

Indirect Tax News

A KPMG Singapore Tax Services Letter | January 2004

GST RATE INCREASE

WHICH RATE TO CHARGE?

The introduction of the Goods and Services Tax in Singapore signalled a fundamental shift in long term fiscal policy from an emphasis on direct taxes on income to indirect taxes on consumption. Cuts were made in corporate and personal tax rates to maintain Singapore's international competitiveness, attract inward investments and create jobs. To make up for the revenue deficit, the GST rate was raised from 3% to 4% on 1 January 2003 and to 5% from 1 January 2004.

One of the basic concepts relating to the GST rate change is the 'time of supply', which determines when a supply is made for GST purposes. Conventional time of supply rules state that a supply is made at the earliest of the following dates: delivery of goods/performance of services, receipt of payment or issue of tax invoice. If the tax invoice is issued within 14 days of the delivery of goods/performance of services, and if no payment has been received, the time of supply would be the date of issue of the tax invoice. The Inland Revenue Authority of Singapore (IRAS) has issued transitional rules for the determination of the time of supply for transactions where the three determining events span across the GST rate changeover date¹. The significance of the transitional rules lies in the fact that GST can be charged at the old rate of 4% for supplies where the goods were delivered, services were performed or payment received prior to 1 January 2004, notwithstanding that the tax invoices were only issued on or after 1 January 2004.

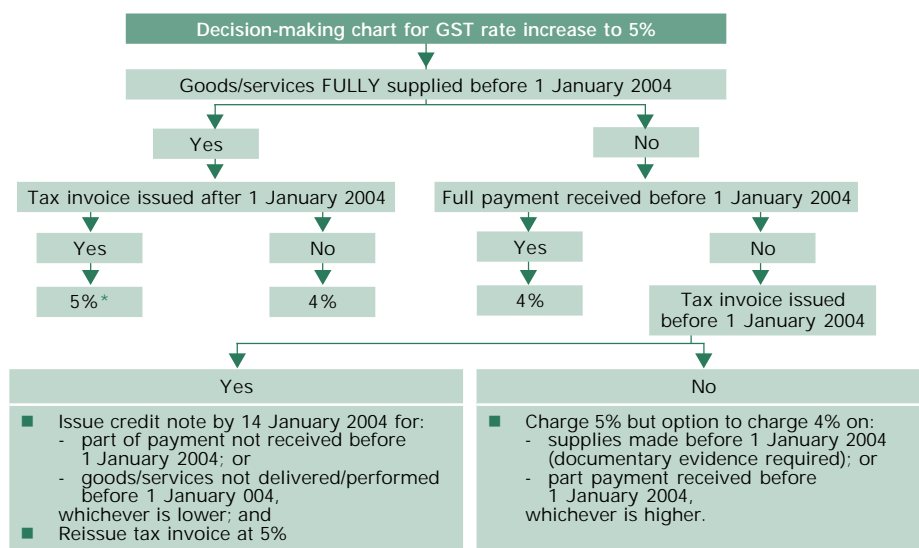
¹ 31 December 2003

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The following chart illustrates the process of determining whether a supply is charged at 4% or 5% based on transitional rules issued by the IRAS.



* Where the tax invoice is issued within 14 days of the date the goods and services are fully supplied, the time of supply would be at the time the tax invoice is issued. The GST rate is therefore 5% but there is an option to charge 4%.

Administrative Concessions

The IRAS has also granted the following administrative concessions relating to the transitional period of the GST rate change:

- Payments received via cheques will be considered received before 1 January 2004 if the cheques are presented to the banks by 5 January 2004 and cleared successfully.
- Payments received via GIRO will be considered received before 1 January 2004 if the GIRO deductions are successfully effected by 31 January 2004 and relate to invoices which, when issued in accordance with the business' normal billing cycle, are dated before 1 January 2004.
- Sales made between midnight of 31 December 2003 to 7am of 1 January 2004 will be recognised as sales made before 1 January 2004 and GST would be chargeable at 4%, provided it is the businesses' normal accounting practice to treat the sales made after midnight as the preceding day's sales, and the cash registers and accounting system have already been so programmed (eg convenience stores).
- Credit notes for goods returned may be issued without GST if the supplier is unable to relate the returned goods to the tax invoice for the original sale, and both the supplier and the customer agree with this arrangement in writing.
- Where a credit note and 5% tax invoice must be issued under the transitional rules, the credit note and 5% tax invoice can be combined in one document.

