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Synopsis on Transfer Pricing in Hong Kong, Thailand, and Vietnam

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I. Introduction

Transfer Pricing becomes highly important as soon as a business entity decides to expand its operations across international borders. *Transfer Pricing* is the financial term for the price calculation for transactions between related parties, e.g., within a group of companies. Transfer prices play an important role in accounting and tax compliance in cross-border business matters.

Every Multinational Enterprise (**"MNE"**) wishes to minimise its tax obligations to maximise its overall profits. In principle, multi-corporate businesses must pay tax in their host countries based on the profit share which arises in (or is allotted to) the respective business in such host country (e.g., for the purpose of this synopsis, Thailand, Hong Kong or Vietnam). Host countries can differ in various respects, e.g., tax systems, customs duties, currency exchange rates, legislation etc. As a result, *Transfer Pricing* also affects revenue and customs authorities, investors, creditors etc.

The obligation to comply with national and international tax regulations regularly conflicts with the goal of a tax-efficient allocation of profits within MNEs. In the recent decades, most national legislations in accordance with international tax regimes have significantly increased compliance requirements and restrictions on inter-company transaction of assets and profits, particularly through multilateral projects such as the OECD's Base Erosion and Profit Shifting ("BEPS") framework.

Thus, anticipatory business and corporate tax planning which ensures both efficiency and compliance with national law is vital.

II. Different Methods of Price Calculation

In most countries, *Transfer Pricing* regulations are built around the core concept of the *Arm's Length Principle*. According to this principle, the transaction (or transfer) price charged between affiliated companies must be the same as the price which would have been charged to an independent company.

There are six generally accepted methods by which to compute the transfer price in accordance with the Arm's Length Principle. These six methods can be separated into two categories:

- Traditional methods (Transaction Methods) focus on the facts of the actual transaction in question to compute an appropriate transfer price (*bottom-up method*).
- Other methods (Profit-based Methods) utilise the profit generated by comparable companies when undertaking similar transactions to determine the price of the intercompany transaction in question (*top-down method*).

Transaction Methods are generally considered to be more accurate and appropriate.

1. Transaction Methods (TM)

a) Comparable Uncontrolled Price Method (CUP) and Comparable Uncontrolled Transaction Method (CUT)

Both CUP and CUT compare the price of the intercompany transaction with the price of an identical or sufficiently similar independent transaction (i.e., the price charged in transactions between independent parties).

b) Cost Plus Method

This method summarises all the original costs of the unfinished product and then adds the customary net profit for such transactions to calculate the applicable transfer price.

c) Resale Price (Resale Minus) Method

Under this method, the transfer price is computed by deducting the customary profit margin from the respective resale price. The customary profit margin is calculated on a partial cost basis.

2. Profit-based Methods (PBM)

a) Comparable Profit Method (CPM)

This method is based on the operating profit gained from the intercompany transaction and the allocation of this profit to the respective business segment, which is then defined and subdivided as precisely as possible. In order to compare these profits, the profit margins of comparable independent businesses are used for each business segment. A target operating result can be computed by applying this method to the total profit of the multinational organisation. By comparing this result with the individual entities' actual financial statements, it can be assessed whether the correct transfer price was used.

b) Profit Split Method (PSM)

PSM is based on the total profit an MNE gains from an intercompany transaction. This profit is divided according to the functions and risks which each related party adopted, just as it would be in the case of a transaction between non-related parties.

c) Transactional Net Margin Method (TNMM)

The net profit gained from the intercompany transaction is analysed in relation to an appropriate basis (cost, turnover, assets etc.) and the resulting profit margin is checked against comparable independent transactions (this method is similar to Resale Minus or Cost Plus, thus strictly speaking it is a bottom-up method as well).

