A Study on the Improvement of Income Tax reporting For Business Combinations in Mongolia

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Abstract

In line with the international trend and practice of deeming associated entities as a single economic unit and assessing the taxable income at the group level based on the consolidated income tax statements, many countries in the world including the United States, Australia, New Zealand, and France allow the preparation of consolidated income tax returns and provide special tax credits and exemptions for transactions between the parent and subsidiaries companies of the group, unrealized gains (losses) arising from them, and intercompany dividends.

This study aims to examine the needs and demand to prepare a consolidated income tax report, the current practice of business combinations to file income tax returns, and some issues related to the methodology of preparing a consolidated income tax statement. This study also attempts to prepare a consolidated income tax statement form for national business combinations according to the international trend within the framework of the currently acting laws and regulations of Mongolia and to prepare recommendations for improving the consolidated income tax reporting for the business combinations. This paper uses a Ten-step methodology for recording the impact of income tax within the framework of IFRS used in the research of B.Byambakhishig (2017). Our data covers separate financial statements, income tax reports, intercompany transactions, and other related financial data of "AM" LLC (Canadian-invested mining company) and its fully controlled "ASI" LLC, which operates business in mining subcontracting, software development, and analytics.

The study lacks a recording of the impact of income tax and income tax consolidation, therefore, a further study will be conducted on the consideration related to the analysis of the Consolidated Income Tax Statements.

Keywords: Consolidated income tax statement, intra-group transactions, unearned gains (loss), tax discount and redemption, transfer pricing adjustment

1. Introduction

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The role of business combinations and multinational companies is important in the growth and development of the economy of any country as well as the world. It is estimated that about 65% of the world's total trade turnover is not between multinational companies but between parents and subsidiaries within group companies. As of today, about seven thousand business combinations are operating in our country (NSO's Business Register Database in Mongolia 2022)

The revised Accounting Law of Mongolia (2015) requires that a company or enterprise with more than one subsidiary prepare consolidated financial statements and assign the responsibility to prepare and present the consolidated financial statements to the parent company of a group.

However, Mongolia has no legal provisions or regulations for preparing and presenting consolidated income tax statements.
Despite the attention focused on accounting issues associated with consolidated entities, income tax effects cannot be ignored. Certain tax considerations have a direct impact on the financial reporting of any consolidated entity.

For independent and group companies, the optimal recording and reporting of income tax is the basis of management decision-making as well as tax planning, so Mongolia joined the OECD as the 111th member country of the Organization against Base Reduction and Profit Shifting ("BEPS"). Internal transactions of interrelated parties or groups (intra-group transactions of business combinations) based on the recommendations of the Cooperation Development Organization) in domestic legislation, with particular attention to tax planning and implementing regulations on BEPS and General Anti-Avoidance Prevention Rules ("GAAR") in the General Tax Law and Corporate Income Tax Law to a certain extent.

Currently, in our country, each legal entity prepares a separate corporate income tax return, and the tax legislation does not yet provide for the preparation and presentation of a consolidated income tax return.

This paper uses a Ten-step methodology for recording the impact of income tax within the framework of IFRS by IASB (2023) used in the research of B.Byambakhishig (2017).
To optimize tax planning and harmonize taxation with the basic principles of fairness and efficiency, it is necessary to prepare consolidated income tax statements of group companies, and it is important to study the intra-group transactions, their income tax implications, and their impact on consolidated financial statements.

Therefore, based on the income tax impact of the internal transactions of the group company, its inclusion in the consolidated financial statements, and international experience, we have determined the importance of preparing and presenting consolidated income tax statements, developing a methodology for preparing the consolidated income tax statements of the group companies by the relevant laws of Mongolia.

Methods of collecting data were adopted in consolidation and performance techniques gathered by reviewing a wide range of financial and tax reports including separate financial statements, tax reports, intercompany transactions, and other related financial data of "AM" LLC (Canadian-invested mining company) and its fully controlled "ASI" LLC, which operates business in mining subcontracting, software development, and analytics in 2021.
This study is regarded to help provide financial and strategic information to top managers of business and policymakers.

2. Literature review

Tax consolidation, or consolidated reporting, is a regime adopted in the tax or revenue legislation of many countries that treats a group of controlled companies as a single entity for tax purposes.

