

Arm's Length Price Compliance Requirements For Intercompany Loans And The Importance Of DEMPE Analysis In The Context Of Intangibles

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About the speaker



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- Sahil specializes in the field of Transfer Pricing and has around 16+ years of rich experience spanning across 2 Big 4 firms in India and with another reputed mid-tier firm in Singapore. His expertise is spread across various domains like compliance, advisory and litigation with a significant length, breadth, and depth covering all kinds of Transfer Pricing assignments and projects.
- Sahil has been assisting various clients in developing appropriate inter-company Transfer Pricing policies, undertaking detailed diagnostic reviews of existing transactions and business models, highlighting the potential red flags and suggesting the appropriate arm's length prices while conducting robust economic analyses for intercompany services, manufacturing, distribution, loan benchmarks, royalty fee, license fee, trademark fee etc.
- He has also assisted clients in terms of Transfer Pricing compliance (Documentation and Planning assignments) and advisory assignments in accordance with the 3-tiered documentation rules as per OECD's BEPS Action Plan 13 and other Action Plans as well. He has also assisted many clients on Transfer Pricing aspects related to Advance Pricing Agreements, Permanent Establishment attribution issues etc with significant experience across various industries.
- He has also been actively involved in various Transfer Pricing webinars, seminars and professional body discussions as one of the leading speakers and has also drafted various technical articles on different topics related to Transfer Pricing.
- Further, he has also been featured in leading and well-renowned global magazines as one of the Transfer Pricing experts with significant expertise.

Agenda

Intercompany loans – Concept and issues involved

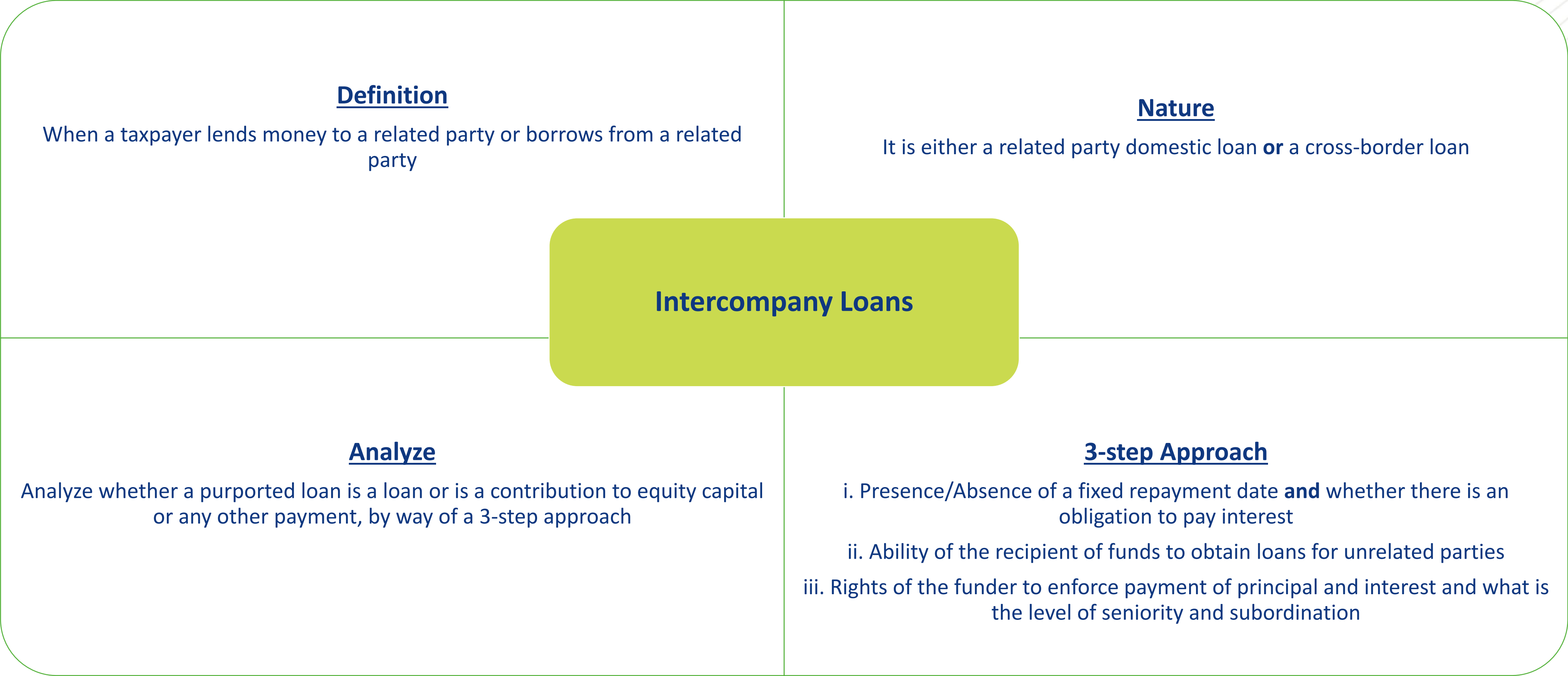
Intangibles – Definition, issues involved and what is DEMPE analysis

Intercompany loans - Transfer Pricing compliance requirements

Intangibles - Transfer Pricing compliance requirements

Q&A

Intercompany loans – Concept and issues involved (1/2)



Intercompany loans – Concept and issues involved (2/2)

- Arm' length principle needs to be applied for each intercompany loan (whether domestic or cross-border)
- If an intercompany loan is not at arm's length, the tax authority will either:
 - a) Disregard any interest expense in excess of the arm's length amount determined by the authority for tax deduction purpose; or
 - b) May not support the taxpayer in any MAP discussions to resolve any double taxation related issues arising from any TP adjustments made by the local tax authority or any foreign tax authority

