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Singapore 2016 Pre-Budget Feedback

Preparing for the Future Economy

15 January 2016

Towards a value-creation economy

Foreword

Budget 2016 marks the first Budget that would be delivered by Singapore's new Finance Minister, Mr. Heng Swee Keat.

Minister Heng is also chairing the Committee on the Future Economy ("CFE") which would chart Singapore's next lap of growth. A key focus of CFE, and by extension, Budget 2016 and future Budgets, would be to move the Singapore economy up the innovation ladder, from one that is "value-adding" to one that is "value-creating".

Value-creation, or innovation-led enterprises, is core to every sector of the economy and is crucial to deliver new sources of growth and high-wage jobs. The focus on building new business capabilities and value-creation is ever more important for Singapore as a slower pace of growth is expected in 2016 and middle and back office jobs in the country are under threat from lower cost locations.

Fiscal policies drawn up to achieve this would be introduced amidst an international drive to combat tax avoidance. In this connection, Budget 2016 will be keenly watched as it will also be the first Budget to be released after the publication by the OECD of its final set of recommendations under the Base Erosion and Profit Shifting ("BEPS") Project for a 'comprehensive, coherent and co-ordinated reform of international tax rules'.

Our proposals for Budget 2016 include recommendations on:

- **Shaping fiscal policy with a view of encouraging a culture of innovation and promoting start-ups in Singapore**
- **Preserving Singapore as an attractive destination for foreign investments in an environment where international tax issues are high on the political agenda**
- **Connecting to new markets and promoting internationalisation of Singapore businesses**
- **Reviewing certain tax policies in a bid to keep Singapore's tax regime competitive while meeting increased spending on social safety nets**
- **Maintaining our edge over the competition in select industry sectors by ensuring our tax policies evolve in tandem with business developments**
- **Refining personal tax rules to address rising healthcare and childcare costs**

Thus, a balance must be achieved between keeping Singapore's tax system simple whilst ensuring that it remains coherent and acceptable in the international tax arena, such as calibrating and articulating our available tax incentives such that they are only awarded based on substantive activities being performed in Singapore.

Mindful of these constraints, our proposals for Budget 2016 calls for the strengthening of initiatives to promote innovation whilst meeting the twin challenges of keeping our tax regime competitive and addressing the implications arising from the BEPS Project.

Content

1. Abbreviations

AEC	ASEAN Economic Community
AITD	Angel Investor Tax Deduction
ASEAN	Association of Southeast Asia Nations
AUM	Asset under Management
BEPS	Base Erosion and Profit Shifting
CBCR	Country-by-Country Reporting
CFE	Committee on the Future Economy
CIP	Collaborative Industry Projects
CPF	Central Provident Fund
CTC	Corporate Treasury Centre
ETF	Enhanced-Tier Fund Exemption Scheme
F&B	Food and Beverage
FRS	Financial Reporting Standard
FTC	Finance and Treasury Centre
G20	Group of Twenty
GST	Goods and Services Tax
HR	Human Resource
IE	International Enterprise
IHQ	International Headquarters
IRAS	Inland Revenue Authority of Singapore
IRU	Indefeasible Right of Use
IT	Information Technology
LNC	Local Network Companies
M	Million

M&A	Mergers and Acquisitions
MAS	Monetary Authority of Singapore
MSI	Maritime Sector Incentive
NOR	Not Ordinarily Resident
OECD	Organisation for Economic Cooperation and Development
PIC	Productivity and Innovation Credit
QEEBR	Qualified Employee Equity-based Remuneration
R&D	Research and Development
R&R	Renovation and Refurbishment
RCEP	Regional Comprehensive Economic Partnership
ROV	Remotely Operated Vehicle
S$	Singapore Dollars
SEA	Southeast Asia
SITA	Singapore Income Tax Act
SME	Small and Medium-sized Enterprise
SPR	Singapore Permanent Resident
SPV	Special-Purpose Vehicle
TPP	Trans-Pacific Partnership
UK	United Kingdom
WDA	Writing-Down Allowance
WHT	Withholding tax
WMCR	Working Mother Child Relief
YA	Year of Assessment

2. Value creation

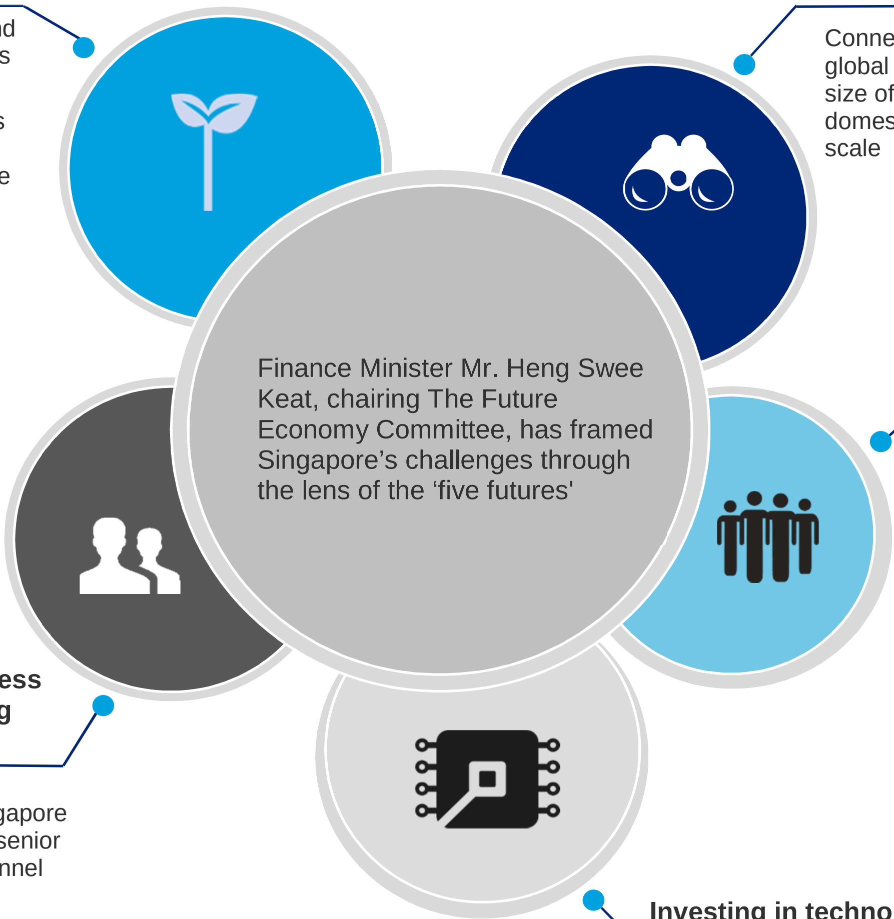
Building new business capabilities

Deepen corporate and innovative capabilities

Reinventing business models, encouraging businesses to venture out of their comfort zone

