

TRANSFER PRICING BRIEF

August 2021

CONTENTS

**CHINA:
STATE ADMINISTRATION
OF TAXATION
ANNOUNCEMENT NO. 24
OF 2021**
Page 2

**INDONESIA:
THE PROMISING
DEVELOPMENT OF APAs
AND MAPs**
Page 6

**SINGAPORE:
TRANSFER PRICING
UPDATES RELEVANT TO
YA 2021**
Page 10

**HONG KONG:
TRANSFER PRICING
UPDATE**
Page 15

INTRODUCTION

Welcome! Thank you for picking up our first Transfer Pricing brief from Moore Asia Pacific!

While the world has been witnessing COVID-19 roaring across the globe since early 2020 and a Delta variant hitting us even stronger in the second half of 2021, in the professional world, the tax experts from Moore Asia Pacific have been reaching out to each other and building a better tax community for this part of the world.

Among this group of people as well as the Moore Asia Pacific Tax Committee, the sub-committee of Transfer Pricing ("TP") is one of the pioneers trying to do even more than they were doing before the pandemic.

This first Moore Asia Pacific TP brief will provide you with the combined knowledge and intelligence from all the countries and jurisdictions in the region including India, Nepal, Bangladesh in the west, across to Greater China, Japan, Mongolia, ASEAN countries, and Australia and New Zealand in the east.

You will also hear from some of the Moore Global voices including Anthony Hayley, APAC Leader of TP, and his fellow global leaders across various service lines and industry sectors.

Together with our global colleagues having expertises from the other regions outside Asia Pacific, Moore Asia Pacific TP team hopes to bring you an informative and professionally-valuable peice of reading, to help you to get on top of the most recent developments and related news across Asia Pacific and the world.

At the same time, as one of the most possible tax areas for collaboration cross-border, we are more than happy to explore any TP client opportunity together with you.

We will share with you some of the insights from mainland China, Hong Kong, Indonesia and Singapore. You will also find our TP experts' contact details at the end of the Bulletin. We are more than happy to hear from you and to read your comments or ideas.

Last but not least, before we fully get out of the pandemic and can literally see and work with each other, we will keep virtual and innovative ways to work with you on any opportunity. Stay healthy, stay safe and stay in touch!

Best regards,

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STATE ADMINISTRATION OF TAXATION ANNOUNCEMENT NO. 24 OF 2021

Announcement of the State Administration of Taxation on Matters Relating to the Application of Summary Procedures to Unilateral Appointment Pricing Arrangements State Administration of Taxation Announcement No. 24 of 2021

The full text effective

Announcement of the State Administration of Taxation on Matters Relating to the Application of Summary Procedures to Unilateral Appointment Pricing Arrangements State Administration of Taxation Announcement No. 24 of 2021

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In order to implement the Opinions on Further Deepening the Reform of Tax Collection and Administration issued by the Central Office and the State Office, deepen the reform of “management and administration” in the field of taxation, optimize the business environment, promote the cooperation between taxation and enterprises, improve the level of personalized services and tax certainty for cross-border investors, in accordance with the Enterprise Income Tax Law of the People’s Republic of China and its implementing regulations In accordance with the Enterprise Income Tax Law of the People’s Republic of China and its implementing regulations, the relevant provisions of the Tax Levy and Administration Law of the People’s Republic of China and its implementing rules, the following is the announcement on matters relating to the application of simplified procedures for unilateral appointment pricing arrangements.

1. Enterprises applying for unilateral appointment pricing arrangements in accordance with the relevant provisions of the Notice of the State Administration of Taxation on Matters Relating to the Improvement of the Administration of Appointment Pricing Arrangements (No. 64 of 2016, hereinafter referred to as Notice 64) may apply the simplified procedures if they meet the requirements of this Notice.

2. The simplified procedure includes 3 stages of application and assessment, negotiation and signing and monitoring and execution.

