Members' Conference
on
Transfer Pricing Regulations in Bangladesh

Key-note Speaker

Mohammed Tofazzul Hussain FCA

Senior Consultant

HUSSAINS™
Business Consultants Ltd.
Creating Business Knowledge

Dhaka, April 23, 2015

BRIEF PROFILE OF THE KEY-NOTE SPEAKER

MR. MOHAMMED TOFAZZUL HUSSAIN FCA

Senior Consultant

HUSSAINS Business Consultants Ltd.
Creating Business Knowledge

UTC Building, Level 19, 8 Panthapath, Kawran Bazar
Dhaka 1215, Bangladesh

July 2014- date:	Senior Consultant, HUSSAINS Business Consultants Ltd
June 2008- June 2014:	Partner, A. Qasem & Co, Chartered Accountants, cooperating firm of PwC
April 2006- May 2008:	Partner, Octokhan, Chartered Accountants
April 2004- March 2006:	Asst. Manager, KPMG, Rahman Rahman Huq, Chartered Accountants
April 2001- March 2004:	Audit trainee Rahman Rahman Huq, Chartered Accountants

BRIEF PROFILE OF THE KEY-NOTE SPEAKER—contd..

Area of expertise:	Business Advisory, Corporate Tax
Overseas work experience:	Sri Lanka, UK
Training and presentation:	UAE, Germany, Hong Kong, China
Hobbies:	Reading, Cycling, Football, Travelling
Social work:	Capacity Building Program (Bishwamver Pur Shiny Kids Scholarship) at countryside Bishwamver Pur, Sunamgonj

TOPICS

1. INTRODUCTION AND BACKGROUND OF TRANSFER PRICING (TP) REGULATIONS

2. TRANSACTIONS AND FACTS THAT LEAD TO A TP SITUATION

3. APPLICABLE TP REGULATIONS IN BANGLADESH including pricing method, record keeping, reporting obligation, assessment and penalties

4. ANALYSIS OF LAW AND RELATED DISCUSSIONS ON TP RULES

5. CONCLUSION

6. Q&A

1. INTRODUCTION AND BACKGROUND OF TRANSFER PRICING (TP) REGULATIONS

- Greetings
- Welcome to today's members' conference on Transfer Pricing Regulations in Bangladesh.
- The main objective of this conference is to disseminate the much discussed information on transfer pricing regulations of Bangladesh- a current phenomenon in our tax regime.
- In Bangladesh, though TP regulations came into being in 2012, impetus for implementation is being observed since 2014
- Accordingly, there have been a lot of seminars and discussions on this topic of transfer pricing.

1. contd--

- Global definition of ‘Transfer Pricing’ is the setting of the price for goods and services sold between controlled (or related) legal entities within an enterprise.
- Globally, over 70 countries have adopted TP rules recently to monitor substantial amount of related party transactions (about 60% of transactions are executed among affiliated companies/ members of group companies)
- Such transactions allow companies ample scope to fix transaction prices at their best advantageous terms considering tax regimes
- Consequently, tax agencies may lose revenues, and this concern of tax avoidance through transfer pricing give rise to the concept of transfer pricing of related parties

1. contd--

- TRANSFER PRICING = TRANSACTION PRICING FOR PROFIT
- The motto of TP rule is not to discourage such inter-company/ related party transactions, rather it is to ensure that those transactions are being occurred at fair price i.e. arm's length price
- Thus focus of TP is on price - which is comparable and market driven

1. contd--

TP mechanism @ Unique Currency Unit

Multinational Company (MNC) Global ***Transaction at Market price in respective countries***				
MNC Cyprus Ltd		+	MNC Bangladesh Ltd	
Tax rate 10%			Tax rate 35%	
Sales	300		Sales	600
Purchases and Expenses	200		Purchase	300
			Expenses	100
Profit	100		Profit	200
Tax@10%	10		Tax@35%	70
Combined tax liability for MNC Global is (10+70)= 80				

1. contd--

TP mechanism @ Unique Currency Unit

Multinational Company (MNC) Global *Transaction at beneficial TP*				
MNC Cyprus Ltd		+	MNC Bangladesh Ltd	
Tax rate 10%			Tax rate 35%	
Sales	400		Sales	600
Purchases and Expenses	200		Purchase	400
			Expenses	100
Profit	200		Profit	100
Tax@10%	20		Tax@35%	35
Combined tax liability for MNC Global is (20+35)= 55				

1. contd--

from the above illustration, how much tax does our regime lose?