Connecting to new markets

Connect to regional and global markets to transcend size of Singapore's domestic market and build scale



Optimising resources by collaboration

Overcome resource constraints in land and labour by collaborating (amongst businesses)

Grooming business leaders, inspiring people

Grow or groom Singapore leaders, especially senior management personnel

Investing in technology

Encourage investment in R&D, especially in infocomm technology as it will transform every business and allow them to create value in new areas and in new ways that one may not expect

2.1 Building new business capabilities

Small, innovative, high-growth start-up companies are often in need of capital and management experience in order to expand their operations. In relation to the former, obtaining funding from traditional financial institutions can be difficult for a small but growing business due to the lack of a track record and stable cash flows.

2.1.1 Enhance existing tax incentives for early stage investors

Alternative sources of capital for such businesses generally start with friends and family, before moving on to angel investors / venture capital firms. We propose enhancing existing tax incentives for early stage investors. These incentives include the Angel Investor Tax Deduction Scheme ("AITD"), which provides enhanced deductions based on the amount of capital invested in a qualifying start-up company, against the angel investor's total taxable income. However, the enhanced deductions are clawed back if the gains derived by the angel investor from the subsequent disposal of his investment are adjudged to be taxable. In this regard, upfront certainty on the non-taxation of such investments should be granted to such angel investors.

2.1.2 Make capital gains safe harbour provision a permanent feature, with enhancements for disposals of investment in start-ups

On a broader note, the Singapore Income Tax Act ("SITA") currently provides for the certainty of non-taxation of gains derived from the disposal of share investments, but this is set to expire on 31 May 2017. Briefly, gains or profits derived by corporate investors from the disposal of ordinary shares in another company is exempt from tax if the investor company owns a minimum of 20% of the ordinary shares of the investee company for a continuous period of at least 24 months immediately prior to the sale.

The aforementioned safe harbour rules should be made a permanent feature in Singapore's tax legislation, or at least be extended for another five years, as it has been useful to give certainty to corporate shareholders, especially in a group restructuring context, and also enhances Singapore's position as an attractive holding company location.

With a view to encouraging a greater pool of equity financing for start-ups, the following enhancements should be considered:

- Reduce the minimum shareholding percentage (currently 20%) if the investment is made in start-ups to allow equity financiers to spread the risk;

- Expand the scope of the safe-harbour rule to include individual investors if the investment is made in start-ups; and

- Expand the scope of the rule to include quasi-equity instruments such as convertible bonds, redeemable preference shares etc., if the investment is made in start-ups, as start-up owners may prefer to retain majority equity control at the outset.

Also, to simplify compliance, consideration could be given to remove the requirement for foreign companies to file a tax return in Singapore in order to avail themselves to this capital gains certainty.

2.1.3 Make it easier for start-ups to secure new business partners / opportunities

Separately, the shareholder continuity test in relation to utilisation of brought forward tax losses and capital allowances (which currently requires no more than 50% change in the beneficial shareholders of the company with such unabsorbed loss items) should be relaxed for start-ups so that equity investors can be introduced to secure new funds for the business without impacting the ability of start-up companies to carry forward such tax loss items.

2.1.4 Refine employee share schemes

Singapore should also refine employee share scheme tax rules to make them more attractive to start-up companies or SMEs in hiring and retaining staff (given the importance of stock option awards to such companies). These include:

(i) Tax Deferral Scheme

Gains arising from the exercise of the stock options/vesting of the share awards are generally taxed in the year of exercise / vesting (unless there is a moratorium imposed). As the individual may not sell the shares in the same year and realise the gains, it may create a cash flow challenge for the individual if the tax arising from the share gains is substantial, especially if the said individual is bearing his/her own Singapore tax liability.

Currently, under the Qualified Employee Equity-based Remuneration ("QEEBR") scheme, payment of tax arising from stock option or share gains that arise during the relevant Year of Assessment ("YA") can be deferred up to five years, subject to an interest charge (linked to the "average of the prime rate" offered by the Big Three local banks in Singapore). In view that an interest charge is applicable on the tax deferral, it is not common for individuals to apply for the scheme.

To assist employees to mitigate any cash flow issues with regard to the settlement of their tax liabilities due to the exercise of the stock options or vesting of the share awards, consideration may be given to remove the interest charge for the first three years of the tax deferral (i.e. interest charge to apply from the 4th year of the tax deferral). Alternatively, the Government may wish to consider granting preferential or discounted interest rates when calculating the said interest charge, which are lower than the average prime rate. To make the scheme more favourable for Singapore Citizens and Singapore Permanent Residents ("SPRs"), the above-said benefits could be limited to this group of taxpayers.

(ii) Tracking option

When a non-Singapore Citizen or SPR ceases employment in Singapore, any unexercised stock options or unvested share awards as at the date of cessation of Singapore employment, are deemed to be exercised or vested one month prior to the date of cessation of Singapore employment and the deemed gains are reportable for tax in the tax clearance return (Form IR21). This is known as the deemed exercise rule. Tax arising on these deemed gains would have to be settled immediately prior to the said person leaving Singapore. As the share gains have not been realised, this generally creates a cash flow challenge for the departing employees.

To provide mitigation for the above challenge, the tracking option in lieu of the deemed exercise rule has been made available to employers who have applied for the scheme and obtained approval from the IRAS. Under this scheme, the employers are allowed to track and report the income when the “income realisation event” of the foreign employee occurs and report the relevant gains to the IRAS at that juncture.

However, as it may be very difficult to fulfil all the qualifying conditions of the scheme, the Government should consider revisiting the qualifying conditions for the tracking option, especially the capital requirement condition[1]. This would allow more employers to qualify for the scheme and more taxpayers to benefit from the scheme.

(iii) Mitigation of double tax exposure

Currently, gains from employee share plans are fully taxable in Singapore if the grant is made during Singapore employment, without consideration of sourcing of income during the vesting period of the grant. In addition, no foreign tax credit is allowed for tax suffered outside of Singapore on the same stock option/share gains subject to tax in both Singapore and another country.

