2021 Budget tax developments

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February 23, 2021

Introduction

As Singapore continues the fight against COVID-19, Deputy Prime Minister and Finance Minister Heng Swee Keat delivered the 2021 Budget Statement in Parliament on 16 February 2021, building on measures implemented in the 2020 Budget and reaffirming Singapore's expansionary fiscal policy in tackling the widespread impact of the pandemic. In this article, we comment on the key tax changes introduced in this Budget and also take the opportunity to highlight notable tax developments that have taken place over the previous year.

A. Summary of Budget 2021 tax changes:

1. Extension of Budget 2020 temporary tax measures to support businesses

a. Extension of the enhanced carry-back relief scheme for YA2021;
b. Extension of accelerated relief for Plant & Machinery, Renovation & Refurbishment for YA 2022;

2. Key changes to Singapore's GST regime will take place in coming years and businesses with cross-border activities would need to plan ahead accordingly

a. The planned GST increase from 7% to 9% will take place between 2022 and 2025, subject to the economic outlook in Singapore;
b. GST will be extended to low-value imported goods and business-to-consumer (B2C) non-digital services with effect from 1 January 2023;
c. In view of the growth of online advertising, the basis for determining the supply of media sales for GST zero-rating purposes will be updated to reflect the growth in online advertising with effect from 1 January 2022;

3. Maintaining the competitiveness and resilience of our tax system

a. Enhance the Double Tax Deduction for Internationalisation scheme;
b. Extend and refine the double tax deduction for qualifying upfront cost attributable to retail bonds approved by MAS;
c. Extend and legislate the withholding tax exemptions for the financial sector;
d. Extend the WHT exemption on payments made for structured products and payments for over-the-counter financial derivatives;
e. Extend the Not-for-Profit Organisation tax incentive till 31 December 2027;
f. Allow the Automation Support Package to lapse, but retain the 100% Investment Allowance scheme to support automation;
g. Extend and enhance the Investment Allowance (Energy Efficiency) scheme;
h. Allow the Insurance Business Development-Specialised Insurance scheme to lapse after 31 August 2021;

i. Withdraw the Accelerated Depreciation Allowance for Highly Efficient Pollution Control Equipment scheme;

4. Singapore’s move towards environmental sustainability

a. Enhancement of the Electric Vehicle Early Adoption Incentive for electric cars and taxis; and
b. Increase in petrol duty rates.

Extension of the Enhanced Carry-back Relief Scheme

The carry-back relief scheme was introduced in the 2005 Budget, which allowed a one-year carry-back of unabsorbed capital allowances and trade losses (Qualifying Deductions) to be deducted against assessable income of the previous year. To further help businesses cope with cash-flow problems as a result of the COVID-19 pandemic, this scheme was enhanced in the 2020 Budget to allow qualifying deductions to be carried back up to three immediate preceding year of assessments (YAs), capped at S$100,000.

To continue supporting businesses, the scheme will be extended to YA2021, with the same parameters.

Extension of accelerated relief for Plant & Machinery (P&M), Renovation & Refurbishment (R&R)

The accelerated relief for P&M is an enhancement to the capital allowance deduction regime for qualifying fixed assets. Prior to the introduction of this relief, businesses were able to claim capital allowance on the cost of qualifying fixed assets over a period of three years. However, with the accelerated relief for P&M, businesses are able to claim capital allowance for all qualifying assets over a period of two years instead, with 75% of the cost to be written-off in the first year and 25% to be written-off in the second year. This is to support businesses who are intending to expand and invest in new assets and ease the cash flow of other businesses.

Similarly, deductions for R&R could normally only be claimed by a company over three consecutive YAs starting from the year the R&R expenditure is incurred. This meant that approximately 33% of the cost of the R&R expenditure could be claimed each year. However, with the accelerated relief for R&R, business may opt to claim R&R deduction in one YA, capped at S$300,000 for every relevant period of three consecutive YAs.

Both accelerated reliefs have been extended to YA2022, with the same parameters.

GST increase from 7% to 9% to take place between 2022 and 2025

In the 2018 Budget, the Government announced its intention to increase the GST rate from 7% to 9% somewhere between 2021 and 2025. In the 2020 Budget, to support the economy during the uncertainty caused by COVID-19, the Government announced that the GST increase will not take place in 2021.

This Budget, the Government has reaffirmed this intention. However, to meet recurrent spending needs, and to maintain fiscal discipline and prudence, the GST increase will happen between 2022 and 2025 – sooner rather than

later, depending on the economic outlook in Singapore.

