

30 July 2019

Global Tax Alert

News from Transfer Pricing

Mongolia amends its transfer pricing regulations

NEW! EY Tax News Update: Global Edition

EY's new Tax News Update: Global Edition is a free, personalized email subscription service that allows you to receive EY Global Tax Alerts, newsletters, events, and thought leadership published across all areas of tax. Access more information about the tool and registration [here](#).

Also available is our [EY Global Tax Alert Library](#) on ey.com.

Executive summary

Mongolia recently revised its key tax laws including the General Law on Taxation, Corporate Income Tax Law and Personal Income Tax Law. The new laws were adopted by the Mongolian Parliament (the legislative body) on 22 March 2019, under the Government's tax reform packages.

A number of important changes that may have a material impact on taxpayers, requires taking appropriate actions to comply with the new requirements. Among others, the transfer pricing laws and associated rules have been amended to align with recent international developments and standards.

The Ministry of Finance is expected to release a number of implementing guidelines on the new rules.

The new tax rules will take effect on 1 January 2020.

This Alert highlights key changes regarding the transfer pricing developments.

Detailed discussion

Overview of transfer pricing developments

Various sections in the current tax laws refer to the need for transactions between related parties to be conducted on an arm's-length basis. Failing this, the tax authorities may seek to adjust the transaction to a fair market value.

The transfer pricing rules are currently set forth in various individual tax laws including the General Taxation Law (GTL), Corporate Income Tax (CIT) Law, Value Added Tax (VAT) Law, and Personal Income Tax (PIT) Law. Definitions and rules sometimes differ among the various laws, creating uncertainty in application.

The new transfer pricing law, which will be governed mainly by the GTL and its associated guidelines, replaces the existing hodgepodge of separate laws.

Definition of related parties redefined

The old rules define related party as:

- ▶ Under Article 48.4 of the GTL - related party shall mean "bodies who are authorized to participate directly or indirectly in the management, control or ownership" of other entities.
- ▶ Under Article 6.1 of the CIT Law - if the following relation is present with a taxpayer, it shall be a related party: (1) owns 20% or more of the common stock of the other entity; or (2) has the right to receive 20% or more of the dividends or distributions from the other entity; or (3) has the right to appoint 20% or more of the management of the other entity or is otherwise able to determine its policies.

Under the new transfer pricing rules, the term "related party" means:

Article 27 of New GTL - Related parties:

The entities who have the ability to influence each other on the conditions or economic outcome of a transaction by way of a direct or indirect participation, by a person in the other, or the same person in two or more persons, of the assets, control or managerial activities.

In addition, unrelated parties may be treated as related parties if they have entered into an arrangement for which the parties have agreed to a common position or common interest for a particular transaction.

Transfer pricing documentation requirements

Under the transfer pricing regulations, taxpayers are required to maintain contemporaneous documentation to comply with the arm's-length standard. Part of that documentation must substantiate the most reliable measure of an arm's-length result, given the transfer pricing methods and data available.

Consistent with the Organisation for Economic Co-operation and Development (OECD), Mongolia now will require taxpayers with related-party transactions to adopt the internationally-standardized **Master file, Local file, and Country-by-Country (CbC) Report** three-tiered approach to transfer pricing documentation.

The main objectives of the updated transfer pricing documentation requirements are to ensure that taxpayers give appropriate consideration to transfer pricing requirements in establishing prices between related parties; to provide tax administrations with the information necessary to conduct an informed transfer pricing risk assessment; and to provide tax administrations with useful information to conduct an appropriately thorough audit of the transfer pricing practices of entities subject to tax in their jurisdiction.

The Mongolian Tax Authority (MTA) will be further introducing detailed tax and transfer pricing reporting forms on the above transfer pricing reports.

Deadline for filing transfer pricing documentation

Type of documents	Deadline	Who shall file?
Transfer Pricing Transactional Report (an annual report) (New GTL doesn't provide a description on the content of this report and it is expected to be further clarified with upcoming implementing guidelines)	10 February following the year end	All taxpayers with related-party transactions
Master file	10 February following the year end	Companies or groups with annual turnover of more than MNT6 billion for the preceding tax year; or foreign-invested companies irrespective of size
Local file	10 February following the year end	
CbC report	Within the 12-month period after the last day of group financial year	A group parent entity which resides in Mongolia; or other assigned entities

Taxpayers shall be required to provide additional information related to transfer pricing documentation prior to or during the tax audits.

Threshold and exemption from transfer pricing documentation obligations

Mongolia has not set any threshold to exempt smaller transactions from transfer pricing documentation obligations. Instead, Smaller and Medium Enterprise group companies under MNT6 billion annual turnover are exempt from certain transfer pricing documentation requirements (i.e., local file and master file). The CbC reporting threshold is set at MNT1.7 trillion or approx. €630 million (while the OECD's recommendation was €750 million).

Administrative penalties for failure to comply with transfer pricing documentation obligations

As outlined in the table above, all transfer pricing documentation is required to be submitted by taxpayers to the MTA within the specified timeframe by law.

The new rules have imposed severe administrative penalties for failure to comply with transfer pricing documentation requirements i.e., if transfer pricing documentation is not filed with the tax authorities within the specified deadline, there will be automatic penalties. These automatic administrative penalties are equal to 2% - 4% of transaction value (as set out in the table below), apart from penalties and fines resulting from transfer pricing adjustments (if any).

Type of documents	Automatic administrative penalty	Frequency
Transfer Pricing Transactional Report (an annual report)	2% of respective related party transaction value	Per non-compliance
Master file	3% of respective related party transaction value	Per non-compliance
Local file	3% of respective related party transaction value	Per non-compliance
CbC report	4% of respective related party transaction value	Per non-compliance

OECD Transfer Pricing Guidelines

Despite the fact that Mongolia is not a member of the OECD, Mongolia has endorsed the OECD Transfer Pricing Guidelines in the GTL. With this, the OECD Transfer Pricing Guidelines may be applied by the MTA for assessing pricing arrangements of related parties provided that the OECD Transfer Pricing Guidelines do not conflict with the arm's-length principles set out in the domestic tax laws and relevant implementing guidelines.

Actions required

The new transfer pricing documentation requirements will create additional compliance and due diligence work for taxpayers. It is expected that it will be time consuming to arrange the internal department structure and business processes to perform the work required, and to collect overseas related party information. Local group companies or multinational enterprises should proactively review their global tax framework, the value chain related to the Mongolian business, and determine whether related-party pricing arrangements are arm's length.

Based on the new transfer pricing risk assessment tools, the MTA would likely select the target companies for special transfer pricing audits. Therefore, it is important that taxpayers pay special attention to the information provided in the new forms submitted. Incomplete or inconsistent filings or documentation could attract the attention of the MTA and lead to transfer pricing audits.

For additional information with respect to this Alert, please contact the following:

Ernst & Young Tax Services Limited, Hong Kong

- ▶ Martin Richter martin.richter@hk.ey.com

Ernst & Young TMZ LLC, International Tax Services – Transfer Pricing, Mongolia

- ▶ Khishignemekh Regzedmaa khishignemekh.regzedmaa@mn.ey.com

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

Transfer Pricing Group

© 2019 EYGM Limited.
All Rights Reserved.

EYG no. 002863-19Gbl

1508-1600216 NY
ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com