In line with the international trend and practice of deeming associated entities as a single economic unit and assessing the taxable income at the group level based on the consolidated income tax statements, many countries in the world including the United States, Australia, New Zealand, and France allow the preparation of consolidated income tax returns and provide special tax credits and exemptions for transactions between the parent and subsidiaries companies of the group, unrealized gains (losses) arising from them, and intercompany dividends.

Many researchers and academicians indicate the advantages of preparing consolidated Income tax statements and have developed a methodology for recording the impact of income tax within the framework of IFRSs.

The practice of preparing a consolidated Income tax statement and its advantages

Preparing a consolidated income tax statement:

- Losses reported by the tax return of a related party can be used by other members of the group to reduce their taxable income. In most circumstances, it is regulated so that the losses reported by the separate tax returns of a group member before the consolidation can only be carried forward against the future taxable income of that particular company;
- Inter-company dividends are not included in the taxable income;
- Unrealized gains arising from intercompany transactions are not included in the taxable income and are deferred until realized. (On the other hand, unrealized losses arising from intercompany transactions are not included in expense deductible from the taxable income and are equally deferred until realized);
- It reduces the administration and audit costs of tax authorities; and
- It reduces the costs, time, and complexity associated with preparing and reporting income tax statements for parent and subsidiary companies within the group.

U.S. GAAP by FASB on accounting for income taxes and International Accounting Standard 12 by IASB each require consolidated entities to recognize both current tax effects and anticipated future tax consequences using deferred tax assets and liabilities. For many financial reporting tax issues that arise with consolidated entities, the standards are the same.
The 10-step methodology for recording the impact of income tax within the framework of IFRS is defined at the theoretical level as follows:

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(1) Determining differences between financial and tax accounting; (2) Calculation of tax expenses for the reporting period; (3) To calculate the adjustment of tax expenses for the previous reporting period;(4). Calculation of deferred tax assets and liabilities on the reporting date;(5) Assess all deferred tax assets to be recognized;(6) Identification, recognition, measurement, and recording of tax uncertainty;(7) Consolidation of income tax accounts;(8) Calculate tax expenses/income and include them in the profit and loss statement, other comprehensive income, and appropriate assets;(9) Determining the effective tax rate and preparing adjustments.

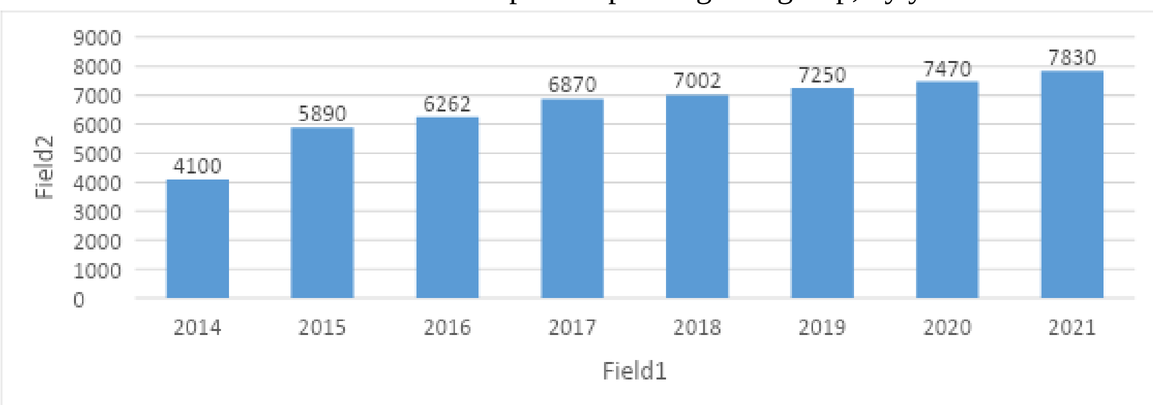
3. The Income Tax Reporting of Business Combinations in Mongolia

According to the statistical data of National Statistical Office (NSO) and Mongolian Tax Authority (MTA), the number of active companies or taxpayers registered as Economic Entities Income Tax (EEIT) taxpayers has been increasing every year and has reached nearly 71,000 by the end of 2022.

