News Alert on the 2019 Singapore Budget and Other Recent Tax Developments

In the bicentennial year of the founding of modern Singapore, Finance Minister Heng Swee Keat delivered an expansionary 2019 Budget that was centred on building a "Strong, United Singapore", in a sustainable and fiscally responsible way. Mr Heng announced a raft of measures, including the Bicentennial Bonus, and provided details on the Merdeka Generation Package for eligible citizens born in the 1950s, the restructuring of diesel taxes to tackle climate change, the tightening of Goods and Services Tax (GST) import relief for travellers, support for small-and-medium-sized enterprises (SMEs) in building deep capabilities, the tightening of the foreign worker quota in the service sector, and increased defence spending, among others.

On the corporate and individual tax front, the 2019 Budget saw no significant changes, with the existing tax incentives being refined, extended, or rationalised in order to reflect evolving policy considerations. The Minister has reiterated the government's commitment to ensuring that the tax policy remains fair, progressive, and pro-growth; the renewal of the existing tax measures – especially in the areas of investment in intellectual property and the financial services sector – is a reflection of this commitment, which has long been a cornerstone of Singapore tax policy.

This alert summarises selected key tax proposals from the Budget, as well as the major tax developments over the previous year, which may be of interest to businesses and investors operating in Singapore.

Corporate Tax

The prevailing corporate tax rate remains at 17%.

Extension of tax amortisation for the acquisition of intellectual property rights

Section 19B of the Income Tax Act (ITA) provides for writing down allowances (WDA) on the capital expenditure that is incurred in acquiring qualifying intellectual property rights (IPRs), over a writing down period of 5, 10, or 15 years. This tax benefit had a sunset clause of YA 2020 (i.e. only qualifying expenditure that had been incurred on or before the basis period for YA 2020 was eligible for the WDA claim). Recognising the importance of IPRs as value-drivers in a knowledge-based economy, and in line with Singapore's aspiration to be a global IP hub, the Minister has extended the expiry of the scheme by a further five years, to YA 2025.

Extension of the investment allowance claim under the Automation Support Package

The Automation Support Package was first introduced in 2016 Budget, with the objective of incentivising businesses to automate. Taxpayers are eligible to claim a 100% investment allowance (IA) on approved capital expenditure of up to S$10 million (net of any grants and on a per project basis) that has been incurred on projects approved by Enterprise Singapore during the three-year period from 1 April 2016 to 31 March 2019. The support package has been extended for another two years, until 31 March 2021. Enterprise Singapore is expected to release further details in due course.

Financial Services Sector

Singapore continues to attune its tax policy to the needs of the financial services industry, in order to retain its position as one of the most prominent financial centres in the world.

The extension and refinement of tax incentive schemes for funds that are managed by Singapore fund managers

Currently, a Singapore-managed fund may qualify for one of the following fund tax incentives if the approval is granted by 31 March 2019:

- The basic tier – offshore fund exemption under section 13CA or the Singapore resident fund exemption under section 13R.
- The enhanced tier fund exemption under section 13X.

As anticipated by most, the 2019 Budget extends the above fund tax incentives till 31 December 2024.

As a further boost to the Singapore fund industry, the 2019 Budget announced the following enhancements in the basic and enhanced tier incentives:

- With effect from 19 February 2019, the enhanced tier fund scheme (under section 13X) will be enhanced to (i) include co-investments, non-company special purpose vehicles

(SPVs), and more than two tiers of SPVs, (ii) allow debt and credit funds to access the "committed capital concession", and (iii) include managed accounts.

- Under the existing treatment, the securities issued by basic tier funds (under sections 13CA and 13R) must not be 100% beneficially owned, by Singapore persons. This condition will now be removed, with effect from YA 2020. This relaxation provides impetus to Singapore-based investors/venture capital funds in terms of applying for the section 13R scheme, in cases where the requisite conditions under the section 13X scheme could not be met (e.g. the minimum fund size of S$50 million could be too high for them to meet).
- The list of Designated Investments (DIs) will be expanded by removing the counter-party and currency restrictions, and by including investments such as credit facilities and advances, as well as Islamic financial products that are the commercial equivalents of DIs. This enhancement will apply to income that is derived on and after 19 February 2019.
- The list of Specified Income (SI) will be enhanced to include income in the form of payments that fall within the ambit of section 12(6) of the ITA (i.e. interest on debt, etc.), in respect of income that is derived on and after 19 February 2019.
- Qualifying non-resident funds, under sections 13CA and 13X of the ITA, will be eligible for the concessionary withholding tax rate of 10% applicable to qualifying non-resident non-individuals when investing in Singapore-listed Real Estate Investment Trusts (S-REITs) and Singapore-listed Real Estate Investment Trusts Exchange-Traded Funds (REITs ETFs). This will apply to S-REITs and REITs ETFs distributions made from 1 July 2019 to 31 December 2025.

