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Singapore's 2016 Budget: Corporate Tax Implications

The 2016 Budget was delivered by the Minister for Finance Heng Swee Keat on 24 March 2016. This was his first budget as Minister for Finance and it was appropriately themed "Partnering for the Future", in charting Singapore's next phase of development. While there will not be drastic changes to Singapore's economic policy, smaller changes will be introduced to address concerns about a slowing economy, as Singapore embarks on a journey to transform its economy through innovation and enterprise.

The Budget introduces tax benefits targeted primarily at Small and Medium Enterprises ("**SMEs**"), while improving long term growth by encouraging innovation and increasing productivity.

At the heart of the 2016 Budget is a S$4.5 billion Industry Transformation Programme that will be implemented to help businesses and industries create new value and drive growth. The programme features initiatives such as the introduction of a new Automation Support Package, and increased flexibility for businesses to claim writing-down allowance for the acquisition of Intellectual Property Rights ("**IPRs**").

We highlight the key changes below.

1. Key Corporate Tax Changes

A. Changes to Section 19B Writing-Down Allowance

Providing for an Election of Writing Down Period

Currently, under Section 19B of the Income Tax Act ("**ITA**"), writing-down allowances ("**WDA**") are available on capital expenditure incurred to acquire qualifying IPRs. The writing-down period is over 5 years.

Following the 2016 Budget, taxpayers may elect for the WDA to be claimed over a period of 5, 10, or 15 years. The election must be made at the point of submitting the tax return of the Year of Assessment ("**YA**") relating to the basis period in which the qualifying cost is first incurred. Once made, the election is irrevocable.

The change will apply to qualifying IPR acquisitions made within YA 2017 to YA 2020. The Inland Revenue Authority of Singapore ("**IRAS**") will release further details by 30 April 2016.

Comments: This change provides flexibility to businesses in choosing a writing-down period that will allow them to maximize tax benefits from the WDA. A shorter writing-down period may result in the unintended consequence of leaving businesses in an overall loss position. This may have knock-on effects such as creating a pool of unutilised allowances, which may not be carried forward unless the relevant carry-forward rules are satisfied. In addition, an overall loss position may sometimes be disadvantageous if the business would like to claim foreign tax credits due to tax credit limitation rules. Similarly, if a business is currently

enjoying a tax incentive, choosing a longer writing-down period that extends beyond the incentive period may allow the business to maximise the tax benefits granted by Section 19B. As the election is irrevocable, businesses should consider the implications of making the election carefully, particularly for businesses that enjoy tax incentive.

Introducing an Anti-Avoidance Mechanism

An anti-avoidance mechanism for IPR transfers will be introduced. The proposed mechanism will empower the Comptroller of Income Tax to make the following adjustments to the transacted price of the IPR, if the IPR is not transacted at open market value ("**OMV**"):

a) If the acquisition price of the IPR is higher than the OMV of the IPR, the Comptroller may substitute the acquisition price with the OMV of the IPR and restrict the writing-down allowance based on the OMV of the IPR; and

b) If the disposal price of the IPR is lower than the OMV of the IPR, the Comptroller may substitute the disposal price with the OMV of the IPR for the purpose of computing the balancing charge.

This change will apply to acquisitions, sales, transfers or assignments of IPRs that are made from 25 March 2016.

Comments: Currently, to claim WDA, an independent valuation report on the acquired IPR is already required if the acquisition cost of the IPR is equal or more than (a) S$ 0.5 million for related party transaction, and (b) S$ 2 million for unrelated party transaction. The administrative practice adopted by IRAS is to limit the amount that is eligible for WDA to the lower of the actual capital expenditure incurred and the amount stated in the valuation report. This change announced in the 2016 Budget appears to legislate the administrative practice.

We note that there is currently no corresponding mechanism that requires a taxpayer to support the consideration for its disposal, for the purpose of calculating the balancing charge when a taxpayer has previously claimed WDA has disposed of the IPR. The proposed change imposes the requirement on the taxpayer to seek independent valuation to support the disposal value of the IPR and makes clear IRAS's powers, perhaps in addition to IRAS's powers under existing general anti-avoidance provisions in Section 33 of the ITA, in relation to computing the balancing charge and fills this existing gap.

In addition, given the new flexibility introduced with regard to the election of the writing-down period, and the heightened international focus on the Base Erosion Profit Shifting ("**BEPS**") project, the proposed anti-avoidance mechanism is a logical development to guard against the potential abuse of the newly modified Section 19B. It is therefore expected that there will be increased scrutiny from IRAS especially in relation to significant WDA claims. Businesses should therefore ensure that they maintain proper documentary evidence to support both IPR acquisitions and disposals for the purpose of WDA claims.

