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Tax Lookout

An outlook on recent tax changes

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Foreword

Dear Readers,

Welcome to PwC Singapore's first edition of ***Tax Lookout***. There is no doubt that some people find dealing with tax (incorrectly in our view) a mind-numbing experience, so with this publication we are attempting to dispel that myth (and with it a number of others - see our Mythbuster article on page 14) and provide you with the lighter side of things while still keeping you up-to-date on what is going on in our tax world.

When I was a boy learning the tax ropes in (what was then) PW London, what made life fun and interesting, was getting into a good punch-up with the tax authorities. This was akin to trench warfare. Tax cases were your ammo. The Revenue would open up with some sniper fire. You would reply by slinging a case reference grenade over the top, hoping it would hit the target and blow their arguments to bits; but all too often a well-aimed grenade came flying back and took you by surprise. Fortunately, nobody died, but the exercise certainly sharpened your wits and in many cases ended in satisfying victory. Reading the cases was also fun. People did get up to some strange things.

So inevitably, and as this publication is meant to inform as much as entertain, we start with a number of recent tax cases heard in the Singapore courts. The first, and probably most alarming because of a throw-away one-liner (known in the trade as an obiter dictum) by the Judge, concerns the deductibility of costs associated with an issue of bonds.

The second concerns a lump-sum payment by a telecom provider and whether it was deductible. Not perhaps of direct interest in the context of the businesses of many of our readers, but it does reconfirm some old general principles of the capital versus revenue argument and gives a glimpse of the judiciary's take on it.

The third article deals with requests by foreign tax jurisdictions for information from Singapore in relation to the tax affairs of residents of that foreign jurisdiction, and how far the courts will go in acceding to requests. The general approach taken in these cases will have largely been superseded though by the removal of the need for High Court approval, the process now being left to the Inland Authority of Singapore to make their own judgement.

Then the lighter side. There is no doubt that there are some misconceptions out there about how Singapore tax works, and our Mythbuster article attempts to straighten some of these out. Last year we also had the pleasure of welcoming some newbies to the partnership rank, and we have produced a little article to help you get to know them.

Finally, yours truly has whipped up a cryptic crossword. The prize for the first 5 correct entries will be a free pass to our PwC Budget seminar on 28 February 2014 (see page 20). A real triple-whammy. Firstly, you will be able to show your boss how clever you are; secondly you will be saving your company money; and thirdly you get a great day of tax discussion and networking.

Enjoy!

David Sandison

Deductibility of costs associated with an issue of bonds

The judgment for *BFC v Comptroller of Income Tax* [2013] SGHC 169 (BFC) was published on 9 September 2013. In it, the High Court ruled that the tax deduction claims by the taxpayer for certain borrowing expenses incurred in respect of two bond issues should be disallowed.

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Background

BFC carried on the business of hospitality, investment holding and property investment. It owned and operated a hotel (the "Hotel") in the period concerned. In 1995 and 1996, BFC issued bonds (referred herein as the "1995 Bonds" and the "1996 Bonds", respectively, and collectively, the "Bonds"). The salient terms of both issues of Bonds and the usage to which the Bond proceeds are applied are summarised below:

	Discount on issue and/or premium on redemption	**Purpose(s) of bond issue**
1995 Bonds	Issued at a discount and carries a premium on redemption.	(a) Financing of the renovation of the Hotel; (b) The refinancing of existing borrowings of both BFC and its subsidiaries; and (c) As working capital for the business operations of BFC.
1996 Bonds	Issued at a discount to the principal value but does not carry a premium on redemption.	(a) The refinancing of existing borrowings of both BFC and its subsidiaries.

Basis for the Judgment

The High Court stated that the discounts on the issue and premium on redemption of the Bonds in 2000 and 2001 did not rank for deduction for the following reasons:

a) Discounts and redemption premium, while economically similar to interest, are not interest as they do not bear the fundamental feature of accrual with time. Accordingly, the discounts and redemption premium do not qualify for deduction under section 14(1)(a)[1] of the Income Tax Act (ITA);

[1] Section 14(1)(a) as it applied to the years of assessment concerned read: "For the purpose of ascertaining the income of any person for any period from any source chargeable with tax under this Act (referred to in this Part as the income), there shall be deducted all outgoings and expenses wholly and exclusively incurred during that period by that person in the production of the income, including —

(a) except as provided in this section, 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;"

b) As a consequence, the Courts have to be satisfied that a deduction is available under section 14(1) of the ITA. The judge first dealt with the issue as to whether the discounts and premium have been incurred by the taxpayer. Relying on Federal Commissioner of *Taxation v James Flood Pty Ltd*[2], she held that in redeeming the Bonds, the taxpayer had incurred actual outgoings and expenses within the requirements of section 14(1) of the ITA, overturning the Board of Review's decision that the discounts were not deductible as an expense or outgoing because no payment was made.

c) Next, the judge considered if the discounts and redemption premium were capital expenses and therefore prohibited from deduction under section 15(1)(c) of the ITA[3]. In arriving at her decision, Lai Siu Chiu J held that:

(i) Firstly, one needs to examine the purpose of the taxpayer in entering into the loan. In this case, the Bonds were issued to fund a hotel refurbishment project, to refinance existing borrowings of the taxpayer and its subsidiaries and to finance the day-to-day operations of the taxpayer as working capital;

(ii) There should be sufficient linkage or relationship between the loan and the main transaction or project for which the loan was taken. In this case, the judge found evidence that the Bonds were connected with each of the purposes stated in (i). It is worth noting that as the main Subscription Agreements for the Bonds did not specifically state the purpose of the Bond issues, the judge arrived at this finding based on her review of the other available evidence, i.e. it is a question to be determined based on the full facts and circumstances of the case;

(iii) Once the linkage was established, she proceeded to examine whether the main transaction(s) was of a capital or revenue nature.

