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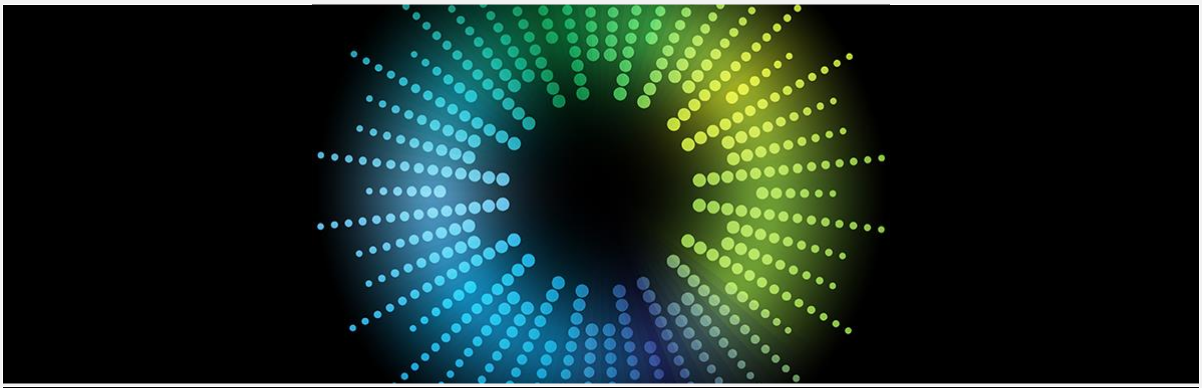

Singapore Business Tax developments

Income Tax (Amendment) Bill 2017

Overview

The Ministry of Finance (MOF) conducted a public consultation exercise from 19 June to 10 July 2017 on the draft Income Tax (Amendment) Bill 2017 ("draft Bill") and various draft subsidiary legislations arising from changes to the tax framework for insurers.

Comments on the draft Bill will be considered by the MOF and, where appropriate, incorporated into the draft Bill prior to its introduction in Parliament for approval.

Key proposed changes

The draft Bill incorporates legislative amendments to the Income Tax Act arising from announcements made during Budget 2017 as well as other non-Budget updates.

Key changes include:

1. New accounting standards taking effect for annual periods beginning on or after 1 January 2018

- FRS 109—Financial Instruments

FRS 109—Financial Instruments will apply to entities for annual periods beginning on or after 1 January 2018 and replaces the existing FRS 39—Financial Instruments: Recognition & Measurement.

Briefly, the proposed legislation in the draft Bill largely aligns the tax treatment of financial instruments (insofar as the instruments are on revenue account) to the accounting treatment. As currently drafted, there is no option for taxpayers to 'opt-out' of this tax treatment and this would result in revenue gains on financial instruments to be taxed on a marked-to-market basis (i.e., unrealised gains are taxable), unless specific exceptions apply.

The IRAS has previously issued a draft e-tax guide on the proposed income tax treatment arising from the adoption of FRS 109 and this guide is expected to be updated once the relevant legislation is passed.

- <u>FRS 115—Revenue from Contracts with Customers</u>

FRS 115—Revenue from Contracts with Customer will be effective for annual periods beginning on or after 1 January 2018 and supersedes the following existing accounting standards:

- FRS 11—Construction Contracts
- FRS 18—Revenue
- INT FRS 113—Customer Loyalty Programmes
- INT FRS 115—Agreements for the Construction of Real Estate
- INT FRS 118—Transfers of Assets from Customers; and
- INT FRS 31—Revenue: Barter Transactions involving Advertising Services

Legislation has been proposed to prescribe the tax treatment for transitional adjustments arising from the adoption of FRS 115. Briefly, an entity applying FRS 115 may be required to adjust its revenue amount in its financial accounts for previous basis periods.

If the income assessed for a past year of assessment (Amount A) is different from the amount that would have been computed had the Comptroller used the adjusted revenue amount as the starting point for the computation (Amount B), then the shortage (i.e., B-A) is treated as income chargeable to tax (specific rules apply if the taxpayer's income is subject to tax at rate(s) other than 17%) in the year of assessment of the basis period in which FRS 115 is first adopted.

If the difference results in an excess (i.e., A-B) amount, the excess is treated as:

i. A reduction of the amount of exempt income (if applicable); or

ii. Allowable as a deduction against income (specific rules apply if the taxpayer's income is subject to tax at rate(s) other than 17%) for the year of assessment of the basis period in which FRS 115 is first adopted.