About 92% of actively operating companies are small and medium-sized enterprises with assets up to MNT500 million and sales income up to MNT1.5 billion, however their share in total assets is 2% and the share in sales income is about 10%. The number of public interest companies with assets over MNT 500 million MNT and sales income over MNT1.5 billion account for 8% of the total number of companies, but they generate 98% of the total assets and about 90% of the sales income.

Results of the survey of business combinations show that the number of enterprises that operate a group has been growing rapidly since 2014.

Chart 1. Number of enterprises operating as a group, by years



Source: Review by researchers based on data from the National Statistics Office's Business Register Database

As of 2022, about 8% of all EEIT payers and all 100 large taxpayers except for 10 state-owned joint-stock companies recognized by the MTA (Erdenet Mining Corporation LLC OyuTolgoi LLC Mongol Alt MAK LL Erdenes Tavantolgoi JSC Boldtumur Eruu Gol LLC Golomt Bank LLC Energy resource LLC Unitel LLC…) as top taxpayers operate as a business combination.

The statistics above illustrate that companies operating in the form of a group have a significant contribution to the collection of the state budget tax income. Therefore, it is of utmost importance to ensure that these business combinations, as a single economic unit, assess and report their taxes, particularly the EEIT in a fair and just manner on the grounds of basic principles of tax fairness and efficiency.

Under Article 48.4 of the currently acting General Taxation Law, related party shall mean ”bodies who are authorized to participate directly or indirectly in the management, control or ownership” of other entities. Furthermore, under Article 6.1 of the Economic Entities Income Tax Law – if the following relation is present with a taxpayer, it shall be a related party:

- owns 20% or more of the common stock of the other entity; or
- has the right to receive 20% or more of the dividends or distributions from the other entity; or
- has the right to appoint 20% or more of the management of the other entity or is otherwise able to determine its policies.

On December 24, 2015, “*The Arms-length Pricing Methodology*” was adopted by Order No. 353 of the Minister of Finance, and “Form for reporting transactions of work, services, and goods between related parties” (Form XMX-01) was approved by Order A/96 of the Commissioner of the Mongolian Tax Administration on April 28, 2017. Taxpayers have been filing transfer pricing reports since 2017 using this Form to disclose their related party transactions.

Where the price, payment, and fee applied by the taxpayer for transactions such as sales, purchases, sending personnel, providing technical services, and conducting cooperative production with related parties in Mongolia and abroad (starting now referred to as "prices") are greater or less than the arms-length price, the arms-length pricing method is used to assess the taxes.

As Mongolia became the 111th member country of the Organization Against Tax Base Erosion and Profit Shifting (“BEPS”), it was necessary to incorporate the transfer pricing-related recommendations of the Organization for Economic Co-operation and Development (OECD) into the domestic legislation and pay special attention to the transactions and tax planning between related parties or business combinations. Therefore, in 2019, the tax laws were revised to adopt BEPS and General Anti-Tax Avoidance Rules (“GAAR”), principles and good practices under the "Tax Base Erosion and Profit Shifting" project implemented internationally.

4. Data and Findings (case study) for Consolidated Income Tax Statement

"AM" LLC is a Canadian-invested mining company that was established in 2007. "ASI" LLC is a fully controlled subsidiary of "AM" LLC that does business in mining subcontracting, software development, and analytics. The following statement has been prepared by the guidelines to prepare a consolidated financial statement based on the separate financial statements, the EEIT returns, and the details of intra-group transactions of the related companies in the business group.

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1. Identification of the business entities to be consolidated.
AM LLC and ASI LLC are a parent and subsidiary under the definition in the company law of Mongolia. Under article 6.4 of the Company Law, ASI LLC, the subsidiary shall file a separate financial statement, in contrast, AM LLC, the parent company shall file a consolidated financial statement for the group.