Expenditure incurred in respect of hotel refurbishment was held to be capital expenditure since the hotel premises were a permanent asset of BFC.

The judge went on to consider whether the refinancing of the existing borrowings of the taxpayer and its subsidiaries was a transaction of a capital or revenue nature. Since the taxpayer was not in the business of financial operations and it could not be proven that these existing borrowings were for a revenue purpose, the refinancing transactions were capital in nature.

(iv) Finally the judge considered the third use to which the Bond proceeds were applied, i.e. the financing of the day-to-day operations of the taxpayer's business, and observed that the Bond proceeds went into a mixed pool of funds. Accordingly, the bond proceeds were held to have been raised for the general purpose of augmenting its capital structure.

Based on the above, the Bonds were found to be capital in nature. As a result, the discounts and redemption premium incurred in respect of the Bonds were also capital in nature and disallowed from deduction.

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[2] (1953) 88 CLR 492

[3] Section 15(1) (c) ITA provides that, "[n]otwithstanding the provisions of this Act, for the purpose of ascertaining the income of any person, no deduction shall be allowed in respect of…(c) any capital withdrawn or any sum employed or intended to be employed as capital…"

PwC's observations

a) The judge devoted a significant part of her judgment to settling what appears to be a straightforward matter – despite their economic similarities, discounts and redemption premium on debt financing are not to be treated as interest on a debt, at least for tax deduction purposes.

As the case dealt with the deduction of the discounts and redemption premium in 2000 and 2001, it should be recognised that the law has since been changed to allow certain prescribed types of borrowing costs (as which discounts and redemption premiums would qualify) which are paid in lieu of interest to rank for deduction with effect from the year of assessment 2008, subject to conditions. Therefore, although the BFC case provided clarity, this distinction would be of limited practical impact given the new legislative provisions.

The decision on the test for what amounts to the incurrence of an outgoing or expense is, however, much welcomed as it overturned the Board's decision that discounts cannot be deductible on the mistaken notion that there was no outgoing involved.

b) The judgment in the BFC case followed a series of cases on the deductibility of interest expenses and other borrowing costs from *JD Ltd v Comptroller of Income Tax*[4] (JD) to *Comptroller of Income Tax v IA*[5] (IA) and applied the framework for distinguishing capital from revenue expenses laid out in *ABD Pte Ltd v Comptroller of Income Tax*[6] (ABD).

Lai J made it clear that the Singapore Courts will follow the approach first set out in IA, where the determination as to whether a loan or other form of debt financing is of a revenue or capital nature will be based on the purpose of the borrowing. In ascertaining its purpose, one would look to the nexus between the borrowing and the main transaction to which the borrowing relates. Where such a nexus is established, the borrowing would take on the same characterisation as that for the main transaction.

c) The Court in BFC distinguished the purpose of the bond issues from the uses to which the proceeds were put, given its view that it is the former which will determine the capital or revenue character of the Bonds, not the latter.

In practical terms, the taxpayer's purpose in borrowing money may not differ from the actual use to which the borrowed money was put but in principle at least, it is entirely possible that a taxpayer (which is not engaged in the business of financial operations) may raise financing without a specific purpose in mind, i.e. for general funding purposes. Applying the principle set out in BFC, this would mean that the borrowing should be considered capital in nature and any associated borrowing costs would be capital in nature and not deductible, unless there is a clear change of the purpose.

It is not difficult to foresee the potentially adverse impact of such a ruling on taxpayers. Where the actual use of the loans does not correspond with the stated purpose, the IRAS and taxpayers are likely to find themselves engaged in arguments over the purpose of the borrowings. While there is no doubt about the primacy of the purpose test in ascertaining the revenue or capital characterisation of a transaction, it should be noted that the actual use to which the borrowed funds is applied may well reflect that there had been a change of purpose over time.

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[4] [2005] SGCA 52
[5] [2006] SGCA 24
[6] [2010] 3 SLR 609

d) The most alarming feature of this case however was Lai J's *dictum*[7]. In it, she stated unequivocally that the purpose test should apply to interest for which a tax deduction is claimed under section 14(1)(a) of the ITA, but did not elaborate on how this test is to be applied to loans taken to finance the purchase of capital assets that are employed to generate income. It should be noted that BFC is not the highest authority in Singapore on the deductibility of interest and borrowing costs under section 14(1)(a), which remains *T Ltd v Comptroller of Income Tax*[8] (T Ltd) wherein the Court of Appeal cited with approval the Privy Council decision of *Wharf Properties Ltd v Commissioner of Inland Revenue (Hong Kong)*[9] that:

"Each payment of interest must be considered in relation to the purpose of the loan during the period for which the interest is paid. Once the asset has been acquired or created and is producing income, the interest is part of the cost of generating that income and therefore is a revenue expense".

It is hoped that the judge's *dictum* of interest deductibility (in relation to a loan taken for capital purposes) will be clarified by the Court of Appeal and reconciled with the decision in T Ltd, as it is understood that the taxpayer in BFC has appealed against the High Court's ruling. This should be of interest to many taxpayers given the importance of the issue of deductibility of financing costs.

[7] Paragraph 131
[8] [2006] SGCA 13
[9] [1997] STC (at paragraph 351)

Deductibility of lump-sum payment

The judgment for *BFH v Comptroller of Income Tax* [2013] SGHC 161 (BFH) was published on 22 August 2013. In it, the High Court ruled that a lump-sum payment made by a telecommunications company for a 20-year licence constituted capital expenditure which was not tax deductible.

