

# *Singapore tax authorities tighten APA process in latest Transfer Pricing Guidelines*

*Tax Insights from  
Transfer pricing*

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## ***In brief***

On 4 January 2016, the Inland Revenue Authority of Singapore (“IRAS”) published its latest third edition of **Transfer Pricing Guidelines** (“3Edn TPG”). This came barely a year following release of the second edition of Transfer Pricing Guidelines (“2Edn TPG”) on 6 January 2015, which introduced contemporaneous transfer pricing documentation requirements in Singapore for the first time.

Contrast the current pace of update with the almost 9-year time lag between the publication of the first edition of Transfer Pricing Guidelines on 23 February 2006 and that of the 2Edn TPG on 6 January 2015, it should be clear by now, if this was not already so before, that transfer pricing is one tax area which IRAS is increasingly focusing on. We should therefore expect that IRAS will continue with its stepped up efforts to enforce taxpayers’ compliance with the arm’s length requirement for related party dealings.

The 3Edn TPG is positioned to give enhanced guidance on the Mutual Agreement Procedure (“MAP”) and Advance Pricing Arrangement (“APA”) process as well as the application of the cost plus method, aside from certain other editorial updates. While it has been so described, it may also be said that the changes introduced to tighten the APA process go beyond mere enhancements.

The key updates contained in the 3Edn TPG and the related implications for taxpayers are elaborated below.

## ***In detail***

### ***Changes to APA process***

In the 3Edn TPG, the IRAS has maintained the stringent timeline that APA applicants should meet for pre-filing meeting and the submission of requisite pre-filing meeting materials i.e. at least 9 months and 10 months respectively, before the first day of the proposed APA covered period (hereinafter referred to as “first day of covered period”).

Previously, based on guidance provided in the 2Edn TPG, an APA applicant should be able to obtain a broad indication of the IRAS’ inclination to accept its APA request at the pre-filing meeting based on the IRAS’ review of requisite pre-filing meeting materials submitted, which typically involve fairly intensive efforts to prepare, and supplementary explanation and clarification provided during the pre-filing discussion. This relatively forthright and open process affords the APA applicant a greater degree of certainty and comfort earlier on in the APA process, and definitely benefits the applicant in this sense.

This will change under the 3Edn TPG. It is now stated therein that the IRAS will only indicate any inclination to accept an APA request no later than four months before the first day of covered period. In other words, unlike previously, the APA applicant will now have to wait patiently up to 5 months after the pre-filing meeting, and most likely only after a much more intense information gathering process before it may get some certainty of the IRAS’ inclination to accept its APA request.

While the IRAS’ desire for more time to review and accept an APA request is understandable and the new practice is also not unique compared to the increasingly stringent APA regimes adopted by some tax administrations, this change made by the IRAS seems incongruent with the desire expressed by taxpayers for the IRAS to expand and enhance its dispute resolution capacity to provide an even more efficient process of supporting them in addressing or mitigating cross-border tax risks. In addition, given that the IRAS is prepared to indicate acceptance of the APA request only some months after the pre-filing meeting, it now begs the question as to why the IRAS should still require APA applicants to provide requisite pre-filing meeting materials a month before the pre-filing meeting.

Under the new rules, IRAS will have to make greater efforts to ensure that taxpayers do not experience a higher level of uncertainty in that an APA request may not be successful despite months of intense efforts and costs expended.

Other tax administrations, particularly in the region, have a more intense information gathering process during the pre-filing phase (i.e. prior to the filing of the APA request). In the case of bilateral APAs, the new rules can be used by IRAS to coordinate a more streamlined process for the taxpayer concerned in that similar information requested by the two Competent Authorities can be prepared at the same time. It is hoped that, despite the potential higher uncertainty, the new rules will mean that in the case of successful applications, the post-filing process will be shorter and lead to a faster negotiation and outcome.

Perhaps to mitigate the potential negative impact on taxpayers, the IRAS has complemented the change with a relaxation of the requirement for the APA applicant to file the APA application 6 months before the first day of covered period. Going forward, the applicant is only required to file the APA application within 3 months of go-ahead indication given by the IRAS. Like before, the IRAS has also committed to issue its APA acceptance letter within 1 month from the receipt of the APA application.

It is unclear whether the adjusted timeline for submission of APA application will help relieve the greater sense of uncertainty felt by taxpayers with respect to the APA process. Given the critical importance of a robust APA regime, the IRAS should consider additional measures to address potential misperception issues. For example, the IRAS should consider providing examples of situations or circumstances where it will not be inclined to accept an APA application. With this, there will be greater clarity on the IRAS' position concerning acceptance of an APA application into its APA regime.

