



cutting through complexity

Global Transfer Pricing Review

Bulgaria

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TAX



Bulgaria



KPMG observation

Tax authorities are showing increased interest in transfer pricing and in recent years, KPMG in Bulgaria has observed several material tax audit assessments related to transfer pricing.

Bulgarian taxpayers increasingly seek to prepare transfer pricing documentation or localize their group-level master files in order to mitigate the tax risk associated with related party transactions.

The Bulgarian tax authorities currently do not have access to the Amadeus database. Their transfer pricing efforts are mainly focused on

- scrutinizing available transfer pricing documentation
- exploring potential internal comparables
- obtaining comparable data from competitors of the taxpayer; and
- assigning transfer pricing analysis of related party transactions to external valuation specialists. These valuers may not have access to Amadeus and their approach may be discretionary sometimes.

The preparation of transfer pricing documentation therefore provides the taxpayer with a relatively strong defense for the price levels of its related party transactions.

Transfer pricing study snapshot

The purpose of a transfer pricing study

	Not applicable	Applicable
Legal requirements		●
Protection from penalties	●	
Reduce risk of adjustment		●
Shifts burden of proof		●

Basic information

Tax authority name

The tax authority in Bulgaria is the National Revenue Agency at the Ministry of Finance. The National Revenue Agency reviews transfer pricing issues in the course of ordinary tax audits.

Citation for transfer pricing rules

The transfer pricing legislation in Bulgaria is contained in:

- Article 15 of the Corporate Income Tax Act
- Article 27, paragraph 3 of the VAT Act
- Article 116 of the Tax and Social Security Procedure Code (TSSPC)

- Ordinance N-9 of 14.08.2006 on the application of transfer pricing methods.

Under the rules set out in the legislation, if related parties perform transactions at prices different from market levels, the taxable base may be adjusted to market prices. This applies for corporate income tax and, in limited cases, for VAT purposes. As a result of these adjustments, an

additional 10 percent corporate income tax and in certain cases, a negative VAT effect of 20 percent may apply.

Further, the difference between related party transaction prices and market levels may be classified as hidden distribution of profits. In such cases, a 20 percent administrative penalty and five percent withholding tax may be applied.

Taxpayers have the burden to prove to the authorities that their transactions are performed under market conditions. If they are unable to do so, the tax authorities are allowed to establish an appropriate market price and adjust the taxable base to it.

In 2010 a transfer pricing manual (Manual) was published by the tax authorities, containing guidance on transfer pricing issues. The Manual is generally based on the 2009 Organisation for Economic Co-operation and Development (OECD) Guidelines and the European Union (EU) Transfer Pricing Code of Conduct.

Effective date of transfer pricing rules

Detailed transfer pricing rules were first introduced through Ordinance N-9 of 14 August 2006.

What is the relationship threshold for transfer pricing rules to apply between parties?

The Tax and Social Security Procedure Code (TSSPC) sets a threshold of direct ownership of five percent of the capital of a company. Other criteria for related parties also apply, including common directors, ability to exercise control, etc.

What is the statute of limitations on assessment of transfer pricing adjustments?

The general statute of limitations for tax liabilities is five years from 1 January of the year following the year when the tax was payable (i.e. when the corporate tax return was filed). For example, the statute of limitations for 2009 expires at the end of 2015.

Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be submitted to the revenue authority on an annual basis (e.g. with the tax return)?

Yes. Part of the FY 2014 tax return required information regarding related party transactions and transactions with low-tax jurisdiction entities to be

submitted. The FY 2015 return has not been published yet and it is not clear whether this disclosure and its form would be preserved.

What types of transfer pricing information must be disclosed?

Total value of revenue and costs from related party transactions and separately from transactions with low-tax jurisdiction entities.

Outstanding receivables and liabilities to related parties and to entities from low-tax jurisdictions.

Please consider this information was already changed for the FY 2014 tax return as compared to the FY2013. Thus, it may change for the purposes of the FY 2015 tax return again.

What are the consequences of failure to submit disclosures?

There is still ongoing debate regarding the mandatory nature of the disclosure included in the tax return. Thus, explicit penalties have not been introduced regarding failure to submit this disclosure. However, our experience shows that a conservative approach would usually involve submitting the disclosure.

Transfer pricing study overview

Can documentation be filed in a language other than the local language? If yes, which ones?

No.

When a transfer pricing study is prepared, should its content follow Chapter V of the Organisation for Economic Co-operation and Development (OECD) Guidelines?

Generally yes, although Bulgaria is not an OECD member and the OECD Guidelines are not mandatory for taxpayers and the tax authorities. However, the tax authorities usually accept the principles outlined in the OECD Guidelines.

