Corporate Tax

2017

Fifth Edition

Consulting Editor:
William Watson

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Singapore

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Overview of corporate tax work over last year

The tax practice in WongPartnership LLP is one of the leading tax practices in Singapore. We collaborate with the firm's other practices to holistically provide advice to clients through the entire spectrum of tax-related issues, including tax planning and advice, corporate and international tax, stamp duties, goods and services tax and property tax. We also advise on tax issues arising in debt financing, restructuring, swaps, funds, securitisations and real estate deals. Quite often, these transactions involve novel structures and issues.

Over the past year, our tax practice has been involved in multiple award-winning deals including acting for CMA CGM S.A. in its acquisition of all the issued and paid-up ordinary shares in the capital of Neptune Orient Lines Limited. This acquisition was awarded the "M&A Deal of the Year (Premium)" at ALB SE Asia Law Awards 2017. We also advised Broadcom Corporation in relation to Singapore tax aspects in its US$37 billion acquisition by Avago Technologies Limited. This acquisition was awarded the "M&A Deal of the Year (Premium)" and "Deal of the Year" at ALB SE Asia Law Awards 2016. We also acted for Tata Communications in the sale of a 74% stake in Tata Communications' data centre business in India and Singapore worth approximately US$640 million to ST Telemedia. The deal was awarded "M&A Deal of the Year" by Indian Business Law Journal 2016.

On the litigation front, we also acted for a leading shipbuilding company in a tax appeal before the Income Tax Board of Review in relation to the deductibility of facility fees incurred for obtaining banking facilities.

Key developments affecting corporate tax law and practice

<u>Domestic – cases and legislation</u>

AXY and ors v. CIT [2017] SGHC 42

The case of *AXY* is a recent Singapore High Court decision which discusses the obligations of the Singapore Comptroller of Income Tax ("Comptroller") under Singapore's exchange of information ("EOI") regime in dealing with requests by foreign tax authorities for protected information from financial institutions. In particular, *AXY* involved an application to commence judicial review of the Comptroller's decision to issue notices to various banks seeking protected information after receiving such a request from a foreign tax authority. In *AXY*, the Singapore High Court had to consider whether the applicants could establish an arguable case of reasonable suspicion that the Comptroller's decision was either illegal or irrational.

Prior to amendments to the Singapore Income Tax Act ("SITA") in 2013, the Comptroller had to apply to the High Court for an order to issue such notices seeking protected

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information. The High Court had to be satisfied that certain requirements were met before the application would be granted. However, in 2013, this requirement for a court order was removed, thus vesting significant control over such matters in the Comptroller. The High Court in *AXY* was of the view that these legislative amendments merely changed the identity of the authority assessing the EOI requests from the judiciary to the Comptroller, while the legal requirements for exchange of information did not change. As a result, the Comptroller would be the authority extending the same safeguards over taxpayers' interest in confidentiality when dealing with such requests.

Under section 105D of the SITA, the Comptroller would have to be satisfied that the foreign tax authority's request for information, firstly, complies with the requirements set out in the Eighth Schedule of the SITA and, secondly, concerns information foreseeably relevant to the administration or enforcement of the relevant double taxation treaty or the requesting state's tax laws.

The applicants in *AXY* argued that the Comptroller had acted illegally in issuing the notices to the banks as he failed to make sufficient prior inquiry into the compliance of the foreign tax authority's request with the requirements under section 105D. However, the High Court held that in determining whether the section 105D requirements were met, the Comptroller was entitled to take the statements and information provided by the foreign tax authority at face value and did not have to second-guess their veracity.

Based on the court's decision in *AXY*, it appears that the Comptroller only has to cross a low threshold in order to fulfil his obligations in response to a request for information by a foreign tax authority. The court's role in this process is limited as well – the court would only examine the Comptroller's decision-making process and not the substantive decision itself, and would refrain from substituting the Comptroller's decision with its own view of how best to exercise discretion when a request for protected information is received.

