070 companies have suffered double taxation due to transfer pricing audits, and 24,070 companies have suffered tax penalties in the past three years. 28% of companies are trying to seek assistance from their own government.[11] Resolve transfer pricing tax disputes. The report also pointed out that the global tax regulatory environment will remain severe in the next few years.

2.4.1 Loss of tax revenue

Generally speaking, when multinational companies formulate or implement transfer pricing, they will evade the tax burden of the host country as one of their purposes, because taxation is not a small expense for both domestic and foreign companies. Some countries have already given great tax concessions to multinational corporations relative to domestic enterprises. With the policy and financial support given by the local government, the various preferential treatments enjoyed by multinational corporations are almost comparable to those of tax havens. However, some of them have the highest interests. Multinational companies will still use transfer pricing to evade tax burdens, with the aim of maximizing corporate value and minimizing tax burdens.

[11] Ernst & Young "2012 Survey of Global Transfer Pricing Tax Authorities"

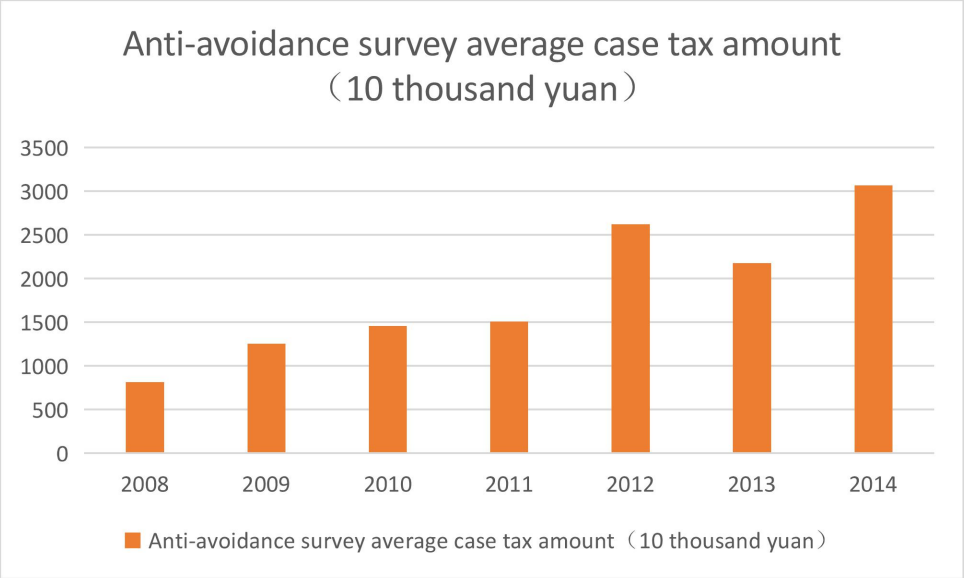

Figure2-1 Anti-avoidance survey average tax amount/case

Source: China State Taxation Administration

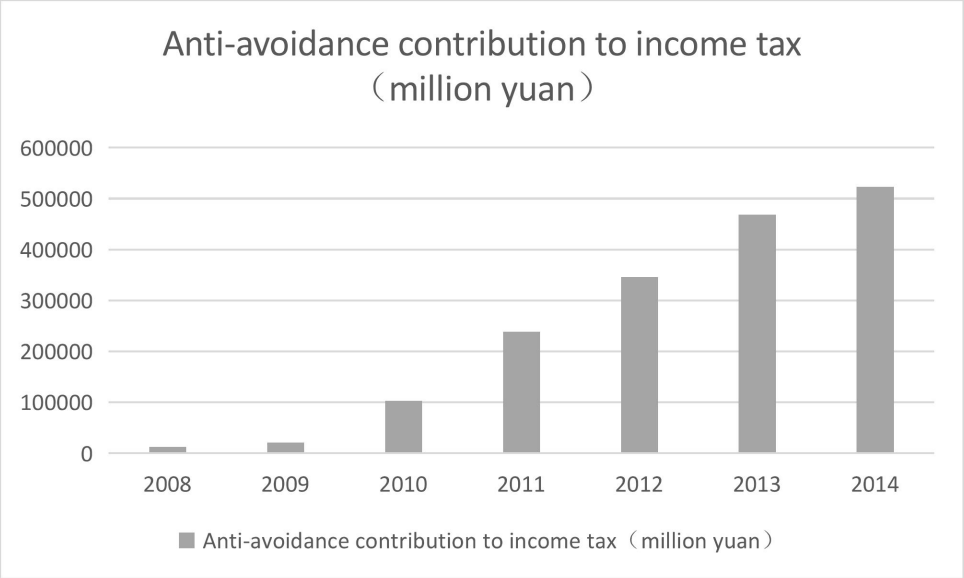

Figure2-2 Anti-avoidance contribution of tax revenue increase

Source: China State Taxation Administration

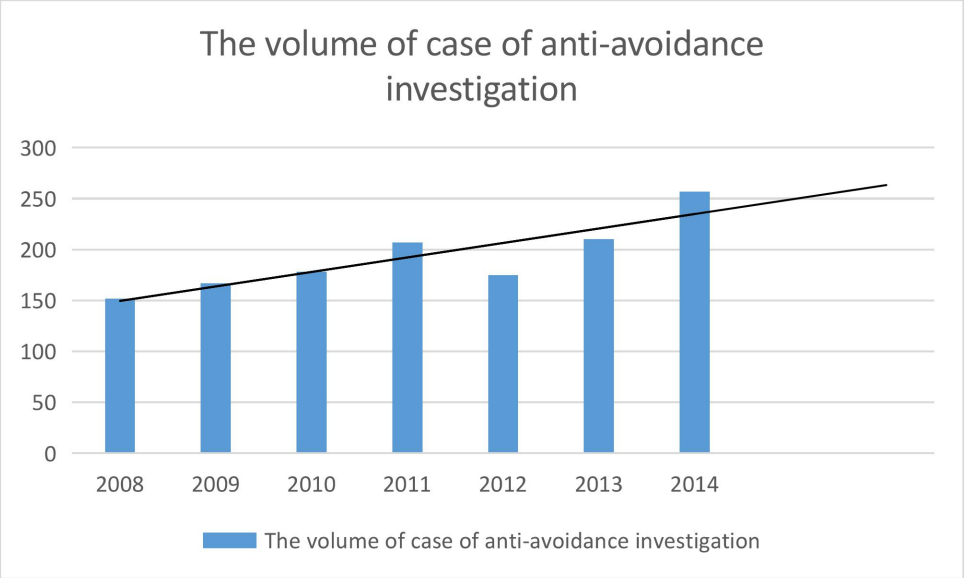

Figure2-3 The volume of cases of anti-avoidance investigation

Source: China State Taxation Administration

The impact of the transfer pricing of domestic and foreign affiliates has a particularly serious impact on China's taxation. This can be seen from the average tax replenishment amount of tax anti-avoidance investigations over the years (as shown in Figure 2-1). The contribution of tax revenue increase (as shown in Figure 2-2), as well as the statistics of the volume of tax anti-avoidance investigations over the years (as shown in Figure 2-3).

Foreign-invested enterprises established in China usually have three forms of organization: joint ventures, cooperative enterprises and sole proprietorships. Some foreign investors will transfer the business profits to the Abroad when a Chinese investor participates in equity participation or formation, the Chinese investors may not be able to obtain operating income and may have to continue to invest to make up for their losses. The final result is that the Chinese side sells equity to reduce losses and lose ownership.

For example, A Chinese company called Wuxi Little Swan transferred 12-year joint venture with Japan's Matsushita in 2007. Between the two joint venture companies, Wuxi Refrigerator achieved profitability only in 2002 and 2003, and suffered substantial losses in the rest of the year; while Wuxi Cold Press achieved meager profits in 2002, it has been at a loss. Finally, Wuxi Little Swan was insolvent and withdrew after the transfer of assets, while Japan's Matsushita withdrew more than 300 million yuan in technology royalties from the two joint ventures during its operation.

2.4.2 Undermine fair competition

The principle of formulating tax systems is tax fairness in various countries and regions, but some foreign-funded enterprises use transfer pricing strategies to keep their profits at lower level and minimize tax burdens, which against the principle of tax fairness.

According to the provisions of China's "Anti-dumping Regulations", imported goods cannot be dumped on the Chinese market at low prices. However, multinational companies look for other methods. Such as by registering and establishing subsidiaries overseas, they implement transfer pricing when conducting related transactions with Chinese subsidiaries, so that their subsidiaries can sell at low prices in the Chinese market.It disrupt undoubtedly the market transaction order with a potential risk of unfair price competition.

III. China's transfer pricing and taxation strategies

3.1 The relationship between transfer pricing and tax planning

3.1.1 Tax planning should conform to the principles of transfer pricing

Under normal circumstances, when there is a difference between the price of a multinational company’s related transaction and the price of a comparable unrelated transaction, it faces transfer pricing adjustments by the tax authority, which means make a reasonable choice after such factors can avoid adjustment risks.

(1) Long-term

Like other business strategies, transfer pricing strategies must first serve the overall strategic goals of the company. If it is limited to short-term goals such as avoiding taxation and foreign exchange control, it is bound to be revised and improved in the future implementation process to adapt to the long-term strategic goals of the enterprise. The untimely and inappropriate transfer pricing strategy may also affect the business efficiency of the enterprise. Therefore, the goal of sustainable development must be put in the first place to ensure that the transfer pricing becomes a part of the strategic objectives of the enterprise and is implemented throughout the entire business process of the enterprise. The established transfer pricing should be able to promote the realization of the overall business objectives, and coordinate the business objectives of all aspects and levels on the premise that the partial interests are subordinate to the overall interests. unified allocation and scheduling

At the same time, it is also necessary to establish a dedicated transfer pricing management department so that transfer pricing can be truly integrated into the corporate strategic goals and better serve the corporate strategic goals. Many multinational corporations set up global prices transfer Center, which is responsible for global transfer pricing branches, unified allocation and scheduling, improve the efficiency of the formulation and execution.

(2) Legality

Multinational companies in the development of transfer pricing strategies, any negligence may cause the company to suffer the risk of investigation. It is necessary to maintain risk awareness at all times, reasonably assess whether the transaction mode and the pricing of related transactions meet the requirements of the tax authority, as well as prepare for work-related information. Be prepared to prevent and reduce the risks of transfer pricing audits, and take precautions before they happen.

Simultaneously, it is necessary to carefully study China's various transfer pricing regulations, compare the transfer pricing regulations of the home country and the country where the affiliated company is located, study the commonalities and characteristics and

formulate a transfer pricing strategy that suits the company's overall strategy and is not inconsistent with the laws and regulations of various countries.

(3) Rationality

The rationality of a transfer pricing strategy's formulation affect directly the economic benefits of each subsidiary in the host country. It is necessary to consider fully the reasonable distribution of capital among various stakeholders and also consider the compliance of the distribution amount with the tax authority. A good transfer pricing strategy not only needs to cater to the company's overall strategic goals, but also needs to consider the business plan of the host country where the branch located.

(4) Advantage

The implementation of tax planning must meet the expectations of cost-effectiveness,and the benefits of transfer pricing should be able to offset the increasing in coordination and management costs. Not only that, but also consider whether the formulation of transfer pricing can stimulate the enthusiasm of related companies in operation and management, and Make their work input consistent with the income they receive. Finally, on the premise of pursuing overall interests, each affiliated company should have a certain degree of autonomous management. What's more,The transfer pricing of internal transactions must be acceptable to all parties, and the transfer pricing policy should be selected. In line with the company's strategy, when some factors that affect transfer pricing change significantly, the corresponding pricing policy can be adjusted in due course.

3.1.2 The manifestation of the application of transfer pricing in tax planning

The transfer price is not determined according to the relationship of supply and demand in the market, but according to the global business strategic goals of multinational companies, with the ultimate goal of profit maximization, and is stipulated by the administrative means of multinational companies. Generally speaking, related party transactions include: transfer of the right to use or ownership of tangible assets, transfer of financial assets, transfer of the right to use or ownership of intangible assets, financial communication, labor service transactions.[12] Based on the above transactions methods, the price transfer of multinational companies can be mainly divided into four categories: tangible asset price transfer, intangible asset price transfer, product price transfer, and transfer prices in other transactions.

(1)Tangible asset price transfer

The transfer price of tangible assets refers to the price at which tangible assets such as machinery and equipment are transferred between associated companies. Tangible assets include tangible commodities such as raw materials, machinery equipment and parts, finished

[12] Transfer pricing methods -https://www.shui5.cn/article/aa/114871.html

products, and semi-finished products. Affected by the different market structures in the international market, multinational companies take the advantages of internal unified deployment to form an internal market between the parent companies and their subsidiaries, change the sale price, useful life of fixed assets or use equipment financing lease and as well as using the various advantageous resources of the host country where the subsidiary is located to adopt a "high-in-low-out" approach for conducting internal transactions and transferring profits, or use the "low-in, high-out" approach to avoid tax burdens and the impact of unstable transaction prices, reduce costs and control the company's overall operating costs.

(2)Intangible asset price transfer

Intangible assets include company know-how, patents, registered trademarks and management fees, etc. The transfer price of intangible assets is the price used by multinational companies to transfer intangible assets, such as technology, patents, and trademarks, between related companies. In this way, multinational companies often use a certain percentage of the price of these intangible assets to calculate related expenses which is determined by all the costs of R&D activities and the operating expenses paid by the multinational companies to provide technology and trademark services. Multinational companies sign franchise, management and technical support contracts between the parent company and its subsidiaries, and according to the company’s integrated business strategy, arbitrarily reduce or increase the reservation price to transfer and adjust profits in the transaction process to achieve the best state of the company's production and operation. In the process of transferring intangible assets such as non-patent technology, franchise rights, trademark rights, etc., there are certain technical difficulties in assessing the exact market price and the true value of the business. Therefore, multinational companies can appropriately adjust or exempt transaction prices to avoid the tax burden of the host country and reduce transaction costs.

(3)Product price transfer

Product transfer price is also a kind of transfer price method, which refers to the price of purchasing raw materials and selling commodities among associated companies. In order to transfer the profits from parents to subsidiaries, the usual practice of the parent company is to transfer the right of supply and sell to associated companies abroad, afterwards sell the products to overseas affiliates at a lower price compared to the market price. As well as purchasing the required goods from overseas companies at a price higher than the market price. Reduce or increase the cost of the final product by adjusting the import and export prices of raw materials and semi-finished , so as to increase or decrease the product cost of its

affiliates, thereby reducing or increasing the profits of the affiliates. In this way, multinational companies transfer their profits through transfer pricing.

(4)Transfer prices in other transactions

In addition to the above-mentioned price transfer methods, there are other methods, such as financial lending methods, labor services and the provision of leasing services. One of the financing methods is financial lending, which is the interest of borrowing financial capital between the affiliated enterprises of the multinational company, that is, the lending interest rate. Multinational companies set interest rates higher or lower than the market to achieve the purpose of transferring profits. The service transfer price refers to the price at which the service fee is charged when the service is provided between the affiliated enterprises of the multinational company. For example, the maintenance costs of a certain company's machinery and equipment are handed over to an overseas subsidiary. In this way, the company's profits are transferred to the subsidiary by charging higher fees. In addition, multinational companies can also pay lower processing fees to achieve the purpose of transferring profits. Regardless of the adjustment of labor costs mentioned above, the enterprise can also adjust the product sales link to the sales department and organization of the affiliated company to increase or reduce the commission, management, advertising, consulting and other labor service fees. For instance, raising the standard of management fees charged to affiliated companies, or transferring their own management fees to affiliated companies, or apportioning research and development expenses, or the logistics and transportation system under the company's jurisdiction, charging affiliated companies with freight and miscellaneous fees at different prices to reduce profits. Transfer from a high-tax country to a low-tax country.

3.1.3 Implementing tax planning decisions with transfer pricing

If tax planning is to adopt transfer pricing methods, then tax planning must follow the transfer pricing rules, and the decision-making on transfer pricing will follow the company's management model. There are three main decision-making modes listed in Table 3-1:

Decision Mode	Description	Applicable Conditions	strong points	weak points
Unitary Center	Decision-making power at the highest level of the	Centralized management model	Conducive to the formulation of the best price and comprehensive resource allocation.	1.Each execution unit is passive and lacks motivation to control the cost of the department and

	company			improve its own operating performance. 2.Poor coordination.
polycentrism	Determined by each associated company independently	Decentralized management model	It represents their own interests, can make decisions based on time and conditions, and is convenient for timely response, which has great incentives for the executive unit.	It is difficult to balance and unify the interests of all structures.
Negotiation	The parties have to negotiate and decide together	Centralized and decentralized balance management model	1. It can balance the interests and expectations of all parties and maintain their consistency. 2. Take into account the partial objective situation,	Poor communication and coordination and information asymmetry may occur.

Table 3-1 tax planning decisions

3.2 Companies using transfer pricing for tax planning in China

3.2.1 The status quo of Chinese companies using transfer pricing for tax planning

Currently, the use of transfer pricing for tax planning by multinational companies is in the initial stage, as Chinese companies' multinational operations are in their infancy. Accordingly,Wang Yuting and Wang Jing (2005) conducted a survey on the use of transfer pricing by Chinese multinational companies through questionnaire surveys, including transfer

pricing awareness, analysis of transfer pricing influencing factors, and current status of Chinese multinational companies' use of transfer pricing.[13]

In terms of the perception of transfer pricing, 13% of multinational companies use transfer pricing to achieve global strategies, and 24% use transfer pricing to gain price advantage to expand and occupy the market. However, the reason for transfer pricing of more than half of the companies is to use various tax system differences to reduce tax burdens for tax planning. It can be seen that tax reduction is still the main motivation for the transfer pricing behavior of Chinese multinational companies, which can be ranked in order of importance: tax reduction, profit adjustment, strategic competition and risk aversion.[14] Therefore, the main purpose of Chinese multinational companies using transfer pricing in multinational operations focuses on reasonably reducing tax burdens for tax planning and maximizing overall total profits according to table 3-2.[15]

Number	Value Perception of Transfer Pricing	Percentage %	Application Stage
1	Tax planning for tax reduction	55	Flexible method in research phase
2	Prices reduction and market occupation	24	Maturity stage
3	Global development strategy	13	Research phase

Table 3-2 Chinese Multinational Corporation's Understanding of Transfer Pricing and Its Application Statistics

Among the factors that affect the use of transfer pricing, including long-term development strategies, short-term business objectives, macro policies and many other influencing factors, it is obvious that regional tax burden differences have the highest impact, and manager preferences have the least impact on transfer pricing strategies.