Tax Effect ***For Transactions at beneficial TP /Transfer Mispricing***		
Particular	Tax @	
	Market price	Transfer Mispricing
COMBINED TAX LIABILITY OF MNC GLOBAL	**80**	**55**
Tax Revenue for Bangladesh	70	35 !! half of regular tax
Tax Revenue for Cyprus	10	20

1. contd--

further slight change can cause NBR lose more taxes!!

MNC Cyprus Ltd		+	MNC Bangladesh Ltd	
Tax rate 10%			Tax rate 35%	
Sales	400		Sales	600
Purchases and Expenses	200-50 =150		Purchase	400
			Expenses + Management exp	100+50 =150
Profit	250		Profit	50
Tax@10%	25		Tax@35%	17.5
Combined tax liability for MNC Global is (25+17.5)= 42.5				

1. contd--

more tax losses for NBR for slight change in inter-company expenses sharing arrangement

Tax Effect		
Particular	Tax @	
	Market price	Transfer Mispricing
COMBINED TAX LIABILITY OF MNC GLOBAL	**80**	**42.5**
Tax Revenue for Bangladesh	70	17.5 !! Merely 25% of regular tax
Tax Revenue for Cyprus	10	25

2. TRANSACTIONS AND FACTS THAT LEAD TO A TP SITUATION

On the face

- International transactions
- Associated relationship
- International transaction exceeding BDT 30 million in a year
- Negotiated/ intentional pricing arrangement
- Head office expenses
- Charge for intellectual property or intangible assets (eg royalty, technical know-how, copyright, franchise, patent etc)
- Sharing of common cost

2. TRANSACTIONS AND FACTS THAT LEAD TO A TP SITUATION

In the eye of the DCT (courtesy- NBR CIC presentation at ICAB workshop on TP)

- Price deviated from the market price
- Gross profit rate is too low compared with industry average
- Shared expenses too high

3. APPLICABLE TP REGULATIONS IN BANGLADESH including pricing method, record keeping, reporting obligation, assessment and penalties

- The regulations on TP are stipulated under a separate new chapter XIA (section 107A- 107J- total of 10 sections) of Income Tax ordinance 1984 to be read in conjunction with related rules of the Income Tax Rules as amended upto date.

- The chapter containing the sections regarding TP is pretty thin, not so much daunting. 8 pages only. However, for the gravity of the topic, and its global popularity, transfer pricing is seemingly intimidating.

3. APPLICABLE TP REGULATIONS IN BANGLADESH

•Emanates from the authoritative sources such as:

ITO 1984 Chapter XIA

ITO Rules- 70-75A

SROs, Workshops conducted by ICAB in partnership with the tax officials of the National Board of Revenue

• Chapter XIA Transfer Pricing of the Income Tax Ordinance (ITO) 1984 of Bangladesh.

Microsoft Office Word Document

•Income Tax Rules 1984. Relevant Rules 70-75A

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3. ITO Sections and Rules on TP

- The Sections and Rules concerning us are:

107 A – Definitions

107 C – Computation of arm's length price in relation to any international transaction in combination with Rule 70, 71, 72

107E Maintenance and keeping of information, documents and records- As prescribed under section 107EE, 107F and Rule 73

107EE. Statement of international transactions to be submitted-

Re rule 75A

107F. Report from an accountant to be furnished- Re Rule 75

Penalty sections:

107 G-I

3. Section 107A Definitions are explicit though cross references may entangle any company engaged in international transactions

- Arm’s length price
- Associated enterprise
- Enterprises
- International transaction
- Permanent establishment
- Property
- Record
- Transaction
- Uncontrolled transaction

3. Section 107B

Determination of income from international transaction having regard to arm's length price-

Primary responsibility is of the assessee to ensure prices are fixed fairly and can be compared with the market prices