GBG v. The Comptroller of Income Tax [2016] SGITBR 2

This case involved the issue of whether certain payments made by the taxpayer GBG to financial institutions were deductible under Singapore's general deduction formula under section 14(1) of the SITA. The general deduction formula allows the deduction of "all outgoings and expenses wholly and exclusively incurred … in the production of income". However, this is subject to certain restrictions. One of the restrictions, which is provided for under section 15(1)(c) of the SITA, states that the outgoings or expenses must not be capital in nature.

The payments made by GBG were for three facility agreements which were entered into with various financial institutions. The first was a term loan facility agreement to fund capital expenditure and general working capital requirements. The second was a term loan facility agreement for general corporate funding and the third was a revolving facility agreement to serve as standby funds to finance any funding shortfall for GBG's expansion project. GBG argued that the payments were made for the purposes of its business looked at as a whole set of operations directed toward producing income, with the object of conducting its business on a profitable basis, and were wholly and exclusively incurred in the production of income. There were in the event no drawdowns under these facility agreements, and GBG argued that the payments were made for the short-term benefit of having access to the loan facility during a contractual period of three years or shorter. Additionally, GBG argued that the payments were not capital in nature.

To determine whether the payments were deductible, the Singapore Income Tax Board of Review ("SITBR") first considered whether they were capital in nature, and thus prohibited

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from deduction. The SITBR applied the approach taken in the Singapore Court of Appeal decision of *Comptroller of Income Tax v. IA* [2006] 4 SLR(R) 161 to distinguish between revenue and capital expenses. In *IA*, the Court of Appeal stated the approach to be as follows:

(a) One should first ascertain the purpose of the taxpayer in entering into the loan, i.e. whether it was for the purposes of revenue or for the purposes of capital. In order to ascertain such a purpose, a reasoned approach would include the relevant steps in (b) to (d) below.
(b) One ought to ascertain, first, whether a sufficient linkage or relationship exists between the loan and the main transaction or project for which the loan was taken.
(c) If, in (b) above, no, or an insufficient linkage is established, the purpose of the loan must, *ex hypothesi*, be merely to add to the capital structure of the taxpayer and is therefore capital in nature.
(d) On the other hand, if in (b) above, a sufficient linkage is established, one must then (and secondly) proceed to ascertain whether the main transaction is of a capital or of a revenue nature. If it is of a capital nature, then (given the linkage to the loan) the loan is also of a capital nature. If on the other hand, the main transaction is of a revenue nature, then (once again, given the linkage to the loan) the loan is also of a revenue nature. In the nature of things, the process outlined here necessarily involves a consideration of the purpose of the main transaction and is also factual in nature.

The SITBR concluded that the payments were capital in nature and there was no evidence pointing otherwise. The STIBR also held that the payments were incurred to augment the taxpayer's funding and capital structure and therefore were not revenue in nature. The taxpayer's appeal was therefore dismissed.

GBK v. The Comptroller of Income Tax [2016] SGITBR 3 and BML v. Comptroller of Income Tax [2017] SGHC 118

These two cases, the former at the SITBR and the latter on appeal to the Singapore High Court, considered the issue of deductibility of interest expenses incurred by the taxpayer GBK on certain fixed rate subordinated bonds.

The SITBR considered the interplay between the prohibition of deduction of capital expenses under section 15(1)(c) of the Singapore Income Tax Act, and the specific deduction provision under section 14(1)(a) allowing deductions for interest payable on capital employed in acquiring income. Section 14(1)(a), specifically, provides that "any sum payable by way of interest upon any money borrowed by that person where the Comptroller is satisfied that the interest was payable on capital employed in acquiring the income", is deductible.

The SITBR held that even though capital expenditure is not a deductible expense pursuant to section 15(1)(c), it will be deductible so long as section 14(1)(a) is satisfied. However, to avail itself of section 14(1)(a), GBK had to show that there is a direct link between the proceeds from the issuance of the bonds and the acquiring of GBK's income. The SITBR found that GBK's income was derived independent of the issuance of the bonds. The issuance of the bonds was found to have been undertaken voluntarily, and partially for GBK's shareholders to obtain a return in the form of interest rather than dividends. As there was no "direct link" to constitute an exception to the prohibition under section 15(1)(c) of the SITA, the taxpayer's appeal was dismissed.