B. Automation Support Package - Investment Allowance

As part of the initiative to drive productivity and encourage companies to automate, the Government will introduce a new Automation Support Package ("**ASP**"). The new package will be administered by SPRING Singapore.

Part of the ASP includes a 100% investment allowance ("**IA**") on the amount of approved capital expenditure (net of grants) for qualifying projects. The approved capital expenditure is capped at S$10 million per project. The proposed IA is in addition to the existing capital allowance for plant and machinery.

The Ministry of Trade and Industry ("**MTI**") will announce more details at the Committee of Supply.

Comments: Pending the release of further details from the MTI, it remains to be seen the types of projects that will qualify for the IA and how the scheme will interact with existing capital allowances for plant and machinery, as well as the current investment allowances under the *Economic Expansion Incentives (Relief From Income Tax) Act*.

C. Removal of Tax Concession on Home Leave Passages for Expatriate Employee

Currently, home leave passages enjoyed by expatriate employees (up to one passage per year), their spouses (up to one passage per year) and children (up to two passages per child per year), are taxed in the hands of the employees at 20% of their value, instead of the full value of the benefit. This concession will be removed effective from YA 2018.

Comments: With this change, employees who are provided with home leave passage will see a reduction in their take home pay after tax. Employers who bear the tax liability for their employees may also see an increase in costs.

In addition, as cash paid in lieu of home leave passage have been taxed at 100%, removal of the administrative concession for home leave passages also removes the disparity in tax treatment between the two. As such, multinational corporations that provide home leave passages may need to review and modify their existing policies in light of this change.

D. Allocation of Pre-commencement Expenses and Section 14U Expenses

Currently, where pre-commencement expenses are allowed tax deductions under Section 14U and Part V of the ITA[1]. Businesses enjoying tax incentives are not required to allocate the expenses between pre-incentive and incentive income.

Following the 2016 Budget, pre-commencement and Section 14U expenses incurred by businesses enjoying tax incentives will need to be allocated to the pre-incentive and incentive income according to the following allocation method:

a) Section 14U and pre-commencement expenses that are directly incurred to derive the pre-incentive income or incentive income will be specifically identified and set off against the relevant income; and

b) For all remaining Section 14U and pre-commencement expenses, they will be allocated between the pre-incentive and incentive income based on income proportion (e.g. using turnover, gross profit).

This change will take effect for expenses that are incurred from 25 March 2016 onwards. IRAS will release further details of the change by June 2016.

Comments: Currently, IRAS will typically accept taxpayer's allocation of expenses between pre-incentive and incentive income if taxpayer can demonstrate that the allocation is reasonable and consistently applied. It remains to be seen whether the prescriptive method of allocating the balance of Section 14U expenses and pre-commencement expenses based on the income proportion will be a fair representation of how the expenses are actually incurred

[1] Under Sections 14A(3), 14D(2), 14Q(4) and 14S(5). These provisions allow pre-commencement expenses relating to IP registration, R&D, renovation and refurbishment and design to be deemed as incurred on the actual date of commencement and hence tax deductible

and whether IRAS would make exception for certain businesses and industries. Businesses should plan ahead, track and document their expenses carefully in order to justify the allocation adopted.

E. Extension of Finance and Treasury Centre ("**FTC**") Scheme

The FTC scheme was due to expire on 31 March 2016. Following the 2016 budget, the FTC scheme will be extended till 31 March 2021 with the following enhancements:

a) The concessionary tax rate will be lowered to 8%. The substantive requirements to qualify for the scheme will be increased;

b) The FTCs will be allowed to obtain funds indirectly from approved offices and associated companies. Safeguards will be put in place to address round-tripping risks; and

c) Tax exemption under Section 13(4) will be expanded to cover interest payments on deposits placed with the FTC by its non-resident approved offices and associated companies, provided the funds are used for the conduct of qualifying activities or services.

These changes will take effect from 25 March 2016. The Economic Development Board ("**EDB**") will release further details by June 2016.

Comments: The lowering of concessionary tax rate from 10% to 8% and the expansion of the FTC Scheme will bring new opportunities for FTCs in Singapore. These changes should make Singapore more attractive in encouraging multinational corporations to house global treasury activities in Singapore, particularly if these multinational corporations already have substantial business operations in Singapore.

Against the backdrop of the BEPS project, the emphasis on substantive requirements and the introduction of safeguards against round-tripping risks are not unexpected. Pending the release of further details, FTCs that are renewing their applications should assess whether they will be able to meet such enhanced requirements.

