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Review of 2017 Singapore Tax Controversies: Disputes on Income Tax, GST, Stamp Duty and more

In 2017, we saw a total of 12 reported decisions with taxpayers litigating against the tax authority in Singapore. This is a marked increase from the previous year, which had only six reported decisions on tax-related issues.

Of the 2017 decisions, six cases dealt with substantive income tax issues involving taxpayers' challenge against the Comptroller of Income Tax's ("**Comptroller**") assessments, at both the High Court and Board of Review stages. As for the remaining cases, there was one decision on stamp duty, two on non-payment of income tax and goods and services tax ("**GST**"), one on exchange of information, and another two which dealt with interlocutory applications in the court proceedings convened in the aftermath of *AQQ*[1]. In this alert, we provide a snapshot of these cases below (though necessarily not in the same order).

A charitable trust does not have to pay Additional Buyer's Stamp Duty

Zhao Hui Fang v Commissioner of Stamp Duties [2017] 4 SLR 945 ("***Zhao Hui Fang***") concerned a dispute over liability for Additional Buyer's Stamp Duty ("**ABSD**"). In that case, the deceased had set up a charitable trust and also left behind a will. The will provided that his surviving family members (including his wife) may use a certain property as their personal residence, and that if none of them wished to use it as such, the property may be leased or disposed and any income or proceeds shall be paid to a charitable trust. Subsequently, the executors of the will sold the property, and bought a replacement property to house the deceased's wife.

The dispute was centred on whether the purchase of the replacement property attracted ABSD. Under the Stamp Duties Act ("**SDA**"), sale of residential property to a "foreigner" or "entity" attracts 15% ABSD. Where the property is transferred to a trustee, the chargeability of ABSD depends on whether the beneficial owner is a "foreigner" or an "entity".

The High Court found that no ABSD was payable on the transaction, because the replacement property was the property of a charitable purpose trust, under which the beneficial interest of trust assets was suspended. There was no ascertained or ascertainable beneficial owner of the replacement property. The High Court had arrived at this conclusion by applying trust law principles, and had rejected finding any of the following parties as the beneficial owners: (i) the deceased's wife, who merely had a personal license to use the replacement property (ii) the persons who factually benefit from the trust, (iii) the trustees, or (iv) the public at large.

[1] *Comptroller of Income Tax v AQQ* [2014] SGCA 15

It is also notable that the High Court cautioned against the reliance on government-issued press statements to aid a purposive construction of statutes. Several reasons were given, *inter alia*, that they are generally prepared post-enactment, and that their purpose is to explain the regime to laypersons in a simple and easily understood way without being legally precise or with the intent to have legal effect. In this particular case, the High Court held that the press statement regarding the ABSD regime which both parties relied on was anyway ambiguous on the issue of whether ABSD was intended to apply to conveyances to a charitable purpose trust.

While we observe that the decision would appear to be a strict adherence to trust law principles, there is a question of whether the holding would leave a lacunae in the ABSD regime that could have been unintended by Parliament. It would be interesting to see whether the same analysis (and consequences) may be applied to other types of trusts under which the beneficial interest is suspended based on trust law principles. In particular, we note that under Singapore law, while non-charitable purpose trusts are generally held to be void, there are exceptions to this principle.

Deductibility of interest payments under Section 14(1)(a) of the Income Tax Act ("ITA")

BML v Comptroller of Income Tax [2017] SGHC 118 ("***BML***") is the latest decision on interest deductibility under section 14(1)(a) of the Income Tax Act (Cap. 134) ("**ITA**"). The decision arose from an appeal against the Board of Review decision reported in *GBK v The Comptroller of Income Tax* [2016] SGITBR 3.

The taxpayer owned and operated a mall. It underwent a securitisation exercise whereby it assigned its rights to rental income from the mall as security for a $520 million loan. Subsequently, the shareholders decided to convert their equity holdings into fixed rate bonds, so that they could earn interest on their investments instead of dividends. The conversion was implemented via a reduction of share capital, followed by the issuance of bonds.

