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OUTCOME OF PROCEEDINGS

From:	General Secretariat of the Council
To:	Code of Conduct Group (Business Taxation)
Subject:	Singapore's Foreign source income exemption (SG013) - Final description and assessment

ROLLBACK REVIEW PROCESS

On 20 May 2019, the Code of Conduct Group (COCG) agreed on an approach to assess foreign-source income exemption (FSIE) regimes. Based on this approach, on 5 December 2019 the ECOFIN Council endorsed guidance for jurisdictions that have already taken a commitment to amend their FSIE regime, which also served as a basis for the screening of other jurisdictions with similar regimes in 2020.

On 5 December 2019, Singapore received a letter from the Chair of the Code of Conduct Group (COCG) conveying the message that the Group had identified an foreign-source income exemption (FSIE) regime in Singapore and invited the authorities to cooperate with the Commission Services to discuss the features of the regime. Consequently Singapore's FSIE regime was assessed by the Group (the assessment is annexed to this note) and considered not harmful. This conclusion was endorsed by the Council on 5 October 2021.

ANNEX

Assessment of Singapore's foreign-source income exemption regime (SG013)

	1a	1b	2a	2b	3	4	5
Singapore – Foreign Source Income Exemption	X	X	X	X	X	?	X

V: Harmful; X not harmful

Gateway criterion – Significantly lower level of taxation

"Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code"

Singapore imposes a corporate income tax (CIT) at a flat rate of 17%.

As the Code of Conduct looks at the effects that tax legislation may have on the location of business activities in general terms, a full tax exemption may be regarded as a reason for businesses to establish in one jurisdiction instead of another. In this sense, these provisions are relevant for the Code.

The Code of Conduct uses a broad term ('tax measures') to describe what should be assessed under its criteria. This definition is not limited to specific pieces of legislation nor does define what is intended as a 'tax measure'. In the specific case of Singapore, it is relevant to take into account the general tax system, in order to understand whether the legislation provides for a significantly lower level of taxation. This is the case in Singapore, as in certain circumstances income from foreign source can be exempted from taxation.

The provisions are therefore potentially harmful and should be evaluated under the Code.

Criterion 1 and 2 – Targeting non-residents and Ring-fencing

"whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents"

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Under Section 13 of the Income Tax Act (SITA), Singapore levies tax on any income accrued in or derived from Singapore (domestic-sourced income) and on any income that is received in Singapore from outside (foreign-sourced income). Singapore operates a remittance basis of taxation, according to which taxpayers can claim relief for tax paid abroad.

Singapore has in place a broad operations test to determine whether income is Singapore or foreign-sourced. After applying the broad operations test, when an income is considered foreign-sourced, it is subject to tax when received in Singapore, regardless of being active or passive in nature.

The concept of source of business or trade income (referred to as the "operations test"), has been developed in Singapore through case law principles. When ascertaining whether an item of income is sourced in Singapore, Singapore considers all operations of the taxpayer in question and all relevant facts, i.e. broad operations test. If the business operations of a taxpayer in Singapore amount to a trade or business which is carried on in Singapore, the income derived from that trade or business is generally regarded as sourced in Singapore.

Under this test, a Singapore-based business may effectively be taxed on its worldwide business income, unless (i) part of the business is carried on through operations outside Singapore, and (ii) the income can be attributed to operation outside Singapore only. In connection with the latter, Section SITA(8) provides that taxpayers must evidence a fixed place of operation that has features of permanence. If there is no fixed place of operation abroad, the Inland Revenue Authority of Singapore (IRAS) will not consider the income as having a foreign source. To be exempt under the FSIE regime, it must also meet the qualifying conditions (see below).

However, under Section 13(8) of the SITA a tax exemption is provided for certain foreign-sourced income, namely foreign-sourced dividends, foreign branch profits and foreign-sourced services income. This exemption is granted only if certain conditions are met:

- the foreign-sourced income must have been subject to tax in the foreign jurisdiction;
- the headline tax rate of that jurisdiction must be at least 15%. It is noted that where a preferential tax rate is granted to a taxpayer in a foreign jurisdiction, this qualifying condition is not met even if the headline rate is above 15%.

