Bulgaria will implement country-by-country reporting requirements

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In brief

On 25 May 2016, the European Council adopted rules on country-by-country ("CbC") reporting by multinational companies of tax-related information and exchange of that information among member states. The new rules cover groups of companies with a total consolidated revenue of at least €750 million. The principal aim is to prevent multinationals from exploiting the specifics of a tax system or mismatches between different tax systems, in order to reduce their tax liabilities.

As a Member State Bulgaria should adopt these rules in the domestic legislation by June 2017. The first CbC reports for Bulgaria should be prepared for FY 2016 and submitted to the National Revenue Agency by 31 December 2017. The exchange of CbC reports among the EU tax administrations should take place by 30 June 2018. After that date, the National Revenue Agency should have access to all CbC reports of multinational groups with operations in Bulgaria, which were submitted to the tax administrations of the other Member States. Thus, the Bulgarian tax administration will be able to assess to what extent the multinational groups operating in Bulgaria report reasonable profits in the country, which correspond to their actual local activities.

Country-by-country reporting

On 25 May 2016, the European Council adopted a Directive 2016/881 (the "Directive") that introduced mandatory country-by-country ("CbC") reporting within the European Union ("EU"). The Directive amends Directive 2011/16/EU with regard to mandatory automatic exchange of information in the field of taxation.

Bulgaria has to adopt the CbC reporting requirements in its legislation by June 2017.

The CbC reports contain information for each tax jurisdiction on revenue, profits, taxes paid, capital, earnings, tangible assets, number of employees as well as the business activities for all group members.

The Directive applies to EU and non-EU based multinational groups with operations in EU Member States having total consolidated group revenue exceeding EUR 750 million (unless lower thresholds are introduced at a local level by the Member States).

The CbC reports should be filed by the ultimate parent company of a multinational group to the tax authorities in its home jurisdiction. If the parent company is not required to file CbC reports (e.g. as it is based outside the EU), a designated group member or all group members located in the EU would be obliged to file (i.e. a secondary reporting mechanism will apply).

Once filed, the CbC reports will be subject to automatic exchange of information among the tax administrations of the Member States in which the group operates. As a result, the respective tax administrations will have an overview of the business activities of the group in all tax jurisdictions, allowing them to assess whether profits are taxed where the substance and people are located or instead profit shifting techniques are used (e.g. shifting profits to low tax jurisdictions without having substance there).

The first reports should be prepared for FY 2016, filed by 31 December 2017 and exchanged within the EU tax administrations by 30 June 2018. The filing deadline for the secondary reporting could be extended by one year (i.e. applying for FY 2017 onwards).

With the Bulgarian National Revenue Agency CbC reports should be filed by Bulgarian parent companies of multinational groups or Bulgarian subsidiaries/ permanent establishments of multinational groups which do not report in other EU states or non-EU states that exchange effectively information on the subject with Bulgaria.

OECD Transfer Pricing documentation requirements

On 23 May 2016 the OECD Council approved the incorporation of the three-tired transfer pricing (TP) documentation approach of BEPS Action plan 13 in the OECD TP Guidelines. These Guidelines serve as a basis for the countries when developing their local TP documentation rules.

The three-tired approach requires taxpayers to prepare transfer pricing (TP) documentation consisting of:

- Master file, containing standardised information relevant for all multinational group members;
- Local file, providing more detailed information on specific intercompany transactions, and
- CbC report, aggregating tax jurisdiction-wide information on the allocation of income, taxes paid and certain other indicators within the group, as discussed above.

Generally, the Local file should be finalised by the deadline for submission of the company's tax return, whereas the Master file should be ready by the tax return due date of the ultimate parent company.

Belgium, Germany, Italy, France, Poland, the Netherlands are among the countries that will adopt the above approach in their local legislations. Many others have announced to do the same.

Although Bulgaria is not an OECD Member, in their practices so far the local tax authorities tend to follow the OECD TP Guidelines.

So changes in the local tax legislation as regards TP documentation requirements may be also expected. In view of this, for illustrative purposes, we present below the information that is typically included in a Local TP file of group companies.

Skeleton of a Local TP file

1. Group overview (if not covered in a Master file)
   - History of the Group
   - Group financial data
   - Organisational, legal and operational structure of the Group
   - Functional profile of the Group
   - Ownership of intangible assets within the Group
   - Overview of applicable Group TP policy
   - Overview of Group inter-company transactions
   - Advance Pricing Agreements
   - Business strategy within the Group
2. Industry overview
3. Company Overview
   - Short history and description of activity, including products, markets, competitors
   - Main financial indicators
   - Legal, organisational and operational structure, including information on business reorganisations involving the company
   - Local business strategy of the company
   - Overview of company's affiliated transactions
4. Description and contractual basis of company's affiliated transactions, including amounts of intra-group payments & receipts per transaction per related party
5. Functional and Risk Analysis, describing functions performed, risks assumed and assets used
6. Economic Analysis
   - Selection of transfer pricing method
   - Tested party
   - Profit level indicator
   - Multiple year / Annual analysis
   - Description of any comparability adjustment performed
   - Interquartile range
   - Individual economic analysis for each related party transaction (including benchmarking study) & conclusion

Takeaway

The introduction of the CbC reporting in Bulgaria will increase the compliance burden of Bulgarian parent companies and Bulgarian subsidiaries of large multinational groups.

The CbC reporting will provide the Bulgarian tax administration with information allowing it to expand its scrutiny beyond the locally available data and perform an analysis on the tax position of the Bulgarian companies in the context of the overall group operations. As a result, the new rules are likely to trigger an increase of TP related tax audits.

Therefore, a proactive approach and preparing strong TP documentation in place is recommendable in view of the forthcoming changes.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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