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Proposals to enhance Singapore's economy

Digital Transformation – The Way Forward

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Executive Summary

Technology is rapidly changing service delivery in both the public and private sectors. Against the backdrop of Singapore's continuing digital transformation to become a Smart Nation, Prime Minister Lee Hsien Loong and Finance Minister Heng Swee Keat have reiterated the need for the country to have sustainable revenues for investing in its future, and yet remain competitive internationally. It is in the light of these considerations that PwC suggests the following changes to enhance the fiscal environment to make it more conducive for Singapore to continue with this transformation, whilst at the same time encourage innovation and enterprise.

Key recommendations to help Singapore embrace digital disruption include enhancement to the writing down allowance for acquisition of intellectual property, and enhancements on the research and development (R&D) front to promote the creation of a more conducive environment to anchor high value added activities and intellectual property ownership (IP) in Singapore. We also submit measures to encourage local businesses to reinvent themselves to expand their footprint locally and overseas; these include enhancement to the double deduction for internationalisation and tax concessions for training and to help companies "go digital".

We have separately provided the Monetary Authority of Singapore (MAS) with suggested tax measures relating to the financial sector. These are attached as Appendix A.

Digital transformation to drive value creation

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Digital transformation to drive value creation

1. Section 19B writing down allowance for acquisition of IP

IP rights underpin the growth of modern economies; countries with robust IP environments have a Gross Domestic Product (GDP) per capita 21 times that of countries with the weakest regimes.[1] Singapore is recognised as having robust IP protection and is a preferred location for IP ownership. Even so, multinational companies may not be able to transfer full ownership of their IP to Singapore in the light of legal or commercial constraints. Nonetheless, they should be encouraged to locate activities relating to the management and control of their IP in Singapore and exploit it from here, as this will create economic spin-off for the Singapore economy.

Recognising this, we suggest that the writing down allowances for intellectual property under section 19B of the Income Tax Act (ITA) should be extended to the "economic owner" of IP in Singapore, without the need for prior approval from the Economic Development Board (EDB). This would be consistent with practices on IP amortisation around the world (e.g. in Australia and UK) where no distinction is made between the economic and legal owner of IP.

2. Enhanced deduction for overseas R&D activities with nexus to Singapore

Certain aspects of R&D activities cannot be carried out in Singapore for practical reasons such as inadequate sample size and different geographical environment. By necessity, these activities must be carried out overseas by businesses intending to locate and exploit the resulting IP in Singapore.

With the expiry of the Productivity and Innovation Credit (PIC) scheme, qualifying R&D activities conducted overseas would not qualify for enhanced deduction. Section 14DA of the ITA should therefore be amended to include qualifying R&D activities conducted overseas so long as the activities have a nexus to the Singapore business, e.g. the majority of the IP developmental activities will be carried out in Singapore or the IP developed out of the R&D will be owned by a Singapore resident enterprise.

3. Enhanced deduction for R&D after PIC expires

With the expiry of the PIC scheme, qualifying R&D expenditure would only be allowed 150% tax deduction. This is not really competitive, particularly in light of the extensive documentation required to prove that the project is a qualifying one. By way of comparison, UK provides a 225% "super" deduction for qualifying R&D expenditure by small and medium enterprises (SMEs) and Ireland provides a 300% deduction for qualifying R&D expenditure. In order to maintain an attractive fiscal regime for R&D in Singapore, qualifying R&D expenditure should be allowed at least 200% tax deduction.

4. Transparency in tax administration

Certainty and transparency in the administration of tax treatment will help to promote investor confidence. While we appreciate that the Inland Revenue Authority of Singapore (IRAS) has made laudable efforts to increase transparency in its tax administration, to better inform the public of tax treatment accorded to such transactions, the following measures could be considered:

- The technical merits (i.e. novelty, technical risk) of the claim could be evaluated by the relevant economic agencies which in many cases are already responsible for awarding grants in the same subject/ field of study.

- While it is helpful that an independent panel has been set up to evaluate R&D claims, given the inherent technical nature of the subject matter, taxpayers should be allowed to meet the panel to clarify or explain the technical aspects of its case to the panel.