2. Preparation of separate EEIT returns of the entities for consolidation.

Table 1. Economic Entities Income Tax returns

A. Assessment of tax at the common rate: /accrued from the beginning of the year, in MNT/

Indicators	Row	Parent	Subsidiary
1. The total amount of income	1	2,597,625,844	930,948,778
2. Costs of goods sold and other expenses	2	1,949,424,338	765,545,132
3. Taxable income (row 1-2)	3	648,201,506	165,403,646
4. TAX PAYABLE AT COMMON RATE (row 3x10%)	4	**64,820,151**	**16,540,365**

Source: Researcher's review based on separate EEITreturns of the parent and subsidiary companies

B. Calculation of tax to be imposed at special rate:

Indicators		Row	Parent	Subsidiary
5. Interest income		5	25,557,500	1,829,755
	Tax inposed on interest (row 5 x 10%)	6	2,555,750	182,976
6. TAX PAYABLE AT A SPECIAL RATE		**7**	**2,555,750**	**182,976**

Calculation of taxes withheld by others in accordance with the law:

Indicators		Row	Parent	Subsidiary
7. Dividends income		8	67,500,000	-
	Taxes withheld (row 8 x 10 percent)	9	6,750,000	-
8. THE AMOUNT OF TAXES WITHHELD BY OTHERS IN ACCORDANCE WITH THE LAW		**10**	**6,750,000**	**-**
9. TOTAL TAXES PAYABLE (Table A, row 4 + Table B, row 7)		**11**	**67,375,901**	**16,723,340**

Intra-group transactions

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Table 2. Transactions between parent and subsidiaries

№	Indicators	Total /in tugrug/	Total /in tugrug/
Related party transactions:		Purchases, loan received and costs allocated 185,753,300	Sales, loan provided and benefits expected 4,552,678

Transactions with subsidiaries-related parties

№	Name and type of transaction	The amount of purchases /tugrug/	The sales amount /tugrug/	Profit percentage	Intra-group profit /tugrug/
Software, management consulting services and office rent		125,800,000	950,224,000	4%-25%	185,279,000

Related party loan transactions

№	Type of loan	The amount of loan provided	Interest rate	Loan repayment schedule	Period to accrue the the loan interest
Acquizition of fixed assets and main operations financing		896,000,000	22,057,500 Per annum 8.5%	At the end of the year over 10 years	1year

Source: Overview by the researcher based on details of related party transactions

3. Adjustment was made in the consolidated EEIT return to fully eliminate the effect of intra-group transactions.

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Table 3. Entry to eliminate the effect of inter-company transactions.

A. Calculation of tax to be imposed at a common rate:

Indicators	Row	Parent	Subsidiary	Elimination entry		Amount to be reported by the consolidated income tax return
				Parent	Subsidiary	
1. The total amount of income	1	2,597,625,844	930,948,778	*b(147,431,000)* *c (6,600,000)* *d (11,120,000)* *e (4,552,678)*	*a(20,128,000)*	**3,338,742,945**
2.Cost of goods sold	2	1,137,800,905	525,830,900			1,663,631,805
3. Management and sales operations expenses	3	829,788,469	246,106,878			1,075,895,347
4. Non-core operating expenses	4		125,000			125,000
5. Profit+, loss- before payment of taxes (rows 1-2-3-4)	**5**	**630,036,470**	**158,886,001**	**(169,703,678)**	**(20,128,000)**	**599,090,793**
6. "Statement on reconciliation of the financial and income tax statements" /the amount increasing the profit before payment of taxes/	6	71,590,800	15,308,165			86,898,965
7. "Statement on reconciliation of the financial and income tax statements" /the amount decreasing the profit before payment of taxes/	7	53,425,764	8,790,520			62,216,284

8. Taxable income (row 5+6-7)	8	**648,201,506**	**165,403,646**	**(169,703,678)**	**(20,128,000)**	**623,773,474**
9. TAX PAYABLE AT COMMON RATE (row8*0.1)	9	**64,820,151**	**16,540,365**			**62,377,347**

B. Calculation of tax to be imposed at a special rate:

Indicators	**Row**	**Parent**	**Subsidiary**	**Elimination entry**		**Consolidated income tax return**
				Parent	**Subsidiary**	
10. Interest income	10	25,557,500	1,829,755	*f (0)*		27,387,255
Tax imposed at interest (row39 x10%)	11	2,555,750	182,976			2,738,726
11. TAXES PAYABLE AS SPECIAL RATE	12	**2,555,750**	**182,976**			**2,738,726**

