

Singapore issues the 7th Edition Transfer Pricing Guidelines

July 2024

In brief

The Inland Revenue of Authority of Singapore (“IRAS”) issued revised Transfer Pricing (“TP”) Guidelines (Seventh Edition) (“7th Edition”) on 14 June 2024. Notable changes in the 7th Edition include a step up in TP audit, along with stricter conditions for surcharge remission. There is also added emphasis on commercial rationality and substance of related party (“RP”) transactions, as well as adequacy of TP documentation and contemporaneous supplementary analyses in a TP audit. The MAP process has been tightened to include a more detailed evaluation step before IRAS accepts a MAP application.

In addition, IRAS has incorporated various clarifications around treatment of government assistance, capital transactions, application of working capital adjustments, the use of base reference rates arising from the global interbank offered rate (“IBOR”) reform for related party (“RP”) loans and dating requirement for simplified TP documentation. New exemption rule for RP domestic loans entered into on or after 1 January 2025, and clarified expectation for annual review of long-term RP loans are also included. In this 7th Edition, IRAS has also increased TP documentation exemption threshold for certain transactions, and provides pragmatic guidance around strict pass-through cost, which help to reduce compliance burden for taxpayers for relevant RP transactions.

In detail

[Update to TP audit process, emphasis on adequacy of TP documentation and timely supplementary analyses](#)

Taxpayers should expect an even more stringent TP audit with the updates in this 7th Edition. This is evidenced from the change of TP audit process whereby after the fact finding and discussion with taxpayers and IRAS’ completion of review, IRAS will proceed to make TP adjustment, impose surcharge, and issue closing letter if IRAS considers that the taxpayer’s taxable profit is understated, or loss is overstated due to non-arm’s length RP transactions. Taxpayers must file an objection if they do not accept the adjustment. This is different from the previous “inform and discuss” approach where IRAS would have first discussed with the taxpayer before making any TP adjustment and issuing closing letter. There is also additional emphasis on quality and adequacy of TP documentation during TP audit, whereby the review will also “assess if taxpayer’s TP documentation is adequate” (in addition to “any transfer pricing issues” as per previous guidelines). Taxpayers should review the quality of TP documentation (in addition to the robustness of TP arrangements), to ensure it is at the required standard to avoid costly disputes and potential adjustments. In addition, while not a particular new definition in this 7th Edition, the guidelines have added emphasis in certain paragraphs that non-compliance with arm’s length principle (and hence the risk of IRAS making a TP adjustment) includes overstated loss as well, in addition to understated profit.

The 7th Edition clarifies that IRAS considers additional details or analysis submitted during TP audit to further explain the position covered in a TP documentation as contemporaneous, unless those details relate to subsequent developments analysed with hindsight. This is not particularly new from the current practice where taxpayers would have an opportunity to provide supplementary analyses to justify a position in a TP documentation. The important clarification here is that IRAS only considers supplementary analyses which are not relating to subsequent events or conducted with hindsight. Hence, it is imperative that taxpayers critically evaluate which supplementary analyses would be helpful to strengthen TP documentation's position in the event of a TP audit and put together such analyses as early as possible (ideally contemporaneously) to avoid unnecessary dispute on "subsequent event/hindsight" and enhance the effectiveness of such supplementary analyses.

Stricter conditions for remission of surcharge

Importantly, IRAS also introduces an additional condition for surcharge remission in the 7th Edition, in which only taxpayers with no history of surcharges or penalties for the current year of assessment (YA) and the immediate two preceding YAs are considered for partial or full remission. This update indicates IRAS' strong emphasis on good compliance records of taxpayers in determining the possibility of a surcharge remission. Together with the more stringent TP audit highlighted above, and a stricter condition to be eligible for surcharge remission, it is therefore imperative for taxpayers to place continuous focus on overall tax compliance and governance to avoid adverse outcome from non-compliance.

More stringent Mutual Agreement Procedure (MAP) process

IRAS has updated the MAP process in the 7th Edition to remove (i) notification of intent and (ii) pre-filing meeting as compulsory steps from the previous MAP process. Taxpayers still have the option to initiate a discussion with IRAS before submitting a MAP application if taxpayers prefer. With the new process, taxpayers would need to proactively manage timeline such that the complete MAP application (instead of just an initial notification of intent, per the previous rules) can be submitted within time limit specified in the MAP Article of Double Taxation Agreement ("DTA").

Whilst the update appears to provide a simplified process, the new MAP process is indeed more stringent with an added "evaluation" step by IRAS before accepting a MAP application. In particular, IRAS may require more information from taxpayers for evaluation before indicating if the application is accepted (compared to the previous process whereby the evaluation is based on the MAP application alone).

In addition, a change in the tone is observed when it comes to evaluating and accepting a MAP application. In the previous guidelines, it was indicated that *"unless IRAS or the other relevant foreign competent authority is of the view that the taxpayer's MAP request is not justifiable, the taxpayer should proceed to submit its application"*. The 7th Edition indicates that *"IRAS will review and evaluate the taxpayer's MAP application. ...If IRAS rejects the application, it will notify the taxpayer and the relevant foreign competent authority in writing together with the reasons."* While this does not represent a change in practice of IRAS, this does serve to emphasise the fact that MAP applications (as with APA applications) should be founded on well supported positions and are accepted at IRAS' discretion.

