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Investing in Australian Non-Residential Property

The Feng Shui of Asset Protection

Vietnam, a destination for international IT business

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IN THIS ISSUE

p.3 Investing in Australian Non-Residential Property

p.6 The Feng Shui of Asset Protection

p.8 Vietnam, a destination for international IT business

p.10 Singapore, application of GST on Digital Services effective from 2020

p.13 New Free Trade Agreement

p.15 The importance of maintaining economic substance in international structuring

INVESTING IN AUSTRALIAN NON-RESIDENTIAL PROPERTY

Introduction

Australia actively promotes overseas investment, and unlike many countries it has limited barriers to entry into the market. This is evidenced by the large amount of capital inflows from overseas including Canada, Europe and Asia, due to the "safe haven" status of the Australian property market. However consideration should be given to the potential tax implications for overseas investors, investment vehicles, borrowing and local management to ensure the optimum return out your investment.

Why should you invest in Australian Property:

- **High population growth** is one of the most important criteria in real estate investment. With the population growth in Australia, especially in key cities like Melbourne and Sydney not likely to slow down anytime, it makes investing in these cities attractive to ensure a continuity of both capital and rental growth.
- Australian property is often **praised by investors** for its ability to maintain steady rental yield while achieving positive capital growth.
- As one of the **world's most consistent property market**s for the past three decades, Australian properties see an average return on investment of 7% per annum, with lesser years of decline compared to almost any other property market in the world.
- **Low cost of debt**, with many new lenders active in the market and increased liquidity.
- **Week Australian dollar** against the US Dollar, provides for future exchange risk upside.
- Australian properties have **enjoyed consistent capital growth** over the last 100 years, with property prices doubling roughly every 7 to 10 years.
- The Australian property market has

also displayed **resilience in resisting downward trends**, giving investors the confidence needed to hold on to their investments for longer periods. The low volatility of the Australian property market has made it the preferred choice over stock markets and other property markets worldwide.

The Economy

The Australian economy, however, is not immune to the broader global economy, and while we have not experienced a recession in over 27 years, economic growth has slowed in line with other established world economies. Wage growth remains low, inflation remains below the long-term trend and GDP remains benign, prompting the Reserve Bank of Australia (RBA) to act by cutting the cash rate to 1% with further cuts expected to follow. A recent report released by Westpac Bank (major Australian Bank) provided the following forecast:

	Current	Dec- 2019	Mar- 2019	Jun-2020	Dec-2020
RBA Cash rate	1.00%	0.75%	0.50%	0.50%	0.50%
10 Year bonds	0.91%	0.90%	1.00%	1.00%	1.10%
AUD/USD	$0.675	$0.67	$0.67	$0.66	$0.67

The above table, highlights Westpac' views of a reduction in the cash rate from 1.00% to 0.5%, with some economists seeing rates heading to 0% and remaining low for a long period to come, which is in line with other central banks globally. A low interest rate environment will stimulate investment activity and consumer spending, however, it reduces greatly the returns investors have received from cash. Many investors are now searching for yield and with commercial property yields over 5% in Sydney, Melbourne and Canberra and over 6% in Brisbane, Adelaide and Perth, the asset class has become increasingly popular. Yields at this level are some 400-500 basis points over the risk-free cash rate and with economic forecasts looking to a prolonged period of low rates we expect to see yields fall further thus increasing commercial property values.