3. An enterprise may apply for the application of the simplified procedure if the connected transactions occurring in each of the three years preceding the tax year to which the competent tax authority serves the Notice of Acceptance of Application for Tax Matters are of an amount of RMB 40 million or more and if one of the following conditions is met

(i) Contemporaneous information for the three tax years prior to the year in which the application is to be submitted has been provided to the competent tax authorities and complies with the provisions of the Announcement of the State Administration of Taxation on Matters Relating to the Improvement of the Management of Linked Declarations and Contemporaneous Information (No. 42 of 2016).

(ii) In the 10 years preceding the tax year to which the enterprise submits the application, the appointment pricing arrangement has been implemented and the results of the implementation meet the requirements of the arrangement.

(iii) Within 10 years prior to the tax year to which the date of submission of the application by the enterprise belongs, it has been subject to special tax investigation adjustment by the tax authorities and the case has been closed.



4. The enterprise shall submit an application for applying the simplified procedure to the competent tax authority, which will decide whether to accept the application after analysis and assessment.

(a) If an enterprise intends to apply, it shall submit to the competent tax authority the Application for Simplified Procedures for Unilateral Appointment Pricing Arrangement (Annex), together with an application report. The application report includes the following contents:

1. the related parties and related transactions involved in the unilateral appointment pricing arrangement.
2. the applicable year of the unilateral appointment pricing arrangement
3. whether the unilateral reservation pricing arrangement applies retrospectively to previous years.
4. the organisational structure and management structure of the enterprise and the enterprise group to which it belongs
5. the production and operation of the enterprise for the last three to five tax years, financial and accounting reports, audit reports and information on the same period;
6. a description of the functions and risks of each related party involved in the unilateral appointment pricing arrangement, including the institutions, personnel, expenses and assets on which the division of functions and risks is based
7. the pricing principles and calculation methodology used for the unilateral reservation pricing arrangement, as well as the functional risk analysis, comparability analysis and assumptions that support the pricing principles and calculation methodology
8. value chain or supply chain analysis, and consideration of geographically specific advantages such as cost savings and market premiums
9. a description of market conditions, including industry trends and the competitive environment
10. the annual scale of operations, forecasts of operating efficiency and business plans for the period to which the unilateral reservation pricing arrangement applies
11. relevant laws and regulations of domestic and foreign industries that have an impact on the unilateral appointment pricing arrangement
12. relevant circumstances consistent with Article 3 of this announcement.
13. any other circumstances that need to be explained.

(2) The competent taxation authority shall not accept the application submitted by the enterprise if any of the following circumstances apply.

1. the taxation authority has already implemented a special tax adjustment case investigation or other tax-related case investigation on the enterprise and the case has not yet been concluded
2. the annual report form on connected business transactions has not been completed in accordance with the relevant provisions and is not corrected on time
3. failing to prepare, maintain and provide contemporaneous information in accordance with the relevant provisions
4. fails to provide relevant information in accordance with the requirements of this announcement or the information provided does not meet the requirements of the tax authorities and does not make corrections or corrections on time
5. refusing to cooperate with the tax authorities in conducting functional and risk field interviews.

(3) Upon receipt of an enterprise's application, the competent taxation authority shall carry out analysis and assessment, conduct functional and risk field interviews, and serve a Notice of Tax Matters to the enterprise within 90 days from the date of receipt of the enterprise's application, informing it of its acceptance or otherwise; if it is not accepted, stating the reasons.

5. After accepting the application of an enterprise, the competent tax authority shall negotiate with the enterprise on whether its connected transaction is in compliance with the principle of independent transaction and complete the negotiation within six months from the date of serving the Notice of Tax Matters to the enterprise on the acceptance of the application. During the consultation period, the competent tax authority may request the enterprise to submit additional relevant information, and the time for the enterprise to submit additional information shall not be counted as part of the above-mentioned six-month period.

(i) If the competent tax authority and the enterprise reach a consensus, it shall draw up the text of the unilateral appointment pricing arrangement. The legal representative of both parties or the authorized representative of the legal representative shall sign the unilateral appointment pricing arrangement.

(b) If the competent tax authority cannot reach a consensus with the enterprise, it shall serve the enterprise with a Notice of Tax Matters terminating the simplified procedure. The enterprise may re-apply for the unilateral appointment pricing arrangement in accordance with the provisions of Circular 64. Information that has already been submitted need not be submitted again.

