WHITE PAPER

Ministry of Finance, Trade and Economic Planning

POLICY CHANGES AROUND THE TAXATION OF BUSINESSES.

White Papers communicate a decided Government policy or approach on a particular issue. They are chiefly intended as statements of Government policy.

The Ministry of Finance, Trade and the Economic Planning is proposing the following policy changes for the implementation of a simpler Business Tax Act.

The majority of the amendments proposed are to come in force on the 1st January 2018 at the exception of the amendments relating to the tourism sector for reasons given in the document.

This document will be used for consultation with stakeholders before finalisation. There will be a series of consultation meeting which will be communicated to the public in the coming days.

1. Introduction

Business Tax represents 17% of the total revenue collection and 5.5% of GDP.
The purpose of the reform is to have the simplest regime possible for both the taxpayers to comply with and for SRC to administer.

Although priority is given to simplicity, certain loopholes need to be closed, particularly with regards to sole traders currently benefitting a more attractive business tax regime than the regime existing for employed persons. Certain loopholes with regards to partnerships and trusts are also being considered.

Certain sectors have been treated differently and special recommendations are also being made to harmonize the tax treatment of all businesses regardless of the sector they operate under.

Finally, certain amendments are being proposed to strengthen certain provisions which today are not fulfilling the intention of the policy maker or are not in accordance with the best practice.

2. Proposals

A/ A new tax system based on turnover for small to medium businesses

This proposal will apply across the board for all businesses, regardless of their legal nature (sole trader, entities, partnerships and trusts) or the sector under which they operate (Tourism, agriculture, fishery, and specified businesses) for as long as they meet the threshold.

There will be no option to opt out. Taxpayers will move to another regime only if they do not meet the threshold requirement anymore.

The reason for this proposal is it is much simpler and harder to avoid.

In the current system a taxpayer is allowed to claim expenses, this means that at the end of the tax year, it will have to ensure that the expenses being claimed are allowable, apply the rate of depreciation according to the type of depreciable asset, reintroduce the expenses incurred but not allowed, and from there calculate the profit. Then, he or she will have to apply the amount of tax corresponding to the different rates available depending on the legal nature of the business- sole trader, companies and depending on the type of activity it has.

In addition, based on the payment by instalment principal, a business will have to estimate its business tax payable and at the end of the year, when lodging the return, it will have to claim for a refund or pay the difference in case the estimated amount was lower than the actual liability.

This proposal at the opposite is not requiring anything else to the taxpayer than to continue to capture the assessable income it derives during the year and make the necessary monthly or yearly payment. It is therefore a simpler regime for the taxpayer.

It is also a harder regime to avoid paying taxes and in this way contribute to a better revenue collection by SRC.
Indeed, one principal ways to decrease one's tax liability is to decrease its taxable income by increasing allowable deductions. By only considering the turnover, the taxpayer pays tax on its gross receipts and not on its profits, therefore reducing opportunities to claim more expenses than what should be allowed.

In order to determine the turnover of a business and hence the regime under which it will fall, the reference point is the turnover of the business for the year before the tax year concerned. However, if any exceptional events occurred during a given tax year, this will not be taken into account for the purpose of determining in which regime the taxpayer falls (sale of depreciable asset and or of amortizable intangible). Only the revenue derived from the operation (trading income), interests or royalties income of the business needs to be taken into account

The term turnover should not create any issues of interpretation as it will have the same content as the assessable income currently used under the business tax act and will include the following for as long as they are derived by the business during the tax year from sources in Seychelles-

(a)the gross receipts from the carrying on of the business, including the consideration received from the disposal of trading stock; and the gross fees for the provision of services;

(b) the gross receipts from the employment of the capital of the business, interest, royalties, rent, technical services fee and natural resource amounts;

(c)the amount of any bounty or subsidy derived in relation to the carrying on of the business;

(d)the amount of an expense, loss, or bad debt allowed as a deduction in the year before the entry into force of the turnover tax, that has been reimbursed or recovered by the business, including by way of insurance, compensation, damages, or an indemnity;

(e) an amount derived by way of an indemnity, compensation, or damages for the non-performance of the lessee of an obligation to carry out repairs to property of a business;

(g) an amount derived from the disposal of a depreciable asset of a business exceeding the written down value of the depreciated asset at the time of disposal;

(h) an amount derived from the disposal of an amortized intangible of a business exceeding the written down value of the amortized asset at the time of disposal.