The Manual of the tax authorities also refers to the EU Transfer Pricing Code of Conduct as a source for the content of transfer pricing documentation.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

Transfer pricing methods

Does your country follow the transfer pricing methods outlined in Chapter II of the OECD Guidelines? If exceptions apply, please describe.

No. The hierarchy of TP methods is still applicable in Bulgaria.

Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? And if so, how many days?

Yes. 14 days.

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? Please explain.

Usually, the tax authorities submit a request for provision of documents and the taxpayer has 14 or 15 days to comply. However, this deadline may be extended or the tax audit procedure may be suspended for up to three months.

If the taxpayer does not submit the documentation within the required deadline, the tax authorities may assume that no documentation is available and may perform a transfer pricing analysis of their own.

If an adjustment is proposed by the tax authority, what dispute resolution options are available?

The decision of the tax authorities may be appealed at the administrative level (before a regional appeal directorate) and subsequently at the judiciary level (before a court).

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

An administrative penalty of 20 percent may be applied where an expense charged by a related party is deemed to be hidden distribution of profits.

To what extent are transfer pricing penalties enforced?

The extent of enforcement cannot be monitored in detail as tax proceedings

are not public until the court appeal phase. Nevertheless, in recent years KPMG in Bulgaria have observed a significant increase in the number and materiality of transfer pricing issues being identified by tax authorities.

Recently, for the purpose of performing transfer pricing adjustments, the authorities have been assigning transfer pricing studies to valuation specialists from their "List of independent experts". Although these experts may not have access to Amadeus and their transfer pricing experience may be sometimes limited, their studies may be used by the authorities and possibly accepted in the process of court appeals.

What defenses are available with respect to penalties?

The established way of substantiating related party transactions is by the preparation of a local transfer pricing file covering the Bulgarian market.

In a limited number of cases, transfer prices may be defended by building up arguments based on pricing policies, cost allocation methodologies, market analyses etc.

However, such an approach highly depends on the specific circumstances of the case and its success may not be guaranteed.

What trends are being observed currently?

As noted, there is an increasing interest in transfer pricing issues by both taxpayers and the tax administration. It has been noted in transactions involving goods that the authorities generally seek price adjustments, however, in services transactions they tend to focus on the actual provision of the services.

Special considerations

Are secret comparables used by tax authorities?

Tax authorities have indicated in informal discussions that they may use secret comparables. However, the feasibility of this approach is not yet certain.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

Yes, the authorities require a benchmarking study to start the initial search from the Bulgarian market.

Do tax authorities have requirements or preferences regarding databases for comparables?

No. However, Amadeus is generally accepted.

Does the tax authority generally focus on the interquartile range in a TNMM analysis?

Yes, sometimes.

Does the tax authority have other preferences in benchmarking? If so, please describe.

Not applicable.

What level of interaction do tax authorities have with customs authorities?

Moderate, however, currently increasing.

Are there limitations on deductibility of management fees beyond the arm's length principle?

Yes, subject to proper documentation and benefit for the recipient.

Are management fees subject to withholding?

Yes.

Are there limitations on the deductibility of royalties beyond the arm's length principle?

Yes. Royalties may not be deductible if the licensing transaction is classified by the authorities as artificial and aimed at tax evasion. Arguments for this may be lack of actual benefit for the local entity from the transaction.

Are royalties subject to withholding?

Yes.

Are taxpayers allowed to file tax return numbers that differ from book numbers?

Yes, subject to substantiation with documents, budgets and a transfer pricing study.

Other unique attributes?

None.

Tax treaty/double tax resolution

What is the extent of the double tax treaty network?

Extensive. About 70 tax treaties are in force.

If extensive, is the competent authority effective in obtaining double tax relief?

With respect to the usual application of tax treaties – frequently.

With respect to Mutual Agreement Procedures (MAPs) – only one MAP has been initiated so far and is not yet complete, noting that it was initiated by a foreign tax administration.

When may a taxpayer submit an adjustment to competent authority?

Not applicable.

May a taxpayer go to competent authority before paying tax?

There are no formal rules. A taxpayer may submit a request for guidance from the tax authorities on specific issues. However, receiving an answer from the tax authorities does not guarantee consistent treatment of the issues in future.

Advance pricing agreements

What APA options are available, if any?

None.

Is there a filing fee for APAs?

Not applicable.

Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

Not applicable.

Are there any difficulties or limitations on the availability or effectiveness of APAs?

Not applicable.

KPMG in Bulgaria

Kalin Hadjidimov

Tel: +35929697700

Email: khadjudimov@kpmg.com

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