

Insurance Tax Highlights – Asia Pacific Malaysia

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Malaysian transfer pricing landscape – Spotlight on compliance

Transfer pricing landscape

In line with the increasing focus on transfer pricing in Malaysia, the Inland Revenue Board of Malaysia (IRB) introduced a new transfer pricing disclosure requirement in the corporate tax return for the financial year 2014, which now makes it mandatory for taxpayers to check the box as to whether transfer pricing documentation has been prepared for the particular year of assessment.

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As a precursor to the above change, over the past few years, the IRB has been making significant changes in the Malaysian transfer pricing regime by introducing Transfer Pricing Guidelines (“TP Guidelines”), Income Tax (Transfer Pricing) Rules (“TP Rules”), Income tax (Advance Pricing Arrangement) Rules and Advance Pricing Arrangement Guidelines. Coupled with the TP Guidelines and TP Rules, the IRB has also been actively carrying out specific transfer pricing field and desk audits. These audits are comprehensive, and generally cover both tangible goods transactions such as sales and purchases as well as other related party transactions including management service fee, technical fee and royalty.

The IRB has also been paying special attention to taxpayers that have recently carried out business restructuring focusing on change in functions, risks and assets, and how this has translated into the level of profitability.

Transfer pricing documentation is now crucial in justifying that related party transactions have been carried out at arm’s length. The TP Guidelines require transfer pricing documentation to be prepared on a contemporaneous basis i.e. at the point of developing or changing a related party arrangement and at the time of filing the tax return. Paragraph 25 of the TP Guidelines provide very detailed guidance of what is expected in a complete and comprehensive set of transfer pricing documentation. This includes organisational structure, group financial report, nature of the business / industry, details of controlled transaction, services rendered, benefits received, pricing policies, comparability, functional and risk analysis and selection, and application of transfer pricing method.



Related party transactions in the insurance industry

Insurance and reinsurance arrangements are some of the common related party transactions between group entities operating in the insurance industry. Further, many multinational insurers, centralise some of the functions at regional or global level to achieve greater consistency and efficiency within the group. As such, a head office charge / management fee is charged by the regional / global service provider to the operating entities. Most of them usually have in place global policies determining their pricing of support services provided by the head office or regional office.

In light of the new disclosure requirement, insurance companies having related party transactions would be required to review their current position with respect to related party transactions, and ensure that they have prepared local transfer pricing documentation which meets the requirements set out in Paragraph 25.4 of the TP Guidelines. This will help to mitigate any penalties in the event of any adjustment made during a transfer pricing audit. Some of the aspects generally scrutinised by the IRB during an audit with respect to intragroup services or head office services include the cost base considered for the service fee to verify whether non-chargeable cost such as shareholder service cost, etc. has been included, allocation methodology adopted to verify whether appropriate allocation key has been used which

is reflective of the services received and reasonableness of mark-up, if any, etc. It is equally important to demonstrate that the local operating entity requires such services and benefits from paying for these services. In many instances, this would include proper evidence (e.g. e-mails, notes of meetings, travel schedules, learning events) to be available to demonstrate the level of services received.

In documenting such services, Appendix A of the TP Guidelines sets out in detail, the list of specific information in relation to intragroup services to be included as part of the transfer pricing documentation. This includes a detailed description of the relevant service transactions, proof of provision of intragroup services, documentation of the relevant functions involved, documentation in support of services rendered as a justification to the fee, justification of the allocation keys in case of indirect charge method and details of the cost base considered.

The new requirement for transfer pricing documentation on a contemporaneous basis makes it important for companies to ensure that they not only have a robust transfer pricing policy in place but also are able to demonstrate that their related party transactions are of arm's length through complete documentation.

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