Section 14(1)(a) of the ITA requires interest to be payable "on capital employed in acquiring the income", in order to be deductible. The taxpayer argued that the money borrowed on the bonds represents the capital of the company, which is represented by income-producing assets. Therefore, the interest on the bonds was deductible.

The High Court upheld the principle established in earlier cases that to meet the test in section 14(1)(a), there must be a direct link between the money borrowed and the income produced. It went on to hold that it must be "real tangible, precise, and factual", which requires a consideration of a number of factors. The High Court considered the following factors to be relevant: whether the money borrowed had an observable effect on income produced, the purpose of borrowing the money, and whether it was necessary to borrow the money. Further, the High Court held that section 14(1)(a) gives the Comptroller a discretion in determining whether the requirements under the provision are met.

The High Court dismissed the taxpayer's appeal because it "faced a few problems" in establishing a direct link between the bonds and the mall's rental income. First, the mall was already owned by the taxpayer and was generating income – the bond issue did not change that. Second, the taxpayer's shareholders admitted in evidence that the bond issue was part of a capital restructuring plan and not for financing needs or the desire to generate more rental income.

Section 10(1)(g) of the ITA – the "catch-all" provision

There were two reported decisions in 2017 applying Section 10(1)(g) of the ITA: *GBU v The Comptroller of Income Tax* [2017] SGITBR 3 ("***GBU***") and *GCA and GCB v The Comptroller of Income Tax* [2017] SGITBR 5 ("***GCA and GCB***"). Section 10(1)(g) is the "catch-all" provision that taxes any "gains or profits of an income nature" even where such income does not fall within the heads of charge under Sections 10(1)(a) to (f) of the ITA.

The gains in *GBU* arose from the disposal of share counters by a Singapore company which carried out the principal business of operating supermarkets; whereas in *GCA and GCB*, the gains arose from the disposal of residential properties by a husband and wife. Both decisions were centred on a factual inquiry which examined the motive of the taxpayer at the time of acquisition of the relevant asset, but the outcomes differed.

In *GBU,* the Board was convinced that the company had purchased the share counters as long-term investments. It appears that the Board was persuaded by evidence that the company had substantial cash and had purchased shares to enjoy a better return than the interest rate offered by the bank. The Board rejected the Comptroller's arguments that the shares were not long-term investments because the company intended to sell the shares prior to it being listed, or when the share values sufficiently appreciate. The Board reasoned that the listing of the company was not a fixed event at the time of acquisition, and found that the company had taken a long-term perspective towards the appreciation of the shares. The exact holding period was not clear from the decision, but the Board emphasized that the concept of "long-term" may be different for an investor in shares and for an investor in real property.

In *GCA and GCB*, however, a different conclusion was reached. The taxpayers had bought and sold three properties in succession over a five-year period, without occupying any of them. Each property was held for less than 1 year. At the audit stage, the taxpayers initially stated that they had acquired the properties for their own use or for rental purposes, and disposed of the same to "realise profit". During the proceedings, however, the taxpayers asserted that they had to use each property as their personal residence, but had then sold them due to their unsuitability as family homes. The Board found that the taxpayers gave contradicting evidence and held that they had, at the time of acquisition, an intention to buy and sell the properties to make a profit.

Taxation of employment income

GBS v Comptroller of Income Tax [2017] SGITBR 1 ("***GBS***") is the first case in Singapore that decides on the taxability of a payment to an employee upon the termination of his employment.

The Comptroller's administrative position is that severance payments that are made to compensate loss of employment are not taxable as they are capital receipts, but other payments such as gratuity for past services are taxable as employment income. In *GBS*, it appears that the legal test was not significantly disputed. Instead, the taxpayer argued that the payment in question was a redundancy payment given that he departed upon his position being made redundant. It did not help the taxpayer's case, however, that his service agreement with his employer had explicitly provided for a long service gratuity and the amount of payment was consistent with the method provided in the agreement. The Board held that the payment was indeed made pursuant to the agreement as a gratuity for services, and therefore taxable.