Checklist for GST rate increase

With the GST rate changeover date behind us, you may wish to check that the following have been performed:

- Ensure that your GST accounting system is capable of:
 - issuing tax invoices and credit notes at 3%, 4% and 5%;
 - issuing credit notes by 14 January 2004 for supplies invoiced in 2003 at 4%, but chargeable at 5%; and
 - relating credit notes to the original tax invoices raised.
- Review all your contracts to ensure that the terms allow you to charge GST at 5%.
- Adjust your price lists to reflect a GST-inclusive price at the GST rate of 5%.
- Perform a valuation for continuous supplies of services as at 31 December 2003.

Please note that the above serves only as a general summary of the transitional rules of the GST rate change. The increased GST rate coupled with the complexity of GST concepts means that businesses should develop and maintain a sound understanding of the relevant rules, and implement a robust GST accounting system to ensure that the appropriate amounts of input and output tax are claimed and accounted for respectively.

ZERO-RATING OF INTERNATIONAL TELECOMMUNICATION SERVICES

The newly enacted Fifth Schedule to the GST (International Services) Order prescribes the types of telecommunication services that may be zero-rated.

Section 21(3)(q) of the GST Act was enacted with the passing of the GST (Amendment) Act 1996 to provide for the zero-rating of:

"**prescribed services** comprising the provision of any means of telecommunication transmitted:

- (i) from a place outside Singapore to another place outside Singapore;
- (ii) from a place in Singapore to a place outside Singapore;
- (iii) from a place outside Singapore to a place in Singapore."

Prior to the enactment of this subsidiary legislation, the provision of international telecommunication services could not be zero-rated because no such services had been prescribed. The Fifth Schedule to the GST (International Services) Order (Fifth Schedule), which attends to this, was enacted only recently on 18 November 2003.

To illustrate the effect of the enactment of the Fifth Schedule, consider the provision of International Direct Dialling (IDD) call services. Such overseas call services clearly fall within the scope of section 21(3)(q) of the GST Act and should qualify for zero-rating as an international telecommunication service. Before the enactment of the Fifth Schedule, IDD call services could not be zero-rated under the GST legislation. However, in order to place the local telecommunication companies on a level playing ground with their overseas competitors, the Minister for Finance had approved the remission² of the tax payable on IDD call services rendered by the local telecommunication companies in the interim period. This remission was however granted only until such time when the services pursuant to section 21(3)(q) were prescribed (ie on 18 November 2003).

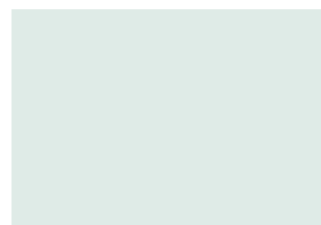
Would the Fifth Schedule benefit overseas telecommunication companies in Singapore?

Paragraph 4 of the Fifth Schedule allows a person who has received the international telecommunication service from the main supplier (ie the telecommunication companies), to zero-rate the onward supply to a third person of the "right to access or use" these services. In practical terms, this would mean that a landlord who was billed by the telecommunication company for telephone charges incurred by his tenant, may zero-rate the reimbursement of IDD call expenses from his tenant without having to seek the Comptroller's prior approval for the remission of tax, as was required before the enactment of the Fifth Schedule.

In addition, it is worth noting that paragraph 6 of the Fifth Schedule explicitly disallows the zero-rating of 'any part of a supply comprising the sale or supply (including the letting on hire) of any equipment or goods and any repair, maintenance or management thereof which is **not** in connection with the international transmission of the telecommunication'.

With the enactment of the Fifth Schedule, the remission previously granted to businesses rendering international telecommunication services ceased to be effective. Consequently, businesses rendering telecommunication services, as well as businesses that were previously granted remission should now conduct a review of their services to determine if their supplies would qualify for zero-rating under the Fifth Schedule. If the services rendered do not fall within the provisions of the Fifth Schedule, businesses should seek clarification from the IRAS on the appropriate GST treatment.

² Section 89(2) of the GST Act empowers the Minister for Finance to remit the whole or part of the tax or penalty payable under the GST Act.