Extension of GST remission for qualifying Singapore-managed funds

Qualifying funds managed by prescribed fund managers in Singapore are allowed, to reclaim the GST input tax on expenses at a fixed recovery rate. In line with extension of above fund tax incentives, this concession will also be extended until 31 December 2024.

Extension of tax concessions for S-REITs, REITs ETFs, and Registered Business Trusts (RBTs)

Currently, S-REITs and REITs ETFs enjoy various tax concessions, such as tax transparency treatment, tax exemption on distribution to individuals (except those deriving it through a partnership in Singapore or business) and concessionary 10% tax rate for distributions to non-resident non-individual investors. S-REITs also enjoy tax exemption on qualifying foreign-sourced income.

To continue to enhance Singapore's status as a REITs hub in Asia, the expiry of above tax incentives for S-REITs and REITs ETFs will be extended from 31 March 2020 to 31 December 2025. The 2019 Budget also removes the sunset clause on exemption of distributions to individuals from both S-REITs and REITs ETFs.

On similar lines, the expiry of GST remission will also be extended to 31 December 2025 for the listed S-REITs and RBTs in the infrastructure business, ship leasing, and aircraft leasing sectors.

The Monetary Authority of Singapore (MAS) is expected to provide further details on all the above changes by May 2019.

Non-renewal of the Designated Unit Trust (DUT) and Approved Unit Trust (AUT) schemes

As part of a regular review of existing tax incentives, the Minister has decided not to extend the DUT and AUT schemes, which are set to lapse after 31 March 2019 and 18 February 2019**,** respectively.

Existing unit trusts with DUT status will continue to receive the tax deferral benefits under the DUT scheme, on and after 1 April 2019, subject to meeting all the conditions. New funds, in the form of unit trusts, may apply for other tax incentives for funds.

Existing AUTs, on the other hand, will continue to receive the tax concession under the AUT scheme for a five-year transitional period, from YA 2020 to YA 2024 (both inclusive), to allow for time for them to transition to alternative tax incentive schemes (where relevant).

Personal Income Tax

The top marginal tax rate remains at 22%, with the rates and bands also remaining unchanged.

Personal income tax rebate of up to S$200

As part of the Bicentennial Bonus, for the year of assessment (YA) 2019 (i.e. the 2018 calendar year), all individual tax residents will be entitled to a personal income tax rebate, at the lower of 50% of tax payable or S$200 per taxpayer.

Removal of the child's age requirement for the claims for grandparent caregiver relief

From YA 2020 (i.e. the 2019 calendar year), working mothers will be eligible to claim grandparent caregiver relief, in respect of handicapped and unmarried dependent children, regardless of the child's age (which had to be 12 years old or below, previously). All existing conditions remain unchanged.

Non-renewal of the Not Ordinarily Resident (NOR) scheme

The NOR scheme was introduced in the 2002 Budget, with the objective of attracting the relocation of talent with regional and global responsibilities to Singapore. The NOR scheme allows eligible individuals to enjoy tax concessions for a period of five years, namely, the exemption of Singapore employment income tax corresponding to the number of days spent outside of Singapore for business reasons (through time apportionment) and tax exemptions on the employer's contribution to non-mandatory overseas pension funds.

In line with the wider policy of reducing the reliance on foreign workers (including the tightening of the service sector that was also introduced in this year's Budget), the NOR scheme will be allowed to lapse after YA 2020 (i.e. no NOR status will be granted after YA 2020). Taxpayers already enjoying the NOR status, or those who may be accorded the status in YA 2020, will continue to enjoy the tax concession until the relevant five-year qualifying period expires.

