Singapore Institute of ACCREDITED TAX PROFESSIONALS

Technical Group Discussion

Cross Border Taxation

Are you gingerly crossing borders amidst a tax ocean of sharks?

25 January 2013, Friday

Facing a room packed with experienced tax consultants, finance heads and public sector staff, *Accredited Tax Advisor (Income Tax and GST) Mr Goh Bun Hiong shared his valuable experience on cross border tax issues.*

Venturing overseas has never been an easy task for businesses. With hidden tax exposures aplenty, businesses need to proactively monitor and manage the tax risk closely when managing for cross border transactions.

Accredited Tax Advisor (Income Tax and GST) Mr Goh Bun Hiong, Tax Director of PKF-CAP LLP, shed light recently on the pitfalls and blind spots that one needs to take note of when crossing borders.

Bun Hiong then shared his thoughts on features of best-in-class tax functions companies may adopt to manage the tax risks of an organisation.

Business structures are adapting to current business climate

An international organisation may typically comprise a group headquarters supported by country heads who are in turn assisted by in-country functional teams. While this structure may still work for many organisations, there are also businesses which are changing their business structures (as shown in Diagram 1) to optimise the value chain, amongst other reasons.

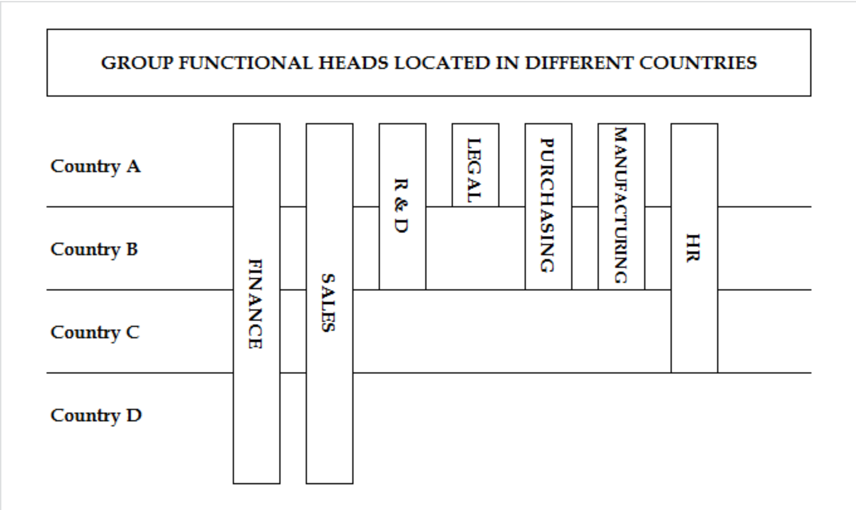

Diagram 1: Companies have re-organised their global operations to optimise the value chain amongst other reasons.

Organisations may unknowingly face a myriad of business issues which have tax implications

Staff movement results in broader tax implications

With businesses restructuring as such, employees may be sent to their overseas offices for various assignments. Businesses are generally aware that this may result in personal tax issues for the organisation.

However, sometimes it may not be simply a case of personal tax issues. Organisations need to take into consideration if the activities undertaken by the employee are significant enough to trigger foreign taxation.

Source of profits must be determined

As businesses expand overseas, profits may be attributed to Singapore from an accounting perspective. Business owners may conveniently assume that if profits are accounted for in Singapore, taxes are then paid in Singapore. This is a wrong assumption.

The source of profits must be determined when managing cross border taxes. Companies may be accounting for their profits in Singapore. However, if the foreign tax authority deems the income earned is derived from business activities done in its country, the company is likely to be taxed on the income even if there is no office set-up in the country.

Permanent Establishments (PEs) issues must be managed

Businesses are said to have a PE in a country when some level of business activities are undertaken in that country which cannot be disregarded as incidental. For example, a company's salesperson, who flies into Country A to negotiate and conclude a contract with a local supplier, may be deemed to have a PE in Country A, even if there is no office presence in that country as tax deals with the substance and not the form.

Conversely, even if businesses have assets located in a country, it does not necessarily mean that these businesses have a taxable presence in that country. A foreign organisation may, for example, have a warehouse in Singapore. If the warehouse is solely used to maintain a stock of goods for the purpose of storage, display or delivery of goods, such a presence may not be sufficient to trigger tax liabilities.

In essence, when a company is deemed to have a PE in the foreign country, the foreign tax authority will tax based on the amount of profits attributable to the PE, regardless of whether the company has an office there. The amount of profits in turn is usually dependent on the extent of the business activities done in that country.

<u>Goods and Services Tax (GST) is often forgotten in PEs</u>

Even if there is no profit attributable to a PE, it does not automatically imply that the company does not have other tax obligations. Companies often forget there is GST (or value-added tax as known in other countries) to be accounted for. While the PE may have made a loss, GST obligations might have been triggered in the course of its supply activities.

<u>Tax myths in split payrolls should be debunked</u>

When companies send their employees abroad, many split the payrolls of these employees between the Singapore and overseas offices. With Singapore having one of the lowest tax rates, companies often assume that by splitting the payroll, they can save on taxes as only part of the payroll will be apportioned to the overseas office.

