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Stricter enforcement of tax residency requirements by IRAS

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Latest developments

In line with Singapore´s increased efforts to comply with the recommendations deriving from the Base Erosion Profit Shifting project ("BEPS") and the Common Reporting Standard ("CRS"), two major OECD projects aimed at preventing tax evasion and unjust tax avoidance, it appears that the Income Revenue Authority of Singapore ("IRAS") has lately started to enforce the existing requirements on tax residency increasingly strict. In our experience, this is especially true in cases where taxpayers apply for a Certificate of Residence ("CoR"). In the last couple of months, very much contrary to its practice in the past, IRAS would in many cases only issue a COR if the tax payer was able to provide comprehensive documentary proof in respect of the tax residency.

Background

According to Singapore´s income tax law (consistent with most jurisdictions worldwide), tax residency of a company is determined by the place of its effective management. In other words, the question is where the actual control and management of the business, i.e. the decisions on strategic matters such as those on company policies and strategies, are exercised. This is a question of fact and may therefore change from year to year. It is important to note in this respect that the place of incorporation of a company is not necessarily indicative of the tax residency of a company.

In order to determine the tax residency status, two types of companies have to be distinguished depending on their sources of income.

Standard case – company with income from active sources

The standard case is that of a company generating active income, i.e. income which does not derive income from financial investment sources, such as shares, securities or loans.

In such case, the company is considered to be tax resident in Singapore provided that control and management of the company are exercised in Singapore.

Special case: Foreign-owned investment holding companies

The second type is that of a foreign-owned investment holding company[1] with purely passive sources of income or receiving only foreign-sourced income. These kind of companies are generally regarded as non-residents from a tax perspective because they usually act instructions of its foreign companies/shareholders. However, they may still be regarded as Singapore tax residents if they are able to satisfactorily prove to IRAS that:

- the control and management of the company are exercised in Singapore; and
- the company has valid reasons for setting up an office in Singapore.

Besides this, to be regarded as Singapore tax resident, the foreign-owned investment holding companies must be able to demonstrate that:

- there is at least one related company in Singapore which is a tax resident or which has business activities in Singapore; or
- it receives support or administrative services from a related company in Singapore; or
- it has at least one director based in Singapore who holds an executive position and is not a nominee director; or
- it has at least one key employee (e.g. CEO, CFO, COO) based in Singapore.

Consequences of not being considered as tax resident in Singapore

While resident and non-resident companies are generally taxed in the same manner, certain benefits are reserved for companies which are tax resident in Singapore, for instance:

[1] A foreign-owned company is a company where 50% or more of its shares are held by foreign companies/shareholders.

- tax benefits (in particular reduced withhold tax rates on dividends, interest and royalties) provided under Avoidance of Double Taxation Agreements (DTAs) which Singapore has concluded with other jurisdictions; and

- tax exemption for new start-up companies.

What taxpayers should do

As mentioned earlier, tax residency in respect of a company is determined by its place of management and control. In particular in cases where the management team and/or board members are (partly) located outside Singapore, IRAS might ask for further proof in this respect, i.e. companies would have to show that the strategic business decisions were made in Singapore.

Taxpayers are therefore advised to have supporting documents readily available. As a starting point, taxpayers should be able to demonstrate that board meetings have been physically held in Singapore. Board resolutions and minutes of the board meetings may serve a documentary proof in this regard. There is no general rule as to the number of board meetings to be held. However, as a rule of thumb and according to our experience, three to four board meetings a year are recommended.

Helpful are also the following supporting documents:

- Travel calendars and passport copies showing that the directors and management team (if located outside Singapore) spent time in Singapore on a regular basis;

- Material contracts concerning the taxpayer's business which have been signed in Singapore; and

- Any correspondence (such as meeting notes) between the management team/board of directors demonstrating that discussions and decisions were made during meetings in Singapore.

Last but not least, also employing locals or PRs ,in particular in key positions, will help supporting a company's tax resident status in Singapore.

For further guidance and information, please feel free to contact us anytime.

Sincerely yours,
Luther LLP

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