1 IP Rights Promote Innovation and Prosperity, Lorenzo Montanari – https://www.forbes.com/sites/lorenzomontanari/2017/04/26/ip-rights-promote-innovation-and-prosperity/#2943391c6514, value is increasingly driven by intellectual property

Encourage enterprise and innovation

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Encourage enterprise and innovation

5. Angel Investors Tax Deduction scheme

Access to funds is crucial for start-ups. Many start-ups are eligible for the early stage financing and co-investing programme which the government has implemented. However, to boost the growth of start-ups particularly in the technology industry, the government can consider liberalising the Angel Investors Tax Deduction (AITD) scheme to make it easier for individual investors to qualify. A suggestion could be to waive the eligibility conditions and approval requirements for an angel investor under the AITD scheme for certain classes of wealthy individuals e.g. Accredited Investors as defined in the Securities and Futures Act. In addition, the scheme should be extended to companies and venture capital funds that provide financing to help the qualifying start-ups in such industries and help them to commercialise their product. This will also help in the marketing of Singapore as a global venture hub on the international stage.

On a related note, more needs to be done to build the talent pool. As such, employment rules for work visas could be eased for certain employers in the venture fund and technology start-up space.

6. Liberalise requirements for carry back of losses

The cap on the amount of unutilised loss items a company is allowed to carry back should be removed altogether and companies should be allowed to carry back losses to any year of assessment that has not been time-barred. This is of particular relevance to insurers with exposure to natural catastrophe risks as they typically find themselves in cycles of profitable years and when a significant disaster occurs, in significant loss positions. The current carry-back loss relief system is grossly inadequate in view of the cyclical nature of writing natural catastrophe risks. The offshore and marine sector is also facing a downturn which is expected to last several years. The ability to carry back losses would also provide some relief to these companies.

In addition, the Income Tax (Amendment) Act 2017 introduced a new section 34AA to provide for the tax treatment of financial instruments when Financial Reporting Standard 109 – Financial Instruments (FRS 109) replaces FRS 39 – Financial Instruments: Recognition & Measurement. Unlike in the case of FRS 39, taxpayers are not given a choice to opt out of FRS 109 tax treatment; the ability to carry back losses could help to mitigate the tax impact of the transition from the realisation basis of taxation to FRS 109 tax treatment.

The ability to apply losses to offset unrealised gains is of particular relevance today, given the increase in volatility of business cycles.

7. Liberalise requirements for carry forward of losses

It is not uncommon for start-up companies to bring in new investors at different stages of their development. This may result in a change in shareholders and possible forfeiture of the unutilised losses. Whilst it is possible to seek a waiver of the continuity of shareholders test from the IRAS, losses preserved by such an avenue are subject to the same trade test. Although genuine investors typically should not be deterred by the potential inability (or otherwise) of the company to utilise past losses, these rules could deter companies from venturing into new fields and seeking investors.

The same business test and continuity of shareholdings test were introduced as anti-abuse measures; however, they inhibit change and innovation and may be removed as the general anti-avoidance rules are sufficient to clamp down the trading of loss-making companies.

8. Tax concessions to help companies "go digital" that are tied to growth

There are hefty costs involved for a company to move into a digital environment. With the impending expiry of the PIC scheme, companies including start-up enterprises that have yet to benefit from the scheme will incur expenditure that span from the hardware infrastructure to labour costs of digitising data, information migration and staff training. In this regard, targeted reliefs (e.g. enhanced deductions or capital allowances) would help:

- certain SMEs or certain sectors lagging in investments in automation to alleviate the investment cost of "going digital" and;
- encourage businesses to digitise their data and modernise their processes, e.g. relief for expenditure such as the gathering, analysis and utilisation of big data would encourage the adoption and use of data analytics.

To safeguard revenue, the scheme can be tied to actual growth of the claimant; for example, companies which have invested in digital technology and are able to demonstrate revenue growth for the year could be given enhanced allowances/ deductions.

9. Liberalise deductions for borrowing costs

In today's uncertain economic climate, businesses may take up standby credit and similar facilities to better manage financing costs and cash flow in order to ensure they can sustain business operations. The upfront cost of securing these standby facilities could be viewed as capital in nature and hence not deductible. As such, the list of prescribed borrowing cost should be expanded to cover such borrowing costs regardless of whether the facilities are drawn down.

