UPnC: Serving Internationalising Clients

Be a Head Above Complex International Taxation Issues

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As companies internationalise and engage in cross-border transactions, they are often unaware that their actions may have tax consequences that could derail their plans. Tax advisors have to be sharp, especially in this era of rapid international tax changes, to understand all the relevant tax issues and advise their internationalising clients.

At a recent *Up Close and Personal with Tax* session, Accredited Tax Advisor (Income Tax and GST) Professor Sum Yee Loong, Board Member of the Singapore Institute of Accredited Tax Professionals, shared his vast experience on the subject. Through various business scenarios, Prof Sum demonstrated the art of critically evaluating and logically deriving solutions to international tax issues.

One key concept in international taxation is Permanent Establishment (PE). PE is used to allocate the taxing rights in situations where a company of one state derives business profits from another. Such business profits will generally be taxed in the other state to the extent that they are attributable to a PE there. It should be noted that PE only applies to business profits. As such, if an income (such as royalty or dividend income) is not a business profit, it will be irrelevant to consider PE in determining its taxability.

There are several types of PE (such as physical PE, construction PE and agency PE), each having its own conditions. The presence of each type of PE should be separately considered to ascertain the tax implications.

While the definition of PE can be found in the Income Tax Act (ITA) and the Double Taxation Agreements (DTAs) signed between Singapore and its treaty partners, it is important to note that the exact phrasing and conditions may differ in each DTA. It is thus critical for tax advisors to always check the exact phrasing in the ITA or the applicable DTA when considering the presence of PE.

The following cross-border issues were discussed at the session.

Management Services

An overseas holding company (HCo) provides management services to its Singapore subsidiary (SSub) by sending a management staff to Singapore for a few days each month. SSub pays a management fee to HCo for the management services performed in Singapore. HCo does not provide any other service to SSub.

In analysing HCo's Singapore tax implications, the tax advisor should first consider whether HCo is taxable in Singapore under the country's domestic tax law provisions. Based on Section 12(7)(c) of ITA, the management fee paid to HCo is deemed to be derived from Singapore as the management services are performed in Singapore. Accordingly, SSub is required to withhold tax on its payment to HCo.

Once it is established that HCo is taxable in Singapore under domestic tax law provisions, the tax advisor should then consider whether Singapore has a DTA with the country where HCo is a resident.

If so, the management fee should only be taxable in Singapore to the extent that it is attributable to a PE in Singapore. This is on the proviso that there is no standalone article in the DTA. In other words, if HCo does not have a PE in Singapore, the management fee will not be subject to tax in Singapore and SSub will not be required to withhold tax on its payment to HCo.

A key takeaway is that while DTA may override domestic tax law provisions to provide double taxation relief, it does not by itself impose tax. Hence, if no tax is imposed under domestic tax law provisions, there is generally no need to apply the provisions of the DTA.

RENDERING OF SERVICES

A Singapore incorporated and resident company (SCo) has a wholly-owned subsidiary (Sub) incorporated and resident in Country A. An employee of Sub occasionally supports SCo and works in Singapore. There is a DTA between Singapore and Country A.

The evaluation of the Sub employee's taxability in Singapore should start with an analysis of Singapore's domestic tax law provisions. Generally, the Sub employee will be regarded as a Singapore tax resident if he stays or works in Singapore for at least 183 days in a calendar year or for a continuous period of at least 183 days spanning two years, or continuously for three consecutive years. However, he will still be taxed on all employment income earned in Singapore as a non-resident if he stays or works for less than 183 days. If his exercise of employment in Singapore does not exceed 60 days in the year, his employment income will be exempt from tax in Singapore.

If the Sub employee's income is taxable in Singapore under domestic tax law provisions, the tax advisor should then consider whether the employee may obtain a double taxation relief under the DTA.

Generally, the employee will be exempt from Singapore tax if his exercise of employment in Singapore does not exceed 183 days in a 12-month period, he is paid by an overseas employer resident in the other treaty country and his emolument is not borne by a PE or fixed base that the employer has in Singapore.

WAREHOUSING

A Singapore resident company (SGCo) is in the business of manufacturing electronic products. SGCo stores its raw materials in its warehouse in Country B, but does not otherwise perform any activities in Country B. There is a DTA between Singapore and Country B.

Generally, activities that are preparatory or auxiliary in character are specifically excluded and will not constitute a PE under Singapore's DTAs. As such, the mere storage of goods in its warehouse should not create a PE for SGCo in Country B.

However, if SGCo is in the business of online sales and its warehouse in Country B acts as its regional distribution hub, its warehousing activity in Country B may no longer be considered as "preparatory or auxiliary" in character, but will instead constitute a key business activity for the company. Consequently, the warehousing activity of this online entity may now create a PE for SGCo in Country B.

SIATP's Up Close and Personal with Tax session saw board member Accredited Tax Advisor (Income Tax & GST) Professor Sum Yee Loong facilitating an engaging session on international tax issues.

INDIVIDUAL WORKING OVERSEAS

A regional tax director of a Singapore resident company frequently travels to regional countries to oversee the tax matters of its subsidiaries, spending less than 183 days in Singapore in a year. As part of his role as a regional tax director, he spent in Malaysia an aggregate of 30 days and 200 days in 2014 and 2015 respectively. The regional tax director is a Singapore citizen.

Notwithstanding that he spent less than 183 days in Singapore in a year, the regional tax director should be fully taxable in Singapore in 2014 as his business travels are incidental to the performance of his Singapore employment. As he had only spent 30 days in Malaysia in 2014, he should not be taxable on his short-term employment income in Malaysia.

In 2015, the regional tax director will not qualify for the exemption for short-term employment income as he had spent 200 days in Malaysia. As such, his employment income for the 200 days should be taxable in Malaysia. The same income should not be taxed in Singapore.

AGGRESSIVE CLIENTS

A multinational corporation (MNC) approaches a local tax advisor to conduct a transfer pricing study. At the end of the transfer pricing study, it was found that the MNC's transfer price for a particular transaction is significantly lower than other comparable transactions. Instead of adjusting its transfer price, the MNC requests that the tax advisor revises the results to ensure that its transfer price is within range. The MNC is a substantial client of the tax advisor.

The tax advisor may want to first review the transfer pricing study to ensure technical accuracy. If the tax advisor is confident of the validity of the transfer pricing study, it is important to highlight that a revised transfer price may not stand up to scrutiny by the tax authorities. From an ethical standpoint, it is also imperative that the tax advisor stands firm to his work and explains to the client why the results cannot be revised. As a tax professional, he has an obligation to uphold professional and ethical standards. The client will generally also be pleased to note that his tax advisor is able to provide independent and objective professional advice.

International taxation is dynamic and ever-evolving. Change is the only constant. Companies need to be mindful of the potential tax consequences which could derail their internationalising plans. If you are planning to venture abroad but are unsure of the potential tax implications, you may want to call up an accredited tax professional. You could just avoid a landmine… or two.

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