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Global tax development

1 Update on BEPS 2.0 - Pillar One

On 4 February 2022, the Secretariat of the Organisation for Economic Co-operation and Development (OECD) released a public consultation document with draft rules on nexus and revenue sourcing in connection with Pillar One of the OECD/G20 project on Addressing the Tax Challenges Arising from the Digitalisation of the Economy (the so-called BEPS 2.0 project).

Pillar One involves the development of new nexus and profit allocation rules that assign a greater share of the taxing rights over global business revenue to the market jurisdictions. These new nexus rules are intended to apply solely for purposes of determining whether a jurisdiction qualifies for profit reallocation under Amount A of Pillar One and are not intended to affect the nexus determination for any other tax or non-tax purpose.

Under the draft model rules included in the consultation document, nexus in a particular jurisdiction is determined based solely on revenue arising there and revenue is to be sourced on a transaction-by-transaction basis using a reliable indicator or, as a back-stop, a specified allocation key. Different sourcing rules, indicators and allocation keys are provided for the different categories of revenue that are identified in the draft rules (e.g., sale of finished goods, advertising services).

In February and April 2022, the Secretariat of the OECD also released several other public consultation documents with draft rules for tax base determinations, scope and extractives exclusion from scope in regard to Amount A for Pillar One of the BEPS 2.0 project.

All consultation documents indicate that they are working documents released to obtain input from stakeholders. The release of the documents does not reflect consensus of the Inclusive Framework member jurisdictions on the substance of the documents.

2 Update on BEPS 2.0 - Pillar Two

On 20 December 2021, the OECD released the Model Rules on the Pillar Two Global Minimum Tax, as approved by the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS). The Model Rules cover the scope and mechanics of the Income Inclusion Rule and the Undertaxed Payments Rule, collectively referred to as the Global Anti-Base Erosion (GloBE) rules.

Together with the Model Rules, the OECD also released a summary of the rules (The Pillar Two Model Rules in a Nutshell), an overview of the key operating provisions of the GloBE rules (Fact Sheets) and a Frequently Asked Questions document.

The OECD press release indicates that it expects to release the Commentary relating to the Model Rules and to address the interaction with the US Global Intangible Low-Taxed Income rules in early 2022. In addition, the Inclusive Framework is developing the model treaty provision for the Subject to Tax Rule, which is the third element of the Pillar Two global minimum tax framework, and a multilateral instrument for its implementation, which the OECD expects to release in the early part of 2022. Finally, the OECD notes the work to be done on development of an implementation framework addressing administration, compliance and coordination matters related to Pillar Two.

On 14 March 2022, the OECD also released the long-awaited Commentary together with some illustrative examples on the Pillar Two Model Rules.

The Model Rules provide a substantial update to the Pillar Two Blueprint. Implementation of the Model Rules will lead to significant changes to the overall international tax rules under which businesses operate and will introduce a new filing obligation that will require gathering additional data and adaption of companies' internal processes and systems.

Hong Kong tax development

3 Hong Kong unveils the proposed tax concession for family-owned investment holding vehicles (Family Office incentive)

On 8 March 2022, the Hong Kong Government revealed the long-awaited consultation proposal to introduce a dedicated tax concession regime for family-owned investment holding vehicles (FIHVs) managed by single-family offices (SFOs) in Hong Kong. The proposal aims to create a more conducive operating environment for family offices and to expand Hong Kong's role as a family office hub by providing tax certainty to FIHVs. This is an exciting development for the Asset and Wealth management sector in Hong Kong, as it should help to attract high net-worth Asian families to establish family offices in the city, and also help to attract related talent to support these offices.

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3 Hong Kong unveils the proposed tax concession for family-owned investment holding vehicles (Family Office incentive) (cont.)

Subject to satisfying proposed conditions relating to the FIHV and the SFO, an FIHV would be exempt for profits tax in respect of its assessable profits earned from qualifying transactions carried out or arranged by an SFO in Hong Kong, including, subject to the 5% trading receipts threshold, profits earned incidental to the qualifying transactions.

According to the consultation paper, the qualifying transactions refer to transactions in the same classes of specified assets under the Unified Tax Exemption Regime for Funds (UFE). In line with UFE, an FIHV is allowed to established family-owned special purpose entities (SPEs) to hold and administer the specified assets. Such SPEs would also be exempt from Hong Kong profits tax if the FHIV is eligible for the proposed tax concession.

