Steering through Turbulence

Transfer pricing, Dispute resolution

Hanoi -- October 2019
Transfer Pricing audit trends in 2019
Tax audit/inspection target in 2019

7% ▲
Increase Tax Revenue (VND1,2 trillion ~ USD55 billion)

18.5% ▲
Increase # tax audit/inspection (~88,000 companies)

Tax payers at high risk of transfer pricing audit/inspection

✓ Enterprises having continuous loss making, fluctuating profits
✓ Enterprises which have not been audited for a long period
✓ Enterprises having intra-group services (e.g. royalties, license fee…)
✓ Enterprises having significant related party transactions
Transfer Pricing audit actual figures

* Source: Ministry of Finance web portal; Vietnam Financial Times
Procedures on Transfer Pricing audit/inspection
Procedures on Transfer Pricing audit/inspection

1. Identify the subject of inspection

- Local Tax Department (LTD) initiates risk analysis to conduct the list of inspected companies

November

December/January of the following year

• LTD sends out the inspection list to General Department of Taxation (GDT) for approval

by February of the following year

• LTD receives the approved list of inspected companies

Announce the annual inspection plan

• Announce to tax payers and their relevant tax authorities within 30 working days from the issuance date of the decision on the approval of the inspection plan.
Transfer Pricing audit / inspection procedures are conducted similar to tax audit / inspection procedures as there is no separate procedure available.

1. Preparation for inspection at taxpayer’s premise
2. Announce the inspection decision
3. Tax inspection terms applied for taxpayers
4. Extension of the inspection terms
5. Cases where audit/inspection decisions are postponed
6. Cases where audit/inspection decisions are abolished
7. Audit/inspection procedures are paused
8. Taxpayers do not comply with tax audit/inspection decision
9. Additional inspection contents
10. Changes of the head/members of the inspection team
11. On-site tax audit/inspection at the Company
12. Make inspection minutes
13. End of the inspection
14. Keep records of the inspection
3. Procedures on Transfer Pricing audit/inspection

- **Inspection Decision**
  - **Sent out to the Taxpayer**
  - **GDT conducts the procedure within (i) 45 working days or (ii) 70 working days for cases where extensions are applicable**
  - **Tax Department/ District Tax Department conducts the procedure within (i) 30 working days or (ii) 45 working days for cases where extensions are applicable**

- **Inquiry for documents/Conduct minutes of data confirmation**
  - **Taxpayer signs**
  - **5 working days**

- **End of Inspection**
  - **Announce the Inspection Minutes**
  - **Taxpayer does not sign**
  - **On-site Inspection**
  - **5 working days**
  - **GDT conducts the procedure within (i) 45 working days or (ii) 70 working days for cases where extensions are applicable**

- **Conclusion of the Inspection**
  - **Sign the Inspection Minutes**
  - **Taxpayer files a written request for delay of inspection**

- **Decision on sanctioning Tax and Administrative violations**
  - **(i) Decision on sanctioning Tax and Administrative violations. (ii) Conclusion based on the Inspection Minutes**

- **Conclusion**

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Procedures on Transfer Pricing audit/inspection

4. General procedures and descriptions on Transfer Pricing audit/inspection

Transfer Pricing audit/inspection could be carried out separately or conducted together with general tax audit/inspection

- **Separate Transfer Pricing Audit**
  - Standard requests typically include around 11-16 items
  - Highlights: items that can be used for adjustment purposes
    - Details of purchases from both related and unrelated parties
    - Details of sales to both related and unrelated parties
    - Transfer pricing documentation

- **Inspection conducted together with general tax audit/inspection**
  - Tax inspectors can request for transfer pricing documentation; and
  - Challenge the taxpayer’s transfer pricing position
Areas of Transfer Pricing audit focus / key challenges
Areas of Transfer Pricing focus / challenge

- Compliance
- Data reporting (accuracy & consistency)
- Comparable data
Areas of Transfer Pricing focus / key challenges

Art 9-2(d) Art 12-3 of Decree 20:

“Tax authorities have the right to make TP assessment (using database of tax authorities, i.e., ‘secret’ data)…if taxpayer commits the following violations:

- Failure to submit RPT declaration (Form 1) or submitting incomplete forms
- Failure to provide TP documentation within the permitted time limited as requested by tax authority; or submitting “insufficient” information
- Providing untruthful / unlawful information
- Inappropriate application of safe harbor / exemption rules (Article 11)”
## Areas of Transfer Pricing focus / key challenges