Synopsis:

Jurisdiction	Hong Kong	Thailand	Vietnam
Competent Authority	Inland Revenue Department	Revenue Department	Ministry of Finance, General Department of Taxation, Department of Taxation and Sub-department of Taxation
Affected Entities	1) **Associated Persons:** a) One party participates directly or indirectly in the management, control, or capital of the other party, or b) the same person participates in the management, control, or capital in both parties, or c) the parties are controlled by the same third party. 2) **Multinational Enterprise Groups** ("MNE Group") means a group in the usual sense that includes 2 or more enterprises the tax residence of which is in different jurisdictions; or an enterprise that is resident for tax purposes in one jurisdiction and is subject to tax in another jurisdiction with respect to the business carried out through a permanent establishment in that other jurisdiction (Section 58B IRO); 3) **Ultimate Parent Entities** ("UPE") of MNE groups: an entity that owns directly or indirectly a controlling interest in any other entity; and is not owned, with a	1) **Associated Company or Juristic Partnership:** a) Juristic person directly or indirectly holding not less than 50% of shares in the other juristic person, or b) Shareholders of one party who directly or indirectly hold 50% of the other's equity, or c) Parties sharing the same management, capital or control to an extent that makes it impossible to run both parties independently. 2) **Group of International Companies** having a consolidated group revenue of THB 28 billion (approx. USD 810 million) or more. 3) **Ultimate Parent Entities** ("**UPE**") of a Group of International Companies.	**Related parties:** a) One party controls at least 25% of the other's equity. b) Both parties are indirectly or directly controlled by the same third party with at least 25% of each party's equity. c) One party is the largest shareholder and controlling at least 10% of the other's equity. d) One party provides a guarantee or loan to the other that constitutes (i) 25% or more of the contributed capital, and (ii) more than 50% of the total value of the long- and medium-term loans of the said other enterprise. e) One party appoints more than 50% members of the total members of the board of executive directors or the control board of the other enterprise, or one member appointed by one party has power to decide on financial policies or business activities of the other enterprise. f) Both parties have more than 50% of members of the board of directors or a member of the executive board who has power to decide on financial policies or business activities of each of

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	controlling interest, directly or indirectly by another entity; or a stand-alone MNE entity (Section 15F IRO)		the two enterprises are appointed by the same third party. g) Both parties are managed or controlled in personnel, financial and business activities by individuals who are in family relationship. h) Both parties have transactions, either between their head offices and permanent establishments or between permanent establishments of overseas entities or individuals. i) One or more enterprises being controlled by the same individual through either his capital participation into that enterprise or his direct involvement in administration of that enterprise. j) An enterprise has transactions involving the transfer or receipt of at least 25% of the contributed capital of the enterprise's owner. k) An enterprise borrows or lends at least 10% of the owner's contributed capital at the time of arising transaction in the tax period from the enterprise's operator or controller or his/her family member. l) Any other cases in which one party is effectively controlled through business activities of the other.
Legal Sources	**Inland Revenue Ordinance (IRO Cap. 112)** a) Sec 50AAD: Application of TP Rules	**1) Revenue Code** a) Sec. 65 Bis (4), (7): Conditions in the Calculation of Net Profit and Loss	– Law on Corporate Income Tax 2008 – Law No. 32/2013/QH13 amending Law on Enterprise Income Tax

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	b) Sec 50AAE: Consistency with OECD rules c) Sec 50AAF: Rule 1: ALP provision between associated persons d) Sec 50AAG: participation condition e) Sec 58 C: Country by Country Report f) Sec 58 C: Master file and Local file	b) Sec 65 Ter (13), (14), (15): Non-deductible Expenses c) Sec. 71 Bis: Adjustment of income and expenses of related juristic persons. d) Sec. 71 Ter: Submission of documents/reports of related juristic person. **2) Notifications of the Director-General of Revenue** a) No. 400, B.E. 2564 re: Price Adjustment of Related Companies. b) No. 407, B.E. 2564 re: Required Documents or Evidence for a Price Assessment of transactions between Related Companies (“**TP Document**") c) No. 408, B.E. 2564 re: Country by Country Report. **3) BOI Announcement No. 1/2566 dated 16 May 2023** on Investment Promotion Measures to Alleviate Impacts from New Tax Collection Guidelines (OECD Pillar 2)	– Decree No. 132/2020/ND-CP on prescribing tax administration of enterprises having transactions with related parties – Circular 45/2021/TT-BTC: Advance Pricing Arrangement.
Methods	1) **Traditional Transaction Methods:** a) Comparable Uncontrolled Price, b) Resale Price, c) Cost Plus 2) **Transactional Profit Methods:** a) Transactional Net Margin b) Transactional Profit Split	1) **Traditional Transaction Methods:** a) Comparable Uncontrolled Price, b) Resale Price, c) Cost Plus 2) **Transactional Profit Methods:** a) Transactional Net Margin b) Transactional Profit Split	1) **Traditional Transaction Methods:** a) Comparable Uncontrolled Price, b) Resale Price, c) Cost Plus 2) **Transactional Profit Methods:** a) Transactional Net Margin b) Transactional Profit Split 3) **Total loan interest between related parties:**