Table 3-3 Statistical Table of Transfer Price Method

Transfer price method	Proportion %	Main industry types	Features of Products
Cost-based approach	59	Manufacturing	Reliable and effective

[13] 'Investigation and Analysis on the Status of Transfer Pricing of Chinese Enterprise Groups"-Wang Yuting and Wang Jing (2005)-https://xueshu.baidu.com/usercenter/thesis/show?thesisid=8a26ff18c3729583b6d3a2ceda72db3f&site=xueshu_se

[14] <Business Economics>-"Research on Transfer Pricing of Multinational Corporations"(2008)-Liu Shengjun, Zhang Yuanyuan 11:94-96

[15] "Research on the problems and countermeasures of Chinese transnational corporations' transfer pricing"(2010)-Yu Qian.

		industry	cost measurement
Market-based approach	29	Developed industry	well-developed product market competition

The status quo of the specific methods used by multinational companies to use transfer pricing for tax planning is shown in Tables 3-3. When multinational companies use transfer pricing for planning in multinational operations, in manufacturing, they are mainly based on cost rather than Transaction-based. In general, 59% of the surveyed samples used cost as the basis for setting transfer prices, market-based methods accounted for 29%, and other methods accounted for 12%.[16]

3.2.2 Comparison of Tax Planning between China and Western Countries Using Transfer Pricing

Chinese and Western multinational corporations have similarities and differences in their purpose and motivation, awareness, analysis of influencing factors, application methods, and current performance when using transfer pricing for tax planning.

The similarities in the use of transfer pricing by Chinese and Western multinational companies for tax planning include: First, the purpose and motivation of the two are basically the same. Among the many motivations for using transfer pricing, international tax planning is the most important motivation for using transfer pricing for reducing tax burdens and maximizing total profits. Second, the main influencing factors are basically the same for instance, they often weigh the differences in the tax system of the investment home country and the host country, and the amount of tax subsidies that may be obtained, to make tax planning and implement transfer pricing. The most critical factor is the difference between the income tax rate and tariff rate of the countries where the two parties to the transaction are located. The third is that the general operation is basically the same, that is, using the differences in the tax systems of different countries, and using transfer pricing to transfer profits from high-tax countries to low-tax countries.

The differences between the two are shown in: At first, foreign multinational companies do not only focus on regional tax burden differences, but also consider many influencing factors such as corporate long-term development strategies, short-term business behaviors, macro policies, as well as managerial preferences. Conversely, Chinese multinational companies are more single to consider the tax burden. Secondly, the methods of using transfer

[16] "Investigation and Analysis of the Status of Transfer Pricing of Chinese Enterprise Groups"（2005）-<Foreign Taxation>-2：35-38

pricing in multinational operations are different that Chinese multinational companies set transfer pricing methods mainly based on cost. On the contrary, foreign multinational companies mostly use cost-based pricing methods in their own countries, and they use transaction-based and negotiated market prices in China (accounting for more than 60%). The third is the difference in application degree and scope. Many foreign multinational companies use transfer pricing for tax planning have become mature, and widely use transfer pricing as a means of international tax planning, showing the characteristics of concealment, flexibility, and reciprocity. However, Chinese companies lag far behind foreign multinational companies in terms of awareness, application methods, application level and scope.

In addition, the theoretical research and application experience of China's transfer pricing are far behind that of developed countries, and many multinational companies lack the support of a scientific transfer pricing decision-making system. Therefore, the situation and level of using it for tax planning are more lagging behind.

3.2.3 Issues of Chinese multinational companies using transfer pricing for tax planning

Differences in the tax system of various countries have a great impact on the overall profits of multinational groups, but Chinese multinational companies rarely use transfer pricing tax planning methods to improve and protect their own interests. Some companies have also been sanctioned by the host country for using improper methods. The development stage, transnational operation capability, and characteristics of transnational operation of Chinese companies' foreign investment restrict their use of transfer pricing. The reasons for this have given us enlightenment, mainly in the following aspects.

First, Chinese multinational companies have insufficient awareness of transfer pricing. Most of the multinational operations of Chinese companies are still in the initial stage, and they have not been able to clarify their own business objectives and global strategies. The effect of transfer pricing, especially through tax planning, to transfer profits has not been fully realized, and most of them are even in a state of unconsciousness. In addition, there are many small and medium-sized enterprises in China, and relevant organizations do not promote and popularize tax planning. Many small and medium-sized enterprises have a simple understanding of tax planning, which is to reduce taxes as much as possible, rather than maximize the benefits of the group's business as a whole. This behavior has caused the Chinese tax authorities to distrust the enterprise, thus restricting the development of tax planning[17].

Secondly, the foundation for applying transfer pricing is weak. Chinese multinational companies lack effective international management systems, fast and scientific information

[17] “The status quo of SME tax planning”(2017)- https://www.jieshui8.com/article/412.html

systems and specialized talents in their international operations, which restricts the use of transfer pricing. For companies, imperfect tax planning will lead to many risks. Companies need to comprehensively weigh the pros and cons from legal, financial, tax and risk aspects. This requires the formation of a professional team and it is very difficult for most companies in China who lack funds..

Due to lack of resources, most Chinese companies choose to use their own internal financial personnel for tax planning. However, tax planning is a highly professional project, and the financial personnel in the enterprise are limited by their own knowledge and experience, in this case, they cannot formulate a perfect plan. Therefore, the tax planning plan with potential risks not only fails to play the value effect of tax planning, but may also bring unnecessary economic losses to the enterprise.

Thirdly, Chinese companies are also in the process of exploring transfer pricing methods. Not only are they relatively unfamiliar with the host country's transfer pricing regulatory policies and measures, but they are not good at coordinating various interest relationships when adopting methods, which limits their tax planning functions. On the one hand, China's taxation laws and policies are very complicated, many systems are imperfect, conceptual expressions are vague and prone to ambiguity. These factors are obstacles to tax collectors from truly grasping the connotation of the tax law. On the other hand, China's tax law has been constantly revised and reformed, which has brought great challenges to tax collectors. For example, changes in corporate income tax in 2008, changes in business tax reform to value-added tax in 2016[18], and other changes in transfer pricing have caught tax collectors by surprise and caused many decision-making errors.

Fourthly, the scope of application of transfer pricing by Chinese companies is narrow. At present, the main application area is the transfer pricing of tangible assets, and it is rarely applied to the internal transactions of intangible assets. This is due to the fact that the scale of Chinese multinational companies is still relatively small and the R&D capabilities of intangible assets lag behind the level of developed countries.

Finally, most Chinese multinational companies have a single foreign investment and operation business, their internal international division of labor and coordination system is not yet mature and refined, they have not been able to build an efficient international business network, internal transactions are not active, and the platform for tax planning using transfer pricing is affected. limit.

[18] Announcement No. 11 (2017) of the State Administration of Taxation-
http://www.chinatax.gov.cn/n810341/n810755/c2567296/content.html

It should be noted that the use of transfer pricing for tax planning by foreign multinational companies has reduced the amount of tax payment to China and infringed on China's tax rights and interests. With the integration of the global economy, China needs to actively learn from the successful experience of multinational companies in developed countries, which has very positive significance for Chinese multinational companies to "go global" to make international investment and participate in international competition.

IV China's transfer pricing and anti-tax avoidance

From outside a multinational point of view when the company is doing tax planning, transfer pricing subject to certain developing external constraints, the government generally adopts OECD's transfer price method and advance pricing method (APA) to restrict and adjust the results of transfer pricing.

4.1 Government restrictions - Transfer Pricing under OECD

4.1.1 The three main ways of transfer prices

Multinational companies use transfer pricing to implement tax planning, which may be able to maximize overall profits, but they cannot set transfer prices to meet their own wishes arbitrarily, because governments and tax authorities have formulated many provisions to restrict multinational companies from using these methods. The OECD transfer price law recognized by the OECD has relevant standards. If a company's transnational operations violates these terms, the local government or tax authority will review the transfer pricing behavior. And if the verification is confirmed, it may be subject to tax adjustments or penalties.

Multinational companies attach great importance to transfer pricing strategies because this strategy brings many positive effects to the business operations of multinational companies. However, multinational companies are not arbitrarily when making transfer pricing and confirming transfer prices. They must follow relevant laws, regulations and international standards. At present, the transfer pricing rules formulated by the World Economic Cooperation Organization (OECD) are recognized and used by countries all over the world widely. The basic principle pursued by the World Economic Cooperation Organization is the principle of "fairness and independence", which requires that the transfer pricing between affiliated companies and the normal transaction price between independent companies must not be too large, and must be based on the normal transaction price between independent companies. As a prerequisite, the transfer price of related transactions is determined by combining the actual operation mode of the enterprise and the economic policy environment in which the enterprise is located. The following is a detailed analysis of several main methods used by multinational companies to confirm transfer prices.

(1) Based on cost

The cost-based price confirmation method is called the cost pricing method, which refers to the fact that the company mainly sets prices for related party transactions based on the actual cost of producing products or providing labor services. When confirming the transfer

price, a multinational enterprise sets the internal transfer price of related transactions on the basis of the costs incurred in each link of product production or the actual cost of providing labor services.

Since the enterprise can choose the full cost, standard cost or variable cost as the basic cost for confirming the transfer price reference object when setting the transfer price according to actual needs, or even add the opportunity cost that does not actually occur, when choosing the cost measurement method, The best measurement plan can be selected from a variety of cost measurement methods such as complete cost method, marginal cost method, and complete cost plus method. Therefore, the enterprise can control the level of the cost as the basis of the transfer price in a wide range, thereby controlling the transfer price The heights. In addition, compared with other transfer pricing methods, the data of the cost pricing method is easier to obtain, and it is simpler to use. Therefore, many multinational companies have chosen to use the cost pricing method to determine the transfer price. The cost pricing method can also realize the adjustment of corporate financial statements through the apportionment of indirect costs, which can help subsidiaries create a phenomenon of good business conditions, improve the public, corporate shareholders and the majority of shareholders' evaluation of subsidiaries, enhance the competitiveness of subsidiaries, and promote the rise of the share price of the subsidiary at the same time. The cost pricing method also has its corresponding shortcomings, depending on the specific cost measurement method selected (for example, when the cost pricing method including opportunity cost is used), it may not truly reflect the ability of the product to bring benefits.

(2) Based on the market

When the transfer price is confirmed under the premise of market-based, the level of the transfer price is mainly determined by the external market price. At this time, multinational companies generally adopt market price pricing method or negotiated pricing method to confirm the transfer price. The common feature of these two methods is that they are based on the principle of fair trade and take the product price in the competitive market as a reference. Compared with the cost pricing method, the transfer price determined under this method is closer to the market price. Compared with cost-based transfer pricing, because the scope of price confirmation has become smaller, the effect of market-based transfer pricing in fund recovery or tax avoidance would be reduced to a certain extent. However, this method can provide effective incentives to subsidiaries, avoiding subsidiaries blindly relying on the parent company's financial assistance through transfer pricing when their financial status is poor, and is conducive to improving the subsidiary's operating performance and enabling the parent company to make changes to the subsidiary.

(3) Based on profit

The profit-based transfer pricing method refers to the use of profit as the basis for the adjustment of transfer pricing. It mainly includes the transaction net profit method and the profit split method. The transaction net profit method uses the profit when an unrelated third party conducts independent and comparable transactions. And the split method uses the profits made by the company in internal transactions with related parties. Compared with the cost pricing method, the profit split method can establish a smaller transfer price range, so the effect of the transfer pricing method is not as significant as the cost pricing method. However, because the profit-based transfer price determination method can effectively reflect the economic benefits brought by the product or labor service, it overcomes the shortcomings of the cost valuation method that cannot objectively reflect the true added value of the product, which is beneficial to the profitability of the product or labor service. To conduct inspections to better allocate resources, so profit-based transfer pricing methods are gradually becoming the choice of more and more multinational companies.

The World Economic Cooperation Organization (OECD) stipulates that when companies conduct transfer pricing of goods or services, they should follow the principle of fair trade and adopt the transfer pricing method permitted by the organization. The transfer pricing methods permitted by the World Economic Cooperation Organization include the following five types: comparable uncontrolled price method, resale price method, cost-plus method, transaction net profit method and profit split method. Among them, the comparable uncontrolled price method, resale price method and cost-plus method prefer to use direct transaction price as the basis for determining the transfer price. Because these three methods are relatively simple to use, and there is a large room for price confirmation, many transnational Companies tend to choose these three transfer pricing methods. The transaction net profit method and the profit split rule use the profit of an unrelated third party in independent and comparable transactions and the profit of the enterprises in internal transactions as the basis for determining the transfer price, then compare and analyze the profit of specific transaction items. Or the division of contribution and residual value to confirm a reasonable transfer price.

4.1.2 Comparable Uncontrolled Price Method (CUP)

The comparable uncontrolled price method refers to the price confirmation of a controlled transaction that purchases, transfers assets, or provides services under comparable conditions (such as the same type of transaction, the same nature of the contract, the same transaction partner, etc.). Take the price of asset purchase, transfer or service provision in a comparable uncontrolled transaction in the same period as a reference. Since this method has a strict definition of comparable objects, and requires that the objects of controlled

transactions and uncontrolled transactions must be related in nature and content closely. It is mainly suitable for comparison of tangible assets or labor services that can be reliably measured, but it is difficult to apply it to the comparison of intangible assets such as trademarks, property rights and patented technologies.

China's 1998 *Regulations on the Tax Administration of Business Transactions between Related Companies* stipulated that the use of the comparable uncontrolled price method must consider the comparability factors between the selected transaction and the transaction between the related companies. These factors include:[19]

(1) The process of buying and selling comparability, including the time and place of the transaction. Such as terms of delivery, delivery procedures, payment terms, the number of transactions, service time and location;

(2) Purchase and sell comparability, including factory sectors, the wholesale segment. Such as retail, export and other sectors;

(3) Purchase and sale of goods comparability, including product name, brand, size, model. Such as performance, structure, appearance and packaging, etc.

(4) The comparability of the buying and selling environment, including social environment (ethnic customs, consumer preferences, etc.), political environment (political stability, etc.) and economic environment (finance, taxation, foreign exchange policies, etc.).

A good example of CUP would be a foreign-invested company invested in China sells 100,000 mobile phones produced to its parent abroad at a price of 500 yuan/unit, although it sells 10,000 mobile phones to a domestic retailer at a price of 800 yuan/unit. Such kind of pricing strategy can be questioned by the tax authorities easily. At this time, how do companies adjust the price of internal transactions between related companies? Companies can make further analysis of sales to related companies and sales to third-party companies from the perspective of the number of product sales, technical support and possible bad debts. For example, because companies sell more mobile phones to related companies than domestic retailers, they get a certain price discount. And because it is within the group, the corresponding marketing expenses and technical support expenses can be minimized. In addition, in the future collection of accounts, the possibility of bad debts between related companies is much lower than that of third-party unrelated companies. Therefore, combining the above factors, the company can appropriately increase the transaction price with the affiliated company, but it is lower than the transaction price of the third party. Even if taxation department raises doubts about this, the company can explain the above factors to it.

[19] State Taxation Bureau [1998] No. 59 Tax Management Regulations for Business Transactions between Affiliated Enterprises

4.1.3 Resale Price Method (RPM)

The resale price method refers to the fact that when an enterprise determines the internal transaction price of the related party, the transaction price when the product is purchased from the related party and then sold to a third party without a related relationship is the main basis for setting the transfer price. This method requires that the purchaser cannot substantially process or increase the value of the purchased products. Therefore, it is mainly applicable to the situation when the buyer purchases finished products. If the purchaser does not purchase finished products from related companies, but purchases production equipment, production technology or production patents, and then produces other products on its own to sell to unrelated third parties, obviously the resale price method cannot be used to confirm its related party transactions.

For example, a Chinese parent company transfers a batch of products to foreign subsidiaries for US$10,000, and the foreign subsidiary sells them locally at a market price of US$15,000. The gross profit margin of sales of similar products sold by foreign subsidiaries to local non-associated companies is 20%, and the Chinese tax authorities adjusted the sales price of the parent company = 1.5 × (1-20%) = 12,000.

American company A sells a piece of equipment to a branch company located in China at a price of 200,000 dollars, and the branch company resells it to an unrelated company C at a price of 180,000 dollars. At this time, the tax authority adjusts the price of the products between the head office and branch companies based on the price it resells to Company C minus the reasonable sales margin. Here, the ordinary reasonable sales gross profit margin of the branch company is 10%, and the reasonable price between the head office should be 162,000 yuan (18-18 × 10%). The tax authority can adjust the purchase price of branch B from company A according to this price.

4.1.4 Cost plus method (CPM)

The cost-plus method refers to a method in which companies mainly base their prices on the actual cost of producing products or providing labor services as the basis for price confirmation, and then determine the transfer price through a reasonable profit addition on this basis, and the reference profit used for the addition is the main reference The gross profit obtained when the enterprise conducts comparable transactions with non-related parties. The guidelines of the World Economic Cooperation Organization indicate that the cost-plus method is mainly applicable to the pricing of internally traded products or services in the absence of comparable uncontrolled price information. In the actual confirmation and measurement of the transfer price, the cost-plus method is mainly derived from the gross profit rate. Add a reasonable gross profit amount to the actual cost incurred by the supplier in

providing the product or service to arrive at a price that complies with the principle of independent trading.

4.1.5 Trading net profit method (TNMM)

Refers to the net profit obtained when a third-party unrelated company conducts the same or similar internal transactions profit, as a benchmark for confirming the profit level of the company when conducting the same internal transactions. The Transaction Net Profit Law requires that both the company and non-associated comparable companies have internal transactions with their respective related parties, and the content, objects and nature of the internal transactions must be similar or even the same. If the above conditions are met, even if the non-associated comparable company is from a country or region different from the company, the transaction net profit method is also applicable. Because the transaction net profit method examines the net profit excluding various financial expenses and income taxes, this method is affected by differences in accounting standards (such as different cost allocations and different income tax rates) compared with the cost-plus method and the resale price method Smaller. This is especially important when comparable companies come from a range of different countries and adopt different accounting standards.

4.1.6 Profit split method (PSM)

The profit split method means that the profits or losses of the entire enterprise are first calculated, and then these profits or losses are distributed among its internal affiliated enterprises according to a certain standard. The profit split method generally aims at splitting the net profit, and the gross profit is split only when the financial expenses of the affiliated company or the income tax payable cannot be confirmed. From the definition of the profit split method, it can be seen that, unlike the transaction net profit method, this method does not need to be directly compared with strictly independent and comparable transactions of unrelated third parties, so it can be mainly applied to cases where there is no independent comparable transaction. In addition, since the profit split method evaluates both parties to the related transaction, the profit result after the split should be a result acceptable to both parties of the related transaction, so as to facilitate profit adjustments as soon as possible. However, the profit split method is very complicated and highly subjective. Using this method usually involves confirming the group profit of a certain related transaction, but it is very difficult to confirm the group profit of a single transaction, and it often involves a large number of costs, expenses and other item. Therefore, the profit split method is mainly applied to transactions with complex background but few related transaction items and relatively closely related transactions.