Commercial Property Overview

The strong influx of foreign capital, and the ongoing appetite of major Australian investment funds looking to chase quality assets and yields, has added a great deal of liquidity to the market. Together when coupled together with highly attractive costs of borrowing continue to put downward pressure on cap rates and with rising rents capital values continue to improve. NSW and Victoria remain as the preferred destination for investment, however there is increasing transaction activity occurring in Brisbane and Adelaide. The table below highlights average A grade commercial property yields across Australia:

State	Yield
Perth	6.5%
Brisbane	5.75%
Sydney	4.75%
Adelaide	7.10%
Melbourne	5.10%
National Average	5.8%

"Since June 2004 the average yield spread to 10-year bonds has been 2.5% verses June 2019 at 4%, highlighting the potential for further capital value appreciation"
Source: Savills Research

Due to the underlying strength of the Sydney and Melbourne economies, Fidinam has active mandates in investing in both these markets on behalf of its clients. We are also seeing interest grow in the Adelaide market due to the higher income yields, a lower entry point to invest and the South Australian government undertaking a number in initiatives to promote South Australia as an investment destination, the largest of these being the removal of stamp duty for commercial property investments, saving some 5.5% of the property value when you purchase in Adelaide. As active investors and managers across all Australian markets the Fidinam team can assist your investment in any major capital city of Australia.

Investment Considerations for Overseas Investors

The Australian Government proactively promotes overseas investment within in Australia; however investors need to carefully consider their approach and be aware of ownership structures, federal and state-based taxes, and property types open for overseas investment. Consideration should include:

1. **Ownership**
   You can own property in your personal capacity; however it may be more beneficial to own the property in an Australian domiciled company and or via a Managed Investment Scheme, these provide more flexibility when managing borrowings, capital gains and distributions.
2. **Government approval**
   Depending on the asset size you may require Foreign Investment Review Board approval; in many instances this is for assets of state significance and or over $150million AUD.
3. **Property Taxes**
   With the exception of Adelaide all states charge stamp duty at an average rate of circa 5.5% of the purchase price when you acquire a property and charge ongoing annual Land Tax, with Victoria and Queensland charging an additional "absentee Owner" Land Tax surcharge. This is where ownership structuring of your investment can

require addition advice to mitigate risk around these surcharges. Other taxes to consider is the effect of Goods and Services Tax (currently 10%) and if the asset is sold the potential for Capital Gains Tax.

4. **Asset types**
   Overseas investors can acquire all types of non-residential property and are restricted to only being able to purchase new residential property.
5. **Borrowing**
   There is a strong banking and non-banking market that will assist with securing the right property finance. Borrowing for an overseas investor, while not difficult can be challenging due to Australia Anti Money Laundering laws and the "Know Your Customer" required by the lender to understand the ultimate beneficial owner of the asset.
6. **Australia's legal system is** based on the UK system just like Hong Kong or Singapore, so it's familiar to many overseas investors, and property acquisition if one of the most transparent in the world with strong consumer protection.

Borrowing

Leveraging a property investment in Australia, is a prudent strategy for investors, as it allows you to hedge part of your investment, as you are acquiring in Australian dollars, and with local interest rates at historical lows can substantially improve you cash on cash investment return, as example of this is as follows:

Property purchase price		*$20million AUD*
Investment income (yield)	5% per annum	$1million AUD
Mortgage (loan)	50% of purchase price	$10million AUD
Equity	50% of purchase price	$10million AUD
Mortgage interest	3% per annum	($0.3milliom) AUD
Net income after interest		$0.7million AUD
Cash on Cash return		**7% per annum**

Adopting a leverage strategy can increase your cash on cash returns from 5% to 7% per annum or over a 28% per annum increase in investment return. However a leverage strategy needs to be carefully considered, as too much leverage can be risky if the market cycle changes and values fall.
As a broad overview of the debt market in Australia, and depending on the type of property acquired a typical mortgage facility would look like:

Mortgage (loan)	40-50%
Interest rate	2.75%-3.25%
Finance fees (establishment)	0.3 to 0.5%
Covenants	
Interest cover ratio	2 times
Loan to value ratio	50%

Local Management

Local management is an important part of your overall investment strategy. Local management will be well versed in what is happening within with the domestic property market, have strong and deep networks to assist in acquiring property, provide active management to ensure the successful financial performance of the asset and/ or portfolio, work with the investor in developing and implementing prudent debt strategies, and advise on ownership structures to ensure maximum financial performance from the investment.