6. The tax authorities shall monitor the implementation of the unilateral appointment pricing arrangement in accordance with the requirements of Circular 64.

If, during the implementation of the unilateral appointment pricing arrangement, substantial changes affecting the unilateral appointment pricing arrangement occur, resulting in the termination of the implementation, the enterprise may re-apply for the unilateral appointment pricing arrangement in accordance with the provisions of this Notice.

7. The unilateral appointment pricing arrangement is applicable to connected transactions for three to five years from the tax year in which the competent tax authority serves the Notice of Acceptance of Application on the enterprise.

For unilateral appointment pricing arrangements involving two or more tax authorities of provinces, autonomous regions, municipalities directly under the Central Government and municipalities separately listed in the plan, the simplified procedures shall not apply for the time being.

Other unilateral appointment pricing arrangements not specifically provided for in this Notice shall be implemented in accordance with the provisions of Notice 64.

10. This Notice shall come into effect on 1 September 2021.

This Notice is hereby made.

Annex: Application for Simplified Procedures for Unilateral Appointment Pricing Arrangements

Translated with www.DeepL.com/Translator (free version). Nickel West suite of assets.

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INDONESIA

THE PROMISING DEVELOPMENT OF APAs AND MAPs

Indonesia has strengthened its tax disputes framework by adapting a more sophisticated procedure when handling advance pricing agreements (APAs) and mutual agreement procedures (MAPs). Charles Setia Oetomo and Felic Setiawan of GNV Consulting Services examine how the developments are an attractive premise for businesses in the region.



As transfer pricing (TP) controversies become increasingly common and more important for multinational companies, the emergence of the advance pricing agreement (APA) and the mutual agreement procedure (MAP) in recent years as possible dispute resolution mechanisms are seen as beacons of hope for taxpayers. This article explores the regulatory background, progress, challenges and the anticipated future of APAs and MAPs in Indonesia.

BUILDING NEW PLATFORMS

The Indonesian transfer pricing landscape has developed over the past couple of years. The introduction of regulatory frameworks, as well as the ever-growing number of TP cases, has seen the Directorate General of Taxes (DGT) substantially grow to wage a campaign against the base erosion and profit shifting (BEPS) practices of multinational companies.

Fueled by the developing regulatory frameworks and the continuously increasing annual tax revenue target of the DGT, multinationals are regularly facing TP disputes and related issues regarding double taxation.

Despite the availability of existing domestic dispute resolution mechanisms, the uncertainty surrounding recent tax court decisions on transfer pricing issues, along with strong progress in the number of resolved APA and MAP cases, have shed light on bilateral negotiations and have boosted the confidence of taxpayers.

REGULATORY DEVELOPMENT

In 2010, the introduction of DGT Regulation No. 48/PJ/2010 on guidelines for the implementation of MAPs based on the agreements to avoid double taxation, and DGT Regulation No. 69/PJ/2010 on APAs, initially kick-started the development of alternative models of dispute resolution in Indonesia.

Since then, the Ministry of Finance (MoF) and the DGT have issued a number of related regulations. Most notably in recent years, a number of regulations relating to transfer pricing have been introduced to align domestic rules with the OECD/G20 BPS Action Plan.

While most of these regulations are game changers, the most important is MoF Regulation No. 7/PMK.03/2015 (PMK-7)¹ on guidelines for the establishment and implementation of the APA, which became effective on April 11 2015. Likewise, another key development was MoF Regulation No. 49/PMK.03/2019 (PMK-49) on the guidelines to implement the MAP, which came into effect on April 26 2019.

The aforementioned regulations outlined the specific procedures and steps that taxpayers need to follow when applying for an APA and/or a MAP. Most importantly, both regulations introduced a time limit within which the Indonesian tax authorities will need to carry out and complete the APA and/or MAP.

CASE PROGRESS

While no notable progress has been observed in the initial years of their introduction, the submission of APA and MAP applications have been picking up pace since 2016, following the release of the final reports on the 15-point action plan to address BEPS by the OECD/G20.