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			Limited at 30% of Earning, Before Profit, Tax, Depreciation and Amortization. (“**EBITDA**”)
Documentation	1) A Hong Kong entity (any entity of a group of businesses that is a Hong Kong tax resident) must prepare a **Master File and Local File.** Exemptions can apply based on the size of the business, the value of controlled transactions, or the domestic nature of the transactions. 2) UPEs of MNE Groups must file a **Country-by-Country Report.**	1) Associated Companies and Juristic Partnerships with annual revenue exceeding THB 200 million must file a **Disclosure Form** and prepare **TP documents.** 2) UPEs of Groups of International Companies must file a **Country-by-Country Report.**	1) Taxpayers engaged in Related Party transactions under Decree 132 must report the transactions in **Appendix I** (disclosure form) and **Appendices II and III** disclosure of the checklist of information and documents required for Local file (**Disclosure Forms**) and Master File respectively **and** prepare **Master file and Local file**. 2) Ultimate Parent Companies must submit a **Country-by Country-Report.** 3) Preparation of Master file and Local file can be exempt under Safe Harbour Rules in Article 19 of Decree 132.
Reporting Obligation	1) **Master File and Local File:** Report upon request of the tax authority. 2) **Country-by-Country Report:** Filing with tax return.	1) **Disclosure Form and Country-by-Country Report:** Filing with tax return (P.N.D. 50) 2) **TP Documents:** Report upon request of the tax authority.	1) **Appendices I, II and III:** Filing with the annual Corporate Income Tax (**CIT**) return. 2) **Country by Country Report:** Within 12 months starting from the ending date of the fiscal year of Ultimate Parent Company, unless there is an international agreement on taxes with Vietnam, including the valid agreement on an automatic exchange of information (**AEOI**)

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			mechanism among the tax authorities.
Sanctions	Up to 100% of the underpaid tax plus interest (however, low tax audit activity).	1) Price adjustment by tax authority: Surcharge of 1.5% monthly up to 100% of the unpaid Corporate Income Tax. 2) Non-filing of Disclosure Form: Penalty up to THB 200,000 (USD 5,600)	1) Non-filing of Disclosure Forms: Penalty up to VND 15,000,000 (around USD 650). 2) Arrears the underpaid CIT tax plus interest of 0.03%/day. 3) Making false declarations leading to any deficiency or underpayment of taxes payable or any increase in amounts of tax exemption reduction or refund: 20% of the underpaid tax amount or the higher-than-prescribed amount of tax exemption, reduction or refund. 4) A fine of 1 to 3 times the evaded tax amount for tax evasion.
Advance ruling	**Departmental Interpretation and Practice Notes (DIPN)** 1) **DIPN 58:** Documentation and Country-By-Country Reports https://www.ird.gov.hk/eng/pdf/dipn58.pdf 2) **DIPN 59:** Transfer Pricing Between Associated Persons https://www.ird.gov.hk/eng/pdf/dipn59.pdf 3) **DIPN 60:** Attribution of Profits to Permanent Establishments in Hong Kong https://www.ird.gov.hk/eng/pdf/dipn60.pdf	**Sources from Revenue Department.** 1) Thailand's CbCR Local Guidance https://cbcr.rd.go.th/aeoi/assets/Doc/cbcr_local_guidance.pdf 2) Guideline on Advance Pricing Arrangement Process https://www.rd.go.th/fileadmin/download/Guideline_on_APA_process_en.pdf 3) Explanatory for filling out a disclosure form https://www.rd.go.th/fileadmin/tax_pdf/cit/2565/DCF_Explanatory_Note_FY2022_Update.pdf**DIPN**	De facto not possible

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	1) DIPN 46: Transfer Pricing Guidelines= Methodologies and Related Issues https://www.ird.gov.hk/eng/pdf/dipn46.pdf.		

We hope that the information provided in this brochure was helpful for you.
If you have any further questions please do not hesitate to contact us.

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