Fidinam is well positioned to assist, it current manages over $400m in assets for offshore investors and has ongoing mandates to acquire more quality investment property in Australia. Should you wish to learn more about investing in Australian property, please do not hesitate to contact our Managing Director at Fidinam Australasia Real Estate via email matthew.burrows@fidinam.com .

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THE FENG SHUI OF ASSET PROTECTION

In Hong Kong, the Chinese practice of *feng shui* has an impact of all walks of life. While the word literally means "wind & water", this geomancy dictates the value of a property's value to whom you should make friends with next. Having an auspicious number 8 on your licence plate is a status symbol. Then factories or offices with leaking pipes are considered to be of bad fortune (as water symbolises wealth).

Believers purchase *feng shui* books at the end of each year to get a sneak peak into the future. Yet few of them could have predicted what would have come of 2019 – a year of everlasting trade tension, Brexit-no-Brexit, as well as a series of geopolitical tug-of-war in Asia.

In a period of uncertainty, it helps to explore the topic of asset protection through the five core elements of this ancient pseudoscience.

Water – Bank account in Switzerland

All wealth start with cash, and there is no better place to deposit them than the safe jurisdiction of Switzerland. The confederation has a world-renowned reputation, as well as a banking system with strong regulatory oversight. In recent years, Switzerland has also become a highly digitised wealth management hub for the sophisticated offshore depositors. Swiss banks stand out for their streamlined approach to onboard non-residents, willing to open personal bank accounts outside their domicile. With a minimum balance of USD 100,000, customers would also benefit from a debit card to access cash worldwide, as well as a powerful online trading platform to purchase everything from U.S. equities to the most obscure local currency bond. This solution is particularly useful to middle class individuals who venture abroad for the first time but need the comfort of full control over their asset.

Wood – Secondary Residency

We plant trees in the name of sustainability. In turbulent times, families also seek secondary residency to ensure children's future is well protected.

At Fidinam we make a distinction between citizenship and residency. In acquiring citizenship, one is expected to fully immerse in a new culture. In parallel, residency can be a bridging solution to serve specific purpose for a defined period of time.

British Citizens who are concerned by their access to continental Europe may consider the resident non-domiciled regime in Italy or Portugal. Likewise, young Asian families seeking new growth opportunities (and better schools) may consider moving to the UAE at a fraction of the cost of a full emigration to an Anglophone country.

Some of these programmes require as few as 2 days a year to reside in the country. Yet they could move and settle there at a short notice. In the case of the UAE, residents also benefit from a tax-free environment on their income and a world class healthcare system.

The key to a successful alternative residency is to understand your objective. Therefore, receiving impartial advice prior would be as important as the application process itself.

Metal – Trust

The strongest defence of all is to distance oneself from his/her own asset. While it seems counterintuitive, entrusting your prized estate to a licenced trustee can protect you on an unexpected rainy day.

Trust is a tool for succession planning. Unlike a standalone will, a trust is less likely to be contested in court for its authenticity. A trustee would validate the deed and distribution mechanism in advance – often with the participation of a protector and a trust lawyer – to ensure cross-generation functionality.

As entrepreneurs expand their business worldwide, their sudden death could potentially disrupt operation. In jurisdictions such as China and Vietnam, a change of shareholder could necessitate reapproval by the competent authority. Or in the case of an IPO, the founder would often cash out at trust level (in tandem with residency planning) to maximum tax efficiency.

A trust is a practical estate planning tool for enterprising businessmen with operations in more than 3 countries/regions.

Fire – Investment diversification in Australia

The fiery growth in the emerging market has slowed in recent years. Investors again look for assets in jurisdictions with sound legal protection.

Australia is a worth-looking case. Aside from being a Common Law jurisdiction, the country is intrinsically tied to Asia. New wealth generated in China, Korea and Southeast Asia allowed Australia to enjoy a decade of uninterrupted growth. Recently, a lower AUD coupled with an appetite to attract foreign investors have put Australia on the global investment heat map again.

