



PKF Hong Kong Tax Newsletter (September 2020)

Hong Kong Transfer Pricing 2020 — Master File and Local File Deadlines

If your Hong Kong entity is part of a multinational enterprise (“MNE”) group and carries out related party transactions, it could be subject to mandatory Master File and Local File documentation requirements if it does not satisfy the exemption criteria (please refer to Appendix for details on the exemption criteria). If this is the case, your Hong Kong entity would need to meet one of the following approaching deadlines:-

Deadlines for Master File and Local File

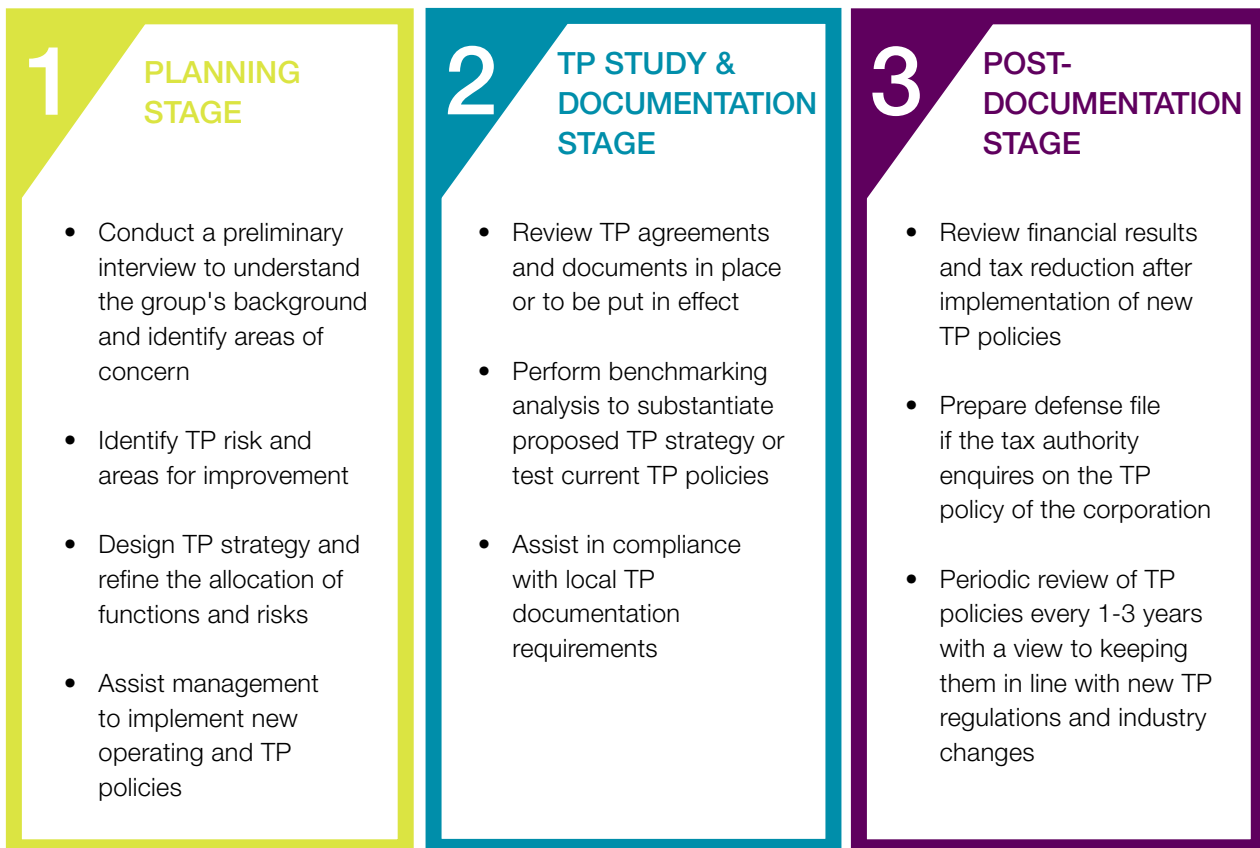
<u>Financial year-end date</u>	<u>Deadlines</u>
Year ended 31 December 2019	30 September 2020
Year ended 31 March 2020	31 December 2020
Year ended 30 June 2020	31 March 2021

How We Can Help

It is imperative for your Hong Kong entity to work towards the above deadlines if it does not satisfy the exemption criteria. Please note that failure to prepare the Master File and Local File documentation without a reasonable excuse would trigger the Hong Kong Inland Revenue Department to impose penalties on your Hong Kong entity.

