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GBF v Comptroller of Income Tax

In GBF v Comptroller of Income Tax (2016) SGITBR 1, the Income Tax Board of Review had to determine whether Singapore's general anti-avoidance rules ("GAAR") applied to an arrangement put in place by the taxpayer, a medical practitioner, in which "physician compensation" was paid to a partnership comprising two corporate partners owned by himself and his wife respectively.

GBF facts

- In 1996, the taxpayer incorporated a company to carry on the business of plastic and cosmetic surgery. The taxpayer has been employed by the company since its incorporation and is the sole medical practitioner at the company. Although not stated explicitly, the taxpayer's income arising from this arrangement should comprise primarily dividends and salaries.

- The taxpayer sold the company in early 2008. Post-sale, the taxpayer remained as an employee and sole medical practitioner of the company; likewise there were no changes to the business operations of the company.

However, the taxpayer elected to form the aforementioned partnership to receive "physician compensation" – essentially his medical practitioner's income. In streaming this income to be taxed in the hands of the partnership's corporate partners, the taxpayer was able to enjoy the start-up tax exemption scheme[1] twice, resulting in substantial tax savings.

- The Comptroller of Income Tax sought to disregard the arrangement by invoking anti-avoidance provisions under Section 33 and treat the physician compensation as income as derived by the taxpayer instead of the partnership, so as to negate the benefits of the start-up tax exemption scheme.

Deloitte's views

Having considered the overall circumstances of the arrangement and evidence and submissions presented, the Board found that the taxpayer's arrangement triggered the anti-avoidance provisions[2] and that he was unable to rely on the statutory exception in Section 33(3)(b) of the Singapore Income Tax Act, which require proof that the arrangement was carried out for bona fide commercial reasons and had not as one of its main purposes the avoidance or reduction of tax.

In arriving at its conclusion, the Board followed the principles laid down in the landmark case of AQQ v Comptroller of Income Tax (2014) SGCA 15, in which Singapore's apex court first considered the statutory construction of Section 33. In this regard,

- Based on an objective assessment of the arrangement, the Board regarded it as being formed solely[3] to receive the physician compensation in the most tax efficient manner. In other words, the Board was not convinced that formation of a partnership to receive physician compensation was capable of explanation by reference to ordinary business or family dealings and the "obvious"[4] effect of the arrangement resulted in substantial tax savings.

- Based on a subjective assessment of the taxpayer's intention for entering into the arrangement, the Board rejected the expressed intention of the taxpayer that the purpose of forming the corporate partnership is due to the various business benefits that it offered and

[1] Briefly, the first $200,000 of chargeable income derived by a company enjoying the start-up tax exemption scheme is tax exempt.
[2] GBF v Comptroller of Income Tax (2016) SGITR 1, at [10](iii); " … the requirements of Section 33(1)(a), (b) and (c) have clearly been satisfied"
[3] Ibid., at [10](i)
[4] Ibid., at [10](iii)

protection from practice and business risks. There was no contemporaneous documentation that such benefits were the reasons considered by the taxpayer at the material time when the corporate partnership was formed. In addition, the Board also inferred, based on the acts of the taxpayer and other objective evidence, that such business benefits never materialized; amongst others, there was no record of the partnership (instead of the taxpayer) providing medical services to the company, no other practitioner was ever invited to join the partnership, and the role of the taxpayer's wife as a partner in the partnership was 'inexplicable'[5] as the taxpayer remained the sole medical practitioner.

- It is not apparent whether the Board considered if the tax advantage obtained by the taxpayer was "within the intended scope and Parliament's contemplation and purpose, both as a matter of legal form and economic reality within the context of the entire arrangement"[6]. This consideration formed part of the 'scheme and purpose' approach formulated in AQQ and forms an additional safeguard against the potential 'over-inclusiveness' of Section 33(1), which potentially catches "any arrangement that has an objectively ascertainable purpose of reducing or avoiding tax"[7]. That said, the raison-d'etre for introducing the start-up tax exemption in Budget 2004 was to 'spur entrepreneurship'[8]. In this regard, it is doubtful that the formation of two additional companies, without any material change to the business operations of the medical practice, falls within the object and purpose of the start-up tax exemption.

Conclusion

It has always been in the interest of taxpayers to arrange their affairs so as to mitigate the tax outcome of their transactions. However, the line between permissible tax mitigation and objectionable tax avoidance is not always clearly delineated. In this regard, the framework laid down by AQQ on the statutory construction of Section 33 is undoubtedly helpful and was applied by the Board in GBF in determining whether the arrangement undertaken by the taxpayer constitutes tax avoidance. The IRAS has also issued guidance[9] on, amongst others, what it considers as 'hallmarks' of tax avoidance.

[5] Ibid. 2, at [10](vii)
[6] Comptroller of Income Tax v AQQ (2014) SGCA 15, at [110](c)
[7] Ibid., at [74]
[8] Ministry of Finance, Corporate Income Tax, http://www.mof.gov.sg/Policies/Tax-Policies/Corporate-Income-Tax, Accessed 3 November 2016
[9] Income Tax: The General Anti-avoidance Provision and its Application (First Edition), published on 11 July 2016

These are, namely: -

(i) Circular flow or round-tripping of funds;
(ii) Set-up of more than one entity for the sole purpose of obtaining tax advantage;
(iii) Changes in the form of business entity for the sole purpose of obtaining tax advantage; and
(iv) Attribution of income that is not aligned with economic reality.

With the benefit of hindsight, the arrangement in GBF arguably contains three out of the four 'hallmarks' and the outcome of the case is perhaps not unexpected. Nevertheless, the determination of tax avoidance invariably "depends on the facts" of the specific case and there will be instances where there would be difficulties in the application of the conceptual framework to the facts. As Singapore develops legal jurisprudence in the area of tax avoidance, taxpayers are advised to seek professional advice whenever they are unsure of the tax effects of their contemplated arrangements.

Contacts

For more information on any of these issues, or any other Business Tax matters, please contact **Low Hwee Chua**, or your usual Business Tax Services contact in Deloitte.

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