Source: *The Sunday Times,* pB12
Date: 29 October 2017

FinancialQuotient

What is a tax treaty?

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WHAT DOES IT MEAN?

A tax treaty, also known as a double taxation agreement, is an agreement between two countries aimed at relieving double taxation of income earned in one country by a resident of another.

As companies expand by venturing overseas, they may derive income from a foreign country, which may be taxed both in that country and their country of origin. If unrelieved, this results in international double taxation, which may impede international growth.

WHY IS IT IMPORTANT?

It is important to understand and optimise the benefits accorded by a tax treaty.

In Singapore, a company must be a tax resident before it can avail itself of the benefits accorded under the tax treaties that are signed by Singapore with more than 80 countries. To be a tax resident of Singapore, the control and management of a company, which involves the determination of a company's strategic decisions typically made during the board of directors' meetings, must be exercised here.

A tax treaty can eliminate or reduce the impact of international double taxation by spelling out the tax rights between Singapore and her treaty partners on the different types of income arising from cross-border transactions.

For example, a tax treaty may specify that a certain source of income cannot be taxed by the country where the income arises, but only by the country of residence; or vice versa.

A tax treaty also provides for reduction or exemption of tax on certain income such as interest or royalties.

IF YOU WANT TO USE THE TERM, JUST SAY:

"A company must be a tax resident of Singapore before it can avail itself of the potential benefits accorded by Singapore's tax treaties."

• The writer is Associate Professor (Practice) at the Department of Accounting at NUS Business School. The opinions expressed are those of the writer and do not represent the views and opinions of NUS.

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