



FEBRUARY 2006

Association of Taxation Technicians Singapore (ATTS)

TAX BULLETIN

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UPDATE ON THE GOODS AND SERVICES TAX (GST)

by Mr Yeo Kai Eng, Ernst & Young

Goods and Services Tax (Amendment) Act 2005

After the public consultation exercise on the draft Goods and Services Tax (Amendment) Bill 2005 conducted between July and August 2005, the Goods and Services Tax (Amendment) Act 2005 [GST Amendment Act] was passed by Parliament on 21 November 2005 and came into operation on 1 January 2006.

The GST Amendment Act contains several **key** changes affecting GST-registered businesses. In this update, we highlight what are these key changes.

1. Repayment of input tax to the Comptroller of GST

Presently, a GST-registered person would be able to make a deduction for the input tax incurred for the supply of goods and services made by a supplier to him in the prescribed accounting period in which the tax invoice is issued by the supplier (or in the case of imports, the import permits issued by Singapore Customs). His entitlement to claim a deduction for the input tax incurred is not dependent on him paying the supplier.

With effect from 1 January 2006, a GST-registered person would be required to repay to the Comptroller of GST, the input tax deducted previously that is related to any part of the consideration for the supply of goods or services made by his supplier to him that remains unpaid after 12 months from the due date for payment of the consideration. The input tax is to be repaid to the Comptroller of GST in the prescribed accounting period during which the 12-month period expires.

However, if, after the repayment of the input tax to the Comptroller of GST and within 6 years from the end of the prescribed accounting period during which the relevant input tax was first deducted, the GST-registered person pays the supplier for the outstanding consideration, he would be entitled to reclaim the relevant input tax in the prescribed accounting period in which the outstanding consideration is paid.

With this change and except for GST-registered businesses that currently deduct their input tax incurred in the prescribed accounting period in which payments are made, GST-registered businesses would now need to track the duration of their unpaid suppliers' tax invoices. This would require a review of the existing processes relating to accounts payable and GST return preparation and instituting the necessary controls to ensure the proper monitoring of outstanding debts and the repayment of the input tax previously deducted to the Comptroller of GST.

2. Compulsory electronic filing of GST returns

Presently, GST-registered businesses are given the option to file their GST returns either manually or electronically. As part of the move towards making the filing of GST returns electronically compulsory for all GST registered businesses, the GST Amendment Act has empowered the Comptroller of GST to require any prescribed class of GST-registered businesses to file their GST returns electronically and to prescribe any procedures relating to such electronic filing.

Recognising the needs and constraints of different groups of GST-registered businesses, the Comptroller of GST is expected to implement electronic filing in phases.

Some of the benefits of filing the GST returns electronically as highlighted by the Inland Revenue Authority of Singapore [IRAS] include:

- faster GST refunds (if the returns are not subject to audit review);
- immediate acknowledgement by the IRAS upon successful e-filing; and
- the flexibility of filing the return immediately after the end of the prescribed accounting period instead of waiting for the receipt of the GST return from the IRAS by post.

As it is only a matter of time before all GST-registered businesses are required to file their GST returns electronically, GST-registered businesses should start early and get their staff, processes and systems ready for e-filing.

3. Zero-rating of maintenance, repair and broking services of ships and aircraft

Previously, under section 21(3)(p) of the GST Act, services relating to the repair, maintenance and broking of any ships or aircraft could only be zero-rated if the services are provided to the "owner, operator or agent" of the ship or aircraft.

"Aircraft" excludes those that are used or intended for use for recreation or pleasure. "Ship" excludes those designed/adapted for use for recreation or pleasure and also those licensed as a passenger harbour or pleasure craft.

Recognising that the maintenance, repair and broking services are directly related to ships or aircraft which are internationally bound, the zero-rating relief restricted previously to the "owner, operator or agent" has now been lifted in the new section 21(3)(p). The new section 21(3)(p) allows zero-rating relief to be applied on "prescribed services comprising the repair, maintenance, broking or management of any ship or aircraft". The lifting of the restriction is certainly welcome news for those involved in the ship and aircraft repair, maintenance and broking businesses.

In addition, Ernst & Young had participated in the public consultation exercise on the draft GST Amendment Bill 2005 and had recommended that the list of "prescribed services" under the new section 21(3)(p) should also include services carried out on parts and components of ships and aircraft. This is especially helpful for businesses involved in the repair, maintenance and overhaul ("MRO") of ships and aircraft. In the MRO business, the services are normally provided to parts and components of ships and aircraft, as opposed to the entire ship or aircraft. This poses a practical difficulty for those relying on section 21(3)(p) to zero-rate their services as the parts/components might not be fitted back onto the aircraft/ship immediately after repair, or they might be fitted onto a different aircraft/ship. The recommendation has been accepted and the list of prescribed services, as discussed below, also includes services in relation to parts/components of ships/aircraft.