Our Sydney office will dive into deeper details on this topic. Go check it out on this newsletter!

Earth – Re-domiciliation in Singapore

Corporations do not benefit from sensationalised decision-making. But in the interest of protecting company assets, the management cannot exclude any scenario from its ongoing SWOT review. When time calls, thou shall move heaven and earth.

Singapore is known for its stability, good governance, and an increasing focus on tech. Little known is that Singapore is one of the few Asian jurisdictions that offers a route for re-domiciliation.

If an entity's asset or yearly revenue exceeds SGD 10M and/or if it hires more than 50 employees, it is allowed to be redomiciled in Singapore.

Moving the corporate headquarters to Singapore has become a popular chatter topic among companies in the board room across Greater China. But it was a British design company, Dyson, that counts among the firsts to reap benefits from this programme. As manufacturers gradually move out of China to Southeast Asia, Singapore's leadership within the ASEAN and a broad network of Double Taxation Avoidance Agreements also render the city state a "future proof" platform for growth.

While Fidinam cannot advise clients on *feng shui*, we are happy to help protect your personal and corporate assets.

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VIETNAM, A DESTINATION FOR INTERNATIONAL IT BUSINESS

Information technology (IT) has been growing at an impressive rate of 30 percent per year, playing an important role in Vietnam's socioeconomic development. According to the Vietnam Software and IT Services Association (VINASA), Vietnam IT industry has been growing steadily over the past recent years.

What follows is a brief description of the main factors having an impact on the IT industry in Vietnam such as governmental support, workforce, infrastructure & environment.

Governmental support

According to the VINASA, Vietnam government has been creating favourable conditions for IT industry's development. Those includes Resolution 36-NQ/TW dated July 1, 2014 of the Politburo on enhancing IT application and development. In this resolution, the Politburo emphasized the importance of IT development both at the governmental level (transforming paper-based processes into application and software-based processes in all level of governmental governance offices) and at the provincial level (installing security cameras, applying smart cameras for local police on their vehicles, etc.). The Politburo set out a plan for IT industry development in the period on 30 years since 2014. This resolution is perceived as a 'golden opportunity' for IT development nation-wide.

In 2015, Vietnam Prime Minister's decision No. 392/QD-TTg was approved and in the decision, it is stated clearly that by 2025, the information technology sector will become a fast, sustainable and profitable economic sector with large export earnings. The IT sector will thrive for a minimum 15% growth rate per year from 2015 to 2020 in software, digital and IT services and aim to attract more foreign direct investment (FDI) projects in the key fields, among which were electronic hardware and digital outsourcing services. In addition, Vietnam will increase the competitiveness and stay among the top 10 countries providing software and digital outsourcing services in the world.

The government also issued the Resolution

41/NQ-CP dated May 26, 2016 on tax incentives to promote IT application and development in Vietnam in order to improve competitiveness and attract investment in the sector. This resolution provides preferential terms on corporate income tax and personal income tax. For example, new IT projects with over 1,000 full-time employees enjoy an annual corporate income tax of 10 percent for 15 years.

Workforce

Vietnam is rapidly developing a labour force to meet the requirements of the IT surge. Mathematics and IT are the top choices of Vietnamese students. With more than 290 universities offering IT studies and 55,000 students enrolled each year, Vietnam is a leading IT service destination in Asia.

According to a report from the Ministry of Education and Training, the country has a total of 235 universities nationwide, including 153 IT training colleges with annual output of 50,000 IT graduates.

"The matter of training high quality IT personnel is becoming a focus of both the education sector and IT businesses to satisfy work demand," the report said.

Infrastructure & environment

Vietnam has been known for its IT & software outsourcing services and capability. For many years, MNCs such as Intel, IBM, Samsung Display, Nokia and Microsoft have chosen Vietnam to outsource their software projects. In 2018, Vietnam exported $3.5 billion worth of software, up 11.6 percent from 2017, according to the Ministry of Information and Communications (MIC).