In addition, if a taxpayer remits its foreign-sourced income into Singapore but only a portion meets the above qualifying conditions, it will be only the part that meets the conditions that can be exempted under FSIE, while the rest of the foreign-sourced income is subject to tax in Singapore.

According to Singapore:

- less than 1% of companies have claimed tax exemption under the FSIE regime in 2019;
- the foreign-sourced income which is tax exempt under FSIE is about 5% of the income of profitable companies in Singapore.
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Based on the above, the regime is to be considered not harmful for criterion 1.a and 2.a as well as for criterion 1.b and 2.b.

Criterion 3 – Substance

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

Under Section 13(8) of the SITA, taxpayers claiming a tax exemption under FSIE are required to track their income. In addition, taxpayers shall not be Shell companies. On the basis of the information provided by the taxpayer in its declaration, the FSIE exemption is granted after the Singapore tax authorities (IRAS) have verified that these conditions are met.

Under the FSIE regime, there is no distinction between active and passive income. With regard to foreign-sourced income received in Singapore, only Singapore resident taxpayers are eligible to the benefits under the FSIE. In addition, when a taxpayer has wrongly claimed tax exemption under the FSIE regime (for example it did not meet the conditions), the claim will be disallowed. Finally, there are penalties for furnishing an incorrect return.

Under section 2 of the SITA, there is residence in Singapore where a company or body of individuals exercise the control and management whosever their business in Singapore. This requirement is a question of facts and circumstances relating to a company and depends notably on: a) whether the company carries out business activities in Singapore; b) whether there are office, assets and employees in Singapore; c) whether the key decision-makers are in Singapore; d) where the Board of Directors meetings are held.

In the specific case of royalty income, Singapore introduced an IP regime (Innovation Box) in 2018. This regime was assessed not harmful by the FHTP and the COCG. More broadly, the taxation of IP income is no different from the taxation of the other types of income described above.

While there are no targeted anti-abuse rules to tackle the specific risk of lack of substantial activities in Singapore, the above general anti-abuse rule seems to be broad enough to appropriately cover abusive situations. Besides, taxpayers are required not to be shell companies (see above). However, it remains uncertain how this requirement is applied in practice by Singapore.

In light of the above, the regime is to be considered not harmful for criterion 3.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

The definition of permanent establishment (PE) can be found under section 2 of the SITA. It is defined to mean a fixed place where a business is wholly or partly carried on. This definition seems to be in line with the OECD standard.

However, the source rules for taxation of income in Singapore are generally not dependent on the definition of PE. As described for criteria 1 and 2 above, Singapore operates a broad operations test to determine if an income is Singapore-sourced (taxed on an arising basis) or foreign-sourced (taxed on a remittance basis). In addition, uncertainty remains on the implications in practice of the use of a broad operations test in determining whether an income is foreign-sourced, as compared to the use of the domestic PE definition.

Only in limited circumstances the SITA follows the concept of PE in determining whether the income should be taxed in Singapore. For example, under section 12(6) of the SITA, interest is deemed to be derived from Singapore if it is borne, directly or indirectly, by a person resident in Singapore or a PE in Singapore. In such situations, withholding tax will apply.

In its double tax conventions, Singapore has modelled the definition of PE after Article 5 of the 2014 OECD model. This definition would be relevant in determining when Singapore or its partner may impose taxation on profits arising from within its territory. Should the treaty definition of PE be different from domestic legislation, Singapore has confirmed that treaty definition would prevail.

Finally, Singapore ratified the OECD Multilateral Instrument (MLI), which entered into force on 1st April 2019.

In light of the above, the analysis for criterion 4 is inconclusive.

Criterion 5 - Transparency

"*whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way*"

As described above, taxpayers must claim remittance to benefit from the FSIE regime in Singapore. The competent administration is granted under the SITA a discretionary power to assess taxpayers' claims and verify that all conditions are met. However, all conditions necessary for granting the tax benefits are clearly laid down in the legislation.

Therefore, the regime is to be considered not harmful for criterion 5.

Overall assessment

In light of the analysis above, Singapore's FSIE regime can be considered not harmful under criterion 2.1.