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GROUP TREASURY COMPANIES

Background:

The globalization and growth of multinational enterprises is dependent upon many features but perhaps the more important of those include access to great ideas, great clients, fabulous employees and finance. While finance can come from shareholders and third-party institutions it can also emanate from clients but once inside the group the finance needs to be channeled to the business requiring funds for fund growth, operations or to fund payments to shareholders. This thought piece covers MNEs global treasury centers as these are an attribute of the finance arsenal.

I was recently called upon to consider which of the UAE, Singapore and Hong Kong offers the easiest to achieve, most tax effective and easiest to comprehend and abide by treasury tax concession. After completing the advice, I thought a wider audience may find the results interesting.
Clearly this article does not and cannot consider all the features and concepts which found their way into the advice and that's not the purpose of this article, but I believe that CFOs, MNE treasury teams, tax authority policy teams and even tax advisors may find the comparison fascinating.
I certainly do!

Not unlike other people, I have my own preconceptions of what should or does happen in the tax world and in this case, I thought I knew which country would be the best place in which a treasury center should be established. Naturally, being based in the UAE, I anticipated or hoped the UAE would be the best. I wonder whether the reader has the same intuitive expectation.
So now I plan to share my thoughts on which of the UAE, Hong Kong or Singapore is the easiest to establish a global treasury center, which of the three countries has the best tax rates and which of the three countries has the most transparent rules and simplest to abide by rules.

Which is the easiest jurisdiction for establishing a tax effective treasury center; UAE, Hong Kong or Singapore?

Forming a tax effective group treasury company in the **United Arab Emirates** can be accomplished with either a UAE Free Zone company or with a UAE Free Zone branch of a non-UAE company. To qualify, that company or branch must satisfy a business substance rule, an audit rule, a qualifying activity rule, a transfer pricing rule and a deminis income rule. There are other tests, but these are the main tests.

The substance rule is satisfied if the company has an "appropriate" number of personnel to conduct the business and a "fit for purpose" infrastructure and carries on its core income generating activities in the UAE either through its own employees or through contractors. Satisfying these conditions becomes easier the more employees or contractors are on the

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books and the more money spent the better but unfortunately, there is neither a brightline test for employees nor for money nor is there publicly available guidance. The company's financial accounts need to be audited… which brings a cost, but the audit fee might only be a few thousand dollars. To be qualifying the Treasury and financing services must be provided to Related Parties (and they can be inside or outside the UAE) which in the main means companies having a 50% or greater commonality of shareholder or other control.

The **Hong Kong** Treasury Centre rules require the profits to be be derived from so called "Corporate Treasury Activities" performed by the Hong Kong centre for overseas group entities. This is narrower than the UAE where customers can be UAE or non-UAE resident. The potentially qualifying company must only conduct the Corporate Treasury Activities in Hong Kong. In each case the company must be centrally managed and controlled in Hong Kong and the treasury activities must have been executed from Hong Kong or arranged by it in Hong Kong. So, while the UAE allows a non-resident to establish a qualifying treasury centre as a branch Hong Kong does not.

The **Singapore** Finance & Treasury Centre (FTC) Incentive is a little different again as it makes no bones about being designed to encourage companies to use Singapore as their base for conducting group and global treasury management activities. The concession applies to income of a Qualifying FTC service if income arises from an approved network company and from Qualifying FTC activities conducted by the FTC on its own account with funds obtained from qualifying sources. Income earned from a network company cannot be included in the concession until the network company has been approved for this purpose. With companies qualifying as approved network companies having, in the main, at least 25% ownership commonality Singapore offers the tax concession to a wider group of related companies than qualifies for the UAE or Hong Kong concession.

Any entity wishing to be a qualified Singapore treasury company can apply if it has an established international business and operations and is registered in Singapore and satisfies pre-determined staffing and expenditure conditions.

The quantitative and qualitative conditions include spin-offs for the Singapore economy and the depth and breadth of the services and activities including controlling cash and liquidity positions, corporate finance advisory services, interest rate management, foreign exchange, liquidity and credit risks, and overall business planning, investment research and analysis and working with potential partners, such as in the professional services and financial sectors.

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Treasury Centre Tax Benefits:

If the UAE Free Zone company or branch conducts the qualifying activity and providing each of the other tests has been satisfied, then the treasury center's taxable income is taxed at 0%. If the company fails any one of the tests, then the applicable tax rate is 9% with a $100,000 tax free threshold. If the test is failed due to a breach of the de minis test, then the company is locked out for the current and ensuing four tax periods. An incentive to get it right.

The Hong Kong qualifying Hong Treasury centre is taxed at the 8.25% tax rate if the profits were derived from so called "Corporate Treasury Activities" performed by the Hong Kong centre for overseas group entities. The Singapore treasury centre is taxed at an 8% rate, or a 10% rate on the approved FTC's qualifying income derived from Qualifying FTC services to approved network companies and from Qualifying FTC activities.

So, a straight tax rate shoot-out comparison with the UAE leaves both Hong Kong and Singapore trailing.

The low corporate tax rates are supplemented by an exemption from Singapore withholding tax on interest paid by the approved FTC on Loans from banks and non-bank financial institutions outside Singapore; Loans and deposits from an approved network company outside Singapore if the loan relates to the conduct of Singapore qualifying FTC services and activities.

A withholding tax exemption for treasury centers is not unique to Singapore because Hong Kong generally does deduct tax from interest paid to non-residents and currently the UAE applies a 0% rate to be deducted from interest payable to a non-resident lender.

Easy to comprehend:

The UAE's engine room definition of qualifying treasury company activity is straight forward but relatively brief. The Ministerial Decree confirms to us that Treasury and financing services includes the provision of cash and liquidity management, financing, debt management, and financial risk management and related advisory services, including centralised payment and collection activities for or on behalf of related parties.