An FIHV who wishes to avail itself of the proposed regime shall observe substantial activities requirements as well as safeguards including the anti-avoidance and the anti-round tripping provisions.

The detailed legislative provisions on the proposed regime will be contained in a bill which is expected to be introduced shortly. Subject to the legislative process, the proposed tax concession will apply retrospectively from the year of assessment commencing on 1 April 2022.

Singapore tax development

4 The Inland Revenue Authority of Singapore announces additional voluntary compliance initiatives for companies

The Inland Revenue Authority of Singapore (IRAS) has published the tax governance and tax risk management initiatives on their website to promote the adoption of good tax governance principles and practices for large companies, including the issuance of an e-Tax Guide on the Tax Risk Management and Control Framework for Corporate Income Tax (CIT).

Designed to operate as independent voluntary compliance initiatives, eligible companies in addition to Goods and Services Tax (GST) Assisted Compliance Assurance Programme (introduced in 2011), may also choose to participate in the following IRAS initiatives depending on their readiness and business needs to demonstrate their good tax governance and tax risk management:

- Tax Governance Framework (TGF) - The company will enjoy a one-time extended grace period of two years for voluntary disclosures (VD) of CIT, GST and withholding tax (WHT) errors made within two years from the date of the IRAS' approval of the TGF application, during which the voluntarily disclosed errors will not attract penalties. This benefit does not apply to fraudulent errors or errors discovered under IRAS' audit or investigation.
- Tax Risk Management and Control Framework for Corporate Income Tax (CTRM) - A company that has been assessed to have an effective CTRM by the IRAS will be granted a CTRM status with a three-year validity period. With a CTRM status, the IRAS will (a) apply a one-time waiver of penalties once for VD of prior years' CIT errors and once for VD of prior years' WHT errors. This excludes any non-compliance involving deliberate tax evasion or serious tax avoidance and (b) step-down on CIT compliance audit for the next three consecutive years of assessment.

With the introduction of TGF and CTRM, the IRAS has further reinforced its emphasis on tax governance and tax control framework as an integral part of their risk assessment protocols and its efforts to shift tax compliance upstream. The TGF and CTRM are both voluntary initiatives wherein companies may participate with the objective of adopting good tax governance and tax risk management practices.

5 Singapore enhances tax incentive criteria for Single Family Offices

The Monetary Authority of Singapore (MAS) has announced enhanced criteria for the Singapore Resident Fund Tax Exemption Scheme and Enhanced-Tier Fund Tax Exemption Scheme, provided for under Sections 13O and 13U of the Income Tax Act, 1947 (SITA) respectively, for fund vehicles managed by Single Family Offices (SFOs). As the family office eco-system in Singapore grows and matures, the MAS seeks to increase the professionalism of family office professionals in Singapore, and enhance the positive spillovers to the Singapore economy.

The updated guidelines shall apply to fund vehicles managed or advised directly by a family office that constitutes:

(i) An exempt fund management company managing assets for and on behalf of a family(ies); and

(i) are wholly owned or controlled by members of the same family(ies).

All new applications submitted to the MAS from 18 April 2022 (inclusive) onwards shall be subjected to the updated conditions. However, the MAS has clarified that the following applications / awardees shall not be subject to the updated conditions:

- Applications which have submitted preliminary information before 18 April 2022 and with correspondences with the MAS in the last 6 months; or
- Applications that the MAS had received formal MASNET application before 18 April 2022, but approved after 18 April 2022; or
- Applications which were formally approved, with the issuance of a letter of offer from the MAS, before 18 April 2022.

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5 Singapore enhances tax incentive criteria for Single Family Offices (cont.)

The updated guidelines are relevant for funds managed by managed by SFO who are not required to be regulated or licensed by the MAS. However, other applicants such as funds managed or advised by licensed fund managers, such as multi-family offices should not fall within the purview of the new guidelines. In order to attract the relevant pool of High Net Worth Individuals (HNI's) and Ultra HNI's, the MAS has particularly put these condition of enhanced investments in Singapore and annual business spending. The new criteria requiring at least one non-family manager in the SFO managing or advising larger funds will further encourage professional wealth management.