Tax authorities however generally ignore how payroll is divided between the two countries. If the employee is essentially only performing his duties for the overseas office, the overseas tax authority will consider the entire remuneration and tax accordingly.

<u>Resolution of tax audit in one country has tax implications elsewhere</u>

Companies need to bear in mind the broader picture when managing tax authorities in various countries as companies cross borders. For example, when queried, companies may choose the easy way out and accept a particular tax authority's adjustment. However, the company replicates the same business model across the various jurisdictions and another tax authority may, upon receipt of the requested documentation, make reference to the tax adjustment made by the former tax authority and apply an identical tax treatment. Organisations are then stuck in a difficult position.

With the above issues coupled with challenging economic conditions which have led to falling revenue, tax authorities have progressively focused on these 'grey areas'. Transfer pricing and PEs tax risks continue to haunt corporations if these are not managed well. What can be done to manage these murky waters organisations thread and avoid being caught off-guard?

With over 18 years of tax experience in both consultancies and multi-nationals, Bun Hiong then went on to share on best practices companies should adopt to best manage taxes across jurisdictions as they expand.

Participants leveraged on the opportunity to network during tea break and get to know their peers as well as business leaders who were amongst the audience.

Monitoring systems should be in place to track key information

As companies expand across jurisdictions, companies should put in place systems to keep track of key factors. These include the following:

i) When each country was last audited
In some countries, companies are audited on a rotational basis. It is important to know which countries would be audited in each year and be ready for the audit.

ii) When the various filings are due and whether the returns have been filed
Organisations, at the group level, should have headline knowledge of the various filing dates of each jurisdiction and the corresponding tax amounts.

iii) What, if any, were the deviations and the resulting resolutions
Management at the group level need to be aware of the deviations and how these were resolved because, as mentioned above, the resolutions may have repercussions for the rest of the entities in the group.

Tax should be part of the strategic planning process

Companies tend to approach the in-house tax department or their tax agents to seek advice on minimising tax payments after the business direction is set. Tax is perceived to be a compliance function.

This needs to be changed. Tax should be a facilitator and not a policing department.

The tax function should be based at the group level as part of the Group Chief Financial Officer's (CFO) office and headed by an appropriate senior tax practitioner so as to effectively contribute in the business strategy formulation process right from the start and provide advice on tax implications.

For example, a business decision to open a factory in a certain country due to availability of labour may reflect a different conclusion when reviewed from a tax perspective. Once a strategic business decision is implemented upon, there is little that the tax department can do to avoid tax liability, except to possibly minimise it.

Periodic reporting on key areas must reach the Group CFO

A tax control framework should be designed to enable periodic reporting of key information and risks, and highlight these to the Group CFO. For example, the tax department should have information across the board on the tax holidays and their expiry dates, the deferred tax implications as well as tax positions taken in each country which may have resulting impact at the group level.

Tax reporting should be reviewed with other parts of Group's financial reporting

With key information reported to the Group CFO, these should be collated and reviewed with other parts of Group reporting such as cash flow forecasting in order for businesses to proactively plan to minimise any unnecessary complications.

Direct meetings with local tax consultants are important

Group CFOs should make the effort to meet up with the local tax agents advising the organisation during his trips to the various overseas offices. The tax consultants will be able to offer an unbiased view of issues.

In short, the tax department should not be seen as a fix-it department. Companies need to proactively invest in a tax department to prevent future complications.

The session ended with SIATP thanking Bun Hiong for generously sharing the many anecdotes he had experienced in cross border taxation as he explained the various points.

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About SIATP's Technical Discussions

SIATP's technical discussions have continually been very well received by accredited tax professionals. Unlike the run-of-mill Continuing Professional Educational courses which typically cover tax fundamentals, SIATP's interactive technical discussions are designed to cover tax issues that do not have clear-cut solutions or situations that may have different interpretations. Over time, these discussions contribute in boosting the overall tax standards in Singapore.

About Mr Goh Bun Hiong

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Bun Hiong's career started in 1994 with Arthur Andersen Singapore where he was involved in tax compliance and advisory work. Subsequently, he joined the Asia Pacific headquarters of the Philips Electronics Group and was part of the pioneer team supporting the conglomerate's growing interests in the region. In addition, Bun Hiong was also involved in various high profile merger, acquisition and spinoff deals with LG, Taiwan Semiconductors, and Lucent, amongst others.

Bun Hiong has been the Tax Director of PKF-CAP LLP since October 2011. With over 18 years' of experience, his diverse tax expertise spans many areas, including dispute resolution, incentive and investment negotiations, risk exposure management, and transfer pricing management.

This technical event commentary is written by SIATP's Senior Manager, Ms Joanna Wong. A brand specialist with over 15 years of experience in various multi-nationals as well as the public sector, she now leads the SIATP secretariat team in initiatives to achieve SIATP's mission of promoting excellence in tax standards and professional conduct of tax specialists in Singapore.