4.2 Government restrictions - Advance Pricing Method (APA)

Advance Pricing Agreement (APA) refers to that when taxpayers determine the transfer price of controlled transactions in a specific period, they apply to the tax administration department, and through communication and negotiation among taxpayers, affiliated companies and tax departments, they predetermine the applicable standards of controlled transactions (such as methods, comparable appropriate adjustments, key assumptions of future events, etc.), Sign an agreement to decide the transfer price.

Before reaching an agreement with the tax administration on the method of transfer pricing, multinational companies should master their own tax burden and control the possible adjustment of tax burden during the effective period of APA. So as to avoid disputes and disputes caused by different views and positions, eliminate the uncertainty of tax, avoid and reduce the interference of tax collection and management on the normal operation of the company, such as tax inspection, tax litigation, tax levy punishment, etc. The traditional transfer pricing method adopts an ex post adjustment method. There are three difficult problems in this ex post adjustment mode: first, it is difficult to determine the adjusted price, and it is difficult to find an adjustment price that meets the normal transaction standard. Second, it is difficult to provide complete evidence. On the one hand, in order to obtain sufficient information, tax authorities constantly increase the requirements for taxpayers to provide evidence. On the other hand, taxpayers also need to provide a lot of information to prove that their transfer pricing method is in line with the normal transaction price; Third, it is difficult to eliminate the new phenomenon of double taxation. Through the adjustment of enterprise transfer pricing, the taxable income of the adjusted enterprise is increased. However, if the other party's affiliated enterprises do not make corresponding adjustment, it will cause new international double taxation and tax disputes. Therefore, the pre recognition system represented by the APA is the inevitable outcome of the development of the transfer pricing tax system. The introduction of APA has made the transfer pricing tax system with the post adjustment method out of the woods. It can be called a milepost monument in the history of the transfer pricing tax system, indicating that the transfer pricing system has entered a new historical period.

4.2.1 The concept, generation and development of APA

An advance pricing agreement refers to the taxpayer’s application to the tax authority for the transfer pricing method involved in internal transactions and financial transactions between it and overseas affiliates in advance. After the tax authority has reviewed and approved it, it can be used as an accountant for the calculation of income tax. The Organization for Economic Cooperation and Development (OECD) stipulated in the 1995

transfer pricing guidelines: “APA is such an agreement: before the occurrence of controlled transactions, it pre determines a series of appropriate criteria (such as method, comparability number, etc.) for the transfer pricing of these transactions, but stipulates that the criteria are only valid for a certain period of time."

APA was first proposed by Japan in April 1987, which was initially called pre confirmation system (PCS). However, due to the fact that Japan's transfer pricing tax system was just established in 1986, lack of practical experience of transfer pricing tax system, and Japan did not formulate and promulgate perfect rules or regulations for the implementation of PCs, APA developed quite slowly in Japan, and Japan did not promulgate perfect APA guidelines until 1999.

Since the 1980s, the IRS has been actively exploring APA. In June 1990, the draft of the advance rule procedure was published, followed by the signing of the first advance pricing agreement in January 1991. Subsequently, the domestic Revenue Bureau set up the APA project office, which is specially responsible for reviewing, negotiating and signing the APA applications submitted by taxpayers. This marks the emergence of more perfect APA and its institutions in the United States. The changes made to APA in the "tax procedure" and "joint consultation guidance manual" in 1996 are regarded as "a milestone for the development of APA", which makes the whole consultation procedure a big step forward towards cooperation and efficiency. Moreover, in 1998, the United States specially promulgated the APA rules for small enterprises, in order to simplify the procedures and procedures for small enterprises to apply for APA, reduce the cost of applying for APA, and attract small enterprises to join the ranks of APA. The United States has become the fastest developing, most perfect and most operational country in the world.

After the American Internal Revenue Service (IRS) formally implemented APA in March 1991, countries such as Canada, Mexico, Australia, Spain, Germany, the Netherlands, the United Kingdom, New Zealand, Japan and South Korea all subsequently implemented the APA system. Ernst & Young’s 1999 survey showed that more and more multinational companies and tax authorities said they would consider using advance pricing agreements. Ernst & Young’s 2003 survey showed that nearly 20% of the respondents had adopted APA, but 90% of them indicated that they would adopt APA again.

4.2.2 The purpose and basic principles of creating an advance pricing agreement

The purpose of implementing advance pricing agreements is to find a flexible way to solve problems based on cooperation and negotiation between taxpayers and tax authorities, as well as promoting tax payment by reducing uncertainty and improving the predictability of the tax consequences of multinational affiliated company transactions. People voluntarily

obey the tax law, thereby reducing the administrative burden on taxation departments and taxpayers. Specifically, an advance pricing agreement is supposed to be able to achieve the following purposes:

-To enable taxpayers to reach an understanding with tax authorities on three basic issues: (1) the true nature of the inter-company transactions involved in the advance pricing agreement; (2) reasonable transfer pricing methods applicable to these transactions; (3) application The range of effects that these transfer pricing methods can achieve.

- Create a mechanism for mutual understanding and cooperation between taxpayers and tax authorities.

- Solve transfer pricing in a way that is cheaper and more efficient for taxpayers and tax authorities issue..

- Avoid double taxation as much as possible.

Drawing lessons from the APA practices of various countries, the creation of an advance pricing agreement should generally be based on the following principles:

(1)The principle of normal trading

Also known as the arm's length principle which refers to the treatment of transactions between affiliated companies as relations between independent competing companies. The normal transaction principle is the most reasonable basic principle recognized in the field of international transfer pricing anti-avoidance, which is Determine the most important cornerstone of transfer pricing adjustment. The obvious advantage is that it makes related enterprises and non-affiliated enterprises in a fair competitive environment without causing any tax advantages or disadvantages to enterprises and maintaining tax neutrality. Advance pricing agreements are used as a solution, as a means of transfer pricing issues, this principle should also be adhered to, so that transactions between related companies are consistent with transactions between independent companies.

(2)The principle of ease of application

The fundamental purpose of the conclusion of an advance pricing agreement is to quickly negotiate and resolve transfer pricing issues through mutual trust and cooperation between taxation companies and enterprises. Therefore, the program design of advance pricing must conform to the principle of ease of application, and effectively reduce the time and expense spent by both parties on investigation, proof, audit, reconsideration and litigation.

(3)The principle of non-public disclosure of information

Advance pricing emphasizes the mutual trust and cooperation between taxpayers and tax authorities. Taxpayers are obliged to provide tax authorities with all kinds of information related to transfer pricing, including some business secrets; However, the tax authorities must

keep the information provided by the taxpayers confidential and have the obligation not to disclose it publicly. The laws of various countries generally have many restrictive clauses on the disclosure of this information. The OECD model clearly stipulates that taxpayers cannot be arbitrarily audited based on such information; In administrative disputes and judicial proceedings, such information can not be used as evidence for taxpayers to admit a certain situation; The tax authorities should not abuse the information about taxpayers in the unplemented or canceled advance pricing agreements; Moreover, when the tax authorities exchange information with each other according to the terms of the agreement, they can only disclose it according to the provisions of the agreement.

(4)The principle of separate application of agreement

The advance pricing agreement signed by a taxpayer and the tax authority is only applicable to the parties to the agreement, and is not generally applicable to other taxpayers. The application of the agreement to taxpayers of one of the contracting parties is mainly used for transactions in the next year. The general agreement is valid for 3-5 years. If both parties agree, the agreement can also be applied retrospectively to similar issues in previous years of unaudited cases. It should be pointed out that the separate application here only refers to the advance pricing agreement and the entire advance pricing procedure is universally applicable.

(5)The principle of binding both parties

Once an advance pricing agreement is signed, it will be legally binding on any party signing the agreement, not only the taxpayer, but the tax authorities of all relevant countries must abide by the agreement. Of course, the agreement can also be amended, but the relevant procedures must be strictly followed. The binding force of advance pricing agreements on both tax and enterprise parties fundamentally guarantees taxpayers' business reasonable expectations and ultimately benefits the transaction security of the entire society.

(6) The principle of essential legal behavior

There are high procedural requirements for advance pricing agreements. From the beginning of the taxpayer's application to the preparatory meeting, from the taxpayer's advance pricing proposal to the signing of the agreement, there are detailed procedural requirements, and there must be written materials and so on.

(7) Voluntary principle

Advance pricing agreements emphasize the voluntary participation of taxpayers. It is first applied by the taxpayer voluntarily, and the taxpayer is the initiator of the whole procedure of advance pricing. It can be said that the key to opening advance pricing is in the hands of taxpayers. Without the voluntary activation of taxpayers, the tax authorities cannot take the initiative, let alone force taxpayers to negotiate advance pricing. Before reaching an

advance pricing agreement, taxpayers have a right to withdraw from the advance pricing agreement process at any time for any reason.

(8) The principle of information equivalence

All tax authorities participating in the signing process of the double (multi) side advance pricing agreement are in the same position in terms of information acquisition. The additional information given by the taxpayer to the tax authorities must be notified to other relevant tax authorities. Once the informed tax authorities request for information, the taxpayer must submit it.

4.2.3 Procedures and contents of advance pricing agreements

The signing of an advance pricing agreement generally involves the following steps:

1. Preliminary stage: research and strategy. Taxpayers should conduct special research on the pros and cons of applying for advance pricing, prepare appropriate strategies, and reserve the right to decide whether to seek advance pricing agreements. The data accumulated in the research will also play a role in future tax authorities' investigations on transfer pricing.

2. Pre-application. After economic analysis, if the company thinks it is necessary to APA with the tax authority, the company should make an appointment with the tax authority and conduct a pre-application consultation meeting with the tax official before filling out the form. The purpose of the meeting is to evaluate and decide whether signing an advance pricing agreement is beneficial to taxpayers. This link is an important aspect of the advance pricing agreement procedure. It can provide the applicant company with an opportunity to create a good first impression in front of the tax authorities of both countries.

By demonstrating the rationality of the method and reasonable interpretation of the observable facts in the preparatory analysis, the company can create a positive atmosphere for negotiation, which will help solve the difficulties that may arise in the future process. Regarding the appropriateness of the cost and burden of APA, to a large extent depends on the success of the pre-application meeting.

3. The formal application stage. After the pre-application negotiation meeting, if the taxpayer decides to formally apply for an APA, the company must submit a formal APA application. Tax authorities in some countries charge certain fees. For example, the US requires taxpayers to pay US$5,000-25,000 in application fees. The tax-paying company shall submit relevant materials and explain to the relevant competent authorities on previous or current taxation issues as part of the taxpayer’s request to sign the APA to the taxation authority if they want to apply.

4. Evaluation and negotiation. After the tax authority receives the advance pricing declaration materials of the applicant company, it shall conduct a detailed review of these

materials and then evaluate the taxpayer's suggestions. In this process, the APA negotiator of the applicant company will work with the negotiation team of the tax authority to ensure that the tax authority understands the content of the proposed APA, the reason for the transfer pricing measure and the principle of how to achieve a fair price. The transfer pricing method proposed by the applicant company may not be fully approved by the tax authorities, and sometimes needs to be changed. Once the tax authority is satisfied with the handling of the issue, the negotiation will move from the assessment to the negotiation stage. In the negotiation, if the two parties can reach a consensus on the differences in the APA, a draft of the APA can be formed.

5. Sign an advance pricing agreement. After the tax authority approves the taxpayer's application, both parties must sign a formal advance pricing agreement and implement this agreement. Once signed, the advance pricing agreement has legal effect. If there are no special circumstances that need to be revised, both parties must strictly implement the agreement.

6. Follow-up supervision. During the implementation process, the taxation department will carry out follow-up supervision and management. The taxation department mainly adopts annual reports and audits to supervise the performance of taxpayers. Taxpayers should provide the tax authorities with an implementation report of APA every year, and keep relevant original materials and accounting vouchers for inspection by the tax authorities.

At the same time, the existence of advance pricing agreements does not prevent the tax authorities from taking audit actions in the future, but the subject of the audit is limited to the extent to which the taxpayer fulfills the conditions of the arrangement, as well as whether the selected pricing method depends on the applicable circumstances and whether the assumptions continue to exist .

7. Update and revision. If a major change occurs in the production and operation of an enterprise, which makes the original key assumptions no longer applicable, taxpayers must report to the tax authorities in a timely manner and apply for necessary amendments.

The core of the advance pricing agreement is to reach an agreement on the transfer pricing method and the transfer price calculation method adopted by the taxpayer's transfer pricing transaction, so as to ensure that the tax authority obtains a satisfactory tax declaration. Its content is determined around this core. Advance pricing agreements can appear in any form acceptable to taxpayers and tax authorities, but they should usually include the following: (1) Related parties; (2) Related party transactions and tax year or accounting period involved; (3) Transfer pricing Adjustment method; (4) Agreement clause setting and valid period; (5) Definition of related terms; (6) The important assumptions on which the law is based; (7) The

calculation method used by the taxpayer; (8) The taxpayer's obligations, including annual reports, record keeping, notification of changes in assumptions, etc; (9) The legal effect of the agreement, the confidentiality of the documents submitted by the taxpayer and the information exchanged; (10) Mutual liability clause; (11) Amendment of agreement; (12) Ways and methods for resolving disputes.

According to the parties participating in the negotiation, advance pricing agreements are divided into unilateral agreements, bilateral agreements and multilateral agreements. A unilateral agreement is an agreement signed in advance between a taxpayer and its tax authority regarding the tax treatment and tax requirements that the taxpayer and its international affiliates enjoy when conducting transfer pricing activities. Bilateral agreements are advance pricing agreements reached between taxpayers and the tax authorities of two different countries. A multilateral agreement is an advance pricing agreement reached between a taxpayer and the tax authorities of three or more national governments. It essentially involves an agreement between tax authorities, but it still requires the full participation of the taxpayer.

4.2.4 Analysis of the advantages of APA

(1) Solve the transfer pricing problem in one or several countries at the same time to maintain the certainty of taxpayers' operations. Advance pricing agreements may be the best way to resolve transfer pricing issues in one, two or more countries. Advance pricing agreements can help multinational companies obtain safe transfer pricing results in their global taxation plans and enhance the predictability of operating results. By reaching an agreement, taxpayers can know exactly how the tax authorities are going to react to transfer pricing in their own business activities in the future, if it is a bilateral agreement, taxpayers can also know the reaction of foreign tax authorities to their own transfer pricing activities. On the other hand, it can protect the reasonable tax rights they deserve for tax authorities.

(2) Help solve the problem of double taxation

A double (multiple) advance pricing agreement can effectively solve the problem of double taxation of multinational companies, provided that the two parties to the contract can reach an agreement on the same transfer pricing issue.

(3) Reduce the risk of transfer pricing investigations

The conclusion of APA has a possibility limit the investigation work of tax authorities to the inspection of taxpayers' implementation of the terms of the agreement, so that multinational companies will not be subject to detailed investigation on transfer pricing within the term of the agreement.

(4) Reduce costs and risks in the transfer pricing process and improve efficiency.

The taxpayers who apply for APA usually make a decision on the basis of detailed analysis. The adoption of APA is based on the consideration of cost-effectiveness ratio. Generally, it will only be adopted when it is beneficial for taxpayers to reduce the overall cost and improve the overall efficiency. On the surface, the negotiation of advance pricing is usually less hostile, so it usually takes less time to reach an agreement than to defend to the tax authorities, and it helps taxpayers to understand the tax authorities' preference for pricing methods and the possible adjustment direction, which is conducive to tax payers to make correct decisions. From the perspective of tax authorities, due to the active participation and cooperation of taxpayers and the provision of detailed information in the process of the agreement, it helps tax authorities to have a more in-depth and accurate understanding of taxpayers' transfer pricing issues, which is more effective than the unilateral investigation of tax authorities, thus improving the ability and efficiency of tax authorities to solve transfer pricing issues.

(5) Reduce the annual workload of taxpayers supporting transfer pricing.

Advance pricing agreements can greatly reduce the burden of taxpayers on retaining original vouchers and documents. After the taxpayer has reached an agreement with the tax authority, it is only necessary to retain the original information related to the reasonable transfer pricing method. Documents related to other methods are not necessarily retained. In the past, the tax authority often had to adjust the transfer pricing inspections. Read it, so it must be saved. On the other hand, advance pricing agreements can also enable tax authorities to obtain taxpayer information in a cheap way.

(6) The advance pricing agreement can enable both parties to avoid litigation disputes.

If there is no advance pricing agreement, taxpayers may be subject to transfer pricing investigations by tax authorities, and disputes between the two parties may arise, and even lawsuits by tax authorities. On the other hand, tax authorities' transfer pricing adjustments to taxpayers cannot be subject to taxpayers' Acceptance may also result in litigation by the tax authority. Such examples are not uncommon in the United States. Advance pricing agreements can avoid all these disputes.

4.2.5 Issues to be resolved in the implementation of APA

(1) Confidentiality

APA is an administrative contract, so it must be established on the voluntary basis of the parties. Its important function is to improve the efficiency of the transfer pricing review by sending the information asymmetry in the transfer pricing review. However, most of the taxpayer's private information is a business secret, which should be protected by law within a certain range, otherwise it will dampen the taxpayer's confidence and enthusiasm to

participate in APA. Therefore, in order to enhance the attractiveness of APA to taxpayers, appropriate legal means must be used to keep the taxpayer's information materials in the APA procedure confidential. For this reason, many countries attach great importance to the issue of APA confidentiality, which is reflected in their APA legislation in recent years, but the concerns of taxpayers have not been eliminated. The practice in the United States shows that the issue of APA confidentiality is a controversial area at present and in the future. In a case of 1999, the Federal Court required the Internal Revenue Service (IRS) to submit a large number of established APAs to the court for evidence review. From the perspective of the development of the APA system, the IRS was reluctant to disclose this information.

This case has aroused a wide controversy on APA confidentiality in the United States. Although the bill was finally approved by Clinton on December 17, 1999, the voice of opponents is still very high. They think that the legislation of Congress does not fully consider the opinions of all walks of life, and warn that "doing so will make APA out of the supervision of the public and Congress".

From an international perspective, the confidentiality issue of APA will be more important and complicated. The business activities of multinational companies are transnational and global. They not only hope that their trade secrets will be protected by the laws of their home countries, but they also hope that they will be protected uniformly on an international scale. Therefore, when adopting bilateral or even multilateral APAs, it is convenient for them to keep information confidential. Become an important factor considered by multinational companies. However, international practice is still quite lacking on this issue. Although the tax information confidentiality clause contained in some bilateral tax treaties can be applied to APA, it is still far from enough. In a specific bilateral APA, even if the tax authorities of various countries can provide certain guarantees for information confidentiality, such guarantees can only be based on the APA confidentiality standards recognized by the domestic laws of each country, and it is difficult to meet the requirements of multinational companies fully. Regarding the issue of APA's confidentiality, The most fundamental difficulty in APA's confidentiality is that there is no and no international uniform standard.