The 3Edn TPG has not included specific transitional provisions. It is therefore unclear whether the changes to the APA process are applicable to cases where a taxpayer has initiated the request but has not yet been notified to file under the previous process or are applicable only for new APA requests. Nonetheless, given that the changes have been positioned as IRAS providing enhanced guidance on the APA process, we expect that the IRAS will likely subject all pending APA requests to the new process.

### *Other changes or updates*

#### *a) Application of cost plus method*

IRAS has made fairly substantial updates to paragraph 5.58 in the 3Edn TPG concerning the application of the cost plus method. An example is now provided to emphasize and illustrate the need for taxpayers to ensure the correct cost base is determined for the purpose of applying the cost plus method (presumably, the same consideration should apply to cases where return on total costs is used as the Profit Level Indicator under the Transactional Net Margin Method). In particular, IRAS may now deem additional cost to be included in the cost base of the provider of services and/or goods even if such additional costs are not actually incurred and accounted for in the accounts.

The above change seeks to ensure the correct level of costs incurred by group service providers and consequently, the correct level of remuneration earned by them under the above transfer pricing methods, regardless of whether they are charged with full costs for providing the services. While it cannot be disputed that this is a theoretically sound approach to adopt, it appears to ignore the practical difficulties faced by taxpayers in complying with this approach. As a result, it exposes group service providers which may not have the wherewithal to dictate or ensure that other group entities charge them with appropriate costs, to potential non-compliance issues and associated penalties. Group service providers may also find it unfeasible to put in place an elaborate mechanism to track and/or compute the costs incurred by other group entities that may be attributable or allocable to them for the purpose of adjusting their cost base.

b) Clarification of understanding of expectations and obligations arising from MAP and APA process

The IRAS has included a clarification in paragraph 8.29 in the 3Edn TPG that the IRAS is not precluded from conducting a tax audit on a taxpayer if there is non-compliance with the Singapore tax laws in the event that the IRAS or the foreign competent authority rejects the taxpayer's MAP or APA application. It is unclear why and under what circumstances the IRAS will seek to do this i.e. rejects an APA or MAP application and yet mounts an audit on the taxpayer concerned. Doing so would put the taxpayer in the precarious position of being exposed to double or multiple taxation, for which it will be denied any avenue to mitigate the associated risks other than through domestic legal and judicial proceedings. Clarification on this aspect of the update should be provided.

*Takeaways*

The publication of the 3Edn TPG barely a year following release of the 2Edn TPG on 6 January 2015 indicates that the IRAS is closely monitoring the evolving international tax developments vis-à-vis transfer pricing compliance level and practices in Singapore, and that IRAS stands ready to make changes to further tighten the transfer pricing regime and related aspects in Singapore to address or respond to evolving needs. In the post-BEPS world, taxpayers in Singapore and elsewhere expect to face, and therefore to deal with, a rising number of cross-border tax disputes going forward. Taxpayers all over have expressed increasing desire to be able to receive greater support from the Competent Authorities of their home jurisdictions to help them brace the looming storms. From this perspective, changes introduced to tighten the APA process in Singapore may need to be closely monitored to ensure that they create the intended effect of better streamlining of information gathering process and the highlighting of key issues at an earlier stage rather than the opposite effect of greater uncertainties and compliance costs for Singapore taxpayers. Some updates such as the clarification on the application of the cost plus method are likely to pose practical challenges for Singapore taxpayers and therefore may expose them to potential non-compliance issues and related penalties on matters that they may not be in the position to fully address.

Faced with these challenging circumstances, what Singapore taxpayers can do, and must do, to effectively help mitigate transfer pricing risks is to ensure they have robust transfer pricing and related documentation in place to serve as a strong first level of defence against potential challenges by tax authorities, including the IRAS. The current tax environment makes it critically important that taxpayers pay adequate attention in ensuring implementation of sound transfer pricing policies and practices, which are supported by robust transfer pricing documentation. In addition, having robust transfer pricing policies, practices and related documentation should put them in a good position to access and support the APA process should they decide to pursue such cross-border tax dispute prevention strategies to mitigate their transfer pricing risks.

## Your PwC Contacts

If you have any questions or require further discussion of how this issue might affect your business, please do not hesitate to contact any of the following from our Transfer Pricing team:

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