On appeal (the same taxpayer GBK was renamed BML for the purposes of the case report), the Singapore High Court upheld the SITBR's judgment. The High Court agreed with the SITBR that to avail oneself of section 14(1)(a), the taxpayer has to establish a direct link

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between the money borrowed and the income produced. Moreover, there has to be a close relationship between these two items, and the money borrowed has to be instrumental in acquiring the specific income against which the deduction is sought. The High Court went on to state that the direct link "has to be real, tangible, precise, and factual, and this requires the consideration of a number of factors, which includes but is not limited to whether the original source of income … can be said to be the same source as the income against which a deduction is now sought".

For completeness, the High Court also held that section 14(1)(a) gives the Comptroller discretion in deciding whether or not a direct link exists between the money borrowed and the income produced, and how much deduction should be allowed to the taxpayer.

BEPS

Standard for Automatic Exchange of Financial Account Information in tax matters

In connection with Singapore's implementation of the common reporting standard ("CRS"), Singapore ratified the Convention of Mutual Administrative Assistance in Tax Matters ("MAATM") on 20 January 2016. Doing so expanded Singapore's network of partners for the exchange of information and prescribed the methods through which such exchanges can be performed. These methods include the exchange of information on request, automatic or simultaneous exchange of information, simultaneous tax examinations and tax examinations abroad. Singapore enacted legislation implementing the CRS on 1 January 2017. The CRS, being an internationally agreed standard for the automatic exchange of financial account information, includes provisions on the documentation, due diligence and reporting standards which financial institutions in adopting countries are required to implement. As at 12 June 2017, Singapore has concluded 23 bilateral competent authority agreements ("CAAs"). The CAA is an agreement which countries intending to adopt the CRS are required to sign. It specifies the type of information to be exchanged between two jurisdictions, the time and manner of exchange, and the confidentiality and data safeguards to be respected. Singapore-based financial institutions have to provide the IRAS with the financial account information of an account held by a tax resident of the jurisdiction with which Singapore has concluded a CAA.

Country-by-country reporting

Acting on Singapore's commitment to implement some of the measures under the OECD's Base Erosion and Profit Shifting ("BEPS") Action 13 Report, the Singapore Parliament has amended the Singapore Income Tax Act to confirm the implementation of country-by-country reporting. Under the new requirements, the ultimate parent entity of a Singapore multinational enterprise will be required to file a country-by-country report for all entities in the group. This report should be submitted to the Singapore tax authorities within 12 months from the end of the ultimate parent entity's financial year. The multinational enterprise group is required to file a country-by-country report if the following conditions are met:

1. the ultimate parent entity is a Singapore tax resident;
2. the consolidated group revenue in the preceding financial year is at least S$1,125m; and
3. the group has subsidiaries or operations in at least one foreign jurisdiction.

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("the Multilateral Instrument")

Joining more than 100 countries, Singapore signed the Multilateral Instrument on 7 June 2017. The Multilateral Instrument seeks to facilitate the implementation of measures to counter BEPS by allowing the efficient updating of DTAs between countries which are

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signatories to the Multilateral Instrument. This approach avoids the need to re-negotiate each DTA. These measures include BEPS minimum standards on preventing treaty abuse and enhancing dispute resolution.

Developments affecting attractiveness of Singapore for holding companies

The Mergers & Acquisitions Scheme

The Mergers & Acquisitions scheme ("M & A Scheme") was first introduced in 2010 to encourage companies to consider mergers and acquisitions as a strategy for growth and internationalisation. The M & A Scheme was extended and refined in 2015, providing for the following:

- An income tax deduction based on 25% of the value of the qualifying acquisition, subject to a cap of S$20m on the value of qualifying acquisitions per year of assessment. This allowance is written down over five years.
- Stamp duty relief on the transfer of unlisted shares, capped at S$20m of qualifying merger and acquisition deals.
- 200% income tax deduction on transaction costs (which includes due diligence costs, legal and valuation fees) incurred on the qualifying merger and acquisition deal, subject to an expenditure cap of S$100,000 per year of assessment, which is written down in one year.