6 Processing timelines for Singapore Resident Fund Tax Exemption Scheme and Enhanced-Tier Fund Tax Exemption Scheme

Singapore Resident Fund Tax Exemption Scheme and Enhanced-Tier Fund Tax Exemption Scheme are provided for under Sections 13O and 13U of the SITA. These Schemes are amongst the popular fund tax incentive schemes providing exemption from Singapore tax on "specified income" from "designated investments". While Singapore Resident Fund Tax Exemption Scheme is available to a company which is tax resident in Singapore, Enhanced-Tier Fund Tax Exemption Scheme is wider in its coverage and is available to all legal forms whether set up in Singapore or offshore so long as certain base minimum thresholds on fund size and number of headcount are met. Both the Schemes require that the applicant fund is directly managed or advised by a fund manager holding Capital Markets Services (CMS) License for undertaking fund management activities issued by MAS (or is exempt from such licensing such as single family offices).

The Singapore tax exemption benefit under these Schemes is subject to approval at the discretion of the MAS, upon a formal application. In view of the technological and digital advancements, the application process is paperless such that the application (in prescribed form) is required to be submitted on-line by the fund's authorised representative. The estimated review and processing time for these applications was 6-8 weeks. The recent trend shows that the review and processing tome for these applications have increased to 10-12 weeks, with an even longer time for applications filed by family offices (due to higher level of diligence required). This is due to high volume of applications filed by the fund managers for the MAS' consideration.

Currently, the MAS follows a practice to offer a date of commencement of the award (if granted) to be effective from the date of application on the basis that the applicant has complied with all the requisite conditions as on the date of application. While this is helpful to support fund managers who need to deploy capital imminently in identified investment opportunities, the discretionary nature of the approval leaves an element of uncertainty on tax position on income or gains earned from investments made during the application processing period.

Singapore continues to be a key wealth and asset management hub in Asia Pacific region. This is evidenced by the fact that the global and regional fund managers are seeking to set up and expand their business presence in Singapore. In addition, the fund managers are increasingly considering the viability and implementation of pooling capital in Singapore for investing in the Asia Pacific region. The introduction of Variable Capital Company, a new legal form for investment funds, in January 2020 has enhanced Singapore's appeal as a fund location. The policy measures coupled with socio-economic factors and geo-political stability have helped Singapore to attract senior talent and witness Singapore-led deal activities. These factors lay a foundation for fund managers to consider applying for substance-based fund tax incentives schemes to obtain a higher tax certainty for their investors and the uptrend is likely to continue. We hope that the MAS will look at measures to reduce the application processing time by deploying additional resources to meet the strong demand.

Australia tax development

7 Australian Budget and Patent Box Expansion

The Australian Federal Budget 2022 was delivered on 29 March 2022 by the Federal Treasurer Josh Frydenberg. This Budget builds on last year's announcement of a new Australian patent box regime, by:

- Expanding support from the current focus on medical and biotechnology industries to new innovations in the agricultural chemical and low emission technology areas. The expanded patent box regime will provide an incentive for companies to innovate with a concessional patent tax rate of 17% to apply to income derived from patents which have the potential to lower emissions, or patents linked to agricultural and veterinary chemical products listed on the Australian Pesticides and Veterinary Medicines Authority, Public Chemicals Registration Information System register, or eligible Plant Breeder's Rights. This will apply to patents granted or issued after 29 March 2022, and for income years from 1 July 2023

- Expanding the 2021 Budget measure to allow patents granted or issued for medical and biotechnology innovations after 11 May 2021 to be eligible as well as allowing standard patents granted by IP Australia, utility patents issued by United States Patent and Trademark Office and European patents granted under the European Patent Convention to be eligible. However, taxpayers will still only benefit from the concessional tax treatment to the extent that the R&D occurred in Australia.

While it is pleasing that the patent box regime has been extended to new industry areas, it is disappointing that it still applies to a narrow range of industries, as most global patent box regimes are industry agnostic. We also note that there is a misalignment of the eligible patent dates between different industry sectors. It is expected that there will be a consultation period around these proposed measures.

