2.2 History of transfer pricing in Singapore

Following on from the introduction of the Transfer Pricing Guidelines in 2006, the IRAS introduced the transfer pricing consultation process in 2008 to assess the level of compliance with Singapore's Transfer Pricing Guidelines and identify areas where IRAS can further assist taxpayers on transfer pricing.

In addition, in 2008, the IRAS also provided additional administrative guidance on negotiating and concluding Advance Pricing Agreements (APAs).[3] It should be noted that the IRAS has concluded APAs even before the transfer pricing guidelines were formally introduced. However, with the experience gained in responding to APAs, the IRAS realised that taxpayers were not aware of their obligations in requesting for an APA. The 2008 administrative guidance on APAs provided taxpayers with procedural requirements and timelines that they needed to adhere to when requesting for an APA. The circular also outlined circumstances in which the APA may be discontinued by the IRAS.

In 2009, the IRAS issued its circular on transfer pricing for related party loans and related party services. As far as related party loans were concerned, the IRAS provided its view on the safe harbours that will be applicable for domestic related party loans and provided preliminary guidance on how cross-border related party loans should be structured. With respect to services, the IRAS introduced the:

- safe harbour for routine services;
- cost pooling;
- notion of pass-through costs.

In 2010, the IRAS formally enacted transfer pricing provisions, through the introduction of s 34D, in the *Singapore Income Tax Act*. This was a significant development for both taxpayers and tax authorities as it essentially shifted the burden of proof from the IRAS to the Singapore taxpayer.

Prior to 2010, the IRAS had to essentially rely on the provisions of Articles 7 and 9 of the DTA to review transfer pricing arrangements. However, if the Singapore taxpayer was transacting with a related party located in a country that did not have a tax treaty with Singapore, the IRAS would have had to rely on its domestic legislation (e.g. anti-avoidance provisions). In other words, the IRAS had to demonstrate that the Singapore taxpayer was transacting in a manner to avoid paying taxes.

3 See 14.1 for the definition of APA.

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With the introduction of s 34D in the *Singapore Income Tax Act*, the IRAS now has the ability to review the transfer pricing arrangements of all Singapore taxpayers based on the arm's length principle, irrespective of whether they are transacting with a treaty partner or not.

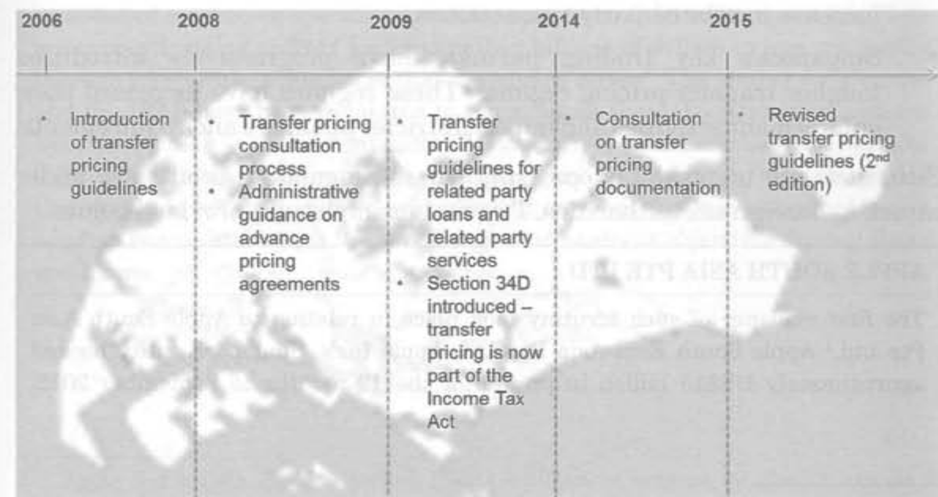
The year 2015 culminated in a substantial revision of the transfer pricing guidelines. The revised transfer pricing guidelines, hereafter referred to as the 2015 Transfer Pricing Guidelines, consolidates all the previous guidance and circulars provided by the IRAS. In addition, it provides clarity to various technical issues that arise from the practical implementation of transfer pricing.

The 2015 Transfer Pricing Guidelines addresses the needs of majority of the taxpayers in understanding and complying with transfer pricing requirements in terms of :

- Applying the arm's length principle.
- Stating the objectives of preparing transfer pricing documents and adopting certain parties to reduce compliance costs for the taxpayer.
- Detailed guidance in avoiding and resolving transfer pricing disputes using MAP and APA.
- Setting out various types of adjustments relating to transfer pricing issues.

The growth and development of transfer pricing is depicted in the diagram below:

Figure 2.1



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authorities will be satisfied if they see that the royalties paid by the Vietnamese company to its headquarters in Singapore are not higher than those that would be paid to an independent enterprise for a similar transaction. But if the royalties are too high, there is a possibility that profits are being shifted out of Vietnam to Singapore to reduce tax liabilities there.

In the above situation, the "arm's length principle" will be used by both the Vietnamese tax office/the Inland Revenue Authority of Singapore (IRAS), as well as the MNC Group to demonstrate that transactions among group/affiliate companies are appropriate.

3.2 Legal basis of arm's length

The legal basis for applying the arm's length principle in Singapore is s 34D of the *Singapore Income Tax Act*. Section 34D(1) provides:

> "Where 2 persons are related parties and conditions are made or imposed between the 2 persons in their commercial or financial relations which differ from those which would be made if they were not related parties, then any profits which would, but for those conditions, have accrued to one of the persons, and, by reason of those conditions, have not so accrued, may be included in the profits of that person and taxed in accordance with the provisions of this Act."

The arm's length principle is also found in all of Singapore's DTA, typically in Paragraph 2 of the Business Profits Article, which states that when attributing profits in a contracting state/party to a permanent establishment in that state/party, the permanent establishment should be considered as "a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions".

Furthermore Paragraph 1 of the Associated Enterprises Article states:

> "Where...conditions are made or imposed between...two [associated] enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly."

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The above references are consistent with the arm's length principle found in Paragraph 1 of Article 9 of the OECD Model Tax Convention.[1] Article 9 provides:

> "[Where] conditions are made or imposed between the two [associated] enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly."

The United Nations has also produced a *United Nations Model Convention for Treaties between Developed and Developing Nations* in 1980. The UN Model has been updated and was finally launched as the 2011 Update on 15 March 2012. The UN Model is in many respects similar to the OECD Model but the differences (such as preserving greater taxation rights to countries hosting investments) are very significant, especially for developing countries.

The UN Model contains similar provisions to the OECD Model in Article 9 (at Paragraph 1 especially) and therefore serves as a guide for applying the arm's length principle for developing countries. However the UN Model also includes an additional paragraph (Article 9(3)) which stipulates that a Contracting State is not required to make the corresponding adjustment referred to in Article 9(2) where judicial, administrative or other legal proceedings have resulted in a final ruling that, by the actions giving rise to an adjustment of profits under Article 9(1), one of the enterprises concerned is liable to a penalty with respect to fraud, or to gross or wilful default.