It appears that if the Comptroller would not have used the adjusted revenue amount as the starting point in assessing such income (e.g., in the case where accounting revenue recognised previously defers from the taxable revenue), these transitional adjustments should not apply.

As with FRS 109, the IRAS has previously issued a draft e-tax guide on the proposed income tax treatment arising from the adoption of FRS 115. The draft e-tax guide recognised that the timing of revenue recognition under FRS 115 would differ from existing accounting practices under certain circumstances. However, we note that the draft

Bill does not prescribe legislation to address the effect of FRS 115 on a prospective basis. In this regard, where accounting practice under FRS 115 runs counter to tax principles, the latter prevails and tax adjustments should be required.

2. Tax treatment for foreign companies domiciled in Singapore

The draft Bill introduces a tax framework for companies that re-domicile into Singapore under the inward re-domiciliation regime, which was introduced in the Companies (Amendment) Bill 2017.

Under the tax framework, amongst other changes, the re-domiciled company will be subject to the following tax treatment:

i. Allow the claim of capital allowances for transferred-in plant and machinery used for business in Singapore, based on the lower of their market value on the date of re-domiciliation or net book value;
ii. Allow the claim of writing-down allowance for transferred-in intellectual property rights used for business in Singapore, based on the lower of their market value on the date of re-domiciliation or net intangible value;
iii. Disallow the deduction of transferred-in trade receivables that have subsequently become bad or impaired after the re-domiciliation, and not tax all subsequent recoveries of the bad debts or reversal of impairment losses that have not been allowed tax deduction;
iv. Disallow the deduction for impairment loss and not tax the reversal to impairment for financial assets on revenue account, unless gains or losses from such assets will be taxed or allowed in Singapore;
v. Allow a tax credit to relieve double taxation on Singapore sourced income on an approval basis; and
vi. Allow a deduction for the pre-commencement expenses incurred by a re-domiciled company that has not commenced business in the original jurisdiction.

As currently drafted, the tax framework for inward re-domiciliation does not appear to cover foreign entities that have carried on a trade or business in Singapore (such as those that have a Singapore branch) prior to its re-domiciliation.

The framework also provides for tax credits to be given (upon approval) to a re-domiciled company if its originating jurisdiction imposes an exit tax on its unrealised profits and those profits are also taxed in Singapore. We expect the authorities to issue further details on qualifying conditions in due course.

3. Transfer pricing changes

Please refer to the Tax Alert on Singapore Transfer Pricing Developments dated 28 June 2017 for details.

4. Tax incentives

The draft Bill amends the Income Tax Act to give legislative effect for the following schemes announced during Budget 2017:

i. Extension and refinement of the Aircraft Leasing Scheme;
ii. Extension of tax exemption on payments made to non-resident non-individuals for structured products offered by financial institutions; and
iii. Extension of the Tax Incentive Schemes for Infrastructure Project.

The draft Bill also includes updates and refinements to several tax incentives that were not announced during Budget 2017. These include:

- Insurance Business Development scheme

The Monetary Authority of Singapore had in May 2017 released details on refinements to the Insurance Business Development (IBD) Scheme, which takes effect for new awards granted or existing awards renewed on or after 1 June 2017. Legislative effect will be given to these refinements via the draft Bill and the relevant subsidiary legislations.

Briefly, the following activities will be included within the scope of the IBD:

i. Underwriting income derived from insuring and reinsuring both onshore and offshore insurance risks for IBD and IBD-Captive Insurance;
ii. Both onshore and offshore investment income (dividend, qualifying interest, gains from sale of qualifying investment) relating to the incentivised insurance business lines for IBD, IBD-Marine Hull and Liability Insurance Business, IBD-Captive Insurance and IBD-Specialised Insurance; and
iii. Onshore and offshore broking business income for IBD-Insurance Broking Business and IBD-Specialised Insurance Broking Business.

The following activities and income will be excluded from the scope of IBD:

i. All underwriting income, investment income, and insurance broking commission and fee income from onshore and offshore direct life insurance;
ii. All underwriting income, investment income, and insurance broking commission and fee income from onshore and offshore direct stand-alone fire, motor, work injury compensation, personal accident and health insurance;
iii. Interest income other than qualifying interest;
iv. Gains from sale of investments other than qualifying investments; and
v. All investment income relating to immovable properties, not relating to any prescribed asset or project, in and outside Singapore.