10. Double deduction for internationalisation

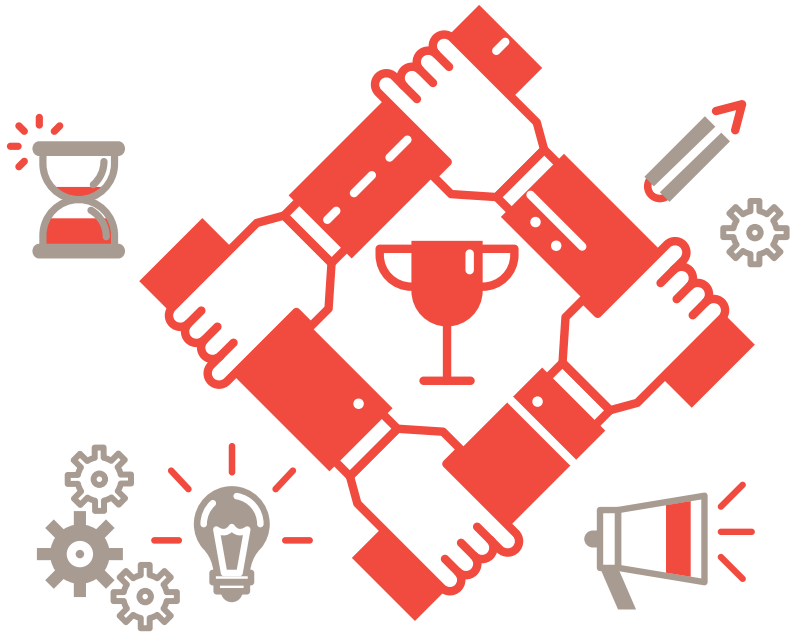
Section 14KA(1)(a) of the ITA requires that salary expenditure for its employees posted to an overseas establishment be incurred by the Singapore firm or company. We suggest tweaking this scheme so that more companies may benefit from it.

We understand that the objective of this incentive scheme is to provide support to businesses looking to expand overseas through deploying their Singaporean employees abroad. These overseas postings are usually done by way of secondment to the overseas establishment, in order to avoid creating an overseas permanent establishment exposure for the Singapore firm or company. There are also immigration, personal tax and other considerations which warrant a secondment arrangement.

This means that, for the duration of the overseas posting, the employee will cease to be on the payroll of the Singapore firm or company; hence salary expenditure incurred for that individual would not qualify for the incentive. Instead of requiring that the salary expenditure be incurred for the Singapore firm's or company's employee, the criterion to be met should be that the individual must be an employee of the firm or company prior to the secondment. Alternatively, a bond requiring the individual to return to work for the Singapore firm or company could be implemented.

As mentioned, as part of the secondment arrangement, the employee's salary would typically be borne (wholly or partially) by the overseas establishment, although the Singapore firm or company may assist in processing the payment. It should be clarified if the double deduction is available in the following scenarios:

- where the employee's salary expenditure which is borne by the overseas establishment (which may or may not claim a deduction for the expenditure) and recharged to the Singapore firm or company with a mark-up under transfer pricing rules.



- where the overseas establishment does not charge a service fee, but is taxed on a deemed service fee (i.e. a mark-up on the salary expenditure) under domestic tax rules.

As the salary cost is no longer borne by the Singapore firm or company, double deduction should be accorded to cost incurred in relation to the secondment that is borne by it. Section 14KA(18) defines "salary expenditure" to be any expenditure comprising wages and salary for the employee, but excluding any bonus, commission, gratuity, leave pay, perquisite, allowance, or any other prescribed payment (whether in cash or kind). The cost qualifying for double deduction should be expanded to cover secondment related costs borne by the Singapore firm or company e.g. relocation allowance or tax equalisation.

Lastly, section 14KA uses the term "country outside Singapore". The expression "territory outside Singapore" should be adopted instead of "country outside Singapore" wherever the latter is used in section 14KA, to be consistent with section 50A.

