



HONG KONG TAX ALERT

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Hong Kong concluded first unilateral Advance Pricing Arrangement

Summary

While the IRD concluded bilateral APAs in the past, there was no precedent for unilateral APAs, thus making this a landmark case.

This is certainly a positive step as it gives the much needed assurance to Hong Kong taxpayers that the IRD is open to concluding unilateral APAs in addition to bilateral and multilateral APAs.

The Inland Revenue Department (IRD) has recently signed its first unilateral Advance Pricing Arrangement (APA) with one of KPMG's key clients. While the IRD concluded bilateral APAs with Hong Kong's treaty partners in the past, there was no precedent for unilateral APAs, thus making this a landmark case.

Our client is a Hong Kong taxpayer who engaged KPMG to review its transfer pricing (TP) policy which has been adopted by the group for many years. In anticipation of the new TP law not yet enacted at that time, the group has proactively reviewed its related party transactions in order to develop a more robust policy which can better reflect the value contributed by a major group company. The taxpayer then applied for an APA from the IRD with regards to its royalty and service fee arrangements. We provided detailed technical support and analysis to substantiate to the IRD that the new TP policy is more robust and appropriately reflects the contribution made by the respective group companies in the value chain. Armed with its past APA experience and increasing technical capabilities, the IRD has critically reviewed the application and was fully supportive during its review. After various discussions between the IRD and KPMG, the IRD accepted our client's APA application making this the first-ever unilateral APA concluded in Hong Kong.

This is certainly a positive step as it gives the much needed certainty to our client on its new TP policy and, at the same time, demonstrated the IRD's commitment to adopt a TP regime in Hong Kong which complies with the global international taxation development. It also provides taxpayers the assurance that the IRD is open to concluding unilateral APAs. Taxpayers may consider concluding unilateral APAs with the IRD in cases where no double tax agreement is applicable or as an alternative to multilateral APAs where the related party transactions involve many jurisdictions. Seeking an APA remains as one of the best options to avoid disputes in the future and allow taxpayers to focus on its business development in the current highly competitive business environment. We look forward to seeing more APAs being concluded by the IRD in the near future.

With the new TP regulation enacted in July 2018, taxpayers should take a proactive approach to address the following issues:

- Is the group's TP policy robust to withstand challenges from tax authorities?

- When was the last time the group performed a detailed review of its TP policy and assessed whether it is defensible under the current regulatory environment?
- Does the group develop or possess any intellectual property where the owner has not been properly remunerated?
- Does the group's TP policy properly reflect the value contributions of the relevant group entities?
- Is APA an appropriate means for the group to manage its TP issues and obtain certainty from tax authorities?

KPMG can help you to review your group's TP policy to assess whether it is BEPS compliant and robust. We have both the technical expertise and experience in addressing tax authorities' issues and concerns including those relating to APAs if you wish to pursue this means to avoid disputes with tax authorities.

For more information and assistance, please contact any of our KPMG tax professionals.

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