

Singapore issues the 6th Edition Transfer Pricing Guidelines

August 2021

In brief

The Inland Revenue Authority of Singapore (IRAS) issued revised Transfer Pricing Guidelines (Sixth Edition) (6th Edn) on 10 August 2021. While there are no fundamental changes from the 5th Edn TPG, there is new guidance on cost contribution arrangements (CCAs) and enhanced guidance on financial transactions, intercompany services and TP audits and adjustments.

The 6th Edn reveals a marked change in tone, with more focus on the quality of TP documentation (TPD), audit and enforcement. Coming on the back of two IRAS e-Tax Guides on special topics dealing with the TP aspects of centralised activities in multinational enterprise groups and commodity marketing and trading activities, the release of the 6th Edn suggests taxpayers can expect to encounter a closer and more forensic examination of their TP arrangements going forward.

The 6th Edn is notably more closely aligned with the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration (July 2017) (OECD TPG) and the opportunity has been taken to reference the mandatory binding arbitration procedures that are available under many of Singapore's post BEPS double taxation treaties. One might speculate this to be in anticipation of increased bilateral tax disputes going forwards.

In detail

Quality of transfer pricing documentation

The 6th Edn includes a new section on Frequently Asked Questions in relation to TPD (Section 6 Appendix B). This deals with matters which are required to be covered in the TPD and additional matters which IRAS notes "will be useful" to cover. One might expect IRAS to routinely focus on things that "will be useful" in a TP audit, where not addressed in the TPD. Notable things that "will be useful" include an explanation of the contribution of related parties to the overall value chain, the reasons for entering into a particular transaction and an explanation of margin performance vis-à-vis competitors and selected comparables. Elsewhere, in the section on TP adjustments, IRAS specifically addresses the circumstances in which they would disregard a transaction, drawing on the language of the OECD TPG to highlight that in the exceptional circumstance that a transaction is commercially irrational and cannot, for that reason, be benchmarked, it may be disregarded or re-constructed.

Taking all of this together with the attention drawn to the importance of the risk control framework in the IRAS e-Tax Guide on Centralised Activities in Multinational Enterprise Groups (issued on 19 March 2021), taxpayers should expect, upon audit, a deeper and more forensic examination of their substance and of the overall commercial rationale for entering into the transactions which are presented. Taxpayers should not assume TP audits will be limited merely to an examination of the pricing of the transaction presented. Instead, taxpayers should be prepared to explain why entering into tested transactions was arm's length in the first place, having regard to the surrounding economic circumstances and the options realistically available to the parties.

Intercompany services

Section 14 has been re-drafted to align more closely with the OECD TPG. There is a fuller explanation of the benefits test and the treatment of stewardship costs, with specific reference to the OECD TPG. In addition, the list of activities qualifying for the 5% routine services safe harbour (Annex C) has been expanded, and in a further administrative concession, services which are not listed in Annex C but which do meet the OECD TPG definition for low value adding services may similarly be charged at 5%, provided the treatment is accepted on both sides of the transaction and subject to the satisfaction of other hygiene factors. Note, this does not remove the requirement to prepare contemporaneous TPD.

TP audit, TP adjustments and Bilateral Advance Pricing Agreements (BAPAs)

The guidelines on TP compliance in the 5th Edn have been amended in the 6th Edn to reflect the shift in focus; TP consultations are re-named TP audits.

New sections 8 and 9 have been introduced to the 6th Edn to provide more comprehensive guidance on TP adjustments (either taxpayer initiated or IRAS initiated) and on the application of the 5% surcharge which is applied to the gross value of upwards adjustments. IRAS reminds taxpayers that the 5% surcharge automatically applies to an upward TP adjustment (other than where agreed between competent authorities) unless remission is offered, at the sole discretion of the comptroller. Hygiene factors to be taken into account in the exercise of this discretion include the taxpayer's compliance history, the preparation of contemporaneous TPD, and cooperation through the audit process.

To encourage voluntary disclosure of unsupported TP positions, IRAS note that full remission of the 5% surcharge will be available to taxpayers making upwards self-initiated TP adjustments within two years of the tax return filing deadline provided this is prior to any queries being raised by IRAS or the receipt of a TP audit notification and provided further that the above mentioned hygiene factors are also satisfied.

It is noted that self-initiated retrospective downward adjustments will not be accepted by IRAS unless the adjustments are due to an error or mistake under Section 93(1A) of the Income Tax Act and are supported by contemporaneous TP documentation.

The guidance on the process for initiating BAPAs has been updated, most notably to draw taxpayers' attention to the fact that IRAS will not entertain BAPAs for transactions undertaken for mainly tax avoidance purposes. This does not represent a change in practice for IRAS, but does serve to underline the fact that BAPA applications are accepted at IRAS's discretion.

Cost contribution arrangements

The 6th Edn provides detailed guidance on CCAs through the introduction of Chapter 17, which is aligned with the OECD TPG.

A key observation is the emphasis IRAS places on the value of current contributions to a CCA, specifically noting that the cost of current contributions does not necessarily reflect the value of such contributions. Instead, each CCA participant's contribution should be valued at arm's length. This may mean that cost contributions should be rewarded with a mark-up, although in some circumstances, IRAS may be prepared to accept measuring contributions at cost. Taxpayers with

CCAs, in particular those with substantial contributions by the Singapore taxpayer, should revisit the methodology employed to ensure compliance.

It is also noteworthy that IRAS has provided guidance on the Singapore corporate income tax treatment for payments under CCAs. This provides a helpful reminder that taxpayers should consider the interaction between transfer pricing and the taxability/ deductibility aspects of CCA payments.

Related party financial transactions

IRAS has provided further guidance on the application of the arm's length principle to related party financial transactions other than related party loans, such as cash pooling arrangements, hedging transactions, financial guarantees, and captive insurance. When applying the arm's length principle, IRAS expects taxpayers to take guidance from the OECD Transfer Pricing Guidance on Financial Transactions issued on 11 February 2020 (OECD FT TP Guidance).

In relation to related party loans, IRAS has also provided the following key updates, which are mostly in line with the OECD FT TP Guidance:

- A summary of economically relevant characteristics that may be useful indicators in assessing whether a purported loan should be regarded as a loan.
- A reminder that the creditworthiness of the borrower is one of the main factors in determining an arm's length interest rate, together with guidance on the circumstances in which the implicit support that arises from group membership should be considered in establishing the borrower's creditworthiness.
- A confirmation that taxpayers can choose to determine the arm's length interest rate for comparable loans on an aggregate basis, using similar loan features as a way to aggregate the loans. This should help to reduce compliance costs.
- A confirmation that IRAS will not regard interest-free related party loans as arm's length transactions unless taxpayers have reliable evidence that independent parties under comparable circumstances would similarly provide such loans without charging any interest.

Note that the 6th Edn does not touch on the TP considerations relating to the cessation of (most) LIBOR rates after 31 December 2021. We expect that IRAS will provide an update on this in time to come.

Concluding remarks

The 6th Edn marks a clear change in the tone from IRAS with an increased focus on enforcement and the quality of TPD. Moreover, the closer alignment with the OECD TPD and the reference to the availability of mandatory binding arbitration suggest that IRAS expects cross border disputes to continue to grow post BEPS 2.0. Taxpayers should take the opportunity to review their TP arrangements and TPD, to ensure it is at required standard to avoid costly disputes and potential adjustments.



Contact us

If you would like to discuss any of the issues raised, please get in touch with your usual PwC contact or any of the individuals listed below.



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