C. Calculation of taxes withheld by others in accordance with the law:

Indicators	Row	Parent company	Subsidiary company	Elimination entry		Consolidated income tax return
				Parent company	**Sub/ company**	
12.Dividend income	13	67,500,000	-	*g(0)*		67,500,000
Taxes withheld from dividends	14	6,750,000	-			6,750,000
13. TAXES WITHHELD BY OTHERS IN ACCORDANCE WITH THE LAW	15	**6,750,000**	**-**			**6,750,000**
14. TOTAL TAXES PAYABLE (Table A, row 9 + Table B, row 12)	16	**67,375,901**	**16,723,340**			**65,116,073**

Source: Researchers' estimates based on separate EEIT returns and details of transactions between the related parties

Explanation of the elimination entries:

A. Inter-company gains on upstream software sales by the subsidiary to its parent are eliminated: Intra-group Upstream Sales Gain= Sales Income x Profit Margin 20,128,000 = 125,800,000 x 16%

B. Intra-group gains on downstream sales by the parent to its subsidiary are eliminated: Intra-group Downstream Sales Gain = Sales Income x Profit Margin 147,431,000 = 589,724,000 x 25%

C. Gains attributable to management consulting services rendered by the parent to its subsidiaries are eliminated:

Management Consulting Services Gain= Service Income x Profit Margin 6,600,000 = 82,500,000 x 8%

D. Gain relating to the lease of office space by the parent to its subsidiary is eliminated: Rental Service Gain = Rental Income x Profit Margin 11,120,000 = 278,000,000 x 4%
E. Gains related to costs allocated by the parent to the subsidiaries are eliminated: Gain attributable to cost allocation = 4,552,678
F. Interest income is taxed at a special rate according to the provisions of the EEIT Law, therefore it was not eliminated.
G. Dividends income is taxed at a special rate in accordance with the provisions of the EEIT Law, and there is no specific credit for groups, therefore, it was not written off.

4. Consolidated EEIT cost estimates and allocations.
Total tax expenses = MNT 62,377,344 (Calculation of taxes payable at a common tax rate)

Under the contribution method, the total tax expenses would be allocated as below (allocated based on the income tax expense that would have been incurred if the group member was a separate taxpayer):

Parent = 64,820,151 / (64,820,151 + 16,540,365) x 62,377,344 = 49,696,205
Subsidiary = 16,540,365 / (64,820,151 + 16,540,365) x 62,377,344 =12,681,139

5. Transfer pricing adjustment.
As discussed in this study, after preparing a consolidated EEIT statement, a group may adjust for the tax effects of intra-group transactions, or transfer pricing adjustments. This would allow for avoiding potential transfer pricing risks, tax reassessment, fines, and penalties.

Transfer pricing adjustments related to intra-group transactions:

Intra-group interest-free financing: The parent company provided MNT 636,500,000 interest-free loan to its subsidiary to finance its main operations. The following transfer pricing adjustment is made to calculate the arms-length interest income and relevant taxes based on the interest rate for a comparable loan of 8.5% per annum:

Interest income = Loan Amount x Arms-length Interest rate = 636,500,000 x 8.5% = 54,102,500
EEIT= Interest income x 10% = 54,102,000 x 10% = 5,410,250

Cost allocation profit level: The parent company did not calculate the return expected for expenses other than salaries and wages, per-diem expenses, as well as accounting and financial expenses. Therefore, the 2.5% rate of return used for similar cost allocation can be used for all types of cost allocation. Accordingly, the estimated additional return and relevant EEIT as per the transfer pricing adjustment shall be as follows.

Expected Return = Other Expenses x Benchmark Rate of Return = 7,146,200 x 2.5% = 91,155

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EEIT= Expected Return x 10% / 25% = 91,155 x 10% = 9,155.

