



IRAS releases the 4th edition of Transfer Pricing Guidelines

On 12 January 2017, the Inland Revenue Authority of Singapore ('IRAS') released the fourth edition of the Singapore Transfer Pricing Guidelines. The revised guidelines make explicit reference to the Base Erosion and Profit Shifting ("BEPS") Action Plans 8 – 10 *Aligning Transfer Pricing Outcomes with Value Creation* and Action Plan 13 *Transfer Pricing Documentation*, thereby demonstrating compliance with international transfer pricing standards. The continued revision of the Singapore Transfer Pricing Guidelines also highlights the IRAS' focus on transfer pricing analyses and documentation to ensure that Singapore based corporate taxpayers are engaged in related party transactions in a manner compliant with the arm's length standard.

The key changes made in the Singapore Transfer Pricing Guidelines (4th edition) can be summarised as follows:

1. Aligning transfer pricing outcomes with value creation

In line with Action Plan 8 -10, the IRAS has explicitly noted that profits should be taxed where the real economic activities generating the profits are performed and where value is created. This has been a growing concern for tax authorities globally and is one of the cornerstones of the BEPS. In recent years, foreign tax authorities such as the Australian Tax Office, have also scrutinised transactions entered by Australian taxpayers into with Singapore counterparty along the same lines (i.e., is there true economic value being created in Singapore to justify the profits being booked).

In addition, in line with the changing guidelines, a more robust risk analysis is now required to demonstrate not only that an entity is contractually bearing risks, but also that the entity has the capacity and capability, from both a financial and operational perspective, to assume and manage the specific economically significant risks. To reflect the importance of risk in the functional analysis process, the IRAS has provided additional guidance and examples on risk analysis.

These changes suggest that a more robust function, asset and risk ("FAR") analysis may need to be prepared in respect of Singapore's operations. Furthermore, in line with Action Plan 8 – 10, we would also recommend that a value chain / creation analyses is carried in respect of the transactions that Singapore is involved in.

2. Administrative practice / safe harbour provided for intercompany loan transactions

In an effort to reduce transfer pricing compliance costs, the IRAS has finally introduced an administrative practice / safe harbour interest margin to be applied for cross-border intercompany loans provided / received by the Singapore taxpayer. Such a practice is with effect from 1 January 2017, which suggests that this safe harbour provision may not apply to any loans provided or received in prior years. The interest margin, which will be published on an annual basis, can be applied on all new loans, which are below the S\$15 million threshold, provided or received by Singapore taxpayers. It should be noted that the interest rate margin needs to be applied on the selected interbank rate (i.e., LIBOR / SIBOR) in the case of floating interest rate arrangements or the swap rate in the case of fixed interest rate arrangements. In the event that a taxpayer chooses not to apply the safe harbour interest rate margin, then a robust transfer pricing analysis will need to be carried out to support the arm's length interest rate.

This administrative practice is beneficial for Singapore taxpayers as it eliminates the need to prepare transfer pricing analysis. However, the interest rate margin may not be accepted / may not be in compliance with the foreign jurisdiction transfer pricing rules. Thus, we suggest that Singapore taxpayers adopt a holistic position, keeping in mind the transfer pricing provisions of Singapore as well as foreign jurisdiction, in terms of how the safe harbour is applied on intercompany loan transactions.



3. Guidance on the application of the related party transaction thresholds

Although the related party transaction threshold (in Paragraph 6.19(f)) seems to apply to all related party loans, Paragraph 13.30 suggests that with respect to loans, the IRAS will apply the threshold to each related party, individually and not in aggregate. While this makes it easier to qualify for the administrative provision explained above, this is substantially different to the treatment of all other related party transaction whereby the aggregation is done on each category of related party transaction (irrespective of the number of related parties).

Furthermore, the IRAS has also noted in passing that strict pass-through costs should be explicitly included for service transactions. The explicit reference to strict-pass through costs suggests that the IRAS will want to ensure that such costs will indeed qualify as strict pass through costs. This also underscores the IRAS' continued focus on ensuring that the cost base in service arrangements are arm's length.

4. Enhanced guidance on Mutual Agreement Procedures ("MAPs") and Advance Pricing Arrangements ("APAs")

With respect to APA applications, IRAS has provided additional clarification on roll-back years for APAs, as well as additional information that should be included in APA submissions.

Similar clarifications have also been provided for MAPs. For example, the IRAS is open to considering a refund of any interest / penalties that may have already been imposed in a transfer pricing audit during the MAP discussions. Furthermore, with respect to MAPs, the IRAS has noted that any negotiation between the IRAS and the foreign competent authority may be challenging if the taxpayer has already chosen to accept the transfer pricing audit settlement.

Thus, with respect to both APA and MAP applications, taxpayers need to understand the procedures and limitations that such negotiations may place on both the IRAS as well as the foreign competent authorities before deciding to proceed with such strategies.

In addition, the IRAS has also made reference to Action Plan 5 - *Countering Harmful Tax Practices More Effectively, taking into Account Transparency and Substance* – to outline the framework by which IRAS will exchange information on unilateral APAs with foreign jurisdictions.

Concluding remarks

The continued revisions that IRAS makes in respect of its transfer pricing guidelines demonstrates IRAS' commitment to the global issue of BEPS. The release of Singapore Transfer Pricing Guidelines (4th edition) shows IRAS' continued focus and attention on transfer pricing and highlights the need for Singapore based corporate taxpayers to adhere to the arm's length standard.

With the global implementation of the BEPS Action Plans, transfer pricing continues to receive attention across multiple jurisdictions. It is likely that many of Singapore's trading partners will be reviewing and repositioning their transfer pricing provisions in line with the global standards this year. The changes that are likely to take place will require multinational corporations to holistically review and document the related party transactions entered into by the Group in a consistent manner.