The growth has also increased because of Indonesia's active participation as a member of the OECD/G20 Inclusive Framework (IF) on BEPS. This is particularly in line with Action 14 of the BEPS Action Plan, which reflects a commitment by countries to make dispute resolution mechanisms more effective by implementing a minimum standard on dispute resolution (comprising of specific measures to remove obstacles) and an effective and efficient mutual agreement procedure. The plan also calls for the establishment of a monitoring mechanism to ensure that such commitments are being effectively satisfied.

In 2016, the DGT also began internal restructuring to cope with the demands of international tax. The organisation sought to increase its capacity and capability in handling international tax cases, particularly MAP and APA cases.

The DGT consequently formed the Directorate of International Taxation by transforming what was formerly the Sub-Directorate of Tax Treaty and International Tax Cooperation to oversee three other sub-directorates, namely:

- Sub-Directorate of Tax Treaty and International Tax Cooperation
- Sub-Directorate of International Tax Dispute Prevention and Settlement
- Sub-Directorate of International Tax Information Exchange.

The Directorate of International Taxation was appointed as the competent authority (CA) which negotiates the APAs and MAPs.

The DGT has also been highly proactive in handling applications while maintaining transparency over the number of APA and MAP requests being made and closed over time.

The 24-month timeline for MAP (and effectively also for APA) negotiations, as prescribed within PMK-49, has also sped up the process. However, the implementation of such a timeline is not as strict when it comes to the applications submitted before the regulation came into effect. Both APAs and MAPs, when they relate to the same taxpayers, may also be negotiated simultaneously.

Based on the APA and MAP statistics published by the DGT on its website, the number of cases being closed from year-to-year are as follows:

Year	Number of cases closed		Total
	MAP	APA	
Prior to 2016	1	0	1
2016	32	3	35
2017	20	3	23
2018	17	15	32

The same source indicates that the average time needed to close MAP cases, relating to transfer pricing, is as follows:

Average time needed to close MAP cases relating to transfer pricing in 2016	
Cases started before 1 January 2016	39.98 months
Cases started as of 1 January 2016	N/A

Average time needed to close MAP cases relating to transfer pricing in 2017	
Cases started before 1 January 2016	42.21 months
Cases started as of 1 January 2016	29.67 months



The data published shows a notable number of MAP and APA cases being closed from the beginning of 2016.

Similarly, the average time needed to close MAP cases (relating to transfer pricing) are evidently shorter now than when compared to the average time needed to close MAP cases (relating to transfer pricing), which had started prior to January 2016. These statistics seem to imply that the progress of MAP and APA cases have seen significant improvements, as the number of cases being closed increases and the time required to complete an MAP decreases.

The closed cases may not necessarily result in favourable outcomes for taxpayers, as the majority of MAP cases being closed in 2016 eventually resulted in the Indonesian and partner country tax authorities agreeing to enforce decisions issued by the tax court. Closed MAP cases in 2017 represented an outcome with varying degrees of success, where a good number of closed cases resulted in the full or partial elimination of double taxation.

So far, the implementation of APAs and MAPs, which have been concluded, are observed to follow the steps prescribed within the prevailing regulations, portraying it as being quite clear. Nonetheless, where an APA has been concluded, taxpayers are expected to submit an annual compliance report within four months after the end of the fiscal year. APA renewals are also observed to take a shorter time to conclude when compared to new APA applications.

Where a MAP has been concluded to grant tax relief to taxpayers, it will be enacted domestically (through the amendment of corporate income tax returns, tax assessment letters, amendment of tax assessment letters, objection decision letters, amendment of objection decision letters, etc.).

While the request for a tax refund will generally follow the normal procedures, an examination process (in line with Ministry of Finance Regulation No. 187/PMK.03/2015 on the guidelines for the refund of taxes that should not have been paid or PMK-187) will be carried out when the MAP is enacted through an amendment of a tax assessment letter. However, such an examination process is not expected to be as exhaustive as a tax audit.

CHALLENGES

Despite the clarity of the regulations, as well as the cooperativeness of the DGT, APAs and MAPs are not without their own challenges.

