

Preface

Transfer pricing is a reality for any multinational company. As a result of a globalised economy and complexity in business models, tax authorities globally are actively protecting their revenue base through the introduction of transfer pricing regimes that particularly focus on the taxation of profits that come about due to related party transactions. These transfer pricing regimes typically provide guidance to taxpayers on how related party transactions should be priced and how taxpayers can discharge the burden of proof that their transfer pricing arrangements are consistent with the arm's length standard.

If designed and implemented early in a business life, a transfer pricing system can complement and support an MNC's business model and commercial objectives, as well as optimise its global effective tax rate.

The Inland Revenue Authority of Singapore (IRAS) first introduced the concept of transfer pricing in 2006 with the release of the transfer pricing guidelines. Since then, consistent with developments both regionally and globally, the IRAS has continued to focus on transfer pricing which culminated in the release of the 2nd edition of the Transfer Pricing Guidelines in January 2015. Recent developments at a global level, particularly BEPS as a game changer for international taxation has also contributed to additional focus on transfer pricing both in the region as well as in Singapore.

This book is organised in the following 5 parts:

Part 1 provides an overview to transfer pricing and why it has become such a critical topic in recent years.

Part 2 discusses the preparation of transfer pricing documentation in Singapore.

Part 3 details the key transfer pricing issues arising from intercompany services, intercompany royalties and intercompany financing.

Part 4 details the manner in which companies can deal with tax authorities. Interactions with the tax authorities can take place by way of audits/advance pricing agreements.

Part 5 deals with various global transfer pricing developments and their impact on Singapore.

TABLE OF CONTENTS

About Wolters Kluwer.....	iii
About the Author	v
Preface	vi

PART 1: OVERVIEW

CHAPTER 1 What is Transfer Pricing?	3
1.1 General concept.....	5
1.2 Transactions entered into by multinational corporations	7
1.3 The increasing prominence of transfer pricing	9
1.4 Transfer pricing & tax planning – tax optimisation vs tax avoidance.....	11
CHAPTER 2 Transfer Pricing in Singapore.....	13
2.1 Background to Singapore Transfer Pricing Guidelines	15
2.2 History of transfer pricing in Singapore	16
2.3 Need for transfer pricing in Singapore	18
CHAPTER 3 Arm's Length Principle.....	21
3.1 Definition of arm's length	23
3.2 Legal basis of arm's length	24
3.3 Prevalence of the arm's length principle	25
3.4 Difficulties in the application of arm's length	26
3.4.1 Separate entity vs group synergy	26
3.4.2 Associated enterprise engages in transactions that independent third parties will not undertake	27

3.4.3	Different pricing strategies adopted between related and independent entities.....	27
3.5	Global formulary apportionment.....	28
CHAPTER 4 Application of the Arm's Length Principle.....		31
4.1	The Three-Step Approach.....	33
4.2	Step 1: Comparability factors.....	33
4.2.1	Evaluate transactions on an aggregate or separate basis.....	35
4.2.2	Characteristics of goods, services or intangible properties.....	37
4.2.3	Functional analysis (FAR).....	38
4.2.4	Commercial and economic circumstances.....	42
4.2.4.1	<i>Economic circumstances</i>	42
4.2.4.2	<i>Government policies and regulations</i>	44
4.2.4.3	<i>Business strategies</i>	45
4.2.5	Practical application of the comparability analysis.....	46
4.2.5.1	<i>Characteristics of product, services and intangibles</i>	46
4.2.5.2	<i>Functional analysis</i>	47
4.2.5.3	<i>Commercial and economic circumstances</i>	48
4.3	Step 2: Selection of the appropriate transfer pricing method.....	48
4.3.1	Comparable uncontrolled price method (CUP).....	50
4.3.2	The resale price method (RPM).....	53
4.3.3	Cost plus method (CPM).....	59
4.3.4	Transactional net margin method (TNMM).....	64
4.3.5	Profit split method (PSM).....	68

