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PREMIER TAX EVENT OF THE YEAR
NATIONAL TAX CONFERENCE
2020

25 & 26 AUGUST 2020 | TUESDAY & WEDNESDAY
VIA LIVE STREAMING

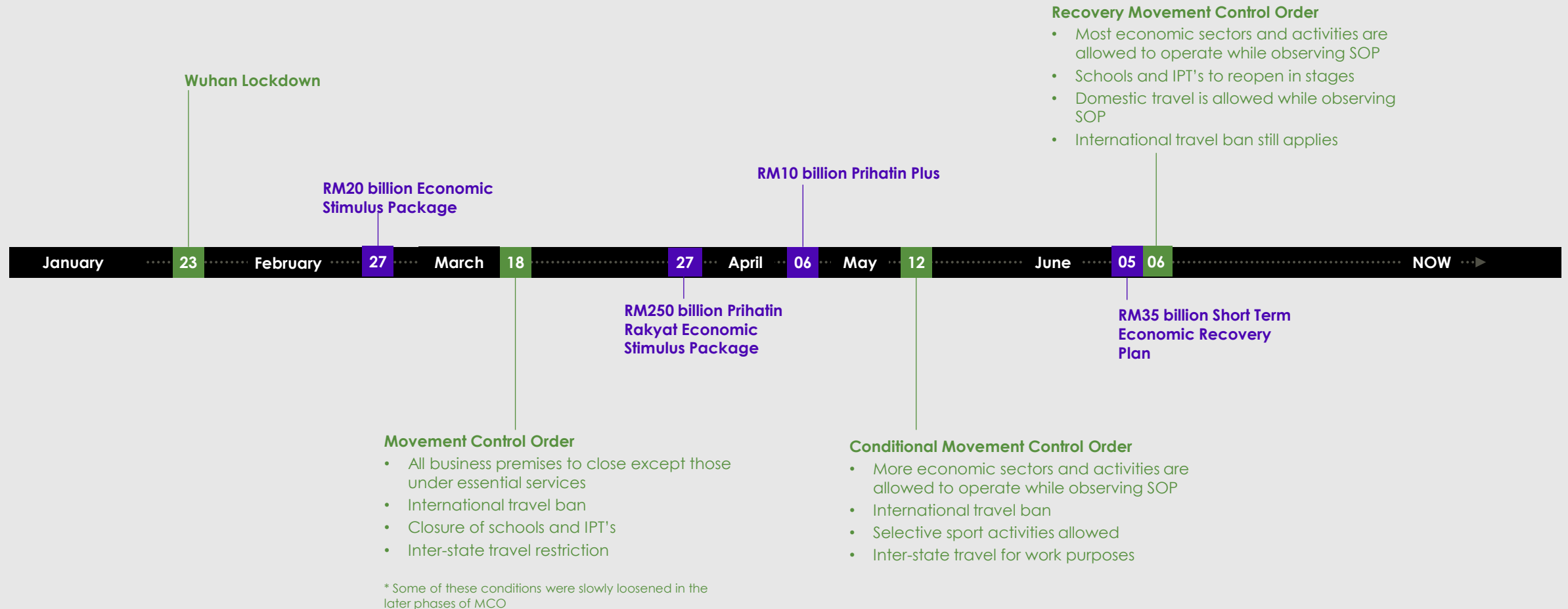
Speaker:

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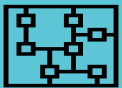


TOPIC 5: **TRANSFER PRICING NOT IMMUNE TO COVID-19**

OVERVIEW


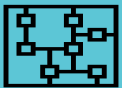


A Timeline of Major Events Emanating from Covid -19



Impact of Covid-19 – A Sectoral Perspective for Malaysia

Industry	 Aerospace	 Automotive	 Oil and Gas	 Property
Operational	<p>Each day of halted production will require 13 days recovery period to resume operations at optimum rate.</p> <p>Some companies may not be able to fulfill demands.</p> <p>Potential job-losses of 10%-20%</p>	<p>Manufacturing and after-sales activities were completely stopped during MCO</p> <p>Potential losses of export business for certain component manufacturer</p> <p>Potential job-losses of 10%-20%</p>	<p>Research predicts worsening outlook for the oil industry due to the demand slump brought about by reduced travel during this pandemic.</p>	<p>Decline in property purchases over the months.</p> <p>Delay in projects throughout the supply chain following the outbreak</p>
Financial	<p>Potential losses of RM1.2 billion – 2.2 billion in revenue</p> <p>Some companies are forecasted to cease operations</p>	<p>Potential losses of 30% in revenue by end of 2020 if the industry fails to boost back sales</p>	<p>Potential losses of RM31 billion in revenue due to the low price of crude oil, which continues to be buffeted by the Covid-19 pandemic</p>	<p>Cost overruns due to delay in projects.</p> <p>Secondary property prices expected to be 10% lower.</p>