- Financial Sector Incentive (FSI) Scheme

The draft Bill amends the Income Tax Act to prescribe for a tax rate of 13.5% (in addition to 5%, 10%, and 12%) for qualifying income derived by taxpayers that were granted or have renewed their Financial Sector Incentive—Standard Tier award (FSI-ST) on or after 1 June 2017.

The Monetary Authority of Singapore had, earlier in May 2017, announced the refinement of the scope of incentivised activities under the FSI-ST along with an increase in the scheme's concessionary tax rate from 12% to 13.5%. Updated Regulations (Income Tax (Concessionary Rate of Tax for Financial Sector Incentive Companies) Regulations 2017) that were issued shortly thereafter did not reflect the updated tax rate.

It is not clear whether the 2017 Regulations will be updated following the amendment of the main Income Tax Act.

- Maritime Sector Incentive (MSI)

The draft Bill amends the definition of "corporate services" in Section 43ZF(8) under the MSI-Shipping Support Services (MSI-SSS) award to exclude the following services effective from the Gazette date:

i. Marketing control, planning and brand management services under paragraph (a) of the corporate service definition;
ii. Research and development (including test bedding) services carried out on behalf of the approved related company; and
iii. Intellectual property management services under paragraph (f) of the corporate service definition.

In addition, paragraph (l) of the definition of "corporate services" is also amended to clarify that Information Technology (IT) services refers to IT support services, effective from 2 June 2011.

Companies enjoying the MSI-SSS tax incentive for providing qualifying corporate services would need to scrutinise the transactions carefully and ensure that income derived from the above excluded services are identified and taxed at the normal tax rate.

- Global Trader Programme (GTP)

The draft Bill amends the definition of "global trading company" to allow a company that carries on the following businesses to be approved under the GTP, subject to conditions:

i. International trading in commodities derivatives; and
ii. Brokering international trades in commodities.

Currently, businesses conducting such activities can only be approved under the GTP if they are also in the business of physical trading.

- Real Estate Investment Trust (REIT)

The draft Bill extends the expiry date of the concessionary income tax rate of 10% (i.e., the withholding tax rate) on distributions made by the trustee of a REIT to qualifying non-resident non-individual investors of listed REITs from 31 March 2015 to 31 March 2020.

This was previously announced during Budget 2015.

5. Other tax changes or comments

- Liberalised tax deduction for payments under Cost Sharing Agreements (CSAs) for Research & Development (R&D) projects

The draft Bill provides for the following treatment for payments under CSAs:

i. Payments made under a CSA need not be related to the taxpayer's trade or business, and need not be undertaken in Singapore if unrelated to the taxpayer's trade or business, in order to be deductible.

   In addition, Section 15 of the Income Tax Act has been amended to allow a full deduction of the aforementioned CSA payments without the need to provide a breakdown of the expenditure covered by the CSA payments. This is an improvement over the Budget 2017 announcement, whereby it was proposed that taxpayers may opt to claim a tax deduction for 75% of CSA payments incurred for qualifying R&D projects without providing the breakdown of expenditure covered by the CSA payment.

ii. Allow an additional 50% deduction on qualifying costs incurred on R&D performed in Singapore, by the taxpayer or a research and development organisation on his behalf, under a CSA, even if the costs are reimbursed under the CSA. The additional 50% deduction is subject to a prescribed cap.

These changes will apply from the Year of Assessment 2018.

- Digital tax notices

The Income Tax Act will be amended such that the receipt of hardcopy tax notices by taxpayers, going forward, will be on an 'opt-out' basis.

In practice, the Comptroller will notify the taxpayer of the notices (for example, notices to file chargeable income estimates) that it intends to serve via electronic means and the taxpayer will be given an opportunity to 'opt-out' (i.e., continue to receive hardcopies) within a specified time frame.

This change will take effect from the date the Amendment Act is published in the Gazette.

- Intellectual Property Development Incentive (IDI)

It was announced in Budget 2017 that the IDI will be introduced to incentivise income generated from the exploitation of Intellectual Property arising from R&D activities performed by the taxpayer in Singapore or outsourced to third parties.

The IDI is slated to take effect from 1 July 2017. To-date, the Economic Development Board has yet to release details on this incentive and we note that legislation on the IDI is absent from the draft Bill.

Contacts

For more information on any of these issues, or any other Business Tax matters, please contact **Low Hwee Chua**, or your usual Business Tax Services contact in Deloitte.

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