In addition, even if your Hong Kong entity is exempt from the above Master File and Local File documentation requirements, it should still be able to justify that its transfer pricing ("TP") policies and related party transactions are in line with the arm's length principle. **If a corporation's related party transactions do not meet the arm's length standard and result in a tax advantage**, adjustments to the related party transactions would be required, causing significant time and costs to be incurred, and giving rise to **additional tax liability plus potential penalties of up to 100% of the tax undercharged.**

In this regard, we highly recommend that you should seek professional advice on your corporation's related party transactions sooner rather than later. For your information, the range of TP services we offer and our usual work approach are summarized as follows:-



For more information, please refer to our previous TP newsletters:

- [Hong Kong Transfer Pricing 2020: Approaching Deadlines And Tax Efficient Planning 2019](#)
- [Transfer Pricing Documentation Standards 2019](#)

Appendix

Master File and Local File — Exemption criteria

An MNE group entity which is carrying on a trade or business in Hong Kong and has engaged in related party transactions will be required to prepare the Master File and Local File, unless it is eligible for any one of the two exemptions as follows:-

Business size test	
Total revenue	Not exceeding HK\$ 400 million
Total assets	Not exceeding HK\$ 300 million
Number of employees (average)	Not exceeding 100
<i>If an enterprise meets any <u>two</u> of the above conditions (i.e. any two of the “total revenue”, “total assets” and “number of employees” are below relevant thresholds) for an accounting period, the enterprise will be wholly exempt from preparing the Master File and Local File.</i>	

Related party transaction size test (four categories of transactions ¹)	
Transfer of tangible assets (including trading of goods and properties, etc.)	Not exceeding HK\$ 220 million
Transactions of financial assets (including granting and repayment of loan, interest, etc.)	Not exceeding HK\$ 110 million
Transfer of intangible assets (including sale or acquisition of patents, trademarks, etc.)	Not exceeding HK\$ 110 million
Any other transactions (including provision service, royalty, rent, etc.)	Not exceeding HK\$ 44 million
<i>If the total transaction amount under a category does not exceed the relevant threshold for the accounting period, the enterprise shall not be required to cover that category of transactions in the Local File. If the total transaction amount under each of the categories do not exceed their respective thresholds, the enterprise will be wholly exempt from preparing the Master File and Local File.</i>	

Please note that the threshold for each type of related party transactions applies to the aggregate amount of the same type of transactions. A related party transaction can be a revenue item or an expense item. **Each transaction should be considered separately without setting off each other** (e.g. paying \$100 interest expense and receiving \$150 interest income will be counted as \$250). Furthermore, it is the arm’s length amount of the transaction which should be aggregated for determining whether the threshold is exceeded.

¹ The local file of an enterprise need not cover specified domestic transactions (i.e. where no overall tax advantage was derived), which are to be disregarded when determining whether the thresholds of the four categories of transactions above are exceeded.

Contact Us

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Who We Are

As a member firm of PKF International, PKF Hong Kong provides business solutions to clients on a global basis through sharing resources of the PKF network with our offices located across 150 countries. We offer a comprehensive scope of tax advisory and compliance services in Hong Kong and the PRC. Our tax professionals have extensive experience and knowledge on Hong Kong, PRC, and cross border tax issues. In addition, our TP professionals in Hong Kong and PRC are experienced in providing advisory services on tax-efficient group restructuring and compliance services with TP regulatory requirements.

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