Singapore Fund Tax Incentives

Asset & Wealth Management

Updates and clarifications

The Singapore Budget 2019 ("Budget 2019") was delivered on 18 February 2019, and several key proposals with regard to the fund tax incentive schemes were announced. Following this announcement, the MAS has issued a circular (FDD Cir 09/2019) on 7 June 2019 (the "Circular"). Here are the salient points of the Circular.

Designated Investments

Effective from 19 February 2019, the list of designated investments has been enhanced. Please refer to Appendix I for the key changes.

The list has been expanded to include additional qualifying investments and simplified to remove the need to track specific currency and counterparty restrictions in the previous list.

We welcome the expansion of the list, however, there is one complexity not removed and the industry was hoping that it would have been addressed in the Circular. This relates to investments in private trusts. In order for an investment in a private trust to qualify as a designated investment, the private trust itself needs to solely invest in designated investments. This means even a single investment, howsoever small, by that private trust in a non-designated investment will taint the entire investment into the private trust. It was hoped that this item would have been aligned to the change made in the item "units in any unit trust".

Specified Income

Effective from 19 February 2019, the list of specified income is enhanced to include income that fall within the ambit of section 12(6) of the Income Tax Act (the "Act"), except such income that is derived in respect of an immovable property situated in Singapore. The approach adopted here was expected (given similar carve outs for investments in the previous list of designated investments for Singapore immovable property).

We welcome the enhancement to the specified income list.

Reporting Obligations - 13CA and 13R Scheme

With effect from Year of Assessment 2020, instead of issuing annual statements to all investors of a 13CA / 13R fund, fund managers have the option of publishing relevant information on their website for investors to assess if they are liable to pay a financial penalty. Whichever method is chosen by the fund manager, it should be applied consistently.

Whilst other reporting obligations remain the same as before, it seems that a new reporting obligation has been introduced. The Circular mentions that the offering document of the 13CA / 13R fund should also state that the non-qualifying investors are required to declare the financial penalty in their income tax returns. There can be circumstances where the Singapore fund manager is only delegated a mandate to manage a small portion of the overall assets of a global fund. In these situations, the fund would be able to rely 13CA and perform the reporting obligation of issuing annual statements. It, however, introduces additional cost for global fund(s) to update their offering document for a Singapore matter (merely because there is one small mandate running from Singapore).

Further, in our view, the authorities should consider removing all reporting obligations where the fund has only qualifying investors. This is usually the case and such removal will reduce an administrative burden for managers.

13X Scheme

Master-Feeder-SPV Scheme

As expected, the Circular is clear that the SPVs under this umbrella scheme can be in any legal form, there can be any number of tiers of SPVs and the SPVs need not be 100% owned by the master.

However, one aspect will need to be clarified. This relates to the mention that where a feeder will "derive taxable income" from the master, it would be considered a trading feeder. We note that the language used is different from the legislation where reference is made to the carrying on of any "income-deriving activity" for one to be considered a trading feeder. The circular should have kept the language aligned to the legislation and we hope a clarification is issued in this regard. The feeder may derive income (e.g. dividends) from the master and if this makes it a trading feeder then the non-trading feeder option under 13X will have limited use. In our view, that cannot be the intention.

We hope the authorities are able to address this point.

Co-investments allowed in Master-Feeder-SPV and Master-SPV structures

Effective from 19 February 2019, SPVs in a Master-Feeder-SPV or Master-SPV structure no longer need to be wholly-owned by the master fund provided the co-investors in the SPV are foreign investors or incentivised funds (i.e. approved under 13CA, 13R, 13X or 13Y Scheme).

Foreign investor is defined in the Circular as bona fide non-resident investor that does not have a permanent establishment in Singapore (other than a fund manager) and does not carry on a business in Singapore.

13X Scheme for managed accounts

A managed account has been defined as a dedicated investment account where an investor places funds directly with a fund manager without using a separate fund vehicle.

Effective from 19 February 2019, the 13X Scheme has been extended to managed accounts subject to 13X conditions being met. In addition, to avail himself of the 13X Scheme, the investor of a managed account (i.e. the account holder) must:

- maintain separate custodian accounts for different managed accounts with the same or different fund managers; and
- show that he has entered into an investment management agreement (IMA) with the fund manager. As part of the 13X application process, the IMA which makes reference to the managed account will need to be provided to the MAS.

It is clarified in the Circular that a separate 13X application is required to be made for each managed account even if they are held by the same investor / account holder. Further, it is also clarified that the economic commitments under the 13X Scheme (i.e. the S$50 million minimum fund size and S$200,000 annual local business spending) are to be met separately for each account.