3.3 Prevalence of the arm's length principle

Several countries have adopted the arm's length principle as the appropriate measure for transfer pricing. A major reason is that the arm's length principle provides broad parity of tax treatment for members of multinational groups and independent enterprises. Because the arm's length principle puts associated and independent enterprises on a more equal footing for tax purposes, it avoids the creation of tax advantages or disadvantages that would otherwise distort the relative competitive positions of either type of entity. In so removing these tax considerations from economic decisions, it is

1 The Model Tax Convention forms the basis of bilateral tax treaties involving OECD member countries and an increasing number of non-member countries.

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of the comparability analysis is to identify any differences between the third party and related party situations that can materially affect the price and margin being compared. Where differences do exist, it is necessary to determine if reasonably accurate adjustments can be made to eliminate the effect of such differences.

The IRAS notes that such a comparability analysis should consider the following three aspects:

(a) characteristics of goods, services and intangible properties[1];

(b) analysis of functions performed, assets used and risks assumed (i.e. FAR);[2] and

(c) commercial and economic circumstances.

The requirements for comparability analysis under the 2015 Transfer Pricing Guidelines are somewhat different from those outlined in the OECD Transfer Pricing Guidelines. The OECD Transfer Pricing Guidelines require the following aspects to be reviewed from a comparability perspective:

(a) characteristics of property or service;

(b) functional analysis;

(c) contractual terms;

(d) economic circumstances;

(e) business strategies.

Although the OECD Transfer Pricing Guidelines seem to require additional comparability factors to be reviewed, the 2015 Transfer Pricing Guidelines are broadly consistent with the OECD Transfer Pricing Guidelines as the factors included in "economic circumstances" and "business strategies" have been combined into "commercial and economic circumstances" in the 2015 Transfer Pricing Guidelines.

However, under the 2015 Transfer Pricing Guidelines as well as the 2006 Transfer Pricing Guidelines, there is no explicit requirement to compare the contractual terms between the related party and third party transactions.

The contractual terms of a transaction generally define explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the parties. Contractual terms are important because in transactions between

1 Although this factor refers to the comparability of goods, services and intangible property, please do note that it will also include intercompany financing. The explicit comparability factors that should be considered for intercompany financing have been detailed in Paragraph 13 of the 2015 Transfer Pricing Guidelines.

2 Going forward, this will be referred to as the function asset risk (FAR) analysis.

independent enterprises, the divergence of interests between the parties ensures that they will ordinarily seek to hold each other to the terms of the contract, and that contractual terms will be ignored or modified after the fact (generally only if it is in the interests of both parties). The same divergence of interests may not necessarily exist in the case of associated enterprises. It is therefore important to examine whether the conduct of the parties conforms to the terms of the contract or whether the parties' conduct indicates that the contractual terms have not been followed or are a sham. In such cases, further analysis is required to determine the true terms of the transaction.

Although this might be the case, a close read of the 2015 Transfer Pricing Guidelines make plenty of references to contracts and contractual terms. As a matter of fact, when a review of related party transactions is conducted, the IRAS does ask for intercompany agreements. Thus, an analysis of contractual terms should be a part of the functional analysis process. The terms of a transaction (from a contractual perspective) may also be found in correspondence/communications between the parties other than a written contract.

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4.2.1 Evaluate transactions on an aggregate or separate basis

Before the comparability factors are reviewed, it is necessary to determine whether the transactions are reviewed on a transaction-by-transaction basis or on an aggregate basis. In general, any analysis should be applied on a transaction-by-transaction basis to obtain the most precise approximation of arm's length conditions.[3] In other words, each transaction should be evaluated on a stand-alone basis.

In addition, the IRAS notes that if the individual transactions are highly inter-related and it can be demonstrated that independent parties in comparable circumstances would typically price the individual transactions on an aggregate basis, taxpayers may consider evaluating the transactions on an aggregate basis.[4]

To further understand whether transactions should be considered on a stand-alone basis or collectively, please refer to the following examples:

3 Paragraph 5.25 of the 2015 Transfer Pricing Guidelines.

4 Paragraph 5.26 of the 2015 Transfer Pricing Guidelines.

protect the inventory. The functions performed can be quantified by the additional personnel that need to be hired to carry out the warehousing and distribution activities. Finally, the cost of the asset can either be determined through depreciation expense (if the asset is owned) or lease expense. Once these costs have been identified, an adjustment can then be made to the third party price.

Careful analysis is required if such calculations are performed. In addition, the tax authorities are likely to query the validity and appropriateness of any or all adjustments.

4.2.4 Commercial and economic circumstances

Arm's length prices may vary across different markets even for transactions involving the same property or services. Therefore, achieving comparability requires that the markets in which the independent and associated enterprises operate do not have differences that have a material effect on price or that appropriate adjustments can be made. As a first step, it is essential to identify the relevant commercial and economic circumstances, taking account of available substitute goods or services.

Such commercial and economic circumstances can be broadly categorised as follows:

- economic circumstances (see 4.2.4.1);
- government policies and regulations (see 4.2.4.2);
- business strategies (see 4.2.4.3).

4.2.4.1 *Economic circumstances*

This is an important factor surrounding any transaction. Market prices for the transfer of the same or similar property may vary across different markets owing to cost differentials and/or differences in purchasing power and habits prevalent in the respective markets, which may affect the market price. Given that the price of the same property or service may vary from one market to another, it is necessary to evaluate the economic circumstances that surround the transaction to give rise to a meaningful comparison of price or margin.

The economic analysis examines the industry and the circumstances in determining market comparability. Some of the factors are listed below:

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- industry overview and analysis;
- geographic location;
- market size;
- level of market at which the taxpayer operates (e.g. wholesale or retail);
- market share;
- extent of market competition;
- consumer purchasing power;
- availability of substitute goods or services;
- price of production factors;
- cost of transportation;
- government regulatory control, etc.

Markets can be different for numerous reasons. It is not possible to list exhaustively all the market conditions which may influence transfer pricing analysis but some of the key market conditions are discussed below.

Geographic markets

In general, third party comparable companies or transactions should be derived from the geographic market in which the controlled taxpayer operates. This is because there may be significant relevant differences in economic conditions between different markets. If information from the same market is not available, an uncontrolled comparable derived from a different geographical market may be considered if it can be determined that:

(i) there are no differences between the two markets that would materially affect the price or profit of the transaction; or

(ii) reasonably reliable adjustments can be made to account for such material differences between the two markets.

Level of market at which the taxpayer operates

The level of market in which the taxpayer operates can be a key factor in determining comparability. An example is detailed below.

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In view of the above, tax authorities tend to view market penetration strategies with suspicion. Therefore, the taxpayer will need to maintain proper documentary evidence and prove that there is sacrifice of profitability for a certain period under similar economic circumstances with a view to establish a market and long term profit.

4.2.5 Practical application of the comparability analysis

As one may observe based on the above discussion, it is difficult to perform a robust comparability analysis between controlled and uncontrolled transactions due to lack of available information.

However challenging it may be, establishing a comparable situation is important. This is because reasonable accurate adjustments may be made to eliminate such differences.