11. Double deduction for overseas investment development expenditure

Automatic double deduction is available for the first $100,000 of eligible expenses incurred by a Singapore company for the following activities:

- Overseas business development trips and missions
- Overseas investment study trips and missions
- Overseas trade fairs
- Approved local trade fairs

Expenditure in excess of $100,000 is subject to approval.

For Singapore companies trying to expand in the region, the $100,000 threshold is easily exceeded if frequent travel is needed, even though the cost of individual trips is typically low. In order to reduce the administrative burden of seeking approval for numerous low-value trips, the government could consider introducing a threshold of, say, $2,000 per trip below which automatic deduction may be granted. Alternatively, the threshold of $100,000 could be increased.

12. Training costs

Singapore businesses should be incentivised to train and upskill their existing employees. As the PIC scheme expires after the Year of Assessment 2018, the government could consider granting a double deduction for training costs.

Tax regime rationalisation

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Tax regime rationalisation

13. Financial Reporting Standard 115 – Revenue from Contracts with Customers

The Income Tax (Amendment) Act 2017 introduced a new section 34I to allow adjustments to be made to the amount of statutory or exempt income of a person for the year of assessment of the basis period in which FRS 115 is first applied. In the event that the person's income is subject to different tax treatments, the amount to be adjusted against the respective income streams should be determined in accordance with formula set out in sections 34I(3)(b) and 34I(5)(b).

While this will ease the administrative burden of taxpayers of needing to revise the prior years' tax computations to re-compute the tax payable for each year of assessment, it may not be equitable for some taxpayers when the adoption of FRS 115 only result in changes in exempt income or income subject to concessionary tax rates.

For example, a company with pioneer incentive may also derive income subject to the corporate tax rate of 17%. Assuming that with the adoption of FRS 115, this company is required to record an increase in revenue by adjusting the retained earnings and the increase is solely due to the contracts qualifying for pioneer incentive. In accordance with the section 34I(3)(b), the company is then required to allocate the difference against the respective income streams using the formula prescribed. This would result in its paying additional taxes on the amount allocated to the normal tax category notwithstanding that the increase solely relates to pioneer trade (which would have qualified for tax exemption).

For such cases, we suggest that an avenue be provided for taxpayers to approach IRAS on a case-by-case basis to agree on the tax treatment of revenue.

14. Financial Reporting Standard 109 – Financial Instruments

The Income Tax (Amendment) Act 2017 also introduced a new section 34AA to provide for the tax treatment of financial instruments when FRS 109 replaces FRS 39 – Financial Instruments: Recognition & Measurement.

Gains and losses on transactions undertaken to hedge capital risk will be disregarded. This broadly mirrors the equivalent provision in section 34A and the position in common law. However, it has now been held in Singapore courts that deductions under section 14(1)(a) may be allowed even when they are capital in nature: *BFC v CIT* [2014] SGCA 39. As such, there could be mismatch in tax treatment if gains and losses from the corresponding hedging instrument are disregarded (as required by section 34AA(3)(f)). At the very least, this treatment appears inconsistent with section 14(1)(a) which has been held by the courts to accord deduction for prescribed cost of borrowing taken for capital purposes. Further, gains and losses from hedging instruments not listed in the prescribed borrowing cost regulations will not be taxable and deductible respectively, when the interest expenses to which they correspond are deductible under section 14(1)(a).

We suggest that the legislation be updated to accord symmetry in tax treatment, such that gains and losses from hedges of a capital nature should be similarly assessed and deductible if the corresponding losses and gains from the underlying transaction are deductible and assessable.

15. Work from home

As telecommuting and home offices become increasingly common, employees who work from home should be given some personal tax relief as their residence and resources are partially used for employment purposes. The government could consider introducing home office relief, which can be given as a percentage of expenses incurred or at a per-day rate.

Another option is to allow deductions for work-related expenses such as business telephone calls, additional utilities, etc., like in the UK or in the US. In Malaysia, personal tax reliefs are available for the purchase of computers and broadband subscription fees, subject to a cap.

16. Foreign tax credit

In certain prescribed scenarios, such as where an operating company is held by an intermediate holding company in another country, foreign dividends received in Singapore may be exempted under section 13(12) of the ITA if they were paid out of income that had been subject to tax at the operating company level, notwithstanding that no further tax is paid by the intermediate holding company. For parity of treatment and to encourage the repatriation of foreign income, foreign tax credit should similarly be allowed for tax at lower (operating company) levels where dividends flow to Singapore via a chain of companies.

