Singapore’s Updated Transfer Pricing Guidelines – Key Changes

Introduction


This update examines some of the key changes in the 2015 Guidelines that businesses should be aware of. The changes include clarifications on TP documentation, exclusions and materiality thresholds, the Transfer Pricing Consultation (“TPC”) process, the Mutual Agreement Procedure (“MAP”) and Advance Pricing Arrangement (“APA”). For a comprehensive overview of all the updates to the 2015 Guidelines from the previous guides, please see the comparison table attached in the appendix to this update.

Background

Transfer Pricing (“TP”) is the practice of setting prices in transactions between related parties operating across different countries. Related parties are parties that directly or indirectly control each other, or are under the direct or indirect control of a common person. Since prices are determined by related parties, tax authorities are concerned that such prices are set not to reflect true independent market prices but to reduce taxable profits in their jurisdiction. This has led to the rise of TP regulations and enforcement, making TP a major tax compliance issue.

In Singapore, IRAS applies the arm’s length principle to ensure that taxpayers transact with their related parties at pricing that reflects the true independent market price.

The renewed emphasis on transfer pricing in many countries, including Singapore, comes as the Organisation for Economic Co-operation and Development (“OECD”) starts to address the problem of aggressive tax avoidance by multinationals, through the OECD’s Base Erosion and Profit Shifting (“BEPS”) project. The project aims to help governments protect their tax bases and offer increased certainty and predictability to taxpayers, while guarding against new domestic rules that result in double taxation, unwarranted compliance burdens or restrictions to legitimate cross-border activity. The OECD has issued discussion drafts on revising the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations in 2015, under the Action Plan on BEPS published in July 2013.

Effective Date

IRAS has clarified that as the TP documentation guidelines do not vary significantly from the 2006 Guidelines, it is not necessary to provide an effective date for the guidelines, nor a transitional period for taxpayers to prepare TP documentation. Taxpayers are advised to continue their TP documentation efforts, or if they have not done so, to prepare TP documentation without delay.
Key Changes

Contemporaneous TP Documentation

The 2015 Guidelines make it clear that IRAS requires taxpayers to prepare TP documentation on a contemporaneous basis. The date of creation or update of each document should be stated in the document.

Contemporaneous TP documentation means the documentation of information that taxpayers relied on to determine the transfer price prior to or at the time of undertaking the transactions. The TP documentation should be organised at Group level and Entity (Singapore taxpayer) level.

For ease of compliance, the 2015 Guidelines clarify that IRAS will accept as contemporaneous any TP documentation prepared before the tax return for the financial year in which the transaction takes place is completed and filed.

Review of TP Documentation

As the 2015 Guidelines emphasise, IRAS now requires taxpayers to review their TP documentation periodically to ensure that the financial and economic analyses remain accurate, the applied transfer pricing method remains relevant, and the transfer pricing supported by the TP documentation is correctly adjusted to the arm’s length price.

Taxpayers should update their TP documentation when there are material changes to the operating conditions that impact their functional analysis or transfer pricing analysis.

As a best practice, IRAS encourages taxpayers to update their TP documentation at least once every three years.

Self-Initiated Retrospective Adjustments

IRAS now takes a firm view that it will not allow any retrospective downward adjustments of tax returns in the absence of contemporaneous TP documentation supporting the adjustments.

Further, IRAS can bring retrospective upward adjustments to tax, in accordance with arm’s length price.

Exclusions from the TP Documentation Requirement

Recognising that preparation of contemporaneous TP documentation could be onerous, the 2015 Guidelines introduced exclusions where IRAS does not expect taxpayers to prepare TP documentation. However, taxpayers should note that they are not exempted from compliance with the arm’s length principle, and that usual business records should still be kept.

Examples of such exclusions include the related party transactions (excluding related party loans) conducted in Singapore which are subject to the same Singapore tax rates, or related party transactions covered by an agreement under the Advance Pricing Arrangement.