The IRAS has addressed such issues in the 2015 Transfer Pricing Guidelines as described below.

4.2.5.1 *Characteristics of product, services and intangibles*

In the case of physical characteristics, it may be difficult to opine as to whether the product subject to the related party transaction is a product with better quality or more features than the uncontrolled transaction. In addition, even if the product subject to the related party transaction may have more features, it may not necessarily enhance the value of the product, and therefore be sold at a higher price.

The nature and features of goods, services and intangibles transacted between related parties in comparison to independent parties must be examined closely. The reason being that similarities and differences should be identified as this will impact the value.

As mentioned earlier, some important characteristics identified by the IRAS are as follows:

(1) Transfer of goods – the comparisons will be physical features, quality, reliability, availability and volume of supply.

(2) Provision of services – the comparisons will be the nature and extent of services.

(3) Intangible properties – the comparisons will be form of transaction, type, nature, duration, extent of rights and anticipated benefits from its use.

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In general, it is extremely difficult to translate a value judgement on the product (i.e. a product is of a better quality or more reliable) to one of quantitative measure.

4.2.5.2 *Functional analysis*

The extent of information required to determine the functional analysis comparability is difficult to obtain.

Looking back at Example 4.3, let us assume that the A-B transaction is the related party transaction, while the C-D transaction is the third party transaction.

Given that A-B is the related party transaction, it is clear that a determination of the functional-asset-risk split between the manufacturer and distributor can be arrived at as all the information needed for the FAR analysis can be obtained from within the Group.

On the other hand, information on transaction C-D may not be available. It should be noted that in any transfer pricing analysis, one can only rely on publicly available information. Publicly available information can be obtained from websites, industry or market publications, as well as financial statements. In the case of transaction C-D, in order to evaluate the comparability of the uncontrolled transaction, we first need to establish that Party D is a customer of Party C. No company is required to disclose who its customers or suppliers are. Therefore, it is often difficult to isolate a particular transaction between one supplier (i.e. Party C) and a customer (i.e. Party D). In addition, information on the extent of functions, assets and risks may not be available on either of the parties. At best, the analyst will know if Party D operates as a manufacturer (disclosed in the principal business activities in the financial statement) but the extent of such manufacturing activities will not be evident. In addition, information at the transaction level/product price level will not be available. Financial statements typically provide the aggregated income and expenses across all products, across all suppliers. Thus, it would be difficult to pinpoint that the particular transaction price between Party C and Party D would be, for example, S$50.

Some of this information may be more readily available in the scenario detailed in Example 4.4 where Party A sells products to both related and third parties. Given that most of the information is internal to Party A, it would be easy to determine:

(a) comparability in terms of product characteristics;

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Summary

As one would expect, in the application of the external CPM, it is critical to ensure that the cost bases that are being evaluated are comparable. However, in most cases, when relying on external data, it may be difficult to ensure that the cost bases are comparable as there are insufficient disclosures on how each entity treats each segment of costs. For example, machines used in manufacturing may either be owned by the manufacturer or leased. If such differences exist between the related party manufacturer and the third party manufacturer, the cost plus mark-up calculations are likely to be tainted. In addition, similar to the RPM, the CPM is also affected by how expenses are categorised into cost of goods sold versus operating expenses.

In Example 4.12, there is a disclosure statement that says that US1, US2 and US3 account for supervisory and G&A costs in their COGS, while SingCo accounts for it through operating expenses. Such disclosures will typically not exist in real-life situations. Therefore, the applicability of the CPM in real-life situations is low.

The CPM would be most appropriate where there are semi-finished goods which are sold between related parties or where the related party transaction involves the provision of services.

The CPM is considered a one-sided method as it essentially evaluates the transaction from the perspective of the manufacturer or service provider. In the case of the CPM, if the gross cost plus mark-up earned by the manufacturer/service provider is consistent with the arm's length standard (i.e. what other third party service providers earn), then it necessarily means that the sale of the product/service by the related party manufacturer/service provider is arm's length, which essentially means that the related party purchase, from the perspective of the other related party, is arm's length.

4.3.4 Transactional net margin method (TNMM)

The TNMM determines the net margin of related party transactions based on the indicator of profit margins of comparable unrelated transactions.[14] The TNMM is usually applied to the related party transactions of sales, transfer and usage of tangible goods, and provision of labour services.

The TNMM is considered an extension of the RPM or the CPM. The RPM and CPM evaluate the margins of the distributor and manufacturer, respectively,

14 Paragraph 5.72 of the 2015 Transfer Pricing Guidelines.

at the gross profit level. However, the TNMM evaluates the compensation earned by the distributor or manufacturer at the net profit level as follows:

1. With respect to the distributor, the TNMM will evaluate the net profit margin, while the RPM evaluates the gross profit margin.
2. With respect to a manufacturer/service provider, the TNMM will evaluate the net cost plus mark-up rather than the gross cost plus mark-up.

The types of profit level indicators[15] that are typically referred to include:[16]

- Return on sales, which is defined as the ratio of operating profit to sales/revenues. This essentially is an extension of the RPM to the operating profit level rather than the gross profit level.
- Mark-up on total costs, which is defined as the ratio of operating profit to total costs. As explained above, this essentially is an extension of the CPM to the operating profit, where the operating profit to total costs is evaluated, as opposed to evaluating the gross profit to cost of goods sold.
- Return on assets/capital employed, which is defined as the ratio of profits to assets or capital employed. Assets or capital employed is a balance sheet entry and there are multiple definitions depending on whether the assets include liabilities. It should be noted that the 2015 Transfer Pricing Guidelines do not explicitly define "assets". The OECD Transfer Pricing Guidelines notes that only operating assets should be used in the definition of assets. Operating assets include tangible operating fixed assets, including land and buildings, plant and equipment, operating intangible assets used in the business, such as patents and know-how, and working capital assets such as inventory and trade receivables (less trade payables). Investments and cash balances are generally not operating assets outside the financial industry sector.
- Berry ratio, which is defined as the ratio of gross margin to operating expenses.[17] The Berry ratio is typically used for distributors that do not perform any value-added activities. While the distributor has its

15 It should be noted that the OECD Transfer Pricing Guidelines that was revised in 2010 refers to profit level indicators as net profit indicators. Thus, profit level indicators and net profit indicators are used interchangeably.

16 It should be noted that Singapore Transfer Pricing Guidelines do not explicitly define any of these profit level indicators. As such, we have relied on the definition of these profit level indicators based on either conventional wisdom or traditional practice.

17 This net profit indicator (NPI) has been named after Charles Berry who devised this profit indicator while serving as an expert witness for the Inland Revenue Service. The argument that was made was that distributors should earn a return commensurate with the distribution services performed.

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4.3.7 Selection of transfer pricing method and the tested party

IRAS does not have a specific preference for any one method. Instead, the method that produces the most reliable results, taking into account the quality of available data and the degree of accuracy of adjustments, should be selected. The choice of the most appropriate transfer pricing method depends on the facts and circumstances of each case. In order to select any one method as the most appropriate to justify the arm's length nature of the related party transactions, taxpayers have to actively consider the following:

(a) strengths and weaknesses of the five methods above;

(b) nature of the transaction and appropriateness of the method applied to the transaction;

(c) availability of reliable information needed to apply the method; and

(d) degree of comparability between the related and independent party transactions, and the accuracy with which comparability adjustments can be made to eliminate differences.