Some of the challenges that taxpayers will have to note before deciding on whether to pursue an APA or MAP are:

- While taxpayers may be able to exert a certain amount of control when it comes to a unilateral APA process and/or domestic remedy, bilaterally negotiated APAs and MAPs can keep taxpayers' involvement to a minimum.
- There is always a likelihood or possibility that any bilaterally negotiated APA or MAP results in a disagreement between tax authorities.
- A MAP may be concluded in disagreement when a tax court decision has been issued. This gives rise to the general concern that MAP negotiations may not progress as quickly when taxpayers also pursue a domestic remedy. As such, in most cases, taxpayers pursuing a MAP will decide against pursuing any domestic remedy, or alternatively, pursue such a domestic remedy but have to deal with the risks of the MAP not being concluded until the issuance of the tax court decision.
- The profit split method (if not, other transfer pricing methods that provides entrepreneurial return for Indonesian taxpayers) is still the most preferred TP method for the Indonesian tax authorities in APA and MAP negotiations.

EXPECTED FUTURE UPDATES

New regulations on APAs are expected to be issued in 2020. Plans are in place to enable an APA to be applied as a rollback on prior open years. The proposed APA regulations may, however, eliminate the firewall that has so far prevented information submitted for the purpose of APA applications from being used during tax audits, preliminary investigations or the investigation of a tax crime.

The recent issuance of Presidential Regulation No. 77 (2019) has ratified the Multilateral instrument (MLI) on November 12 2019. The MLI is a multilateral convention that implements changes agreed under the BEPS project. Article 17 of the MLI, regarding corresponding adjustments, has also enabled tax authorities of partner countries to provide corresponding adjustments relating to transfer pricing on a unilateral basis and ensure that access to a MAP for TP cases are provided by partner countries even when the relevant tax treaty does not contain Article 9(2) of OECD Model Tax Convention. Similar changes are also found in Article 16 of the MLI concerning MAPs, notably on the applicable time limits for a MAP application and implementation, notwithstanding any time limits under the domestic law of the contracting jurisdictions.

Indonesia will adopt these articles whenever applicable. This MLI will become effective once submitted to the OECD (as the Depository of the MLI) before it becomes effective. Based on publicly available information, the deposit of the notice of ratification will be made in early 2020 and is expected to take effect for Indonesian tax purposes on 1 January 2021.

KEY TAKEAWAYS

Some of these observations seem to imply that the DGT are treating both APAs and MAPs seriously, reflecting the spirit based on which the regulations were drafted and enacted. This, thereby, brings down the myths that these efforts are merely gimmicks where realisations and tangible progress was unlikely. Despite the progress made so far, taxpayers will need to take note of the potential issues that may arise when applying for APAs and MAPs. Understanding the timing and potential changes brought about by the upcoming regulations are just as crucial.

Like the available domestic remedy, APAs and MAPs may not necessarily address double taxation and still provide uncertainty in terms of outcome. Strategic considerations and cost-benefit analysis are still required in deciding if APAs and MAPs provide taxpayers with greater chances of obtaining the required tax relief. For better or worse, with careful planning and due care, there is no denying that APAs and MAPs may just be an appropriate dispute mechanism for taxpayers.

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SINGAPORE

TRANSFER PRICING UPDATES



1. Introduction to Transfer Pricing (“TP”) compliance

The IRAS explicitly endorses the arm’s length principle as the standard to guide all transactions with related parties in the Singapore TP Guidelines issued from time to time. The arm’s length principle requires RPTs be conducted under conditions and circumstances comparable with transactions with unrelated parties.

The TP Guidelines also explained that taxpayers should exert reasonable efforts to ensure that RPTs have been conducted at arm’s length. A taxpayer is considered to have exerted reasonable efforts when he has undertaken a sound transfer pricing analysis (such as benchmarking the related party transactions to market prices/ returns) and has documented the process adequately.

2. Contemporaneous Transfer Pricing (“TP”) Documentation requirements

Unless specifically exempted, taxpayers are required to prepare and maintain contemporaneous TP Documentation to support the pricing of the RPT and to substantiate that their RPT are undertaken as per arm’s length principle.