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Background

The case deals with the deductibility of a $100 million lump-sum payment (the Expenditure) made by BFH, a telecommunications company, in 2001 for a 20-year grant of both a 3G Facilities-based Operator Licence (3G FBO Licence) and for the right to use a particular bandwidth of the electromagnetic spectrum (3G Spectrum Rights)[10].

BFH had claimed a tax deduction for the Expenditure, arguing that it was revenue in nature and therefore deductible under section 14(1)[11] of the ITA. This deduction was denied by the Comptroller of Income Tax (the Comptroller) on the grounds that it constituted capital expenditure, which is disallowed under section 15(1)(c)[12] of the ITA.

The Comptroller's position was upheld by the Income Tax Board of Review (the Board)[13] which held that the Expenditure had secured an enduring benefit for BFH.

The key issue before the High Court was therefore whether the Expenditure was capital or revenue in nature.

Basis for the Judgment

The High Court applied the composite and integrated approach laid down by Andrew Phang JA in ABD for determining whether a specific item of expenditure is capital or revenue in nature. Pursuant to this approach, the Court would first examine the purpose of the expenditure and ascertain whether or not it created a new asset, strengthened an existing asset or opened new fields of trading not previously available to the taxpayer (which would render the expenditure capital in nature). In making this enquiry, the manner of the expenditure (a one-time as opposed to a recurrent expenditure) and the consequence or result of it (whether it strengthens or adds to the taxpayer's existing core business structure), are some of the guidelines that the court would consider.

In applying the approach laid down by Phang JA, the High Court addressed the following major points of contention:

a) Manner of the Expenditure

Ang J disagreed with BFH's argument that since the payment structure was dictated by the government for policy reasons, the manner of the Expenditure (as a lump sum payment) was irrelevant in ascertaining whether it was of a capital or revenue character. He

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[10] A spectrum right is the right to transmit telecommunications at a certain frequency of the electromagnetic spectrum. A mobile communication system, be it 2G or 3G, refers to the actual technology and infrastructure used to provide telecommunications. The telecommunications company is required to obtain an FBO Licence before the relevant authority will grant it the spectrum rights that are required to provide the telecommunications systems and services.

[11] Section 14(1) provides:
"For the purpose of ascertaining the income of any person for any period from any source chargeable with tax under the Act…there shall be deducted all outgoings and expenses wholly and exclusively incurred during that period by that person in the production of the income,…"

[12] Section 15(1)(c) provides:
"Notwithstanding the provisions of this Act, for the purpose of ascertaining the income of any person, no deduction shall be allowed in respect of –
…(c) any capital withdrawn or any sum employed or intended to be employed as capital…"

[13] *BFH v Comptroller of Income Tax* [2013] SGITBR 1

acknowledged that, given a choice BFH might not have opted to pay a lump sum, however, the fact remains that the Expenditure was a one-time lump-sum payment.

He also distinguished this case from *Vodafone Cellular Ltd and others v Shaw (Inspector of Taxes)*[14] as the latter refers to a payment made to get rid of or replace an extant liability, which was not the case here.

b) Consequence or result of the Expenditure

BFH argued that the Expenditure was incurred to protect its existing business and market share, and not to open up a "new field of trading". This was because the 3G network was not a new business, but was part and parcel of its existing telecommunications business.

Ang J, however, rejected this argument. He was of the view that the advantage of being able to use a certain part of the electromagnetic spectrum designated for 3G services as well as to develop and operate a 3G network strengthened and enhanced BFH's existing telecommunications systems, which constituted the permanent structure of the business that was used for the generation of profits. He therefore held that the nature and duration of the rights constituted benefits of an enduring nature.

The judge also held that it was irrelevant that BFH obtained no relative or competitive advantage by virtue of the Expenditure as the other two telecommunications companies had acquired the same rights.

In arriving at his decision, the judge distinguished the Expenditure from cases cited by BFH in which revenue expenditure was incurred to preserve a business, avoid a catastrophic event or overcome or avert some obstacle or difficulty that would prevent the taxpayer from carrying on its existing business. In none of the cases cited by BFH was there any asset or advantage of an enduring nature created. In this case, however, the court was of the view that the Expenditure was not incurred merely to enable BFH to continue its existing trade in the same way that it had done in the past. There was no obstacle or difficulty that was impeding or threatening to impede its existing business, let alone an impending "catastrophic event".

PwC's observations

a) Growth potential

Ang J was of the view that the the 3G FBO Licence provided BFH with vast potential to develop and provide innovative 3G data services. He was therefore of the view that the Expenditure was incurred with the purpose of strengthening and enlarging BFH's existing profit-making telecommunications systems, as well as providing avenues for growth of its business. Hence, the result of the Expenditure was an improvement in BFH's core business structure. Ang J also rejected BFH's interpretation of Phang JA's expression "new field of trading", opining that it could not have been intended to exclude expenditure incurred for the expansion of the scope of an existing business.

b) Relevance of tax treatment of 2G FBO licence fees

Although not explicitly pursued as a separate line of argument, one recurring theme throughout the taxpayer's case was that because the Comptroller had treated payments for the 2G Spectrum Rights and 2G FBO Licence as revenue expenses, the Expenditure should similarly be treated as revenue in nature.

[14] [1997] STC 734 at 739

Ang J disagreed that the two payments are identical in nature and purpose. He noted that the subject matter of the two payments was transmission rights to use identified portions of the electromagnetic spectrum. These rights should be distinguished from the underlying electromagnetic spectrum, which is a natural phenomenon. He felt that it "…makes absolutely no sense to speak of charging for electromagnetic waves of a certain wavelength."[15] The rights granted here, on the other hand, are human constructs and could be different, even if the underlying electromagnetic spectrum was the same.

He was therefore of the view that the character and manner of use of the advantages gained under the respective payments are different, even though the underlying subject matter of both payments concerned spectrum rights and rights to develop mobile telecommunications services.