This results in a misalignment of individual tax treatment compared to other countries which may adopt the OECD model of sourcing for stock option/share gains, thus resulting in a genuine double tax exposure since no foreign tax credit is allowed in Singapore on such gains.

As such, the Government should relook at the basis of taxation of stock options and shares in Singapore to be aligned with the OECD model of sourcing, or consider to grant foreign tax credits in situations where there is double tax exposure.

2.1.5 Enhance loss carry-back relief

The existing loss carry-back relief is capped at S$100,000 and can only be carried back to the immediate preceding YA. This amount now looks inadequate given that businesses, particularly SMEs, are still facing challenges in restructuring their business model to include greater automation and measures to reduce reliance on labour and hence may incur losses in the short term. The authorities should consider removing the cap for loss carry-back relief permanently, or in the alternative, to enhance the cap for loss carry-back relief to S$300,000 for the assessment years 2016 to 2018, with a view to reviewing the situation in YA 2018 in line with the expiry of the PIC incentive.

In addition, it should be noted that the adoption in 1 January 2018 of the new accounting standard for revenue recognition, FRS 115, would in certain instances result in, for tax purposes, mismatches of taxable income and deductible expenses. Either allowing for losses to be carried back to at least two back years, or removing the cap for carry back, may, in conjunction with tweaks to existing tax rules, mitigate the adverse impact of the changes brought about by the adoption of the new accounting standard.

2.2 Grooming business leaders / inspiring people

In recent years, the focus has shifted from attracting overseas talent to fuel Singapore’s economy growth to developing Singapore talent to fill key regional or global roles.

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[1] Under the tracking option, where the employer is a Singapore-incorporated company, its capitalisation must be within the top 25% of market capitalisation in the Straits Times Industrial Index. For a branch of a foreign-incorporated company registered in Singapore, the capitalisation of its parent company must be within the top 25% of one of the leading and universally recognised stock index in the parent company’s country of incorporation.

2.2.1 Expand scope of Not Ordinarily Resident ("NOR") scheme to include Singapore citizens and SPRs

The Not Ordinarily Resident ("NOR") scheme was introduced in 2002 with the objective of attracting foreign talent to relocate to Singapore and incentivise them for their regional or global roles. The primary benefit for an individual who is accorded NOR status is that he enjoys time apportionment of employment income (i.e. income tax is paid only on that part of his employment income that corresponds with the number of days he spends in Singapore) for a period of five years.

Singapore citizens and SPRs may hold the same regional or global roles and responsibilities as foreigners working in Singapore and face similar significant business travel requirements. However, they would generally not be able to qualify for time apportionment of employment income under the NOR scheme due to the requirement to be a non-Singapore resident in three years of assessment prior to the year in which the NOR status applies. To level the playing field between overseas and Singapore talent, the requirement for NOR applicants to be a non-resident for the preceding three consecutive YAs prior to the YA of claim for Singapore citizens / SPRs should be removed or relaxed. This should make the scheme more equitable for all taxpayers instead of being skewed in favour of foreigners, and encourage more Singaporeans to take up such regional or global roles.

2.2.2 Consider granting enhanced tax deduction for costs of recruiting Singaporeans in key roles

Further deduction can be granted to corporate taxpayers on costs incurred to recruit Singapore citizens / SPRs to fill key management roles or positions. This scheme can be modelled after the Further Tax Deduction Scheme for Expenses Incurred in Relocation or Recruitment of Overseas Talent, which was allowed to expire on 30 September 2013.

2.3 Connecting to new markets

A major part of future global growth will come from emerging markets. In Asia, rapid urbanisation and the attendant increased demand for higher-value services will provide Singapore companies with opportunities to expand in these markets.

Exposure to competition in the international arena helps sharpen the competitive edge of Singapore companies

Venturing abroad not only helps Singapore companies overcome the constraints of the domestic market, keen competition in the international arena also sharpens these companies' competitive edge. Collectively, raising productivity, **promoting** innovation and supporting the growth of globally competitive Singapore companies create a positive feedback loop that forms a virtuous cycle. Companies that create value will find it easier to penetrate foreign markets; likewise companies that are required to face international competition will find it necessary to create value.

2.3.1 Enhance foreign-sourced income exemption and foreign tax credit schemes

Internationalisation efforts were given a boost in Budget 2015, which saw the introduction of the International Growth Scheme, the expansion of the Double Tax Deduction for Internalisation Scheme, and beefing up of certain IE Singapore grants to promote internationalisation. As such, we propose tweaks to the existing tax regime surrounding the taxation of foreign-sourced income so that companies would continue to invest and derive income from overseas markets and to fully enjoy the fruits of internationalisation.

Briefly, Singapore does not tax income sourced outside Singapore unless such income is remitted into Singapore. Where foreign income derived by corporate entities is remitted into Singapore:

- Exemption from Singapore income tax may apply for foreign-sourced dividends, service income and branch profits under the foreign-sourced income exemption scheme; or

- Where foreign income is taxable in both the foreign country as well as in Singapore, a tax credit may be granted by Singapore for the foreign tax suffered by the corporate taxpayer, with the amount of tax credit normally restricted to the lower of the tax paid / payable in the foreign country and the Singapore tax payable on that foreign income. Foreign tax pooling is also available to allow foreign tax credits to be computed on a pooled basis (and hence potentially reduce the amount of excess foreign tax credits which will be disregarded) as opposed to a source-by-source, country-by-country basis.

(i) Foreign-sourced income exemption

With the formal establishment of the ASEAN Economic Community ("AEC") in end 2015, consideration should be given to granting full exemption of foreign-sourced income derived from markets within AEC. This should help entrench Singapore as a headquarters location and a nerve centre for investments into the ASEAN region, which is expected to be a key growth engine in the world economy in the coming years.

(ii) Foreign tax credit scheme

Currently, any excess foreign tax credit is not available for carry forward, regardless of whether the foreign tax credit is pooled or otherwise. The foreign tax credit scheme should be tweaked to allow excess credits to be:

- carried forward for offset against future Singapore tax payable on foreign-sourced income;
- carried back for offset against foreign-sourced income taxed in the immediate preceding year

This is to encourage companies to continue deriving foreign income in order to utilise the excess foreign tax credit.