The Goods and Services Tax (International Services) (Amendment) Order 2005 ["the Order"] prescribing the following services under the new section 21(3)(p) was issued by the Minister for Finance on 28 December 2005 and came into operation on 1 January 2006:

1. The repair and maintenance of any ship or aircraft where –
 - (a) the repair or maintenance is carried out on board the ship or aircraft;
 - (b) any part or component of the ship or aircraft is removed for repair and reinstalled on the ship or aircraft;
 - (c) any part or component of the ship or aircraft is removed for repair and returned to the ship or aircraft as a spare; or
 - (d) any part or component of the ship or aircraft is removed and replaced by an identical part or component.
2. The making of arrangements for the supply (including the letting on hire) of, or of any space in, any ship or aircraft.

3. Management services, in relation to any ship or aircraft, provided to the owner, operator or agent of the ship or aircraft.

4. Prescribed services in connection with import/export of goods

A new section 21(3)(t) has been added to the GST Act to provide zero-rating relief for prescribed services “in connection with the provision of an electronic system relating to the import of goods into or the export of goods out of Singapore”.

Revised Handbooks

In addition to the GST Amendment Act, the IRAS has also recently updated the following e-Tax guides:

1. Clarification on “directly in connection with” and “directly benefit”

In January 2005, the IRAS issued the e-Tax guide on the interpretation and application of the two expressions “directly in connection with” and “directly benefit” as they are used in section 21(3) of the GST Act. Section 21(3) of the GST Act provides the list of international services qualifying for zero-rating GST relief.

The IRAS has issued a revised guide on 4 November 2005. Other than the additional examples provided by the IRAS, the following two new administrative concessions are provided in the revised guide:

- As a further concession, the IRAS would now allow a local beneficiary to claim the GST charged by a local supplier to an overseas customer (not registered for GST) as the local beneficiary’s input tax credit subject to certain conditions. This is a common GST issue, especially for global contracts where a local supplier would contract with an overseas customer to perform services that “directly benefit” a local person. Under this new concession, a written application must be made to the IRAS and the conditions must also be satisfied in order for the local beneficiary to claim the input tax. The IRAS has decided to allow this concession in recognition of the fact that the GST burden on the overseas customer may have an adverse impact on the international competitiveness of our local service sector.
- As an administrative concession, the IRAS had previously indicated that it would allow the apportionment of the value of services such that only the portion of services that “directly benefit” any local person need to be standard rated. The IRAS had also provided certain acceptable methods of apportionment and prior approval from the IRAS had to be sought for the use of any other apportionment methods. With effect from 4 November 2005, the IRAS would now recognise any other reasonable methods of apportionment and prior approval from the IRAS is no longer required. The GST-registered person is however required to maintain the necessary records to explain the method adopted and details of the transactions undertaken.

2. Transfer of a business as a going concern

The Goods and Services Tax (Excluded Transactions) Order provides that where a business or part thereof is transferred as a going concern, the supply of assets to the transferee pursuant to the transfer of the business would be treated as neither a supply of goods nor a supply of services (i.e. out-of-scope) under certain circumstances.

Administratively, the IRAS would treat the transfer of the assets of a business as not a supply if the transfer satisfies certain conditions as prescribed in the GST Practice Note 17 Volume 6 No. 1 (published on 30 May 1998).

The IRAS has released an updated e-Tax guide on "Transfer of business as a going concern" on 1 September 2005 with a further revision on 10 October 2005 to replace the above GST Practice Note.

Under the updated e-Tax guide:

- the IRAS has removed the restriction prohibiting any transfer of assets which the transferor had obtained by way of a transfer pursuant to the transfer of a business or part thereof which had been treated as not a supply under the GST (Excluded Transactions) Order.
- a new condition has however been added requiring both the transferor and transferee to maintain sufficient records on the transferred assets. The records should contain such information as description and value of each asset or class of assets transferred, including the reconciliation on the difference of the values of assets before and immediately after the transfer of business with the value of the transferred assets.

The guide also provides further guidance on the claiming of input tax incurred on expenses by both the transferor and transferee in relation to the business transfer.

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Kai Eng has contributed various articles on GST topics to The Business Times and Singapore CCH.

He has over 15 years' experience in the area of tax compliance, planning and consultancy work for local and multinational companies and individuals.

He is a GST specialist and is actively involved in SOX 404 work, Major Exporter Scheme (MES) audits, GST health checks, advisory and planning assignments including assisting clients in negotiations with and obtaining rulings from the IRAS on critical GST specific transactions and refunds.

He is a co-developer of the firm's GST training materials and has conducted numerous external and customised training seminars and workshops.

Between 1996 and 1998, Kai Eng worked in Hanoi, Vietnam, advising multinational clients on income tax, VAT, customs issues and the business aspects of doing business in Vietnam. He worked closely with the various Vietnam government agencies to facilitate business opportunities and investment projects for clients in Vietnam.

Kai Eng is a graduate of the University of Washington and a member of the American Institute of Certified Public Accountants (AICPA).