Interestingly, Ang J also observed that the Comptroller is not empowered to make binding determinations of law concerning the provisions of the Act[16]. The Comptroller's treatment of the earlier 2G licence payments as being revenue in nature does not bind him to treat future payments as such even if they are identical in all material respects to the earlier payments. The Comptroller is charged with the administration of the tax laws and therefore is required to make interpretations of the laws, however, this clarifies that the Court is the appropriate forum for interpretation of the laws.

c) Consistency with tax treatment of cellular licence fees in other jurisdictions

Ang J also found it instructive to see how three other common law jurisdictions, the UK, Australia and Malaysia dealt with similar expenditure. He deduced that, but for statutory intervention in those countries, the expenditure would not have been deductible as revenue expenditure nor would it have qualified for depreciation allowances.

In addition, South African case law has confirmed that lump sum 3G expenditures are capital in nature for two reasons: first, because the licences confer an advantage of an enduring nature; and second, because lump sum payments are more closely connected with the income-earning structure rather than the income-earning operations of the telecommunications company. The court there, however, did hold that an accompanying annual licence fee component, over and above the capital sum paid upfront, was revenue in nature and deductible.

BFH reiterated the principles of ABD in ascertaining the capital-revenue distinction and adds to the tax jurisprudence in Singapore. It is pertinent to note that, in arriving at his decision, the judge had referred extensively to various materials related to the roll-out of the 3G technology, including industry feedback provided by the taxpayer so as to establish the relevant facts. This goes to show that the capital-revenue distinction is very much an application of tax principles to the relevant sets of facts, and hence the importance of having contemporaneous documentation to substantiate the purpose of the expenditure in securing tax deductions.

[15] Paragraph 58
[16] *Comptroller of Income Tax v ACC* [2010] 2 SLR 1189 at [30]

Exchange of Information in Singapore

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There have been a number of cases considered by the High Court of Singapore dealing with information requests from the tax authorities of other jurisdictions. The success of these exchange of information (EOI) requests is perhaps a sign of the times. It is confirmation that the Singapore judiciary will not apply domestic EOI provisions strictly, or in such a way as to frustrate the investigation of foreign nationals by foreign tax authorities where there is reasonable suspicion of non-compliance.

The context

Singapore has successfully positioned itself as a private banking and financial services hub. In doing so it has had to, among other things, strike a balance between endorsing client confidentiality in a meaningful way, and protecting the integrity of the financial services system.

Singapore's efforts in striking this balance have been under the spotlight of the international community in recent times. Somewhat inauspiciously, Singapore was initially grey listed as a country which had committed to, but not substantially implemented, the Organisation for Economic Co-operation and Development (OECD) standard for EOI. It has since been named as a white-listed country after making the necessary revisions to domestic law and signing a number of bilateral EOI provisions that allow it to implement meet the OECD standard for EOI.

Earlier this year Singapore was named in a joint statement from the Australian Taxation Office, Her Majesty's Revenue and Customs and the Internal Revenue Service as a country thought to harbour the proceeds of tax evasion.[17] This followed the anonymous delivery of a hard disk containing confidential client information to the International Consortium of Investigative Journalists. The legislature has responded fairly swiftly to claims that Singapore is somehow facilitating tax evasion. Within days of the joint statement, it was announced that Singapore would enhance its EOI regime, including signing the OECD Convention on Mutual Administrative Assistance in Tax Matters. This immediately increased the number of EOI provisions meeting the OECD standard from 41 to 83[18].

Separately, tax evasion has now been added as a money laundering predicate offence. This is in line with best practice promulgated by the Financial Action Task Force. This now creates a positive disclosure obligation on financial intermediaries to file a suspicious transaction report if they know or have reasonable grounds to suspect that funds, among other things, represent the proceeds of tax evasion. This extends to the equivalent of income tax and goods and services tax evasion committed in a foreign jurisdiction.

The broader international context is also highly relevant, and has undoubtedly been a catalyst for progressive change in Singapore. The Swiss private banking scandals of 2007 are a telling example of what can happen when a high threshold is applied to the exchange of client confidential information. The attendant developments including the introduction of the US Foreign Account Tax Compliance Account Act (FATCA), create onerous customer due diligence requirements on financial institutions the world over. The scope of this legislation demonstrates the resources that developed countries are willing to throw at stamping out tax evasion - low hanging revenue in times of bulging debt ceilings and fiscal deficits.

[17] "Authorities Announce Tax Haven Investigation", article dated 9 May 2013 by The International Consortium of Investigative Journalists.
[18] "Singapore to Significantly Strengthen Framework for International Tax Cooperation", press statement issued by the Ministry of Finance, Monetary Authority of Singapore and Inland Revenue Authority of Singapore on 14 May 2013.

EOI legislation

A matrix of rules currently apply to the disclosure of information requested by a foreign tax authority. Following the grey-listing of Singapore in 2009, many of the bilateral EOI provisions of Singapore's network of tax treaties were renegotiated to align with the OECD standard. This is expressed as Article 26 of the OECD Model Tax Convention on Income and Capital (Article 26). It requires the disclosure of information that is 'foreseeably relevant' to the collection of taxes of every kind imposed by a contracting state. This disclosure obligation is subject to a number of exclusions, including circumstances where the information is not obtainable under the laws of a contracting state; would result in the disclosure of commercial secrets or processes; or would be contrary to public policy. EOI is not merely limited to instances of suspected foreign tax evasion, but is also relevant for the administration of taxes of a contracting state.