6. Preparation of Work Sheet for Consolidated Statement of Financial Position and Income statement.

Table 4. Consolidation of financial statements of a group company

Indicators	Parent	Subsidiary	Elimination entries		Amount to be reported in the consolidated income tax return
			Debit	Credit	
Income Statement					
Sales income	1,620,791,667	805,148,778			2,279,918,560
Income earned from the parent company	-	125,800,000	(a)125,800,000		-
Income earned from the subsidiaries	1,162,587,478		(b)589,724,000		-
			(c) 82,500,000		
			(d) 278,000,000		
			(e) 190,305,978		
			(f) 22,057,500		
			(g) 146,021,885		
Cost of goods sold	1,137,800,905	525,830,900	(a) 20,128,000	(a)125,800,000	1,115,666,805
			(b) 147,431,000	(b)589,724,000	
Operating expenses (Excluding income taxes)	829,788,469	246,231,878	(c) 6,600,000	(c) 82,500,000	525,429,547
			(d) 11,120,000	(d)278,000,000	
			(e) 4,552,678	(e)190,305,978	
				(f) 22,057,500	
Income tax expense	59,001,955	12,864,115	(h) 7,852,189	(j) 16,755,900 (k) 7,120,770	78,016,894
			(i) 5,419,405		
Control share in net profit	756,787,816	146,021,885			560,805,314
Retained earnings /Parent company/	120,896,790	-			120,896,790

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Retained earnings /Subsidiary company/	-	59,765,380			59,765,380
Dividends		67,500,000		(g) 67,500,000	-
Retained Earnings as of12/31	**877,684,606**	**138,287,265**			**741,467,484**
Indicators	**Parent**	**Subsidiary**	**Elimination entries**		**Amount to be reported in the consolidated income tax return**
			Debit	**Credit**	
Inventory	923,670,264	283,670,264		(a) 20,128,000 (b)147,431,000	1,039,781,528
Other assets	2,356,745,839	594,796,494	(j)16,755,900 (k)7,120,770	(c) 6,600,000 (d) 11,120,000 (e) 4,552,678	2,936,390,425
Investment in the subsidiaries	276,521,885	-		(g)276,521,885	-
Total assets	**3,556,937,988**	**878,466,758**			**3,976,171,953**
Income tax liability	137,502,846	13,221,813		(i) 5,419,405	156,144,064
Other liabilities	1,120,874,536	528,957,680		(h) 7,852,189	1,657,684,405
Equity capital	1,420,876,000	198,000,000	(g) 198,000,000		1,420,876,000
Accumulated profit	**877,684,606**	**138,287,265**			**741,467,484**
Total liabilities and equity	**3,556,937,988**	**878,466,758**	**1,835,512,635**	**1,835,512,635**	**3,976,171,953**

Source: Estimates of researchers based on the separate financial statements of related parties and details of transactions between them

Explanation of the elimination entries:

A. The subsidiary wrote off upstream software sales to its parent, cost of sales sold, and intra-group gains:

Dr. Sales income	125,800,000	
Cr. Cost of goods sold		125,800,000

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Dr. Costs of goods sold	20,128,000	
Cr. Inventory		20,128,000

B. Downstream sales made by the parent to its subsidiaries, cost of goods sold, and intercompany gains were written off:

Dr. Sales income	589,724,000	
Cr. Cost of goods sold		589,724,000
Dr. Cost of goods sold	147,431, 000	
Cr. Inventory		147,341,000

C. Sales income, operating expenses of the subsidiary, and the gains of the parent related to management consulting services provided by the parent company to its subsidiary were written off:

Dr. Sales income	82,500,000	
Cr. Operating expenses		82,500,000
Dr. Operating expenses	6,600,000	
Cr. Accounts receivable		6,600,000

D. Income and rental expenses related to office leased by the parent to its subsidiaries were eliminated:

Dr. Sales income	278,000,000	
Cr. Operating expenses		278,000,000
Dr. Operating expenses	11,120,000	
Cr. Accounts receivable		11,120,000

E. Gains related to expenses allocated by the parent company to its subsidiaries were eliminated:

Dr. Sales income	190,305,978	
Cr. Operating expenses		190,305,978
Dr. Operating expenses	4,552,678	
Cr. Accounts receivable		4,552,678

F. Interest income and expenses related to loans provided by the parent to its subsidiaries are eliminated:

Dr. Interest income	22,057,500	
Cr. Interest expense		22,057,500

G. Accounts for investment income, dividends, and investments in subsidiaries were adjusted to the opening balances of the reporting period.

