

Extension and Refinement of the Financial Sector Incentive Scheme

July 2023

In brief

It was first announced during the Singapore Budget 2023 on 14 February 2023 that the Financial Sector Incentive (“FSI”) scheme will be extended till 31 December 2028 and that the concessionary tax rates for certain awards approved on or after 1 January 2024 under the FSI scheme will be streamlined.

Further to the above announcement, the Monetary Authority of Singapore (“MAS”) has issued a circular (FDD Cir 09/2023) on 21 June 2023 providing further details on the extension and refinement of the FSI scheme. Broadly, the circular covers the following:

- Extending the FSI scheme
- Streamlining the concessionary tax rates, refining and simplifying the requirements for certain FSI awards
- Enhancing, refining and clarifying the scope of certain FSI qualifying activities

The salient points of the MAS circular are detailed below.

In detail

The FSI scheme was first introduced in Budget 2002 as an umbrella scheme with a view to streamline the various then existing tax concessions for the financial sector, as well as to encourage high value-added financial activities in Singapore. Over the years, there have been several refinements to the FSI scheme to ensure it continues to remain competitive and relevant. The FSI scheme now comprises the following seven sub-schemes (classified into ‘enhanced-tier’ and ‘standard-tier’) which supports a wide range of financial sector activities:

Enhanced-tier awards:

- (i) FSI-Credit Facilities Syndication (“FSI-CFS”)
- (ii) FSI-Capital Market (“FSI-CM”)
- (iii) FSI-Derivatives Market (“FSI-DM”)

Standard-tier awards:

- (iv) FSI-Standard Tier ("FSI-ST")
- (v) FSI-Trustee Companies ("FSI-TC")
- (vi) FSI-Headquarter Services ("FSI-HQ")
- (vii) FSI-Fund Management ("FSI-FM")

Extending the FSI scheme and streamlining of concessionary rates

The FSI scheme, including the withholding tax exemption¹ granted for interest payments on qualifying loans made by an FSI-HQ company to qualifying non-residents during its FSI-HQ award tenure, will be extended for a further period of five years till 31 December 2028.

For new and renewal awards approved on or after 1 January 2024, the following revised concessionary tax rates and requirements will apply. Existing award holders will continue with the existing concessionary tax rate, till the expiry of their current awards.

FSI scheme	Concessionary Tax Rate	
	Existing	Revised
FSI-CFS (Note 1)	5%	10%
FSI-CM	5%	10%
FSI-DM	5%	10%
FSI-ST	13.5% (no change)	
FSI-TC	12%	13.5%
FSI-HQ (Note 2)	10% (no change)	
FSI-FM	10% (no change)	

Note 1:

To streamline the administration of FSI-CFS, the requirement to submit a return on the facility and declaration form by the Singapore arrangers to the Inland Revenue Authority of Singapore is removed. The MAS will release a simplified version of the return on the facility and declaration form by Singapore arranger(s) separately. This change will apply on or after the date the amended Income Tax (Concessionary Rate of Tax for Financial Sector Incentive Companies) Regulations 2017 are published in the *Gazette*.

Note 2:

With the focus on business spending and headcount to reflect the economic substance of FSI-HQ company's activities in Singapore, the qualifying criteria relating to "number of network companies" and "number of HQ services" have been removed for new and renewal of FSI-HQ awards approved on or after 1 January 2024.

¹ Refer to Income Tax (Exemption of Interest and Other Payments for Economic and Technological Development) (No. 6) Notification 2009 (G.N. No. S 574/2009)

Enhancing, refining and clarifying the scope of certain FSI qualifying activities

The scope of FSI qualifying activities have also been enhanced and refined (see below).

FSI scheme	Current qualifying activity	Enhanced / refined qualifying activity
Enhancement / refinement for income derived on or after 15 February 2023:		
FSI-DM	Income derived from trading in, or providing services as an intermediary in connection with transactions relating to financial derivatives, commodity derivatives, emission derivatives or freight derivatives.	Expanded to include income derived from trading in, or providing services as an intermediary in connection with transactions relating to all carbon derivatives . ²
FSI-CM FSI-ST	<p><u>Structured notes³ (being financial assets of an FSI company)</u> Treated as income derived from “trading or investing in, or providing services in respect of debt securities” under FSI-CM or FSI-ST.</p> <p><u>Structured notes (being financial liabilities of an FSI company)</u> (a) Bifurcated⁴ – the mark-to-market (“MTM”) gains/losses relating to the derivative components treated as income derived from “trading in derivatives” (if the derivative component relates to financial, commodities, emission or freight derivatives) under FSI-DM or FSI-ST, where applicable.</p> <p>(b) Non-bifurcated – none</p>	Expanded such that all MTM gains/losses recognised in income statement and income from activities (e.g. issuing, trading or investing in, or providing services) relating to structured notes , regardless whether they are financial assets or financial liabilities (whether bifurcated or not) of the FSI company, will qualify under FSI-CM, FSI-DM ⁵ or FSI-ST, where applicable.
FSI-CM FSI-ST	None	<p>(a) Income derived from providing services (including advisory services and services as a broker, nominee or custodian) in relation to an equity interest⁶ in a limited partnership (“LP”).</p> <p>(b) Income derived from trading in an equity interest in a qualifying LP.⁷ A qualifying LP excludes a LP that is – (i) in the business of trading or holding immovable properties (other than immovable</p>