The necessary TP Documentation for FY 2020 should be prepared and in place, at the time the YA 2021 tax return is submitted i.e. latest by 30 November 2021 in order to be considered contemporaneously prepared.

With effect from YA 2019, a failure to comply with contemporaneous TP Documentation may result in:

- Upon conviction, a fine not exceeding S\$10,000;
- Potential additional taxes from the TP adjustments made by the IRAS; and
- a 5% surcharge on the TP adjustments regardless of whether they result in any additional tax to the Company or a reduction of losses to be carried forward.

Information to be detailed in TP Documentation, inter-alia, includes – note that list below is non-exhaustive):

- group level and entity level information
- details of RPT
- analysis of functions performed, risks undertaken, and assets used by each party
- rationale for the chosen transfer pricing method and tested party; and
- approach and details on comparability analysis.

3. Administrative concession by the IRAS as set out in Rule 4 of the TP Documentation Rules

Taxpayers are not expected to prepare TP Documentation in any of the following scenarios, as prescribed in the TP Guidelines:

- Where a company transacts with a related party in Singapore and such local transactions (excluding related party loans) are subject to the same Singapore tax rates for both parties.
- Where a related domestic loan is provided between a company and a related party in Singapore and the lender is not in the business of borrowing and lending money.
- Where a company applies the 5% cost plus mark-up for the IRAS’ prescribed list of routine support services or under the OECD’s simplified approach for low value-adding intra-group services in relation to the RPT concerned, subject to meeting the relevant conditions.
- Where a company applies the indicative margin (note that the indicative margin will be +200 bps and +275bps for loans not exceeding S\$15million obtained or provided during the year 2020 and 2021 respectively) for related party loans, subject to meeting the relevant conditions.
- Where the RPT are covered by an Advance Pricing Arrangement (“APA”). However, an annual compliance report is still required.
- Where the value or amount of the RPT disclosed in the current year’s financial accounts does not exceed the threshold as shown in TABLE 1 on the following page.

4. Mandatory TP Documentation requirements from the YA 2019

The TP Guidelines provide guidance on TP Documentation pursuant to Section 34F of the Singapore Income Tax Act (“SITA”) and the Income Tax (Transfer Pricing Documentation) Rules 2018, which takes effect from YA 2019.

A summary of TP Documentation requirements under Section 34F of the SITA as follows on TABLE 2 following.

TABLE 1

Category of related party transactions*	Threshold (S\$) per FY
Purchase of goods from all related parties	15 millions
Sale of goods to all related parties	15 million
Loans owed to all related parties	15 million
Loans owed by all related parties	15 million
All other categories of RPT. EG: service income/payment, royalty income/expense, rental income/expense, guarantee income/expense	1 million per category of transactions

* For the purpose of determining if the threshold is exceeded (a) aggregation should be done for each category of RPT e.g. all service income received from related parties is to be aggregated and (b) strict pass-through costs should be included.

TABLE 2

Scope	TP Documentation requirement
When it takes effect	From YA 2019
Who must prepare	Unless the transactions fall within administrative concession, taxpayers should prepare TP Documentation for their related party transactions undertaken in a basis period when either of these two conditions is met: <ul style="list-style-type: none"> • Gross revenue derived from their trade or business is more than S\$10 million for that basis period; or • TP Documentation is required to be prepared for the previous basis period. In other words, taxpayers who were required to prepare TP Documentation for a previous basis period, would continue to be required to do so for the subsequent basis period. Gross revenue excludes passive source income (example, dividend income) and capital gains or losses.
When to prepare	Not later than the statutory filing due date of the income tax return
Penalty for non-compliance	Up to S \$10,000
Surcharge	5% on the amount of TP adjustments (whether or not the TP adjustments are taxable) Full or partial remission of surcharge is possible subject to certain conditions
When to submit	Within 30 days from a request by the IRAS to submit the TP documentation
Taxpayers exempt from preparing TP documentation	Exemption from preparing TP Documentation applies where: <ul style="list-style-type: none"> • Gross revenue for the current basis period and two preceding basis periods is not more than S\$10 million even if the taxpayer was required to prepare TP documentation for the two preceding basis periods; or • Exemption for specified transactions set out in Rule 4 of the TP Documentation Rules as above.
How long to retain TP documentation	A period of at least five years from the end of the basis period in which the transaction took place

5. Reporting of Related Party Transactions (“RPT”) in income tax returns

Companies are required to complete the Form for Reporting of Related Party Transactions (“RPT Form”) and submit it together with the Form C, if the total value of RPT as disclosed in the financial statements exceeds S\$15 million. Note that the RPT Form is not required to be completed if the company files the Form C-S or Form C-S (lite).