(2) Internationalization

Transfer pricing is a global tax issue. If APA is limited to one country, its development space will be extremely limited. Recent international practice has shown the internationalization trend of APA system. The APA legislation of many countries has made provisions on bilateral APA, among which France is the most typical. France issued a new APA rule in September 1999, which stipulates that taxpayers can only apply for bilateral APA, and the other party of bilateral APA is limited to the countries with which France has signed a

bilateral tax agreement, and the tax agreement must contain provisions similar to article 25-3 of the *1992 OECD Model bilateral tax treaty*.

The OECD issued guidelines on multilateral APA negotiation procedures in October 1999, stating: APA should be reached on a bilateral or multilateral basis through the multilateral negotiation procedures of the corresponding treaty whenever possible. It can be seen that the current APA system is gradually developing to solve the problem of transfer pricing by combining international law with domestic law. The internationalization process of APA ultimately depends on the degree of agreement between countries on the adjustment method of transfer pricing. Therefore, it is necessary to ensure that dialogue and consensus can be reached between developed and developing countries on the basis of respecting sovereignty, equality and mutual benefit.

4.3 Adjustment rules of transfer pricing

4.3.1 Principles of transfer pricing adjustment

The standard formulation of the OECD "Arm's length principle" is embodied in Article 9 Section 1 of the *OECD Model Agreement on Taxation of Income and Property*:[20] "When an enterprise of one Contracting State directly or indirectly participates in the other Contracting State The management, control or capital of the enterprise, or the same person directly or indirectly participates in the management, control or capital of the enterprise of one of the contracting states and the enterprise of the other of the contracting states. And in any of the above cases, there is a commercial or financial relationship between the two enterprises The transaction conditions reached or imposed by the independent enterprise are different from the transaction conditions reached between independent enterprises. At this time, the profit that should have been obtained by one of the enterprises but did not obtain due to these conditions can be included in the profit of the enterprise, and then Taxation". Today, the arm's length principle[21] has been accepted and adopted by most countries in the world. Under the premise of comparable transactions, the arm's length principle can effectively solve the problem of transfer pricing and anti-tax avoidance. The adjustment principle adopted by China in dealing with the distribution of income and expenses among related enterprises is the arm's length principle.

[20] OECD -<Model Agreement on Taxation of Income and Property>-https://www.oecd.org/tax/treaties/oecd-model-tax-convention-available-products.htm

[21] OECD iLibrary-The Arm's Length Principle - https://www.oecd-ilibrary.org/taxation/oecd-transfer-pricing-guidelines-for-multinational-enterprises-and-tax-administrations-2010/the-arm-s-length-principle_tpg-2010-4-en

4.3.2 Transfer pricing adjustment method

The use of transfer pricing by multinational companies to avoid taxation harms the tax interests of relevant countries and undermines domestic competition and fairness. In order to protect national rights and interests, countries have begun to adjust various transfer pricing behaviors of multinational companies. There are two main types of adjustment methods, one is the transaction-based separation accounting method (SA), and the other is the profit-based formula distribution method (FA).

(1) Separation Accounting (SA)

Separated accounting methods are mainly divided into the following five types: comparable uncontrolled price method (CUPM), resale price method (RPM), cost plus method (CPM), profit split method (PSM), transaction net profit method (TNMM) . The comparable uncontrolled price method, also known as the market price method, is used to identify comparable prices between independent third-party transactions. It is the most direct and ideal method to establish or test the transfer price between a low-cost subsidiary and a parent company. According to the second paragraph of *Article 111 of the Implementation Regulations of the Enterprise Income Tax Law of China*: The resale price method refers to the price at which goods are purchased from related parties and then sold to non-related parties, minus the same or similar method of pricing the gross profit of the business according to the first paragraph of Article 111 of China's *Regulations on the Implementation of the Enterprise Income Tax Law*[22]:

The method of pricing in accordance with cost plus reasonable expenses and profits. This method is usually suitable for adjusting the profit distribution between manufacturers and service providers. the profit split method is guided by the principle of normal transactions, based on the functions, risks, and assets performed by several affiliated companies in the transaction. Invest in the transfer pricing method that adjusts the final consolidated profit and loss. The transaction net profit method mainly evaluates the net profit rate obtained by the taxpayer from the controlled transaction based on cost, sales, assets, etc., including: asset income rate, full cost plus rate, sales profit rate, Berry ratio, etc., to adjust the final price of transfer pricing.

(2) Formula distribution method (FA)

In the practice of transfer pricing anti-tax avoidance management, the implementation of the above five methods requires a lot of human, financial and material resources. At the same time, due to the lack of negotiation between various countries, it is easy to adopt the same

[22] 《Regulations on the Implementation of the Enterprise Income Tax Law of the People's Republic of China》-http://zwfw-new.hunan.gov.cn/hnvirtualhall/zcwj/detail.jsp?xh=A6B2373E2250CAE7E053651515AC88DA

method for the same transaction, resulting in repeated tax collection or leakage Close. Therefore, on the basis of practice, many countries have begun to test a new adjustment method — the formula distribution method. Now calculate the global pre-tax profit of multinational companies in the same way, and then assign corresponding weights to different indicators based on different indicators, such as asset amount, sales, and worker wages, which can be asset amount (1/3), sales (1/3) , wages (1/3), assets (1/4), sales (1/2), wages (1/4), or just refer to one of the indicators, and percentages between each country Make an assignment. Now the United States, Canada, and Switzerland have gradually explored this approach in practice, but this approach requires the relevant countries involved to recognize the relevant proportional distribution, which requires the active participation of all parties to achieve good implementation results.

(3) Evaluation of transfer pricing adjustment methods

The choice of the appropriate transfer pricing adjustment method depends on the results of the comparability analysis. The comparable uncontrolled price method requires a high degree of comparability between the assets or services transferred in the two transactions that need to be compared. These comparability include multiple factors such as the purchase and sale process, links, goods and environment. This method is more difficult to operate, and methods are not suitable if one factor does not meet. The resale price method is generally only for the profit adjustment of the manufacturer or distributor, and the product or service is simply processed or simply purchased and sold, and there is no value-added change, and the cost-plus method is suitable for the manufacturer The cost of purchasing from non-related parties and selling to related parties is comparable to the cost of uncontrolled transactions, the profit split method requires more comprehensive information in actual operation, including the specific circumstances of the entire transaction, involving multiple entities. However, these data are difficult to obtain in other jurisdictions. Compared with the traditional method, the transaction net profit method uses operating profit, which is less affected by the difference in transaction functions, and has an impact on the function of controlled transactions and uncontrolled transactions. In addition, the required relevant information can be obtained from the financial information in the financial statements published by listed companies, and the dependence on information in other jurisdictions is weak.

In China, the transaction-based approach should be considered in preference to the profit-based approach. *State Tax Development (1998) No. 59*[23] pointed out: "When the comparable uncontrolled price method, resale price method and cost-plus method adjustment

[23] State Administration of Taxation [1998] No. 155 Notice of the State Administration of Taxation on the Determination of the Scope of Living Subsidies - https://www.shui5.cn/article/a9/27430.html

methods are not applicable, other reasonable alternative methods can be used for adjustment." However, China's current transfer pricing adjustment method is mainly biased towards the transaction net profit method in the profit-based method. This is due to the relatively high requirements for the integrity of information under the transaction-based method, which is difficult to achieve in actual operations. The formula distribution method based on profit has higher requirements for international cooperation and negotiation. China has not adopted it at present, but in the future, it can learn from the experience of countries that have adopted this method and try boldly.

4.4 Current management status of anti-tax avoidance on transfer pricing in China

Since China's accession to the World Trade Organization in 2001, China's economy and society have been more rapidly, deeply and fully integrated into the world economy than before, the conflicts of taxation interests between various countries have intensified,with economic development and international trade activity's increasing. In order to alleviate tax conflicts, promote the development of international trade and strengthen international cooperation, many countries have signed international tax treaties which is a bilateral agreement made by two countries to resolve issues involving double taxation of passive and active income of each of their respective citizens.[24]

China has also signed a large number of tax treaties with other countries. Specifically, China has officially signed 109 tax treaties with foreign countries, and 102 of which already come into effect, as of the end of October 2018, that reducing the tax burden of "going out" and "bringing in" enterprises effectively.[25]

With the development of international exchanges, China has further expanded the introduction of foreign capital and advanced technology, and its taxation relationship with other countries has become closer. It requires the signing of tax treaties with other countries to actively, steadily and standardly resolve international double taxation.

However, multinational enterprise groups still try to minimize the overall tax burden of the group through pricing arrangements for related party transactions within the group. This method causes losses to the country and other enterprises. Based on this, the tax authorities of various countries have tried lots of means to ensure that their own tax benefits are not lost. They supervise transfer pricing issues by formulating relevant regulations and conducting transfer pricing audits. The construction of China's transfer pricing anti-avoidance laws and regulations has gone through an exploratory stage and a development stage since 1987.

[24] Tax Treaty Definition - Investopedia-https://www.investopedia.com/terms/t/taxtreaty.asp
[25] CBN(30/11/2018)-"China signed 109 tax treaties with foreign countries, effectively reducing corporate tax burden"

Finally, the anti-avoidance work of the Chinese tax authorities embark on a standardized road and entered a more mature and standardized stage. China's legal system on transfer pricing is mainly composed of laws, regulations, rules and a series of double taxation agreements signed with other countries.

4.4.1 The status quo of Legal system of transfer pricing and anti-tax avoidance

The Shenzhen Municipal Government of China promulgated the "Interim Measures for the Tax Administration of Transactions between Foreign-invested Enterprises and Related Companies in the Shenzhen Special Economic Zone"[26] in November 1987, marking the starting point of China's transfer pricing tax system. The reason is that the city, Shenzhen, as a special economic zone, became a relatively concentrated area for foreign investment due to its loose investment environment and preferential tax policies in 1987. However, because of the imperfect of China's tax laws, the methods of collection and management were still relatively backward, and the quality of tax personnel was not high overall, a large number of foreign-funded enterprises transferred their profits to foreign countries through transfer pricing methods, resulting in a large loss of tax revenue in China.

The *Income Tax Law of the People's Republic of China on Foreign-invested Enterprises and Foreign Enterprises* passed in 1991[27] is the earliest official transfer pricing regulation in China, and Article 13 stipulates that foreign-invested enterprises or foreign enterprises' establishments in China to engage in production and business operations, The business transactions between the site and its affiliated enterprises shall be in accordance with the business transactions between independent enterprises to collect or pay prices and expenses. If the taxable income is not collected or paid in accordance with the business transactions between independent enterprises, and the taxable income is reduced, the tax authority has the right to make reasonable adjustments.[28] Consequently, this provision gives China a legal basis for the management and control of tax avoidance by transfer pricing by multinational companies, and marks the beginning of China's implementation of a transfer pricing tax system in foreign tax management. Furthermore, the *Detailed Rules for the Implementation of the Income Tax Law of the People's Republic of China on Foreign-invested Enterprises and Foreign Enterprises* (1991) [29] set out specific provisions on the tax treatment of affiliated

[26] Effective on January 1, 1988, the State Administration of Taxation of the Ministry of Finance on January 4, 1988 forwarded the above interim measures to the country for reference and implementation in "(87) Caishuiwaizi No. 376" on January 4, 1988.

[27] The "Income Tax Law of the People's Republic of China on Foreign-invested Enterprises and Foreign Enterprises" adopted by the Fourth Session of the Seventh National People's Congress on April 9, 1991 and the "Interim Regulations on Enterprise Income Tax of the People's Republic of China" promulgated by the State Council on December 13, 1993 "Abolished at the same time in 2008.

[28] http://www.mohurd.gov.cn/zcfg/fl/200611/t20061101_159482.html

[29] This regulation will be repealed at the same time as the "Enterprise Income Tax Law of the People's Republic of China" comes into effect on January 1, 2008

enterprises, clarified the standards for the identification of affiliated enterprises' business dealings, and the requirements for the provision of materials, and The adjustment method of the transfer price is proposed for related purchase and sales business, financing funds, provision of labor services, transfer of property, and other businesses that are not priced according to the business transactions between independent enterprises.The *Detailed Rules for the Implementation of the Tax Collection and Management Law of the People's Republic of China* promulgated in 1993 is China's first tax management method that specifies the detailed rules from tax registration to tax collection.[30]

In 1998, the State Administration of Taxation issued the *Notice of the State Administration of Taxation on Further Strengthening the Administration of Transfer Pricing Taxes* [31]which is carried out in order to correct and overcome the management of transfer pricing tax extreme imbalance between regions and it is the only one that contains the term "transfer pricing tax administration" among the transfer pricing tax issues issued by the State Administration of Taxation at that time. In addition, the State Administration of Taxation issued the *Regulations for the Tax Administration of Business Transactions between Related Companies (Trial)*[32] in April 1998 which is regarded as the crystallization of China's practical experience and marks the systematic acquisition of the transfer pricing tax system. The regulations have a total of 12 chapters and 52 articles, including the identification of related parties and the declaration of business transactions, the identification of business transactions between related companies, reconsideration and litigation, filing and filing of case files, tracking management, etc., which greatly enriched the content of the transfer pricing tax system in China.

Subsequently, China entered the development stage of the transfer pricing tax law. For example, the National People's Congress passed the *Income Tax Law* in 2007[33], Chapter VI of it provides "special tax adjustment" specifically, mainly for transfer pricing and general anti-avoidance behaviors. In terms of adjusting the internal transaction prices of foreign-funded enterprises and their affiliates, collecting income tax, and verifying profits, the Income Tax Law draws on The Arm's Length Principles generally adopted internationally, improves the original transfer pricing and advance pricing laws and regulations, and strengthens transfer pricing adjustments. For the first time, China has formed a comprehensive anti-tax avoidance

[30] In accordance with the State Council Order No. 362 of 2002, the implementation rules of the Tax Collection and Administration Law of the People's Republic of China, the full text of this regulation shall be repealed from October 15, 2002.
[31] National Tax Development Bureau [1998] No. 25
[32] Replaced by "The Tax Collection and Management Law of the People's Republic of China" (2001) and the "Detailed Rules for the Implementation of the Tax Collection and Management Law of the People's Republic of China" (2002)
[33] Adopted at the Fifth Session of the Tenth National People's Congress on March 16, 2007

law, which has become the legal basis for cracking down on various tax avoidance activities in the future.

In 2009, the *Notice of the State Administration of Taxation on Printing and Distributing the Implementation Measures for Special Tax Adjustments (Trial)*[34] made a more detailed supplement to the Income Tax Law. By learning from the experience of Western countries, the tax law includes all aspects off transfer pricing related matters. It is the most complete transfer pricing regulation in China so far, and it's a core regulation of China's transfer pricing as well, which laying a good foundation for China's transfer pricing to gradually mature. Since then, the State Administration of Taxation has successively promulgated some regulations to continuously strengthen the transfer pricing theory. in other words, these laws and regulations have formed anti-tax avoidance management guidelines and legal frameworks covering various legal levels, and provided a legal basis for tax authorities to enforce the law.

In 2011, the Chinese tax authorities issued the *Notice of the Ministry of Finance and the State Administration of Taxation on Printing and Distributing the Interim Measures for the Administration of Anti-Tax Avoidance Special Funds*, which regulates how to use anti-avoidance funds and fund performance evaluation. Then, the State Administration of Taxation, combined with China's transfer pricing management, advance pricing arrangement management, cost sharing agreement management, controlled foreign enterprise management, thin capitalization management, and general anti-avoidance management, and other special tax adjustment work practices, formulated the "*Notice on Special Tax Adjustment Internal Working Procedures (Trial)*" (2012). Simultaneously, it was replaced by the State Administration of Taxation on the issuance of the "Special Tax Adjustment Internal Working Procedures" in the year of 2016. What is particular, transfer pricing investigation cases involving tax reimbursements of more than 10 million yuan, cases involving cost-sharing management and cases involving Cases managed by controlled foreign companies are defined as major cases.

On the whole, China's anti-tax avoidance laws and regulations for multinational companies can be summarized as table 4-3 Laws and regulations of anti-avoidance in China.

Table 4-1 Statistical Table of the Methodology Survey of Chinese Multinational Corporations' Tax Planning for the Establishment of Transfer Prices

	regulation	comment
1991	Income Tax Law of the People's Republic of China on Foreign-invested Enterprises and Foreign	The first laws and regulations for

[34] http://www.chinatax.gov.cn/n810341/n810765/n812166/n812652/c1189827/content.html

	Enterprises	international tax avoidance
1991	Detailed Rules for the Implementation of the Income Tax Law of the People's Republic of China on Foreign-invested Enterprises and Foreign Enterprises	Clarified the identification standards for related business transactions
1993	Detailed Rules for the Implementation of the Tax Collection and Management Law of the People's Republic of China	The first tax management method that specifies the detailed rules from tax registration to tax collection
1998	Notice of the State Administration of Taxation on Further Strengthening the Administration of Transfer Pricing Taxes	A document that first mentioned the term "transfer pricing tax administration"
1998	Regulations for the Tax Administration of Business Transactions between Related Companies (Trial)	Systematic Signs of the Transfer Pricing Tax System
2006	Working Regulations for International Tax Information Exchange	Strengthen international tax cooperation
2007	Income Tax Law	Important anti-avoidance laws
2009	Notice of the State Administration of Taxation on Printing and Distributing the Implementation Measures for Special Tax Adjustments (Trial)	Advance Pricing Arrangement Matters
2011	Interim Measures for the Administration of Special Funds for Anti-Tax Avoidance	Proposed to train professional tax talents
2012	The State Administration of Taxation on Printing and Distributing Internal Working Procedures for Special Tax Adjustments (Trial)	Anti-Tax Avoidance Funds and Fund Performance Evaluation
2016	Special tax adjustment internal working procedures	Top ten important cases

The implementation of the "Enterprise Income Tax Law of the People's Republic of China" is conducive to China's better anti-tax avoidance work and has played a very important role in China's anti-tax avoidance work. Especially, it has improved the relevant anti-avoidance clauses in light of the actual situation in China, which not only expands the scope of anti-avoidance investigations, but is also easy for tax officials to operate and apply in

tax collection and management. The following describes in detail the comparison between the new special tax adjustment in Chapter VI of the new corporate income tax law and the old one.

(1)Two adjustment methods have been added, trading net profit method and profit split method:

The new corporate income tax law expands the scope of application of the arm's length principle. The new law stipulates that all business transactions between related enterprises can be applied to the arm's length principle. In contrast, the old law only applies to collections or receipts due to business transactions. The payment of the price has limitations.