Important amendment made to Singapore TP guidelines

- With effect from 1 January 2025, IRAS will not accept any interest-free related party loan as an arm's length transaction, unless taxpayers have reliable evidence that independent parties under comparable circumstances would similarly provide loans without charging any interest.
- **Thus**, it becomes extremely important for taxpayers to examine any interest-free arrangements and revise the underlying pricing policy, appropriately and with immediate effect.
- Further, the pricing policy must be supported by an appropriate benchmarking analysis conducted in proper accordance with the prescribed rules

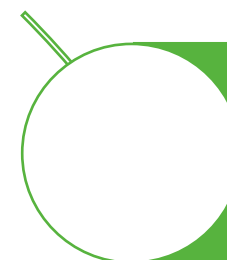
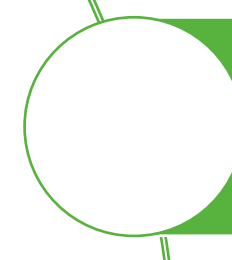



Intangibles – Definition, issues involved and what is DEMPE analysis (1/2)

- **OECD Definition of intangible** - Intended to address something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances. Types include:
 - ✓ **Marketing intangible** – May include trademarks, trade names, customer lists etc
 - ✓ **Trade intangible** – Generally includes patents, copyrights, know-how etc

- **Issues/Challenges involved** – Most significant issue/challenge pertains to the correct determination of the entity or entities within a group who are actually entitled to a share in the returns derived by the group, from the underlying intangibles. Other significant issues/challenges include:
 - ✓ Lack of availability of appropriate comparability
 - ✓ Ownership and/or use of different intangibles by different related parties within the group
 - ✓ Difficulty of isolating the impact of any particular intangible on the group's income
 - ✓ Hard to correctly delineate the actual DEMPE functions performed by different related parties within the group etc

Intangibles – Definition, issues involved and what is DEMPE analysis (2/2)

What is DEMPE analysis – An extremely important analysis to be conducted in conjunction as well as to support the FAR analysis, in order to appropriately determine the correct allocation of the returns derived by the group from the exploitation of intangibles, and for the appropriate allocation of costs and other burdens related to the intangibles among the group members

-  **D** – Development would include all functions leading to the conception and creation of any intangible asset(s). Will entail activities like R&D, testing, etc.
-  **E** – Enhancement would include all functions that enhance the value or utility of the intangible asset(s). Will entail activities like improvements, or upgrades or any amendments/modifications.
-  **M** – Maintenance would include functions that are required to increase the longevity and durability of the intangible asset(s). Will entail activities like regular monitoring, upkeep etc.
-  **P** – Protection would include functions that aim to ensure protection of the legal rights, and any proprietary interests associated with intangible assets. Will entail activities like applying for patents, copyrights etc
-  **E** – Exploitation would include functions that lead to the enjoyment or utilization of the intangible assets, as part of economic rights vested with such an asset. Will entail activities like usage or licensing or even sale of intangible asset(s)

Intercompany loans - Transfer Pricing compliance requirements

Details
Intercompany loan arrangements must be carefully analyzed and evaluated with an appropriate interest rate, determined as per the guidelines
With effect from 1 January 2025, <u>interest-free loan arrangement will be completely disregarded by the IRAS</u>
Intercompany loan Agreements should also be in place for a loan transaction, to support the relevant benchmarking analysis and the TP Documentation
For a loan transaction (whether cross-border or domestic), wherein the principal loan amount is SGD 15 million or more , a proper database-based benchmarking analysis is mandatorily required to demonstrate that the transaction is at arm's length
For a loan transaction (whether cross-border or domestic), wherein the principal loan amount is less than SGD 15 million , taxpayer need to choose 2 options: <ul style="list-style-type: none">• Either the taxpayer needs to apply IRAS indicative margin rates; or• A proper database-based benchmarking analysis can be undertaken to demonstrate that the transaction is at arm's length
<ul style="list-style-type: none">• Generally, the Comparable Uncontrolled Price (CUP) method is the preferred method for determining the ALP for related party loans. However, when using this method, 3 steps should be adopted to determine the arm's length interest rate:<ul style="list-style-type: none">a) Conduct a comparability analysis (consider factors like nature & purpose of loan, market conditions of the loan, principal amount, duration, terms, credit rating of the borrower etc)b) Identify the most appropriate methodc) Determine the arm's length results

Intangibles - Transfer Pricing compliance requirements

Details
Important characteristics to be examined include: <ul style="list-style-type: none">• Nature of the transaction• Type and nature of the intangible• Duration and extent of rights provided by the intangible property• Anticipated benefits from the use of the intangible property
Typical transactions involving intangible assets include Royalty Fees, License Fees, Trademark Fees, Brand Fee etc
Individual quantum for each set of transaction (as stated above) is 1 million SGD for Financial Year 2024 and all the years before
Individual quantum for each set of transaction (as stated above) is 2 million SGD for Financial Year 2025 and onwards
Depending upon the nature of the transaction involved, the most appropriate method would either be the CUP method or the Transactional Net Margin Method. However , an appropriate benchmarking analysis will be required to determine the arm's length price for any transaction pertaining to intangible asset(s).
Further, depending upon the revenue of the taxpayer in the particular financial year, the results of the benchmarking analysis for the intangible asset(s) related transaction needs to be either captured in a TP Documentation or a TP Memo, to ensure appropriate compliance with the prescribed guidelines

Q&A

Growth beyond boundaries

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