In general, with the description of the methods and an analysis of the intercompany transactions entered into by taxpayers as well as lack of data, certain assumptions can be made in respect to the transaction type and the most suitable method. This is described in the table below.

Type of transaction	Methods that may be suitable	Commonly used method
Provision of manufacturing services / provision of R&D services / Provision of strategic management and administrative services	CUP / CPM / TNMM / PSM	TNMM
Distribution of product	CUP / RPM / TNMM / PSM	TNMM
License of royalty / patent / known-how	CUP / PSM	CUP
Integrated business operation involving intangibles on both parties	PSM	PSM
Intercompany financing	CUP	CUP

4.3.7.1 *Selection of tested party*

Once the appropriate transfer pricing method (keeping in mind the specific factors of the related party transactions) has been selected, the tested party

needs to be selected in the case of the one-sided methods (i.e. CPM, RPM and TNMM).

With respect to the one-sided methods, it is necessary to choose the party to the transaction for which the financial indicator (i.e. gross mark-up on cost, gross margin, or net profit indicator) is applied. This process is known as the *selection of the tested party*.

However, the selection of the CPM automatically implies that the tested party is the entity that manufactures or provides the service. This arises from the fact that the CPM is typically applied to the service provider. Similarly, the selection of the RPM will imply that the tested party is the entity that distributes. This arises from the fact that the RPM, which calculates the gross margins, is applied to the distributor.

Therefore the determination of which entity should be the tested party is only explicitly required in the application of the TNMM.

As a general rule, the tested party is the one where:

(a) a transfer pricing method can be applied in the most reliable manner; and

(b) most reliable comparables can be found.

In other words, the tested party is often the party with the smaller scope of functions and less complex operations. The simpler entity is typically selected as the tested party as it is often easier to find comparable data that reflect these simple operations. In addition, fewer adjustments are likely to be required.

Given that we are selecting the "simpler" entity to the transaction as the tested party, the choice of the tested party should be consistent with the functional analysis of the transaction. As mentioned earlier, the functional analysis will describe the functions, assets and risks that are performed by the various entities to the transaction. Based on such an analysis, it can be determined which entity should be treated as the simpler entity in the transaction.

Let us go back to Example 4.3 that was discussed earlier:

> *Example 4.16*
>
> Party A operates as a manufacturer who owns significant tangible assets, and undertakes a whole range of activities (such as design, manufacturing, logistics, etc) as well as the risks associated with the transaction (e.g. product liability risks, inventory risks, foreign exchange risks). Party B operates as a simple distributor

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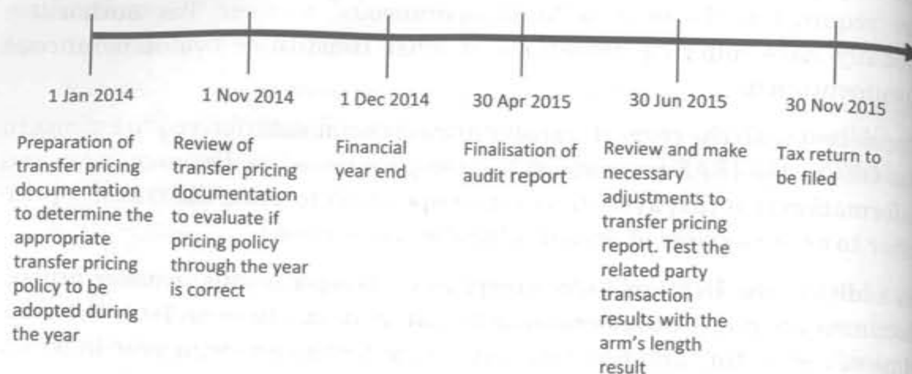
Figure 5.1



5.5 Who should prepare transfer pricing documentation?

In the 2015 Transfer Pricing Guidelines, the IRAS has provided administrative exemptions for the preparation of transfer pricing documentation. Taxpayers that do not meet the administrative exemptions would then have to evaluate if their transactions meet the thresholds.

The administrative exemptions and the related party transaction thresholds are provided to help taxpayers manage transfer pricing documentation compliance and administrative costs.

5.5.1 Administrative exemptions

The IRAS does not expect taxpayers to prepare transfer pricing documentation under the following situations:

(a) Where the taxpayer transacts with a related party in Singapore and such local transactions are subject to the same Singapore tax rates for both parties. With respect to loans, an additional condition is placed where the Singapore taxpayer is not in the business of borrower and/or lending.

(b) Where the taxpayer applies the 5% cost mark-up for routine services in relation to the related party transactions.[5]

5 "Routine" services are defined in Annex C of the 2015 Transfer Pricing Guidelines.

(c) Where the related party transactions are covered by an agreement under an advance pricing agreement (APA).[6] In such circumstances the taxpayer is required to keep proper records for the purpose of preparing the annual compliance report to show compliance and critical assumptions remain valid.

Where the taxpayer does not meet the above administrative exemptions, the taxpayer then has to consider the value or amount of the related party transactions disclosed in the specific year's financial accounts. It should be noted that the related party transaction values exclude the amounts stated in the administrative exemptions.

Category of related party transactions	Threshold (S$) per financial year
Purchase of goods	15 million
Sale of goods	15 million
Loans provided to related parties	15 million
Loans received from related parties	15 million
All other transactions (service income/expense, royalty income/expense, rental income/expense)	1 million per category of transaction

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Key observations

(1) The IRAS applies these thresholds on a transaction-by-transaction basis. For example, if the sale of goods to related parties exceeds the S$15 million threshold while the purchase of goods does not, the taxpayer is only required to prepare transfer pricing documentation to demonstrate that the pricing of the sale of goods is consistent with the arm's length standard.

(2) Some transactions are not explicitly mentioned in the above table. With respect to these transactions, the taxpayer should consider how these transactions should be categorised – if they are broadly considered to be trade transactions, it is likely that the thresholds for the purchase/sale of goods will apply. On the other hand, if it is considered to be an intangible in nature, then it will be categorised under "All Other Transactions". For example, cost sharing agreement payments, as

6 Transactions subject to an APA are excluded as the IRAS would have already reviewed and opined on the related party transaction. The taxpayer is still expected to maintain certain documentation (e.g. the annual compliance report). See 14.1 for the definition of APA.

The risks that should be considered include:

- financial risks (e.g. method of funding, fluctuation in interest rates, funding of losses, foreign exchange risk);
- product risks (e.g. design and development of product, risks associated with R&D, product liability risk, intellectual property risks, inventory risks);
- market risks (e.g. fluctuation in demand and prices, business cycle risks, volume risks);
- collection risk (e.g. credit risk, bad debt risk);
- entrepreneurial risk (e.g. risk of loss associated with capital investment, single customer risk);
- general business risk (e.g. risk associated with the exploitation of a business, inflation risk);
- country/regional risk (e.g. political risk, regulatory risk, risk related to government policies);
- operational risks (e.g. risks relating to breakdown of machinery, reliability of suppliers, inventory risks and carrying costs, R & D risk and environmental risks).