The new corporate income tax law clarifies the powers of the tax authorities, and the tax authorities have the power to adjust unreasonable income arising from related transactions.

The new corporate income tax law adds provisions on intangible assets and labor services. Without a doubt, provisions should be made in accordance with The Arm’s Length Principles, which increases the prevention and adjustment of the use of intangible assets to avoid taxation.

(2) The new enterprise income tax law adds an advance pricing arrangement system

The concept of advance pricing has been explained above. The conclusion can be drawn that advance pricing means that taxpayers apply to the tax authorities in advance before transacting with related companies. Both parties use certain procedures and standards to negotiate prices for transactions with related companies in the future to avoid occurrences. Advance pricing is considered to be the most effective way of anti-tax avoidance of transfer pricing. The traditional transfer pricing system only focuses on adjustment after the fact. In advance pricing, the post-adjustment is changed to an agreed price in advance, which can more effectively prevent multinational taxpayers from avoiding tax, and can avoid or eliminate double taxation on multinational taxpayers. Such rules can enable multinational affiliated companies to have a reasonable expectation of the taxation of their business activities, thereby promoting the transaction activities of multinational companies.

(3) The tax authority has improved the management system

The obligation of enterprises to submit annual transactions and statements of related enterprises to the competent tax authority is added to The new Enterprise Income Tax Law. This provision emphasize the obligation of enterprises to submit relevant business information of their affiliates, which is beneficial to the competent tax authority in a timely manner Master the business dealing information between related companies, and conduct necessary supervision and management of the transaction activities of related companies.

What’s more, the new Enterprise Income Tax Law stipulates the investigation power of the competent tax authority. Accordingly, The tax authority has the power to obtain

information when conducting related investigations. In this way, the tax authority is more proactive in anti-tax avoidance investigations than before, because information obtain channels are increasing.

Finally, punishment would be done if companies provide relevant information inappropriately.

4. Prior to the promulgation of the Corporate Income Tax Law, China's tax laws and administrative regulations only involved the regulation of transfer pricing, and the regulation of tax havens has not yet been touched. For this reason, the inclusion of the regulation of tax havens in the Corporate Income Tax Law is a major step in China's anti-tax avoidance measures, and it is also the beginning of China's relevant laws and administrative regulations to improve further the tax haven tax system.

5. The Corporate Income Tax Law has added new regulations on the evasion of tax obligations by relevant companies through thin capitalization, which is a manifestation of China's new version of corporate income tax law to strengthen anti-tax avoidance measures. China uses the fixed ratio method and clearly stipulates in the law that the debt-to-equity ratio restricts thin capitalization, that is, the safe harbor rules adopted by most countries in the world, they are more rigid and transparent compared with the normal transaction law (independent enterprise principle).

6. The new version of the Corporate Income Tax Law adds tax adjustment regulations. If the taxpayer needs to levy additional tax, in addition to the additional tax, interest must also be added. Therefore, this regulation not only clarifies the power of tax authorities in tax adjustments, but also clarifies the measures that can be taken to increase interest in the collection of supplementary taxes. In general, this provision not only guarantees the taxation interests of the country, but also protects other taxpayers in good faith.

4.4.2 The implementation status of advance pricing management

Among all the tax management rules just mentioned, because transfer pricing is one of the most important parts of anti-tax avoidance management, there are also very clear rules regarding advance pricing. Solving transfer pricing issues and potential transfer pricing disputes through advance pricing management cooperation will help reduce the management costs and energy input of tax authorities, as well as help companies reduce transfer pricing risks. From the perspective of tax management, the State Administration of Taxation recognizes the use of mutual cooperation (such as bilateral advance pricing, etc.) to improve the efficiency of tax collection and management. It also recognizes a bilateral or multilateral advance pricing that involves a tax treaty country (region) signing. Arrangement is an effective tool to improve the certainty of overall tax distribution. According to the *China APA*

Report (2013)[35] issued by the State Administration of Taxation on December 5, 2014, we can see the current status of China's APA implementation from 2005 to 2013. The 2013 annual report is mainly focused on the State Administration of Taxation [2004] No.118 (*APA Implementation Rules for Business Transactions between Affiliated Enterprises (Trial)* and the sixth chapter of [2009] No. 2 (*Special Tax Adjustment Implementation Measures (Trial)*) .

Chinese tax authorities increased investment of APA, and the number of signings increased as well, which has improved the tax certainty of multinational taxpayers. In particular, the promotion of unilateral APA and its retrospective mechanism not only solves the transfer pricing problem of taxpayers in previous years, but also provides tax certainty for future years, which is conducive to the stable development of multinational taxpayers in China. In more detail, transfer pricing in the past was mainly based on investigations. But investment transfer pricing has focused more on management and services in the recent years. Taxation authorities and taxpayers are more inclined to resolve transfer pricing risks through harmonious cooperation. Unilateral APA also becomes one of the important options. More than it, some provincial and municipal tax authorities simplified the working procedures of unilateral APA, encouraging more taxpayers to use this method to solve transfer pricing problems.

In terms of bilateral APA, even in the case of the COVID-19, tax authorities continue to negotiate with tax authorities of other countries. They maintain communication with relevant national tax authorities through online methods to provide more possibilities for achieving bilateral APA actively.

From the quantitative point of view to reach, Chinese tax authorities signed a total of 21 cases of APA in 2019, 12 cases of unilateral, bilateral in 9 cases, a record high since 2009. From the perspective of industry distribution, the APAs signed between 2005 and 2019 are dominated by manufacturing, with a total of 141 cases, accounting for 80% of the total. Although the number of APA signings in the wholesale and retail industry is only 18, accounting for 10%, it has shown a clear growth trend in the past two years. With the diversification of the Chinese economy and the further opening of the market, KPMG expects that the number of APAs involving the service industry and other types of industries will further increase in the future.

Among the APAs signed by China from 2005 to 2019, tangible asset use rights or ownership transfer accounted for 60.66% of all related-party transactions, and intangible asset use rights or ownership transfers and labor transactions accounted for 17.62% and 21.72%

[35] http://www.chinatax.gov.cn/n810219/n810724/c1371141/part/1371156.pdf

respectively. And the most commonly used transfer pricing method is the transaction net profit method, used 165 times, accounting for 79.33% of all methods.[36]

Compared with the data from 2005 to 2018, among all the types of related transactions involved in China's signed APA, the proportion of rights or ownership transfer of tangible asset has declined. Different from this, the proportion of rights or ownership transfers of intangible asset has decreased. In recent years, China's intangible asset transactions and labor service transactions have gradually increased the proportion of all related transaction types involved in the signed APA. With the development of China's tertiary industry, it is expected that more service companies would apply for APA. What's more, APA will also involve more intangible asset transactions and labor service. It is worth noting that although manufacturing companies have signed the largest number of APAs, in recent years, the number of APAs signed by leasing and business service companies, wholesale and retail companies has shown a significant growth trend. It is foreseeable that as the Chinese tax authorities have in-depth understanding and rich practical experience of transfer pricing issues in more industries and transaction types, the application of APA by entities other than the manufacturing industry may be smoother.

According to *The Arrangement Annual Report of China Advanced Pricing (2019)*[37] , the transaction net profit method is still the most widely applicable transfer pricing method. However, as the types of related transactions involved in APA become more diversified, the transfer pricing method is also showing a diversified trend. Various transfer pricing methods are used in APA. For example, five of all the APAs signed in 2019 were used the profit split method. The greater use of the profit split method reflects that Chinese companies occupy a more important position in the global value chain and play a more important role in core value creation activities such as business decision-making, technology research and development, and market development. Therefore, on the basis of mastering the relevant key points of the transaction net profit method, the enterprise can also pay attention to other transfer pricing methods, and finally select the appropriate transfer pricing method based on the functional risk borne by the enterprise itself, financial services and financial asset transfer transactions in the future.

In terms of completion time, under normal circumstances, the goal of the Chinese tax authorities is to complete the review and negotiation of unilateral APA within 12 months, and complete the review and negotiation of bilateral APA within 24 months. Most unilateral APAs (approximately 89%) and bilateral APAs (approximately 62%) signed from 2005 to

[36] "China Tax News"(2020)-Analysis of 2019 China APA Annual Report-http://www.ctaxnews.com.cn/2020-12/14/content_974388.html
[37] https://www.crowell.com/files/STA.pdf

2019 were completed within 2 years. In 2019, most of the newly signed APAs were completed within 2 years. What's more, noteworthy it is that among the 9 newly signed bilateral APAs, 5 of them completed the negotiation and signing within one year. This is the result of the State Administration of Taxation's increased resource investment in APA work, and fully reflects its emphasis on APA negotiation and signing.[38]

Table 4-2 APA review completion time

2019	within a year		one year to two years		within two years	
	unilateral	bilateral	unilateral	bilateral	unilateral	bilateral
Number of completions	2	5	4	2	6	2

The completion time of APA is continuing to be shorten, and the efficiency of negotiation and signing has been improved continuously in recent years. According to the *Announcement of the State Administration of Taxation on Improving the Administration of Advanced Pricing Arrangements* [39]. As mentioned above, the advance pricing work has 6 stages of application, including preparatory talks, intention to negotiate and sign, analysis and evaluation, negotiation and signing, monitoring and execution. Besides, companies applying for APA are often required to provide group value chain analysis and analysis of whether there are special Chinese regional factors. If Chinese domestic companies undertake R&D, marketing and other functions, they need to be based on DEMPE (that is, the development of intangible assets and the value enhancement, Maintenance, protection, application and promotion) and other standards to analyze whether relevant intangible assets are formed, and how relevant profits are reasonably distributed in the group value chain. With the continuous enrichment of the experience of both taxation companies, these previously difficult content formed a relatively standardized analysis method gradually, and the communication between the taxation companies has also become easier to reach a consensus.

4.5 Intangible assets

The definition of the intangible asset is that an no-physical asset in nature. Goodwill, brand recognition and intellectual property, such as patents, trademarks, and copyrights, are all intangible assets. Intangible assets exist in opposition to tangible assets, which include land, vehicles, equipment and inventory. Additionally, financial assets such as stocks and bonds, which derive their value from contractual claims, are considered tangible assets.[40]

[38] “China Tax News”-The State Administration of Taxation released the 2019 APA Annual Report, and the number of new signings hit a record high
[39] State Administration of Taxation Announcement No. 64 of 2016
[40] https://www.investopedia.com/terms/i/intangibleasset.asp

Most importantly, compared with the easy identification and control of tangible asset transfer pricing, intangible asset transfer pricing has three characteristics: the transfer value is difficult to determine, the value contribution judgment is complex, and the boundary between transfer income and other income is blurred.

The first characteristic of intangible assets is that the transfer value is such difficult to determine. Hence, the transfer value of intangible assets is very different from the transfer value of general tangible movable property. Generally, the value of tangible movable property is often based on its production cost, while the value of intangible assets is not only based on its production cost, but also depends on its use value—that is, the expected benefits after using the intangible asset. For example, suppose that two different companies research and develop a patent respectively. The two companies invest the same cost and the nature of the patent is roughly the same. However, the patent developed by one company is expected to bring a lot of benefits, while the other company is expected to only bring lower income. Obviously, the value of intangible assets that can obtain a large amount of income is higher, and the price at the time of transfer should also be higher.

However, due to the uniqueness of intangible assets and the uncertainty of environmental factors in the realization of their value, the actual future returns of intangible assets may deviate significantly from the expected returns. So in most cases, the expected benefits of intangible assets are highly uncertain. For example, when two companies conduct an intangible asset transaction, they estimate the future income of the intangible asset, and after considering other factors, the transfer price of the intangible asset is finally determined. If the two parties to the transaction have biased judgments on the nature of the intangible assets such as the value realization method and value conversion degree of the intangible asset, or have a deviation in the judgment of the environment in which the future value of the intangible asset is realized, for instance, the government issues an announcement restriction clauses in an unexpected situation, competitors develop more advanced intangible assets in the same area, etc. Under these circumstances, the initial estimated expected return of intangible assets will directly leads to the deviation of the transfer price of intangible assets from the true value. The economic life of intangible assets is also directly related to the expected income of intangible assets. Although some patents have a certain legal life, the economic life of the intangible asset will often be different from its legal life due to factors such as market changes and technological development. Therefore, the expected return of intangible assets is also difficult to predict.

In addition, there is often no market price for intangible assets. Out of the reason that world trade competition, mastering the monopoly of intangible assets means having a

competitive advantage in the market. In order to maintain their monopoly, multinational groups have Cross-border transactions mainly occur within the group. This means that only internal prices exist when intangible assets are transferred, but there is no market price.

The second characteristic of intangible assets is that the judgment of the source of value contribution is complicated. The judgment of the value contribution of intangible assets is the key to determining the right of each related party in the multinational group to obtain the income from the transfer of intangible assets. Income from intangible assets refers to the income derived from the transfer of the right to use or ownership of intangible assets that each affiliated company should enjoy based on their contributions in the process of creating the value of intangible assets. If one of the affiliated companies makes a greater contribution Compared with other related parties, the related party is entitled to more intangible asset income. The value contribution of intangible assets is generally embodied as the expenses shared by related parties when the cost of intangible assets is allocated. The judgment of the value contribution of intangible assets is very complicated, which undoubtedly makes it more difficult for the related parties to distribute the income of intangible assets. On the one hand, the value creation process of intangible assets involves the entire process of intangible asset research and development, value enhancement, maintenance, protection and utilization, specifically including the management and control of R&D projects, the implementation of R&D activities, and marketing strategies. And the design of the program, the establishment of sales channels, brand promotion, trademark or patent application and maintenance, etc. The efforts of the related parties involved in the transfer of intangible assets in the links listed above all contribute to the value of intangible assets, and these links are numerous and complicated, and the importance and difficulty of implementation of each link are also different, which increase the complexity of the judgment of the value contribution of intangible assets. On the other hand, it is difficult to quantify the contribution of related parties to the value of intangible assets. If the related parties develop an intangible asset jointly, and the amount of R&D costs paid by each party can be determined, the value contribution of the related parties in this respect is small. But in reality, there are many factors that are difficult to quantify which can affect the value of intangible assets, such as geographic factors and risk-taking, etc., it increases the complexity of the judgment of intangible asset value contributions.

The last feature is the blurring of the boundary between income from the transfer of intangible assets and other income. Compared with tangible assets, intangible assets are non-physical. Intangible assets do not have a physical form. At the same time, they are not like tangible assets that can be occupied or consumed tangibly.

Intangible assets have a certain degree of dependency but they are often attached to tangible assets as well. For example, patent rights are attached to patented products, and land use rights are dependent on land. At the same time, intangible assets are also closely attached to the entire business process of the enterprise.The dependence of intangible assets means that transactions in intangible assets are often closely related to other commercial transactions. When a transaction between related parties involves both intangible asset transactions and tangible asset transactions, transfer pricing based on the arm's length principle makes it difficult to separate the value of intangible assets from the overall transaction. Therefore, it is difficult for tax authorities to judge whether related parties obtain income from the transfer of intangible assets is reasonable. In addition, when companies transfer the right to use intangible assets instead of ownership, they will charge corresponding royalties. At the same time, the transfer of intangible assets between related parties is often accompanied by the provision of certain labor services, and the company may charge corresponding technical service fees or labor fees. However, the royalty income, technical service fee income, and labor service fee income are similar in nature, and the three are integrated in the same transaction easily. Therefore, the income from the transfer of intangible assets is difficult to match the income from technical service fees and labor fees. Multinational companies usually take advantage of the above characteristics of intangible asset transfer pricing to implement tax avoidance. The main tax avoidance methods include three types of methods: setting lower or higher prices to transfer profits to areas with low tax rates, mixing and packaging with other income to obtain income, and sharing costs to transfer profits.

4.5.1 The main methods of anti-tax avoidance in the transfer pricing of intangible assets

Tax authorities should take into account the characteristics of intangible assets, and take corresponding anti-avoidance measures based on the basic principles of intangible asset transfer pricing anti-tax avoidance.

(1) The Arm’s Length Principle

The object of transfer pricing management is the controlled transaction of taxpayers. To solve this problem, the position of independent transaction is generally supported in the world. The arm’s length principle, also known as the normal transaction principle and fair transaction principle, is the core principle of transfer pricing. At present, The Arm’s Length Principle is recognized by the vast majority of countries, which has a clear international definition. *Article 9 of OECD Model Tax Agreement* issued by OECD[41] when the conditions of the commercial or financial relationship between two affiliated enterprises are different from those of the

[41] ARTICLES OF THE MODEL CONVENTION WITH RESPECT TO TAXES ON INCOME AND ON CAPITAL- https://www.oecd.org/tax/treaties/1914467.pdf

commercial or financial relationship between independent enterprises, and because of the existence of these conditions, one of the enterprises does not obtain the profits it should have obtained, then this part of profits can be included in the income of the enterprise. " In terms of definition, The arm's length Principle is aimed at taxpayers. It emphasizes that when some transaction conditions of taxpayers are different from the normal transaction conditions between independent enterprises and result in tax consequences, tax authorities should implement corresponding tax adjustment. The arm's length principle provides a wide range of equal tax treatment for multinational enterprise groups and independent enterprises, which makes the affiliated enterprises and independent enterprises in a more equal position in terms of tax, and avoids the impact of some tax factors on the relative competitiveness of these two types of enterprises. At the same time, the scope of application of the arm's length principle is also very wide, which can play an effective role in most cases.

The application of transaction principle is generally based on the comparison between the conditions of controlled transaction and that of independent enterprise. In order to make the comparison more effective, it is generally required that the transaction terms of the two cases should be fully comparable. According to the description of comparability analysis in OECD transfer pricing guidelines, the comparability analysis should be carried out from five aspects: the characteristics of relevant assets or services, the functions and risks of both parties, contract terms, economic environment and business strategy. The results of action plan 8-10 of BEPS project also emphasize that the comparability analysis of transfer pricing of intangible assets should also consider geographical factors, the synergy effect of multinational groups, and other feasible schemes of all parties. *OECD transfer pricing guidelines*[42] also lists the typical steps of comparability analysis. First, it needs to conduct extensive analysis to identify the necessary major comparability influencing factors, then collect and analyze the data, select the most appropriate transfer pricing method, and finally determine the reward of independent transaction. If it is considered that the transaction price of controlled transaction is too low or too high after the comparability analysis, which does not conform to The Arm's Length Principle and causes tax consequences, the tax authorities can refer to the results of the comparability analysis to adjust the profits of the affiliated enterprises.

(2) The principle of substance over form

[42] https://www.oecd.org/tax/transfer-pricing/oecd-transfer-pricing-guidelines-for-multinational-enterprises-and-tax-administrations-20769717.htm

The principle of substance over form is an important principle of anti tax avoidance as well. It is also called the principle of substantial taxation in civil law countries. Both of them have the same meaning and emphasize the importance of "substance" more than "form".