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New Zealand tax development

8 Proposed dividend integrity measure

Following an increase to the top personal tax rate to 39% from 1 April 2021, policy officials released a discussion document on 16 March 2022, exploring a number of "integrity measures" to mitigate the New Zealand (NZ) Government's concerns of individuals circumventing the top personal tax rate by extracting funds from a company without incurring a tax liability.

From the three proposals put forward, of primary significance is the proposal to treat the sale of shares in a company by a NZ controlling shareholder (but not a foreign controlling shareholder) as a taxable dividend, to the extent that the company has underlying retained earnings. We view this to essentially be a capital gains tax (CGT), dressed up as an integrity measure, potentially in lieu of the NZ government not proceeding with a general CGT back in 2019. Our view, aligned with that of the general NZ market, is that this proposal results in several adverse outcomes and unnecessarily captures a broad range of transactions, rather than specific situations that actually present issues of potential avoidance of the 39% top personal tax rate which can be dealt with specifically.

This would have totally unreasonable outcomes for a long-time family business owner of a company that has accumulated significant retained earnings for the purpose of reinvesting in assets / growth for the future, particularly where no carve-outs are being introduced (e.g., currently there are no carve-outs that only retained earnings accumulated post implementation date are subject to tax, nor are there carve-outs that protect subsequent taxation of the same underlying retained earnings on a subsequent sale).

This sale of shares proposal will likely result in several founder-owned businesses with substantial retained earnings to contemplate selling shares before legislation takes effect, proposedly during the 2023/24 income year. This presents an opportunity for private equity / venture capital networks to offer majority shareholders the chance to de-risk by selling 51% ownership, although some revision / retraction of the proposals is expected. For clients already on the verge of a potential transaction, this could provide the impetus for a deal to occur.

This is only the first of three tranches of integrity proposals in the pipeline. While the Government may look to refine the current proposal (considering the significant adverse feedback around the over-reaching scope and effective capital gains tax), public submissions are likely to push further for a complete reversal.

An additional proposal, to require companies to track their available subscribed capital and capital gain amounts (similar to maintaining an imputation credit account) is more sensible and welcome.

9 Australian limited partnerships and foreign tax credits

NZ policy officials have recently issued a draft public ruling to provide clarity on the ability of a NZ resident partner of an Australian Limited Partnership (ALP) to claim foreign tax credits for Australian tax paid.

Particular guidance to note, is as follows:

- Foreign tax credits will be available to NZ resident partners where Australian tax is paid on the income earned by the ALP. This includes the ALP's trading income, taxable distributions from unit trusts and fee income derived by the ALP as 'head company' of an Australian tax consolidated group.
- No foreign tax credit is available for distributions made by an ALP to NZ resident partners where the NZ resident partners are not receiving taxable distributions, even where Australian dividend withholding tax is withheld. This could cover various different scenarios, but one example given relates to unfranked distributions, where the distribution may be seen as drawings from the partnership, and not taxable for NZ income tax purposes.
- No foreign tax credit is available where the ALP has paid no income tax. Where the ALP receives a franked dividend from its subsidiary, no foreign tax credit will be available for the NZ resident partners in relation to the franking credits, as the ALP has paid no income tax.

We view these rulings to be logical and non-controversial. The significance of these updated rulings is likely minor, as these arrangements are relatively uncommon.

EU tax development

10 EU Member States adopt revised list of noncooperative jurisdictions for tax purposes

On 24 February 2022, the Council of the EU (the Council) updated the EU list of noncooperative jurisdictions for tax purposes (the EU List).

Annex I of the EU List remained unchanged and it still includes American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands and Vanuatu.

With respect to Annex II of the EU List and the state of play of pending commitments, the Council decided to add 10 jurisdictions (Bahamas, Belize, Bermuda, British Virgin Islands (BVI), Israel, Montserrat, Russia, Tunisia, Turks and Caicos, and Vietnam). The 25 jurisdictions now listed on Annex II are Anguilla, Bahamas, Barbados, Belize, Bermuda, Botswana, BVI, Costa Rica, Dominica, Hong Kong, Israel, Jamaica, Jordan, Malaysia, Montserrat, North Macedonia, Qatar, Russia, Seychelles, Thailand, Tunisia, Turkey, Turks and Caicos, Uruguay and Vietnam.

The Council will continue to review and update the EU List biannually, with the next update due in October 2022.

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