<table>
<thead>
<tr>
<th>Compliance</th>
</tr>
</thead>
</table>
| - Failure to file Related Party Transactions Disclosure Forms, **or**, filing of incomplete forms  
- TP documentation **was not** “contemporaneous” (not prepared in reasonable time when RPTs occurred (Cir 66) or by the CIT filing date(Decree 20)  
- TP documentation **not submitted** to the tax authorities within the prescribed timeline, or submission of incomplete TP documentation |
Areas of Transfer Pricing focus / key challenges

- **Data reporting**
  (Accuracy & consistency)

  - Inaccurate figures disclosed (inconsistency with audited financials, source data, etc.)
  - Inconsistent disclosure of RPTs between TP forms and TP documentation
  - Inconsistent disclosure of TP methods between TP forms and TP documentation
Areas of Transfer Pricing focus / key challenges

Comparable data

- Tax officials will attempt to scrutinize the taxpayer’s benchmarking analysis.

Common challenges include:

- No Vietnamese comparables
- Data of comparables not reliable (i.e., no audited financials)
- No evidence to prove comparables enter into transactions at arm’s length
- Comparables having different functions, products, etc.

- By discrediting the comparable data, tax official will assert that taxpayer was non-compliant and make TP adjustment using “secret” data
Areas of Transfer Pricing focus / key challenges

- Intra-group services
- Payment for the right to use intangibles (e.g. royalties, trademark license fee, etc.)
- Payment of interest expense
- Purchases of fixed assets
Case studies
### Case Study 1 – Management Fees (1/5)

<table>
<thead>
<tr>
<th>ABC Vietnam (FY2018)</th>
<th>US$ million</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sales</strong></td>
<td>A</td>
</tr>
<tr>
<td><strong>COGS</strong></td>
<td>B</td>
</tr>
<tr>
<td><strong>GP</strong></td>
<td>C = A – B</td>
</tr>
<tr>
<td><strong>SGA</strong></td>
<td>D</td>
</tr>
<tr>
<td><strong>OP</strong></td>
<td>E = C - D</td>
</tr>
<tr>
<td><strong>OM</strong></td>
<td>E/A</td>
</tr>
</tbody>
</table>

**ABC Company is a manufacturer of furniture**

- Established at the end of 2017
- Sells mainly to 3rd party dealers and retailers in Vietnam
- Related party transactions:
  - Pays management fees of US$ 2 million to its HQ (Thailand)
  - Purchase raw materials of US$ 50 million from related parties in Malaysia and Indonesia
- ABC has not prepared TP Doc and not filed TP forms
- ABC Vietnam has been audited by the HCMC Tax Department.
Transfer Pricing Audit Trends:

Case Study 1 – Management Fees (2/5)

Tax authority challenged two issues:

1. Management fees paid are non-deductible
2. ABC Company incurred loss, so the transfer pricing is not arm’s length. Tax authority wants to make a TP adjustment to increase taxable profits of taxpayer
Management fees paid are non-deductible

- **Have services actually been rendered?**
- **Do the services provide benefit to taxpayer?**
- **Is the amount of the service charge reasonable / reliable?**

### Before – tax / TP adjustment
**US$ million**

<table>
<thead>
<tr>
<th>Item</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>A 100</td>
</tr>
<tr>
<td>COGS</td>
<td>B 85</td>
</tr>
<tr>
<td>GP</td>
<td>C = A-B 15</td>
</tr>
<tr>
<td>SGA</td>
<td>D 16</td>
</tr>
<tr>
<td>OP</td>
<td>E = C-D -1</td>
</tr>
<tr>
<td>OM</td>
<td>E/A -1%</td>
</tr>
</tbody>
</table>

### After adjustment of management fee
**US$ million**

<table>
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<tr>
<th>Item</th>
<th>Value</th>
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<tr>
<td>SGA</td>
<td>D 14</td>
</tr>
<tr>
<td>OP</td>
<td>E = C-D 1</td>
</tr>
<tr>
<td>OM</td>
<td>E/A 1%</td>
</tr>
</tbody>
</table>

Transfer Pricing Audit Trends:

**Case Study 1 – Management Fees (3/5)**

**GM**

1. Have services actually been rendered?
2. Do the services provide benefit to taxpayer?
3. Is the amount of the service charge reasonable / reliable?
Case Study 1 – Management Fees (4/5)

Tax authority made a TP adjustment to increase taxable profits of taxpayer to 3% OM ratio based on secret data of the tax officials.