Given the fact pattern in *GBS*, this area of law has still not been extensively tested. Interestingly, we observe that the Board had added that even if the payment was not a gratuity payment but a "termination payment", it would have been taxable because all "termination payments" are taxable based on cases cited by the Comptroller. We would respectfully submit that this pronouncement is overly wide and potentially misleading. The label of "termination payment" does not say much about the exact nature of the payment, and still requires an examination of what the payment is made for, for taxation purposes.

Another employment tax case that was decided in 2017 is *GBX v The Comptroller of Income Tax* [2017] SGITBR 4. In brief, the taxpayer, who was an Australian citizen, attempted to argue that the income received under a contract of service with an Australian company was not taxable as employment income, because he failed to register an employment pass with that company in Singapore. This was rejected by the Board, which held that an employment contract existed (notwithstanding the absence of an employment pass) and the income received thereunder was taxable as employment income.

AQQ saga continues

AQQ is Singapore's landmark decision on general anti-avoidance rules under section 33 of the ITA. The Comptroller successfully demonstrated that the taxpayer had fallen foul of section 33 but failed to recover the monies for procedural reasons. The Comptroller then commenced a fresh suit to recover such monies via civil proceedings, on the grounds of unjust enrichment, fraudulent misrepresentation, and others. One of the issues in the suit was whether the Comptroller's action was time-barred under the Limitation Act.

Two decisions were reported in 2017 on interlocutory applications that were filed in the new suit. These decisions are unique in that they relate to discovery (i.e., disclosure) sought by the taxpayer against the Comptroller for the Inland Revenue Authority of Singapore's ("**IRAS**") internal documents.

In *Comptroller of Income Tax v ARW and another* [2017] SGHC 16, the High Court ordered the Comptroller to provide discovery of documents relating to the Comptroller's (i) decision to pay tax refunds; (ii) audit on the taxpayer; and (iii) determination that the taxpayer had made use of a tax avoidance arrangement and decision to invoke section 33 of the ITA. The High Court agreed with the taxpayer that these documents were relevant and necessary for the fair and efficient disposal of the matter (as they relate to issues of time bar and the

Comptroller's state of mind), and were not protected by litigation nor legal advice privilege.

Subsequently, the Comptroller sought to submit further arguments, *inter alia,* that the documents relating to the audits should not be disclosed as they are protected by public interest privilege under s 126 of the Evidence Act. In addition, the Attorney General applied to intervene in the discovery application, arguing that it was the guardian of the public interest, and therefore obliged to intervene in applications concerning public interest privilege. The High Court allowed the Attorney General's application as well as the Comptroller's request to submit further arguments in *Comptroller of Income Tax v ARW and another* [2017] SGHC 180. No decisions have been reported to date on the outcome of the argument on public interest privilege.

Issues relating to discovery and privilege aside, we note that the subject of the main suit raises an interesting question. Under section 74(1) of the ITA, the Comptroller is barred from raising additional assessments after the expiry of the statutory limitation period of 4 years. Should the Comptroller be allowed to recover the monies paid out to the taxpayer through a common law action within the limitation period of 6 years, even in the absence of fraud or wilful default? Would this fundamentally change the time at which taxpayers are entitled to regard their tax assessments to be final?

Where the taxpayer fails to pay the tax assessed

Comptroller of Income Tax v BLO [2017] SGHC 50 illustrates the drastic consequences a taxpayer may face if he does not pay the income tax assessed by the Comptroller, regardless of whether he agrees with the tax assessment.

In that case, the Comptroller filed an application to wind up a corporate taxpayer, after the taxpayer failed to comply with the Comptroller's statutory demand for tax due. The taxpayer resisted the application by asserting that there was a substantial and *bona fide* dispute over the debt, because it intended to object or appeal against the Comptroller's assessments.

The High Court refused to stay the application, as the Defendant had failed to show the existence of a substantial and *bona fide* dispute. Under section 85(1) ITA, it was clear that the tax was payable one month after the service of a notice, regardless of any objection or appeal. Any dispute of assessments had to be done via the ITA's statutory process.