3. **Section 107C to be read in light of Rule 70-72**

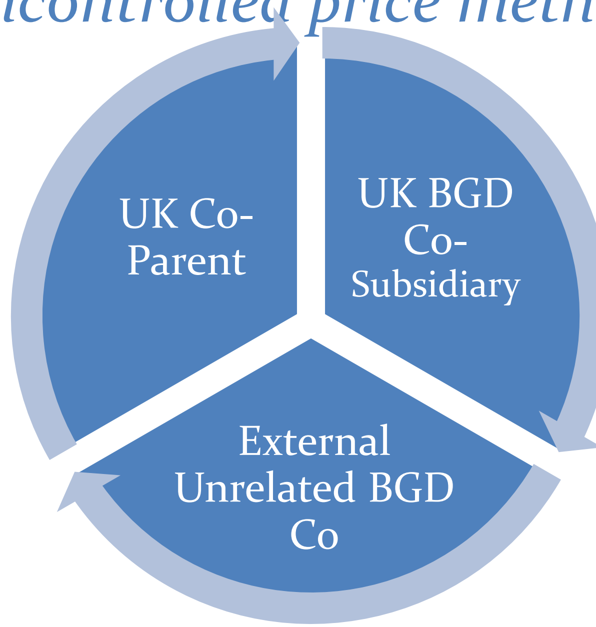
Computation of arm's length price

TP regime globally has 5 methods as recommended by OECD; however in Bangladesh we have 6 (5+1) methods to suit particular situation.

1. *Comparable uncontrolled price method*
2. *Resale price method*
3. *Cost plus method*
4. *Profit split method*
5. *Transactional net margin method*
6. *Any other method where it can be demonstrated that i. None of the methods mentioned in clause a or e can be reasonably applied to determine the arm's length price for the international transaction and ii. Such other method yields a result consistent with the arm's length price*

3.

1. *Comparable uncontrolled price method*



UK Co- Parent sells Smart Watch to	**UK BGD Co- Subsidiary in Bangladesh @ arranged price**
UK Co- also sells/ exports Smart Watch to	External Unrelated BGD Co in Bangladesh @ BDT 15,000/ watch
Here, Comparable Uncontrolled Price is BDT 15,000/ Smart Watch	

3.

2. *Resale price method*

The resale price method compares the gross profit realized when an entity re-sells goods to a related party to the gross profits realized by comparable entities in uncontrolled transactions.

Say, in the preceding example, External Unrelated BGD Co in Bangladesh sells the Smart Watch @ BDT 20,000/ watch	
So, retail price/ final price in Bangladesh	BDT 20,000
Less: Retail margin	BDT 5,000
Therefore, TP is	***BDT 15,000***

3.

3. *Cost Plus method*

Example follows:

Say, to manufacture the Smart Watch UK Co incurs following cost in BDT equivalent, then price the watch at a 50% mark-up on cost:	
Material	7,500
Labor	1,500
Overhead	1,000
Total cost	10,000
Mark-up @50% on cost	5,000
Therefore, TP is	***BDT 15,000***

3.

4. *Profit Split method*
   ref: Rule 70(1)(d)

(d) profit split method is applied in the following manner: —

(i) the combined profit, arising from international transaction or transactions and divisible among the associated enterprises, is identified.

(ii) the combined profit is then divided among the associated enterprises by using the prescribed approaches:

(iii) the profit thus allocated to the assessee under subclause is taken to be the arm's length price.

3.

5. *transactional net margin method*

Company Cost of goods sold	**50,000**
Company operating expenses	15,000
Total cost	65,000
Add: Mark-up @10% on cost	6,500
Therefore, TP is	***BDT 71,500***

3.

Most appropriate method

Re Rule 72

Factors to consider:

- the nature and class of the international transaction, and of enterprises entering into the international transaction;
- the comparability factors

3.

Record keeping

Re Rule 73 Information and documents to be kept and maintained under section 107E

Key information to maintain to support TP :

- Ownership profile
- Business profile
- Brief business profiles of each of the member of the group
- information on the business relationship
- consolidated financial statement of the group
- financial statements of the assessee enterprise
- information on economic and market analyses, forecasts, budgets
- details of all transactions with the associated enterprises;
- Contracts, etc

3.