Vietnam, driven by its growing internet penetration, smartphone adoption, and young demographics, offers huge potential for IT, tech and start-up companies. Especially the ones focusing on fintech, e-commerce, and food technology. These sectors have been the top priorities for investors in the last few years. The other sectors with potential include micro-financing, online travel, and logistics. Noticeably, on 21st of September 2019, Viettel Military Industry and Telecoms Group (Viettel) announced the implementation of 5G service and the placement of the infrastructure of Internet of Things (IoT) in Ho Chi Minh City. The Secretary of the municipal People's Committee Nguyen Thien Nhan underlined the city's determination to build a smart city, saying that the cooperation with Viettel to build modern ICT infrastructure and core platforms for digital society will help the city realize its vision and strategy, maintaining its leading role in the country in digital transition (according to MIC).

In recent years, there have been a bloom for start-up communities and the international unicorns in IT and technologies having their presences in Vietnam such as Grab, Go-Viet (Go-Jek), Alibaba, etc. as well as the local unicorns with investments coming from overseas tech investors namely Tiki, VinaGame (Temasek), VNTrip, Elsa (education technology), etc.

The top 7 trends in the IT sector in 2019 for Vietnam are the following: FinTech, Blockchain, Artificial Intelligence, SaaS – Software as a Service, E-Commerce, Marketplace Platform and Edtech – education technology.

Outsourcing or direct investment

International investors can consider the conventional way to outsource IT service to Vietnam service providers or they can decide to directly invest into the country's vibrant market with high-quality workforce, supportive infrastructure and government via two options: (a) hiring IT workforce in Vietnam remotely for their company's projects overseas or (b) set up an entity in Vietnam, recruit IT professionals in Vietnam to assist the company's business plan both in Vietnam and overseas.

Fidinam has been assisting a number of foreign investors in IT industry to outsource their service and/or to invest in Vietnam. We support the client in decision-making process from industry research to market-entry advisory and set-up of the operations.

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SINGAPORE, APPLICATION OF GST ON DIGITAL SERVICES EFFECTIVE FROM 2020

As it was announced in Budget 2018 by the Singapore Minister of Finance, starting from 1 January 2020 Good and Service Tax (GST) shall be levied in Singapore to imported digital service rendered in Business-to-Consumer (B2C) transactions.

The new regime, also known as Overseas Vendor Registration Regime, aims to level the GST treatment of all digital services consumed in Singapore, regardless if they are rendered from overseas or locally.

As consequence, under certain condition, the overseas digital service providers will be required to comply with Singapore GST registration and reporting rules.

Digital Services

For the purpose of the Overseas Vendor Registration Regime, **Digital Services** are defined as "services supplied over the Internet or other electronic network and the nature of which renders their supply essentially automated with minimal or no human intervention, and impossible without the use of information technology". Accordingly, Digital Services include, among others, the supplying of the following:

- digital content, such as mobile application and e-books,
- software programs, downloading of software, driver and firewalls,
- subscription-based media, including online newspaper, music, films, gaming, live streaming of TV shows and music,
- online courses via e-learning,
- electronic data management, i.e. website hosting, online data warehousing, file-sharing and cloud storage services,
- services providing or supporting a business or personal presence on an electronic network, including subscription for the maintenance of an online professional profile page,
- support services performed via electronic means, to arrange or facilitate a transaction (i.e. booking fees).

Conversely, services such as advertising on intangible media platform circulated outside Singapore and professional services involving human intervention (for instance, legal services from lawyers), are not included in the definition of digital services and do not fall under the new regime.

New regulation on application of GST for overseas supplier

Under the current GST rules, in force until 31 December 2019, a B2C supply of digital services may be subject or not to GST depending from the status of the supplier: indeed, GST applies if the service is rendered by a Singapore supplier, while it is not applied if the supplier is based overseas,

even though consumed in Singapore, being deemed a service falling outside the scope of GST.