Key tax developments in year 2018

Singapore Variable Capital Company – a flexible investment fund vehicle available from 2019

In March 2017, the MAS proposed a new form of corporate structure known as the Variable Capital Company (VCC) for the constitution of collective investment schemes (CIS). The Parliament passed the Variable Capital Companies Bill in October 2018.

The VCC structure offers two distinct advantages. Firstly, unlike a company, the variable capital structure, amongst others, allows payment of dividends to shareholders out of capital instead of profits. Secondly, the possibility of a notional segregation of assets and liabilities within a single entity enables the setup of a stand-alone/umbrella fund with multiple sub-funds. The sub-funds may have different investment strategies to cater to different sets of investors, with the assets and liabilities of each sub-fund segregated and ring-fenced, i.e., performance or solvency of one sub-fund may not affect the other sub-funds.

The VCC structure is expected to become available sometime in 2019. Provisions have been made in the legislation to allow foreign fund structures similar to the VCC to re-domicile to Singapore.

The MAS has recently released details on the tax framework for VCC. Very broadly, VCC will be treated as a single entity for tax purposes, i.e., sub-funds will not need to undertake separate tax compliance. VCC should be eligible to access Singapore's tax treaty network where it is considered a Singapore tax resident. VCC will also be eligible to apply for Singapore fund tax exemptions under section 13X or 13R of the ITA.

The VCC structure provides the flexibility much desired by the fund management industry and puts Singapore on par with other popular international fund domicile jurisdictions such as Ireland and Luxembourg, which have long offered similar structures. This should go a long way in boosting the country's attractiveness as an international fund management centre.

Intellectual Property / Research and Development

Intellectual Property Development Incentive - Singapore's equivalent of the "patent box" regime

The Intellectual Property Development Incentive (IDI) was first announced in Budget 2017 to encourage the exploitation of intellectual property (IP) arising from R&D activities undertaken in Singapore.

The broad design of the IDI is expected to incorporate the modified nexus approach recommended by the OECD's Final Report for BEPS Action 5, whereby only IP income arising from substantive activities carried out in Singapore will be incentivised.

The IDI was legislated into the ITA in October 2018, with the effective date of 1 July 2018. The regulation prescribing the detailed rules (including the definition of qualifying IP and qualifying IP income for IDI purposes) should be forthcoming but are yet to be released on the date of this publication.

While the final regulations are yet to be released, offshore investment funds with Singapore-based investment managers/ advisors may start weighing whether this alternative will help them better align the location of funds with substantive activities; this could become even more important with new tax treaty developments (refer to our comments on MLI).

Exclusion of IP income from the Pioneer Service Companies Incentive and Development and Expansion Incentive

In conjunction with the introduction of the BEPS-compliant IDI, the Government amended the legislation for the Pioneer Service Companies (PC-S) incentive and the Development and Expansion Incentive (DEI) in May 2018 to exclude IP income from the scope of these incentives.

For taxpayers granted the PS-C and DEI status or who had their renewal granted on or after 1 July 2018, IP income (as defined in the relevant regulation) will be excluded from the scope of qualifying income. Under a limited grandfathering provision for existing PS-C and DEI incentive approved prior to 1 July 2018, income from existing IP (subject to certain anti-avoidance provisions for IP acquired from related parties) would continue to enjoy concessionary tax treatment till 30 June 2021.

Given the changes to the tax incentives for IP income, it is timely for taxpayers to review their IP structure and related activities in Singapore to assess the impact of the exclusion of IP income from incentivised income both from a tax compliance and planning perspective, and how they might benefit from the newly introduced IDI.

Enhanced deduction for qualifying expenditure on R&D and IP protection

To encourage innovation and protection of IP, the Government introduced the following enhancements for tax deduction schemes in the R&D and IP space:

- Deduction for qualifying expenditure (i.e. staff cost and consumables) incurred on qualifying R&D projects conducted in Singapore will be increased to 250% from the existing 150%;
- Qualifying IP registration costs, which before this enjoyed 100% tax deduction, will now qualify for enhanced 200% deduction on the first S$100,000 qualifying costs incurred per tax year; and
- Qualifying IP in-licencing costs, which before this enjoyed 100% tax deduction, will now qualify for enhanced 200% deduction on the first S$100,000 qualifying costs incurred per tax year.

The above enhancements will take effect from YA 2019 till YA 2025 (unless extended). While not as generous and expansive in scope, these enhancements nonetheless serve to partially fill the gap left by the expiry of the Productivity and Innovation Credit (PIC) scheme after YA 2018.