² “Carbon derivatives” include one where the underlying is carbon offset or carbon allowance

³ Refer to the definition of “structured product” in section 13(16) of the Income Tax Act 1947 (“ITA”) for the definition of “structured notes”

⁴ For financial accounting purposes.

⁵ There is no change to the scope of FSI-DM, where the derivative component of a bifurcated structured note will continue to be treated as income from trading in derivatives.

⁶ “Equity interest” refers to a partner’s ownership interest in the LP

⁷ Income derived from trading in equity interests in qualifying LP includes:

- (a) Any realised amount of gains or losses arising from the disposal of the FSI company’s equity interests in the LP; and
- (b) Any unrealised amount of MTM gains or losses arising from the valuation or revaluation of the FSI company’s equity interest in the LP,

but exclude any income of the LP to which the FSI company is entitled as a limited partner of the LP.

FSI scheme	Current qualifying activity	Enhanced / refined qualifying activity
		<p>properties that are prescribed assets or projects⁸;</p> <p>(ii) not in the business of property development; and</p> <p>(iii) not listed on a stock exchange in Singapore or elsewhere.</p>
FSI-ST	Foreign exchange transactions	Expanded to include income derived from providing services (e.g. sales and distribution) relating to foreign exchange transactions.
FSI-ST	None	<p>Income derived from trading (i.e. spot trading) in carbon credits, including the following:</p> <p>(a) permits to emit carbon dioxide or other greenhouse gases into the atmosphere; or</p> <p>(b) permits to reduce / remove emissions of carbon dioxide or other greenhouse gases.</p>

⁸ Prescribed in regulation 5 of the Income Tax (Qualifying Project Debt Securities) Regulations 2008 (G.N. No. S 315/2008)

FSI scheme	Current qualifying activity	Enhanced / refined qualifying activity
Enhancement / refinement for income derived on or after 1 January 2024:		
FSI-CM FSI-ST	Trading or investing in, or providing services (including services as a broker, nominee or custodian, and the grant of a loan of the securities under a securities lending or repurchase arrangement) in respect of debt securities.	<ul style="list-style-type: none"> Trading or investing in: <ul style="list-style-type: none"> (a) qualifying debt securities⁹ (“QDS”) and (b) other debt securities, excluding any non-QDS that are issued by a company, a collective investment scheme or a business trust that is – <ul style="list-style-type: none"> (i) in the business of trading or holding immovable properties (other than immovable properties that are prescribed assets or projects); (ii) not in the business of property development; and (iii) not listed on a stock exchange in Singapore or elsewhere. Providing services (including services as a broker, nominee or custodian, and the grant of a loan of the securities under a securities lending or repurchase arrangement) in respect of debt securities.
FSI-CM FSI-ST	Trading or investing in, or providing services (including services as a broker, nominee or custodian, and the grant of a loan of the securities under a securities lending or repurchase arrangement) in respect of stocks, shares, or other equity securities issued by a company, a collective investment scheme or a business trust.	<ul style="list-style-type: none"> Trading or investing in stocks, shares, or other equity securities issued by a company, a collective investment scheme or a business trust, excluding any stocks, shares, or other equity securities issued by a company, a collective investment scheme or a business trust that is – <ul style="list-style-type: none"> (i) in the business of trading or holding immovable properties (other than immovable properties that are prescribed assets or projects); (ii) not in the business of property development; <u>and</u> (iii) not listed on a stock exchange in Singapore or elsewhere. Providing services (including services as a broker, nominee or custodian, and the grant of a loan of the securities under a securities lending or repurchase arrangement) in respect of stocks, shares, or other equity

⁹ Refer to section 13(16) of the ITA for the definition of “qualifying debt securities”

FSI scheme	Current qualifying activity	Enhanced / refined qualifying activity
		securities issued by a company, a collective investment scheme or a business trust.
FSI-ST	Trading on or after 1 January 2019, in loans and their related collaterals (excluding immovable property other than immovable property that is or is used for any prescribed asset or project).	<ul style="list-style-type: none"> Trading in all secured and unsecured loans, where the loans are transacted with a body of persons, trust, company or firm. This is regardless of whether the collaterals of secured loans are immovable properties. Trading in collaterals of secured loans, where the collaterals are not immovable properties (other than an immovable property that is or is used for any prescribed asset or project). <p>Under the refined scope, trading in loans with individuals will no longer be incentivised.</p>