TP documentation is also not required where the value of the related party transactions disclosed in the current year’s financial accounts does not exceed the thresholds (“materiality thresholds”) shown in the following table:
### Category of related party transactions

<table>
<thead>
<tr>
<th>transactions</th>
<th>Threshold (S$) per financial year</th>
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</thead>
<tbody>
<tr>
<td>Purchase of goods from all related parties</td>
<td>15 million</td>
</tr>
<tr>
<td>Sale of goods to all related parties</td>
<td>15 million</td>
</tr>
<tr>
<td>Loans owed to all related parties</td>
<td>15 million</td>
</tr>
<tr>
<td>Loans owed by all related parties</td>
<td>15 million</td>
</tr>
<tr>
<td>All other categories of related party transactions. Examples:</td>
<td>1 million per category of transactions</td>
</tr>
<tr>
<td>• service income,</td>
<td></td>
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<tr>
<td>• service payment,</td>
<td></td>
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<tr>
<td>• royalty income,</td>
<td></td>
</tr>
<tr>
<td>• royalty expense,</td>
<td></td>
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<tr>
<td>• rental income,</td>
<td></td>
</tr>
<tr>
<td>• rental expense.</td>
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</tbody>
</table>

For the purpose of determining if the threshold is met, aggregation should be done for each category of related party transactions. For example, all service income received from related parties is to be aggregated.

### Transfer Pricing Consultation (TPC)

In order to ensure compliance with the transfer pricing guidelines, IRAS audits selected taxpayers through the Transfer Pricing Consultation programme. In the 2015 Guidelines, IRAS lists several factors it considers when selecting taxpayers for TPC as these factors indicate higher risks for TP violation. These factors are:

(a) Transactions with cross-border related parties that are of large value relative to the other transactions of the taxpayer;
(b) Transactions with related parties subject to a more favourable tax treatment;
(c) Recurring losses or large swings in operating results which may be unusual given the functions and assets of the taxpayer and the risks it assumed;
(d) Operating results that are not in line with businesses in comparable circumstances;
(e) Use of intellectual property, proprietary knowledge or other intangibles in the business;
(f) Transactions involving R&D or marketing activities which could lead to development or enhancement of intangibles; and
(g) Indications (for example, through engagement with tax authorities, country’s audit focus, etc.) that the transactions are likely to be subject to transfer pricing audit by tax authorities.

### Mutual Agreement Procedure and Advance Pricing Arrangement

When a Singapore tax resident taxpayer suffers double taxation from adjustments made by IRAS or a foreign tax authority due to TP considerations, it can pursue the following actions:

(a) Take legal remedies in the jurisdiction in which the transfer pricing adjustments are made; and/or
(b) Request IRAS to resolve the double taxation through the MAP.
The taxpayer may avoid transfer pricing disputes by applying for an APA for related party transactions in future years, as well as prior years (not exceeding two financial years).

In the 2015 Guidelines, IRAS also specifies the criteria required before applying for the MAP or APA as follows:

- Taxpayers should only initiate MAP when double taxation has occurred or is almost certain.
- Taxpayers should only apply for APA when:
  - (a) There is a genuine motive to obtain certainty for the avoidance of double taxation;
  - (b) The request relates to specific current or future transactions that are not hypothetical; and
  - (c) They are certain that the cross-border related party transactions will commence or continue to take place throughout the APA covered period.

If an application for MAP or APA is rejected, the taxpayer may seek alternative remedies under the relevant domestic tax law, such as appealing to the Income Tax Board of Review. In addition, taxpayers can apply for MAP and APA while pursuing other remedies available under their respective domestic tax law, such as legal or judicial proceedings. If they do so, taxpayers should inform IRAS and the relevant foreign competent authorities, who will collectively decide if the MAP and APA process should cease or be suspended.

Taxpayers are not obliged to accept the outcome agreed between the competent authorities. They may withdraw the application, terminate the process (with valid reasons) or reject the agreed outcome.

**Adverse Consequences of Non-compliance**

If taxpayers are unable to substantiate with TP documentation that their transfer prices are at arm’s length, they may suffer adverse consequences. For example, IRAS can make an upward transfer pricing adjustment under Section 34D of the *Income Tax Act* (“ITA”), and may not support the taxpayer in MAP discussions or APA applications.