The value of RPT is determined as the aggregate of:

- a) All RPT amounts 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 details required to be disclosed in the RPT Form, inter-alia, include:

- a) Type and amounts of RPTs (based on the financial data at company level and not the consolidated financial data);
- b) Names, locations, and relationships of the top 5 foreign transacting parties (for sales/purchases of goods and service fee income/ expense); and
- c) Loans and non-trade amounts due to or from related parties.

RPT Form is part of the Form C. Penalty may be imposed for non-filing or incorrect filing of Form C.

6. Identifying potential TP exposure

Examples of circumstances in which transfer pricing risks may be considered high are:

- a) Significant variations in the quantum of the related party transactions as compared to prior years
- b) Recording net losses where Singapore company is only providing services to the related parties
- c) Transactions with related parties in tax havens/ low marginal tax rates (transactions can be in the nature of payment for intra-group services, royalties etc.)
- d) Companies with significant related party transactions, and making accounting losses for more than two years, or recording marginal accounting profits or fluctuations in the gross / net margins without commercial rationale to explain such fluctuations
- e) Large payment of management charges not passing the ‘benefit test’
- f) Centralised HQ functions with no or minimal charge-outs
- g) Borrowing of an interest-bearing loan and advancing as interest-free loan to a related party
- h) Huge variation in tax payable between ECI filing stage vs final tax payable in tax return filed, due to year-end adjustments in the related party transaction
- i) TP Documentation prepared is outdated (i.e. more than three years) or was from an overseas country perspective, not covering Singapore TP requirements
- j) CITQ, regardless of the extensiveness or depth, on the company’s related party transactions
- k) Exploring impact arising from a company’s related party transactions due to COVID-19.

7. Conclusion

Taxpayers who do not meet the thresholds for TP documentation requirements should nonetheless consider preparing adequate TP analysis (TP policy, benchmarking analysis, intercompany agreements, etc.) to defend the arm’s length nature of their related party transactions. This is to help mitigate the risk of a surcharge resulting from TP adjustments which may be initiated by the Comptroller.

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HONG KONG

TRANSFER PRICING UPDATE

The Hong Kong Government has enacted Inland Revenue (Amendment) (No. 6) Ordinance 2018 (“Amendment Ordinance”) in July 2018 to allow the Inland Revenue Department (“IRD”) to make appropriate transfer pricing adjustment(s) on companies’ tax computations if they consider the companies’ transaction(s) with their associated person(s) was/were not conducted on an arm’s length basis and confer a potential Hong Kong tax.

The Amendment Ordinance is the first official transfer pricing legislations in Hong Kong.

Domestic transactions between two Hong Kong associated persons that do not give rise to an actual tax difference and do not have a tax avoidance purpose (provided that certain prescribed conditions are met) are generally exempt from transfer pricing adjustments.

The transfer pricing legislations in Hong Kong are largely followed the Organization for Economic Co-operation and Development (“OECD”) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. The Amendment Ordinance adopts the OECD’s recommended three-tiered documentation structure, comprising a Master File, Local File and the CbC Reports.

EXEMPTION THRESHOLD

A Hong Kong entity is required to prepare master file and local file for the period commencing on or after 1 April 2018 unless it is exempt by business size or by volume of the related transactions.

A Hong Kong entity which satisfies any two of the conditions below will not be required to prepare a master file and a local file for an accounting period:

- the total amount of the entity’s revenue for the relevant accounting period does not exceed HK\$400 million
- the total value of the entity’s assets at the end of the relevant accounting period does not exceed HK\$300 million, and
- the average number of the entity’s employees during the relevant accounting period does not exceed 100.