Part XXA of the ITA was added in 2009 to support the treaty EOI provisions. This Part provides the machinery provisions for the collection of information requested by a foreign tax authority in relation to income tax, goods and services tax, stamp duty and property tax[19]. Section 105F of the ITA (read with section 65B) expands the information collection power of the Inland Revenue Authority of Singapore (IRAS) beyond merely the information that a taxpayer may have regarding their own tax affairs. The required form of an information request made by a foreign tax authority is set out in the Eight Schedule of the ITA. This includes a statement from the foreign tax authority that they have pursued all means necessary to obtain the information except for those that would give rise to 'disproportionate difficulties.'

Part XXB of the ITA obliges the IRAS to apply to the High Court where an information request is made for information that is prohibited from disclosure under the secrecy provisions of section 47 of the Banking Act (BA) or section 49 of the Trust Companies Act. The High Court may make an order for the disclosure of information where the two conditions of section 105J(3) are met. These are that:

- the making of the order is justified in the circumstances of the case; and
- it is not contrary to the public interest

Where the High Court makes an order requiring the disclosure of information, either the party against whom the order is made or the person in relation to whom the information is sought may apply for a discharge or variation of the order. Section 105L provides a statutory immunity where a party discloses information in accordance with an order of the High Court that would otherwise give rise to criminal or criminal liability.

EOI cases

The recent string of EOI cases involved requests made by foreign tax authorities for information prohibited from disclosure under section 47 of *the* BA. In 2012 the High Court handed down the decision of *Comptroller of Income Tax v AZP* [20] (AZP) which concerned an information request made by India. The Indian tax authorities believed that an Indian national had transferred amounts to two companies having accounts with a Singapore bank. This belief was based on two unsigned transfer forms that the Indian tax authorities had obtained.

In considering the application made by the Comptroller, Choo J elaborated upon the foreseeably relevant criterion found in the EOI standard. His Honour stated that this requires a foreign tax authority to provide "clear and specific evidence" of a connection between the information requested and enforcement of foreign countries tax laws. His Honour found that this test was failed for two reasons:

[19] Section 105G of the ITA.
[20] [2012] SGHC 112.

- No connection could be demonstrated between the companies having the accounts with the Singapore bank and the Indian national who was the subject of investigation; and
- Insufficient evidence was presented to show that either of the two transfers had actually been made.

The outcome in AZP may be contrasted with the conclusion reached by Ang J in the subsequent case of *Comptroller of Income Tax v BJY and others* [21] (BJY) which also involved a request made by the Indian tax authorities. His Honour referred to OECD standard which describes the foreseeably relevant test as satisfied where there is a 'reasonable possibility' that the information may be relevant to the investigation of a foreign tax authority. Expressed in a negative sense, this test is merely intended to eliminate the disclosure of information in response to speculative requests (or 'fishing expedition') where there is no apparent nexus between the information and an investigation.

This latter approach continued to be adopted by the High Court in *Comptroller of Income Tax v BLM*[22] (BLM). This concerned an application made by the Japanese tax authorities for the information of eight parties having accounts with a Singapore bank. In this case, Choo J seemed to imply that the Court has limited discretion in rejecting an application made under Part XXB of the ITA when all the specified information in the Eighth Schedule has been provided. His Honour commented (at paragraph 8):

> *"In many respects, the High Court's role is an administrative one. There is little room for the Court to examine the substantive merits of the application, much less the granting of the request."*

While there is no doubt the Singapore courts are not in the position to adjudicate on matters related to Japanese taxation, this should not diminish the Court's role in reviewing the quality of evidence adduced, in that the evidence has to be unequivocal in establishing relevance in accordance with the requirement under Article 26, even if 'the test for foreseeable relevance is not envisaged to be a high or exacting standard': Ang J in *Comptroller of Income Tax v BJX*[23] (BJX) (at paragraph 10). The operative provision of section 105J(2) states that in circumstances where the two part test of 105J(3) is satisfied, the Court may make an order requiring the disclosure of information. This drafting clearly vests power in the High Court to make a decision based on the facts before it – a decision that is consistent with Singapore's EOI obligations and the mischief to which Parts XXA and XXB of the ITA are directed. Hence, even though the IRAS may be experienced in handling these matters, this does not override the role of the Court as the ultimate arbiter in assessing whether the requirements under the law has been met.

In addition to providing jurisprudence around the foreseeably relevant test and the two part criteria of section 105J(3), the suite of recent EOI cases also highlight other important features of the EOI process. In both BJY and BLM, it was argued that the relevant foreign tax authority did not have a basis under their domestic law to request the information that was sought from Singapore. In BJY it was suggested that an exposure to Indian tax did not arise because an assertion that the Singapore companies had Indian permanent establishments (and by that fact were liable to Indian tax) has not been proven. In BLM an action was filed in Japan suggesting that the Japanese tax authorities had acted improperly in making the information request.

In both instances the High Court confirmed that Singapore was not a forum for these matters to be considered. Furthermore, a stay of orders would not be granted pending the outcome of these actions against the Indian and Japanese authorities respectively. It is enough that a foreign tax authority confirms that it is empowered to request the information as is required

[21] [2013] SGHC 173.
[22] [2013] SGHC 212.
[23] [2013] SGHC 145.

under paragraph 7 of the Eighth Schedule of the ITA. Consistent with this position is the outcome in BJX where a stay of an order for the disclosure of information that was the subject of a pending appeal was refused. It was concluded that no harm could be caused by the applicant in this case as the foreign tax authority was obliged to keep any information disclosed secret.

PwC's observations

The outcome of these recent EOI cases indicates that the High Court does seek to not impose a high threshold for the foreseeable relevance test under Article 26 before acceding to an information request from a foreign tax authority. It is likely that these authorities represent a new paradigm which is consistent with a more permissive approach to the enquiries of foreign tax authorities. Given the global move towards strengthening the institutions which combat tax evasion, the outcome in these decisions is not surprising.

