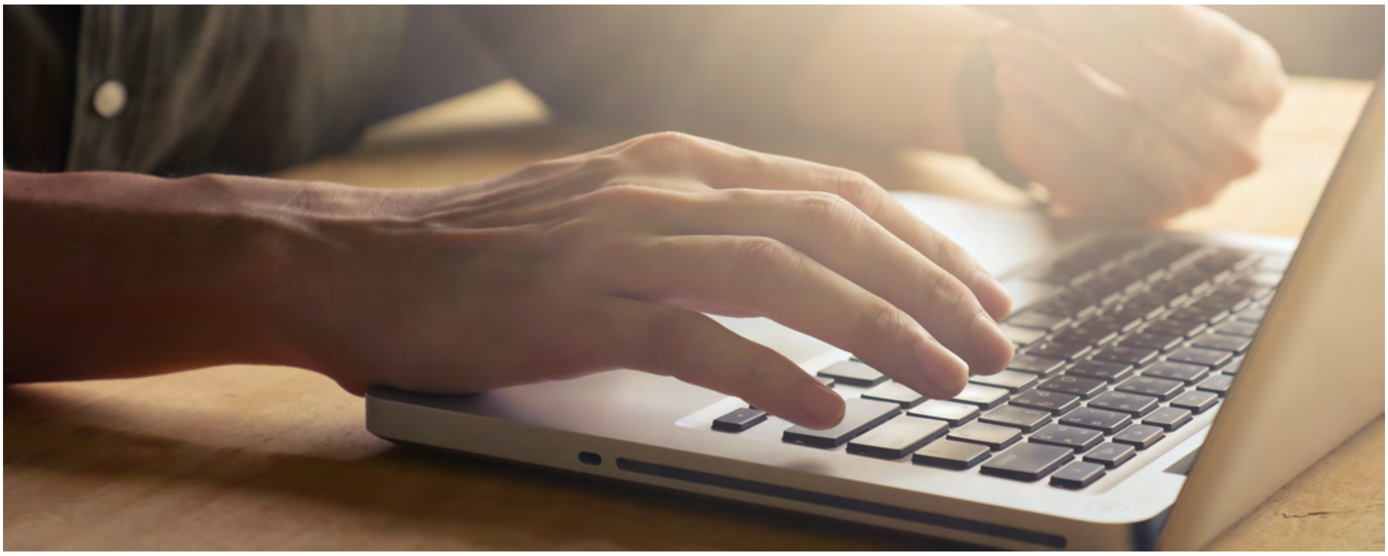
Tax Alert
ISSUE 04 | **MARCH 2020**

Economics and Taxation in the Digital Economy



This article was first published in the Business Times on 12 March 2020.

As businesses transact without being physically present, countries have found it difficult to tax the income earned by foreign corporations in their territories.

Technological advancements have dramatically changed the global trade of goods and services, placing immense pressure on internationally-accepted principles governing the taxation of cross-border business income.

Today, businesses can transact without being physically present in a market; this is increasingly the reality for many businesses across not only retail but other sectors. As this continues to be the new normal, countries have increasingly found it more difficult to tax business income earned in their territories by foreign corporations under existing international tax frameworks.

In the face of this new reality, we are already seeing certain countries starting to adapt their tax laws. As more businesses adopt digitalisation strategies, new tax laws that apply beyond GAFA (Google, Amazon, Facebook, Apple) businesses are being put in place, becoming applicable to brick-and-mortar businesses that operate globally as well.

A growing number of countries have adopted the destination principle, which requires foreign residents who sell goods and services in their territories to register for goods and services tax (GST) purposes. The destination principle is now being considered for application even to taxes on revenue.

Countries seeking to implement unilateral digital service taxes on revenue, such as France, the United Kingdom (UK) and now Spain, have had considerable push back from the US, where many of the large technology firms are based.

Pressure has been placed on those countries to wait for an international consensus on the redesign of the global taxation frameworks to ensure countries get a fair allocation of taxing rights over income from such digital sales and services.

This redesign is currently underway through the Base Erosion and Profit Shifting (BEPS) initiative of the Organisation for Economic Co-operation and Development (OECD).

