



TAX ALERT

New APA Guide in Sri Lanka: Key insights and how it impacts your business

January 2025



On 6 January 2025, the Inland Revenue Department (IRD) unveiled its much-anticipated guidance on Advance Pricing Agreements (APAs) for international transactions.

This groundbreaking initiative represents a major development in Sri Lanka's tax landscape, aligning the country with global best practices and establishing a more predictable and transparent framework for transfer pricing (TP) matters.

We commend the IRD for this progressive move, which reflects its commitment to creating an investor-friendly, competitive economy and bolstering the long-term growth of Sri Lanka's tax system.

Purpose and benefits of an APA

The primary purpose of an APA is to resolve potential disputes between the IRD and taxpayers concerning specific international transactions, minimizing the risk of double taxation or conflicting taxation under applicable Double Taxation Agreements (DTAs). By providing taxpayers with certainty about their TP methodologies, an APA helps avoid time-consuming audits, litigation, and uncertainty. The process also fosters a collaborative, non-adversarial environment between the IRD and taxpayers.

However, the introduction of the new APA guide signals the IRD's ongoing focus on cross-border transactions involving multinational enterprises (MNEs). The guidance emphasizes economic substance, reflecting the IRD's intention to prioritize the underlying economic reality of arrangements over their legal form during assessments.





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Key highlights of the APA Guide

- 1. Types of APAs** - Taxpayers can seek unilateral, bilateral, or multilateral APAs for cross-border transactions. Bilateral and multilateral APAs are contingent on the existence of a DTA between Sri Lanka and the other jurisdiction(s).
 - 2. The APA Team** - The Commissioner General of Inland Revenue (CGIR) will establish a dedicated APA team, consisting of officers from various IRD divisions.
 - 3. The APA process** - The process involves five key stages: pre-filing consultation, formal APA application, evaluation, negotiation, and submission of the Annual Compliance Report (ACR). The APA team will manage the process separately from audit teams to ensure impartiality.
 - 4. APA term and rollback** - APAs will be valid for up to four years, with the possibility of rolling back the APA's outcome to prior periods, depending on specific circumstances.
 - 5. Benchmark timeframe** - The IRD aims to complete the APA process within 24 months, with the pre-filing consultation phase expected to conclude within six months.
 - 6. Record-keeping requirements** - Taxpayers must retain detailed documentation supporting the APA for at least five years and ensure it is readily available for inspection by the IRD.
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Key highlights of the APA Guidance - Continuation

- 7. Consequences of non-compliance** - Non-compliance with APA terms may lead to revocation, cancellation, or revision of the agreement. The IRD may consult with foreign tax authorities in the case of bilateral or multilateral APAs.
 - 8. Renewing an APA** - Taxpayers must apply for renewal at least six months before the current APA expires. If significant changes have occurred, a new APA may be required instead of a renewal.
 - 9. APA fee structure** - Fees for unilateral APAs are Rs. 1 million for new applications and Rs. 750,000 for renewals. Bilateral and multilateral APAs are subject to a direct cost recovery model based on hourly rates and any additional expenses.
 - 10. Audit scope for APA transactions** - The audit scope for APA-covered transactions will focus on verifying compliance with APA terms and assessing the validity of underlying assumptions.
 - 11. Confidentiality of information** - All information collected during the APA process is protected by the secrecy provisions of the IRA and relevant DTAs, though aggregated statistics may be released without disclosing confidential taxpayer information.
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Next steps and how KPMG can help you

Taxpayers engaged in international transactions should review the new APA guidance carefully to determine its applicability and benefits for their operations. Applying for an APA, including rollback (if applicable), provides certainty on TP for a specified period, reducing the risk of disputes and ensuring compliance.

Taxpayers in the following categories would particularly benefit from the protection against double taxation and the certainty an APA offers:

- Taxpayers with significant cross-border intercompany transactions
- Taxpayers with a history of TP audits
- Taxpayers nearing the end or having recently completed their incentive periods
- Taxpayers dealing with low-tax jurisdictions

An APA can help mitigate compliance risks and potential litigation costs for the years covered by the agreement.

KPMG is ready to support you by preparing robust, contemporaneous TP documentation in line with the new APA guide. We can assist with managing the entire APA process, ensuring timely submission, and helping you secure certainty regarding your TP arrangements for material intercompany transactions.

Please do not hesitate to reach out for further assistance.

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