It was announced in May this year that the existing requirement for the IRAS to apply for a Court order to release information covered by bank and trust secrecy provisions will no longer apply. In striking a balance between not stifling international cooperation and respecting taxpayers' privacy, one would hope that the essence of the two part test of section 105J(3) will be administered by the IRAS through its own processes in considering an information request.

Such administrative scrutiny is of particular importance, given the G20's support for the plan of the OECD to move toward automatic, multilateral information exchange and Singapore's signing up to the OECD Convention on Mutual Administrative Assistance in Tax Matters. It thus appears that the days of bilateral information exchange, based on specific and formally documented requests, are coming to an end.

An interesting point to ponder is whether there is likely to be any interaction between tax evasion becoming a money laundering predicate offence, and the receipt of an information exchange request from a foreign tax jurisdiction. There is no evidence that the Inland Revenue Authority of Singapore will work with the Monetary Authority of Singapore to verify the due diligence undertaken by a financial intermediary on an account that is the subject of an EOI request. A joint administrative approach where there is an allegation of foreign tax evasion could potentially broaden the consequences of an EOI request beyond those of the account holder. That being said, it should be recognised that where banks are asked to provide customer information and it was subsequently determined by the requesting (foreign) tax authority that the customer should pay additional taxes, it should not automatically mean the bank has failed to carry out its anti-money laundering (AML) checks properly – for example, additional tax payable following a tax audit may not result from tax evasion. Correspondingly, failure to detect an instance of tax evasion should not be taken to mean the bank's AML process was not robust and constituted a breach.

While there is still some uncertainty as to how EOI will develop, and what the impact will be for financial institutions in Singapore, what is abundantly clear is that further changes are on their way. The noble aim of eliminating the scope for tax evasion and facilitating efficient tax administration is likely to translate into a need to develop even more robust systems and processes.

Read on for myth busters, Q&A with the new tax partners, crossword puzzle and event updates!

Myth Busters

Anulekha Samant and David Sandison take a wry look at some of the common myths about Singapore taxation, and attempt to put the record straight.

Every country or culture has its share of legends and myths. Some of them have been around for so long that they have been taken as gospel truth, until stark reality rears its ugly head and things turn out to be not quite what they may have seemed. Although an article about dragons and demons could possibly be more interesting, our focus is on tax myths. Our purpose in this article is to reveal the truth about some of the common myths that seem to be out there, and at the same time provide some food for thought.

Myth: Singapore does not have a capital gains tax regime

It is quite true to say that Singapore does not impose tax on gains that are capital in nature. However, it is not entirely clear what a capital gain is. Logic would normally dictate that a capital gain is a capital loss but for the fact it is a gain. However what we find in practice is that the IRAS generally starts with the proposition that all capital gains are revenue (which makes them taxable) and all capital losses are capital (which makes them non-deductible). With us so far? To say it is an area of contention is an understatement. Taxpayers who are used to a capital gains tax regime in their own country, are often surprised to find that, what they thought was a slam-dunk profit that would not be taxed as a capital gain, is being treated as some sort of trading profit in Singapore and taxed accordingly.

Until 2012, a degree of relief was provided in the form of a safe-harbour, under which certain gains accruing to an approved Headquarters company would be specifically exempted; but this was still considered too limited, being available only to the privileged multi-nationals. Something was still needed for hoi polloi, something within the reach of all. That did come, again to a degree, in Budget 2012 in the form of broader safe harbour provisions. Under these rules, gains made by a company on the disposal of ordinary shares in another company will be exempt from tax where the seller has owned at least 20% of the issued ordinary share capital of the other company for at least 24 months. Not quite as generous as the so-called participation exemptions we see in other countries, and still absent are other types of investment instruments, as well as, most notably, real estate, but it is undeniably a step forward and we should be grateful for small mercies in this messy no-man's land.

The question the new rules do raise though, is what happens if you fall outside the harbour walls? The answer should be that you are in the open sea and back to the good old Badges of Trade punch-up. It doesn't mean you are automatically taxed, at least that's what we are told.....

Verdict: You can't relax and must stay on your toes. There are still some demons out there.

Myth: It is easy to establish tax residence in Singapore

Singapore has always been careful to avoid the label of “tax haven”. More of this below. However, early in 2009 it was thrust into the limelight when it was reported that it had been placed on an OECD list of nations deemed to be non-cooperative tax centres. The light tap on the knuckles that the publication of the list delivered, seems to have had quite a dramatic effect, which is consistent with Singapore's desire to be seen as a mature and responsible international centre for business. What we have noticed however, is that this enthusiasm towards international acceptance has translated into fierce resistance against companies that are claiming to be tax resident in Singapore for the purposes of obtaining benefits under Singapore's double taxation agreements.

One of the most disturbing features of this trend is the point from which the argument starts - namely that companies (even if Singapore incorporated) that are owned by non-residents are presumed to be non-resident themselves unless it can be shown that there is substance in Singapore. How this can possibly be of relevance to a holding company is a question that remains on the table. The problem is that not only are the arguments put forward in direct disregard of established case law on the subject of residency, but this enthusiastic rush to become the world's tax avoidance policeman is likely to damage any support there may have been to recommend Singapore as a holding company location. It is quite a serious development that a number of multi-national investors do not seem to have quite got hold of, but it is one that needs to be reviewed very carefully at a policy level so as to prevent the meltdown of an initiative the government has long been trying to nurture.

Verdict: Predict the unpredictable. It is not so easy to establish tax residence in Singapore.

Myth: Singapore is a tax haven

The term "tax haven" has been thrown around merrily for the last few years by the international community, most notably in the guise of the OECD, and Barack Obama. As noted above, Singapore has always attempted to steer clear of being labelled as such, as there is no doubt that the term has pejorative connotations these days. A tax haven is variously defined in dictionaries, but the common theme appears to be that it is a country or territory that imposes little or no income tax. The term strictly does not carry with it any secrecy connotations, however traditionally, banking secrecy and low taxes seem to have gone hand-in-hand.