These services can be provided to another Free Zone company or to a UAE mainland company or to any company in any country and will still qualify if the substance, audit, transfer pricing test and the de minis tests are also satisfied. The definition suggests a wide scope, but the descriptions are not as well defined as they could be.

The Hong Kong listing of qualifying activities is very helpful. The broader the description the easier to comply. Hong Kong extensively defines the Corporate Treasury Activities and breaks them into firstly Corporate Treasury Services and secondly, Corporate Treasury Transactions.

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The former has nine sub categories and includes managing cash and liquidity position, processing payments to vendors or suppliers of the corporate group and managing the corporate group's relationships with financial institutions while the latter has four sub categories two of which are transactions related to the provision of guarantees, performance bonds, standby letters of credit or similar risk mitigation instruments in respect of borrowings by associated corporations and factoring and forfaiting transactions undertaken on its own account and related to the business of an associated entity.

Failure to meet the "only" test or failing to meet Corporate Treasury Activities test does not result in the treasury company failing to qualify for the Hong Kong concessionary rate because there are fall back safe harbours.

The first Hong Kong safe harbour allows the concessionary tax rate when the Corporate Treasury Profits and Corporate Treasury Assets constitute not less than 75% of the total profits and assets of the corporation in the year of assessment.

The second safe harbour allows the concession when the 75% threshold current year threshold is not met but when it is met for the average of the current year and the preceding one or two years of assessment. Both these are more generous than the UAE de minimis threshold which only allows a potentially qualifying treasury company to earn up to 5% (or AED5m whichever be the lower) of its total income as non-qualifying income and still qualify for the 0% corporate rate.

If the Hong Kong company is unable to satisfy either of these safe harbours it still can petition the Inland Revenue Commissioner for approval and the Commissioner may approve the application if satisfied that the corporation would have met the tests but for an intervening event.

Neither the UAE nor Singapore have any such safe harbours, nor do they have a right to ask the Authority to ignore an unplanned or unexpected event which breaches the tests.

Meeting the Singapore rule is easier than the UAE rule when it comes to the substance test because Singapore establishes brightline spending and staffing requirements. Let us call them the Singapore substance test. Transparency such as this facilitates the MNEs planning and minimises the probability of a technical breach through overlooking or not understanding a rule.

The substance test requires the Singapore company during the 5 years of the tax break to conduct in Singapore the finance and treasury centre (nothing novel about this!) but specifies that this business must employ at least four FTC professionals and must incur annual Total Business Expenditure of at least S$1.5 million.

When applying for a subsequent FTC license the finance and treasury centre activities must continue to be conducted in Singapore but now one additional FTC Professional must be employed by Year 5 with additional total business expenditure of at least S$400,000 incurred each year by Year 5. Slightly less generous staffing and expenditure rules apply for the 10% FTC concessionary tax rate.

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These brightline tests are very helpful for a MNE to comply with the rule: if it employs 4 people in Singapore conducting the activities and spends **S**$1.5 million a year it qualifies and if it doesn't it doesn't!

Like Hong Kong and unlike the UAE, Singapore extensively defines the Qualifying FTC Services. They fall into one of nine categories, three of which are arranging of approved credit facilities, providing corporate finance advisory service, and performing economic or investment research and analysis.

Qualifying FTC Activities fall into one of eight categories three of which are transacting or investing in stocks and shares of any company; transacting or investing in approved certificates of deposits, notes, bonds, treasury bills, commercial papers, AT1 instruments and collective investment schemes (excluding any collective investment scheme constituted as a unit trust and transacting or investing into private equity or venture capital funds that are not structured as companies. So, Singapore describes seventeen activities which qualify while the UAE describes nine.

Conclusion:

While the UAE clearly offers the lowest tax rate (0% vs 8.25% and 8%) the broader qualifying activities publicly available on offer in Hong Kong and in Singapore are to be commended. We do not know whether the broader activity categories are not encompassed in the UAE fewer categories but at the same time we do not know that they are. Clarity from the UAE Ministry or the FTA would be very helpful. Acting as if those broader categories are embedded in the UAE without being specially mentioned could result in a client being at risk of failing to apply the 0% rate.
With Singapore being more descriptive of the "substance" which qualifies as "substance" than the UAE this again should see fewer unintentional breaches. Clarity from the UAE Ministry or the FTA would be very helpful.

But the bottom line though is that even were the UAE treasury centre to breach the rules its taxable profit would be taxed at 9% which is negligibly worse than the rates on offer in Hong Kong and Singapore.
A group may be persuaded to opt for Singapore instead of the UAE or Hong Kong if its shareholder relationships with the borrowing companies were less than 50%.

Both the UAE and Hong Kong require a 50% relationship to exist for the concession to apply, Singapore allows income from companies having at least 25% shareholding commonality.

I trust these few words have stimulated thinking amongst CFOs, MNE treasury teams, tax authority policy teams and even tax advisors. The treasury concession is a great tool for MNEs planning but beware the significant traps for the untrained eye.

If you have questions or comments (good or bad!) please email us: admin@pbfirstglobaltax.com and we will do our best to respond

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Formed in the UAE in 2016 and advises on domestic and international tax.

Qualifications

Dr Wilson has a PhD in International Taxation from University of London in 2018. Also qualified in law, accounting and tax.

Experience

Dr Wilson has more than 40 years experience in domestic and corporate taxation including inhouse, investment banking and professional including many years as a senior EY international tax partner of the Australian, US and UK firms and a senior PwC international tax partner based in London

Clients

The PB First FZ-LLC clients include funds, companies, foundations, partnerships, trusts, UHNWI and governments on taxation, dispute resolution and compliance covering more than 50 countries.

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