The impact of risk on the related party outcome is a key part of allocating profits between the various related parties. In general, if a taxpayer bears the risks, it would be expected that his/her profitability arising from the related party transaction will vary.

On the other hand, an entity that bears minimal risk, would be expected to earn a consistent level of profits arising from its operations, year on year.

6.4.4 Preparing the functional analysis

The functional analysis is typically carried out by reviewing key financial, legal and business documents obtained from the group as well as the Singapore taxpayer. In addition, additional clarity is obtained by speaking to key operational personnel to understand their key roles and responsibilities and how each division interacts with one another within the company also allows the MNC to gain a better insight to its business, the industry and key responsibilities of different companies in the group.[2]

In most cases, the head of each business division can provide:

- an overview of the value chain;

2 Such a process is known as the functional analysis process (FAR).

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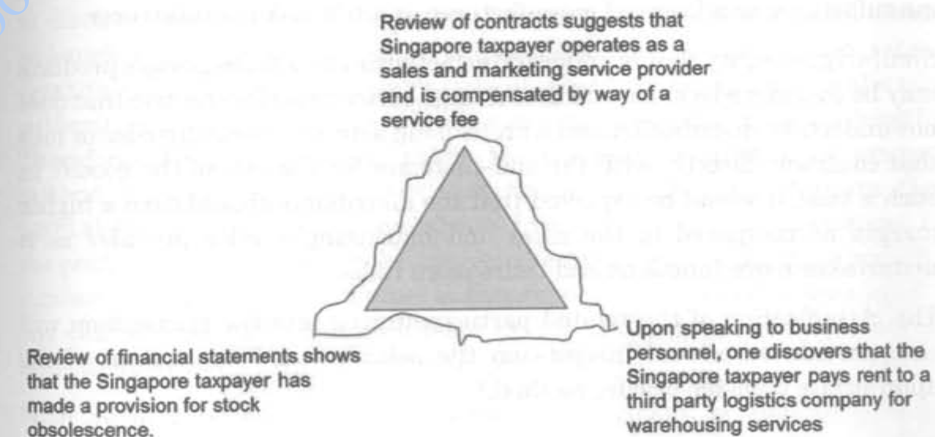
- an explanation of their roles and responsibilities and interaction with other functions and group entities;
- decision making processes within the group and risks borne; and
- relevant industry information and trends as they impact the company.

The functional analysis should also keep in mind the overall business context of the group as well as the industry business models to ensure that there are no inconsistencies between what is being captured during the interview process and the overall business strategy of the group in respect of the Singapore taxpayer.

When preparing the functional analysis, it is critical for the analyst (whether the internal resource or the external consultant) to tick and tie the business reality with the accounting and legal realities. This essentially means that it is necessary to evaluate if the legal contracts, financial statements, invoices and other such documents are depicting a story that is consistent with what the key operational people are detailing.

A perfect example of an inconsistent relationship between the economic/accounting and legal realities is depicted in the diagram below.

Figure 6.1



Based on the above example, it is clear that in reality, the Singapore taxpayer actually undertakes additional distribution related activities which are not explicitly covered or noted in the legal agreements. Although the taxpayer may have classified this entity as a service provider, a tax authority upon reviewing the information about this company may turn around and reclassify the Singapore taxpayer as a distributor, given that it pays for warehousing services and recognises inventory risk on its books.

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6.8.3 Country-by-country report

The country-by-country (CbC) report requires the Group to report annually and for each tax jurisdiction in which the Group does business the following information:

- revenue;
- profit before income tax;
- income tax paid and accrued;
- total headcount;
- total capital and retained earnings;
- value of tangible assets;
- primary business activity of the specific entity.

Based on the requirements, it is most apt for the CbC to be prepared by the head office/the ultimate parent entity of a Group. The OECD has provided a prescribed format for the preparation of the CbC report and this needs to be done for each fiscal year.

The CbC is intended to be for tax administrations only and will not be made public. It is expected that the CbC report will be helpful for high-level transfer pricing risk assessment purposes. The CbC is not meant to be used as a substitute for a detailed transfer pricing analysis of individual transactions and prices based on a full functional analysis and a full comparability analysis.

6.8.4 Will IRAS adopt the revised transfer pricing documentation guidelines?

The Singapore Transfer Pricing Guidelines were revised in January 2015 after the finalisation of Chapter 5 of the OECD Transfer Pricing Guidelines. While the IRAS has revised its transfer pricing documentation to require more information at the group and individual entity levels, the IRAS has remained silent on whether it will explicitly adopt the three-tiered approach, where it can ask for the masterfile, local file, and/or the CbC report. Given that it is the head office that will typically prepare the CbC, it is unclear whether the IRAS will expect Singapore headquartered companies to prepare the CbC report.

In June 2015, the OECD released the implementation package for Base Erosion and Profit Shifting (BEPS) CbC reporting which is expected to

facilitate a consistent and swift implementation of the new transfer pricing standards introduced by the revised Chapter 5.

This is definitely a space to watch to see how Singapore and other regional tax offices are going to adhere to the OECD's suggestions. More on how the IRAS is viewing the BEPS Action Plan is discussed in Chapter 16 of this book.

6.9 Tips for preparing documentation

The contemporaneous documentation requirement will place a significant burden on many taxpayers in Singapore. Although the IRAS is aware of this compliance burden and notes that taxpayers are not expected to incur compliance costs which are disproportionate to the amount of tax revenue at risk or complexity of the transactions, the introduction of contemporaneous annual transfer pricing documentation introduces a new compliance requirement for taxpayers operating in Singapore.

It is therefore important to plan and manage this information collection and documentation as efficiently as possible to avoid excessive costs and time commitment, as well as ensuring maximum benefit is derived from the documentation in addition to fulfilling compliance obligations.

The following are some tips to assist and to gain maximum benefit from this process:

(1) Identify internal resources to be involved in the documentation process. Understand what can realistically be in-sourced and what parts will need the help of an external advisor. Specifically, information on the company/group and the industry is something that may be readily available with the taxpayer and therefore is something that can be prepared in-house. Even if it is decided that the entire documentation will be prepared by an external advisor, it is key to identify a project manager, who will be able to manage the information flow effectively.

(2) Develop appropriate templates and tools to simplify and standardise aspects of the transfer pricing documentation and transfer price setting process. It should be noted that in the first year of implementation, this may take time and cost, but having a standardised process will bear fruit in future years.

(3) Most MNCs have entities that are located in multiple jurisdictions. It is likely that each of these jurisdictions may also require local taxpayers to prepare transfer pricing documentation. Thus, it will make sense for the Group to review the overall transfer pricing compliance burden in

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- costs related to reporting requirements of the parent company, including the consolidation of financial reports; and
- costs of raising funds for the acquisition of new companies to be held by the parent company.