In the field of transfer pricing, the principle of substance over form is also known as the principle of economic substance, which takes the economic substance of related party transactions as the standard to determine the transfer price of related party transactions. The anti avoidance function of the principle of substance over form has been widely recognized in the world, which is reflected in many international models. For example, the results of action plan 8-10 of BEPS project emphasize that the intangible assets identified in transfer pricing analysis can not be determined only by accounting characteristics and legal form, but can be used as reference factors, To judge whether it belongs to intangible assets in transfer pricing analysis, we should fully consider the conditions that independent traders will reach in comparable transactions. The "functional analysis" mentioned in the results of the action plan is also an important embodiment of the principle that substance is more important than form. Multinational companies tend to distribute the future income of intangible assets to low tax areas as far as possible for tax avoidance. For example, the conduit company located in low tax areas has the legal ownership of intangible assets, because multinational groups tend to distribute the income of intangible assets to the conduit company, Although the conduit company has not made significant value creation to the income brought by intangible assets.

The principle of substance over form is an important theoretical support for the tax authorities to avoid tax by using the means of confusing royalties and technical service fees in package sales. The tax authorities can adjust the tax payment for the transactions that do not conform to the form and substance according to the principle of substance over form.

(3) Clearly define the boundary of intangible assets scope

It is very important for tax authorities to clearly define the scope boundary of intangible assets identified by transfer pricing. A reasonable definition of intangible assets should clearly reflect the scope boundary of intangible assets. If the definition of intangible assets is too narrow, taxpayers and tax authorities may think that some objects with the characteristics of intangible assets do not belong to intangible assets, so there is no need to make separate compensation for these objects when they are transferred and used. If the definition is too broad, the taxpayer and the government may identify the subject matter that does not have the characteristics of intangible assets as intangible assets, and think that the subject matter should be compensated separately when it is transferred and used, even if the similar payment will not occur in the uncontrolled transactions of independent enterprises. If the boundary of

the scope of intangible assets is too wide or too narrow, the tax burden of enterprises will not match the economic essence of the actual transfer behavior.

The abstractness and diversity of intangible assets make it very difficult to define the scope of intangible assets, so there are a variety of perspectives. From the perspective of accounting, the definition of intangible assets in GAAP, IFRS and Chinese accounting standards are basically similar, mainly refers to the narrow sense of intangible assets, emphasizes that the intangible asset is an asset which is no physical form, identified, and not included financial assets, including non monetary assets. From the perspective of tax law, China's tax law does not define the scope of intangible assets in a high degree of generality, but only stipulates it in relevant regulations. It adopts the enumeration method, mainly including land use right, copyright, patent, trademark, trade secret and proprietary technology.

There are mainly two kinds of views on the definition of intangible assets from the perspective of transfer pricing. One is that the definition of intangible assets should be consistent with the international accounting standards, and still emphasizes the importance of legal ownership of intangible assets. Another point of view is that it should be analyzed from the perspective of transfer pricing, emphasizing the value of intangible assets. According to the relatively broad definition adopted by BEPS project action plan 8-10, as mentioned above, to judge whether it belongs to intangible assets in transfer pricing analysis, we should fully consider the conditions that independent parties will reach in comparable transactions, and should combine various considerations of accounting, legal and other factors. At the same time, the plan defines intangible assets as "assets different from physical form and financial assets. It is something that enterprises can own and control for commercial activities. Independent enterprises will pay consideration for the use or transfer of this thing under comparable conditions". Compared with the intangible assets from the perspective of accounting, the intangible assets from the perspective of transfer pricing is broader, not only limited to the identification, but also considering the relationship with the profit of intangible assets. In this way, the intangible assets under this definition method include not only the intangible assets listed in the book, but also the intangible assets not reflected in the book.

In fact, the definition of the scope of intangible assets is directly related to the tax interests of different countries, and each country has its own national conditions. At present, there is no unified definition of the scope of intangible assets in the field of transfer pricing.

(4) Adjustment of transaction price

The cover up of tax avoidance by multinational companies is usually embodied in the design of transaction contracts. When the transaction contract is involved, it can be simply transferring the ownership or use right of intangible assets and collecting the consideration, or

it can be internalizing the transfer of intangible assets into the products or services related to intangible assets. In addition, restrictive clauses or special clauses may be added to the contract. In reality, the form of consideration payment in the internal transaction of intangible assets by multinational enterprises is often very complex, which can be paid at the time of transaction, or it can be used to divide the income obtained by the transferee of intangible assets. However, no matter what form the specific transaction contract involves, the determination of the total transaction price of intangible assets in the contract should follow a series of principles.

At present, the research on the determination of the transaction price of intangible assets in the results of action plan 8-10 of BEPS project is more in-depth. It is emphasized that The Arm's Length Principle should be taken as the guiding principle when determining the transaction price of intangible assets. The transfer pricing method and comparability analysis method introduced in *OECD transfer pricing guidelines* are still effective and supposed to be followed. At the same time, this achievement focuses on the analysis method of determining the profit ownership of intangible assets. On the basis of comparability analysis, it puts forward the analysis framework of six step analysis method. The six step analysis emphasizes that each participant should judge the ownership of profits from the five perspectives of intangible assets development, value promotion, maintenance, protection and utilization. It also emphasizes that the essence rather than form of transactions should be deeply analyzed. Various factors involved in intangible assets transactions may be value contributing factors.

In addition, this achievement also divides the possible transaction types of intangible assets into two categories, one is the transfer of relevant rights of intangible assets, the other is the commodity sales or service transaction involving the use of intangible assets, and analyzes the specific problems that may be involved in this two types of transactions.

When the transfer pricing of intangible assets of multinational companies does not conform to the arm's length principle and causes the loss of tax benefits of bilateral countries, the ultimate method of tax authorities is to adjust the transaction price directly after mutual consultation and detailed analysis. Through the adjustment of the transaction price, the profits generated in the intangible assets transaction will be reasonably distributed among the affiliated enterprises of multinational enterprises, and ultimately achieve the purpose of balancing the tax interests of various countries.

As mentioned above, the commonly used transfer pricing adjustment methods in the world mainly include two categories, one is the transaction price method based on the transaction itself, the other is the comparative profit method based on profit. Both methods are based on the principle of comparability derived from The Arm's Length Principle.

Transaction price method is to compare each item in the transaction between affiliated enterprises with the normal transaction price in the competitive market, and finally adjust the price of affiliated transactions to the normal transaction price in the market. Transaction price method mainly includes comparable uncontrolled price method, resale price method and cost plus method. The rule of comparative profit is to compare the profit generated by the affiliated exchange with the reasonable profit in the competitive market, and adjust the unreasonable profit to the reasonable profit.

Comparative profit method includes transaction net profit method, comparable profit method and profit division method. The transaction price method is more widely used than others, especially the comparable uncontrolled transaction price method is used for almost all types of transfer pricing. However, intangible assets transfer is often not comparable, which may cause difficulties in the application of transaction price method. In the comparative profit method, the comparative profit method and the transaction net profit method are not suitable for the transfer pricing of intangible assets because they are easy to violate the principle of substance over form. The adjustment method of intangible assets transfer pricing recommended by the United States and OECD is the profit segmentation method, because it is particularly applicable to the situation where the transfer of intangible assets between related parties is highly integrated and difficult to distinguish.

(5) Strengthen tax management of cost sharing agreement

Cost-sharing agreements are inter-company cooperation contracts, established to provide the correct allocation of costs between different legal entities but which belong to the same economic group, to determine the apportionment of expenses and costs resulting from the exercise of shared activities, such as internal accounting, communication, legal and administrative services.[43]The characteristics of a cost-sharing agreement can be summarized as "sharing costs and risks and sharing benefits", that is, each participant has economic ownership of the intangible assets jointly developed under the cost-sharing agreement, although the legal ownership of the intangible asset may only be owned by one party. Each participant does not need to pay royalties for the use of the intangible assets. Cost sharing agreements are widely used in the tax planning of multinational groups. Cost sharing agreements that use intangible asset transfer pricing for tax planning are the subject of cost sharing agreements. In international practice, about 95% of cost sharing agreements are developed for intangible assets. Therefore, strengthening the tax management of cost-sharing agreements is also an important anti-tax avoidance measure taken by the tax authorities of various countries for the transfer pricing of intangible assets.

[43] https://drummondadvisors.com/en/2020/05/13/tax-aspects-of-cost-sharing-agreements/

Determining whether the cost-sharing agreement complies with the arm's length principle is the core of the cost-sharing agreement's anti-tax avoidance. Specifically, the cost-sharing agreement is divided into three phases: signing, executing, changing, and terminating. All three phases should conform to the arm's length principles.

The first stage is the signing and implementation stage, which includes three important factors: expected benefits, matching principles, and compensation adjustments. The existence of expected benefits is a prerequisite for reaching a cost-sharing agreement that conforms to the arm's length principle, that is, there are expected benefits first, and then costs or contribution shares are allocated based on expected benefits, instead of cost and contribution shares first, and then expected benefits. At the same time, this also means that if the expected benefits of each participant cannot predict, the cost sharing agreement will be unable to reach. The principle of matching is also known as the principle of matching costs with expected benefits, which is the fundamental principle of cost-sharing agreements. The matching principle means that the cost and contribution ratio required by each participant should be matched with the expected revenue share. It is required by independent companies that the cost and contribution ratio to be apportioned should match the expected revenue share in the conventional market. Therefore, the arm's length principle is also satisfied while satisfying the principle of matching. Of course, for some special cases, the matching principle will also conflict with the arm's length principle. Compensation adjustment is a means to re-conform to the independent transaction principle when there is a deviation in the implementation of the cost sharing agreement. When the actual contribution share of a participant is inconsistent with the expected income ratio specified in the agreement, and the deviation is beyond the acceptable range of the independent enterprise, it means that the cost sharing agreement does not comply with the independent transaction principle, and the compensation adjustment is the solution effective means of this problem. Compensation adjustment requires compensatory payment when the above-mentioned mismatch occurs between the participating parties. Therefore, to make the cost-sharing agreement meets the independent transaction principle at the signing and implementation stage, it is necessary to take the three major elements. The third stage is the termination stage that is also the continuation of the matching principle, which means the benefits of each participant from the cost-sharing agreement should be matched with their allocated costs.

The matching principle is the key to making the cost-sharing agreement meet the independent transaction principle. And tax authorities' implementation of intangible asset transfer pricing anti-tax avoidance can start from the three stages of signing, execution, modification and termination, with the principle of matching as the core, standardize the

relevant laws of the country's cost-sharing agreement, and strengthen the tax management of the cost-sharing agreement.

The third stage is the termination stage. This stage is also the continuation of the matching principle, that is, the benefits of each participant from the cost-sharing agreement should be matched with their allocated costs.

It can be seen that the matching principle is the key to making the cost-sharing agreement meet the independent transaction principle. Tax authorities' implementation of intangible asset transfer pricing anti-tax avoidance can start from the three stages of signing, execution, modification and termination, with the principle of matching as the core, standardize the relevant laws of the country's cost-sharing agreement, and strengthen the tax management of the cost-sharing agreement.The third stage is the termination stage. This stage is also the continuation of the matching principle, that is, the benefits of each participant from the cost-sharing agreement should be matched with their allocated costs.

It can be seen that the matching principle is the key to making the cost-sharing agreement meet the independent transaction principle. Tax authorities' implementation of intangible asset transfer pricing anti-tax avoidance start from the three stages of signing, execution, modification and termination, with the principle of matching as the core, standardize the relevant laws of the country's cost-sharing agreement and strengthen the tax management of the cost-sharing agreement.

(6) Advance pricing arrangement

There are more and more disputes among countries with the increasing complexity of the transfer pricing problem. As a prior settlement mechanism of disputes, APA can reach an agreement with the relevant parties in advance and actively solve the transfer pricing problem. APA pays more attention to the management in advance compared with adjusting the transaction price directly after the event. And it is usually negotiated between tax paying enterprises and tax authorities on the issue of transfer pricing. It can be reached by signing an advance pricing agreement, which can reduce the tax risk of enterprises and the difficulty of tax authorities' anti avoidance management after the two parties reach an agreement. It is an international common anti avoidance management method, which has been applied in many countries. APA includes unilateral, bilateral and multilateral. Unilateral APA only involves one country, while bilateral and multilateral APA involve two or more countries. As for the transfer pricing of intangible assets, advance pricing can solve the problem that multinational enterprises transfer profits to low tax areas to avoid tax by setting lower or higher prices because it is difficult to determine the value of intangible assets. However, advance pricing often takes a long time to negotiate and sign, and its timeliness is poor. For some intangible

assets with large value fluctuation, the applicability of advance pricing is poor. But for intangible assets with stable value over time, advance pricing is an effective means to solve the problem. In addition, the cost sharing agreement can also be reached through negotiation and signing of advance pricing arrangement. Therefore, as a general anti tax avoidance management method, advance pricing also has a strong use in the transfer pricing of intangible assets.

(7) Application of general anti avoidance provisions

When the related parties of different countries in a multinational group transfer the right to use intangible assets, it will involve the issue of paying royalties to foreign countries. In order to achieve the minimum tax burden of the group, some multinational companies will take advantage of the preferential tax provisions on royalties in the tax treaties between the contracting countries to enjoy the tax preferences that they should not have enjoyed by setting up conduit companies, The income source countries suffer from tax losses. For this kind of tax avoidance, tax authorities can improve the standard of "beneficial owner" in tax treaties to avoid it. The beneficial owner, also known as the actual beneficiary, is to prevent multinational enterprises from abusing the concept of "tax resident status". If the enterprise meets the application conditions of the beneficial owner, it can apply to be the beneficial owner, so it can enjoy the tax preference between the Contracting States. No matter how complex the form and structure of the conduit companies set up by multinational companies for the purpose of tax avoidance, their essence is the same, that is, these conduit companies have little actual economic contact with the host country, and have no commercial essence. The purpose of their establishment is not to operate in their own country for a long time, but to reduce the actual tax burden of the group. The beneficial owner clause requires that the applicant of the beneficial owner must have a reasonable business purpose, and his business performance must show that he is engaged in substantive business activities. The applicant who does not have a reasonable business purpose, does not constitute substantive business activities, and is suspected of tax avoidance will not be granted the qualification of beneficial owner. Tax authorities in various countries can effectively prevent the risk of multinational groups abusing tax treaties by improving the rigidity of the judgment standard of "beneficial owner".

General anti avoidance provisions are generally applicable when taxpayers implement arrangements that have no reasonable commercial purpose and result in tax consequences. As long as the taxpayer meets the above conditions, the tax authorities have the right to make tax adjustments according to reasonable methods. The general anti avoidance clause, as the bottom line of anti avoidance clause, can forcibly adjust the tax avoidance behavior of

taxpayers when it is difficult to classify the tax avoidance behavior of enterprises into the scope of specific special tax adjustment. When an enterprise uses the transfer pricing of intangible assets to avoid tax, and the tax authorities are difficult to grasp the handle, the tax authorities can advocate the application of general anti avoidance provisions according to the principle of substance over form. However, the general anti avoidance provisions are often difficult to use, mainly because it is difficult to judge whether the business purpose is reasonable or not, and it is difficult to find some hidden business arrangements implemented by enterprises. Moreover, the general anti avoidance provisions will often cause great disputes between enterprises and tax authorities. After the enterprises appeal to the court, the tax authorities have a certain risk of losing the lawsuit. Therefore, the general anti avoidance provisions are often used cautiously.

4.5.2 China's anti-tax avoidance policies on transfer pricing of intangible assets

In China's transfer pricing tax system, special consideration of intangible assets is mainly focused on the *Announcement No. 6, 2017 of the State Administration of Taxation - Administrative Measures for special tax investigation adjustment and mutual consultation procedures*.[44] The regulations of the Ministry mainly stipulate the following aspects:

The first is the regulations on the value contribution of intangible assets. Article 30 of the measures stipulates that when judging the value contribution and income distribution of enterprises and related parties to intangible assets, the global operation process of enterprise groups shall be comprehensively analyzed, and the value contribution of all parties in the development, value promotion, maintenance, protection, application and promotion of intangible assets shall be fully considered. In addition, it also emphasizes that the enterprise should not participate in the income distribution of intangible assets if it only owns the ownership of intangible assets and does not make substantial contribution to the value of intangible assets. That is to say, the amount of royalties is no longer determined arbitrarily by the affiliated enterprises, and the proportion of royalties payment set in the transaction contract must be supported by the transaction essence. This is basically the same guiding spirit as the results of action plan 8-10 of BEPS project.

The second is to regulate the special tax adjustment principle of royalty related to intangible assets transactions. The regulation lists four situations that if the royalties collected or paid by an enterprise and its related parties for transferring or transferring the right to use intangible assets meet the following four situations, the enterprise shall adjust the royalties on its own. If no timely adjustment is made, the tax authorities have the right to implement special tax adjustment. The four situations are as follows: (1) The value of intangible assets

[44] http://www.chinatax.gov.cn/download/pdf/20171122.pdf

changes fundamentally; (2) According to business practice, there should be a royalty adjustment mechanism for comparable transactions between non related parties; (3) During the use of intangible assets, the functions, risks or assets used by the enterprise and its related parties change; (4) Enterprises and their related parties make contributions to the follow-up development, value promotion, maintenance, protection, application and promotion of intangible assets without reasonable compensation. In other words, royalties need to be adjusted at any time according to market conditions, and the royalties paid by affiliated enterprises should match the economic benefits brought by intangible assets to the enterprise or its related parties. At the same time, the measures also provide that the tax authorities can implement special tax adjustment on royalties.

The third is the method of intangible assets transfer pricing and its comparability analysis. *Announcement No. 6 of 2017* specifies the transfer pricing adjustment methods recognized by China, including comparable uncontrolled price method, resale price method, cost plus method, transaction net profit method, profit division method and other methods in line with the the arm's length principle. The comparable uncontrolled price method is still the most widely used transfer pricing adjustment method among them, which is applicable to all types of related party transactions. The transaction net profit method is generally applicable to the intangible assets related transactions of enterprises that do not have significant value intangible assets. The transaction net profit method is not applicable if the intangible assets transferred by enterprises have significant value. The profit segmentation method advocated by OECD is also mentioned in this regulation, which is applicable to the transfer pricing of intangible assets. The business is highly integrated, and it is difficult to evaluate the transaction results of all parties, especially when both enterprises and related parties make unique contributions to profit creation, so the profit segmentation method is an effective way to solve such problems.