Impact of Covid-19 – A Sectoral Perspective for Malaysia

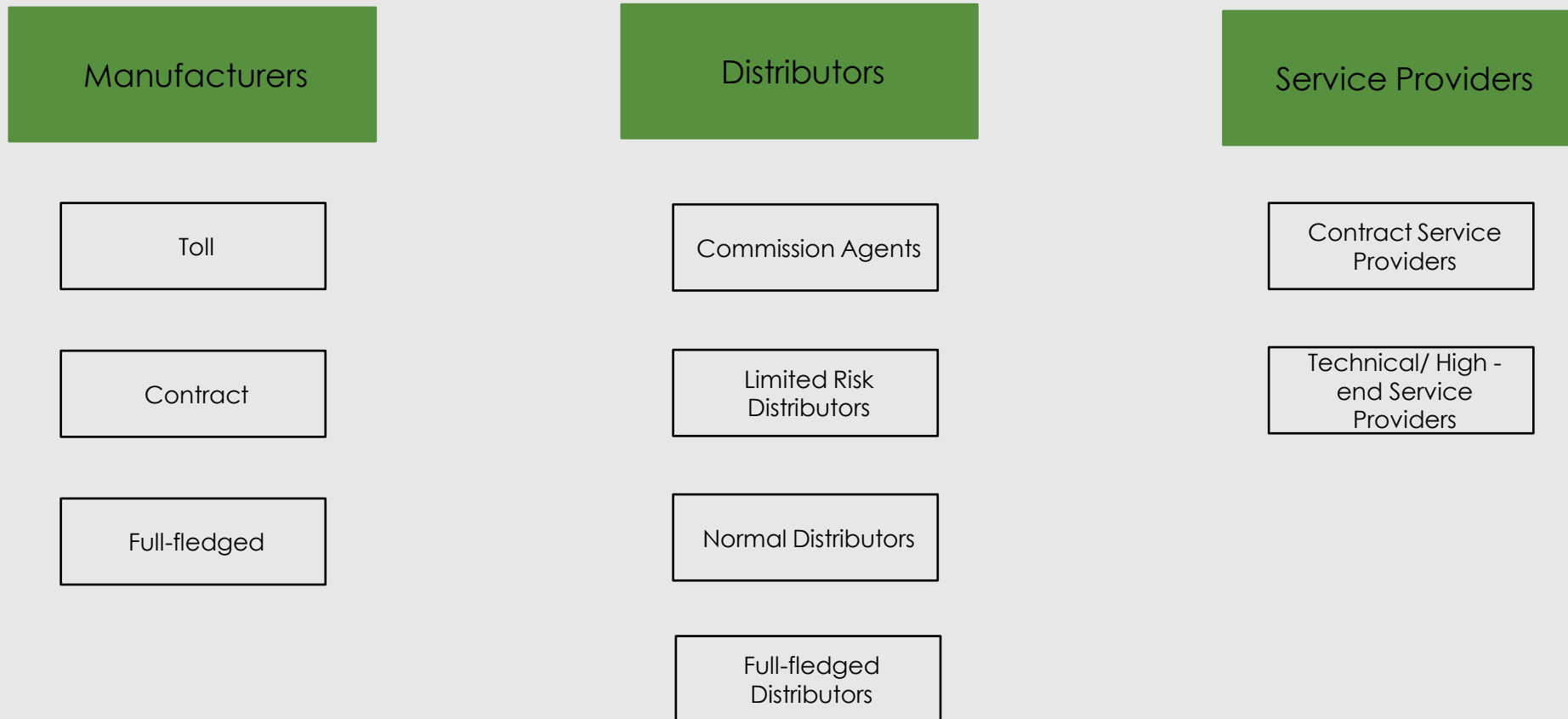
Industry	 Electrical and Electronics	 Metal, Machinery, Equipment and Parts	 Tourism	 Glove Makers
Operational	<p>Many MNCs have put their future investments on hold (some of the investments are between RM2 billion to RM5 billion each)</p> <p>Local SMEs in the supply chain are affected and this will lead to retrenchment of local workers due to lack of business/ projects</p>	<p>M&E is estimated to have 20%-30% job losses due to not able to complete job orders or supply products to customers. Metal is estimated to have 50% of job losses not only due to MCO but also slow demand, losses of orders and continuous impact of Covid-19</p>	<p>Tourism is one of the economic sectors hardest hit by Covid-19 and is expected to be the last to recover</p> <p>Adverse impact on tourism export.</p> <p>In April 2020, employment volume has decreased by 1% to 14.93 million people.</p>	<p>One of the key beneficiaries of the Covid-19 outbreak, glove makers have been enjoying stronger demand from existing customers, as well as the coming on board of new customers such as non-government and government organisations with ad-hoc orders.</p>
Financial	<p>Estimated impact of RM3.1 billion to GDP during 14 days shutdown.</p> <p>Estimated losses of RM14.5 billion in exports for 14 days shutdown.</p>	<p>Potential losses of RM3.18 billion in revenue</p>	<p>Losses of RM45 billion in revenue in first half of 2020</p>	<p>Malaysian glove makers expect glove demand to increase by roughly 30%-50%.</p> <p>This is a sharp contrast to 8-10% pre-Covid-19.</p>