Given the increasing tax and transfer pricing audit globally which may result in audit adjustments for RP transactions (i.e., heightening risk of double taxation), and a more stringent MAP evaluation process by IRAS, taxpayers should critically assess if there are possible and appropriate dispute prevention strategy (e.g., APA) to achieve tax certainty upfront, and/or implementing a robust TP governance process.

Disregard of actual RP transactions by IRAS

In the previous TP guidelines, IRAS has specified circumstances in which IRAS would disregard an actual RP transaction. In this 7th Edition, IRAS clarifies through an enhanced illustration using the same commercially irrational transaction that, IRAS will not disregard the income of a taxpayer in Singapore in the absence of an APA or a MAP; however, if the paying company is a taxpayer in Singapore, IRAS will disregard the payment, making it non-deductible.

It is imperative for taxpayers to review their RP transactions to ensure they are founded on commercial basis, given the heightened risk of double tax arising from disregard of actual transactions (e.g., when

income is taxed in the other country, but deduction is not allowed in Singapore). As with any RP transactions, domestic RP transactions should also be revisited to justify their commercial rationale, else there may be a risk of double taxation where the income of a Singapore taxpayer is subject to tax, while the expense of the other Singapore taxpayer is not deductible.

New exemption threshold for RP transactions previously subject to S\$1 million threshold

IRAS has raised the threshold for which certain transactions are exempted from contemporaneous TP documentation from S\$ 1 million to S\$2 million. This is applicable to transactions previously subject to the S\$1 million threshold (e.g., service fee income/expenses, royalty income/expenses, guarantee income/expenses, etc.), and takes effect from YA 2026 onwards. IRAS also added illustrations in the 7 Edition to guide taxpayers on applying the exemption thresholds during transition period for YA 2025 and YA 2026. Taxpayers should note that while this increase in exemption threshold helps reduce compliance burden, the exemption for preparation of contemporaneous TP documentation does not exempt taxpayers from compliance with the arm's length principle. IRAS expects taxpayers to be able to substantiate the arm's length nature of pricing arrangements upon request with usual business records.

New exemption rule for RP domestic loans entered into on or after 1 January 2025

With respect to RP domestic loan, a loan of any amount entered into on or after 1 January 2025 are exempted from contemporaneous TP documentation preparation if the following conditions are met:

- i. neither the lender nor the borrower is in the business of borrowing and lending money (taxpayers should note that the previous condition only required that the lender is not in the business of borrowing and lending money); and
- ii. the indicative margin is applied in accordance with the administrative practice (taxpayers should note that for ease of compliance, the threshold of S\$15 million for purpose of the indicative margin does not apply to RP domestic loans where neither party is in the business of borrowing and lending money)

This new rule would mean that compared to RP domestic loans entered into before 1 Jan 2025, taxpayers now need to prepare contemporaneous TP documentation for RP domestic loans entered into on or after 1 Jan 2025 if indicative margin (published on IRAS' website) is not applied.

With the above, IRAS also recognises that the approach of interest restriction has become less relevant to achieve arm's length outcome for RP domestic loans where the lender is not in the business of borrowing and lending money. As such, it will discontinue this approach for any RP domestic loans entered into on or after 1 January 2025.

For RP domestic loans entered on or after 1 Jan 2025 where either party is in the business of lending and borrowing, the interest rate applied on such loans should be determined based on arm's length principle. Where the loan does not exceed S\$15 million, IRAS indicative margin may be applied to derive the interest rate.

Guidance on base reference rates arising from the global IBOR reform, and annual review/refresh for long-term RP loans

With the global IBOR reform, the previous base reference rates which were mainly IBORs have been replaced by alternative near risk-free rates ("RFRs"). As a result, existing products/contracts that make reference to IBORs have to be transitioned to reference their corresponding RFRs.

In this 7th Edition, IRAS clarifies that when taxpayers make changes to their existing RP IBORs based loans in response to the IBOR reform and in accordance with the relevant guidance, IRAS will consider such changes as arm's length. It should be noted, however, that where the changes are beyond those expected under the IBOR reform and the relevant guidance, IRAS may consider if any refinancing is involved such that a new loan has been issued. In addition, since RFRs are not economically the same as IBORs, taxpayers with RP loans using RFR as base rate may need to consider if a spread adjustment is necessary to factor in any economic difference between the RFRs and the corresponding IBORs.

Accordingly for TP documentation purposes, IRAS clarifies that (i) for transitioning of existing RP IBOR-based loans, taxpayers need to include the basis of the changes and explanation on how those changes are consistent with the IBOR reform, relevant guidance and arm's length principle; and (ii) for RP loans adopting RFRs as base reference rates, taxpayers to include explanation on whether spread adjustment is necessary and the basis of determining the spread adjustment.