To be noted that an amount which is currently an exempt income under the business tax act will remain exempted for the purpose of this reform, this means that a dividend paid from a resident corporation to a resident business is exempt and will not be included in the turnover of the person receiving the said dividends.

With this new proposal, the Government is proposing to take a step further with simplification as the only obligation of the taxpayer will be to ensure what is the total turnover it falls under and remit the tax to SRC. In order to be the most accurate possible and not create a cash flow issue at the end of the year, it is being proposed that the tax will be paid monthly on the current monthly turnover of the business.

A simplified business tax return will be designed similar to the one that exists for presumptive tax.

However, acknowledging the specificities of micro businesses, two different sub-systems are being proposed.

i. **Flat fee of 3000/- rupees for businesses deriving a turnover of no more than 500,000/- Rupees.**

Today, this category represents 65% of the total taxpayer population.

ii. **A flat percentage of 3% for businesses deriving a turnover between 500,000/- Rupees and 25 million rupees.**

This is an extension of the already existing presumptive tax regime.

From the available data for presumptive tax, more than 85% of the businesses deriving less than 1 million turnover have not opted to leave the presumptive tax regime appraised for its simplicity.

Nevertheless, the proposal is to keep the larger businesses in the current business tax which are already contributing to 86% of the Business Tax Collection. The decision to keep the businesses with a turnover of more than 25 million rupees in the current business tax regime is based on the fact that these businesses are generally sufficiently equipped to lodge a complete business tax return, they often have foreign related parties or belong to groups which already adhered to high accounting standards and there is no justification to simplify further the system for these taxpayers.

B/ Existing business tax regime for large businesses with certain adjustments

There will be no changes to the current rates and principles applicable to entities with a turnover above 25 million. For sole-traders, partnerships and trusts some amendments are being proposed.

i. Treatment of Sole traders

As explained in the introduction, the current rate of business tax applicable to sole trader is more favourable than the progressive income tax for employed person.
The frontier between a sole trader and an employee being very thin and sometimes delicate to determine, it is proposed to align the progressive income tax brackets and rates with the business tax rates applicable to sole traders.

A sole trader will therefore now benefit the following-

From 0 to 102,666 a tax rate of 0%
From 102,666.01 to 120,000 a tax rate of 15%
From 120,000.01 to 1 million a tax rate of 20%
Above 1 million a tax rate of 30% or 33% depending on the sector of activity.

This rates and tax brackets will apply to both Seychellois and non-Seychellois due to WTO legal requirements applicable only for businesses.

ii. Partnership

Partnership is defined as "two or more persons carrying on business jointly for common profit […]". A resident partnership is defined as a "partnership in which one of the partners is a resident person". Person is defined as "an individual, a partnership, an entity, or a trust".

In order to ensure the most consistency possible between the different applicable rates per type of taxpayers, it is being proposed to tax the partnership with corporate partners at the same rate as an entity whereas those with only individual partners will continue to be taxed at the rate applicable to sole trader.

iii. Trust

Presently, a trustee is subject to business tax if no beneficiary has a vested right to the income of the trust. Where an amount is vested in the beneficiary, it is the beneficiary which is taxed. In order to ensure the most consistency possible between the different applicable rates per type of taxpayer, it is proposed that all trust income (whether there is a beneficiary with vested rights or not) be taxed at the trustees level at rate prescribed.

iv. Treatment of tourism operators, agricultural processors and exporters, boat owners and Fisheries processors and exporters.

The tourism sector, agriculture and fishery sectors are special sectors which have been benefiting some tax concessions- holders of Investment and Promotion, Tourism Incentive or Agriculture and Fishery Incentive certificates. This was necessary to attract investments and support these sectors. However, in the spirit of the reform proposed, and keeping in mind simplicity, multiplication of layers of tax treatment is no longer the way forward.
It is therefore proposed that the holders of such certificates, once the certificates expire should become liable to business tax at the same rates and following the same principles as what is being reflected in this white paper.