4.3.5.1	<i>Residual analysis</i>	69
4.3.5.2	<i>Contribution analysis</i>	69
4.3.5.3	<i>Allocation key</i>	70
4.3.6	Other methods.....	73
4.3.7	Selection of transfer pricing method and the tested party.....	74
4.3.7.1	<i>Selection of tested party</i>	74
4.4	Step 3: Determination of an arm's length results.....	76
4.4.1	Selection of internal comparables.....	76
4.4.2	Selection of external comparables.....	77
4.4.3	Multi-year data.....	81
4.4.4	Interquartile range.....	81
4.4.5	Testing the related party transactions.....	82

**PART 2:
TRANSFER PRICING COMPLIANCE**

CHAPTER 5 Singapore's Transfer Pricing Documentation Compliance Requirements.....		85
5.1	Transfer pricing compliance requirements.....	87
5.2	What is a related party?.....	87
5.3	What is a transaction?.....	87
5.4	Contemporaneous documentation.....	88
5.5	Who should prepare transfer pricing documentation?.....	90
5.5.1	Administrative exemptions.....	90
5.6	Why prepare transfer pricing documentation?.....	93
5.7	Compliance matters.....	94

5.8	Transfer pricing risk assessment	94
5.9	Penalties and consequences of non-compliance	95
CHAPTER 6 Preparing Transfer Pricing Documentation.....		97
6.1	Contents of transfer pricing documentation	99
6.2	Group and company overview	99
6.3	Industry analysis	100
6.4	Functional analysis.....	102
6.4.1	Functions performed	103
6.4.2	Assets	104
6.4.2.1	<i>Tangible assets</i>	104
6.4.2.2	<i>Intangible assets</i>	105
6.4.3	Risks.....	105
6.4.4	Preparing the functional analysis	106
6.4.5	Outcome of the functional analysis process	108
6.5	Transfer pricing design and policy.....	108
6.6	Economic analysis.....	110
6.7	Singapore transfer pricing documentation requirements	110
6.8	Revisions to transfer pricing documentation by OECD.....	112
6.8.1	The masterfile	113
6.8.2	The local file.....	113
6.8.3	Country-by-country report	114
6.8.4	Will IRAS adopt the revised transfer pricing documentation guidelines?	114
6.9	Tips for preparing documentation	115
6.10	Common pitfalls associated with transfer pricing documentation.....	116

**PART 3:
KEY TRANSFER PRICING ISSUES ARISING FROM
INTERCOMPANY TRANSACTIONS**

CHAPTER 7 Transfer pricing for intercompany services		121
7.1	Intercompany services	123
7.2	Transfer pricing analysis of intercompany services	123
7.2.1	The “benefits” test.....	124
7.2.2	Determination of arm’s length pricing	127
7.2.2.1	<i>Step 1: Comparability analysis</i>	127
7.2.2.2	<i>Step 2: Selection of a transfer pricing method</i>	128
7.2.2.3	<i>Step 3: Determination of an arm’s length outcome</i>	128
7.3	Treatment of routine support services	133
7.4	Cost pooling arrangements on routine support services	136
7.5	Concluding remarks.....	139
CHAPTER 8 Transfer Pricing for Intercompany Loans and Financing.....		141
8.1	Intercompany loans and financing.....	143
8.2	Transfer pricing of domestic related party loans	144
8.3	Transfer pricing of cross-border related party loans	145
8.3.1	Step 1: Conduct a comparability analysis	145
8.3.2	Step 2: Identifying the most appropriate transfer pricing method	146
8.3.3	Step 3: Determination of the arm’s length results.....	148
8.3.3.1	<i>Identify the suitable base reference rate</i>	148
8.3.3.2	<i>Estimate the credit rating of the borrower</i>	149

8.4	Other intercompany loan structures	150
8.4.1	Cash pooling	150
8.4.2	Guarantees.....	151
8.5	Guidance from the OECD.....	152
8.6	Guidance from other tax authorities	153
8.7	Growth of Singapore as a treasury centre.....	154
CHAPTER 9 Transfer Pricing Involving Intangibles		157
9.1	Transfer pricing of intangibles.....	159
9.2	What is an intangible property?	159
9.3	Ownership of IP	160
9.4	Royalty rate analysis	161
9.4.1	Application of the CUP method	161
9.4.2	Application of the PSM.....	162
9.4.3	Application of the TNMM.....	163
9.4.4	Scrutiny on royalty rates.....	163
9.5	Other tax models involving intellectual property	164
9.5.1	Contract R&D structures	164
9.5.2	Outright sale of IP	165
9.5.2.1	<i>Market-based approach</i>	166
9.5.2.2	<i>Cost-based approach</i>	166
9.5.2.3	<i>Income-based approach</i>	167
9.5.3	Cost share arrangements	167
9.6	Revisions of the OECD Transfer Pricing Guidelines	169
9.6.1	Definition of an intangible	170