2.3.2 Enhance Mergers and Acquisitions tax allowance scheme

Our biggest companies are mainly still government owned. In order to buffer ourselves against external shocks and to tap on opportunities in regional markets such as AEC and the Trans-Pacific Partnership ("TPP"), and continue to make Singapore a nerve centre for businesses, Singapore-headquartered companies should be strongly encouraged to grow in size.

On this note, perhaps the M&A tax allowance (special tax deduction for qualifying acquisitions) should be enhanced to provide better benefits. Currently, it has a cap of S$5M

(20% of value of acquisition up to cap of S$25M). To be fair, this scheme was only recently enhanced in Budget 2015, so it may take time to see if it is achieving the intended policy effect. To make the scheme more attractive and encourage companies to scale up quickly, the cap could be increased to S$100M to encourage bigger acquisitions.

2.3.3 Special tax deduction for interest and other related funding costs incurred to support overseas investments

Generally, interest and related funding costs incurred to support overseas equity investments are not deductible to the extent that such investments yield tax-exempt foreign dividend income or subsequent divestment gains are regarded as capital in nature and not taxable. On the other hand, if funding is sourced locally in the investee location by the overseas entity, such costs are generally tax deductible in the foreign jurisdiction if recorded in the overseas entity's books.

In M&A deals and setting aside interest rate differentials, it is normally difficult to source for local funding, especially if the acquiring Singapore group does not have a track record or sizable operations in the local country. As such, consideration may be given to grant a special tax deduction on interest or related borrowing costs incurred to acquire overseas equity investments, up to a certain cap. This could be targeted at SMEs to encourage them to grow, and may also benefit the local financial industry.

2.3.4 Raising awareness of free trade agreements amongst local enterprises

The level of awareness amongst local enterprises of the opportunities of internationalisation and competition that arises as a result of the introduction of the AEC, the TPP and Regional Comprehensive Economic Partnership ("RCEP") should be increased. Encouraging SMEs to attend seminars / training on this subject should go some way towards better equipping them to understand the benefits and challenges in utilising these Agreements. They would also be in a better position to self-assess their internal readiness to support their internationalisation efforts.

Notwithstanding that enhanced tax deductions on qualifying training expenditure are already available under the PIC Scheme (albeit with a cap), the authorities may consider disbursing training grants (in lieu of PIC claims) for such training courses or seminars.

2.4 Optimising resources by collaboration

Singapore has always faced constraints in both land and labour and the resource crunch will grow even more acute with the slowdown in foreign worker growth.

One way of maximising the use of limited land and labour resources is for smaller businesses to collaborate amongst themselves to achieve economies of scale and reduce overheads.

For example, collaboration projects between enterprises and industry partners or amongst large and small businesses are supported through grants administered by SPRING Singapore. These include the Collaborative Industry Projects (CIP) initiative and the Partnerships for Capability Transformation Scheme.

The authorities may wish to expand on the above initiatives and schemes by exploring ways to strengthen collaboration between industry and academia. Interaction between these parties should not be limited to merely staffing and recruitment. For example, support could be given to allow tertiary students to undertake research projects defined by an industry partner, or for the industry partner to present case studies or participate in guest lectures. This could result in a win-win situation for both parties, whereby students gain practical experience in an industry setting whilst the industry partner may obtain fresh perspectives on issues faced by the business. To incentivise companies, the cost of such projects can be given further tax deductions.

2.5 Investing in technology

A key focus of Budget 2016 and future Budgets would be to move the Singapore economy up the innovation ladder, from one that is "value-adding" to one that is "value-creating". To compete in the "Future Economy", businesses need to go beyond merely improving existing products or services, adding incremental value or maintaining cost competitiveness. Singapore has introduced generous tax incentives granting enhanced tax deductions and allowances for investments in equipment that boost productivity, spending on research and development that involves systematic, investigative and experimental study in a field of science or technology, spending on qualifying manpower training costs, patenting costs, qualifying intellectual property acquisition costs, and spending on approved product or industrial design. However, businesses may find it difficult to make the leap from undertaking activities that increase productivity to carrying out qualifying R&D that would lead to 'breakthrough' innovations or allow them to capitalise on new possibilities and opportunities.

Indeed, companies that claim enhanced deductions on R&D spending have come under intense scrutiny from the IRAS and often have to prove whether the project constitutes R&D as opposed to routine or cosmetic modifications. It is an "all or nothing" approach.

2.5.1 Incentivise 'evolutionary' innovative activities

In this regard, it may very well be that businesses need to undertake 'evolutionary' innovative steps before any 'revolutionary' breakthroughs are achieved. As such, it is suggested that a separate category could be set up for spending incurred on "innovative activities" that lead to the creation of new products or services which may not be considered R&D, such as the integration of two existing technologies. The benefit for such a category could be watered down, say for example PIC additional enhanced deduction of 150% (compared to the current 300%) and further deduction of 25% (compared to the current 50%), etc.

> It may very well be that businesses need to undertake 'evolutionary' innovative steps before any 'revolutionary' breakthroughs are achieved.

2.5.2 Encourage digitisation and software development activities

To encourage development in the IT sector, digitisation and automation of businesses, further tax deductions can be given for consultancy fees paid to engage in digitisation or automation of work processes (such as consultancy fees paid to help set up e-commerce platforms), etc. This is to recognise that digitisation of the business can contribute significantly to productivity and value creation.

Existing incentives for software development expenditure should also be enhanced. Such expenditure currently enjoy PIC enhanced deduction claims under the "Acquisition or leasing of PIC IT and automation equipment" category and there is an annual cap of S$400,000 on such expenditure. It may be helpful to segregate the hardware and software design/development claims, and put the latter under the “Qualifying design expenditure” category (which is seldom utilised) for purposes of claiming PIC. Also, super-deductions could be allowed for such software development costs incurred in excess of the cap. It should be noted that similar incentives are currently granted in China.

2.5.3 Ease administration of R&D claims

Currently claims for R&D expenses incurred in a basis period have to be lodged together with the annual tax return for the relevant basis period. The Government could consider allowing retrospective R&D claims to be made say within three years after the expenses are incurred. This allows taxpayers more time to assess the eligibility of their qualifying projects and discuss with IRAS upfront and avoid having to lodge protective claims in the tax returns which may make it administratively and optically more difficult to withdraw in the future.

