Rödl & Partner

Managing risks

Singapore
Transfer Pricing Guidelines

Background

Based on the IRAS Transfer Pricing Guidelines [TPG] (5th edition) published on 23 February 2018, companies that transact with related parties are required to prepare and maintain contemporaneous transfer pricing (TP) documentation to substantiate that the related party transactions (RPT) are conducted at arm's length.

Singapore has committed to the global implementation of the Base Erosion and Profit Shifting ("BEPS") Project proposed by the Organisation for Economic Co-operation and Development ("OECD"). The key principle underlying the BEPS Project is that profits should be taxed where the real economic activities generating the profits are performed and where value is created. The TPG published on 23 February 2018 reflects Singapore's adoption of the minimum standards under Action 5 (Countering harmful tax practices) and Actions 8 – 10 (Transfer Pricing) of the BEPS project.

We also stand out through our corporate philosophy and client care, which is based on mutual trust and long-term orientation. We rely on renowned specialists who think in an interdisciplinary manner, since the needs and projects of our clients cannot be separated into individual professional disciplines. Our one-stop-shop concept is based on a balance of expertise across the individual service lines, combining them seamlessly in multidisciplinary teams.

Arm's length principle

IRAS endorses the arm's length principle as the standard to guide transfer pricing. It is an internationally accepted standard adopted for transfer pricing between related parties. The arm's length principle requires a transaction with a related party to be made under comparable conditions and circumstances as a transaction with an independent party. The premise is that where market forces drive the terms and conditions agreed in an independent party transaction, the pricing of the transaction would reflect the true economic value of the contributions made by each party in that transaction.

Therefore, if two related parties derive profits at levels above or below the comparable market level solely because of their special relationship, the profits will be deemed as non-arm's length. In such a case, IRAS can make necessary adjustments to the taxable profits of the Singapore taxpayer. This is to reflect the true price that would otherwise be derived on an arm's length basis.

When companies do not comply with the arm's length principle and have understated their profits through understatement of income or overstatement of tax deductions (or both), IRAS will make transfer pricing adjustment to increase their profits.

Documentation

Contemporaneous documentation means that the documentation includes sufficient information i.e. the transfer price should exist at the time of the transactions, to determine the arm's length pricing. The documentation must be prepared no later than the time of completing and filing of the tax return for the financial year in which the transaction takes place. For example, a company's tax return relating to the financial year 2017 is required to be filed by 30 November 2018 / 15 December 2018 (e-filing).

Thresholds

As the preparation of TP documentation may be costly, companies are not expected to prepare TP documentation if the value or amount of their related party transactions in YA 2018 (i.e. financial year 2017) does not exceed the thresholds shown below:

Category of related party transactions	Threshold (S$) per financial year	Meaning of value of transaction
Purchase of goods by the company from a related party	15 million	Amount paid or payable by the company for the goods
Sale of goods by the company to a related party	15 million	Gross revenue derived by the company from the sale

Category of related party transactions	Threshold (S$) per financial year	Meaning of value of transaction
Loan by the company to a related party	15 million	Principle amount of the loan
Loan to the company by a related party	15 million	Principal amount of the loan
Provision of service to the company by a related party	1 million	Amount paid or payable by the company for the provision, i.e. service fee expenses
Provision of service by the company to a related party	1 million	Gross revenue derived by the company from the provision, i.e. service fee income
Grant of a right to use movable property to the company by a related party	1 million	Amount paid or payable by the company for the grant, i.e. royalty expense
Grant of a right to use movable property by the company to a related party	1 million	Gross revenue derived by the company from the grant, i.e. royalty income
Lease of any property to the company by a related party	1 million	Amount paid or payable by the company for the lease, i.e. rental expenses
Lease of any property by the company to a related party	1 million	Gross revenue derived by the company from the lease, i.e. rental income
Grant of a guarantee to the company by a related party	1 million	Amount paid or payable by the company for the grant, i.e. guarantee expenses

Category of related party transactions	Threshold (S$) per financial year	Meaning of value of transaction
Grant of a guarantee by the company to a related party	1 million	Gross revenue derived by the company from the grant, i.e. guarantee income
Any other transaction	1 million	Amount paid or payable by the company to the related party under the transaction, or gross revenue derived by the company from the related party under the transaction, as the case may be

Example: Financial year 2017:

Cross border transactions	Threshold (S$) per financial year	Whether TP documentation required
Purchase of goods from all related parties	S$14 million	No
Sales of goods to all related parties	S$16 million	Yes
Service incomes from related parties: › Accounting service › Sales and marketing service › Technical support service	 S$100,000 S$300,000 S$700,000	Yes, as the aggregate of all the transactions exceed the threshold of S$1 million.