(b) Duplicative in nature

Duplicative services as the name indicates are services that are duplicated at the service recipient. These are services that the service recipient performs on its own, and therefore, given that there is no added commercial value provided by such services, the service recipient would not be expected to pay for the service.

An example of a duplicative service occurs where a person is tasked to handle Human Resource (HR) matters at the service recipient's organization, and yet the service provider charges for services associated with HR activities to the service recipient. In this case, the tax authority in the service recipient's jurisdiction may argue that the HR services provided by the service provider are duplicative. One way to support a HR related service charge would be for the taxpayer to demonstrate that although HR services are provided internally by the service recipient, the nature of the services received from the service provider is different to the nature of services provided internally. To the extent that such distinction is made, it may still be possible to support a similarly labelled service provided by the service provider. The functional analysis is a particular key in highlighting these differences.

The IRAS does not provide detailed explanation/definitions of shareholder and duplicative services in paragraph 12 of the 2015 Transfer Pricing Guidelines. However, these concepts are well-versed through the OECD Transfer Pricing Guidelines. In addition, they are covered broadly under the IRAS "benefit test". Taxpayers therefore need to also keep these distinctions in mind in order to support their intercompany services transactions.

(c) On call services

The OECD Transfer Pricing Guidelines also refer to another special category of services in the context of intra-group services, namely services provided on-call. The availability of such services generally requires the existence of a support group of some sort and an understanding between the group members about the nature of the assistance being provided in any field of operation whenever required, and on an on-call basis. For example, a parent company or a group service centre may be available to provide assistance with regard to legal, finance, technical or tax issues at any time.

The key question here is whether the availability of that service in itself is regarded as a separate service. For example, services provided on a retainer basis are common in the legal/financial consulting space. In such cases, on-call services are considered provision of services that should be charged.

(d) Services that provide incidental benefits.

7.2.2 Determination of arm's length pricing

Once it has been determined that intercompany services have indeed been provided, the next step in the transfer pricing analysis of intercompany services is to determine the appropriate payment for these services.

To determine if the service charge is consistent with the arm's length standard, the IRAS once again adopts the three step approach that was outlined in Chapter 4:

(a) Step 1: Undertaking the comparability analysis.
(b) Step 2: Determine transfer pricing method.
(c) Step 3: Determine the arm's length value for the services provided.

Each of the above steps are discussed as follows:

7.2.2.1 *Step 1: Comparability analysis*

The comparability analysis for related party services will consist of two aspects.

The first aspect of the comparability analysis is to understand the services that are being provided. Specifically, the following factors should be kept in mind:

(a) nature of services;
(b) how are the services provided;
(c) who is involved in the provision of these services; and
(d) benefits expected to be provided from the provision of the services.

In addition, the comparability analysis should also take into account from the perspective of the:

(a) Service provider: how would an independent service provider charge for the services that are being provided; and
(b) Service recipient: what would an independent service recipient have been willing to pay for the services under similar circumstances?

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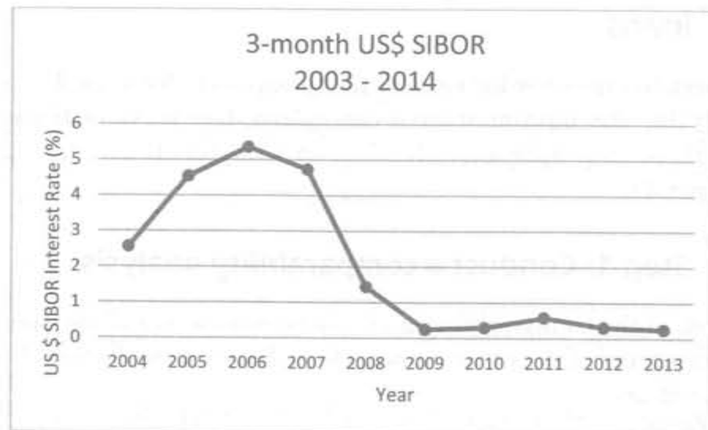
Figure 8.1



(c) The seniority and/or security of the loan is another key consideration. Seniority refers to the order of repayment in the event of a sale of bankruptcy of the issuer. Senior debt is generally considered lower risk and therefore carries lower interest rate than other forms of debt. Similarly, debt that comes attached with security will also have a lower interest rate than other debts.

(d) Principal amount, duration and tenor of the loan.[2] These factors will have an impact on the pricing of the intercompany loan, e.g. the larger the amount of the loan (the principal), all things considered the same, the higher the interest rate likely to be charged because of the higher probability of default.

8.3.2 Step 2: Identifying the most appropriate transfer pricing method

In general, the CUP method is the preferred method for determining the arm's length pricing for related party loans as it is the most suitable method for loan transactions. As a matter of fact, in practice, it is difficult to consider the application of an alternative method, although the IRAS notes that if another method is considered more appropriate, taxpayers may use that method.

Application of an internal CUP

Similar to the discussion in Chapter 4, the taxpayer can choose to apply either an internal CUP or an external CUP.

2 Duration refers to the total repayment period, while tenor refers to the amount of time left for the repayment of a loan or contract.

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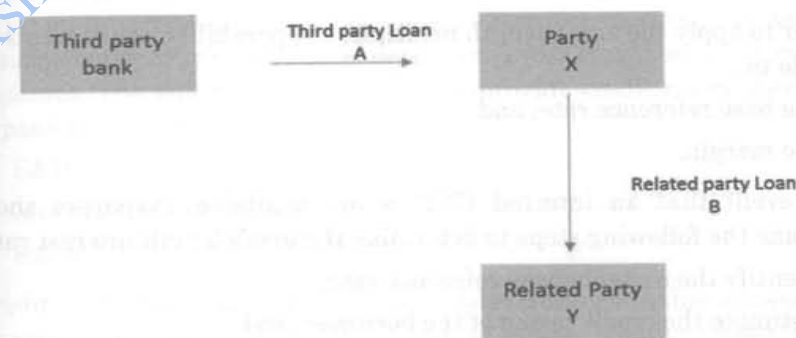
An internal CUP can arise from the following situations:

(a) A Singapore taxpayer borrows funds from both related and third parties. In such a case that interest rate that the Singapore taxpayer pays to the third party bank can provide a reference to the interest rate that the Singapore taxpayer should pay to its related party. Such transactions may exist, although careful consideration of the comparability factors should be undertaken.

(b) A Singapore taxpayer may lend to related parties and to third parties. This is particularly the case if the Singapore taxpayer is in the business of borrowing and lending money (i.e. a bank or a lending institution). The likelihood of a Singapore taxpayer that operates either as a manufacturer or distributor lending funds to a third party is low.

The IRAS notes that an internal CUP may be accepted assuming that all loans are comparable, through a determination of Step 1. An example is detailed below. Additional details may be found in paragraph 13.16 of the 2015 Transfer Pricing Guidelines.