To be a qualifying acquisition, the M & A Scheme requires acquiring companies to acquire ordinary shares in a target company, whether directly or indirectly, that results in the acquiring company holding:

(a) at least 20% ordinary shareholding in the target company (if the acquiring company's original shareholding in the target company was less than 20%); or
(b) more than 50% ordinary shareholding in the target company (if the acquiring company's original shareholding in the target company was 50% or less).

The M & A Scheme was enhanced following the 2016 Singapore Budget Statement. In particular, the following changes were made:

- The cap on the value of qualifying acquisitions for the M & A Allowance per year of assessment for the 25% income tax deduction was revised from S$20m to S$40m.
- Stamp duty relief on the transfer of unlisted shares was correspondingly capped at S$40m on the value of qualifying merger and acquisition deals.

Extension of the income tax exemption on companies' gains on disposal of equity instruments

Under section 13Z of the SITA, the gains derived from a company from the disposal of ordinary shares it legally and beneficially owns in another company are exempt from income tax if the following conditions are met immediately prior to the date of share disposal:

- the divesting company holds at least 20% shareholding in the company whose shares are being disposed of; and
- the divesting company maintained at least 20% shareholding in the company whose shares are being disposed of for a continuous minimum period of 24 months prior to the disposal.

Prior to the Singapore Budget Statement 2016, the section 13Z exemption applied to such disposals occurring between 1 June 2012 and 31 May 2017, both dates inclusive. Following the Singapore Budget Statement 2016, this tax exemption has been extended to include disposals occurring up to 31 May 2022.

Refining the Finance and Treasury Centre Scheme

The Finance and Treasury Centre Scheme ("FTC Scheme") grants a concessionary tax rate of 8% for qualifying income derived by an approved Finance and Treasury Centre ("FTC")

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from qualifying activities carried out on its own account and services provided in Singapore to its approved offices and associated companies. Additionally, an approved FTC can avail itself of withholding tax exemptions on interest payments on certain loans if the funds are used for the approved qualifying activities or services.

To qualify for the FTC Scheme, a company must establish substantive activities in Singapore and perform strategic functions. These activities include, but are not limited to, the following:

- control over the management of cash and liquidity position;
- provision of corporate finance advisory services;
- management of interest rate, foreign exchange, liquidity and credit risks; and
- overall business planning, investment research and analysis.

A company will also be assessed on various quantitative and qualitative aspects of the proposed FTC operations, such as the employment created, total business expenditure and the scale of the FTC operations.

Following the Singapore Budget Statement 2017, the qualifying counterparties for certain transactions of approved FTCs will be streamlined to ease the compliance burden of approved FTCs. The change will apply to new or renewal awards of the FTC status approved on or after 21 February 2017.

The year ahead

There is increasing focus on BEPS and transfer pricing by the Singapore tax authorities. In their latest transfer pricing guidelines issued in January 2017, the Singapore tax authorities have explicitly reiterated their position that "profits should be taxed where the real economic activities generating the profits are performed and where value is created". The implementation of country-by-country reporting is also consistent with Singapore's intent to comply with the BEPS Action 13 Report. This is hardly surprising in light of the global movement to combat BEPS issues.

By signing the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, Singapore also signals its strong support for the principle that profits should be attributable to the jurisdiction where there are substantive economic activities. This Multilateral Instrument allows Singapore to quickly update its treaties to internationally agreed standards without the need for re-negotiating each tax treaty separately.

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He has been admitted as a Fellow of CPA Australia and the Singapore Institute of Arbitrators. He is a Chartered Tax Adviser with The Tax Institute, an Accredited Tax Adviser (Income Tax) with the Singapore Institute of Accredited Tax Professionals (SIATP) and also a member of the International Fiscal Association. Kay Kheng's professional service includes being a divisional councillor of CPA Australia and a board member of the Tax Academy of Singapore and the SIATP. He has taught as Adjunct Faculty at the School of Law, Singapore Management University, and serves on the Inquiry Panel and the Disciplinary Tribunal Panel for the legal profession. At the Law Society of Singapore, he serves as Vice-Chairman of its Compensation Fund Committee and as a member of its AML Committee.

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