The specific anti-avoidance provision, Section 34D, was enacted in 2009 by the *Income Tax (Amendment) Act 2009*, and took effect on 29 December 2009.

Taxpayers should keep their TP documentation and submit it to IRAS within 30 days upon request. If they are unable to do so, taxpayers may be penalized under Section 94(2) of the ITA for not complying with the record keeping requirements.

**Conclusion**

To summarise, the 2015 Guidelines make clear that IRAS now requires contemporaneous transfer pricing documentation, along with periodic review of the documentation. It is also important for taxpayers to perform TP risk management and TP planning. Exclusions from the documentation requirements, such as materiality thresholds, have been introduced. IRAS has also provided details on the selection criteria for the TPC process. The 2015 Guidelines also give greater guidance on MAP and APA applications, such as criteria that taxpayers should satisfy before applying. IRAS now makes clear that it will not allow any retrospective downward adjustments in the absence of contemporaneous TP documentation supporting the adjustments.

The changes and developments reflect IRAS’s increased focus in this area. IRAS is likely to step up its monitoring and compliance efforts. Businesses, especially those that engage in large transactions with cross-border related parties, must therefore thoroughly understand the new TP requirements. To ensure compliance, businesses should apply the arm’s length principle when undertaking contemporaneous...
transfer pricing analysis, and review existing documentation (or at least once in three years). Taxpayers should also take note of the avenues to obtain double tax relief, through the MAP and APA process.

In its Summary of Responses to the Public Consultation, IRAS noted that it is monitoring developments on OECD’s proposed three-tier documentation approach (particularly with respect to the OECD’s country-by-country reporting template). Looking forward, the TP documentation portion of the Guidelines may be revised if the three-tier approach is eventually adopted. In the meantime, taxpayers would do well to observe the updated guidance on TP documentation, with immediate effect.

We will be happy to discuss the above issues further with you, including its implications to your business. Our team has the expertise and capability to help you in the full range of TP compliance matters mentioned above, such as TP documentation, TP review, TP planning, TP risk and functional analysis, TP benchmarking, as well as applications for double tax relief through the MAP and APA process.

Please email us at kala.anandarajah@rajahtann.com or hern.kuan.liu@rajahtann.com if you would like to discuss any of the points raised in this update further. Please feel free to also contact the Knowledge and Risk Management Group at eOASIS@rajahtann.com.

Seminar on 2015 Guidelines

Rajah & Tann Singapore’s Competition and Tax Practices will be hosting a lunchtime seminar on the updated Transfer Pricing Guidelines. The seminar will take place on 25 March 2015, and further details will be released soon. We look forward to seeing you at the event.
Overview of Key Changes

<table>
<thead>
<tr>
<th>Previous Guidelines</th>
<th>2015 Guidelines</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Transfer pricing guidelines 23 Feb 2006 (“2006 Guidelines”)</strong></td>
<td>Guidance on TP documentation is provided in paragraphs 6.9 to 6.15.</td>
</tr>
<tr>
<td>1. Guidance on TP documentation was provided in Annex G.</td>
<td>Where taxpayers are expected to prepare TP documentation, it should be prepared on a contemporaneous basis. The date of creation or update of each document should be stated in the document. Contemporaneous TP documentation is defined as documentation and information that taxpayers have relied upon to determine the transfer price prior to or at the time of undertaking the transactions. For ease of compliance, IRAS will also accept as contemporaneous TP documentation any documentation prepared at any time no later than the time of completing and filing the tax return for the financial year in which the transaction takes place. The definition of contemporaneous TP documentation was clarified using two examples, in paragraphs 6.7 and 6.8.</td>
</tr>
<tr>
<td>2. No guidance provided on contemporaneous TP documentation.</td>
<td></td>
</tr>
<tr>
<td>3. No guidance provided on review of TP documentation.</td>
<td>Taxpayers should review their TP documentation periodically to ensure that: • The financial analysis and economic analysis contained in the TP documentation are still accurate; • The applied transfer pricing method disclosed in the TP documentation is still relevant; and • The transfer pricing supported by the TP documentation is still at arm’s length. Taxpayers should update their TP documentation when there are material changes to the operating conditions that impact their functional analysis or transfer pricing analysis. In any case, IRAS encourages taxpayers to update their TP documentation at least once every three years.</td>
</tr>
<tr>
<td>4. No exclusions specified.</td>
<td>Taxpayers are not expected to prepare TP documentation in the situations specified in</td>
</tr>
</tbody>
</table>
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### 2015 MARCH