Example 8.1



Assuming that no other loan transactions are entered into either by Party X or by Party Y, the third party loan A may be used as an internal CUP for the related party loan B provided that the facts and circumstances of third party loan A and related party loan B are comparable. Specifically, the credit rating of Party Y and the credit rating of Party X must be similar. In the event that they are not, it would be necessary for Party X to charge a margin over and above the interest rate that it pays to the third party bank when it on-lends the funds to Party Y to proxy compensate Party X for bearing the credit risk of Party Y defaulting on the loan. The margin uplift that Party X charges Party Y should also be sufficient to cover any additional costs that Party X may incur in administering the loan.

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(c) Explicit credit guarantee: a legally binding commitment of a party (the guarantor) to pay an amount to another party (the creditor) in case of a group company (the debtor) defaults its obligations to the creditor.

Most countries may not recognize soft commitments (e.g. comfort letters/letters of intent/agreements, etc) for transfer pricing purposes as a discrete transaction which does not exist.

The pricing of a guarantee will need to consider the following:

(a) The underlying reason for the guarantee should be established.
(b) It should be determined whether the guarantee creates a benefit for which the company receiving the guarantee should pay a fee.

The guarantee fee should be established by taking into account the perspective of both the guaranteed group company and the company that is issuing the guarantee.

An arm's length guarantee fee is in practice typically established in the range between the guarantee fee the guarantor would want to receive to cover the costs it incurs with respect to a guarantee, and the guarantee fee that the guaranteed group company would, at most, be willing to pay based on the benefit conferred by the guarantee.

There is currently no international consensus on how to determine the arm's length nature of internal guarantees and the level of the arm's length guarantee fee.

Although a loan guarantee can be considered as a financial instrument from a taxation perspective, the IRAS treats any form of guarantee as a service. Therefore, in general, withholding tax is applicable if the guarantee fees are borne by a person resident in Singapore or a permanent establishment in Singapore.

8.5 Guidance from the OECD

As we noted earlier, there is limited guidance from the IRAS on how intercompany financing, other than intercompany loans, should be addressed. This is not surprising given that the current version of the OECD Transfer Pricing Guidelines was fully updated in its entirety in 1995, when intercompany financing transactions were minimal.

Para 7.15 of the OECD Transfer Pricing Guidelines notes:

"For example, in respect of financial services such as loans, foreign exchange and hedging, remuneration would generally be built into the spread and it would not be appropriate to expect a further service fee to be charged if such were the case."

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The OECD Transfer Pricing Guidelines refer to financial transactions as a special case where it may be appropriate for a tax authority to disregard a taxpayer's characterisation of a transaction and re-characterise it in accordance with its substance.

The example cited in the OECD Transfer Pricing Guidelines is that of "an investment in an associated enterprise in the form of interest bearing debt when, at arm's length, having regard to the economic circumstances of the borrowing company, the investment would not be expected to be structured in any way. In this case, it might be appropriate for a revenue authority to characterise the investment in accordance with its economic substance with the result that the loan may be treated as a subscription of capital."[4]

More recently, the OECD has released a public discussion draft to outline how interest deductions and other financial payments should be evaluated from a tax and transfer pricing perspective, given that the use of interest (and in particular related party interest) is perhaps one of the most simple of the profit-shifting techniques available in international tax planning. The fluidity and fungibility of money makes it a relatively simple exercise to adjust the mix of debt and equity in a controlled entity. Currently, the public discussion draft still does not provide enough insights on how intercompany financial transactions should be reviewed from a transfer pricing perspective.

8.6 Guidance from other tax authorities

Both the Malaysian and Indonesian tax offices have provided some guidance on intercompany financing.

For example the Malaysian Inland Revenue Board has noted that Malaysian taxpayers are required to substantiate and document that the terms of an intercompany financial assistance, specifically the interest rate applied, are arm's length. Such documentation should include the following:

(a) An analysis of how the interest rate has been determined;
(b) A consideration of the various factors of comparability (e.g. loan structure, etc);
(c) Intercompany agreement that is periodically updated to ensure that all terms and conditions of the loan remain at arm's length. Taxpayers need to ensure that these terms and conditions are structured in a

4 Paragraph 1.65 of the OECD Transfer Pricing Guidelines.

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When applying the CUP method, the following steps should be undertaken:

(a) Understanding the transaction. This step is similar to an understanding of the comparability factors between the related and third party transactions. As mentioned in Chapter 4, the comparability factors that one should consider when reviewing intangible property include the form of the transaction, the type and nature of the intangible property, duration and extent of rights provided by the intangible property, etc.

(b) In the event that internal transactions are not available, one would need to select an appropriate database to obtain information on external transactions. Various commercial databases (e.g. the RoyaltyStat/KtMine) are available for this purpose.

(c) Conduct an objective search for unrelated licences of comparable intangible property and verify that the comparable intangible property transactions were conducted under comparable conditions. Care must be taken to ensure that the base upon which the royalty is computed is consistent with the tested transaction. In the above example, the base upon which the royalty is computed is net sales. If the comparable agreement provide that royalty rates are computed as a percentage of gross sales, then an adjustment has to be made to transform gross sales to net sales.

(d) The various comparability factors have to be taken into account. In the above example, it is noted that the licensing is provided on an exclusive basis. In the event that the comparable transactions are agreements that provide the license on a non-exclusive basis, adjustments may be required.

(e) Construct the arm's length range based on selected transactions and evaluate if the royalty rate in the related party transaction is consistent with the comparable transactions.

9.4.2 Application of the PSM

As mentioned in Chapter 4, the profit split method (PSM) may be used where there is an integrated business model or value chain. The PSM, however, cannot be used to isolate the royalty rate that should be paid by the licensor to the licensee. Rather, this method can only be used where both of the parties to the transaction own and use the intangibles to contribute to the overall value chain.

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9.4.3 Application of the TNMM

Where the CUP and/or the PSM do not produce meaningful results, it is possible to rely on the transactional net margin method (TNMM) to provide support on the arm's length nature of the royalty rate. The TNMM essentially focuses on getting the appropriate set of comparable companies, in terms of functions, assets and risks to the licensee which pays a royalty to a related party.

Once the set of comparable companies has been determined and the appropriate profit level indicator is determined, the licensee's profitability is compared to the profitability of the comparable companies.

The difference in the profitability will be considered the appropriate royalty rate that produces the right level of operating profit.

> *Example 9.2*
>
> Party B uses the trademark provided by SingCo and earns an operating margin of 10%. Comparable companies that distribute similar products earn an operating margin of 5%. The application of the TNMM suggests that the royalty rate should be 5% (i.e. the difference between the operating margin earned by Party B and the operating margin earned by the comparable companies).
>
> In other words, through the application of the TNMM, we may argue that Party B paid too little for the right to use the tradename.

While there are advantages to the TNMM, this approach should be used on a selective basis and usually as a secondary or supporting method. In general, there are many other factors that may affect the operating margin, and imputing the royalty rate based on a comparison of operating margins may not be truly accurate.

The TNMM determines the royalty rate of the intangible on an indirect basis (by evaluating the operating margin and subsequently calculating the royalty rate).

Therefore, this method should be used with caution. The more appropriate method would be to directly evaluate the royalty rate through the CUP method.