Goods and services tax

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Goods and services tax

17. Registration

Pursuant to the First Schedule to the Goods and Services Tax Act (GST Act), a person will not have a GST registration liability under paragraph 1(1)(a) if the Comptroller is satisfied that his taxable supplies in the next four quarters will not exceed $1 million.

There are situations where a company may, through a significant contract win, make supplies in one year that exceed $1 million but thereafter, it may not make further taxable supplies or make supplies that do not exceed $1 million. The company will be liable to register for GST under paragraph 1(1)(b) (instead of paragraph 1(1)(a)), which states, "…if there are reasonable grounds for believing that the total value of his taxable supplies… will exceed $1 million".

Had the company been liable for registration under paragraph 1(1)(a), it will not have to register for GST pursuant to paragraph 1(3). However, as it is liable for GST registration under paragraph 1(1)(b), technically, it would have to register for GST first and then apply to be de-registered from GST thereafter.

We would recommend changing the rules so that a person that is liable for GST registration under section 1(1)(b) of the First Schedule to the GST Act should be given an option not to register if he believes that the supplies that exceed $1 million is a one-off event that will not be repeated in the subsequent 12 months.

18. Simplified tax invoice for GST

While the IRAS has administratively allowed GST on entertainment expenses relating to food and drinks to be claimed based on a simplified tax invoice regardless of the value, to take into account the inflation factor since this rule was introduced, our recommendation is to increase the dollar value from $1,000 to $2,500 to allow more transactions to come within the requirement for a simplified tax invoice to be issued.

19. Extending GST concession to non-share trades on overseas exchanges

When a broker buys or sells shares on an overseas exchange on behalf of its client, it incurs transaction charges such as brokerage fees charged by the overseas broker and overseas clearing fees, and the broker will recover the charges from its client. Applying the normal GST rules, the broker would be required to charge 7% GST on the recovery of the overseas charges from Singapore clients, which meant potential increased GST costs to the clients as well as additional GST reporting requirements for the brokers. As such, an administrative concession was granted via a remission in 1996 following industry feedback.

To summarise, the concession allows the GST-registered broker to treat the recovery of the overseas transaction charges on share trades on overseas exchanges as outside the scope of Singapore GST (subject to conditions). The broker is not required to charge GST on the amounts recovered from its client on the basis that the broker is treated as an agent in receiving the relevant services from the overseas service providers. Apart from brokers, the concession is also applicable to banks and fund managers when they trade on behalf of their clients.

The concession presently applies only to share trades (i.e. equity securities). As there are also other securities such as debt securities and derivatives that are traded on overseas exchanges, we recommend that the concession be extended to the recovery of transaction charges relating to other securities traded on overseas exchanges.

We recommend the concession be extended to the recovery of transaction charges relating to other securities traded on overseas exchanges by an amendment to the GST legislation to be treated as neither a supply of goods or services.

20. Allow GST to be recovered on the acquisition of shares

The issue is that the IRAS treats the GST incurred on expenses that are in connection with the acquisition of shares as directly attributable to a future exempt sale of shares and the GST is hence not recoverable as input tax.

In the case of a merger or acquisition deal, the GST incurred on the professional fees will be substantial if local advisors are used for the deal. Based on the current rules, such GST will be irrecoverable unless the business is certain and able to substantiate that the shares will be sold to a person belonging outside Singapore or via an overseas exchange.

We are of the view that it is technically more correct to treat the GST incurred on expenses that are in connection with the acquisition of shares as residual input tax instead of directly attributable to an exempt sale of shares. This is because the actual supply has not happened yet and hence, the supply can be either a zero-rated or exempt supply.

Moreover, the allowance for the recovery of the GST will be in line with the government's initiative to promote the expansion of Singapore enterprises (including through merger or acquisition activities) and help reduce the GST costs of local businesses.

We would recommend treating the GST incurred on expenses that are in connection with the acquisition of shares as residual input tax instead of directly attributable to an exempt sale of shares.