Dr. Equity capital	198,000,000	
Dr. Income earned from the subsidiaries	146,021,885	
Cr. Investment in the subsidiary		276,521,885
Cr. Dividends		67,500,000

H. Tax on the portion of the subsidiary's net profit attributable to the parent company through intra-group investment

The income tax expense related to the dividends declared and received are reflected as

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expenses incurred during the reporting period, and the taxes attributed to the undistributed net profit of the subsidiary is reported as deferred tax liability.

Dr. Income tax expense	14,602,189	
Cr. Deferred tax payable		7,852,189
Cr. Income tax payable		6,750,000

/Since the income tax liability related to the dividends distributed had been previously reported, the income tax related to the remaining undistributed dividends was entered in the account/.

I. Records of tax expenses related to transfer pricing adjustment.

Dr Income tax expense	5,419,405	
Cr. Income tax payable		5,419,405

Additional comments: The consolidated income tax statements were prepared with the condition to exclude the gains related to the upstream and downstream sales of goods, works and services between the companies from the taxable income. Therefore, there will be no mismatch between the consolidated financial and tax statements. Thus, no deferred tax adjustment entries have been made for gains attributable to intra-group transactions. In the opposite case, can be recorded as follows:

J. Intra-group sales transaction gains:

Dr. Deferred tax assets	16,755,900	
Cr. Income tax expense		16,755,900

K. Deferred tax assets of each company are consolidated as below:

Dr. Deferred tax assets	7,120,770	
Cr. Income tax expense		7,120,770

5. Conclusions

Although each economic entity is filing a separate EEIT return under the currently acting EEITlaw of Mongolia, the recent amendments to the tax legislation and ongoing tax reforms have been highlighting the importance of administering the income taxation of business combinations, particularly, the transfer pricing related to intra-group transactions. As of the end of 2021, although the filing rate for the Transfer Pricing Transactional Report to declare related parties and transactions with them was over 90%, the filing rate for Local File and Master File was about 60%. Approximately 50% of the taxpayers who file the Local File submitted inactive reports, failed to declare their related-party transactions, and had not done any functional or comparability analysis of the controlled transactions. This indicates that the legal framework and other regulations to ensure compliance with transfer pricing documentation requirements are not complete.

Through this study, we have concluded that for business combinations, the preparation and filing of consolidated income tax statements would serve as the basis to optimize management decisions and tax planning for these business combinations. This would be in line with the new global trend for business combinations' tax planning tools such as BEPS (Base Erosion and Profit Shifting) and GAAR (General Anti-Tax Avoidance Rules).

It is a global good practice to provide proper tax credits and exemptions to business combinations on the intra-group transactions; and allow filing a consolidated income tax statement. It is highly important to allow business combinations that play the leading role in generating the fiscal revenue of Mongolian, particularly, the EEIT income to objectively assess tax risks and implications arising from intra-group transactions and make necessary reconciliations through a consolidated financial statement.

The following proposals are put forward in the framework of improving the income tax statement and accounting practice of business combinations:

1. It is necessary to establish a legal framework to allow business combinations to file a consolidated income tax statement. Business combinations should be permitted to prepare a consolidated income tax statement in order to optimize tax planning according to the basic principles of fair and effective tax assessment. The benefits of filing a consolidated income tax statement would be as follows:

- Meeting the key principle of ensuring fair and efficient tax imposition at the macro level, and minimizing the income tax administration and tax audit costs of tax authorities;
- At the micro level, business combinations would be able to deduct losses assessed by a related party from the taxable income of other members of the group, exclude intra-group dividends from the taxable income in assessing their EEIT; to exclude the unrealized gains from intra-group transactions from the taxable income until the gain is realized, reduce costs and complexities associated with preparing and filing income tax returns, and it would make tax planning more efficient and comprehensive.

2. Use the transfer pricing adjustment method proposed in the study on related party transactions. This would allow business entities to avoid potential transfer pricing risks that may be identified by future tax audits and prevent respective tax reassessment and penalties.

3. Reflect the implication of the consolidated financial statement and income statement, respective records in the accounting records. This would summarize the implication of income tax assessment in the consolidated financial statements and provide the users with information.

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