SENDING SINGAPOREANS ABROAD - ARE COMPANIES USING THE RIGHT STRATEGY?

As more local Singapore companies expand their presence to foreign shores, a highly talented workforce is essential but one that also can be deployed cost-effectively.

Hence, the importance of implementing appropriate tax strategies as the unwary could end up with unwanted headaches and additional costs of doing business overseas if secondment arrangements are not fully researched, planned and effectively managed.

Companies need to look at four tax-related factors when planning assignments out of Singapore to help companies manage their risk.

Taxation of Singaporeans Working Overseas

Generally, the IRAS considers a Singaporean who is seconded to work overseas by his employer as a tax resident during the overseas employment. Given the individual's intention to return to Singapore, his absence is regarded as being temporary in nature. Prior to 1 January 2004, tax residents would have been subject to Singapore tax on overseas employment income if such income were received in or remitted into Singapore. The tax law has been recently changed to tax-exempt all foreign-sourced income remitted into or received in Singapore on or after 1 January 2004 by tax residents, except if such income were received through a partnership.

Singaporeans who work overseas for at least six months in any calendar year may elect to be treated as a non-resident. For the longer term assignment, it may be advantageous to be treated as a non-resident during the overseas assignment to be afforded the benefit of the Not Ordinarily Resident (NOR) taxpayer scheme upon repatriation to Singapore, particularly if the individual travels overseas extensively on business. Under the NOR taxpayer scheme, one of the requirements is that an individual must be a non-resident for at least three consecutive years of assessment immediately preceding the year he first qualifies for the scheme. An analysis should be prepared to determine the optimal tax filing position while working overseas.

Host Country Tax Considerations

The domestic tax laws of a country may offer tax relief for services rendered by short-term assignees. For example, in Taiwan, if the employee spends less than 90 days in Taiwan and all costs are borne by the non-Taiwan entity the individual would not be subject to tax. In the US, a non-resident alien who is physically present in the US for 90 days or less, performs services for a non-US employer that is not engaged in a US trade or business, and earns US\$3,000 or less for such services would not be subject to US tax. Therefore, when planning short-term assignments for your employees, domestic tax legislation should be reviewed to assist with structuring tax efficient secondments.

Double Taxation Agreement (DTA)

A DTA is an agreement between two countries to avoid double taxation on individuals or companies resulting from the application of their respective domestic tax laws. Singapore has entered into DTAs with over 50 countries and the primary purpose is to define the jurisdictional authority on cross-border transactions or presence.

Many of the DTAs entered into by Singapore allow foreign tax residents an exemption from Singapore tax on employment income provided that the individual's presence in Singapore does not exceed 183 days in a calendar year and the costs are not borne by the Singapore entity. Conversely, Singaporeans working overseas may enjoy the benefit of a DTA in the assignment country if Singapore has concluded an agreement with that country and provided specific conditions for the tax exemption are met.

A common misconception amongst companies is that their assignees will not be taxable in the host location since they will be there for less than 183 days. Host country tax rules and the application of DTAs vary across borders and should be reviewed carefully prior to the commencement of the assignment.

Payroll Reporting Considerations

For a Singaporean working overseas, he or she may be subject to income taxes in the country in which the services are performed, and the employer may be obligated to withhold income taxes and in some locations, social security taxes. In countries such as Malaysia, the US, China, Taiwan and many others, the employee's wages and allowances may be subject to periodic income and social security tax withholding.

Many Singapore employers are not equipped to manage the impact the cross-border presence has on the withholding tax obligations. Delegating the payroll reporting and withholding obligation to a foreign affiliate or venture partner may not always provide the optimal result for the Singapore company and/or the employee. In addition to creating a withholding tax obligation for an overseas employee, in some cases, the company may be exposed to a country's corporate tax reporting obligations through a permanent establishment. Consideration for jurisdiction over litigation matters, labor law, and/or corporate registration obligations must also be considered. Having the employee seconded to a foreign subsidiary or limiting the employee's job description and powers can sometimes be effective tools for managing risk.

Singapore companies must be aware of a foreign country's laws and the consequences of not being in full compliance. Besides heavy penalties and fines, the risk to the company's reputation is not negligible.

Central Provident Fund (CPF)

For a Singaporean working overseas, CPF contributions are not mandatory. If both the employer and the employee choose to continue contributing while the employee is posted overseas, the employer will have to register for a separate Employer Reference Number before making the voluntary payment. If the employer chooses not to pay CPF contributions for the employee working abroad, the employee may still choose to contribute any amount he wishes, subject to limitations.

For calendar year 2005, CPF contributions for Singaporeans and Singapore Permanent Residents, including voluntary contributions, are limited to the mandatory contributions or \$28,050 per year, whichever is higher.

Conclusion

More and more companies venturing overseas in search of new business opportunities means that individual tax planning should not be overlooked. The consequences for companies are multiple - increased business costs, potential non-compliance with the tax laws of foreign countries and most importantly, the reputational risk of the company is at stake.