In addition, in terms of cost sharing agreement, the first time China has stipulated the law is the implementation regulations of *the enterprise income tax law of the people's Republic of China*, which stipulates that the cost sharing principle of the cost sharing agreement shall conform to the arm length principle and the principle of matching cost to expected income, and also stipulate that if it does not conform to the above two principles, the costs apportioned by the enterprise shall not be deducted before the taxable income is calculated. The main regulation of the cost sharing agreement in China is the implementation measures for *special tax adjustment (Trial)*[45], in which the seventh chapter makes more specific provisions on the cost sharing agreement, including the concept of the cost sharing

[45] Which issued by the State Tax Administration [2009] No.2

agreement, the scope of application, the principles to be followed, the composition of the signing elements of the agreement, the change of the participants and the suspension of implementation. It also stipulates that enterprises can reach cost sharing agreement by way of advance pricing arrangement at the same time. After that, the State Administration of Taxation issued *announcement No. 45 on regulating the management of cost sharing agreement* in 2015, which gave further tax authorities the right to implement special tax investigation and adjustment for cost sharing agreements that do not conform to the principles mentioned above. On the whole, China takes *document [2009] No.2* as the main body, and the relevant policies basically cover the main aspects of the cost sharing agreement, all of them formed the policy system of China's cost sharing agreement initially.

In terms of tax treaties, the tax treaties signed by China basically include the royalty clause, which stipulates the bilateral taxation of the royalty paid for the transfer of the right to use intangible assets. On this issue, most of China's tax treaties follow the principle of sharing the right of Taxation between the country of residence and the country of source of income in the United Nations model, that is, the country of source of royalty has priority in taxation, but the limited tax rate must be set. In the tax treaties signed with foreign countries, the limited tax rate of royalty is generally 10%, which is consistent with the preferential tax rate of enterprise income tax law.

In terms of the identification of beneficial owners, the State Administration of Taxation has made detailed provisions on Relevant Issues in the *Announcement No. 9 of 2018* on issues related to "beneficial owners" in tax treaties, specifically listing five factors that should be considered in determining the beneficial owner and the specific circumstances of directly determining whether it belongs to or does not belong to the beneficial owner, It also clarifies the application filing process of the identification of the beneficial owner. On the issue of transfer pricing of intangible assets, the royalty clause in tax treaties and the identification of beneficial owners play a joint role. For example, if a third country enterprise sets up a permanent establishment in China and the permanent establishment pays royalties to Singaporean residents, if the royalties are actually connected with the permanent establishment, according to the China and Singapore agreement, China has the priority to tax. If the Singaporean resident is the beneficial owner of the royalties, he can enjoy the preferential tax treatment of the China Singapore agreement.

4.6 Tangible assets

The main tax avoidance form of transfer pricing of tangible goods is to adjust the declared price, including the following aspects. First, deliberately lower or higher the price of

import goods in general trade. Affiliated enterprises can reduce or increase the production costs of domestic companies by adjusting the prices of imported foreign raw materials and other goods, so as to increase or reduce the profits of domestic companies. The difference of raw material price and tax rate in different countries determines which quotation the enterprise adopts. The low price of import is mainly applied to commodities with high import tariff rate or special tariff and regulatory measures. What's more, the high reported import price is mainly used for low-tariff commodities, and the profits are transferred to the low tax countries or tax haven through the import link. Second, the purchase price of imported tax-free equipment is adjusted artificially. Because the tax reduction and exemption equipment purchase cost will affect the extraction of depreciation cost of fixed assets every year, and it will have a certain impact on the distribution of the final profits of the enterprise. Third, the customs tariff collection is affected by adjusting the trading price of imported and exported goods through adjusting the price of import and export goods processed by the regulatory authorities, or simultaneously carrying out processing trade and general trade business.

Compared with intangible assets, transfer pricing of tangible assets is easier to confirm and control. China adopts OECD pricing method and advance pricing method to reduce the deviation of transfer pricing of tangible assets. In addition, in order to guard against the risk of tax collection and management in import and export, China has successively promulgated corresponding laws and regulations, which are mainly based on the Customs Law of the people's Republic of China (hereinafter referred to as the Customs Law), the regulations of the people's Republic of China on import and export tariffs, and the measures of the people's Republic of China on examining and approving the duty paid price of import and export goods, The core of the supervision mode, which takes customs clearance valuation and subsequent inspection and supervision as the main means, is to adjust the duty paid price of import and export goods.

4.7 Comparison of tax avoidance management between China & Western countries

After years of exploration on the transfer pricing system of intangible assets, all countries have basically formed a set of policy systems with their own characteristics. On some basic principles, the positions of all countries are relatively consistent, but on the formulation of specific policies, all countries have different practices and explorations. As a matter of fact, there is no need for all countries to reach a consensus on every aspect of transfer pricing of intangible assets. The differences in policies of different countries are determined by their specific national conditions.

China, the United States, the United Kingdom, India, Japan, Australia and France all comply with the concept of OECD transfer pricing guidelines, such as the the arm's length principle, the selection of transfer pricing methods, the requirements of comparability analysis and advance pricing, and each country has made legislation on relevant projects. In addition, China's current intangible assets transfer pricing tax system and related tax rules system have made great achievements after nearly ten years of construction. In terms of legislation, China has made relevant legislation on transfer pricing principles, transfer pricing methods, compliance with OECD transfer pricing guidelines, special consideration for transfer pricing of intangible assets, cost sharing agreement system, contemporaneous information, advance pricing arrangements and other administrative dispute settlement means, However, China has not designed special measures to solve the intangible assets that are difficult to evaluate.

4.7.1 International reference for follow-up management of transfer pricing adjustment

the OECD transfer pricing guide states that in order to align the actual profit distribution with the initial adjustment of the transfer pricing, some countries would advocate the adoption of a presumption transaction (also known as a secondary transaction), and the excess profit generated by the initial adjustment is considered to be transformed into another form and taxed accordingly. Secondary transactions usually show the presumption of dividend, loan presumption, or constructive equity investment.

This kind of problem is also stipulated in the transfer pricing regulations of the United States. First, after the transfer pricing adjustment is required, the "subsidiary adjustment" should be considered, because the result of the adjustment may affect other entities within the group. Another is "secondary adjustment", which includes: after the adjustment of transfer pricing, accounting treatment may be in the form of dividend distribution or capital investment. It is necessary to restore its accounting to the state that the enterprise initially followed the principle of independent exchange, and it is allowed to apply for the secondary adjustment tax exemption if the adjustment is allowed.

Among them, for the second adjustment, the first is the accounting adjustment. For taxpayers who meet relevant requirements, the related receivables or accounts payable with interest can be established for each adjusted year according to the adjusted results, and the other is dividend offset. If the second adjustment involves the dividend in the United States, we can choose to offset the dividend. For example, the fees charged by a parent company in the United States to its overseas subsidiaries are considered to be on the low side. After the adjustment, its accounts should reflect the higher amount paid by its overseas subsidiaries to the parent company in the United States. At this time, the enterprise can choose to offset the

amount of secondary adjustment by limiting the dividend amount received from overseas subsidiaries in the current year.

In order to avoid double taxation caused by the secondary adjustment, Japan revised the bilateral tax agreement between Japan and the United States. The main contents of the amendment include: (1) if the profit distribution of the enterprises of both parties does not conform to the the arm's length principle, both parties shall accept the secondary adjustment, so that the taxpayers can avoid double taxation (2) When the beneficiary of the dividend is a (a) or (b) below, the contracting state of the agreement in which the resident enterprise that distributes the dividend is located cannot tax the dividend: (a) the beneficiary is a resident enterprise in the other Contracting State of the tax agreement, directly or indirectly owns more than 50% of the voting shares of the dividend distribution enterprise through one or more resident enterprises located in any Contracting State, And the beneficiary has held the shares for at least 12 months as of the date of dividend distribution, or the beneficiary is an enterprise meeting certain conditions.(b) Pension fund, which is a resident enterprise of the other Contracting Party to the agreement, except where the dividend is derived from the business of which the pension fund operates directly or indirectly.

4.7.2 International experience in defining the scope of intangible assets

Most countries lack a clear definition of the scope of intangible assets from the perspective of transfer pricing. At present, many countries use enumeration method. For example, in the United States*, Section 482, section 4b of the Internal Revenue Code* stipulates that intangible assets must meet the following two conditions:

Patent, invention, formula, process, design, pattern, know-how, copyright and works of literature, music and art, franchises, licenses and contracts, trademark, trade name, brand, market activity, investigation, research, prediction, evaluation, customer list, technical data, other values are derived from the connotation of knowledge, but not from knowledge

Similar items with non physical properties. The asset must have a real value independent of any single service.

In addition, the OECD transfer pricing guide also uses enumeration method to define intangible assets. In Chapter 6 "special considerations on intangible assets", intangible assets are defined as: the right to use industrial assets, such as patents, trademarks, trade names, designs or models, etc., as well as literary and artistic property rights and intellectual property rights, such as know-how and trade secrets. The guide also classifies intangible assets into marketing intangible assets and transaction intangible assets.

In Britain, the definition method is adopted. In the Financial Reporting Standard No. 10 - goodwill and intangible assets issued by the UK in 1997, it is stipulated that "intangible assets

refer to the non-financial assets that are not in physical form but can be identified and controlled by the enterprise through legal rights". In its transfer pricing guidelines, the IRS defines intangible assets as "assets that can be clearly developed and utilized although they do not have physical form". The classification of intangible assets of UK tax authorities is similar to that of OECD transfer pricing guidelines, which classifies intangible assets into transaction intangible assets and marketing intangible assets.

BEPS action plan attempts to formulate a highly general definition: "intangible assets" refers to non-financial assets without physical form owned or controlled by enterprises for use in business activities, and consideration will be paid for their use or transfer among independent enterprises under comparable circumstances. On this basis, the BEPS action plan also explains the definition from the following perspectives. First, intangible assets in transfer pricing analysis are not necessarily recognized in accounting, nor are they necessarily protected by law. Second, whether it can be transferred independently is not a necessary condition of intangible assets in transfer pricing. Third, intangible assets should be distinguished from market conditions or local market environment. They are not intangible assets, but need to be considered in comparability analysis. In addition, BEPS action plan also uses non exhaustive enumeration to illustrate intangible assets under transfer pricing, including, patents, know how, Trademarks, contract rights and government permission. At the same time, it also enumerates and explains that company registration obligation, group synergy and special market factors are not intangible assets.

At present, the international dispute is whether collective labor, on-the-job labor, goodwill and sustainable use value constitute intangible assets from the perspective of transfer pricing. For example, there are many conflicts between the cases of the United States Internal Revenue Service and the court regarding the collective labor force and the on-the-job labor force. For example, in the case of cost sharing agreement of Veritas software company in the United States, for the issue of on-the-job labor, the Internal Revenue Service of the United States considers that on-the-job labor belongs to the "pre existing Intangibles" stipulated in *Section 482, section 7of the internal revenue code*, However, the judge held that the on-the-job labor force was not listed in *Section 482, article 4b of the internal revenue code*, and it did not have any real value independent of personal labor service. Therefore, the court ruled in 2010 that the on-the-job labor force involved in this case was not an intangible asset.[46]

As for the problem of collective labor force and on-the-job labor force, most countries do not include them in the list of intangible assets, and some countries are open to it. The tax

[46] “An analysis of international tax revenue of China's multinational corporations' "going out" -- from the perspective of transfer pricing of intangible assets”-http://www.51fabiao.org/shuishou/lw201809150926349511.html

regulations issued by Australia in 1998 listed the "intellectual assets", in which human capital and its capabilities, such as the knowledge possessed by managers, R & D personnel, technical workers and functional specialists, are listed. Japan's 2006 revised "cdotp" bill also included human resources in the scope of intangible assets. In addition, the bill also included "soft intangible assets" such as production process, negotiation and development management, distribution and financing network in the scope of intangible assets. After the 1990s, Japan transferred labor-intensive factories to low-cost areas, and used the advanced technology of its parent company for production. As a result, the scope of intangible assets in Japan is relatively wide, which is beneficial for the company to claim that a larger proportion of profits should be attributed to its parent company when pricing intangible assets transfer.

There is also a heated debate on whether goodwill and sustainable use value should be regarded as intangible assets in the context of transfer pricing. Some people think that goodwill and going concern value are monetary compensation paid by independent enterprises when transferring part or all of their assets. These factors should be taken into account when related enterprises trade. In order to ensure that this value is taken into account in appropriate circumstances, goodwill and going concern value are supposed to be regarded as intangible assets. Some people think that goodwill and sustainable use value have not been defined clearly and cannot exist independently. If goodwill and sustainable use value are regarded as intangible assets, it means that excess return or undefined value can be regarded as intangible assets at will, which will undoubtedly increase the uncertainty of transfer pricing of intangible assets. In this regard, the United States Internal Revenue Service believes that the definition of goodwill and going concern value is too broad and should not be recognized as intangible assets. In view of the great differences between the parties on this issue, Goodwill is recognized as intangible assets in *China's Regulations for the implementation of the enterprise income tax law*, while the list in Document No. 2 of 2009 does not include goodwill. At the same time, there is no authoritative explanation for the concept of goodwill in Chinese law. The value of continuous use has not appeared in the law of our country, so relevant laws and regulations on this issue are not very clear in China.

4.7.3 International experience of cost sharing agreement

There are great differences in the development degree of cost sharing agreements among countries in the world. Among several OECD countries with large economies, only China, the United States and Japan have separately issued relevant provisions on cost sharing agreements. Although there is no separate legislation on cost sharing agreements in other countries, they generally agree with the OECD transfer pricing guidelines, and domestic regulations generally state that the relevant issues should be handled in accordance with the OECD

transfer pricing guidelines. The developed countries in Europe generally take a cautious attitude towards the cost sharing agreement. They think that signing the cost sharing agreement is a lazy way to deal with the traditional related party transactions, and this method will bring great challenges to the risk control, so there are few specific practice cases. However, the United States has a relatively loose attitude towards the cost sharing agreement, and believes that the cost sharing agreement is an advanced "simplified" approach.

As for the basic principles, there are both similarities and differences among countries. China, the United States and Japan all emphasize that the the arm's length principle and the principle of matching costs with expected benefits are the basic principles to measure the compliance of cost sharing agreements, The most distinctive feature of cost sharing agreement is that the basic condition of the agreement that each participant is willing to accept a total amount of contributed resources without additional compensation is the expectation of the common interests of each participant. The *U.S. Treasury regulation No. 482* emphasizes that the existence of clear and divisible interests is a necessary condition for the formation of cost sharing agreement. And *China's announcement No.2 of 2009* also emphasizes that the beneficial right of intangible assets or services involved in the cost sharing agreement should have reasonable and measurable expected income, which should be based on reasonable business assumptions and business practices. In addition, they all emphasize that the existence of expected benefits is the premise of reaching a cost sharing agreement in line with the the arm's length principle.

As for compensation adjustment, the provisions of China's announcement No.2 in 2009 are basically the same as those of the OECD transfer pricing guidelines, both of which emphasize that compensation adjustment may be required for cost sharing agreements. Only when the actual contribution of each participant is consistent with the expected income ratio specified in the expected agreement after balanced payment adjustment, can it be considered as in line with the the arm's length principle. It should be noted that the balancing payment of compensation adjustment in OECD transfer pricing guidelines. And there are two concepts about compensation adjustment in *Section 482 of the Revised Internal Revenue standards of the United States in 2009*. One is cost sharing transactions payment (CST payment) and platform contribution transactions payment (PCT payment). Cost sharing transaction payment refers to the compensation adjustment for the development cost of intangible assets arising from the implementation of the cost sharing agreement according to the matching principle. The platform contribution transaction payment is a compensatory adjustment based on the matching principle for the platform contribution intangible assets formed by the participants before the implementation of the cost sharing agreement. This concept also includes the value

of intangible assets that can provide platform contribution of each participant before the signing and implementation of the cost sharing agreement. Compared with the practice in the OECD transfer pricing guidelines, the concept proposed by the United States takes into account the factors of platform contribution intangible assets, because platform contribution intangible assets indeed affect the expected returns of all participants.

On the whole, different countries attach different importance to cost sharing agreements. China is one of the few countries that make separate provisions on cost sharing agreements, and conforms to the international mainstream views in terms of principles and institutional framework. However, compared with the United States, China's provisions on cost sharing agreements are still too simple and framed, Many specific provisions still need to be further refined.

4.7.4 International experience of advance pricing

APA has been widely used in the world. Countries with large international economic volume have basically formulated the relevant system of booking pricing, and at the same time, there are relevant provisions for unilateral, bilateral and multilateral APAs. Taking the United States as an example, the relevant documents of APA originated in March, 2000. At first, tax authorities were cautious about the pricing of appointment, and the level of documents issued was not high. However, since 2000, in order to regulate APA, the United States has promulgated a series of tax procedures. With the progress of BEPS project, the United States authorities also realize that the current international tax situation is becoming more and more complex. The attitude of the tax authorities to APA has shifted from unilateral APA to bilateral and multilateral APA. Generally speaking, unilateral APA is more common, and countries have a positive attitude towards unilateral APA, while for bilateral and multilateral APAs, countries' attitudes are relatively negative. The reason may be that unilateral APA is easier to reach and directly solve the transfer pricing problem in China, while the negotiation and signing of bilateral APA is more troublesome and the cost is higher. However, multilateral APA is rarely used because of the complexity of the negotiation and signing process. However, unilateral APA can only solve the transfer pricing problem of domestic part, and it will often have adverse effects on tax authorities in other countries.

In addition, China has a high threshold for the formation of APA, which leads to its low popularity. Notice No. 64 of 2016 of the State Administration of Taxation of the people's Republic of China "*Notice of the State Administration of Taxation on matters related to improving the management of advance pricing arrangements*" stipulates that "advance pricing arrangements are generally applicable to the related party transactions with an amount of more than RMB 40 million in each of the first three tax years of the tax year on the date when

the competent tax authorities deliver the notice of tax matters to enterprises to receive their negotiation and signing intention Enterprises on the Internet. " This means that only large-scale enterprises can apply for APA. But the fact is that the demand for APA is often not directly related to the size of the enterprise. On the contrary, even many SMEs have more frequent transactions in intangible assets. Moreover, France has designed a set of simplified procedures for the advance pricing of small and medium-sized enterprises, so that small and medium-sized enterprises can also enjoy the advance pricing arrangement. Additionally, although the UK's APA threshold is also high, its threshold standard is only allowed when the intangible assets of the enterprise can not obtain the market comparable price or the traditional transfer pricing adjustment method is not applicable, and the size of the enterprise is not an important factor, which is more suitable for the enterprise's demand for APA arrangement. Therefore, the design of advance pricing system in China needs to be improved.