Starting from 1 January 2020, the application of GST on digital services will be subject to a two-tier registration threshold based on (i) value of annual global turnover; and (ii) value of digital services made to customers in Singapore, **regardless of the country of establishment of the provider.**

In particular, GST shall be levied by any overseas supplier when it satisfies both the following conditions:

- global taxable turnover exceeding S$ 1 million in a calendar year, either calculated on a retrospective or prospective view; and
- yearly supplies of digital services to customers residing in Singapore exceeding S$100,000 for a calendar year, either calculated on a retrospective or prospective view.

Overseas suppliers meeting both the above criteria shall be required:

1. To apply to Singapore Inland Revenue Authority (IRAS) for the GST registration.
2. To charge GST on services provided on B2C basis, where B2C refers to transaction made to non-GST registered customers, either private individuals or entities, which are not GST registered in Singapore. It must be noted that the responsibility to provide GST registration number lies with the GST-registered customer and therefore overseas suppliers are allowed to treat services as being supplied to a non-GST registered customer, charging and accounting for GST, unless the customer provides its own GST registration number.

3. Submit quarterly GST report to IRAS and pay GST.

For ease of compliance, the Overseas Vendor Registration Regime provides overseas suppliers of digital services to register with ACRA according to a simplified pay-only regime, and that input tax claims incurred on taxable purchases made in Singapore are not allowed. The GST report submitted by overseas suppliers on quarterly basis must therefore state only the value of supplies and the GST collected in the relevant accounting period.

Electronic Marketplaces

To reach a wider network of customers, suppliers may choose to market and sell their products through intermediaries such as **Electronic Marketplaces**.

An electronic marketplace is defined as a medium that allows the suppliers to make supplies available to customers by electronic means. This includes marketplaces operated via any types of electronic interface such as website, internet portal, gateway, distribution platform, so excluding payment processors or internet service providers.
Given the electronic marketplace's involvement in the digital supply chain and its interaction with both the suppliers and consumers, under certain conditions both local and overseas operators of electronic marketplaces may be regarded as suppliers of digital services made through the marketplace, on behalf of overseas suppliers.

Specifically, the operator of electronic marketplaces is regarded as the suppliers if any of the following conditions is met:

- The electronic marketplace authorises the charge to the customer;
- The electronic marketplace authorises the delivery of supply to the customer
- The electronic marketplace sets the terms and conditions under which the supply is made;
- The documentation provided to the customer identifies the supply as made by the marketplace, and not the merchant; or
- The electronic marketplace and the merchant contractually agree that the marketplace is liable for GST.

If any of the above-mentioned requirements is met, the electronic marketplace operator will be deemed a supplier pursuant to the Overseas Vendor Registration Regime.
In this scenario, it may be required to charge GST on B2C supplies of digital services made in Singapore on behalf of the overseas suppliers listed on its platform. This includes all supplies of digital services made through the platform by the overseas suppliers, regardless of whether they are registered or liable to register for GST.

It must be noted that the above-mentioned threshold condition set forth for overseas suppliers of digital services shall also apply to overseas electronic marketplace operators: they must GST register if the yearly global taxable turnover and the yearly value of digital services provided to customers in Singapore are above the two-tier threshold of S$ 1 million and S$ 100,000, respectively.

Overseas Vendor Registration Regime will apply on invoices issues and payment received from the 1 January 2020 onwards. With GST chargeable across the border, businesses in Singapore will no longer suffer a competitive disadvantage due to extra tax liability on digital services provided to non-GST registered consumers.

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NEW FREE TRADE AGREEMENT

2019 is a flourishing year for the negotiations and finalisation of free trade agreements, especially between the European Union and APAC countries.

What follows is a summary of what has been signed and what is still pending.

Free Trade agreement UE - Singapore
The EU-Singapore trade and investment agreements were signed on 19 October 2018. Following the European Parliament's consent to the agreements on 13 February 2019, ratification procedures are underway for their entry into force.