2.5.4 Consider introducing a separate assessing body for R&D claims

Currently the IRAS, as the revenue collection body, assesses the R&D tax deduction claims and this is handled by the relevant case officer. Setting up a separate body instead of IRAS to assess the technical aspects of such claims may help to ensure consistency of technical queries and approach. This also allows IRAS to focus on the financial aspect being its core expertise.

3. Adapting to changes in international tax rules

The international tax world is currently undergoing unprecedented change as a result of the Base Erosion and Profit Shifting ("BEPS") project being carried out by the Organisation for Economic Cooperation and Development ("OECD") under instruction from the G20 group of countries.

Fundamentally, the aim of the BEPS project is to ensure that profits of a multinational group are taxed where substantive economic activities are performed and where value is created. This is in direct response to tax planning techniques and structures used by multinational groups to reduce or avoid (albeit legally) taxes on their cross-border investments or transactions.

Although Singapore is neither an OECD nor G20 member country, the changes arising from the BEPS project will potentially have a significant impact on Singapore, both as a "hub" location and preferred destination in Asia Pacific for foreign investment, as well as for Singapore-based companies investing overseas.

3.1 Maintaining relevance in a post-BEPS world

One key priority for the Government would be to look at how Singapore can remain an attractive destination for foreign investment in a BEPS environment. We understand that Singapore is seeking to play a more proactive role in the BEPS project as it moves into implementation and we would recommend that this is an area of focus to ensure that Singapore's interests are well represented.

One key priority for the Government would be to look at how Singapore can remain an attractive destination for foreign investment in a BEPS environment.

Specifically in relation to certain BEPS actions that are of most relevance to Singapore, we would make the following recommendations to ensure that Singapore continues to be an attractive destination for investment and does not fall out of line with internationally accepted minimum standards:

- **Action 5 (Harmful Tax Practices)** – to date the OECD has only considered preferential tax regimes of OECD member countries. As they move to examine regimes of non-OECD member countries (including Singapore), Singapore should seek to collaborate with other developing countries with similar tax incentive regimes to ensure that views are represented to the OECD in this area in a coordinated manner. Singapore has already stated that it supports the BEPS principle that profits should be taxed where substantive economic activities generating the profits are performed and where value is created. In this regard, Singapore should continue to monitor its tax incentives framework to ensure it is in adherence with the minimum standards that have been established, whilst continuing to be a key factor in attracting foreign investment.

Singapore may also wish to consider publishing more detailed guidelines on the criteria required to obtain certain tax incentives (e.g. minimum headcount and local business spending requirements). Transparency is a key tenet of the Action 5 recommendations and this is an area where Singapore may be viewed as an exception when benchmarked against other countries.

- **Action 6 (Treaty Abuse)** – in order for Singapore to maintain its attractiveness as a hub location, it must ensure that it adheres to the minimum standards established through Action 6. Singapore should also ensure it represents its interests proactively through the negotiations for the multilateral instrument to implement these minimum standards. In the short term, these new minimum standards may cause some investors to consider restructuring out of Singapore (e.g. if they have a low level of activity in Singapore) or to invest elsewhere, so it is critical that Singapore continues to promote its (non-tax) value proposition more widely to ensure that inward investment continues to grow.

- **Actions 8-10 (Transfer Pricing)** – as new transfer pricing approaches are being defined by the OECD in certain areas, Singapore should ensure that it reviews and implements these new approaches into its Transfer Pricing Guidelines where OECD countries do so. A key area of concern for taxpayers is the potential for increased disputes between tax authorities, so ensuring that Singapore adopts consistent transfer pricing approaches with its key trading partner and investor countries will be important to ensure this risk is reduced where possible.

- **Action 13 (Country-by-country reporting)** – a material number of OECD and G20 countries have already announced that they will adopt country-by-country reporting ("CBCR"). Assuming that this trend continues and more countries adopt CBCR, we would recommend that Singapore should also adopt CBCR to ensure it is in line with international standards and to not put itself at a disadvantage in bilateral negotiations (i.e. if another tax authority has more information available to it through the CBCR). Clearly, this would represent an increased administrative burden for taxpayers, but it would appear that this is becoming widely adopted globally so Singapore should ensure it is in line with common practice.

3.2 Tax treaty network

Singapore can do more to pursue new tax treaties (particularly in developing markets, such as East Africa) and re-negotiate old ones concluded many years ago on more competitive terms. In particular, some of Singapore's older treaties (e.g. with Australia and Taiwan) do not include any preferential tax treatment for technical service fees, while other treaties (such as with Indonesia) do not include any exemption or reduced rates for capital gains, which may be a disadvantage for Singapore investors looking to expand into these countries and ultimately affect Singapore's competitiveness as an international hub.

In addition, we note that other countries such as Hong Kong are proactively growing and improving their treaty network, and in some cases agreeing tax treaties that contain more favourable terms than the equivalent treaty with Singapore (e.g. the respective treaties with Indonesia). This may create the risk that, all other things being equal, investors do not choose Singapore as an investment destination if better terms are available in an alternative tax treaty.

3.3 Pervasiveness of the digital economy

As GST collection is now almost a quarter of our total tax collection, the Government may perceive a lesser need for a GST rate increase in the short term. In the longer term, as with many other countries, the Government will need to balance fiscal spending against sources of revenue in which case the Finance Minister will probably review the GST rate and make an appropriate decision.

A less eye-catching but equally important issue is whether the scope of GST would be broadened due to, amongst others, the pervasiveness of the digital economy. Presently, paying a fee to an overseas vendor to stream movies online would not attract GST in Singapore. However, paying for a Blu-ray disc or going to the cinema to enjoy the same movie would attract GST. Following recent discussions by the OECD on levelling the playing field between resident and non-resident vendors as well as to plug potential GST 'leakages', countries in the region are moving or have already moved to impose GST on such digital supplies and Singapore would need to consider whether the scope of GST should be broadened due to, amongst others, the pervasiveness of the digital economy. This is an area that should be considered in the near future.

3.4 Transfer Pricing

We note that Singapore has recently issued the Third Edition of its Transfer Pricing Guidelines and also in 2015 introduced new contemporaneous documentation requirements. Although this is more burdensome for taxpayers, this change is generally welcome and puts taxpayers in a stronger position when seeking to defend transfer pricing positions.

Assuming that Singapore implements CBCR, Singapore should develop specific guidelines so that taxpayers have greater clarity on local requirements.