Transfer Pricing

Revised e-Tax Guide on Transfer Pricing (Fifth Edition) (the "Singapore TP Guidelines") and Regulation for Transfer Pricing Regulation

In October 2017, the Government introduced the following transfer pricing (TP) related legislative changes in the ITA:

- Introduction of a 5% surcharge on the amount of adjustment with effect from YA 2019;
- Introduction of compulsory requirement for contemporaneous TP documentation (TPD) for businesses (i.e. generally only for businesses with turnover exceeding S$10 million) with effect from YA 2019 under section 34F of ITA. Non-compliance may result in a fine not exceeding S$10,000.

On 23 February 2018, the Government released the Income Tax (Transfer Pricing Documentation) Rules 2018 (the TPD Rules), which prescribe the form and content required to be followed in preparing TPD documentation from YA 2019 and applicable exemptions. The Singapore TP Guidelines were also updated to provide details on the above.

As a practical note, prior to the above developments from 2017 to-date, contemporaneous TP documentation was already required under general record keeping requirements (though non-compliance may result in a fine not exceeding S$1,000). Many of the key requirements and exemptions prescribed in the TPD Rules were already required under the existing TP guidelines. Other than changes such as the introduction of surcharge and stiffer penalties for the non-preparation of TPD, the legislative developments are significant in that they mark the transformation of the Singapore TP regime from one that is guidance-based to one that is more formal and legislation-based.

In addition, taxpayers with related party transactions exceeding S$15 million are now required to submit a disclosure form with their tax return from YA 2018; such data will be used by the IRAS to assess TP risk of taxpayers for audit purposes.

Given these developments, taxpayers are advised to gear up their defence against TP audit by reviewing the adequacy of their existing related party transactions and ensure that contemporaneous TPD is readily in place. In particular, given the penalty for failure to maintain contemporaneous TPD can be up to S$10,000, taxpayers who are currently not in compliance with the documentation requirements should act now and get the documentation completed by 30 November 2019.

Double Taxation Agreement

Multilateral agreement (MLI)

Singapore signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) on 7 June 2017, that will see various modifications to its tax treaties, including the adoption of the principal purpose test (PPT) rule and other anti-treaty abuse rules.

On 21 December 2018, the Singapore government ratified the MLI, which will enter into force for Singapore on 1 April 2019. The timing on when the MLI modifications will come into effect for a given tax treaty would depend on when relevant treaty partners completed their ratification procedures. From the perspective of Singapore's tax treaties, assuming that a treaty partner had ratified its MLI at around the same time as Singapore, the MLI modifications would apply to taxes arising – at the earliest – from year 2020 onwards.

Given that the various anti-treaty abuse rules are expected to see wide adoption in more than 1,000 bilateral tax treaties concluded amongst the more than 80 (and growing) jurisdictions signing the MLI, tax administrations will have more ammunition than ever to deal with tax structures perceived as abusive use of tax treaty, especially those lacking commercial substance. Taxpayers currently availing of treaty benefits are therefore well advised to assess the viability of their existing cross-border structures, and where required, take the necessary remedial action.

Information Sharing

Agreements for exchange of tax information and reciprocal exchange of financial account information with the United States

On 13 November 2018, Singapore signed a Tax Information Exchange Agreement (TIEA) and a reciprocal Foreign Account Tax Compliance Act Model 1 Intergovernmental Agreement (reciprocal FATCA IGA) with the United States.

The new FATCA IGA allows for reciprocal two-way exchange of financial account information between Singapore and the US; it will supersede the current non-reciprocal IGA

(i.e. one-way sharing of information with the US) signed on 9 December 2014 when it comes into force.

Court of Appeal upheld decision to allow exchange of tax information: AXY and others v CIT [2018] SGCA 23

The Court of Appeal affirmed the decision of the High Court in upholding the decision of the Comptroller to share information with Korea's national tax authority pursuant to an exchange of information (EOI) request made under the Singapore-Korea tax treaty, and provided important clarification on the principles applicable to the EOI regime in Singapore.

With Singapore already committed to implementing the automatic exchange of offshore financial account information (AEOI) for tax purposes with more than 90 jurisdictions under the OECD's Common Reporting Standard (CRS) by September 2018, the above development is a continuation (or reflection) of the unstoppable global trend towards greater transparency and exchange of information.