As with other 13X funds, an investor of a managed account will be required to file a tax return in respect of income derived through the approved managed account. If the investor is already filing a tax return in Singapore, such income derived through the approved managed account is to be reported in the same tax return, but with separate identification from other income of the investor.

13CA Scheme

Waiver of qualifying investor test for retail unit trusts for the initial period

As retail unit trusts constituted on or after 1 April 2019 will not be able to rely on the Designated Unit Trust (DUT) Scheme, to alleviate the tax impact to these unit trusts, they are granted waiver of the qualifying investor test under 13CA. For this purpose, a retail unit trust means:

- a unit trust which is included under the Central Provident Fund Investment Scheme (CPFIS); or
- a unit trust which meets all of the following conditions:
  - the unit trust is a collective investment scheme (CIS) that is authorised under section 286 of the Securities and Futures Act and the units of which are open to public for subscription;
  - the unit trust is not a real estate investment trust (REIT) or a property trust that invests directly in Singapore immovable properties; and
  - the trustee of the unit trust is tax resident in Singapore.

Do note that the above waiver applies only for the first two years of assessment from the date of the unit trusts' constitution. After the above initial period, these unit trusts would either have to apply for 13X Scheme (if conditions are met) or continue to rely on 13CA but the fund managers will have to track the profile of the investors in the unit trusts for the purpose of the qualifying investor test.

Although the proposed change is welcome, we hope the qualifying investor test would be entirely removed for retail funds (and not limited to just two years) in due course.

13CA Scheme for managed accounts

With effect from the year of assessment 2020, a managed account that belongs to a bona fide non-resident person or a designated person (as defined) will be deemed to meet the qualifying fund and qualifying investor tests under the 13CA Scheme.

We expect that this change will boost the asset and wealth management industry as it simplifies the administration of managed accounts.

13R Scheme

Condition to not derive income before application filed now modified

Effective 19 February 2019, funds that have derived income prior to their 13R application can apply for the 13R Scheme in the following scenarios: (a) warehousing of investment, (b) setting up bank accounts in anticipation of commencing operations and (c) placement of monies in deposits or money market instruments on a temporary basis.

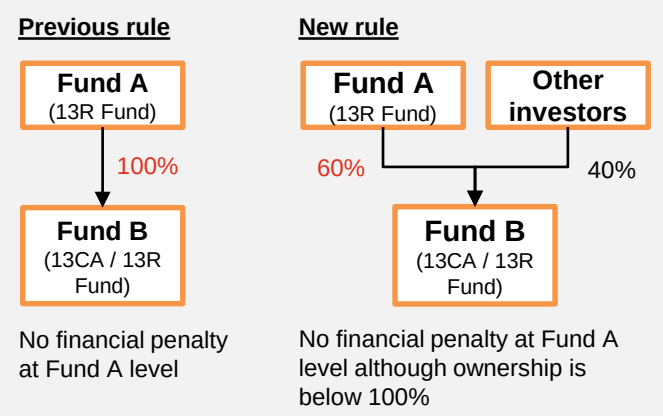
The Circular defines "warehousing of investments" as a fund acquiring investments at an initial stage of the fund's existence, prior to closing the fund. It will need to be clarified how the above relaxation would apply in the context of 13R applicants which do not have fund closing per se (these could be entities used for ring fencing under the main fund). It may also be worthwhile clarifying whether the above refers to final closing of the fund.

Further, there has not been guidance provided on how the "temporary basis" in item (c) is to be measured. For instance, can income derived by a money market fund from short-term placements in deposits or money market instruments be covered under the above exclusions? Further clarification may be needed.

No financial penalty for 13R fund

Previously, where a 13R fund owned more than the prescribed percentages (30% / 50%) in issued securities of a 13CA fund or another 13R fund as at the last day of the financial year of the 13CA / 13R fund, the first 13R fund can still meet the "qualifying investor" test if, among others, the 13CA / second 13R fund is wholly owned by the first 13R fund (shareholder) at all times during the basis period.

This "wholly-owned" condition has now been removed. This removal is a welcome move as it helps to facilitate co-investment structures at level of the 13CA / 13R fund.



Investments in S-REITs and REIT ETFs qualify for 10% concessionary rate

Non-resident funds under 13CA, 13X and 13Y Schemes can now enjoy the 10% concessionary tax rate applicable to qualifying non-resident non-individuals when investing in S-REITs and REIT ETFs provided:

- the fund does not have a permanent establishment in Singapore (other than the fund manager in Singapore); or
- the fund operates through a permanent establishment in Singapore (other than the fund manager in Singapore), but the funds used to acquire units in the S-REITs or REIT ETFs are not obtained from the operation in Singapore.

