

# Transfer Pricing Country Summary Bulgaria

September 2018

## Legislation

### Existence of Transfer Pricing Laws/Guidelines<sup>1</sup>

Regarding the Bulgarian transfer pricing regime, the following primary legislations are relevant:

- Corporate Income Tax Act (CITA) (Prom. SG No. 105 from December 22, 2006, last amended SG No. 97/5.12.2017, effective 1.01.2018, supplemented, SG No. 103/28.12.2017, effective 1.01.2018);
- Tax and Social Security Procedures Code (TIPC) (Prom. SG No. 105 from December 29, 2005, last amended, amended and supplemented, SG No. 97/6.12.2016, effective 1.01.2017. In particular, Article 116, which states the relationship thresholds that determine related party status);
- Double taxation treaties enacted by Bulgaria;
- Value Added Tax Act ( 8, amended, SG No. 96/1.12.2017, effective 1.01.2018, amended and supplemented, SG No. 97/5.12.2017, effective 1.01.2018);
- Accountancy Act (Prom. SG No. 95 from December 8, 2015, applicable from January 1, 2016 and amended and supplemented, SG No. 97/5.12.2017, effective 1.01.2018).
- Administrative Procedure Code, published in the Official Gazette 30/11 April 2006, last amendment by SG No. 74/20.09.2016.<sup>2 3</sup>

The following secondary legislations are also relevant:

- Ordinance No. H-9 for implementation of transfer pricing methods (the Ordinance H-9) (Prom. SG 70 from August 29, 2006). This Ordinance was issued by the Minister of Finance and is binding as long as it does not contradict acts of higher rank.

In terms of the Bulgarian transfer pricing regime, Ordinance H-9 is the explicit regulation defining the mode of application of the methods to define market prices. The CITA also provides definitions of market price, transfer price and it sets arm's length price (Articles 15 and 16). In addition, the TIPC provides the definition of related party, market price and the method for determining the market price.

In general, these regulations are in line with both the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD TP Guidelines) and the European Union's Code of Conduct for Transfer Pricing Documentation for Associated Enterprises.

### Definition of Related Party

<sup>1</sup> Sources: <http://www.minfin.bg/en/174>

<sup>2</sup>[https://uk.practicallaw.thomsonreuters.com/w-007-3438?transitionType=Default&contextData=\(sc.Default\)&firstPage=true&comp=pluk&bhcp=1](https://uk.practicallaw.thomsonreuters.com/w-007-3438?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1)

<sup>3</sup> file:///C:/Users/A.mendes/Downloads/Code\_of\_Administrative\_Procedure.pdf

The Bulgarian Corporate Income Tax Act refers to the definition of related parties contained in the Tax and Social Security Procedures Code (TSSPC). According to the TSSPC, related parties are:

- Spouses, lineal relatives, collateral relatives up to the third degree of consanguinity, and affines up to the second degree of affinity and, for the purposes of Item 2 of Article 123 (1) herein, where included in a common household;
- Employer and employee;
- Shareholders/partners;
- Persons, where one of them participates in the management of the other or its subsidiary; or in whose management or controlling body participates one and the same person (legal or natural person), including cases when the natural person is a representative of another person;
- A company and a person, where the person owns more than 5% of the company's shares with voting rights. Note that according to the Bulgarian regulations, a related party relationship for tax purposes is established not only in case of control, but also in the case where one of the parties holds 5% of the voting shares of the other party. However, the taxpayer should be aware that the definition of related party for Bulgarian tax purposes is significantly different from that used for Bulgarian accounting purposes. The latter requires common control.
- Persons, where one of them exercises "control" over the other;
- Persons whose activity is controlled by a third person or its subsidiary; Persons exercising joint control over a third person or its subsidiary;
- Persons, where one of them is a commercial representative of the other;
- Persons, where one of them has made a donation to the other;
- Persons, who participate (directly or indirectly) in the management, the control or the capital of another person or persons, thus being able to negotiate terms, different from the regular ones.