One of the key aims of the BEPS programme is to combat tax planning strategies used by some multinational companies to avoid taxes, including by "shifting" profits from higher-tax jurisdictions to be allocated to lower-tax jurisdictions, thus eroding the tax-base of the higher-tax jurisdictions.

The initiatives that have already been implemented in the last five years under the original round of BEPS proposals have seen significant changes in the field of international taxation.

The new round of proposals (BEPS 2.0), expected to be finalised later this year, seek to address the challenges of the digitalisation of the economy. The preliminary proposals look set to introduce arguably even more radical changes to the international tax framework, including a dramatic overhaul of transfer-pricing principles.

While it will be important to calibrate the country's tax regime and incentives in response to BEPS 2.0, any changes are unlikely to take place until the measures are clearer and the full implications to Singapore can be determined.

International tax developments are of special interest to Singapore, which has been the preferred springboard for investments into the Asia-Pacific region for numerous reasons, including its regulatory environment and political stability. These factors, combined with business-friendly tax rules and targeted incentives, have been key considerations for attracting overseas investments to Singapore and making Singapore a more compelling location for commercial ventures, for both large and small enterprises.

The BEPS 2.0 proposals can have implications for Singapore in a number of ways. The transfer pricing changes in Pillar 1 of the proposals seek to allocate greater taxing rights to jurisdictions where the consumer is based, and there is concern that Singapore will lose out on revenue given its relatively small population.

In this regard, Deputy Prime Minister and Minister for Finance Heng Swee Keat said during his Budget 2020 round-up speech that "hub economies with small markets like Singapore stand to lose corporate income tax revenue if new rules (under BEPS 2.0) are adopted".

In the latest OECD updates on the proposals, the key types of businesses in scope of the Pillar 1 measures are those that generate revenue from the provision of automated digital services (such as social media platforms or online marketplaces) and consumer-facing businesses.

Carve-outs for particular industries such as the extractive sector, including commodity players and the financial-services sector, are still being considered. The OECD estimates a drop of taxable revenue in investment hub countries by up to 5 per cent.

Multinational groups are also concerned that the corporate tax changes in Pillar 2 of the proposal, which seeks to impose a global minimum tax concept, may undermine Singapore's position by neutralising the effects of its tax incentives. A key concern of businesses centres on whether Singapore will increase its corporate tax rate or the basis of taxation in an attempt to balance any potential loss of revenue.

While it will be important to calibrate the country's tax regime and incentives in response to BEPS 2.0, any changes are unlikely to take place until the measures are clearer and the full implications to Singapore can be determined.

That said, without immediate counteracting measures to attract multinational investment, Singapore's competitiveness as a business and technology hub could be threatened and diminished.

To protect its hub status, we believe Singapore should continue to pursue a broad mix of policy tools, including enhancing its tax competitiveness in new ways to encourage businesses to generate substantive economic activities in Singapore.

In particular, a holistic approach should be undertaken to review the attractiveness of Singapore as the Transformation Capital of Asia, if not globally, to position it as the best place in the region for enterprises to lead the digital transformation of their business models and operational practices.

Singapore should continue to focus on building industry-sector ecosystems for enabling and funding collaborations to transform and innovate solutions to be used in solving issues faced by the country in the areas of productivity growth, sustainability, rising healthcare and digital adoption.

Aside from benefiting companies based in Singapore, these solutions can also be then exported to countries outside Singapore, putting the country in a leadership position for the region in this sector.

The "transform-and-grow" announcements in Budget 2020 are steps in the right direction, with some new measures and enhancements to existing grants to drive transformation. Indeed, moving towards more cash-based incentives could be one of the ways forward as BEPS 2.0 seeks to neutralise the effect of tax incentives. With support from the Government, companies operating in Singapore will become more profitable and invest locally in expanding their operations and employing people.

It would also enhance Singapore's competitiveness to attract the best global talent from around the world. All this will help Singapore to withstand and counteract the challenges posed by the new international tax frameworks aimed at digitisation of the economy.