CHALLENGES FACED BY MALAYSIAN TAXPAYERS

Visible Disruptions

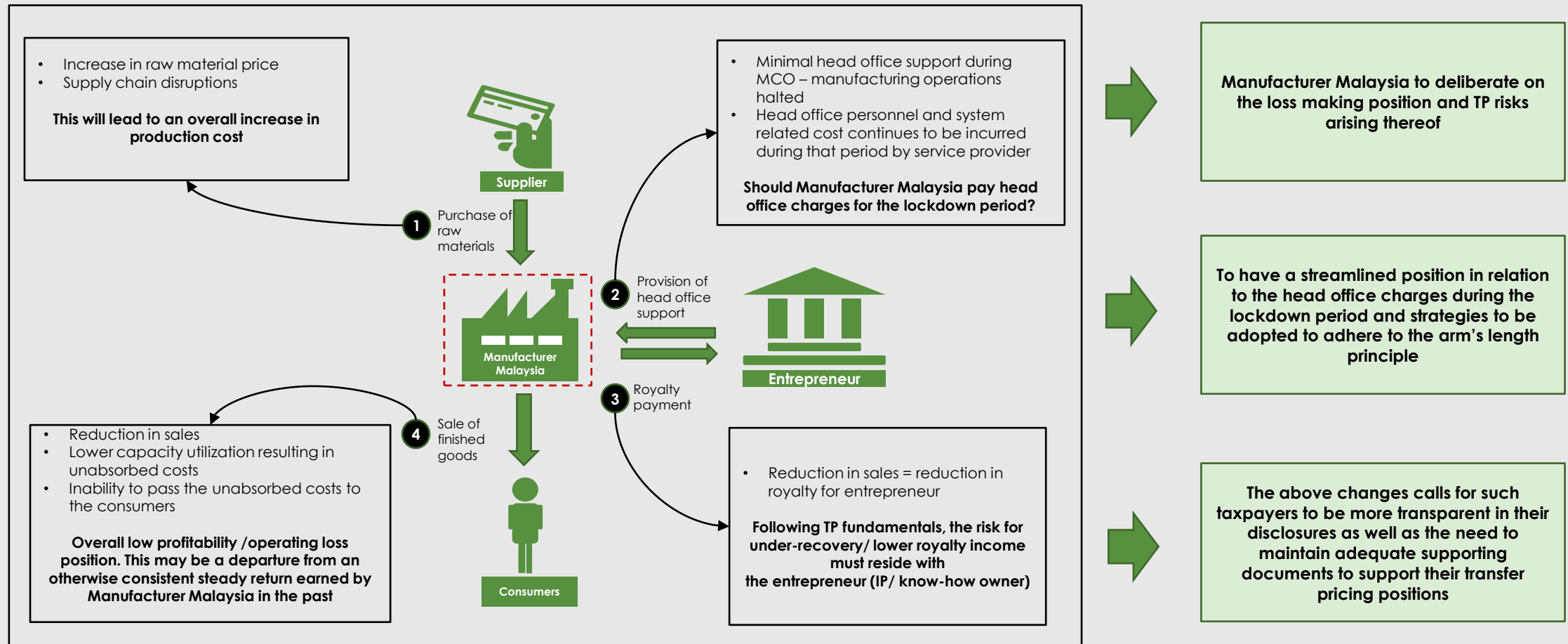


Common Operating Structure of Taxpayers



Manufacturing Operation in Malaysia

A case study on impact of Covid-19



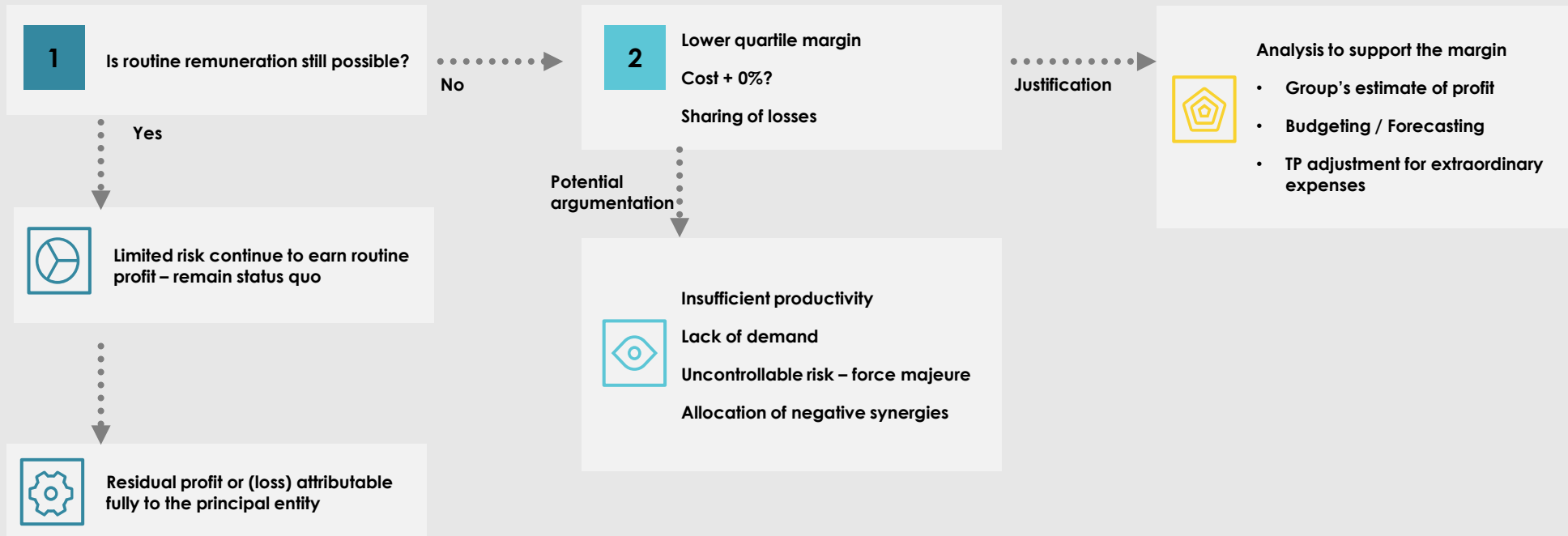
Is routine remuneration possible for limited risk entities?

- Entities carrying out routine functions are typically the least complex entity
- Expected to earn relatively small but stable profit margin
- Most commonly the tested party in a benchmarking exercise
 - Cost plus → gross margin based
 - TNMM → net return of sales, costs or assets
- Allocating losses to routine functions in normal circumstances is highly unusual