GST on low-value imported goods

To level the playing field between overseas and local suppliers, GST on certain imported services was introduced in the 2018 Budget. This change took effect on 1 January 2020 to tax overseas supplies of services via a reverse charge mechanism for business-to-business (B2B) imported services and an Overseas Vendor Registration system for B2C imported services (e.g. Netflix, Spotify). In our Budget alerts for previous years, we noted that the Government had yet to implement corresponding changes in the GST treatment of the import of overseas goods by post or air with a value below S$400, which is presently exempt from GST. As predicted, this lacuna would eventually have to be addressed to reduce GST discrimination against local businesses.

With effect from 1 January 2023, the Government will be extending GST to goods imported via **post or air regardless of value**. This will be effected via the Overseas Vendor Registration and reverse charge regimes.

GST will also be extended to B2C imported non-digital services, to be effected via the existing Overseas Vendor Registration regime. Non-digital services may include live interaction with overseas providers of educational learning, fitness training, counselling and tele-medicine. These measures thus close the remaining gaps and ensures that our GST system remains updated in an increasingly digital economy.

Details of the above changes will be published soon. IRAS has stated that it will consult the industry shortly before the implementation details are finalised.

Updating the basis for determining the supply of media sales for GST

Under the existing GST regime, the basis for determining whether zero-rating tax treatment applies to a supply of media sales was based on the place of circulation of the advertisement. Media sales may include advertising in newspapers, websites, TV and radio, and the sale of advertising spaces.

However, due to developments in digital technologies and the growth in online advertising, it has become increasingly difficult for suppliers of digital media sales to determine the place of circulation for GST purposes. As such, the Government has sought to update the basis for determining whether zero-rating applies to a supply of media sales, to be based on the place where the **contractual customer and direct beneficiary of the service belong**. For example, if a customer belongs outside Singapore and the direct beneficiary either belongs outside Singapore or is GST registered in Singapore, the media sales will be zero rated.

B. Amendments to the Singapore tax regime in 2020 – 2021

In summary, we have observed a strengthening of IRAS' powers of enforcement under Singapore's tax legislation to combat tax avoidance. In particular, IRAS has been given additional powers to impose surcharges and penalties on taxpayers for tax avoidance and non-arm's length payments under the transfer pricing regime.

Surcharge on anti-avoidance arrangements under

the Income Tax Act, GST Act

The general anti-avoidance provision in Singapore is Section 33 of the Income Tax Act (ITA), which empowers IRAS to disregard or vary tax avoidance arrangements and make an appropriate adjustment to counteract any tax advantage obtained by the taxpayer.

With effect from YA2023, a the Government has implemented a surcharge equal to **50%** of the amount of tax or additional amount of tax imposed on a taxpayer or of the tax assessed pursuant to Section 33 of the ITA.

Similarly, Section 47 of the GST Act confers similar powers on IRAS to counteract arrangements for the avoidance of GST. With effect from 1 January 2021, a surcharge was introduced equal to 50% of the amount of additional tax imposed on the taxpayer pursuant to Section 47 of the GST Act.

The above penalties also bring to mind similar provisions implemented in the transfer pricing context in 2018. In general, transactions between related parties must be conducted at arm's length. Section 34D of the ITA empowers IRAS to make tax adjustments to transactions not conducted at arm's length. For example, IRAS may disregard the form of actual commercial or financial relations between related parties where the substance of the transaction is inconsistent with the form of the transaction, and to increase a taxpayer's income, reduce its deduction, and/or reduce its loss based on arm's length considerations.

With effect from 1 January 2018, a 5% surcharge was introduced on the amount of transfer pricing adjustments made by IRAS pursuant to Section 34D. The surcharge is generally levied on the quantum of the adjustment, rather than the tax arising from the adjustment.

Overall, the above developments reflect Singapore's increasing enforcement of its tax avoidance and transfer pricing rules and can also be seen as part of a global trend of countries reinforcing their tax enforcement powers. This could be due in part to the need to raise revenue to alleviate the economic impact of the COVID-19 pandemic.

C. International Developments

Beneficial ownership transparency

There has been a growing consensus towards beneficial ownership transparency led primarily by the EU in the last ten years. For example, countries such as the UK and Switzerland have implemented measures requiring companies and corporations to disclose their beneficial owners in certain circumstances. While the US did not initially take action, they have recently enacted legislation to require disclosure of beneficial owners. Similarly, traditional offshore jurisdictions such as the BVI, Cayman Islands and Jersey have also implemented beneficial ownership register schemes due to the mounting global pressure. As a result of these global trends, there are fewer jurisdictions where assets can be hidden and there will be less of an incentive to do so.