C/ CALCULATION OF THE TOTAL INCOME OF A PERSON

Clarification on how a taxpayer having several businesses taxed at different rates shall be considered for the purpose of levying the business tax.

With this new proposal, what will determine the tax payable on is the turnover of the person. In order to simplify the treatment of persons who have several businesses which are not all falling under the same tax bracket, it is being proposed to aggregate all businesses income of one person and apply the rate corresponding depending on the bracket within which the person falls in.

However, due to the fact that the tourism, fishery and farming operators are liable to a tax rate until 2019, it is important to legally plan for the treatment of such taxpayer with income liable to different rates of tax.

With the proposal, the person will be considered to have two businesses and will have to separate the accounts for each of the business and pay the tax in accordance with the rates applicable per business, with an obligation to lodge two returns. It is important to note that if it is possible to ring fence the profits made by a same taxpayer, the losses shall also be ring fenced. The amendments to be proposed will ensure consistency of treatment for the profits and losses.

If the person has two businesses but the two businesses are liable to the same rate of tax, (for instance a person has a car hire business and a guest house business), the person will aggregate all income derived to apply the rate corresponding.

C/ Amendments to strengthen anti-avoidance rules

i. A new definition of "Arrangement"

The terms arrangement is already defined in our current revenue law, in section 40(1) of the

Revenue Administration Act in relation with a taxpayer entering into such with the intention or effect of rendering a company unable to satisfy a current or future revenue liability under a revenue law. The term is defined as “any contract, agreement, plan, or understanding whether express or implied and whether or not enforceable in legal proceedings”.

In the context of the Business tax, section 55 already makes reference to the term arrangement.

The purpose of both the revenue administration act and the section 55 of the business tax act is to capture any avoidance schemes being entered into by the taxpayer to reduce tax liability. It is therefore proposed to rely on the existing definition and include it in the business tax.

In addition, it is worth noting that this definition is in line with best practices and will therefore assist Seychelles to deliver on the fight against the erosion of its tax base and reducing the risk of profit shifting.

The wideness of what can be an arrangement is based on the wideness of ingenious montages taxpayers come up with internationally or domestically to avoid paying taxes.

ii. Amendment of section 54 on Transfer Pricing Rules

It is proposed to amend the section 54 to provide for the following-

- Where an arrangement exists between associates, the persons must calculate their income and tax payable according to the arm's length standard.

- The arm's length standard requires associates to quantify, characterise, apportion and allocate amounts to be included or deducted in calculating income to reflect arrangements that would have been made between independent persons.

- Where, in the opinion of the Revenue Commissioner, a person fails to comply with its duty to calculate their income according to arm’s length standard, the Revenue Commissioner may make adjustments consistent with subsection (1) and in doing so the Revenue Commissioner may-

  (a) Re-characterize an arrangement made between associated persons, including re-characterizing debt financing as equity financing;
  (b) Re-characterize the source and type of any income, loss, amount or payment; and
  (c) Apportion and allocate expenditure, including that of a permanent establishment, based on turnover."

Transfer pricing is one of the heating international topic as the focus is on Governments to ensure that everyone pays its fair share of tax where the economic value is created.

Transfer pricing rules as currently drafted in our section 54 does not reflect an efficient way for the SRC to identify and assess the transfer pricing risks and ensure that this goal is achieved.

The purpose of the amendment is therefore to enable the SRC to ensure an efficient application of the transfer pricing rules and also develop responsibility for the taxpayer to price their transaction or arrangements at arm's length. Indeed, transfer pricing rules shall not be initiated only when the Revenue Commissioner requests it, it should be automatic. The amendment aims at reflecting this change.

It is to be noted that the Revenue Commissioner may make adjustment to the assessment that would be made by a taxpayer when it is felt that this assessment is not reflecting the actual liability of the taxpayer. This is in line with the section 11 of the Revenue Administration Act which applies to all revenue laws, including the Business Tax.

Conclusion

The government is aware of the impacts these new policies may have on the Businesses but it is felt that the proposed system will reduce the compliance burden for taxpayers and ensure revenue collection from SRC.