"Control", under the definition provided by the Bulgarian legislation, is present when the controlling party: owns directly or indirectly, or under an agreement with another person, more than half of the votes at the general meeting of another person, or has the possibility to determine directly or indirectly more than half of the members of the managing or controlling body of another person, or has the possibility to manage, including through or together with a subsidiary, in accordance with a particular statute or contract, the activity of another person, or as a shareholder or a partner in an entity controls independently, in accordance with a deal made with other partners or shareholders of the same entity, more than half of the votes in the general meeting of this entity, or can be by other means exert a decisive influence over the decision-making with respect to the activity of the entity.

There is no separate procedure for transfer pricing investigations. In terms of transfer pricing issues, the relevant investigations are performed as a part of the general tax audit procedures.

## Transfer Pricing Scrutiny

In February 2010, the Bulgarian National Revenue Agency (NRA) announced new Transfer Pricing Documentation Guidelines, which is a part of the NRA's TP audit manual. It is to clarify the documentation requirements, which is in line with both the OECD Transfer Pricing Guidelines and the

Code of Conduct for Transfer Pricing Documentation for Associated Enterprises of the European Union. However, the 2010 version of the OECD Guidelines, in which the hierarchy of methods is abolished, has not yet been introduced in the local transfer pricing legislation. Ordinance № H-9 of 14.08.2006 for the Order and Ways of Applying the Transfer Pricing Methods, art. 62 and art. 63.<sup>4</sup> Furthermore, the Bulgarian transfer pricing rules do not explicitly deal with business restructuring.

Despite the fact that the new Transfer Pricing Documentation Guidelines are not a part of the binding law, NRA reserves the right to challenge the data prepared by the taxpayer in the course of a tax audit. Considering the fact that the burden of proof concerning transfer pricing policy is allocated to the taxpayer, compliance with the new transfer pricing guidelines may minimize the risk.

## Transfer Pricing Penalties

As an incentive, it may be considered that, if during a tax audit, a taxpayer presents TP documentation (that meets certain requirements) to the revenue authorities, then they should start their analysis from the method chosen by the taxpayer, and only if it is deemed inappropriate, use another one.

If, a reporting entity, that has an obligation to file CbC report in Bulgaria, but doesn't do it, within the stipulated deadline, should be subject to a fine of BGN 100,000 to BGN 200,000.

If, a reporting entity, files a CbC report, but omits, or declares false or incomplete data in it, the reporting entity should be subject to a fine of BGN 50,000 to BGN 150,000. The same fine should be applied if the incomplete or wrong data are due to a refusal of the ultimate parent entity to present the required data.

If, a constituent entity, that has an obligation to file a CbC report and does not notify the Bulgarian tax authorities if the ultimate parent entity has refused to provide the requested information, that constituent entity should be subject to a fine of BGN 10,000.

If, a constituent entity, fails to notify the revenue authorities whether it, or some other group entity, will file the CbC report, it should be subject to a fine of BGN 50,000 to BGN 150,000.

In case of a repeated violation of the rules higher fines apply

## Advance Pricing Agreement (APA)

There is no regime for Advance Pricing Agreements ("APAs"). However, the taxpayer may obtain a non-binding opinion from the NRA on a case-by-case basis.

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<sup>4</sup> <https://www.oecd.org/tax/transfer-pricing/transfer-pricing-country-profile-bulgaria.pdf>

## Documentation And Disclosure Requirements

### Tax Return Disclosures

As of 2014, the taxpayers are required to submit an appendix to their annual tax return presenting information regarding the annual turnover of transactions with related parties.

A failure to prepare or submit disclosures has as a consequence an administrative sanction in the amount of EUR 50-500.

### Level of Documentation

Taxpayers bear the burden of proof regarding the arm's length nature of the controlled price, and must present all relevant evidence. However, there is no legally binding transfer pricing documentation requirements. It is recommended that the taxpayers follow the Transfer Pricing Documentation Guidelines in this respect.

