

Light at the end of the tunnel?

Our early observations on the finalisation of the OECD BEPS Project and what it means for Singapore

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The Organisation for Economic Co-operation and Development (OECD)'s Base Erosion and Profit Shifting (BEPS) Project came to a close on 5 October 2015, where the OECD released their final recommendations. A number of these recommendations have significant implications on Singapore's open economy – in particular those relating to Singapore's tax incentive regime and our regional hub position. In this newsletter, we consider how some of these recommended changes to fundamental key principles around tax treaty access, transfer pricing and transparency impact Singapore.

The topics covered are:

- The need to rethink Singapore's platforms for dispute resolution
- Our tax treaty framework:
- Singapore's incentive regime
- Increased tax transparency
- How the tax function will need to evolve.

Background

Tax systems around the world have evolved in various forms from tax principles established close to a hundred years ago. Given international trade growth and changes in how business is conducted the OECD launched the BEPS Project with an ambitious timeline of 2.5 years to come up with a comprehensive action plan with 15 Actions to help tax principles keep pace.

2.5 years after the launch, on 5 October 2015, the OECD released the final reports¹ for all the various actions identified in the OECD BEPS project as well as a plan for any additional follow-up work, including an implementation timeline. Despite the original scepticism around the timelines and ability to achieve consensus on such a broad range of topics, these final recommendations reflect consensus of the participating countries on the major principles identified by the OECD BEPS project. These were presented to the G20 Finance Ministers meeting on 8 October in Lima, Peru and followed by the G20 Leaders Summit in November 2015 in Antalya, Turkey.

What it means for Singapore

Our tax system is based on principles of substance, fair play and rule of law. We remain attractive to Multi-National Enterprise (MNE) investors because of the fundamentals of our nation. Given the need for continuing international trade we remain hopeful the BEPS recommendations will continue to promote growth and certainty, accord proper recognition of substance and allow for fair competition.

This is also echoed by Singapore's Ministry of Finance (MoF) communication of 6 October 2015, which welcomed the BEPS recommendations. Singapore believes that the sound implementation of the BEPS principles, with broad acceptance by tax jurisdictions globally, will help foster free and fair economic competition manner with participation on an equal footing by all relevant tax jurisdictions."

¹ Please note that while 15 Comprehensive Action Plans were identified by the OECD, only 13 reports were finally issued. This was due to the fact that 3 transfer pricing related action plans have been consolidated into one report.

Our early observations of the key implications to Singapore are outlined below

1. Double taxation as the new norm

Singapore strives on international trade. Having a level playing field and the avoidance of double taxation are paramount. With the current focus on clamping down on tax practices that are not consistent with economic substance, Singapore should not be impacted but there is still concern that countries are taking uncoordinated actions to address these tax practices. This is where double taxation can occur. It is hoped that in implementing the OECD's BEPS recommendations, countries do not introduce measures that impede trade flows enshrined in international agreements such as the Trans-Pacific Partnership.

The OECD's recommended measures have provided more tools for tax authorities to clamp down on aggressive tax practices. Singapore enterprises going abroad will very likely expect more uncertainty in this new environment, as these measures are likely to be subject to differing interpretations internationally.

While the OECD has taken much effort to build consensus in the BEPS project, the raft of measures is likely to result in increase in cross border tax disputes. Thus, it is timely for Singapore to consider providing for arbitration² in our tax treaties to help resolve double taxation.

2. Treaties - Refresh existing/ New

With the introduction of higher minimum standards in treaty access, the BEPS Action Plan will dramatically alter the landscape in international tax. There is thus a greater impetus for Singapore to re-look at its existing treaty framework to preserve and enhance its competitive positioning. While on the subject of tax treaties, the absence of a tax treaty between Singapore and the United States (US), which is still the world's economic powerhouse, remains its Achilles heel both in MNEs positioning Singapore as a global hub and for Singapore enterprises' expansion in the world's largest single developed market.

3. Review of incentive regime

While the OECD has sought to establish the yardstick for preferential tax regimes to be supported by substantial (economic) activity we should take confidence from Singapore's tax regime which has always demanded substance to qualify for incentives.

Singapore's incentive regime will continue to support businesses as long as there is appropriate substance backed by arm's length arrangements. In summary, Singapore's incentive regime generally conforms with OECD's guiding principles. However, Singapore should continue the effort to refine its incentive regime³ to remain relevant in the changing world, and dispel any misconceptions. This is reiterated by the Finance Minister Heng Swee Keat, who said that "Singapore supports an inclusive monitoring mechanism that is conducted in a fair, open and objective

² Arbitration, a form of alternative dispute resolution (ADR), is a technique for the resolution of disputes outside the courts. In Singapore, arbitration is already used to settle commercial disputes. Within the tax community, some territories outside Singapore (e.g., in the US and European Union) have already implemented legislation to enable arbitration in situations where tax disputes have not been resolved under the Mutual Agreement Procedures (MAP) as part of tax treaties.

³ This is generally aligned with Singapore's 2015 Budget which announced a periodic review and phasing out of tax concessions so that Singapore's incentive regime continues to remain relevant to the international tax environment. As examples, the Approved Royalties Incentive and the Approved Foreign Loan incentives, amongst others, have been identified for periodic reviews. As a result, the Operational Headquarters Incentive (under Section 43E of the Income Tax Act (ITA)), the 10% concessionary tax treatment for offshore leasing (under Section 43I of the ITA) and the concessionary treatment for royalties and other intellectual property related income (under Section 10(16) of the ITA) are being phased out.

4. Increased compliance yardstick through tax transparency

The OECD has reaffirmed new tax transparency requirements, which will raise the compliance yardstick globally. If Singapore adopts these new standards, affected MNEs in Singapore will have to submit key financial and other information through a Country-by-Country Report (CbCR). This will provide an overview of the relevant Singapore-based MNEs' global profit allocation relative to their various operations and activities worldwide. The report facilitates the continuing focus on MNEs' transfer pricing and relative substance in assessing profit shifting. These MNEs should carefully assess their global tax footprint and transfer pricing profile with this new disclosure requirement.

5. Impact on tax functions

The impact of the BEPS recommendations on the tax functions of Singapore based companies is likely to be significant and multifold. Different interpretations, enforcement and administration of the BEPS recommendations by revenue authorities will inevitably lead to more tax disputes and increased compliance burdens (e.g. additional reporting and disclosures) will require more senior executives to focus on tax. In addition, a more strategic approach to tax is required than ever before, given increased stakeholder interest that will arise from greater transparency. This will include interest from tax authorities in Singapore and outside who will examine MNE's operations, structures, internal tax risk management, controls and compliance processes. Furthermore there will be continuing focus in the appropriateness of MNE's tax policies as austerity measures intensify.

Your PwC contacts

If you would like to discuss the impact of these developments on your group's affairs, please feel free to reach out to any of the facilitators or your local PwC Contact.

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