With respect to long-term RP loans, IRAS clarifies that taxpayers would need to perform annual review on their long-term loans' facts and circumstances and refresh the arm's length analysis where necessary (otherwise, rely on simplified TP documentation if conditions are met). This does not represent a change in IRAS' practice whereby IRAS has always expected continuous monitoring and review for all RP transactions. However, it does serve as an important reminder to taxpayers that an arm's length analysis for a long-term loan can only be relied throughout the tenor of the loan if there are no changes to the terms and conditions of such loans.

Update on guidance on strict pass-through costs

IRAS has updated Section 14.22 of 7th Edition to accept email correspondence as a 'written agreement' between related parties. IRAS also added examples in Section 14.25 of 7th Edition to guide the determination of strict pass-through costs. This update demonstrates IRAS' recognition of operational challenges which taxpayers may face in complying with strict pass-through cost conditions, provides practical guidance, and helps reduce administrative burdens for taxpayers.

Guidance on treatment of government assistance

Government assistance has gained its prominence especially during the COVID-19 pandemic, where various government assistance such as jobs support scheme has been introduced to ease cash flow for taxpayers. Recognising that such benefits government assistance may have transfer pricing implications and certain government assistance is likely to continue, this guidance aims to assist taxpayers in determining how the benefits from government assistance should be treated for Singapore transfer pricing purposes.

In principle, a comparability analysis (such as how the receipt of government assistance would or would not affect the price of independent party transactions) would need to be undertaken. In practice, IRAS recognises practical challenges that taxpayers may face in performing such analysis and has indicated in the 7th Edition that *"unless otherwise demonstrated, it is generally expected that an independent party acting in a commercially rational manner would retain the benefits from government assistance."* Simply put, taxpayers are not expected to pass on the benefits from government assistance to related parties through transfer pricing (unless there is reliable evidence showing that third parties would have done so under comparable circumstances). In short, this approach is generally consistent with the transfer pricing guidance relating to COVID-19 issued by IRAS previously.

It is important to note that taxpayers receiving government assistance are now required to properly document relevant government assistance information in the TP documentation, including (i) details relating to the government assistance received, (ii) accounting treatment, and (iii) how the government assistance has been considered in comparability analysis.

TP adjustment on capital transactions, guidance around working capital adjustments (WCA), and clarification on dating for simplified TP documentation

With respect to capital transactions, IRAS confirms in this 7th Edition that it will not make TP adjustments on capital transactions if they are not taxable or deductible under the Income Tax Act (ITA), and TP documentation is not required for such transactions. Instead, IRAS will apply the specific provisions in the ITA on the use of open-market price to determine the allowance and balancing adjustment. IRAS also indicates that a separate guidance will be provided in due course on the arm's length principle for capital transactions for the purpose of Singapore's Domestic Top-up Tax.

IRAS added clarification around WCA, including when these adjustments should be applied and the interest rates to be used. This guidance helps taxpayers navigate WCA more effectively. For simplified TP documentation, IRAS clarifies the requirement to state the date of completing simplified TP documentation in the declaration, as proof that the simplified TP documentation has been prepared contemporaneously.

Concluding remarks

Whilst there have been updates demonstrating IRAS' recognition of practical challenges and reducing compliance burden for taxpayers (e.g., increased TP documentation exemption threshold for certain transactions, etc.), there is a clear emphasis on IRAS' expectation for robust TP practice and compliance with Singapore TP requirements by taxpayers. These include expectation for taxpayers to undertake commercially rational RP transactions, adequate and contemporaneous TP documentation (along with recommendation for contemporaneous supplementary analyses), continuous review and timely update of analyses for RP transactions (including long-term RP loans), as well as robust analysis for MAP/APA purposes. Failure (especially repeatedly) to comply with the Singapore TP requirements would put taxpayers in an undesirable position when it comes to TP audit adjustment, surcharge remission, and may also impact the acceptance into MAP (and APA) programs.

The more stringent TP audit and tightened MAP evaluation process both signal an expectation for more controversy around RP transactions at the backdrop of increasingly complex economic landscape. Taxpayers should take this opportunity to review their current transfer pricing arrangements and evaluate appropriate mechanisms to proactively manage potential risks for their RP transactions.

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.



Lennon Lee

Tax Leader
+65 8182 5220
lennon.kl.lee@pwc.com



Falgun Thakkar

Transfer Pricing Leader
+65 9634 7984
falgun.d.thakkar@pwc.com



Yuhui Liu

Partner, Transfer Pricing
+65 9618 3450
yu.hui.liu@pwc.com



Paul Lau

Partner, Financial Services
Tax
+65 8869 8718
paul.st.lau@pwc.com



Lynn Tay

Partner, Financial Services
Tax
+65 9753 0749
lynn.tay@pwc.com



Jie Hong Liao

Partner, Transfer Pricing
+65 9755 2031
jie.hong.liao@pwc.com



Natalie Pham

Director, Transfer Pricing
+65 9839 3800
natalie.tn.pham@pwc.com

For further details on our industry specialists, [please click here](#).



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