In addition to these business-size thresholds, related party transactions can be excluded from the local file if they do not exceed the following amounts:

- Transfers of properties (moveable or immovable, but excluding financial assets and intangibles): HK\$220 million
- Transactions in respect of financial assets or transfer of intangibles: HK\$110 million
- Other transactions: HK\$44 million

Timeline and penalty

Master file and local file must be prepared no later than 9 months after the end of its accounting period and they should be retained for a period of not less than 7 years after the end of the accounting period of the entity.

Taxpayers who fail to prepare master file and local file documentation without reasonable excuse are liable to penalty of up to HK\$50,000 and may be ordered by the court to prepare such documentation within a specified time. Failure to comply with that order would trigger penalty of up to HK\$100,000 on conviction.



COUNTRY-BY-COUNTRY REPORTING (“CbCR”) GENERAL REQUIREMENTS

A multinational enterprise group (“MNE Group”) is required to file a CbCR in relation to an accounting period where:

- the consolidated group revenue for the preceding accounting period is at least EUR750 million (or HK\$6.8 billion), and
- the group has constituent entities or operations in two or more jurisdictions.

The HK Entity is not required to file a CbCR if:

- a CbCR for the relevant accounting period is filed by another Hong Kong Entity of the Reportable Group, or
- Surrogate Parent Entity (“SPE”) -filing-in-elsewhere exception applies (i.e. the Reportable Group has appointed a constituent entity as its SPE to file CbC Report on behalf of the Group, and exchange mechanism is in place between that jurisdiction and HK), or
- SPE-filing-in-HK exception applies (i.e. SPE is appointed as the sole substitute for the Ultimate Parent Entity (“UPE”) to file the CbCR in HK on behalf of the group).

Each HK Entity of a reportable group is also required to file a written notice with the Commissioner containing information relevant for determining the obligation for filing a CbC Return within 3 months after the end of the relevant accounting period.

Timeline and penalty

12 months after the end of the relevant accounting period or the date specified in the assessor’s notice, whichever is the earlier.

A reporting entity must:

- Keep sufficient records to enable the accuracy and completeness of the CbCR filed.
- Retain the records for a period of 6 years beginning on the date on which the return is filed.

Penalties will be imposed in respect of matters such as failing to file CbCR and providing misleading, false or inaccurate information in CbCR. Details as follow:

- On conviction to a fine at HK\$50,000, and the court may order the entity to do, within the time specified in the order, the act that the entity has failed to do (“court order”).
- Further fine of HK\$500 for every day or part of a day during which the offence continues after conviction for committing an offence.
- If a reporting entity fails to comply with an order of the Court, the entity commits an offence and is liable on conviction to HK\$100,000.

The Hong Kong Inland Revenue Department (“IRD”) has recently published some general guidelines on its website on tax issues arising from the COVID-19 pandemic on 29 July 2021.

The IRD’s approach in relation to the tax issues is generally in line with the Updated Guidance on Tax Treaties and the Impact of the COVID-19 Pandemic (the COVID-19 Tax Treaty Guidance) and Guidance on the Transfer Pricing Implications of the COVID-19 Pandemic (the COVID-19 Transfer Pricing Guidance) released by the OECD in January 2021 and December 2020 respectively. These Guidance should be read together with the Commentary on the Model Tax Convention on Income and on Capital (MTC) and OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

In short, the IRD has issued brief guidelines on their practices in relation to the tax residency of companies and individuals, Permanent Establishment (“PE”) and income from employment of crossed border employees, and transfer pricing. These views expressed in the IRD’s website are for general information only. The relevant tax issues will still be subject to further examination of the facts and circumstances of each case.

With regard to PE, whether a non-Hong Kong resident person has a PE in Hong Kong within the meaning of a tax treaty or domestic PE legislations in Hong Kong, (as the case may be) is a question of fact and degree. In determining the issue, the IRD will examine all the relevant facts and circumstances, including the international travel disruption caused by public health measures imposed by governments in response to COVID-19. The IRD advised that they are prepared to adopt a flexible approach when determining the issue, having regard to the relevant principles in the COVID-19 Tax Treaty Guidance.

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