Following queries from the industry on FSI qualifying activities, MAS has clarified the following:

FSI scheme	Current qualifying activity	Clarification
FSI-ST	For a bank or merchant bank, which is an FSI-ST company:	
	- Transacting in loans (other than by way of bonds or debentures) with a body of persons, trust, company or firm.	Includes the granting and origination of loans.
	- Providing services in respect of loans (other than by way of bonds or debentures).	Excludes fee and commission income in relation to credit cards.
	- Transacting in, or providing services relating to, trade transactions or remittances.	Excludes local money transfer services (e.g. NETs, GIRO, local cheques).
FSI-ST	Providing investment advisory services, as well as providing advisory services relating to financial matters (other than investment advisory services in respect of fund management).	Includes research services if the research activities include more than just providing research information and publishing research information. For example, the activities should include meeting clients to provide advice. Mere sharing of the same research information would not be a qualifying activity.

PwC's comments

Staying relevant

The changes to the FSI scheme are an indication of the authorities' continuing efforts to ensure that the incentives remain relevant to the financial services industry¹⁰, while keeping up with changes in the global business and tax environment.

For example, the decision to incentivise carbon credits and carbon derivatives demonstrated the authorities' commitment in advancing the environmental, social and governance ("ESG") agenda by encouraging sustainable investments.

That said, the challenge of this approach is that the list of qualifying activities will need to be updated continually for it to remain relevant with the introduction of innovative ESG financial products, and that the tax regulations may not keep pace with the rate of change in the financial markets. Moreover, there is a risk of the list becoming too prescriptive and hence subject to differences in interpretation, given that the scope of and manner in which financial activities are conducted will evolve.

Increase in tax rate

While the increase in the concessionary tax rates under the enhanced tier awards (i.e. FSI-CFS, FSI, CM, FSI-DM) from 5% to 10% is partly driven by the OECD's Global Anti-Base Erosion Model Rules (Pillar Two) ("GloBE rules")¹¹, we expect it will become less attractive for existing award holders and new market entrants to Singapore given the tax rate differential as compared to FSI-ST is reduced to 3.5%. In this regard, new entrants are likely to weigh the benefit of any tax savings against the additional economic commitments required for the enhanced-tier awards relative to the FSI-ST award.

Classification / treatment in prior years

With the clarifications / updates made to the FSI scheme, existing award holders should review the classification / treatment of such activities in prior years and their implications. Examples include:

- (i) Foreign exchange transactions - the inclusion of services (e.g. sales and distribution) relating to foreign exchange transactions as a qualifying activity may suggest that the current interpretation of "foreign exchange transactions" as a qualifying activity is confined to trading in foreign currencies (i.e. only buying and selling of foreign currencies). In this regard, the Comptroller is likely to scrutinise existing award holders' basis of classifying foreign exchange transactions as a qualifying activity.
- (ii) Structured notes - issuance of structured notes is not new to financial institutions, which may wish to review their current treatment of this item.

Investments in certain property trading / holding companies

The removal of debt and equity investments in certain property trading / holding companies from the list of FSI-CM and FSI-ST activities is in line with the other provisions in the ITA where similar investments were excluded (e.g. section 13W exemption of gains from disposal of ordinary shares). However, FSI-CM and FSI-ST award holders will have to consider how it could identify and distinguish such investments from other qualifying investments.

¹⁰ In 2022, the finance and insurance sector are one of the major contributors to Singapore's economy and GDP growth of 3.7%.

¹¹ Very broadly, the GloBE rules operate to ensure that large multinational enterprises (MNEs) - those with consolidated annual revenues of EUR 750 million or more - pay tax at an effective rate of at least 15% on profits (as defined) earned in countries in which they operate. This is primarily through a top-up tax regime. Singapore has announced via its 2023 Budget Statement that it is planning to introduce the GloBE Rules and a domestic top-up tax for in-scope businesses from financial year beginning on or after 1 January 2025.

Concluding remarks

Even though the above is not yet gazette as law, existing award holders or businesses intending to apply for new awards under the streamlined FSI scheme should analyse and evaluate the implications on its business activities and income classification, both for past years and on a prospective basis.

Given the Comptroller's on-going focus on proper income classification, it is important for relevant stakeholders within the organisation to evaluate whether the current financial systems can be adapted to accommodate the latest changes. Businesses would also need to ensure they have robust internal control procedures to track all incentive qualifying income and direct expenses.

In the meantime, existing award holders and new applicants should factor in the interaction between the concessionary tax rates and the global minimum tax under the GloBE rules, as well as the proposed domestic top-up tax (where applicable), in weighing the merits of the various FSI scheme.



Contact us

If you would like to discuss any of the issues raised, please get in touch with your usual PwC contact or any of the individuals listed below.



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