In addition to the financial thresholds above, there are other non-financial exemption thresholds which can be found in the TPG, amongst others are routine support services and related party loans, highlighted on the next section of this article.

We wish to highlight that while TP documentation is not expected for the transactions below the threshold, companies are still required to keep records to justify that the related party transactions adhere to the arm's length principle. Where the Comptroller is not satisfied that the related party transactions reflect the arm's length principle, he may make the necessary adjustments ("TP adjustments") to the transacted prices accordingly under Section 34D of the Singapore Income Tax Act ("SITA").

If the company has prepared TP documentation, please take note of the following:

a. The TP documentation needs to be updated at least once every three years; and
b. The benchmark used should be updated annually.

Reporting of Related Party Transaction (RPT)

With effect from Year of Assessment 2018, a company with more than S$15 million of RPT (i.e. both local and cross-border RPT) disclosed in the audited financial statements is required to complete the RPT form to be submitted together with the Form C.

For the purpose of determining whether RPT reporting is required, the value of RPT is the aggregate of:

a. All amounts of RPT as reported in the Income Statement but excluding compensation paid to key management personnel and dividends; and
b. Year-end balances of loans and non-trade amounts due to/ from all related parties.

The values of the following categories of RPT are to be reported in the RPT Form:

- Sales and purchases of goods
- Services income and expense
- Royalty and licence fee income and expense
- Interest income and expense
- Other income and expense
- Year-end balances of loans and non-trade amounts

In addition, if the company has any cross-border related party sales or purchases of goods and services, the company is required to list the top 5 foreign related parties that it transacts with (by value of sales or purchases respectively) and provide the details of the RPT including entity names, countries, relationship and amounts transacted.

Related Party Transactions – Routine Support Services Commonly Provided on an Intra-group Basis

As an administrative practice, the Comptroller is prepared to accept a 5% cost mark-up for certain routine support services as a reasonable arm's length charge if these routine support services which the company offers to its related parties are not also provided to an unrelated party.

The list of the prescribed routine support services allowed under the administrative practice are provided in Annex C of the TPG as follows:

Accounting and auditing
Maintaining accounting records, preparing financial statements based on accounting records, reconciling financial data, ensuring authenticity and reliability of accounting records, performing operational and financial internal audits, and performing other services of a similar nature.

Accounts receivable and accounts payable
Collating and verifying data on accounts receivable and accounts payable for the purposes of financial reporting, aging, billing, soliciting payments from customers, payment to vendors, procurement, and other purposes of a similar nature.

Budgeting
Compiling data for the purposes of preparing budget estimates and budget reports.

Computer support
Providing technical assistance services in relation to usage of computer hardware and software, maintenance of IT infrastructure, troubleshooting support, and other services of a similar nature.

Database administration
Performing general maintenance of computer databases including data storage, but excluding analytic services performed on stored data.

Employee benefits and administration
Administrating employee compensation and benefit plans, including healthcare, life insurance, dental, employee incentive compensation and profit sharing, and coordinating with external parties such as hospitals and insurers to implement such benefit plans.

General administration
Performing clerical and administrative functions such as general purchasing, data entry, photocopying or scanning of materials, scheduling appointments, word processing and maintenance of file registries.

Legal services
Provision of general legal services by in-house legal counsel.

Payroll
Compiling and verifying employees' time worked and claims for reimbursable expenses to compute the salaries, commissions and reimbursements due to employees, preparing pay cheques, and arranging the crediting of such payments into employees' bank accounts.

Corporate communications
Handling internal and external communications relating to corporate policies.

Staffing and recruiting
Managing staffing requirements, performance issues and staff welfare, and implementing recruitment plans such as advertising open positions, and screening of candidates.