Individual tax

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Individual tax

21. Align taxation of gains from employee share plans with global norms to avoid double taxation

Most countries' tax authorities follow the guidance of the Organisation for Economic Co-operation and Development (OECD) on sourcing of share-based reward in cross-border situations, i.e. that stock options (and other stock-related awards) should be sourced based on the number of days an individual has spent working in each country during the vesting period.

However, Singapore does not follow the global norm in this respect. Singapore tax legislation currently defines the source of an employee's rights to acquire shares based on whether the right or benefit to acquire shares is granted in respect of employment exercised in Singapore. Shares granted to an individual whilst working in Singapore which vest after he has been transferred to an overseas entity will still be considered fully taxable in Singapore, either under sections 10(6) or 10(7) of the ITA. We would suggest aligning Singapore's basis of taxation with the OECD Model Tax Convention's recommended approach, in order to avoid double taxation.

22. Increase in medical costs and encouraging saving for old age

Individuals should be encouraged to save for their future retirement and medical expenses.

We suggest introducing relief for medical insurance to encourage taxpayers to take up medical insurance policies to supplement their Medishield coverage.

In addition, CPF and life insurance premium relief should be de-linked to encourage individuals to take up life insurance policies.

Taxpayers should also be encouraged to take preventive measures. We suggest allowing a tax relief for relevant expenses such as gym membership fees to encourage more active lifestyles, health screening fees, etc.

23. Promote filial piety and a caring society

Presently, reimbursement of medical and dental care provided to the employee, the employee's spouse and children are not treated as taxable benefits. This should be extended to medical and dental care provided to the employee's parents and parents-in-law.

We also suggest that foreign maid levy relief should be extended to taxpayers who employ foreign maids to care for their elderly parents or parents-in-law. This will help to alleviate the cost for individuals who take care of their parents/parents-in-law.

24. Encourage married women to stay in workforce

To encourage married women to continue to stay in the workforce, we suggest removing Working Mother's Child Relief from the $80,000 cap on personal income tax reliefs.

25. Help the middle-income group

To help reduce the tax burden of the middle-income group, the progressive personal tax rates should be reviewed. We suggest removing the lowest two personal tax rate bands and increasing the income threshold to $40,000.

International tax developments and their impact on Singapore

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International tax developments and their impact on Singapore

26. Harmonise tax treatment within ASEAN

Although this is not a Budget matter, we have included this suggestion for completeness. To promote greater cross-border flow of capital and labour, Singapore, as chair of ASEAN next year, should consider proposing measures to harmonise certain tax treatment within ASEAN. This will help Singapore businesses go international and expand their footprint in neighbouring countries.

For example, harmonising the withholding tax treatment of different income streams so that taxpayers are not subject to double taxation (e.g. to adopt a consistent definition for characterising software payments, as royalties or service fees).

Appendix A

Asset management

1. **Lower qualifying threshold for venture capital funds**

   Currently, venture capital (VC) funds face the following challenges when considering whether to apply for fund tax incentives and therefore rarely do pooling in Singapore:

   - The $50 million fund size requirement for the 13X fund tax incentive is too high as VC funds tend to invest in smaller investees and are usually not able to meet the $50 million requirement.

   - Generally, section 13H is given to funds that focus more on Singapore. Therefore, it is restricted (compared to sections 13CA/13R/13X).

   We propose a lower section 13X threshold for fund size for VC funds to $10 million. This is on the basis that any revenue leakage should be proportionately less.

2. **Expansion of the list of designated investments**

   Purchasing of trade receivables is becoming a popular asset class for funds given the growing demand in trade finance.

   For example, buying trade receivables from a supplier in respect of its customers (buyers) provides early cash flow to the supplier. Large buyers with strong negotiating power often request longer payment terms from their suppliers, ranging from 30 days to 180 days. This creates a substantial working capital requirement for the supplier.

   Though the largest providers of working capital financing are banks, certain trade finance requests from SMEs cannot be catered to by banks due to high administrative costs and given the amounts requested by the SMEs are relatively small. The financing gap is now being fulfilled by funds.

   In addition, given the growing acceptance of cryptocurrencies in today's digital age, fund portfolios may also include cryptocurrencies.