According to the European commission reports:

- Singapore is the EU's 14th largest trading partner in goods and the EU's largest trading partner in the Association of Southeast Asian Nations (ASEAN). The ASEAN region is a dynamic market with some 640 million consumers and ranks as the eighth economy in the world; the ASEAN members are Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam.
- Singapore is a major destination for European investments in Asia, and the third largest Asian investor in the EU (after Japan and Hong Kong).
- In 2017 the existing bilateral foreign direct investment stock between the

EU and Singapore was roughly €334 billion, having expanded rapidly over the past years.

Besides the trade negotiations with individual ASEAN Member States, the EU cooperates closely with the ASEAN region as a whole. Cooperation between the two regions is framed by a biannual ASEAN-EU Trade and Investment Work Program.

The EU-Singapore trade agreement will create new opportunities for EU businesses to export to Singapore and will help create jobs too. In fact, Singapore will now offer better access to its market to EU companies than it does to firms from elsewhere, especially in the transport, telecommunication and financial services sectors. Moreover, Singapore has agreed to make it easier for the EU to export a wide range of goods on its market such us electronics, textile and dairy products.

The agreement will also bring new rules on the custom procedures, simplifying and speeding up paperwork and physical checks, something that will help a lot the smaller companies.

Free trade agreement SAR Hong Kong

The ASEAN – Hong Kong, China Free Trade Agreement (AHKFTA) entered into force on 11th June 2019, for Hong Kong and five ASEAN Member States, namely, Laos, Myanmar, Singapore, Thailand and Vietnam.

Under the AHKFTA, Hong Kong and Singapore will grant tariff free access and will bind their customs duties at zero upon entry into force of the agreement. Brunei, Malaysia, the Philippines and Thailand will eliminate customs duties on 85% of products traded with Hong Kong within ten years and reduce another 10% of tariff lines within 14 years. Indonesia and Viet Nam will eliminate customs duties for 75% of their products within ten years, and reduce another 10% of tariff lines within 14 years. Meanwhile, Cambodia, Lao PDR and Myanmar will eliminate customs duties for 65% of their products within 15 years and reduce another 20% on tariff lines within 20 years.

Free trade agreement Vietnam

The European Union and Vietnam signed a Trade Agreement and an Investment Protection Agreement on 30th June 2019.

The agreements will be presented on the Vietnamese side to the National Assembly for ratification and on the EU side to the European Parliament for its consent, as well as to the respective national parliaments of EU Member States in the case of the Investment Protection Agreement.

The EU is Vietnam's second-largest export market after the United States, with main exports including garment and footwear products. In 2018, Vietnam exported $42.5 billion (€37.32 billion) worth of goods and services to the EU, while the value of imports from the region reached $13.8 billion (€12.12 billion), according to official data.The largest sector of investment by the EU is industrial processing and manufacturing.

Free trade agreement Australia

Australia and the European Union (EU) launched negotiations for a free trade agreement (FTA) on 18 June 2018. As a bloc, the EU is Australia's second largest trading partner, third largest export destination, and second largest services export market. The EU was Australia's largest source of foreign investment in 2018.

The EU and Australia prepare for the next round of FTA negotiations in October.

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THE IMPORTANCE OF MAINTAINING ECONOMIC SUBSTANCE IN INTERNATIONAL STRUCTURING

Hong Kong has an expanding international tax treaty network.

Comprehensive Double Tax Agreements (CDTAs) are bilateral agreements signed between two countries with the aim to protect against the risk of double taxation where the same income is taxable in two jurisdictions, to avoid the absence of taxation, and to facilitate cross-border trades and investments. CDTAs generally reduce the withholding tax rates on investment income (such as interest, dividends, royalties) and provide favorable tax treatment on capital gains, allowing taxpayers to reduce their tax burden.

However, in order to claim the benefits of a tax treaty, the taxpayer must be a resident of at least one of the contracting country.

