



Are you being caught in between an Intra-Group Services (IGS) Arrangement and a Cost Contribution Arrangement (CCA)?

By Transfer Pricing Team

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Defining IGS and CCA

To set the right footing for the discussion, let us first examine the salient features of IGS and CCA from the following aspects:

1. Commercial rationale giving rise to the different arrangements.
2. Transfer pricing methodologies commonly accepted by the authorities.

Intra-Group Services (IGS)

- **Commercial arrangement:** IGS refers to an arrangement between members within a group of companies where one party (service provider) provides services to another party (service recipient).
- **Transfer Pricing:** Cost Plus Method is vastly adopted, where the service fee is calculated on cost incurred by the service provider, with an arm's length profit mark-up to remunerate the service provider.
- **Examples:** Services relating to general management, accounting and finance, human resource, technical support, procurement, marketing, distribution, R&D, information technology, legal, etc.



Cost Contribution Arrangement (CCA)

- **Commercial arrangement:** CCA is a contractual arrangement among members within a group of companies to share common costs and risks of developing, producing or obtaining assets, services or rights.
- **Transfer Pricing:** Cost sharing method by allocating the total costs amongst members participating in the arrangement depending on the extent of the interests of each participant in those assets, services or rights.
- **Examples:** Joint research project to produce a product, joint development of intellectual property rights, cross sharing of services, etc.

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Both IGS and CCA are associated with shared services arrangements between members within the same group of companies. At times, there is a blur line between them, so much so that the same may be perceived differently under different pairs of eyes. By and large, the Inland Revenue Board of Malaysia (IRBM) has keen eyes to ensure that a CCA arrangement remains as such. A slight crossing over by CCA to the IGS zone will alert them right away. Why is that so?



From the tax lens, there is a clear distinction between an IGS and a CCA:



- IGS represents a value added arrangement –**
The service provider is expected to earn an arm's length profit margin.



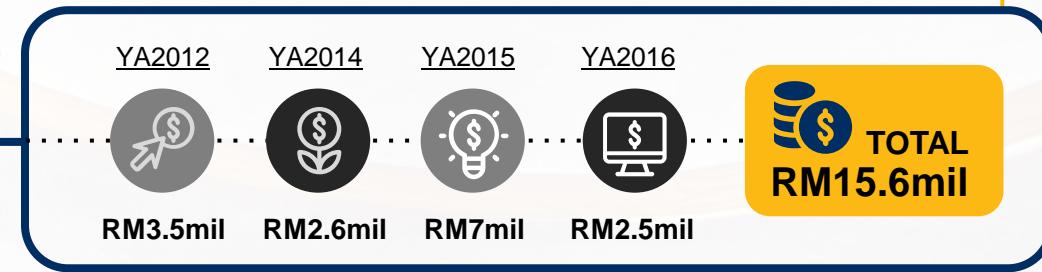
- CCA is a resource sharing arrangement –**
Costs are being shared without a requirement to impose an arm's length profit mark-up.

Tax Case on CCA vs IGS

As highlighted, a cost sharing arrangement under CCA between related companies can be construed as a provision of services (IGS) arrangement by the IRBM. A recent High Court case may shed more light on the IRBM's position with regards to the subject matter.

Background information:

- Shell People Services Asia Sdn Bhd (SPSA) was engaged in providing shared services to its related companies within the Shell Group.
- Separately, SPSA has also entered into a contractual arrangement for the cross sharing of services and resources with other shared service providers within the Shell Group, i.e. a CCA.
- During a tax audit, the IRBM was of the view that the cost sharing arrangement has close resemblance to an IGS arrangement instead of a CCA, and re-characterised the same as an IGS arrangement.
- The additional tax payable on the “deemed profit mark-up” and penalties imposed by the IRBM for the YAs 2012 to 2016 totaled RM15.6 million.