4.8 Difficulties in anti tax avoidance management of transfer pricing in China

4.8.1 The scope of intangible assets is not clear enough

At present, the international community has not yet reached a complete agreement on the scope of intangible assets from the perspective of transfer pricing. There is basically no big difference in the world about proprietary technology, trade secrets and trademarks as intangible assets. However, whether soft intangibles, such as goodwill, value of going concern, collective labor force, on-the-job labor force, market power, first mover advantage, effective supply chain and business opportunities, should be included in the scope of intangible assets from the perspective of transfer pricing is still controversial.

China's tax laws and regulations define the scope of intangible assets in the form of enumeration. According to the implementation regulations of *the enterprise income tax law of the people's Republic of China*, the scope of intangible assets is defined as "mainly refers to patent right, trademark right, copyright, land use right, non patent technology and goodwill". The "measures for the implementation of special tax adjustment" defines the scope of intangible assets as "land use right, copyright, patent, trademark, customer list, marketing channel, brand, trade secret, proprietary technology and other franchises, as well as industrial property rights such as industrial design or utility model". Although both of them define the scope of intangible assets in the framework of income tax, they are slightly different. The former summarizes the scope of intangible assets briefly, while the latter is relatively detailed. In addition, the connotations of the two concepts are somewhat different. For example, the goodwill mentioned in the implementation regulations is difficult to find the corresponding items in the implementation measures. Another example is the marketing channels mentioned

in the implementation measures, which are difficult to correspond in the implementation regulations. The scope of intangible assets is also stipulated in the relevant regulations of value-added tax. The measures for the pilot implementation of replacing business tax with value-added tax divides intangible assets into "technology, trademark, copyright, goodwill, right to use natural resources and other rights and interests intangible assets", and makes specific explanations for the right to use natural resources and other rights and interests intangible assets. The scope of intangible assets defined in the VAT law is slightly different from that in the income tax. It can be seen that the definition of intangible assets in different tax laws and regulations in China is not uniform, and the scope of intangible assets in different versions is slightly different. This kind of confusion increases the compliance difficulty and risk of enterprises, and is not conducive to the development of anti tax avoidance work.

With the progress of science and technology and the rapid innovation of business model, the categories and forms of intangible assets are constantly enriched. It is inevitable that the traditional enumeration method will be outdated to define intangible assets. Although such assets have the relevant characteristics of intangible assets, they are not considered intangible assets because they are not listed in the law. At this time, it is difficult for the tax authorities to distinguish the assets transferred by enterprises from tangible movable assets, intangible assets or other types of transactions, which provides policy loopholes for tax avoidance of multinational companies.

It is worth noting that the relationship among franchise, intangible assets, royalties and royalties. Franchise is a kind of intangible assets, generally refers to the franchise. Royalty is the income from the transfer of intangible assets. To be more specific, the royalty can be understood as the fee charged by the franchiser for the franchiser to operate certain goods or services. For example, an operator authorized by the Olympic Organizing Committee can sell Olympic commemorative goods at a certain price, and the operator needs to pay the royalty to the Olympic Organizing Committee according to the proportion of the sales revenue. Another example is the franchise fee, which is charged by the franchiser for allowing the operator to make use of its brand, reputation and management mode. Of course, the franchise fee emphasizes more on the fees paid at this time point when the operator obtains the business qualification. Royalties are stipulated in State Administration of Taxation [2010] No. 75 (*agreement between the government of the people's Republic of China and the government of the Republic of Singapore on the avoidance of double taxation and the prevention of tax evasion on on income*) and the interpretation of the provisions of the protocol. Royalties refer to the use or right granted to the other party to use various forms of literature and art that

constitute rights and properties, related industries, industries and industries The income that should be collected from the intellectual property rights determined in the words and information of commercial and scientific experiments also includes the income obtained by granting the other party the right to use or have the right to use industrial, commercial and scientific equipment and related information, including the payment under permission and the compensation for infringement. The scope of royalty not only includes franchise, but also emphasizes the transfer of the right to use intangible assets.

4.8.2 The scope of intangible assets is not clear enough

As mentioned above, 95% of the cost sharing agreements in international practice are designed for intangible assets, so the cost sharing agreement is an indispensable part of the transfer pricing of intangible assets. However, there are some problems in the application and collection of cost sharing agreement, which is not only existing in China, but also difficult to reach a consensus in the international community.

It is difficult to determine the expected income of intangible assets in the signing and implementation stage of cost sharing agreement. In determining the expected return, there are generally great disputes on the selection and application of valuation methods and the estimation of service life. Generally speaking, among the three methods of asset appraisal (cost method, market method and income method), market method is the most consistent with the the arm's length principle by definition, but this method is the most difficult to apply, because the intangible assets involved in the cost sharing agreement are unique, it is difficult to find similar and comparable transactions in the market. Generally, the method of cost sharing agreement is income method, and the most commonly used model is future cash flow method, because the income method is most related to the expected income, and the future cash flow is generally one of the basis for determining the expected income. Of course, for intangible assets, the future cash flow is generally not equal to the expected income, because when calculating the future cash flow, it often includes the cash flow brought by non-standard intangible assets, such as the existing labor force, business reputation, going concern value and other resources of the enterprise. These non-standard intangible assets are often contained in the enterprise as a whole and difficult to separate, which means that the amount of future cash flow is going to generally be higher than the expected income of the intangible assets themselves.

In the process of litigation, there is an independent third party enterprise's cost sharing similar to the company's business, the agreement does not include the cost of stock option used for employee incentive into the scope of cost sharing. The court held that the the arm's length principle is the fundamental principle to solve the problem of related party transactions.

The reason why the US revenue agency does not obey the above judgment is that the principle of cost to benefit matching is a special provision of the cost sharing agreement, while the the arm's length principle is not only applicable to the cost sharing agreement, but also belongs to the general provisions, and the special provisions should take precedence over the general provisions.

In addition to the internationally recognized problem of cost sharing agreement, there are also some problems in the collection and management of cost sharing agreement in China. The relevant laws and regulations of cost sharing agreement appeared late in China. In 2009, the implementation measures for special tax adjustment (trial implementation) began to systematically regulate the cost sharing agreement. And the State Administration of Taxation issued t*he Announcement No. 45 on standardizing the management of cost sharing agreement* in 2015, the approval procedure of cost sharing agreement has been canceled and some regulations related to follow-up management have been added. China's provisions on cost sharing agreement are framework, but there are no provisions on many practical problems, such as the pricing of joining payment and compensation payment, the distribution method of expected income, the adjustment of participants' changes, and some of the problems mentioned above. What's more, the cases of cost sharing agreement in China are very limited, which can not provide strong support for tax authorities in dealing with specific cases.

4.8.3 The advance pricing system is not comprehensive enough

Unilateral, bilateral and multilateral APA can confirm the transfer pricing problem of enterprises to a certain extent, but because the subject of unilateral APA is only the tax authorities of one country, it can not solve the international double taxation problem faced by enterprises in cross-border transactions.

Although APA has many advantages in the process of anti tax avoidance management of transfer pricing, APA requires a lot of human, financial and material resources. In addition, companies need to provide a lot of information for the achievement of APA, such as employing a third party to conduct repeated analysis and argumentation, and issuing audit materials, At the same time, it also needs a lot of time and professionals to communicate with the tax authorities, and it also needs to pay a lot of application fees to adopt the APA. Because the cost of making advance pricing agreement is too high, small affiliated enterprises often give up adopting advance pricing system because of cost consideration.

4.9 Suggestions on anti tax avoidance management of transfer pricing in China

4.9.1 Define the scope of intangible assets

On the one hand, the scope of intangible assets is the cornerstone of the whole intangible assets transfer pricing tax system and the premise for the subsequent tax treatment to operate reasonably. On the other hand, the scope of intangible assets is not the same in all countries, Some assets do not belong to intangible assets in other countries, but they belong to intangible assets in China. Clarifying the scope of intangible assets can enhance the standardization of China's tax law and reduce the risk of violation of tax compliance. At present, the definition of intangible assets in China is still a little confused, especially in the *enterprise income tax law* and *measures for the implementation of special tax adjustment*. The scope of intangible assets stipulated by the two laws is slightly different. Therefore, it is necessary to unify the scope of intangible assets in various laws and regulations. Especially for internationally controversial issues, such as collective labor, on-the-job labor, goodwill and sustainable use value, we should first define these concepts, and then specify whether these concepts belong to intangible assets.

From the perspective of anti tax avoidance, China's intangible assets can refer to the OECD transfer pricing guide and try to adopt the definition method. At the same time, It’s better for the scope of intangible assets to be wide rather than narrow, especially in the environment of "market for technology" in China, a large number of foreign capital enter the Chinese market in the form of joint ventures, and a large number of intangible assets royalties flow to foreign countries. Choosing a wide scope of intangible assets can also play an important role in curbing multinational enterprises from using intangible assets to avoid tax. However, for some controversial issues, such as collective labor, on-the-job labor, goodwill and sustainable use value, the government can carefully include them in the list of intangible assets from the aspects of tax compliance and convergence with accounting policies. Generally speaking, China can adopt the combination of enumeration method and definition method. The definition method similar to OECD can clearly classify intangible assets, and then use the enumeration method to assist the definition scope of the above intangible assets, so as to enhance the operability of policies.

4.9.2 Improve the cost sharing agreement

China has formed a relatively complete set of cost sharing agreement tax system, which provides a basic system guarantee for tax workers to work against tax avoidance. However, there are still many details to be improved, such as the introduction of special guidance for many specific issues. The first is the evaluation of expected return. Developing countries have the advantage of low cost of human capital and land rent, and the increase of expected

benefits not only comes from the increase of income, but also can be achieved by developing countries using the cost advantage. Therefore, the cost sharing agreement can be considered from these two aspects, that is, the increased profits can not be fully attributed to investment and technology, and the cost saving factor should also be considered. In addition, the consumer demand in developing countries is strong, and the consumer products turn from low-end to high-end, which will lead to some industries' profit margins higher than the global level. Therefore, when determining the expected return, we should also consider the factor of excess profit. Similarly, not only the factors of cost saving and excess profit need to be considered when quantifying the expected benefits, but also these two factors should be considered when apportioning the costs according to the expected benefits. For example, when the participants in developing countries employ employees with low labor costs but relatively high personnel quality when participating in R & D, they should also be considered, The contribution proportion of the participant will be greater than the cost proportion of the actual expenditure. Therefore, in this case, the tax authorities should consider the cost saving factors to adjust the cost sharing agreement when conducting the anti avoidance investigation.

At present, China is still a developing country, and its labor cost and market consumption demand have certain advantages compared with those of developed countries. Therefore, cost saving and excess profit factors need to be considered not only when China carries out the tax system reform of cost sharing agreement in the future, but also when tax staff carry out the anti tax avoidance investigation. As for the conflict between matching principle and independent transaction principle in cost sharing agreement, China should clearly define the scope of cost sharing. Especially for the controversial cost such as the cost of stock option used for employee incentive, the tax authorities should carefully weigh the tax interests of all parties after being included in the scope of cost sharing, and make clear provisions.

The transaction of intangible assets is very common in western developed countries, so the accumulation of relevant data and cases is also very considerable, which provides great convenience for enterprises and tax authorities to find comparable uncontrolled transactions as reference objects. China can also build an intangible assets trading platform to accumulate intangible assets trading data, so as to cultivate the market mechanism of intangible assets trading. At the same time, tax authorities and judicial authorities can also focus on strengthening the collection of intangible assets transfer pricing cases, and establish and classify the case base of intangible assets transfer pricing, so as to provide clearer legal guidance for enterprises.

4.9.3 Improve the reservation pricing system

At present, most of the APAs that China has completed are signed in the form of unilateral, but unilateral APA has certain limitations, which requires China to actively participate in international tax information exchange, cooperate with tax authorities of other countries on international transfer anti tax avoidance issues, win-win on an equal footing, and strengthen communication and cooperation in bilateral / multilateral APA, In order to better understand the overall tax situation of multinational enterprises and improve the current situation of international double taxation, we should work together.

In the practice of APA, because the successful signing of an APA requires a lot of manpower, financial and material resources, many SMEs give up APA. On March 19, 2021, the State Administration of Taxation issued the notice on matters related to *the application of summary procedures to unilateral Advance Pricing Arrangements (Draft for comments)* (hereinafter referred to as the draft for comments) and the corresponding policy interpretation notes. It intends to further introduce the summary procedures of unilateral advance pricing on the basis of the current advance pricing arrangements system, This rule is conducive to the implementation of advance pricing arrangements for small and medium-sized enterprises. [47] The tax bureau can also make clear the relevant fees of advance pricing arrangements, and carry out certain guidance in the preparation of information at the same time.

4.9.4 Institutional setting of supervision department

Any perfect legislation and legal system needs good implementation in order to achieve the desired effect. At the same time, it is also of great significance to strengthen the law enforcement practice of anti tax avoidance.

China can set up special anti tax avoidance supervision departments to strengthen contact and cooperation with customs, industry and Commerce and other departments. As the object of anti tax avoidance work is generally large multinational companies and enterprises, it is not only professional, but also very difficult. Therefore, the central and local governments should unite to carry out the anti avoidance work, establish a special anti avoidance Department throughout the country, focus on the anti avoidance work, and improve the efficiency of anti avoidance. We can set up transfer pricing investigation center, transfer pricing Arbitration Center, etc. by concentrating excellent professionals nationwide, and the special center is responsible for dealing with professional anti tax avoidance affairs. The work of anti tax avoidance is complex and difficult, so we should prevent in advance, deal with and supervise in the process. The most important thing is to strengthen the daily supervision of multinational companies in China. Anti tax avoidance work should be combined with daily

[47] Unilateral APA summary procedure will provide tax certainty for enterprises quickly- KPMG China Tax News - March 2012

tax collection and management, strengthen the supervision of annual declaration of related party transactions, and find problems in time through strict daily supervision. In addition, we should strengthen the inspection of multinational companies. Select the typical multinational companies with long-term losses but increased investment as the objects of inspection, and make detailed preparations before the investigation, so as to improve the efficiency of anti tax avoidance law enforcement.

The key to anti tax avoidance is to strengthen tax management. The good development of tax collection and management benefits from excellent tax personnel. No matter how perfect the tax law is, no matter how specific tax avoidance measures are, we need experienced personnel who are familiar with the relevant tax laws and regulations, because anti tax avoidance issues involve customs, finance and taxation, law, economy and other aspects, which are highly professional and complex. However, China is especially short of high-level anti tax avoidance professionals, so the training experience of the United States for professionals is worthy of our attention. The United States strictly control the quality of tax staff, carry out special training for them, and timely adjust the training content in the tax way with strong pertinence. First of all, it is necessary to carry out a strict screening system for new employees in the tax department. Moreover, new recruits need to exercise at the grassroots level for a period of time, and only after passing the examination can they become anti tax avoidance supervisors. At the same time, we should attach importance to and strengthen the training of anti tax avoidance personnel. In order to carry out business training and exchange in various forms, we can organize and participate in the study of relevant professional courses, conduct seminars on typical tax avoidance cases nationwide, learn from foreign advanced practical experience, timely understand the latest trends of international tax avoidance, master advanced anti tax avoidance methods, and accumulate rich anti tax avoidance work experience in practice.

Finally, with the rapid development of computer industry, especially artificial intelligence and big data industry in recent years, multinational companies use transfer pricing to avoid tax, which has become a new means of tax avoidance. It increases greatly the difficulty of anti tax avoidance investigation, due to the characteristics of e-commerce transaction virtualization. Moreover, compared with developed countries, as a developing country, China's tax inspection means are single and backward. Therefore, the tax authorities should keep pace with the times, improve the means of tax inspection, use high-tech equipment and means, such as the establishment of a large database to conduct tax inspection, increase the intensity of inspection, and improve the efficiency of inspection.

V.Conclusion

Tax avoidance has always been a hot topic. Chinese and Western scholars, especially economists, have done a lot of research. On the one hand, with the rapid development of economy, multinational companies try every means to avoid tax liability and maximize profits. On the other hand, various countries take various measures to prevent and combat international tax avoidance. The essence of anti international tax avoidance is to fight for and balance international tax sources.

In the past decade, China has made great progress in the construction of transfer pricing system of intangible assets, drawing on the advanced theories of OECD and the practical experience of foreign developed countries, and combining with the specific situation of China. China's tax law departments will adjust the relevant provisions of transfer pricing according to the international situation almost every year. However, compared with the United States, in terms of the degree of detail of the law, there is still a great lack of guidance on some specific problems.

Based on the analysis of the current situation of transfer pricing in China and the comparison of relevant laws and regulations with developed countries in Europe and the United States, this thesis finds out the differences between China's transfer pricing rules and developed countries in Europe and the United States. The first is that the scope of intangible assets is not clear enough. China mostly uses enumeration method to define intangible assets, because the coverage of enumeration method is limited, The definition of the scope of intangible assets is not clear enough.Second, the tax management of cost sharing agreement is not standardized, because China's labor and raw material costs are low, multinational companies need to consider this factor when sharing costs, instead of just considering the value-added part brought by technology and process innovation. Third, the APA system is not perfect. China's APA system is mainly unilateral and the rules are complex. It is necessary to strengthen cooperation with foreign countries, reduce the burden on small and micro enterprises and provide them with some guidance.

Finally, according to the deficiencies and problems mentioned in the appeal, combined with the advanced tax rules of European and American developed countries and the current situation of China's tax law, this thesis proposes a combination of definition method and example method to improve the scope of intangible assets, and adjust the cost sharing agreement considering the cost saving factors, four suggestions on strengthening bilateral or multilateral APA, strengthening communication and cooperation, and setting up supervision department.

Multinational companies are bound to constantly update the means of tax avoidance and seek new ways of tax avoidance with the development of modernization. According to the actual situation, we should improve the relevant anti avoidance legislation, strengthen the sharing of tax information resources at home and abroad, increase the intensity of punishment, prevent and combat international tax avoidance, and safeguard the tax sovereignty of all countries.

The harmfulness of tax avoidance by multinational corporations and the rampancy of tax avoidance activities make the work of anti international tax avoidance imminent. However, anti tax avoidance is a complex and long-term work. The tax avoidance means of multinational companies emerge in endlessly, more and more hidden, more and more complex, which makes the anti tax avoidance work more difficult. Because the principle of tax sovereignty and tax policies of different countries are very different, it brings convenience to multinational companies to avoid tax. However, China's anti tax avoidance legislation is not perfect, and the law enforcement practice is lack of experience, which increases the difficulty of China's anti tax avoidance work to a certain extent, and affects the effectiveness of China's tax collection and management. Therefore, China have to strengthen the fight against Transnational Corporations' tax avoidance from the aspects of perfecting anti tax avoidance legislation and strengthening law enforcement. Due to the complexity and professionalism of anti tax avoidance work, China could strengthen its contact and cooperation with other countries, revise international tax treaties timely, and make use of tax information exchange to intensify anti tax avoidance work.

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