Assuming that Singapore does proceed to implement country-by-country reporting ("CBCR"), Singapore should develop specific guidelines so that taxpayers have greater clarity on local requirements. That said, guidelines issued by the authorities should not be overly prescriptive and divergent from the OECD recommendations. For example, the filing due date for CBCR should be aligned with OECD recommendations (i.e. one year from close of financial year). This allows consistency with practices adopted by other countries and takes into account differing tax filing due dates across countries.

Sufficient notice needs to be given (at least six to nine months) before implementation to allow companies to prepare and put in place necessary changes to internal IT and accounting systems for collating the CBCR data.

4. Review existing tax policies

There is a need to keep tax rates competitive while meeting increased social spending obligations in the years to come.

One way to achieve both objectives is to review and tweak unproductive tax policies, those whose removal should not materially influence investment decisions by companies, has a weak nexus in achieving the policy intention behind implementing the scheme, or is generally outdated.

4.1 Review full tax exemption scheme

The full tax exemption scheme, which provides for 100% tax exemption on the 1st S$100,000 of chargeable income and 50% tax exemption for the remaining chargeable income up to S$300,000 derived by qualifying start-up companies during its first three consecutive years of assessment, was introduced to encourage entrepreneurship and the formation of 'start-ups'.

It was expected that more taxpayers would enjoy this exemption in line with the Government's push for more entrepreneurial activity. Whilst abuse of this scheme through the establishment of shell companies is punishable under the law, the authorities should review the full tax exemption scheme holistically and ensure that the personal income tax base is not eroded by new businesses that have little economic impact and/or generate little employment or value.

It is perhaps timely to consider having more targeted grants for such start-ups as opposed to a tax relief scheme which is broad-based and more open to abuse.

In addition, in reality, start-ups may not be able to fully benefit from the scheme as they would likely be having tax losses in the initial years. It is perhaps timely to consider having more targeted grants for such start-ups as opposed to a tax relief scheme which is broad-based and more open to abuse.

4.2 Productivity and Innovation Credit scheme

To-date, indicators on the efficacy of the PIC scheme in promoting productivity and innovation have not been encouraging, although productivity metrics may be improved going forward by the use of man-hours instead of headcount (which may include part time staff) to track labour productivity.

Nevertheless, the authorities may wish to consider whether the PIC scheme should include some measure of accountability on the part of businesses to actually achieve productivity growth; after all, buying a new laptop may be out of necessity and does not necessarily make one more productive. More targeted incentives for SMEs to engage consultants on digital strategy for their business may be more useful and productive.

5. Focus on industry-specific matters

5.1 Financial Services

5.1.1 Finance and Treasury Centre (“FTC”) incentive

In Asia, both Singapore and Hong Kong are choice locations for a treasury centre. To date, Singapore’s FTC incentive has been instrumental in influencing companies to locate their treasury centre in Singapore as opposed to Hong Kong, especially given the existence of restrictive interest deduction rules in Hong Kong and a smaller tax treaty network.

However, this is changing, with Hong Kong’s proposed tax treatment for corporate treasury centres (“CTCs”), i.e. relaxed interest deduction rules and a 50% reduction in Profits Tax for CTCs for certain specified treasury activities.

In the SEA region, the Treasury Management Centre in Malaysia and the proposed IHQ incentive in Thailand look attractive. While other factors in the choice of locating a treasury centre may limit the current rate of take up in these locations, these countries are emerging as an alternative to Singapore and Hong Kong in the drive to attract regional treasury centres.

To maintain Singapore’s competitiveness in this aspect, the FTC incentive should not only be extended past 31 March 2016, but also be improved to take into account the developments in treasury and financial activities globally. Improvements could be made in the following areas:

- **Align the withholding tax (“WHT”) exemption for bond interest with that for loan interest.** Exemption from Singapore WHT should also be granted to interest arising from loan notes, debentures and other debt securities.

- **Local Network Companies (“LNCs”)**. In considering whether to include Singapore companies in the group as LNCs, there is a requirement that the turnover of a relevant Singapore company cannot exceed 10% of the group turnover. However, this may work contrary to other tax incentives granted to group Singapore companies which require the Singapore companies to achieve a certain level of turnover to enjoy the Singapore tax incentives granted. The FTC incentive should work hand in hand with other Singapore incentives to promote the economic objectives of Singapore.

- **Review and update the regulations which define the qualifying activities and qualifying sources of income**. This should be done in line with the continuous developments on treasury and finance centre activities globally and it may be more useful to have a “negative” list rather than a lengthy list of prescribed qualifying activities and sources of funding.

- **Matching sources of funds and qualifying FTC activities**. Except in an ideal situation where funds obtained / raised by an approved FTC are wholly from approved sources and the activities carried out by the FTC are all qualifying activities, there are always concerns by FTCs as to how to track the funds to determine the quantum of the non-qualifying interest. Practically, it is very challenging for approved FTCs to match the sources of funds to the usage of funds. It is also costly for companies to open separate bank accounts for each source of funds to facilitate tracking for FTC purposes.

It is suggested that a fixed percentage to be determined and agreed with the relevant authorities for the purpose of computing non-qualifying interest would significantly simplify the process for corporate tax purposes.

Importantly, given that cash pooling is a key activity of FTCs and supports the banking / financial ecosystem, we suggest removing the tracking / matching requirement for physical cash pooling.

5.1.2 Fund Management

The Asset Under Management ("AUM") and spending requirements for the Enhanced-Tier Fund Exemption Scheme ("ETF") under the master-feeder-SPV or master-SPV fund structures should not be increased based on the number of entities, i.e. it should remain as S$50M and S$200,000 per annum respectively for the entire approved structure, since there is already a limit of the number of tiers (2 tier) for the SPVs. Otherwise, this has limited practicality as fund managers might as well apply for the resident fund exemption scheme where there is no AUM requirement, or set up SPVs elsewhere. Also, there should be a mechanism to allow MAS to waive the 2-tier limit on an approval or case-by-case basis as in some situations there may be a commercial need to include more tiers of SPV.

An additional issue is on the definition of "qualifying fund" for the purposes of the offshore fund exemption scheme (under Section 13CA) and ETF incentives. Broadly speaking these incentives only apply to a "qualifying fund" that is an "individual", a "trust" a "company", or a "limited partnership".