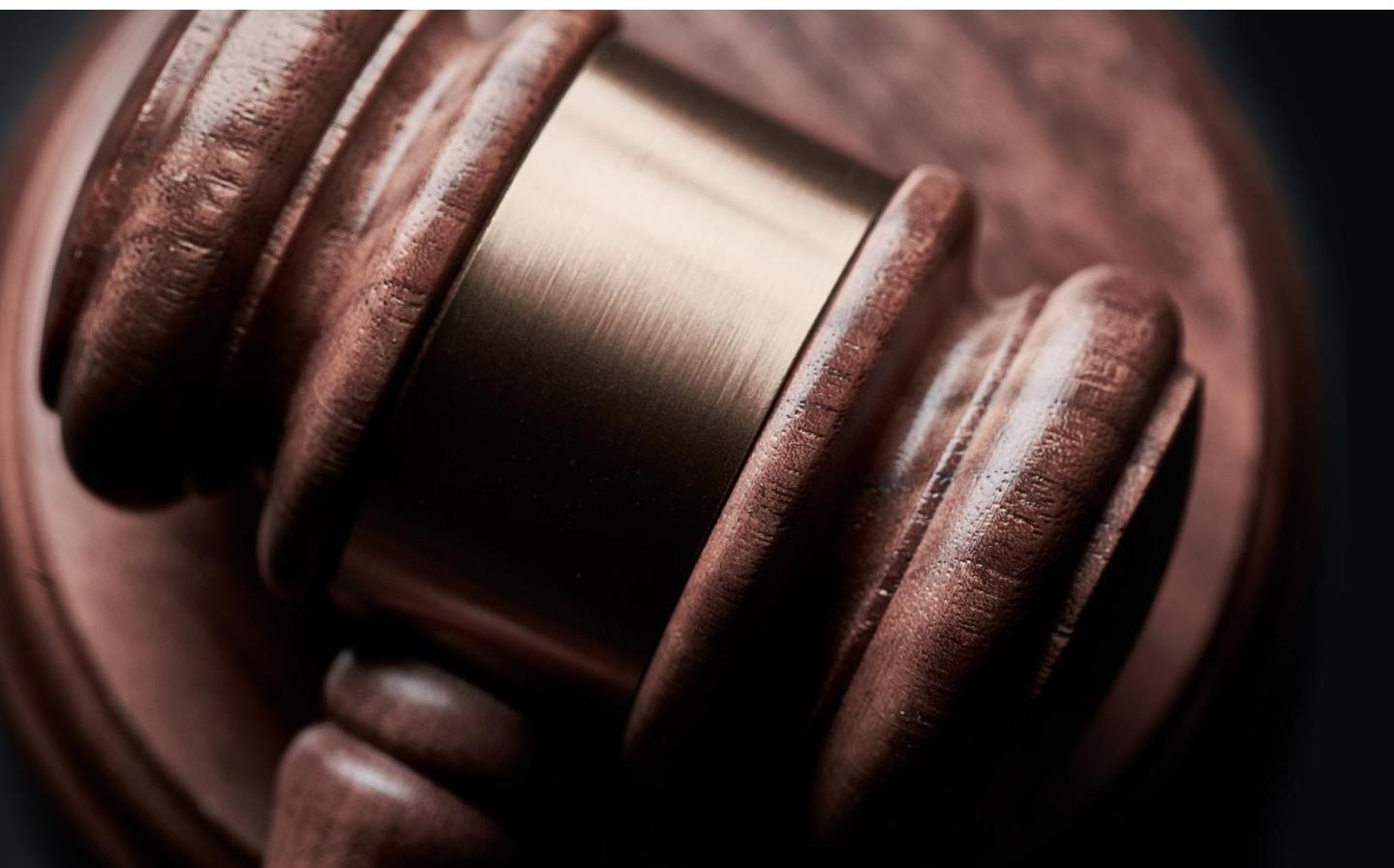


Relevant provisions under the ITA:

- The IRBM has invoked the transfer pricing provisions under Section 140A of the ITA in allowing it to substitute prices set on transactions between associated persons for failure to observe the arm's length principle.
- The normal route is for SPSA to appeal the IRBM's additional assessment to the SCIT pursuant to Section 99 of the ITA. However, instead of SCIT, SPSA submitted an application for a judicial review to the High Court. A judicial review seeks to challenge the lawfulness of a decision made by the IRBM, rather than the technicality of the subject matter under dispute.

Response from the High Court:

- The High Court rejected SPSA's application for judicial review, and asked that SPSA to make its appeal to the SCIT.
- There was no further discussion relating to the issue at hand, i.e. CCA vs IGS.



Example of a CCA – A Simplified View



The 3 companies entered into CCA – Jointly develop a new product

A CCA arrangement is entered into between 3 companies within a group of companies located in Taiwan, Singapore and Malaysia. The CCA involves a joint development of a technology product. Each participant has its own expertise, and all agreed to contribute to a common project that will see benefits being reaped in the future for all of them upon the successful launch of the product in the market.

Considerations from the transfer pricing documentation perspective:

- Clearly specify the objective of formation of a CCA, and the roles and responsibilities of each of the participants.
- Value and cost analysis to demonstrate the contributions and benefits of each participant, and subsequent allocation of the shared costs.

Key Takeaways



Characterisation has been increasingly scrutinized by the IRBM in tax audit cases, as seen from SPSA's case whereby the IRBM has not accepted the characterisation by SPSA with respect to the purported CCA adopted by SPSA with its related companies.

Drawing from the above, your ability to properly characterise a service transaction as a CCA as opposed to an IGS has a consequential impact on the defensibility of the pricing of the controlled transaction during a tax audit.

As a guide, you need to get ready at least the following to defend your position:



1.

To keep proper documentation as evidence to substantiate the essence of the transactions.

3.

To employ an appropriate transfer pricing method to support the transfer prices adopted.



2.

To explain the commercial rationale behind the CCA or IGS, supported by sound qualitative and quantitative analyses.

4.

To align "substance" to "form", meaning that actions taken should correspond to the written agreement between the parties involved in the CCA or IGS.



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