

Commodity marketing and trading activities – transfer pricing guidelines

Overview

In May 2019, the Inland Revenue Authority of Singapore (IRAS) released the transfer pricing (TP) guidelines for commodity marketing and trading activities (e-Tax Guide), which provides guidance on how to analyse the economic value of commodity marketing and trading activities (commodity marketing/trading activities) in Singapore. The e-Tax Guide outlines the various factors that may affect the transfer price for these activities, discusses appropriate TP methods that may be applied and highlights the benefits and common roles of conducting commodity marketing/trading activities in Singapore.

Commodity marketing and trading entities are often part of a complex value chain, performing a wide range of activities and requiring varying levels of effort and contributing in various ways to a commodity multinational enterprise's (commodity MNE) overall value chain. The 2018 Singapore TP Guidelines (Fifth Edition) (2018 Singapore TP Guidelines) should be read and applied together with the principles set forth in the e-Tax Guide.

Commercial objectives and functional profile for commodity marketing/trading entities

The IRAS introduces four broad levels of participation that commodity marketing/trading entities may undertake. These include a service provider, agent, distributor and full risk-taking entrepreneur. The e-Tax Guide examines the various levels of activities, stipulating the key functions that each level of participation should entail.

Further, the e-Tax Guide discusses the specialised assets required to optimise production, plan resources, reduce storage requirements and maximise profits throughout the commodity value chain, including how these assets should be compensated.

Finally, the risks stemming from commodity marketing/trading activities are highlighted, including examples of possible ways to control or mitigate these risks.

TP methods

The e-Tax Guide discusses each TP method in relation to the four broad commodity marketing/trading participation levels and provides specific examples of when a certain method should be applied. For example:

- ▶ Commission rates for activities involving an agent or marketing activities
- ▶ London Metal Exchange (LME) for pricing commodities based on a percentage of the LME price
- ▶ Means of Platts Singapore for pricing jet fuel, gasoline and diesel
- ▶ Combination of indices for pricing liquefied natural gas (i.e., hybrid of crude oil index and Henry Hub gas price)

Additionally, practical solutions are offered for entities encountering difficulties in applying certain methods.

Additional TP documentation requirements

The 2018 Singapore TP Guidelines outline the TP requirements for Singapore taxpayers. In addition to the existing content requirements, the IRAS outlines in the e-Tax Guide additional specific information it expects commodity marketing/trading entities to include in their TP documentation.

Implications

Taxpayers with commodity marketing/trading activities in Singapore should assess their contribution to the commodity MNE broader value chain. A thorough analysis of the functions performed, assets used and risks assumed in each related party commodity transaction should be evaluated, including a review of the TP methodology against the IRAS' proposed methods in the e-Tax Guide.

Notably, for Singapore taxpayers with related party commodity transactions, the e-Tax Guide will enable them to analyse their operations to ensure they have the required substance and support for their commodity marketing/trading activities. This is particularly relevant for entities with related party transactions with Australia, given the Australian Taxation Office (ATO) Practical Compliance Guide (PCG 2017/1) that sets out the ATO compliance approach to TP issues related to centralised operating models (hubs) involving procurement, marketing, sales and distribution functions. The PCG arose from ATO's concern related to offshore entities operating as hubs in supply chains, particularly foreign hubs used by Australian businesses in marketing exports from Australia.

When the PCG is compared with the e-Tax Guide, the key difference lies in the PCG's emphasis on the maintenance of appropriate evidence to justify the economic substance and purpose of the marketing hub, particularly when the taxpayer falls outside the safe risk rating "green zone". This includes evidence on the decision-making capacity, why risks are borne, how risks are managed and how this produces a valuable economic contribution to profits. Further, evidence is requested to support the profit accruing to the hub and why this is reflective of the economic contribution provided by the hub.

In comparison, the e-Tax Guide provides a detailed explanation and highlights the key value being created by strategically placed marketing hubs and provides a myriad of support and potential evidence for the functions being performed by commodity hubs in Singapore. This includes the benefit that Singapore as a country provides, before analysing in detail the various structures seen and value attributed to these structures based on the respective functions performed, risks assumed and assets borne by hubs in Singapore. As such, the e-Tax Guide is helpful in assessing an entity's operations and determining whether they undertake the required functions to support the profitability levels earned in Singapore.

Contact us

Luis Coronado

EY Asia-Pacific Transfer Pricing Leader and Partner
Ernst & Young Solutions LLP
Tel: +65 6309 8826
Email: luis.coronado@sg.ey.com

Stephen Lam

Partner, Transfer Pricing Services
Ernst & Young Solutions LLP
Tel: +65 6309 8305
Email: stephen.lam@sg.ey.com

Jonathan Belec

Partner, Transfer Pricing Services
Ernst & Young Solutions LLP
Tel: +65 6309 6175
Email: jonathan.belec@sg.ey.com

Chai Sui Fun

EY Asean International Tax Policy and Controversy
Leader and Partner
Ernst & Young Solutions LLP
Tel: +65 6718 1128
Email: sui.fun.chai@sg.ey.com

Stephen Bruce

Partner, Financial Services Tax
Ernst & Young Solutions LLP
Tel: +65 6309 8898
Email: stephen.bruce@sg.ey.com

Sharon Tan

Director, Transfer Pricing Services
Ernst & Young Solutions LLP
Tel: +65 6309 6375
Email: sharon.tan@sg.ey.com

Jow Lee Ying

Director, Transfer Pricing Services
Ernst & Young Solutions LLP
Email: lee-ying.jow@sg.ey.com

Rajesh Bheemanee

Director, Transfer Pricing Services
Ernst & Young Solutions LLP
Tel: +65 6309 8274
Email: rajesh.bheemanee@sg.ey.com

Warren Chung

Director, Transfer Pricing Services
Ernst & Young Solutions LLP
Tel: +65 6718 1072
Email: hoonseok.chung@sg.ey.com

Anju Singh

Director, Transfer Pricing Services
Ernst & Young Solutions LLP
Tel: +65 6309 6712
Email: anju.singh@sg.ey.com

Our tax leaders in Singapore

Head of Tax

Soh Pui Ming
Ernst & Young Solutions LLP
Email: pui.ming.soh@sg.ey.com

Business Tax Services

Angela Tan
Ernst & Young Solutions LLP
Email: angela.tan@sg.ey.com

Global Compliance and Reporting

Chai Wai Fook
Ernst & Young Solutions LLP
Email: wai-fook.chai@sg.ey.com

Financial Services Organisation

Amy Ang
Ernst & Young Solutions LLP
Email: amy.ang@sg.ey.com

Indirect Tax Services

Yeo Kai Eng
Ernst & Young Solutions LLP
Email: kai.eng.yeo@sg.ey.com

International Tax Services

Chester Wee
Ernst & Young Solutions LLP
Email: chester.wee@sg.ey.com

Transfer Pricing

Luis Coronado
Ernst & Young Solutions LLP
Email: luis.coronado@sg.ey.com

People Advisory Services

Panneer Selvam
Ernst & Young Solutions LLP
Email: panneer.selvam@sg.ey.com

Transaction Tax

Darryl Kinneally
Ernst & Young Solutions LLP
Email: darryl.kinneally@sg.ey.com

Legal Services

(provided by Atlas Asia Law Corporation,
an independent member firm of the global
EY network)
Evelyn Ang
Email: evelyn.ang@atlasialaw.com.sg

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