We recommend conducting a review of the definition of "qualifying fund" to ensure that it covers all foreign vehicles intended to receive the relevant incentives.

5.1.3 FinTechs

Research and technology is crucial to the development of financial services in Singapore; especially technologies that are transformative. Such technologies in financial services have been identified to include:

- digital and mobile payments;
- authentication and biometrics;
- block chains and distributed ledgers;
- cloud computing;
- big data; and
- learning machines

Underpinning the successful development of these technologies will be innovation, entrepreneurship and product commercialisation.

Given the importance of transformative technologies in financial services; existing financial sector tax incentives and R&D tax incentives should be configured to encourage the undertaking of these activities by existing financial services companies. At the outset the focus should be on the six areas noted above; and efforts made to drive these activities in Singapore. In terms of R&D tax incentives, the qualifying criteria should be defined such that there is a certainty of application for qualifying projects.

…existing financial sector tax incentives and R&D tax incentives should be configured to encourage research into transformative technologies by existing financial services companies.

Tax policy should also recognise that the successful development (to date) of financial services technologies has mostly been undertaken by incumbent technology companies. Thus, key to developing financial services in Singapore is the attraction of the core R&D activities of technology companies to Singapore. Tax and non-tax incentives should be configured to attract financial-related research activities to Singapore.

5.2 Shipping

5.2.1 Broaden scope of existing MSI

Tax exemption on shipping profits under existing MSI should be extended to include income derived by cable ship operators from offshore cable installation / repair works. These operators are also significant maritime players with the proliferation of the cable networks and widespread use of data.

In addition, based on the Income Tax Amendment Bill 2015, tax exemption on income derived from mobilisation, holding and demobilisation of vessels only applies to vessels which are used or to be used for offshore oil and gas activity. This should be extended to all types of vessels.

5.2.2 Revise list of qualifying activities into an exclusion list

It could be timely to revise the list of qualifying activities into an exclusion list such that a broader range of income is included within the incentive regime. For example, shipping companies have been facing pressure to reduce charter rates, leading to businesses finding other uses for vessels.

5.2.3 Withholding tax exemption

Currently, withholding tax exemption is applicable on vessel lease and container lease payments. Consideration may be given to extend withholding tax exemption on payments for rental of equipment used in certain sectors of shipping industry (e.g. ROV equipment commonly used in offshore exploration or marine cable works).

5.2.4 Consider to introduce PIC qualifying equipment list for shipping companies

For simplicity/ certainty, the Government may consider to introduce a PIC qualifying equipment list for shipping industry (similar to that for the cleaning / F&B industry).

5.3 Telecommunications

5.3.1 Withholding tax exemption and tax deduction for payments for the use of domestic IRU and access rights to telecommunications facilities

Currently, withholding tax exemption is granted to payments made to non-residents for the use of or the right to use international submarine cable capacity (including payments for an indefeasible right of use ("IRU")). We propose that such withholding tax exemption should also be extended to payments made for the use of or the right to use domestic IRU. This will be helpful in situations where a non-resident company may enter into a capacity swap arrangement with a Singapore local carrier and such non-resident may then in turn also contract with a Singapore resident in respect of the excess domestic capacity.

In addition, the current tax concession also provides for writing-down allowances ("WDA") over the number of years for which expenditure is incurred for the acquisition of an international IRU for the purposes of a person's trade, business or profession. Along the same argument that consideration should be given to aligning the tax treatment of payment for domestic IRU to that of international IRU, we also propose that a tax deduction or WDA be given on the upfront payment for the use of domestic IRU and also the costs incurred by a telecommunications carrier in acquiring access rights in relation to telecommunications sites and facilities.

5.3.2 Writing-down allowance for spectrum rights payment

Currently, Section 19B of the SITA allows a WDA claim on certain intellectual property rights including patent, copyright, trademark, registered design, geographical indication, lay-out design of integrated circuit, trade secret or information that has commercial value, or the grant of protection of a plant variety. Consideration should be given to extend the WDA to acquisitions of spectrum rights and bandwidths as they are essential for the continual competitiveness of the telecommunications business.

6. Other proposals

6.1 Business Tax

6.1.1 Group relief

Broadly, a company belonging to a group may transfer its unabsorbed tax losses, capital allowances and donations (collectively referred to as “loss items”) for the current year to another company within the group to set off against the assessable income of the claimant company. However, for the purpose of transferring loss items, a “group” is limited to a Singapore-incorporated company and its Singapore-incorporated group members. Two Singapore-incorporated companies that are held through a foreign intermediate holding company or commonly held directly by a third company incorporated outside Singapore will not be able to transfer loss items under the group relief system.

The current definition of a “group” is arguably too restrictive and should be relaxed such that foreign-owned groups are on par with Singapore-owned entities. This expanded definition of “group” is currently adopted for a similar group relief scheme in the UK.

6.1.2 Renovation and refurbishment (“R&R”) expenses

The provisions of Section 14Q currently allows a taxpayer deduction on expenditure incurred for any R&R works for the purpose of his trade or business, subject to certain conditions and exceptions. The deduction is allowed over a period of three consecutive years on a straight-line basis and the amount of R&R expenditure is capped at S$300,000 for every three consecutive tax years for each business entity.

Given the rising costs of doing business in Singapore, the S$300,000 expenditure cap for every three consecutive basis periods seems no longer adequate. As such, consideration should be given to increasing the expenditure cap for R&R works from S$300,000 to S$600,000 for every three consecutive basis periods.

In the alternative, qualifying R&R expenses may be written off over five years (without an expenditure cap), similar to that for Hong Kong.

6.1.3 Increase medical expense cap from 2%

A limit on the deductibility of medical expenses was introduced in YA 1994. The cap was initially set at 2% of total employee remuneration, but has since been reduced to 1% unless certain portable medical benefits options are implemented.

Singapore’s demographics have undergone profound changes in the two decades since the cap was introduced in YA 1994. Affordable health care has been at the top of the Government’s agenda in recent years, due to an aging population and escalating health costs. In this regard, it is hoped that the cap on deductibility of medical expenses can be increased. This will also alleviate the administrative burden on the part of employers to track the qualifying employee remuneration, and whether certain portable medical benefits schemes are implemented, for purposes of determining the amount of deductible medical expenses.

6.1.4 One year write-off for small assets

Companies may choose to write-off low value assets (defined as an asset not costing more than S$5,000) over one year for purposes of claiming capital allowances. In addition, the total claim for a one-year write-off of all low-value assets must not exceed S$30,000 per assessment year.