Tax resident legal entities can be subject to the economic substance requirements, which have been introduced by the OECD, under the Base Erosion & Profit Shifting (BEPS) regulation, with the aim to prevent tax avoidance. The concept of substance concerns not only multinational corporates, but also Small and Medium Enterprises and generally, all businesses with international and cross-border transactions.

Economic substance, nowadays, is a tool used by the tax authorities against tax optimization schemes which are implemented with the exclusive goal to obtain a treaty benefit (the so-called treaty shopping). It is therefore intended for all legal entities considering to have an international expansion by setting up a foreign entity.

What is economic substance?

In a global economy, businesses may decide freely the jurisdiction where to base their operations and establish their entity.

However, the choice should depend on a number of factors, reflecting an economic reality.

Indeed, the company incorporated in the jurisdiction must be necessary from an economic and commercial perspective. Tax considerations can also be taken into account provided that it is not the sole and entire motivation.

Each country has its own definition of corporate tax residence and substance, and tax authorities are paying more and more attention to the respect of these requirements.

What are the economic substance requirements in Hong Kong?

The Hong Kong law does not provide any clear definition of tax/economic substance.

Hong Kong residents who require proof of resident status may apply for a Tax Residency Certificate (TRC).

Under CDTAs entered by Hong Kong with other treaty partners, a Hong Kong resident company is defined as "a Hong Kong incorporated company" or "a company incorporated outside Hong Kong that is managed or controlled in Hong Kong".

Based on this definition, being a Hong Kong incorporated company should be sufficient to obtain a TRC. However, the Inland Revenue Department (IRD) generally requires to obtain information and supporting documents as proof for the applicant's management or control normally exercised in Hong Kong. The substance test is conducted on a case-by-case basis. The tax authorities will assess the activity, and the commercial operations of the company to determine if it has substance.

General list of information/documentation requested by the IRD are as follows:

1. Composition of board – whether the board members have residence in Hong Kong;
2. Board meetings – where the place of board meetings are held, what is discussed and resolved, how the resolved matters are implemented or executed;
3. Business operation, including the business address, management and staff numbers and details, business activities details, place of operation;
4. For business address - the Hong Kong lease agreement (if any) should be provided;
5. For management and staff numbers – employment visas, employment contracts and employer's return submitted as well as their personal particulars (nationality, residential address) and responsibility/place to perform the job;
6. For business activities – nature of income (any passive income or offshore income included);
7. Name of bank in Hong Kong;
8. Audited accounts showing the value of fixed assets/cash maintained in Hong Kong;
9. If the company has establishment outside Hong Kong, details (office address, management and employees details, business activities, income, etc.) is also required.

This list should not be considered comprehensive.

It should be noted that on 1st February 2015, the Inland Revenue Department has adopted stringent rules and procedures for obtaining a certificate of Hong Kong resident status. Hong Kong authorities are now stricter in reviewing these applications.

Finally, in order to minimize the risk of a lack of substance, it is important to pay attention to the location of the human, economic and material resources needed to perform the activity. In fact, the place of effective management is determined after looking into the activity of the company. The level of substance which must be maintained in the jurisdiction of the entity will depend on its actual function.

Consequences of non-compliance and lack of substance

If the substance requirements are not met, or if the management of the company is in another jurisdiction, the risk is to be considered as tax resident not in the country of incorporation, but in the country where the management is effectively done.. Indeed, companies incorporated in Hong Kong but managed outside Hong Kong are likely to be considered as tax residents in the foreign jurisdiction and therefore may be subject to foreign corporate tax (according to the foreign tax law).

If the tax authorities are not satisfied that the company has enough substance, then the application for the tax residency certificate will be rejected.

Entrepreneurs must be aware of these requirements when considering to establish the most appropriate and efficient tax structures for cross-border activities. Others having already set up a foreign company are recommended to review their business structures to ensure that it complies the requirements of substance.

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