



**Operational Transfer Pricing**  
*Resolving Operational Woes;  
Achieving The Right Financial Outcome*

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**Open Your Eyes  
on Operational  
Transfer Pricing**

## KEY TAKEAWAYS

- Through OTP, group companies can implement and continuously monitor their TP policies within the organisation, and ensure that the TP policies are translated into correct financial statement outcomes in the respective legal entities.
- OTP leverages existing resources within the organisation (such as technology platforms, ERP systems, or even Excel spreadsheets) to enhance and streamline the TP lifecycle.
- People are central to the success of OTP implementation. The organisation must ensure that all stakeholders are aligned with the TP strategy, its execution and its defence.

**T**o achieve arm's length pricing for related-party transactions, it is necessary to perform a Functions, Assets, and Risks (FAR) analysis, conduct an economic/comparability analysis and establish the appropriate transfer pricing (TP) policy. Establishing the TP policy is, however, only the start of the TP lifecycle.

“Once the TP policy is in place, operational transfer pricing (OTP) comes into the picture. Through OTP, group companies can implement and continuously monitor their TP policies within the organisation, and ensure that the TP policies are translated into correct financial statement outcomes in the respective legal entities,” explained Accredited Tax Advisor (Income Tax) Elis Tan, Executive Director and Transfer Pricing Leader, BDO Singapore, at a webinar organised by the the [Singapore Chartered Tax Professionals](#).

## Operational Transfer Pricing

### WHAT IS OTP?

At its core, OTP is about actively managing the organisation's TP policies, optimising data flows, enhancing process efficiency, and developing automated solutions. Contrary to popular belief, building an OTP system does not necessarily require a substantial budget. In fact, OTP leverages existing resources within the organisation (such as technology platforms, ERP systems, or even Excel spreadsheets) to enhance and streamline the TP lifecycle.

OTP assessment is beneficial for companies looking to improve their financial reporting systems and controls, particularly those with substantial manual data management and extraction processes, as well as those experiencing inconsistent TP results.

OTP ensures that TP policies are consistently applied across all transactions and jurisdictions within the organisation. This consistency is crucial for navigating increasingly complex local and international TP requirements. It also helps mitigate the risks of penalties and TP adjustments in the event of audits.

## WHAT HAPPENS IF OTP IS NOT CARRIED OUT PROPERLY?

Companies can face several challenges if OTP is not carried out properly. For instance, improper implementation of OTP can lead to significant data management issues.

The absence of a robust audit trail may hinder the organisation's ability to reconcile its financial data with its TP policies, making it difficult to respond promptly to tax authorities. In addition, the organisation may struggle to meet pre-determined margins or targets, potentially resulting in substantial true-ups/downs at the end of the financial year.

### *The TP Lifecycle Activities*

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For OTP to be effective, a holistic approach encompassing the entire TP lifecycle should be adopted. The TP lifecycle consists of four main phases – planning, implementation, compliance and controversy.

#### **(I) PLANNING**

During the planning phase of the TP lifecycle, a FAR analysis is performed to determine the characterisation of the relevant entities. Assuming that a company is determined to be a limited risk distributor (based on its functions performed, assets used, and risks assumed), a benchmarking study would be conducted to determine the routine operating margin to be earned by it. With these results, the company can establish the TP policy and prepare the implementation roadmap.

#### **(II) IMPLEMENTATION**

The implementation phase of the TP lifecycle can be summarised into the following steps:

- **Build:**  
The organisation will implement TP calculations, processes, procedures, and documentation. This may include developing calculation models (with automation, if applicable), defining roles and responsibilities, establishing governance processes, executing intercompany agreements, and conducting training to ensure all staff understand the implementation.

- **Calculate:**  
Based on the established framework, the company will regularly run and reconcile TP calculations. A calculation control framework must be in place to allow staff to escalate issues when abnormalities are identified during reconciliation.
- **Invoice and book:**  
The company will post journal entries, raise and execute invoices, and settle and reconcile intercompany amounts.
- **Monitor:**  
The implementation of the TP lifecycle can only be considered complete with continual monitoring to ensure that year-to-date results reconcile with the TP policies. Processes and procedures should be in place to investigate inconsistencies, calculate adjustments (where necessary), and review the consistency in the conduct of parties and the economic substance of relevant entities. Some companies may also have their own internal audit processes.

#### **(III) COMPLIANCE**

At the end of the year, the company needs to complete both internal and external reporting. This includes feeding TP information (such as the related-party transactions) into financial reports and ledgers, as well as participating in the statutory account preparation process. In addition, the company needs to prepare tax and TP reports for compliance purposes.

## (IV) CONTROVERSY

The organisation must be ready to respond to any tax or financial audits.

In view of the changing tax landscape focusing on tax transparency, organisations should coordinate tax audit responses globally to ensure that their responses are consistent.

### Core Pillars To OTP

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Organisations looking to implement OTP should take note of these core pillars to the TP lifecycle, namely people, process, data and technology.

People are central to the success of OTP implementation. The organisation must ensure that all stakeholders are aligned with the TP strategy, its execution and its defence.

Once everyone is aligned, the process owners should be identified and the end-to-end TP process and sub-processes mapped.

The organisation must determine the data required to execute and document a TP policy, including the timeframe for data collection, data sources, availability, and whether the data is in the necessary format.

Performing TP calculations and reconciling these TP results with the organisation's TP policies in real time (or near real time) is difficult, if not impossible, without the help of technology. The organisation should assess current technology to identify any barriers or enablers, opportunities for increased efficiency, and any missed opportunities due to technological limitations.

### Best Practices in the TP Lifecycle

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To help you on your way to "TP enlightenment", here are some of the best practices to adopt in the TP lifecycle:

- **Process and controls:**

Proper processes and controls are essential. It is good practice for companies to map out who is involved, establish the step-by-step process for calculations, and ensure all necessary documentation is in place.

- **End-to-end Reconciliation:**

Companies must ensure consistency throughout the entire TP lifecycle, from TP policy to intercompany agreements, calculations, financial statements, and tax returns. Companies should also reconcile the variances between management accounts and legal entity results, as well as between forecasts and actuals.

- **Monitoring:**

The ability to monitor on a timely basis and develop nimble responses to strategic or operational business changes is crucial to the proper implementation of TP policies.

### Conclusion

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A well-crafted TP policy is only as good as its implementation. TP compliance is not a one-off project, but a continuous journey. As TP continues to feature in tax authorities' focus areas, it is timely for businesses to consider adopting OTP to ensure that their TP policies are indeed translated into correct financial statement outcomes.

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