It is proposed that the annual cap of S$30,000 be removed so that taxpayers would not be required to distinguish between low-value assets claimed over one year or otherwise (for the purposes of calculating balancing allowances or balancing charges, where applicable) when such assets are subsequently disposed or falls into permanent disuse.

6.1.5 Deduction for group insurance premiums

The deductible rules for corporate income tax in relation to premiums paid for group insurance policies (e.g. group term life, personal accident insurance) and the taxation rules for personal income tax on such benefits-in-kind should be looked at independently.

Currently, where group term life or personal accident benefits are provided to employees or their named beneficiaries, the premiums incurred by the employer are taxable on the employee as a benefit in kind. An administrative concession is allowed such that the employees will not be taxed on such income if the employer elects not to claim such deduction. However, this requires additional administrative effort between the finance and HR teams to communicate and coordinate the reporting.

Given that businesses normally take up such insurance as a package of benefits provided to staff, we suggest that these premiums be treated as such, i.e. staff costs, and be allowed tax deduction to the company when the group insurance premiums are incurred.

Alternatively, a limit for tax deduction could be imposed on life insurance and other group insurance premiums, based on a certain (say 5%) of staff costs, similar to the current deduction rules for medical expenses, while assuring that employees are not taxed on such premiums paid by the employer. This should also significantly alleviate the administrative burden of tracking whether the employees or their families are the named beneficiaries or otherwise, and whether the employer should avail itself of the administrative concession.

6.2 Personal Tax

6.2.1 Earned income relief

The Earned Income Relief for the general population aged 55 years old and below has remained unchanged for decades and is no longer reflective of the income levels and cost of living today. The Government should relook and consider recalibrating the relief to be in line with current income levels and cost of living.

6.2.2 MediShield Life

All Singapore Citizens and SPRs are automatically included in MediShield Life. With better coverage, the premiums payable on MediShield Life have been increased accordingly which increases the burden for individuals who pay the premiums on the same for their elderly parents and dependent children.

The Government should consider providing a tax relief for individuals who pay the MediShield Life premiums for their elderly parents and dependent children.

6.2.3 Cap for claiming deductions on life insurance premiums

Currently, if CPF relief (employee's mandatory contribution) of more than S$5,000 has been claimed by the taxpayer in his tax return, any premiums paid on the life insurance policies will be disregarded and cannot be claimed as a relief. Only individuals whose mandatory CPF contributions are below S$5,000 per annum can claim the relief for life insurance premiums, which disqualifies a large majority of working Singapore citizens and SPRs.

To encourage individuals to take up life insurance policies in order to provide coverage for their loved ones in an unfortunate event, the Government should consider granting a separate relief for life insurance as a supplement to the current CPF relief for mandatory contributions.

In addition, life insurance premium relief is currently available to premiums paid on the taxpayer and/or his wife's life only. The Government may consider extending the relief to life insurance premiums paid on policies for dependent children and elderly parents.

6.2.4 Medical insurance premiums

Due to increasing medical costs, individuals should be encouraged to take on a more comprehensive medical coverage for himself (i.e. on top of the coverage provided under MediShield Life) so that a large part or the full hospital bills can be fully covered by insurance to minimise the financial burden and stress to the individual and family.

Consideration should be given to allow tax relief to individuals for medical insurance premiums paid for himself/herself, spouse, dependent children and elderly parents. This would help to promote individual responsibility for healthcare needs and alleviate the financial burden on individuals in view of the rising medical and healthcare costs in Singapore.

6.2.5 Working Mother Child Relief

Currently, the Working Mother Child Relief ("WMCR") is given to encourage married women to remain in the workforce after having children. Accordingly, only working mothers are eligible to claim the WMCR. In recent years, it has been noted that there is an increasing trend for married men to leave the workforce to care for their children at home instead. In this regard, to recognise that both spouses need encouragement to stay in the workforce, to consider to extend the WMCR to working spouses. Both parents may share the WMCR based on their mutually agreed proportion.

6.2.6 Child care / infant care relief

Due to the increased cost of living, the costs for maintaining a child in Singapore has substantially increased and both parents may decide to remain in the workforce (i.e. dual income family) in order to meet the rising costs and financial demands of the family. In this regard, parents would generally leave their children with child care / infant care centre while they are at work.

To alleviate the costs of bringing up children (who are Singapore citizens), consideration may be given to provide a tax relief/deduction for the actual costs incurred on child care / infant care centre subject to a reasonable cap.

6.3 Goods and Services Tax

6.3.1 To allow input tax incurred on compulsory medical check-ups for renewal of work permits

Currently, input tax incurred on compulsory pre-employment medical check-up is allowed via an IRAS administrative concession. We would recommend that this concession be extended to allow input tax incurred on compulsory medical check-up for renewal of work permits so as to reduce medical costs for employers of foreign workforce (e.g. construction industry).

We would also note that many factory facilities are required to have an on-site medical station. Currently the input tax incurred for such stations is blocked, despite that it is a requirement. We would propose that where a facility is mandated, the input tax claims be permitted.

6.3.2 To allow input tax incurred in connection with the purchase of shares / bonds

Currently, input tax incurred in connection with the purchase of shares / bonds is irrecoverable unless it is certain at the onset that the shares / bonds will be sold to an overseas person / via an overseas exchange (i.e. attributable to a future taxable supply). In some instances, the buyer may not know what they intend to do with the shares / bonds acquired and any intention made at the onset may also change along the way. Therefore, we would propose that input tax incurred on the initial purchase be treated as residual. If the shares / bonds are eventually disposed of, any input tax incurred would be directly attributable to that disposal and would be recoverable according to whether the disposal is taxable or exempt.

6.3.3 Valid tax invoices

If a standard-rated purchase is made in foreign currency, the S$ equivalents for the amount before GST, GST and amount including GST must be reflected and each shown as a separate amount in the tax invoice. We are aware that IRAS has granted administrative concession to some suppliers to show only the GST amount in S$. It is often difficult for the recipients to verify whether the suppliers have indeed obtained the said concession from

IRAS. Therefore, we would recommend that either the requirements under Regulation 11 of the GST (General) Regulations to show amount before GST and amount including GST in S$ be removed or recipients of foreign currency denominated invoices are also allowed via an administrative concession to claim input tax based on such invoices.