   Given that Singapore is positioning itself as the asset management hub in Asia, it is important to add trade receivables and cryptocurrencies to the list of designated investments to attract funds with different strategies to be based in Singapore.

   We suggest to expand the list of designated investments to include trade receivables and qualifying cryptocurrencies (i.e. major cryptocurrencies in circulation).

3. **Designated investments should not be tied to legal forms**

   Currently, unit trusts and private trusts can only be considered designated investments if they invest wholly in designated investments. This requirement imposed on unit trusts and private trusts results in some practical challenges:

   - It requires a significant amount of resource and time to trace depending on the fund structure (e.g. if the investor fund is a fund of funds which invests in say 20 unit trust funds, work has to be undertaken to review the income/investments of those 20 unit-trust funds and if the unit trust funds invest in other unit trust funds, the tracing goes on).

   - Information is not available to the investor fund and public information may not provide sufficient details for the tracing.

   - The investee unit trust fund may have an insignificant amount of investments which may not qualify as designated investments and the whole investment will become non-qualifying.

   Qualifying funds may invest in unit trusts that are managed by external fund managers. The underlying investments of these unit trusts are not within the control of the Singapore fund manager who may not be able to obtain confirmation from the external fund managers that the unit trusts invest wholly in designated investments.

   We suggest that unit trusts and private trusts be considered designated investments as long as these vehicles are either listed, a foreign collective investment scheme or do not invest directly in Singapore immovable properties.

4. **Designated investments should not be tied to legal forms**

   The current scope of designated investments is tied to legal forms which results in disparate tax outcomes simply due to the different legal forms of the business. An example of the scope of designated investments being tied to legal form is where loans may be granted only to offshore companies and trusts (items k and v of Part A of the Third Schedule of the Income Tax (Exemption of Income of Prescribed Persons Arising from Funds Managed by Fund Manager in Singapore) Regulations 2010).

   We suggest that the scope of designated investments should not be tied to legal form of the business. There is a sound basis for this since the rules seem to force the taxpayers to structure investments in a certain way and compromise on legal and commercial pressures. From a policy standpoint there is no disadvantage to Singapore if the link to the legal form is removed. In fact it helps reduce compliance cost and burden.

4. **Specified income – Interest from debt securities**

Under section 12(6), interest is deemed to be sourced in Singapore if, among other things, the funds are used here. In practice, there are cases where there is no mechanism to collect the tax.

In particular, section 12(6)(b), if interpreted too widely, may cause unintended tax consequences for funds with the 13CA, 13R and 13X status:

- Where the proceeds (or part of the proceeds) are used by an overseas issuer or its affiliates to make purchases from Singapore vendors.

- The debt issuance may be arranged by a Singapore financial institution such that although the proceeds are not used in Singapore, they may be temporarily transferred into a Singapore bank account.

Arguably, in these circumstances the funds are brought into or used in Singapore although their nexus with Singapore is at best tenuous and there is no revenue leakage.

Bonds / multi-asset funds typically make portfolio investments in a huge portfolio of debt instruments. Such funds find it difficult to ascertain whether the interest would be caught within section 12(6) of the ITA.

Firstly, as a portfolio investor, they are not able to obtain any representation or confirmation from the issuer on whether the payment falls under the ambit of section 12(6) of the ITA.

Secondly, even if the funds seek to perform their own due diligence, in some instances, they have found that the bond prospectus is not available.

Thirdly, carrying out the due diligence by reviewing each bond prospectus is neither commercially feasible nor efficient, taking into account the huge volume of trades entered into.

Lastly, such due diligence and analysis may not yield conclusive results for the purpose of the tax exemption scheme. Most prospectuses only indicate a broad purpose for the issuance (e.g. for general corporate purposes) which may not be indicative of whether 12(6) is triggered.

As such, the section 12(6) exclusion from specified income results in increased compliance costs for bonds / multi-assets funds which are typically portfolio investors.

We suggest that the government consider adopting any one of the following measures:

- To carve 12(6)(b) out of the exclusion to the specified income list.

- Interest from foreign issuers without Singapore permanent establishment should be deleted from the exclusion to specified income list, as there is no interest deduction taken in Singapore.