<table>
<thead>
<tr>
<th>After adjustment of management fee US$ millions</th>
<th>After TP adjustment US$ millions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sales</strong> A</td>
<td><strong>A</strong></td>
</tr>
<tr>
<td><strong>COGS</strong> B</td>
<td><strong>85</strong></td>
</tr>
<tr>
<td><strong>GP</strong> C = A - B</td>
<td><strong>15</strong></td>
</tr>
<tr>
<td><strong>SGA</strong> D</td>
<td><strong>14</strong></td>
</tr>
<tr>
<td><strong>OP</strong> E = C - D</td>
<td><strong>1</strong></td>
</tr>
<tr>
<td><strong>OM</strong> E/A</td>
<td><strong>1%</strong></td>
</tr>
<tr>
<td><strong>Sales</strong> A</td>
<td><strong>100</strong></td>
</tr>
<tr>
<td><strong>COGS</strong></td>
<td></td>
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<tr>
<td><strong>GP</strong></td>
<td></td>
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<tr>
<td><strong>SGA</strong></td>
<td></td>
</tr>
<tr>
<td><strong>OP</strong></td>
<td><strong>3</strong></td>
</tr>
<tr>
<td><strong>OM</strong> E/A</td>
<td><strong>3%</strong></td>
</tr>
</tbody>
</table>
Transfer Pricing Audit Trends:

Case Study 1 – Management Fees (5/5)

Key issues:

✓ Without TP Doc / TP forms, taxpayer does not have strong position to defend the audit

✓ Intra-group services fee is the key focus of tax authority, and is extremely difficult to defend if not well prepared and without supporting documents.

✓ Loss-making companies are often challenged by tax authority. Key arguments to support losses:
  - Commercial reasons for the loss (start-up, high fixed costs, market entry strategy, etc.)
  - External factors (loss of key customer, market downturn, competition, etc.)
  - Consider ‘appropriate’ benchmarking analysis
### Case Study 2 – ‘True-down’ adjustment (1/2)

#### ABC Vietnam (FY2018) US$ millions

<table>
<thead>
<tr>
<th></th>
<th>A</th>
<th>B</th>
<th>C = A-B</th>
<th>D</th>
<th>E = C-D</th>
<th>E/A</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>100</td>
<td>50</td>
<td>50</td>
<td>5</td>
<td>45</td>
<td>45%</td>
</tr>
<tr>
<td>COGS</td>
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<td>50</td>
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<tr>
<td>GP</td>
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</tbody>
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**ABC Company is a trading company.**

- Purchases all finished goods from Parent Company (Thailand) and sells to 3rd party dealers and retailers.
- ABC Company achieved ‘super’ profits.
- Parent Company wants to make a downward profit adjustment to a “reasonable” level.
Transfer Pricing Audit Trends:

Case Study 2 – ‘True-down’ adjustment (2/2)

Key issues:

Accounting & reporting
- How / timing to actually book the adjustment?
- Will the financial auditor agree to this?

Tax / TP audit
- What are the risks / challenges from tax authority?

Other issues
- Customs risks?
- Cash remittance?
Tips for resolving Transfer Pricing audit/inspection
Tax/Transfer Pricing audits in Vietnam

- No standardized process for transfer pricing audit is available, leading to inconsistent approaches among local tax authorities.

- Taxpayers should pay attention to the timeline request for the submission or supplement/ explanation of information during tax audit.

- Tax authorities are under pressure of conducting and completing audits in tight time frame.

- Content in draft Audit Minutes can be revised and negotiated several times before taxpayers and tax authorities reach an agreement.

- Recourse / appeal available to taxpayer, including review from high-level authority (MoF/GDT), court / litigation and mutual agreement procedures (MAP).
Tips for resolving Transfer Pricing audit/inspection (1/3)

During on-site Transfer Pricing Audit or Inspection

Before Transfer Pricing Audit or Inspection

Upon completion of the Transfer Pricing Audit or Inspection

Before Transfer Pricing Audit/Inspection

- Form 01, Form 03-7, Transfer Pricing Documentation
- Supporting documents for particular RPTs (intra-group services, royalties)
- Understand reasons for tax audit/inspection and a list of documents to be prepared
- Arrange time to fully and well prepare before tax audit/inspection
- Notice to relevant departments (for example, regional/head quarter finance director)
- Involve external advisors to review tax issues for timely adjustments and/or reporting
Tips for resolving Transfer Pricing audit/inspection (2/3)