9.4.4 Scrutiny on royalty rates

In general, royalties or license fees, that are paid in relation to the right to use certain IP (e.g. trademarks, patents, copyrights and proprietary technology)

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This approach starts off with hypothesizing that the PE is a distinct and separate entity. This is consistent from a transfer pricing perspective as such an approach states that "the profits that are to be attributed to a PE are the profits that the PE would have earned at arm's length, in particular in its dealings with other parts of the enterprise, if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the functions performed, assets used and risks assumed by the enterprise through the PE and through the other parts of the enterprise".[2]

Under this approach, the following two-step process is required:

(1) Determine the activities and conditions of the PE based upon functional and factual analysis, including the attribution of assets, risks and free capital as well as the identification of dealings to be recognised between the PE and the home office.

(2) Determine the profits of the PE based on a comparability analysis and application of transfer pricing methods premised on the allocation of risks, assets and other attributes determined in (1) above.

10.4 Case law on attribution of profits to permanent establishment

A landmark case which brought out the issue of profit attribution to PEs was the case of *Director of Income Tax (International Taxation), Mumbai v Morgan Stanley and Co Inc.; Morgan Stanley & Co Inc. v Director of Income Tax (International Taxation) Mumbai*.[3]

Facts:

The taxpayer was a United States investment bank engaged in the business of providing financial advisory, corporate lending and securities underwriting services. It had an Indian subsidiary which provided back office services exclusively for the taxpayer and the Group. The taxpayer proposed to send staff to the Indian subsidiary to ensure that quality standards are met. The taxpayer also sent staff on deputation to the Indian company to work under the Indian company's supervision and control. The deputed staff continued to be employed/engaged and had their salaries/fees directly paid by the taxpayer.

The Indian company reimbursed the compensation costs of the deputed staff to the taxpayer with no profit element. The taxpayer sought an advance ruling as to whether the Indian company was a PE of the taxpayer in India, and if it was, what was the amount of income attributable to the PE in India.

The advance ruling stated that there was a service PE by reason of the deployment of staff to India but there was no PE by virtue of the provision of back office services for the group. Both the tax authority and the Indian taxpayer appealed to the Supreme Court.

Decision:

To determine whether the taxpayer had a PE in India, the Court undertook a functional and factual analysis of each of the activities undertaken by the establishment in India. Specifically:

a. The performance of back office functions did not constitutes a PE;

b. There was no agency PE in India as the establishment in India did not have any authority to enter into or conclude contracts; and

c. With respect to the deputed employees, given that they remained the employees of the overseas company while rendering services in India for periods ranging from a few months to 2 years, it was stipulated that there was a service PE.

On the issue of whether the profit is attributable to the PE, it was held that the transactional net margin method (TNM) adopted by the taxpayer was the appropriate method of determination of the arm's length price in respect of the transactions between the US taxpayer and its Indian subsidiary. Therefore, the computation of remuneration based on cost plus mark-up was accepted as correct.

On the question of whether there would be any further profits attributable to the PE, it was observed that where a related party (which also constituted a PE) was remunerated on an arm's length basis, taking into account all the risk taking functions of the enterprise, nothing further would be left to be attributable to the PE.

10.5 IRAS' position

The IRAS' position reflects the position of the Indian tax authority. Specifically, the IRAS has noted that no further profits should be attributed to a PE if the following conditions are met:

(a) The taxpayer receives an arm's length remuneration from its foreign related party that is commensurate with the functions performed, assets used and risks assumed by the taxpayer;

2 OECD report on the Attribution of Profits to Permanent Establishments, dated 22 July 2010, para 8 and 13.

3 9 ITLR 1124

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(b) Transactions with related parties subject to a more favourable tax treatment;

(c) Recurring losses or large swings in operating results which may be unusual given the functions and assets of the taxpayer and the risks it assumed;

(d) Operating results that are not in line with businesses in comparable circumstances;

(e) Use of intellectual property, proprietary knowledge or other intangibles in the business;

(f) Transactions involving R&D or marketing activities which could lead to development or enhancement of intangibles; and

(g) Indications (for example, through engagement with tax authorities, country's audit focus, etc.) that the transactions are likely to be subject to transfer pricing audit by tax authorities.

Similar guidance has also been provided by the OECD on transfer pricing risk assessments.[3] While the above factors are discussed, the OECD also alludes to the following factors:

(a) Intragroup service charges;

(b) Royalty, management fees, and insurance premium payments, particularly to entities in low tax jurisdictions;

(c) Marketing or procurement companies located outside market countries or countries where manufacturing takes place;

(d) Excessive debt and/or interest expense;

(e) Cost contribution/cost sharing arrangements;

(f) Business restructuring which is defined as change in the way that a company within a group operates. There are two aspects that needs to be considered with respect to business restructuring. The first is the restructuring transaction itself – i.e. the transfers of assets, including intangibles in connection with business restructuring can give rise to difficult valuation and other transfer pricing issues. The second set of issues involves the ongoing transactions following the transaction which flow from the restructuring.[4]

3 Public consultation: draft handbook on transfer pricing risk assessment *30 April 2013*. This handbook has not yet been finalised as of the time of writing this book.

4 It should be noted that the IRAS has not provided explicit guidance on how business restructurings should evaluated from a transfer pricing perspective. However, the IRAS is actively engaged in OECD forums that discuss business restructuring.

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(g) Comparison of the Singapore taxpayers' results to the overall group's results; and

(h) Fluctuations contrary to market trends.

Once possible companies are selected, cases are ranked according to the risks and generally those with a higher risk score will be selected for an audit. Factors such as financial ratios being out of line compared to those in the same industry, significant change in gross and net margins, may push a taxpayers' risk ranking up the scale. In addition to the selection of taxpayers based on risk assessment, the IRAS also practices some forms of random audit to make it difficult for taxpayers to pinpoint the selection criteria, and therefore avoid an audit.

The IRAS has various sources of information available that it relies on to make a decision as to whether a transfer pricing case exists. Some of the sources of information that are available to the IRAS include:

(a) Informers' allegations

The IRAS receives allegations from many informers who can provide information about companies/individuals who are engaged in tax evasion practices. Such allegations are processed and assessed centrally to determine their validity.[5]

(b) Information from Double Taxation Agreement partners

The IRAS may also receive information from treaty partners which may lead to an investigation/audit. This comes in two main forms:

- the first is information on assets (e.g. immovable property, shares and bank accounts) owned by Singapore citizens or residents, and
- the second is on transactions entered into by Singapore entities that treaty partners find suspicious.

(c) Information from local law enforcement agencies

The IRAS also receives information from other law enforcement agencies and ministerial divisions (e.g. the Economic Development Board of Singapore/Monetary Authority of Singapore, etc.) within Singapore when they believe that the practices adopted by the Singapore taxpayer may not result in the "right" outcome from a Singapore tax perspective.

(d) Declarations which are the taxpayers' obligations

The IRAS receives different types of declarations from many parties. These declarations include individuals and companies filing their

5 Where information provided lead to recovery of tax that would otherwise have been lost, the informer may request for a reward.

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