2. Expansion and Extension of Schemes

A. Enhancing the Global Trader Programme (Structure Commodity Finance) ("**GTP(SCF)**") Scheme

Currently, an approved GTP(SCF) company is granted a concessionary tax rate of 5% or 10% on income generated from the following qualifying activities:

a) Factoring;

b) Forfeiting;

c) Prepayment;

d) Countertrade;

e) Warehouse receipt financing;

f) Export receivable financing;

g) Project finance;

h) Islamic trade finance;

i) Transacting in derivatives to hedge against risks relating to any of the activities from a) to h); and

j) Advisory services in relation to any of the activities from a) to h).

Following the 2016 Budget, qualifying activities will be expanded to include:

a) consolidation, management and distribution of funds for designated investments;
b) M&A advisory services and
c) streaming financing

This change will take effect from 25 March 2016. International Enterprise ("**IE**") Singapore will release further details of the change by June 2016.

B. Enhancing Mergers and Acquisitions ("**M&A**") Scheme

Under the current M&A Scheme, tax allowance of 25% is granted for up to S$20 million of the purchase consideration paid for qualifying M&A deals per YA, while stamp duty relief is granted for up to S$20 million of the purchase consideration paid for qualifying M&A deals per YA.

Following Budget 2016, the existing cap will be increased from S$20 million to S$40 million such that:

a) Tax allowance of 25% will be granted for up to S$40 million of consideration paid for qualifying M&A deals per YA; and

b) Stamp duty relief will be granted for up to S$40 million of consideration paid for qualifying M&A deals per financial year.

This change will take effect for qualifying M&A deals made from 1 April 2016 to 31 March 2020.

IRAS will release further details of the change by June 2016.

E. Extension of 13Z Exemption

To provide upfront certainty to companies in their corporate restructuring, the tax exemption for companies' gains on qualifying disposals of equity investments under Section 13Z will be extended till 31 May 2022. All conditions of the scheme remain the same.

F. Extension of Double Tax Deduction ("**DTD**") for Internationalisation Scheme

Following the 2016 Budget, the DTD for Internalisation scheme will be extended for another four years from 1 April 2016 to 31 March 2020. The existing automatic DTD on up to S$100,000 qualifying expenses will also be extended to qualifying expenditure incurred during this same period. All other conditions of the scheme remain the same.

IE Singapore will release further details of the change by June 2016.

3. Scheme to be Phased Out

A. Productivity and Innovation ("**PIC**") Scheme Allowed to Lapse

From 1 August 2016 onwards, cash pay-out under the PIC scheme will be reduced from 60% to 40%. The Government has also decided not to extend the PIC scheme beyond YA 2018.

Comments: The end of the PIC scheme, combined with the introduction of the Automation Support package, signals the Singapore Government's move from a broad-based approach to a more targeted approach to encourage innovation and increase productivity. While businesses can no longer rely on cash payouts and tax deductions under the PIC scheme, they can refine their future business plans

to take advantage of the various initiatives under the ASP, pending the release of details of such initiatives.

4. Industry Specific Tax Changes / Others

A. Refining Tax Incentive Schemes for Insurance Companies

The current incentives include:

a) Marine Hull and Liability Insurance: Under the Tax Incentive Scheme for Marine Hull and Liability Insurance, approved insurers are granted tax exemption or a concessionary tax rate of 5% on qualifying income derived from carrying on of marine hull and liability insurance business. The scheme is scheduled to lapse after 31 March 2016.

b) Specialised Insurance Business: Under the Tax Incentive Scheme for Specialised Insurance Business, approved insurers are granted tax exemption on qualifying income derived from carrying on of offshore specialised insurance business. The scheme is scheduled to lapse after 31 August 2016.

c) Captive Insurance: Under the Tax Incentive Scheme for Captive Insurance, approved insurers are granted tax exemption on qualifying income derived from carrying on of offshore captive insurance. The scheme is scheduled to lapse after 31 March 2018.

d) Insurance Business Development ("**IBD**"): Under the IBD scheme, approved insurers are granted a concessionary tax rate of 10% on qualifying income derived from the carrying on of offshore insurance business. The scheme is scheduled to lapse after 31 Mar 2020.