Reporting obligation

Rule 75

Report from an accountant to be furnished under section 107F

Report from an accountant to be furnished under section 107F

1. The accounts and records of ---

-------(name and address of the assessee with TIN) relating to the international transactions entered into by the assessee during the income year ending on, _______________ has been examined by me.

2. It appears from our examination of the accounts and records that proper information and documents, as are required by the Income Tax Ordinance, 1984, have been kept by the in respect of the international transaction(s) entered into by the assessee.

3. The particulars required to be furnished under section 107F are given in the Annexure to this Form.

4. In my opinion and to the best of my information and according to the explanations given to me, the particulars given in the Annexure to this form are true and correct.

Signature

Name :

Address :

Membership No. :

Place : ______________

Date : ______________

3.

Reporting obligation

Rule 75A Statement of international transaction to be furnished under section 107EE

A. Particulars of the Assessee:

1. Name of the Assessee: ....

2. TIN:

3. (a) Circle: .... (b) Taxes Zone: ....

4. Assessment Year: ....

5. Income Year: From .... to ....

B. Particulars of International Transactions [See section 107A(5)]

Refer to the instructions before completing the following section.

PART-I

Tangible property of revenue and capital nature transaction

Item	Expense	TPM Code	%	Revenue	TPM code	%

3.

Reporting obligation

PART-II

Interest bearing loans, advances and investments (figures in thousand taka)

Item	Opening balance	Increase	Decrease	Closing balance

3.

Assessment

Ref Section: 107D. Reference to transfer pricing officer-

Envisaged assessment:

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3.

Penalties

Maximum 1% of the value of each international transaction

- **for failure to keep, maintain or furnish information, documents or records to the DCT- Section 107G**
- **for failure to comply with the notice or requisition under section 107C – sec 107H**

107I. Penalty for furnish report under section 107F-

- **Where any person fails to furnish a report from a chartered accountant as required by section 107F of this Ordinance, the DCT may impose upon such person a penalty of a sum not exceeding Tk 3 lac.**

4. ANALYSIS OF LAW AND RELATED DISCUSSIONS ON TP RULES

Tax office considers Transfer Pricing is the major tool for corporate tax avoidance by both local and multinational companies (MNCs) through capital flight by lowering profits in a division of an enterprise that is located in a country that levies high taxes and raise profits in a country that is a tax haven that levies no or low taxes.

Impetus came from United Nations Development Programme (UNDP) report in 2011 where UNDP placed it on the top of the list of developing countries suffering financial outflows due to transfer pricing.

Provisions and Rules relating to TP enacted in 2012-2103 followed by yearly addition of new Rule(s) to implement on a pilot basis from fiscal year 2014-2015 for the assessment year 2015-2016

4. ANALYSIS OF LAW AND RELATED DISCUSSIONS ON TP RULES

Selected taxmen are being trained to form TP Cells.

Officials said the full-fledged implementation of the TP law will need extensive preparations of taxmen. An aggressive TP policy might create a negative impression among the foreign companies. http://www.thefinancialexpress-bd.com/old/index.php?ref=MjBfMDhfMjlfMTNfMV8xXzE4MTUwMw==

Tax officials said although MNCs are regularly paying higher amounts of taxes, still there remains enough scope for collecting more taxes.

A total of $34.12 billion flew out of Bangladesh between the years 1990 and 2008, according to Global Financial Integrity (GFI), a Washington-based firm. That means the country lost $1.8 billion in capital a year during the period, causing the tax authority to lose a huge amount of revenue.

The TP cell would handle tax files of the taxpayers involved in international transactions. TP cell officials will determine the price and send a report to the circle office to complete assessment on the basis of decision by the TP official concerned. http://thebangladeshtoday.com/news/2014/08/drive-launched-to-check-tax-evasion-thru-transfer-pricing/

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Envisaged assessment cycle for an MNC under TP Cell: MNC heavily reliant on import purchase>NBR TP Cell>DCT

5. CONCLUSION

Therefore, though TP officials have power to look into any file, they may handle tax files of Companies heavily engaged in international transactions causing outflow of money from Bangladesh.

- THANKS TO ICAB FOR GIVING ME AN OPPORTUNITY TO SPEAK BEFORE YOU ON THIS TIMELY TOPIC.

- THANK YOU FOR YOUR PATIENT HEARING.

6. Q&A