FINANCING INSTRUMENTS

WHEN IS GST CHARGEABLE?

The IRAS recently issued a circular to clarify the GST treatment for financing instruments.

Pursuant to paragraph 1(2)(b) of the Second Schedule to the GST Act, in the event that the possession of goods is transferred under an agreement which expressly contemplates that the property will also pass to the buyer at a later date (determined by, or ascertainable from, the agreements but in any case not later than when the goods are fully paid for), the transfer would be considered a supply of goods for GST purposes.

In hire purchase agreements, the hirer has an option to obtain title to the leased goods upon the payment of all the instalment payments and the fulfilment of all his obligations under the hire purchase agreement. The transfer of possession of the goods under a hire purchase agreement would thus be regarded as a supply of goods in accordance with paragraph 1(2)(b) of the Second Schedule, while the provision of the financing would be regarded as an exempt supply of financial services, if the interest charge is separately disclosed to the hirer.

Financial instruments, notwithstanding the commercial name given it, may contain varying contract terms and conditions. For example, the GST treatment for a finance lease that contains a bargain option to purchase is similar to that for a hire purchase transaction, since it provides an option for the hirer to purchase the leased goods.

Consequently, it is difficult to prescribe a general treatment for each class of financing instruments. The IRAS has therefore decided that where a financing instrument satisfies **both** the following conditions, the GST treatment accorded to the financing transaction would be similar to that for hire purchase transactions, ie there are two separate supplies made by the financier to the hirer - a supply of the goods and a supply of the financing service:

- (i) The lease provides an option or right for the hirer to purchase the leased goods prior to the end of the lease period; and
- (ii) The leased goods are not recognised as the financier's assets in his accounting records.

Otherwise, the transaction would be classified as a supply of services.

A supply of goods or a supply of services - Why does it matter?

Where financing or leasing transactions are concerned, the question of whether the transaction is to be treated as a supply of goods or a supply of services is crucial in determining the "time of supply" for GST reporting purposes. The distinction is as follows:

■ **Supply of goods**

According to the time of supply rules, a supply is made at the earliest of the following dates: delivery of goods/performance of services, receipt of payment or issue of tax invoice.

Consequently, where a financing or leasing transaction qualifies as a supply of goods, output tax must be accounted on the price of the goods at the time the goods are delivered/made available to the customer.

■ **Supply of services**

Where services are rendered on a continuous basis, the supply takes place at the earlier date of when the tax invoices are issued and when the payments are received. In a financing or leasing transaction, this would mean that output tax should be accounted for each time the lease payments are invoiced or paid, whichever is the earlier.

With the issuance of the above guidelines, businesses that provide financing or leasing services should review their existing financing agreements to ascertain whether the proper GST treatment has been accorded to such financing instruments.

APPROVED THIRD PARTY LOGISTICS (3PL) COMPANY SCHEME

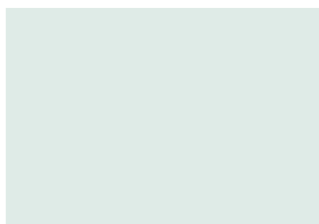
The newly administered Approved 3PL Company Scheme took effect on 1 January 2004.

The Approved 3PL Company Scheme (the Scheme) was designed with the aim of easing the administrative rules encountered by 3PL companies which essentially act as intermediaries between local manufacturers that practice just-in-time operations and the manufacturers' overseas suppliers. KPMG Tax Services is currently seeking the IRAS' clarification on certain issues regarding this Scheme. Details will be published in the next issue of *IndirectTaxNews*.

The crux of the Scheme is to allow the Approved 3PL Companies to import goods belonging to themselves or their overseas principals without incurring the GST that is normally payable upon importation of the goods. It also allows them to deliver the goods locally to other approved 3PL companies or companies approved under the Major Exporter Scheme (MES), free of GST³. The recipients of goods under the scheme are required to report the value of the goods received in Boxes 5 (Total Value of Taxable Purchases) and 9 (Total Value of Goods Imported Under MES/Approved 3PL Company Scheme) of their GST F5 returns.

The Bonded Warehouse Scheme (BWS) is another scheme that provides for the suspension of GST payable on imported goods that are stored in the bonded warehouse. Whether the BWS or the Approved 3PL Company Scheme is more beneficial to the logistics company is a question of fact.