### COMPETITION AND TAX

<table>
<thead>
<tr>
<th>Previous Guidelines</th>
<th>2015 Guidelines</th>
</tr>
</thead>
<tbody>
<tr>
<td>paragraph 6.19.</td>
<td>Materiality thresholds are specified in paragraph 6.19(e), for related party transactions involving purchase of goods, sale of goods, loans, service income/payment, royalty income/expense, and rental income/expense.</td>
</tr>
<tr>
<td>5. No materiality thresholds specified.</td>
<td>IRAS will not allow any retrospective downward adjustments in the absence of contemporaneous TP documentation supporting the adjustments.</td>
</tr>
<tr>
<td>6. No guidance provided on taxpayer self-initiated retrospective adjustments</td>
<td>IRAS can bring retrospective upward adjustments to tax, in accordance with arm’s length price.</td>
</tr>
<tr>
<td>7. IRAS does not require documentation to be submitted when the tax returns are filed. The documentation should be kept by the taxpayers and submitted to IRAS only when requested to do so.</td>
<td>IRAS does not require taxpayers to submit the TP documentation when they file their tax returns. Taxpayers should keep their TP documentation and submit it to IRAS within 30 days upon request.</td>
</tr>
<tr>
<td>8. Taxpayers would not be penalised solely on the basis that the documentation is not sufficient or timely. But, IRAS could enforce the record keeping requirements under sections 65, 65A and 65B of the Income Tax Act if they were violated by the taxpayer.</td>
<td>In the event the taxpayers are unable to provide the TP documentation upon request by IRAS, they may be penalised under Section 94(2) of the ITA for not complying with the record keeping requirements under the ITA.</td>
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</table>

**Transfer Pricing Consultation 30 July 2008; Revised 6 August 2008**

| 9. IRAS to conduct TP Consultation with selected taxpayers to assess their compliance with the TP Guidelines. This Consultation would entail a field visit to the taxpayer. | A flowchart is provided to illustrate the Transfer Pricing Consultation (TPC) process. |
| 10. TP questionnaire: IRAS will send questionnaires to selected taxpayers who have or appear to have significant amount of related party transactions, especially with overseas parties, over a period of time. | IRAS provides risk indicators and examples of circumstances in which transfer pricing risks may be considered high, in selecting taxpayers for TPC. |
| 11. The questionnaire format was provided in Annex 1. | If necessary, IRAS may send questionnaires or information requests to obtain more data or information from taxpayers for risk assessment purposes. |

**Supplementary administrative guidance on advance pricing arrangements 20 Oct 2008**

| 12. Guidance provided for APA applications. | Guidance provided for both MAP and APA applications. |
## COMPETITION AND TAX

<table>
<thead>
<tr>
<th>Previous Guidelines</th>
<th>2015 Guidelines</th>
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<tbody>
<tr>
<td>13. No guidance provided on the criteria that taxpayers should satisfy before applying for the MAP or APA.</td>
<td>Guidance provided on the criteria that taxpayers should satisfy before applying for the MAP or APA.</td>
</tr>
<tr>
<td><strong>Transfer pricing guidelines for related party loans and related party services 23 February 2009</strong></td>
<td>Appropriate transfer pricing methods: CUP method, or Cost plus method, or Transactional Net Margin Method (“TNMM”)</td>
</tr>
</tbody>
</table>
| 15. Appropriate transfer pricing methods for related party services: Comparable Uncontrolled Price (“CUP”) method, or Cost plus method | }
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COMPETITION AND TAX

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