Similarly, Singapore itself has implemented beneficial ownership disclosure requirements since 2017 and is a well-established and leading jurisdiction for offshore wealth management and foreign investments. This is supported by its strong rule of law, sound financial regulation, stable political environment, along with global accounting and legal standards.

Increase in taxes to increase revenue post-COVID

Governments around the world have been running large budget deficits during the COVID pandemic. As world

economies recover, many countries are therefore expected to increase tax rates, or introduce new taxes, or step up their enforcement measures, in order to collect more tax revenue to cover the deficits of the last few years.

Singapore is in a unique position as it is able to tap into its reserves to fund its expansionary fiscal policies. This means that the need for Singapore to increase its tax rates to address budget deficits is less acute than in some other countries. This allows Singapore to remain competitive and continue being a business-friendly tax jurisdiction. Accordingly, it is expected that MNCs will take greater advantage of Singapore’s conducive business environment and shift more substantial business activities here in order to qualify for tax incentives.

Ongoing discussion to revise international tax rules under the Base Erosion and Profit Shifting (BEPS) project

By way of background, the BEPS project was initiated in 2013, where the OECD and G20 countries adopted a 15-point Action Plan to address BEPS (BEPS 1.0 Action Plan). Put simply, BEPS occurs when there is a mismatch between where profits are booked and where profits are generated, leading to a reduction of taxable base for certain countries. As such, certain practices of global tax planning, such as IP holding, have since faced greater scrutiny.

The BEPS 1.0 Action Plan identified 15 actions along with three key pillars: coherence, substance and transparency. More specifically, BEPS Action 5 introduced the “modified nexus” approach in relation to IP regimes due to rising concerns of corporate tax rate reductions on intangibles as part of harmful tax practices. This approach applies the substantial activity factor in the context of IP and builds on the principle that, because IP regimes are designed to encourage R&D activities and to foster growth and employment, a substantial activity requirement should ensure that taxpayers benefiting from these regimes did in fact engage in and incur actual expenditures on such activities. More significantly, this approach contributes to the second pillar of the BEPS Project, namely to align taxation with value creation.

As part of its commitment towards the BEPS project, the Singapore Government excluded IP income from existing tax incentive schemes – the Development and Expansion Incentive-Services / Headquarters and Pioneer-Services / Headquarters Incentive – and introduced the Intellectual Property Development Incentive (IDI) in the 2017 Budget. As of 1 July 2018, the IDI is implemented under Section 43ZI of the Singapore Income Tax Act to cover IP income.

More recently, the Singapore Income Tax (Concessionary Rate of Tax for Intellectual Property Income) Regulations 2021 (the Regulations) came into force on 18 January 2021 and specifies the application of the concessionary tax rates for IP under the IDI.

Under the IDI, an approved company can benefit from a base concessionary tax rate of either 5% or 10% on a percentage of qualifying IP income derived by it during an initial incentive period not exceeding ten years. This percentage is determined by the “modified nexus” approach - there must be a direct nexus between the qualifying IP income and the qualifying IP expenditure. In this regard, the Regulations only permits IP income arising from the exploitation of qualifying IP rights, namely patents and copyrighted software, to benefit from the IDI. This restriction adheres to the BEPS Action 5 plan, which provides that only patents, copyrighted software and other IP assets functionally equivalent to patents can qualify for benefits under the IP regime, and the taxpayer can only receive benefits for R&D expenditure incurred for the production of the IP assets.

Moreover, under the Regulations, an approved company is required to keep records of information in relation to the qualifying IP income, and expenditure incurred in producing the qualifying IP income and the qualifying IP rights. In

particular, they must record details of how each specified right is obtained and the basis for determining that any expenditure incurred is for the purpose of obtaining the specific right.

The current BEPS 2.0 initiative seeks to ensure a global minimum level of taxation and introduces new rules and concepts to tax the ever-growing digital economy. If implemented, and as briefly mentioned in the 2021 Budget, BEPS 2.0 is expected to significantly change the way taxing rights are allocated between jurisdictions. If and when these international tax rules are changed, Singapore's corporate income tax revenues might decrease in some cases but might stand to increase in other cases.

Summary

In summary, Singapore's tax regime strives to keep up to date with local and global developments and presents opportunities for individuals and businesses to anchor their investments and activities here.

Dentons Rodyk thanks and acknowledges Senior Associate Jeremy Goh, Practice Trainees Genevieve Chan and Sam Cho Joo for their contributions to this article.

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