Other Corporate Tax Changes

Increased expenditure cap for further deduction on qualifying internationalisation expenditure without pre-approval

To encourage Singapore companies to internationalise, the tax deduction scheme for internationalisation (DTDi) will be enhanced from YA 2019. Taxpayers will now be eligible to claim 200% deduction on qualifying expenses, subject to a cap of S$150,000 (up from S$100,000 before), without having to apply to the relevant government bodies for approval. For qualifying expenses exceeding S$150,000, prior approval still has to be sought before making the enhanced deduction claim.

Adjustment to tax exemption schemes from YA 2020

With effect from YA 2020, tax exemption under the start-up tax exemption scheme and partial tax exemption scheme will be reduced, with full corporate tax rate of 17% applicable on chargeable income above S$200,000 instead of S$300,000.

Withdrawal of administrative concession for lower WHT rate on arm's length onshore routine service fees to non-resident related parties

Due to low adoption rate, with effect from 1 April 2018, the IRAS has withdrawn the administrative concession for lower withholding tax rate on section 12(7)(b) and (c) payments for prescribed routine services rendered in Singapore by non-resident related parties. Previously, subject to certain conditions, the IRAS effectively allowed the imposition of withholding tax on the arm's length mark-up rather than on gross service fee. Notwithstanding the withdrawal of the administrative concession, taxpayers wishing to benefit from the concession may still apply to the IRAS on a case-by-case basis.

Tax treatment from adoption of accounting standards

The IRAS released the following e-Tax Guides to clarify the tax treatment arising from the adoption of the relevant accounting standards:

- "Income Tax: Income Tax Treatment Arising from Adoption of FRS 109 – Financial Instruments", published on 22 November 2017;
- "Tax Treatment Arising from Adoption of FRS 115 or SFRS(I) 15 - Revenue from Contracts with Customers (Second edition)", first published on 12 January 2018 and revised on 16 November 2018.
- "Tax Treatment Arising from Adoption of Financial Reporting Standard 116 or Singapore Financial Reporting Standard (International) 16 – Leases", published on 8 October 2018.

It is mandatory for companies to adopt FRS 109 and FRS 115 from financial year beginning on or after 1 January 2018 (i.e. YAs 2019 or 2020), and FRS 116 from financial year beginning 1 January 2019 (i.e. YAs 2020 or 2021). Therefore, it is timely for companies required to comply with these accounting standards to carefully examine the tax implications so as to ensure that the correct tax treatment is adopted in the tax computations.

Tax Cases Updates

Tax cases on taxability of gain on disposal of assets

While it is true that Singapore does not have a capital gains tax regime, gains from disposal of properties regarded as revenue in nature would still be subject to tax. Whether a gain is capital or revenue in nature is frequently a matter of contention between the IRAS and taxpayers. Year 2018 saw two tax cases on this very issue – GCH v CIT [2018] SGITBR 1 and *BQY* and *another v* CIT [2018] SGHC 75 decided by the Board of Review and High Court, both in favour of the IRAS.

In *GCH*, the Board of Review held that the individual taxpayer was trading in real properties based on a "badges of trade" analysis; the taxpayer was thus subject to tax on the disposal gains under section 10(1)(a) of the ITA. In BQY, though the individual taxpayers (husband and wife) were not pursuing any property trading activities, the High Court found that they had purchased the properties in question for resale with a view to profit; the gains on disposal were taxed under the "catch all" provision of section 10(1)(g) of the ITA.

These cases highlight the perennial uncertainty around the determination of the revenue versus capital demarcation. It also underlines the importance for taxpayers – both individual and corporate alike – to maintain proper documentation of their intention at the outset of acquiring the properties, and to ensure that their subsequent actions (relating to holding period, etc.) reinforce such intention, if they wish to adopt a capital gains argument.

GST

GST on import of services from 1 January 2020

As announced in Budget 2018, with a view to level the playing field between local and offshore suppliers, Singapore will implement the following GST measures from 1 January 2020 to impose GST on imported services (i.e. supply of services made by offshore suppliers):

- Reverse charge for Business-to-Business (B2B) supplies of imported services; and
- Overseas vendor registration for Business-to-Consumer (B2C) supplies of imported digital services.

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