This enhancement will apply to S-REITs and REIT ETFs distributions made during the period from 1 July 2019 to 31 December 2025.

Others

Please refer to the **Budget 2019 Asset & Wealth Management – Key Proposals newsflash** for information on the other amendments made in Budget 2019 for which no additional details have been provided in the Circular.

Conclusion

The Circular is largely in line with the Budget 2019 announcements. We welcome the announcements and applauds the Government's efforts in continuously taking feedback in order to keep Singapore competitive.

However, there are a few aspects for which we hope the authorities will consider further so as to address the industry's concerns.

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Appendix I

The key changes to the list of designated investments is as follows.

	Prior to 19 February 2019	19 February 2019 onwards
A.	Real estate investment trusts, exchange traded funds or any other securities which are – i. denominated in foreign currency issued by foreign governments; ii. listed on any exchange; iii. issued by supranational bodies; or iv. issued by any company. but excluding any securities which are issued by any company that is – i. in the business of trading or holding Singapore immovable properties (other than the business of property development); and ii. not listed on a stock exchange in Singapore or elsewhere.	Units in real estate investment trusts and exchange traded funds constituted in the form of trusts and other securities (not already covered in other sub-paragraphs of the Designated Investments list) but excludes any securities issued by any unlisted company that is in the business of trading or holding of Singapore immovable properties (other than one that is in the business of property development).
B.	Deposits held in Singapore with any approved bank as defined in section 13(6) of the Act.	Deposits placed with any financial institution.
C.	Foreign currency deposits held outside Singapore with financial institutions outside Singapore.	
D.	Interest rate or currency contracts on a forward basis, interest rate or currency options, interest rate or currency swaps, and any financial derivative relating to any designated investment specified in this list of "designated investments" or financial index, with – i. a financial sector incentive company which is – A. a bank licensed under the Banking Act (Cap. 19); B. a merchant bank approved under Section 28 of the Monetary Authority of Singapore Act (Cap. 186); or C. a holder of a capital markets services licence under the SFA to deal in securities or a company exempted under that Act from holding such a licence; ii. a person who is neither resident in Singapore nor a permanent establishment in Singapore; or iii. a branch office outside Singapore of a company resident in Singapore.	Interest rate or currency contracts on a forward basis, interest rate or currency options, interest rate or currency swaps, and financial derivatives.
E.	Units in any unit trust which invests wholly in designated investments specified in this list of "designated investments".	Units in any unit trust, except: i. a unit trust that invests in Singapore immovable properties; ii. a unit trust that holds stock, shares, debt or any other securities, that are issued by any unlisted company that is in the business of trading or holding of Singapore immovable properties (other than one that is in the business of property development); and iii. a unit trust that grant loans that are excluded under paragraph (j) of the Designated Investments list (please refer to the next item in this table).

Appendix I (cont'd)

The key changes to the list of designated investments is as follows.

	Prior to 19 February 2019	19 February 2019 onwards
F.	Loans that are − i. granted by a prescribed person to any company incorporated outside Singapore which is neither resident in Singapore nor a PE in Singapore, where no interest, commission, fee or other payment in respect of the loan is deductible against any income of that company accruing in or derived from Singapore; or ii. granted by a person other than a prescribed person but traded by the prescribed person.	Loans (including secondary loans, credit facilities and advances), except: i. loans granted to any unlisted company that is in the business of trading or holding of Singapore immovable properties (other than one that is in the business of property development); ii. loans to finance/ re-finance the acquisition of Singapore immovable properties; and iii. loans that are used to acquire stocks, shares, debt or any other securities, that are issued by an unlisted company that is in the business of trading or holding of Singapore immovable properties (other than one that is in the business of property development).
G.	Any loan granted to a trustee of a trust constituted outside Singapore, where i. the trustee is neither resident in Singapore nor a PE in Singapore; and ii. for the year of assessment in question, no interest, commission, fee, or other payment in respect of the loan is deductible under the Act against any income of the trust accruing in or is derived from Singapore;	
H.	Emission derivatives.	Emission derivatives and emission allowances.
I.	Investments in prescribed Islamic financing arrangements under section 34B of the Act that are commercial equivalents of any of the other designated investments specified in this Part.	Islamic financial products (recognised by a Shariah council, whether in Singapore or overseas) and investments in prescribed Islamic financing arrangements under section 34B of the ITA that are commercial equivalents of any of the other designated investments specified in this list.
J.	-	Accounts receivables and letters of credits.
K.	-	Interests in *Tokumei Kumiai* (TK). A TK is a contractual arrangement under which one or more silent investors (i.e. the TK investors) make a contribution to a Japanese operating company (the TK operator) in return for a share in the profit/ loss of a specified business conducted by the TK operator (the TK business).