Following the 2016 Budget, tax incentives schemes for Marine Hull and Liability Insurance, Specialised Insurance Business and Captive Insurance will be subsumed under the IBD umbrella scheme with the following changes:

a) Marine Hull and Liability Insurance scheme will be subsumed under the IBD from 1 April 2016. A concessionary tax rate of 10% will apply to new and renewal awards from 1 April 2016.

b) Specialised Insurance Business scheme will be subsumed under the IBD as an enhanced tier award from 1 September 2016 to 31 Aug 2021. A concessionary tax rate of 8% will apply to new awards from 1 September 2019. As a transitional measure, a concessionary tax rate of 5% will apply to new awards from 1 September 2016 to 31 August 2019. A concessionary tax rate of 10% will apply to renewal awards from 1 September 2016.

c) The scope of qualifying activities will be expanded to cover business of underwriting both onshore and offshore specialised risks from 1 September 2016 for new and current approved insurers.

d) The Captive Insurance scheme will be subsumed under the IBD from 1 April 2018. A concessionary tax rate of 10% will apply to new and renewal awards from 1 April 2018.

The Monetary Authority of Singapore will release further details of the change by June 2016.

B. Enhancing Maritime Sector Incentive ("**MSI**")

Currently under the MSI, ship operators and ship lessors can enjoy tax benefits which include:

a) MSI-Shipping Enterprise (Singapore Registry of Ships) ("**MSI-SRS**") which grants tax exemption on qualifying income derived mainly from operating Singapore-flagged ships.

b) MSI-Approved International Shipping Enterprise Award ("**MSI-AIS**") which grants tax exemption on qualifying income derived from operating foreign-flagged ships.

c) MSI-Maritime Leasing (Ship) ("**MSI-ML(Ship)**") which grants tax exemption on income derived from leasing of ships used for qualifying activities to qualifying counterparties for use outside the port limits of Singapore.

The following changes will take effect from 25 March 2016:

a) The MSI-SRA and MSI-AIS will cover income derived from operation of ships used for exploration or exploitation of offshore energy or offshore minerals, and ancillary activity relating to exploration or exploitation of offshore energy or offshore minerals.

b) The MSI-ML(Ship) Award will cover income derived from leasing of ships used for exploration or exploitation of offshore energy or offshore minerals, and ancillary activity relating to exploration or exploitation of offshore energy or offshore minerals.

c) The restriction on the qualifying counterparty's requirement under MSI-ML(Ship) award will be removed. Therefore, tax exemption will be granted on income derived from leasing of ships used for qualifying activities to any counterparties for use outside the port limits of Singapore.

The Maritime & Port Authority of Singapore will release further details by June 2016.

C. Business and Institutions of a Public Character ("**IPC**") Partnership Scheme ("**BIPS**")

Currently, Corporate Social Responsibility expenditure made by businesses are deductible as part of their business expenses as they receive benefits such as goodwill, branding and enhanced corporate image in return.

Following the 2016 Budget, a pilot BIPS will be introduced from 1 July 2016 to 31 December 2018. Businesses will enjoy 250% tax deduction on wages and incidental expenses when they send their employees to volunteer and provide services to IPCs, including secondments. This will be subject to the IPC's agreement and a yearly cap of S$250,000 per business.

The Ministry of Finance and IRAS will release further details by June 2016.

Comments: The introduction of the BIPS is consistent with the current tax treatment of donations made by companies to IPCs. With the proposed change, businesses will be able to obtain a 300% tax deduction on cash donations, or a 250% on qualifying expenses incurred under the BIPS.

D. Corporate Income Tax ("**CIT**") Rebate

The CIT rebate will be increased from 30% to 50% for YA 2016 and YA 2017, subject to a cap of S$20,000 rebate per YA.

E. Land Intensification Allowance ("**LIA**") Scheme

Currently. the LIA scheme grants an initial allowance of 25% and an annual allowance of 5% on the qualifying capital expenditure incurred for the construction or renovation of a qualifying building or structure.

To qualify for the LIA scheme, the following conditions must be met upon completing the construction or renovation of the building or structure:

a) The Gross Plot Ratio ("**GPR**") of the building or structure meets the GPR benchmark applicable for the qualifying trade or business, or is at least 10% more than its current GPR if the existing building or structure already meets or exceeds the GPR benchmark; and

b) At least 80% of the total floor area of the relevant building or structure is used by a user for undertaking the qualifying trade or business.

Following the Budget 2016, the LIA scheme will be extended to buildings used by a user or multiple users, who are related, for one or multiple qualifying trades or businesses, if certain conditions are met. This change will take effect for LIA applications if the application for LIA is made from 25 March 2016, and the application for planning permission or conservation permission for the construction or renovation is made from 25 March 2016.

The qualifying capital expenditure for which an allowance may be made excludes any expenditure incurred before 25 March 2016. EDB will release further details of the change by July 2016.

F. e-Filing for CIT returns

e-filling of CIT returns will be implemented in stages according to the following timeline:

a) YA 2018: Companies with turnover of more than S$10 million in YA 2017;

b) YA 2019: Companies with turnover of more than S$1 million in YA 2018;

c) YA 2020: All companies.

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