9.6.2	Rights to returns for the development and exploitation of intangibles.....	170
9.6.3	Transfer pricing methods.....	171
9.7	Conclusion	172
CHAPTER 10 Permanent Establishment		175
10.1	Introduction to permanent establishments	177
10.2	What is a PE?	177
10.3	Transfer pricing approach to PE.....	177
10.4	Case law on attribution of profits to permanent establishment.....	178
10.5	IRAS position	179
CHAPTER 11 Year-End Adjustments		181
11.1	Undertaking year-end adjustments	183
11.2	Adjustments at the financial year end	185
11.3	Self-initiated retrospective adjustments	186
11.4	Compensating adjustments.....	186
11.5	Corresponding adjustments arising from transfer pricing audit adjustments.....	187
11.6	Concluding remarks.....	188

PART 4:**TRANSFER PRICING AUDITS AND DISPUTE RESOLUTION IN SINGAPORE**

CHAPTER 12 Transfer Pricing Audits in Singapore.....		191
12.1	Corporate tax scrutiny in Singapore.....	193
12.1.1	Tax audit	193
12.1.2	Trigger points for audit and investigation	193

12.2	Transfer pricing audits	194
12.3	Desk audit	194
12.4	Compliance review	195
12.5	Transfer pricing consultation process	196
12.5.1	Selection of taxpayers	197
12.5.2	The process	201
12.5.2.1	<i>Fact finding process</i>	201
12.5.2.2	<i>Review and discussion with taxpayers</i>	203
12.5.2.3	<i>Transfer pricing adjustment if necessary</i>	203
12.6	Preparing for transfer pricing audit	204
12.7	Concluding remarks	205
CHAPTER 13 Negotiating MAPs		219
13.1	Introduction	221
13.2	Who can apply for MAP or APA?	222
13.3	Step 1: Notification of intent	222
13.4	Step 2: Pre-filing meeting	224
13.5	Step 3: Formal application	225
13.6	Step 4: Review and negotiation	226
13.7	Step 5: Implementation	226
13.8	Success of a MAP	228
13.9	IRAS' experience in MAPs	229
13.10	Concluding remarks	230
CHAPTER 14 Negotiating APAs		233
14.1	Introduction	235

14.2	Categorisation of APAs	235
14.2.1	Unilateral APAs	235
14.2.2	Bilateral or multilateral APA	237
14.3	Who can apply for an APA?	238
14.4	Eligibility for an APA	238
14.5	Period under review	238
14.6	Steps involved in negotiating and concluding an APA	239
14.6.1	Pre-filing meeting	239
14.6.2	Formal application	241
14.6.3	Review and negotiation	242
14.6.4	Implementation	243
14.6.5	Renewal	244
14.6.6	Confidentiality	245
14.6.7	Discontinuation of MAPs and APAs	245
14.7	Success factors for an APA	246
14.8	IRAS' experience in APAs	248
14.9	Concluding remarks	249

**PART 5:
GLOBAL AND REGIONAL DEVELOPMENTS ON
TRANSFER PRICING**

CHAPTER 15 UN Transfer Pricing Guidelines for Developing Countries		253
15.1	Introduction	255
15.2	Transfer pricing issues faced by developing countries	256
15.2.1	Lack of reliable comparables	256

15.2.2 Data availability	257
15.2.3 Location specific advantages.....	257
15.2.4 Intangibles	258
15.3 Singapore as a hub	258
15.4 Concluding remarks.....	260
CHAPTER 16 BEPS Initiative.....	261
16.1 Introduction	263
16.2 BEPS Action Plans	264
16.2.1 Transfer pricing in BEPS.....	264
16.3 How will the Action Plans be implemented?.....	268
16.4 Engagement with developing countries.....	269
16.5 How does BEPS affect Singapore.....	270
Conclusion.....	273
Index.....	275

PART 1: OVERVIEW