Authors

Tan Chee Wei
Partner
T: +65 6213 2470
E: cheeweitan@kpmg.com.sg

Alia Lum
Partner
T: +65 6213 3203
E: alum1@kpmg.com.sg

Contact us

Tay Hong Beng
Partner
Head of Tax
T: +65 6213 2565
E: hongbengtay@kpmg.com.sg

Ajay K Sanganeria
Partner
Deputy Head of Tax
T: +65 6213 2292
E: asanganeria@kpmg.com.sg

BANKING & INSURANCE

Alan Lau
Partner
T: +65 6213 2027
E: alanlau@kpmg.com.sg

Contact us

REAL ESTATE & ASSET MANAGEMENT

Teo Wee Hwee
Partner
T: +65 6213 2166
E: weehweeteo@kpmg.com.sg

Agnes Lo
Partner
T: +65 6213 2976
E: agneslo1@kpmg.com.sg

Anulekha Samant
Partner
T: +65 6213 3595
E: asamant@kpmg.com.sg

Leonard Ong
Partner
T: +65 6213 2038
E: leonardong@kpmg.com.sg

ENERGY, TECHNOLOGY, MEDIA & TELECOMMUNICATION

Gordon Lawson
Partner
T: +65 6213 2864
E: glawson1@kpmg.com.sg

Larry Sim
Partner
T: +65 6213 2261
E: larrysim@kpmg.com.sg

Lim Li Peng
Partner
T: +65 6213 3709
E: lipenglim@kpmg.com.sg

INFRASTRUCTURE, GOVERNMENT & HEALTHCARE

Chiu Wu Hong
Partner
T: +65 6213 2569
E: wchiu@kpmg.com.sg

Gan Kwee Lian
Partner
T: +65 6213 2546
E: kweeliangan@kpmg.com.sg

Toh Boon Ngee
Partner
T: +65 6213 2052
E: btoh@kpmg.com.sg

CONSUMER & RETAIL

Tan Chee Wei
Partner
T: +65 6213 2470
E: cheeweitan@kpmg.com.sg

CORPORATE TAX PLANNING & COMPLIANCE

Mak Oi Leng
Partner
T: +65 6213 7319
E: omak@kpmg.com.sg

Pauline Koh
Partner
T: +65 6213 2815
E: paulinekoh@kpmg.com.sg

PERSONAL TAX & GLOBAL MOBILITY SERVICES

Anna Low
Partner
T: +65 6213 2547
E: alow@kpmg.com.sg

Dennis McEvoy
Partner
T: +65 6213 2645
E: dennismcevoy@kpmg.com.sg

GOODS AND SERVICES TAX

Lam Kok Shang
Partner
T: +65 6213 2596
E: kokshanglam@kpmg.com.sg

Gan Hweee Leng
Partner
T: +65 6213 2813
E: hweelenggan@kpmg.com.sg

Contact us

TRANSFER PRICING

Felicia Chia
Partner
T: +65 6213 2525
E: fchia@kpmg.com.sg

Lee Jingyi
Partner
T: +65 6213 3785
E: jingyilee@kpmg.com.sg

PROPERTY TAX & DISPUTE MANAGEMENT

Leung Yew Kwong
Principal Consultant
T: +65 6213 2877
E: yewkwongleung@kpmg.com.sg

R&D & GRANTS CONSULTING

Harvey Koenig
Partner
T: +65 6213 7383
E: harveykoenig@kpmg.com.sg

TAX TRANSFORMATION & GOVERNANCE

Alia Lum
Partner
T: +65 6213 3203
E: alum1@kpmg.com.sg

US TAX SERVICES

Daniel Joe
Partner
T: +65 6213 2626
E: danieljoe@kpmg.com.sg

TAX – DEALS, M&A

Adam Rees
Principal Advisor
T: +65 6213 2961
E: adamrees@kpmg.com.sg

KPMG
16 Raffles Quay #22-00
Hong Leong Building
Singapore 048581
T: +65 6213 3388
F: +65 6220 9419
E: tax@kpmg.com.sg

Ranked Tier 1 Firm in Singapore – World Tax, World Transfer Pricing and Tax Transactional 2019, *International Tax Review*

National Transfer Pricing Firm of the Year – Asia Tax Awards, 2018 & 2019, *International Tax Review*

Withholding Tax Team of the Year – Asia Tax Awards 2019, *International Tax Review*

For more information, please view our tax services page.

kpmg.com.sg