- Including the following within the scope of specified income: "(b)(vii) interest and other payments from debt securities which are

  (i) listed on any exchange; or

  (ii) issued by issuers which are incorporated or constituted under the laws of a jurisdiction other than Singapore and the investment in the debt security is not made in connection with an arrangement referred to in section 33(1) of the Act".

Making the above proposed amendments would achieve the following objectives:

- reduce tax compliance burden on taxpayers and simplify tax administration for the IRAS; and

- promote the fund industry.

5. **Persons liable for penalty under section 13CA and section 13R of the ITA**

Firstly, there may be co-investors in some fund structures and hence it is not always possible for a section 13R approved company to have 100% ownership in an approved company / prescribed person.

The risk of tax leakage is low for the following reasons:

- Where an approved company (AC1) invests in a prescribed person or an approved company (AC2), income derived by AC1 from this investment will be exempt from Singapore tax, to the extent that the income is specified income from designated investments (e.g. dividends). Any non-specified income will be subject to tax in Singapore as AC1 is required to file annual Singapore tax returns.

- Any financial penalty will be applied to the relevant owners of AC1, where applicable.

Consider removing financial penalty on an approved company (AC1 in this example) with less than 100% ownership in an approved company / prescribed person.

Secondly, statutory boards may invest in approved companies and prescribed persons. While statutory boards are exempt from paying tax on income, they will be subject to a financial penalty if the ownership threshold is breached. Consider excluding statutory boards from being liable to the financial penalty.

Banking and capital markets

1. **Income Tax (Deductible Borrowing Costs) Regulations 2008**

   There have been several high profile cases of bond defaults. In order to encourage issuer to buy insurance against default (so as to in turn protect the investors), it will be useful to consider granting deduction for such bond default insurance premiums.

   We propose that premiums for insuring against bond default be added to the list of prescribed deductible borrowing costs.

2. **Financial Sector Incentive – Derivatives Market (FSI-DM) scheme**

   Certain FSI-DM award holders (e.g. proprietary traders) are not covered under the broad-based withholding tax exemption for payments made by banks, finance companies and certain approved entities.

   We suggest that the broad-based withholding tax exemption be enhanced to cover more payer entities (e.g. proprietary traders).

3. **Withholding tax exemption for specified payment made under a securities lending or repurchase agreement by specified institution**

   Under the Income Tax (Exemption of Interest and Other Payments for Economic and Technological Development) (No. 3) Notification 2003, paragraph 3(4)(b), the exemption for interest payments only applies where cash collateral is placed in banks in Singapore.

   The scheme should be retained as the coverage is broader than the broad-based withholding tax exemption under section 45I. To provide greater flexibility in managing cash, we suggest to remove the requirement for cash collateral to be placed with banks in Singapore.

4. **Withholding tax exemption for section 12(6) payments on inter-bank / inter-branch transactions under section 92(2) remission granted on 2 January 1996**

   We suggest that the remission be retained as it is instrumental in developing Singapore as an international financial centre.

   That said, the scheme can be terminated if the broad-based withholding tax exemption mentioned in point (2) is made permanent.

5. **Tax Incentive Scheme for Approved Special Purpose Vehicle (ASPV) engaged in securitisation transactions (ASPV Scheme) – expiring in 2018**

   Singapore is not as competitive as other countries such as Luxembourg and Ireland which allow for the concessionary tax treatment to apply automatically once prescribed conditions are met. This is unlike Singapore, where specific approval is needed.

   We propose to:

   - Extend the ASPV scheme; and
   - Grant automatic approval for ASPV scheme based on a fixed set of conditions.

6. **Qualifying Debt Securities scheme**

   Currently, only certain types of income are covered by the Qualifying Debt Securities (QDS) regime. Although the law provides an avenue for the authorities to expand the scope upon request, in practice this may not be practical given the tight timeline for debt issues. We suggest broadening the scope to provide greater flexibility in debt structuring of QDS qualifying income.

   We suggest to include all prescribed borrowing costs (other than items 1, 2, 8 and 9 which relate to hedging costs) specified in the Schedule in the Income Tax (Deductible Borrowing Costs) Regulations 2008 as qualifying income for the QDS regime.