Tax
Preparing tax returns and computations and reclaim forms, preparing responses to queries and submitting them to tax authorities, and processing tax payments.

Training and employee development
Managing and implementing training and development programmes for employees.

Related Party Loans

To facilitate compliance for related party loans not exceeding S$15 million each, IRAS has introduced an indicative margin which companies can apply on each related party loan. The indicative margin will be published on the IRAS' website and will be updated at the beginning of every year. For instance, for related party loans not exceeding S$15 million obtained or provided during the period from 1 January 2018 to 31 December 2018, the indicative margin is +175 bps (i.e. 1.75%) per annum.

The indicative margin is an alternative to performing a detailed transfer pricing analysis on the related party loans and it is not mandatory. If the company chooses to apply the indicative margin for its related party loan, the company will not be required to prepare TP documentation for the said loan and the loan amount will also be excluded when determining the threshold of S$15 million for all related party loans.

If the company wishes to use a margin that is different from the indicative margin, the company is required to substantiate that the margin used reflects the arm's length principle.

Consequences of Non-compliance

For companies which are required to prepare contemporaneous TP documentation and failed to comply, the companies may face the following consequences:-

a. Companies may be penalised for not complying with record keeping requirements under the SITA if they are unable to provide TP documentation upon request;

b. Companies that do not maintain contemporaneous documents may face higher risk of TP adjustments under Section 34D of the SITA (as mentioned above);

c. Companies will be denied any year-end pricing adjustments made to the financial accounts if no supporting documentation is available at the time of making such adjustments. For instance, for pricing adjustments that result in a lower taxable income for the companies, the reduction in income will be denied a tax deduction for tax purposes. However, for pricing adjustments that result in a higher taxable income for the companies, the upward adjustment will be brought to tax.

Updates of TP Documentation

In the Income Tax (Amendment) Act 2017 enacted on 26 October 2017, the following legislative changes to the TP documentation requirements and penalties for non-compliance that will take effect from YA 2019:-

a. To ease the compliance burden for smaller companies, companies are exempt from preparation of TP documentation if:-
   - Gross revenue derived from their trade or business is not more than S$10 million for that basis period and the two immediate preceding basis period (even if the quantum thresholds are exceeded); or
   - The total value of the related party transaction does not exceed the threshold quantum mentioned above.

b. The TP documentation must be prepared no later than the filing deadline of the tax return and the companies must submit the TP documentation to the IRAS within 30 days of request.

c. The companies must maintain the TP documentation for a minimum period of 5 years from the end of the basis period in which the transaction took place.

d. Statutory fine up to S$10,000 may be imposed for each non-compliance offence.

e. There will be a 5% surcharge on the TP adjustments made under Section 34D of the SITA. Any additional income arising out of the TP adjustments are also treated as accruing in or derived from Singapore or received in Singapore from outside Singapore and will be taxable in the hands of the companies.

Country-By-Country Reporting ("CbCR")

CbCR is a form of reporting by multinational enterprises (MNEs) initiated by the OECD in the BEPS Action 13 Report. In keeping with Singapore's commitment to implement certain measures under the BEPS Project, Singapore-headquartered MNEs meeting certain conditions are required to prepare and file CbC Reports to IRAS for financial years (FYs) beginning on or after 1 Jan 2017.

Broadly, CbCR is required for an MNE group in relation to a financial year (the first such year being FY 2017), where:

a. The MNE group is a Singapore MNE group;
b. The consolidated group revenue in the preceding financial year is at least S$1,125 million; and
c. The MNE group has subsidiaries or operations in at least one foreign jurisdiction.

If a Singapore MNE group is required to file a CbC Report for a financial year, its ultimate parent entity, which is its Reporting Entity for the purpose of CbCR, will be required to submit a CbC Report to IRAS within 12 months from the end of that financial year. Submission of CbC Reports to IRAS must be done electronically in accordance with the format specified by IRAS.

Recommendation

In view of the above, we strongly recommend the company to review its related party transactions as well as to ensure that the current TP documentation is sufficient and contemporaneous to support the intercompany transactions, where necessary. Going forward, please also be aware and mindful of any intercompany transactions (both domestic and cross-border) as there may be more stringent measures for TP compliance in future.

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