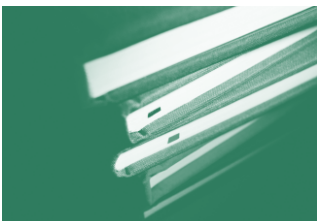
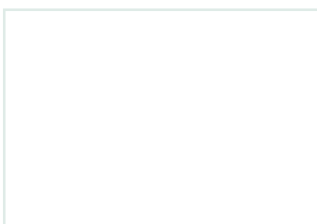
³ The local delivery of goods would otherwise constitute a local supply of goods, for which GST is chargeable at the standard-rate.



GST LEGISLATIVE AMENDMENTS

The following amendments were made to the GST legislation from August 2003 to December 2003.

No.	GST Act/GST (General) Regulations	Amendments
With effect from 1 July 2003		
1.	Section 21(3)(r)	<p>The amendment served to clarify that the zero-rating of trustee services also applies to services provided by a person other than the actual trustee to the trust. The original clause:</p> <p><i>"services supplied by a trustee, where the services and the trustee supplying such services satisfy such conditions as may be prescribed"</i></p> <p>was amended to:</p> <p><i>"services supplied in relation to a trust, where the services and the person supplying the services satisfy such conditions as may be prescribed."</i></p>
2.	Section 28(1)	<p>To provide that the GST Act would also apply to taxable supplies made by the Government in the course or furtherance of business, unless otherwise precluded by the Minister by order in the Government Gazette.</p> <p>Prior to the amendment, the GST Act would not apply to supplies made by the Government or a body incorporated by statute, where similar supplies are not made by other taxable persons.</p>
3.	GST (Non-taxable Government Supplies) Order 2003	<p>This order was made pursuant to the amended section 28(1). It prescribes the supplies made by the Government that are excluded from the scope of GST. These supplies include some of the supplies made by the following Ministries:</p> <ul style="list-style-type: none"> ■ Ministry of Community Development and Sports ■ Ministry of Home Affairs ■ Ministry of Law ■ Ministry of Manpower ■ Ministry of National Development ■ Ministry of Transport ■ The Judiciary



No.	GST Act/GST (General) Regulations	Amendments
With effect from 18 November 2003		
4.	Section 43	<p>To remove the requirement for taxable persons to seek approval from the Comptroller of GST (Comptroller) for the issuance of computer-generated invoices, in order that such invoices may be treated as tax invoices for GST purposes.</p> <p>Prior to the amendment, a taxable person had to submit to the Comptroller, a written undertaking to adhere to specified conditions, for the Comptroller's consideration before approval would be granted for the taxable person to issue electronic invoices to his customers.</p>
5.	5th Schedule, GST (International Services) Order	A new schedule to prescribe the telecommunication services that can be zero-rated under section 21(3)(q) of the GST Act.
With effect from 1 January 2004		
6.	Section 27	<p>Prior to the amendment of this section, the Minister for Finance was empowered to enact regulations, pursuant to this section, to permit certain imported goods to be delivered or removed without payment of tax on the importation. The re-enactment of this section expands the powers of the GST Act to permit certain imported goods to be supplied by the importer to certain persons without the payment of tax on the supply.</p> <p>This amendment was made pursuant to the implementation of the Approved 3PL Company Scheme, which came into effect on 1 January 2004.</p>
7.	Section 12(8)	To expand the scope of the Minister's powers to prescribe regulations governing the time of supply to cover supplies made under the re-enacted section 27.
8.	Section 20(2)	To insert a new subsection to provide for the input tax claims in respect of supplies made without payment of tax pursuant to the re-enacted section 27.
9.	Regulation 45A	This section was enacted pursuant to the re-enacted section 27. It provides for the rules governing the Approved 3PL Company Scheme.

ADMINISTRATIVE UPDATES

With effect from 18 November 2003, businesses no longer need the Comptroller's approval to issue tax invoices electronically, store records in electronic media or store records in imaging systems. Instead, they only need to ensure compliance with the conditions stipulated in the respective revised IRAS Handbooks. For businesses that had not sought the Comptroller's approval prior to 18 November 2003, the Comptroller has also agreed to do away with the need to apply for approval for these past transactions, on the condition that the requirements stipulated in the revised Handbooks have been complied with.

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