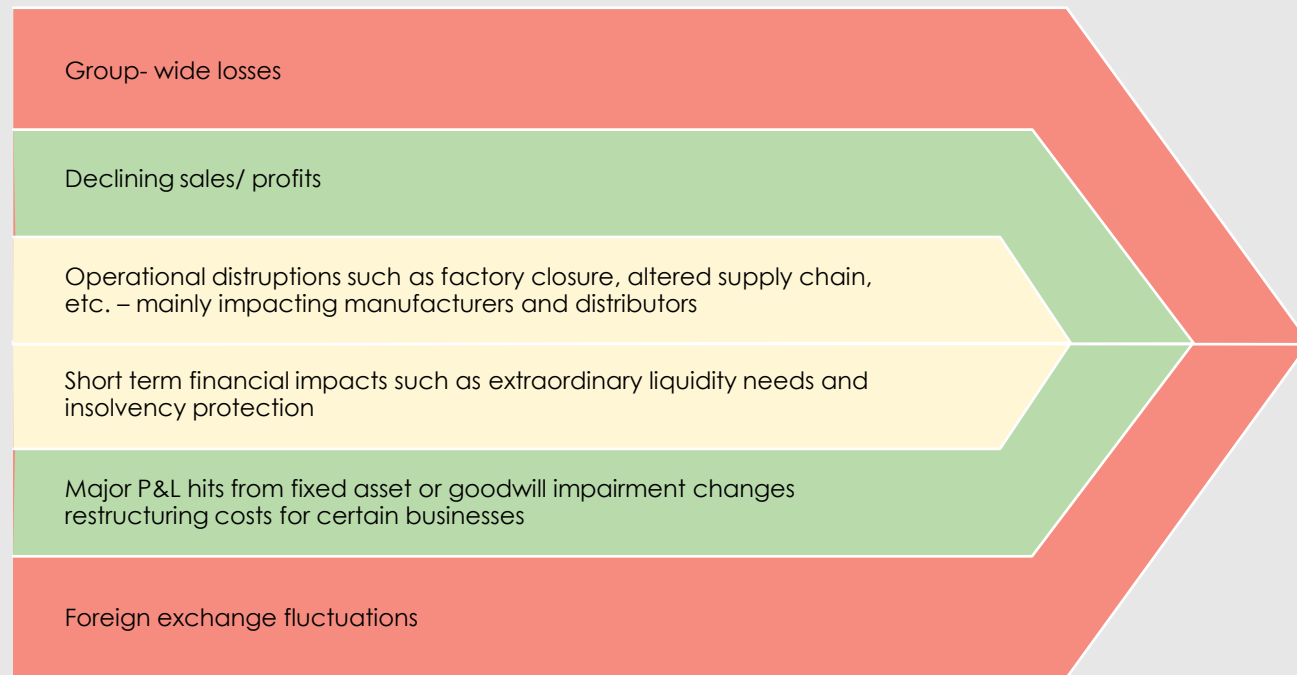
Should not lead to loss position

Can results outside the conventional arm's length range clearly be supported?

Limited Risk Entities - Considerations



Resultant Impact



Bottom Line

Previously efficient TP structures may now produce tax inefficiencies, may not align with changed priorities, or may not be flexible enough to accommodate a severe economic shock

STREAMLINING TRANSFER PRICING

In Depth Transfer Pricing Analysis Needed



Analysis of Covid-19 impact on taxpayers

- Assess and analyse the operational and financial data for FY2020 vs past year data
- Distinguish losses or non – performance arising from economic effects of Covid-19 vs normal risks as a result of business conduct



Review related party arrangements

- Analyse the possibility to amend current intercompany transactions in line with actual conduct of the parties involved.
 - Who performs the major functions and bears the significant risks
 - Conduct of third parties under comparable circumstances
 - Commercial rationale of price adjustments, if any



Transfer Pricing Documentation

- Special attention for the TP documentation prepared for FY2020
 - Any deviation from the standard TP policy must be carefully documented
 - Important to distinguish the period impacted by Covid-19 vs normal business risk in the write -up
 - Capture the key value drivers that are lost or transferred due to Covid-19



Communication with IRBM

- Keep communication channels open on complex TP issues and other tax issues with the IRBM
- Upfront voluntary disclosure with IRBM is optional

Comparability Analysis – Some Considerations

- Establish an approach to justify deviations (if any) from established group TP policies
- Develop appropriate adjustments and possible impact on companies operating in the market
 - Consider capacity utilization (idle capacity) adjustments
 - Consider the use of statistical tools in order to develop appropriate scenarios of how market related events directly impact the financial performance of taxpayers. Use of reliable indicators which show a direct correlation with the financial performance of the taxpayers is the key
 - Carefully investigate whether asset write offs / impairments can be excluded from tested profits
- Extend multi-year analysis window to capture full business cycle (not just “good” years)
- Expand the comparable set to include loss comparables
- Target a different point in the range??
- Modify comparable search criteria to identify comparables experiencing the same economic circumstances: - e.g., sales decline, increased opex/sales ratio

Issuance of IRBM FAQ for Advance Pricing Arrangements (“APA”)

Malaysian Inland Revenue Board published online FAQs on APAs for businesses as a guidance during the coronavirus pandemic. The FAQ touches on the following items:



New APA application

- No new application from businesses affected by Covid-19 will be accepted by IRBM until further notice



Treatment of on-going APA

- IRBM does not allow any amendment or substantial updates on material changes to the on-going application as full impact of Covid-19 not known
- Taxpayer can continue with the on-going APA based on information previously submitted to IRBM or taxpayer can withdraw from the APA application if the probability of the impact of Covid-19 on taxpayer's business is significant.



Treatment of concluded APA

- Taxpayers can notify the IRBM of the need for a revision or apply for cancellation of the APA in the event it cannot fulfil the critical assumptions due to Covid-19
- Taxpayers do not qualify for a renewal if the critical assumptions in the expiring APA are no longer valid or relevant due to material changes on taxpayer's business as a result of Covid-19 pandemic. Hence, under such circumstances, the taxpayer may file a new APA application or choose not to submit a new APA application.



Renewal of APA

- APA can be renewed under the terms and conditions similar to the expiring APA.

THANK YOU