For an appeal against a GST assessment, section 51(8) of the GST Act provides that the taxpayer must pay or deposit the amount of tax assessed before the appeal could be heard, unless the Comptroller or the GST Board agrees otherwise on the grounds that the taxpayer would suffer hardship. In *GBQ v CGST* [2017] SGGST 1 ("***GBQ***"), the issue was whether such grounds of hardship were made out.

Relying on UK case law, the GST Board held that the general test was whether the taxpayer had the capacity to pay the entire sum assessed and not just parts thereof, without financial hardship, at the time of the application hearing. This included considering the ability to pay from resources that are readily available. However, noting that this case involved an individual rather than a business, the

Board declined to set down a general principle that individuals were expected to sell assets to meet statutory tax obligations. Ultimately, a pragmatic approach would be adopted, considering all the facts and circumstances of the case.

The GST Board found that the grounds of financial hardship were not made out because according to the taxpayer, he did not have hardship but merely had a lot of "burden" in running his business. Further, no substantive evidence was provided to support his claim of hardship, and he also failed to explain material facts pertaining to his assets.

Interesting decision on the deductibility of payment on a related party transaction

In *GBT v The Comptroller of Income Tax* [2017] SGITBR 2, the individual taxpayer was employed as a Financial Services Director and received commission income in that capacity. The taxpayer claimed that he reached an oral agreement with a company that was owned by him and his wife, to pay the entire commission income to that company in exchange for consultancy and management services. While the taxpayer did not seriously dispute that the commission income was his personal income, he claimed that he was entitled to deduct the payment to his and his wife's company from his personal income for tax purposes.

The Board found that there was insufficient evidence of an agreement between the taxpayer and the company – in particular, the evidence provided merely showed that the company had employees but there was no credible evidence documenting the consultancy and management services provided by the company. The Board also found that the purported arrangement lacked commercial sensibilities, and the taxpayer's reasons for the arrangement unconvincing. Accordingly, the Board was not persuaded that the payment of commission income to the company was "wholly and exclusively incurred" for the production of the commission income itself.

This is an interesting decision from many aspects. Presumably, the company had already been taxed on the commission income. One question is whether the Comptroller would then agree to revise the company's assessment to exclude that commission income, in light of the decision. Further, it appears that the Comptroller had also raised anti-avoidance arguments under section 33 of the ITA but the Board did not have to consider this in light of the finding on the deductibility issue. Finally, the decision alluded to the question of whether the arrangement would have been entered into if the conditions were arm's length, but no transfer pricing issues were considered.

Another decision on exchange of information

Last but not the least, yet another taxpayer attempted a judicial challenge against exchange of information but failed, in *AXY and others v Comptroller of Income Tax (Attorney-General, Intervener)* [2017] SGHC 42.

In that case, the applicants had sought leave from the High Court to commence judicial review of the Comptroller's decision to issue notices for information to various banks in Singapore to fulfil an exchange of information request made by the Korean tax authorities.

The High Court reaffirmed the test in *ABU v Comptroller of Income Tax* [2015] 2 SLR 420 that the scope for judicial review of the Comptroller's decision to comply with a foreign tax authority's request for information is limited. It was held that the applicants had failed to establish an arguable or *prima facie* case of reasonable suspicion that the Comptroller's decision to issue the notices was either illegal or irrational.

Concluding remarks

2017 has been a relatively interesting year for the development of Singapore's tax case law.

Zhao Hui Fang is a landmark decision on a charitable trust's liability for ABSD. *BML* further develops the case law on interest deductibility, in the wake of a series of earlier cases on the same issue (e.g., the notable Court of Appeal case of *BFC v Comptroller of Income Tax*[2]). There have also been a number of cases which decide on certain Singapore tax issues for the first time, such as *GBS* (taxation of gratuity payment) and *GBQ* (the test for hardship in exempting payment for appeal against GST assessment). Taxpayers secured victories in certain cases while in others, their case had faltered often on evidentiary grounds.

Taxpayers are encouraged to review and consider the impact of the recent decisions on their businesses as well as any ongoing audits or disputes with IRAS.

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[2] [2014] 4 SLR 33