The additional, yet unwritten feature of the tax haven is that traditionally people have booked profits there without any real commercial rationale. It is submitted that Singapore cannot possibly fall into the definition of tax haven, since:

- It imposes a basic rate of corporate tax on businesses which, at 17%, cannot be said to result in "little or no tax".
- Whilst tax incentives can apply to exempt certain types of Singapore sourced income, these incentives carry with them obligations to genuinely contribute to the welfare of Singapore. This will generally imply a need to bring resources into Singapore as well spend money in the economy. In other words, there is a need for genuine substance before businesses can qualify for the reduced rates.
- The new-found enthusiasm for scrutinising residency claims, has also contributed to the view that Singapore takes a serious approach (but one which may be more serious than need be) to its international obligations.
- The government’s enthusiastic adoption of international exchange of information initiatives, shows its commitment to running an open and co-operative business environment.

Verdict: Fear not the rantings of the ogres on the mountain. Singapore is not a tax haven.

Myth: You need to charge interest on inter-company loans

If you speed read the IRAS Circular "Transfer pricing guidelines for related party loans and related party services" published on 23 February 2009, you may come away with the impression that there is a need for a company lending to another company within its group to charge an arm's-length rate of interest on the loan in question; and we have seen many people jump to this conclusion.

A closer reading, and applying some basic logic, will reveal that this is simply not the case in many instances. A loan by a Singapore holding company to fund the operations of its foreign subsidiary would give rise to interest (if interest were charged), that in most cases, has a foreign source; and foreign sourced income is only taxable if received in Singapore. If no interest is charged, then a receipt of interest in Singapore is a physical impossibility.

Where a loan is made to a local group company, then the Circular itself says there is no need to charge interest at arm's length, as the IRAS will continue to apply interest restriction on borrowings by the lender. (Quite what the connection is still baffles us, but again, be grateful for small, publicly announced mercies).

Care however is still required and you cannot then just jump to the opposite conclusion that there is never a need to charge interest or pay attention to arm's length rates. There may still be a need when the lending entity could be regarded as doing the lending as part of its normal day-to-day activities (eg it is a treasury company or a financial institution).

Verdict: The transfer pricing banshee is not so frightening if you look him in the eye. But don't do it alone.

Myth: "I confirm that the income categorised under the reduced tax rate is correct" Means "Wey hey, no need to look".

This misapprehension refers to the confirmations that the IRAS asks from taxpayers relating to income that is subject to tax at reduced rates due to tax incentives. The practice adopted by the IRAS traditionally has been to ask for a confirmation from the taxpayer that he has actually examined each transaction and is confident that the income has been correctly captured under the appropriate rate. In the past, these confirmations were admittedly taken at face value. Not anymore. Detailed questionnaires about procedures and controls applied in determining income classification are being asked. A misclassification uncovered in a submitted tax return will lead to penalties (as indeed has always been the case). Though blanket confirmations are still being asked for by the IRAS, that doesn't mean you can give a blanket response.

Verdict: Be prepared to put your neck on the line when giving blanket confirmations or get some help. The guillotine is waiting…

My friend Roger told me, so it must be correct

We have provided above only some examples of the myths that are at out there (there may be others, we can assure you) with the hope of demonstrating that, in the tax arena, you should never rely on stories that are handed down from generation to generation (or told at cocktail parties – what we call "gin and tonic" advice), but go out and get the real story from those who actually know it.

Q&A

With New Tax Partners

Andy Baik

Tell us something we don't know about you
I have been fortunate to have had the opportunity to live in 14 different countries, with 7 of the countries being in the Middle East. I am originally from Korea and Singapore is the place I have lived the longest (approaching 9 years).If you watched the movie Argo, I was there living in Tehran, Iran at that time - still pretty vivid memories of the revolutionary atmosphere there in late 1970's. I also remember "fondly" coming across (too close for comfort) many snakes as a 6 year old living in a jungle in Bali.

Tell us something which you have done personally or professionally that gives you the greatest satisfaction
In my pre-PwC life, I was asked to take on the tax leadership role in Korea for another professional services firm. This was on top of my existing role heading up the International Tax Services group in Asia out of Singapore. For two years, I commuted to Korea from Singapore and hands down this was the period where I had worked the hardest both physically and mentally, juggling two jobs. But it was absolutely worthwhile because of the opportunity to drive fundamental changes in the Korean tax practice and to spend invaluable time with the staff in adopting people-driven initiatives.

Can you share with us your way of relaxing and de-stressing?
I have to tell you it was much easier when we did not have kids! Now that my two daughters are 9 and 10, it is possible to spend relaxing time with them by playing casual tennis together or playing a board game. My two main means of de-stressing are watching a couple good movies on a long flight and sweating out in the gym.

Brad Slattery

Three words your closest friends would use to describe you?
Loyal. Ambitious. Joker.

What is the best thing about becoming a partner?
Being thrown in the deep-end but with a network of people supporting you to succeed.

What does success as a partner look like for you?
Ensuring that my staffs are given the opportunities to fulfil their professional ambitions.

Chai Sui Fun

Tell us something which you have done personally or professionally that gives you the greatest satisfaction
There were many such moments. One such moment that I felt professionally thrilled was (on 13 November 2009) when I witnessed, Singapore's removal from the grey list of financial centres that had committed to but not yet substantially implemented the internationally agreed standard on exchange of information, and its placement on the white list of jurisdictions that have substantially implemented the standard. My team and I in IRAS had worked tirelessly towards this and it was a great feeling for me that we accomplished this for our Singapore.