During on-site Transfer Pricing Audit/Inspection

- Appoint experienced staff to work with tax audit/inspection teams
- Try to resolve issues through dialogue before being recorded in Minutes on tax audit/inspection
- Negotiate and accept “win-win” solutions that benefit both parties
- Consult the board of directors' opinions on important issues
- Pre-discussion with transfer pricing officials that companies can appeal/dispute transfer pricing audit/inspection results to avoid their surprises
- When requested to sign Memorandum of Facts, ensure the documents have been reviewed and approved by the Board of Directors
- If you do not accept the results, only "confirm" but not "agree" to the adjustments made by tax audit/inspection team
### Tips for resolving Transfer Pricing audit/inspection (3/3)

#### During on-site Transfer Pricing Audit or Inspection

- Carefully review Memorandum of Facts and Minutes on tax audit/inspection and consider consulting with tax consultants.
- Decide which adjustments are acceptable or unacceptable.
- Prepare comments to include in the minutes and sign the minutes on time.
- If there is still a dispute, consider putting a conservative opinion in the minutes and ask for guidance from the GDT/MOF.

#### Before Transfer Pricing Audit or Inspection

- Submit dispute documents on time.

#### Upon completion of the Transfer Pricing Audit/Inspection

- When Decision on tax audit/inspection is issued, pay the tax collection and penalties while carrying out the dispute procedures to avoid interest penalties for late payment and enforcement measures.

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KPMG experience in Transfer Pricing audit/inspection support

In just 3 years

100+

... large FDI companies have been assisted with their tax audit under the MOF, GDT and provincial tax audit programs

We have a strongly dedicated and experienced transfer pricing audit and controversy working team

Co-Team:
9 Partners, 8 Directors

Transfer Pricing:
40+ Transfer pricing professionals in the North
03 Partners, 01 Director, 06 Associate Directors, 07 Managers

Tax Team

Legal Team

20 Associate Directors & Managers
KPMG Transfer Pricing Services

>30 full-time professionals in the North

~90 professionals in Vietnam

- Close relationship with GDT.
- Many TP audit and dispute resolution engagements, resolved successfully

Biggest & most experienced team in Vietnam

Capacity building projects for the GDT
- Work with OECD & World Bank
- Building capacity for officials of the GDT

Strong Dispute and Resolution team

Developing transfer pricing regulations in Vietnam
- Consultation in developing TP regulations in Vietnam
- Circular 201/2013/TT-BTC (APA regulation), Decree 20 and Circular 41.
<table>
<thead>
<tr>
<th>KPMG Transfer Pricing Dispute Services (1/2)</th>
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</thead>
<tbody>
<tr>
<td><strong>Preparation before transfer pricing audit</strong></td>
</tr>
<tr>
<td>- Review transfer pricing compliance to prepare for upcoming transfer pricing audit</td>
</tr>
<tr>
<td>- Assist in preparing/presenting information/documents to transfer pricing audit/inspection teams.</td>
</tr>
<tr>
<td><strong>Technical support in transfer pricing audit</strong></td>
</tr>
<tr>
<td>- Participate in the explanation of the required information for the transfer pricing audit/inspection team</td>
</tr>
<tr>
<td>- Advise explanation of contents for transfer pricing inspection teams</td>
</tr>
<tr>
<td>- Attend the meeting with the transfer pricing inspection team</td>
</tr>
<tr>
<td>- Professional support and strategic advice throughout the transfer pricing audit period to obtain the most favorable results</td>
</tr>
<tr>
<td><strong>Post transfer pricing audit review</strong></td>
</tr>
<tr>
<td>- Review Minutes on transfer pricing audit/inspection</td>
</tr>
<tr>
<td>- Suggest appropriate feedback</td>
</tr>
<tr>
<td>- Advise and analyze which tax issues in the Minutes and Decisions on tax collection should consider making dispute</td>
</tr>
</tbody>
</table>
KPMG Transfer Pricing Dispute Services (2/2)

**Tax ruling**
- Assisting enterprises in sending a written request for tax authorities to clarify or confirm the tax treatment for past or current transactions

**Dispute on tax audit/inspection result**
- Supporting enterprises to solve unresolved tax audit/inspection issues through formal dispute in the tax administration system (Local Tax Department, General Department of Taxation, Ministry of Finance)

**Industry Lobby**
- Representing a group of companies or industries to request tax administration to provide legal support
Q&A
Contact us

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