Based on the Transfer Pricing Documentation Guidelines, the documentation should contain information on the following topics:

- Presentation of the group:
  - Legal, functional, finance and management organization of the group (legal, functional, finance and management organizational charts of the group);
  - Economic role of the divisions within the group;
  - Allocation and financing of intellectual property.
- Information of the controlled company and its activity:
  - Object of activity and market of the company (an economic analysis of the market: structure, size, competitors, development, success factors and risks);
  - Functional analysis of the company;
  - Use of intellectual property;
  - Financing of the enterprise.
- Analysis of associated transactions:
  - Presentation of the selected economic model: an explanation of the specific strategy of the enterprise (for example, the penetration policy to gain a share of a particular market);
  - Presentation of the associated transactions: objects of transactions, distribution, services, financial transactions, contracts, countries involved, special terms and conditions.
- Functional analysis:

- Who plays what role in an associated transaction; analysis of functions, risks and assets of each party in the transaction;
- Analysis of methods: presentation of the transfer pricing method used;
- Economic and financial analysis of the transaction: profits, analysis of the market, nature of the financial terms and conditions.
- In addition, the transfer pricing documentation should be available and be disclosed to the NRA upon request in the course of company audits or as otherwise requested by the authorities.

## Record Keeping

The taxpayer is obliged to keep records for a period of five years after the expiry of the statute of limitations for the relevant tax year, i.e. for a period of 5 years from the end of the calendar year in which the tax for a given tax year is due.

In practice, as the tax return should be submitted (and the tax due should be paid) three months after the end of the tax year, the tax liability for e.g. the tax year 2009 expires at the end of December 2015 (provided the tax year is equal to the calendar year, which is the most common case). The records should be kept during this period.

## Language for Documentation

The documentation should be prepared in Bulgarian. However, the above mentioned file may contain documentation in other languages but the NRA may require certified translations to be made of all or any part of it at the expense of the taxpayer.

## Small and Medium Sized Enterprises (SMEs)

Bulgaria does not apply a special definition of SMEs for transfer pricing purposes. Companies are not subject to different **pro**cedural rules in relation to transfer pricing depending on their size (e.g. assets, employees or turnover).

## Deadline to Prepare Documentation

There is no statutory deadline to prepare documentation. However, the documentation could be requested by the NRA during a tax audit or a tax check. If requested, the transfer pricing documentation must be provided to the tax administration within seven to 30 days of request. In practice, it is typically required within 14 or 15 days after the request. However, the deadline can be extended or a tax audit procedure can be suspended for up to three months pending the information.

NRA's TP audit manual recommends preparing transfer pricing documentation for a given fiscal year by the date of submitting the corporate tax return.

## Deadline to Submit Documentation

There is no requirement for annual submission of documentation.

## Statute Of Limitations

A tax liability is enforceable during 5 years from the end of the calendar year in which the tax for a given tax year is due. In practice, as the tax return should be submitted (and the tax due should be paid) three months after the end of the tax year, the tax liability for e.g. tax year 2009 expires at the end of December 2015 (provided the tax year is equal to the calendar year, which is the most common case).

## Transfer Pricing Methods

In general, the Bulgarian transfer pricing regulations are in line with the OECD Transfer Pricing Guidelines (22 July 2010), although Bulgaria is not an OECD member country. Under the TIPC and Ordinance H-9 there are five methods to define the market price:

- Comparable Uncontrolled Method;
- Resale Price Method; and
- Cost Plus Method.
- Transactional Net Margin Method; and
- Profit Split Method.

The applicability of the CUP method should be tested first. If it is not appropriate, it should be checked whether the Resale Price or the Cost Plus methods could be reliably applied. Only when all the three traditional methods have been deemed inappropriate the transactional ones (the TNMM and the Profit Split) may be used. The taxpayer is allowed to choose the most appropriate transfer pricing method, and the tax authority is obliged to follow the chosen method in the course of audit. However, the tax authorities reserve the right to challenge the taxpayer.

## Comparables

Under the Bulgarian TP legislation, four factors should be considered for the comparability analysis. One of them is the economic environment. The domestic comparables are usually preferred as they are generally considered more reliable, since it is difficult to find other countries with similar economic environment. However, if there are not enough local comparables, foreign ones could be used.

Databases of the National Statistics Institute, economic branch organization, statistical reference books, online and paper publications, as well as database such as Amadeus and Orbis are admissible for transfer pricing purposes. The NRA does not have access to Amadeus and Orbis.

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