Can you share with us your way of relaxing and de-stressing?
I have started exercising at a gym, which helps me relax and de-stress to some extent.

What does being a partner mean to you?
I have become a business owner of a thriving professional practice where opportunities abound for working with highly professional and competent global teams and with top-class businesses.

Liam Collins

Can you share with us your way of relaxing and de-stressing?
My wife and I have a one year old daughter and a three year old son, so relaxing and de-stressing aren't words often used to describe what goes on in the Collins household! But simple things like taking the kids for a swim (which is much easier here in Singapore than it is in Melbourne) or going out to a new restaurant with family or friends are pretty high on my list of "de-stressers".

What does being a partner mean to you?
It means a great deal. I believe a partner is a custodian of our wonderful firm who is obliged to leave the firm in even better shape for the next generation than he or she inherited it from the generation before. In my view, there is only one way to do this and that is to focus very hard on client service every day. Clients who are blown away with our service come back and give us the most interesting work, which means we can attract and retain the best people to work with us, which in turn means we can do an even better job next time and the cycle continues. I'm also very keen on ensuring our people get opportunities to develop their skills and stretch themselves, and am always grateful when our clients are happy to play a part in this process.

What's your first impression of PwC Singapore?
Wow! What a great group of people - everyone here at PwC Singapore has been so warm in welcoming us to Singapore. I have also been struck by the entrepreneurial culture that seems ingrained here. It's terrific to see such a group of talented professionals putting themselves in our clients shoes.

Tan Hui Cheng

What's your strongest trait as a leader?
The ability to set a new direction for the team in response to changes.

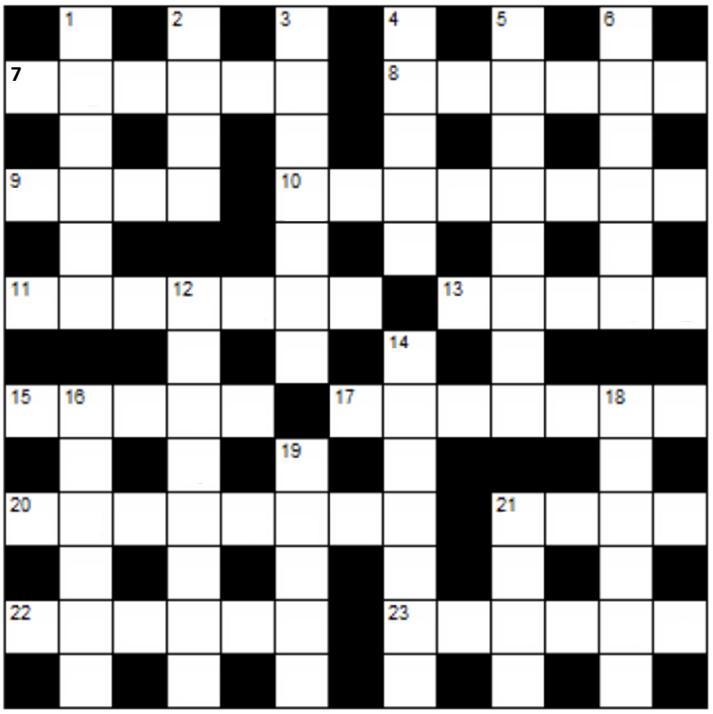
How will the business transform 10 years from now?
It will be paperless and mobile, with all information at our fingertips, wherever we are.

What's one thing you value about being part of PwC?
Having the support of a high quality and dynamic team.

If you only have one day to live, what would you do?
Gather friends and family for a hearty meal.

Crossword puzzle

First 5 correct entries will win a free pass to our PwC Budget Seminar on 28 February 2014!



Across

7 This type of income doesn't loaf about

8 Phew! Loss set-off

9 Disallow and say it wasn't me

10 Out of work accountant is hungry

11 Don't make me angry for this jurisdiction

13 Joins our East for single condos

15 Tied up by precedent

17 Pin one of these for that extra provision

20 Norse pal messes up individual tax

21 Responsibility for tax on booze

22 Hole in the rock at the end. Beware!

23 A stone figure nearly gives us the written law

Down

1 Plan to avoid tax? Intrigue!

2 Comptroller of Income Tax? Yes. That's where we work

3 Male offspring are mixed for more than one purpose

4 Messing with trail leads to court

5 Helen, vet, leaves everything to this hour

6 If you want a monkey, pay in this currency

12 Clergy in government office?

14 I'll be damned if I will do this

16 A poser changes for musicals

18 Taxable supply produced by industry

19 Untie, mix and bring together

21 Distribute and shake hands

Please submit your answers to michelle.sx.goh@sg.pwc.com

Terms & Conditions

1) Employees of PwC and their immediate families are not eligible to participate.
2) Winners will be notified via email and the free pass must be claimed in person latest by 9am, 28 February 2014 (Friday). Seminar fees will be refunded to the winners where payments have been made.

Event Calendar 2014

Date	Title	Partner/ Manager in Charge
February 2014		
13-Feb	RA Client briefing: Outsourcing for vendors #1	Chan Hiang Tiak / Mark Jansen
14-Feb	RA Client briefing: Outsourcing for vendors #2	Chan Hiang Tiak / Mark Jansen
14-Feb	EUM Myanmar Event	Steven Banfield Paul Cornelius
16 - 19 Feb	stars - the Symposium for Leaders of the Next Generation	Yeoh Oon Jin
28-Feb	Singapore Budget Seminar 2014	Alan Ross
March 2014		
27-Mar	Regional Corporate Treasury Survey 2014 Launch	Chen Voon Hoe
April 2014		
03-Apr	Global CEO Survey cross-industry CEO/NEDs client breakfast	Dominic Nixon / Julia Leong
17-Apr	PwC Alumni Night	Deborah Ong

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