

Client Alert

May 2018

For more information, please contact:

Allen Tan
+65 6434 2681
Allen.Tan@bakermckenzie.com

Dawn Quek
+65 6434 2599
Dawn.Quek@bakermckenzie.com

Peter Tan
+65 6434 2669
Peter.Tan@bakermckenzie.com

James Choo
+65 6434 2603
James.Choos@bakermckenzie.com

Shih Hui Lee
+65 6434 2532
Shih.Hui.Lee@bakermckenzie.com

Jaclyn Ho
+65 6434 2254
Jaclyn.Ho@bakermckenzie.com

Amendments to the Economic Expansion Incentives (Relief from Income Tax) Act ("**EEIA**")

The Economic Expansion Incentives (Relief from Income Tax) (Amendment) Act 2018 ("**Amendment Act**") and the Economic Expansion Incentives (Relief from Income Tax) (Intellectual Property Income) Regulations 2018 ("**Regulations**") came into operation on 4 May 2018.

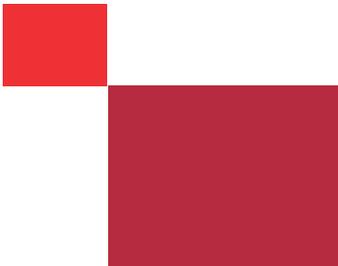
The Amendment Act and Regulations effect, among others, the changes relating to the exclusion of intellectual property ("**IP**") income from certain existing Singapore tax incentives, as announced by the Singapore Government during Budget 2017 in February 2017.

1. IP Income Exclusion

The Amendment Act and Regulations effect the exclusion of IP income from the Pioneer Service Companies Incentive ("**PC-S**") and the Development and Expansion Incentive ("**DEI**"). The changes should be seen in the context of the proposed introduction of the IP Development Incentive ("**IDI**"), details of which have yet to be released publicly. The IDI is intended to incentivise certain IP income under an approach that is compliant with the Organisation for Economic Co-operation and Development's Base Erosion and Profit Shifting project.

Under the Amendment Act and Regulations, IP income derived from IP rights owned by an incentivised company may be excluded from qualifying income that enjoys a lower concessionary tax rate under the company's PC-S or DEI. We set out the key considerations that should be noted in relation to the Amendment Act and Regulations:

- (a) A company "owns" an IP right if the company is the owner of the right or a grantee of a licence to the right. Note that there is no requirement for the grantee to be an exclusive licensee of the IP right.
- (b) "IP right" is defined as any right conferred by any patent, copyright, trade mark, registered design, geographical indication, layout-design of integrated circuit or the grant of protection of a plant variety. In other words, trade secret, information that has commercial value, and goodwill do not fall within the scope of the IP income exclusion.
- (c) Royalties or other income is derived from an IP right (i.e., considered to be IP income) if it is receivable as consideration for the commercial exploitation of that right. In this regard, while the Amendment Act and Regulations do not provide further guidance as to the interpretation of the term "commercial exploitation", we understand that the Singapore Economic Development





Board ("**EDB**") and/or the Inland Revenue Authority of Singapore may provide further guidance as to what this means in due course.

For companies whose PC-S or DEI were approved before 1 July 2018, the IP income derived from IP rights acquired before 1 July 2018 ("**Existing IP Rights**") will enjoy grandfathering and will be subject to the concessionary tax rate under the existing PC-S or DEI until 30 June 2021. However, IP income derived from: (i) IP that comes into the ownership of the company on or after 1 July 2018, or (ii) IP acquired from related parties after 16 October 2017 but before 1 July 2018 where tax avoidance is the main purpose or one of the main purposes of the IP acquisition (collectively, "**New IP Rights**") will not be grandfathered and will no longer fall within the scope of the PC-S or DEI on or after 1 July 2018.

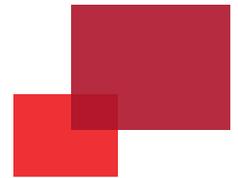
Given the different treatment of the IP income derived from the Existing IP Rights compared to New IP Rights during the interim period from 1 July 2018 to 30 June 2021, companies incentivised under the PC-S or DEI will be required to track their IP income derived from Existing IP Rights and New IP Rights, in order to be compliant with the IP income exclusion. In this regard, the Regulations also provide certain guidance as to how the tracking can be done.

For companies whose PC-S, DEI, or extensions for the PC-S or DEI are approved on or after 1 July 2018, all IP income derived from IP rights that the company owns will be excluded from the scope of the concessionary tax rate under the PC-S or DEI from the date of the award / extension.

2. Other Changes

Among other changes, the Amendment Act also amends the EEIA to grant the Minister discretionary powers to amend the concessionary tax rates of companies that have been granted the DEI. In particular:

- (a) The new section 19J(5DA) allows the Minister to on its own initiative or on the application of the company, amend the company's DEI certificate by substituting the concessionary tax rate specified in the certificate with a concessionary tax rate of either 5% or 10%.
- (b) The new sections 19J(5EA), 19J(5EB) and 19J(5EC) further allow the Minister to on its own initiative or on the application of the company, amend the certificate issued for DEI extension awards with a substituted rate in accordance with the statutorily provided formula. Under the prescribed formula for the calculation of the tax rate to be substituted, the Minister has the discretion to determine whether a component of the formula should be 5% or 10%. In other words, although there is a statutorily prescribed formula, the Minister's discretion will have an impact on the rate of tax that is substituted.



Next steps

The IP income exclusion may have a significant impact on companies with the PC-S or DEI incentives, and derive income from the use of IP. Companies should therefore consider the impact of the IP income exclusion on their operations in Singapore. In particular:

- (a) Companies that have existing PC-S or DEI awards (i.e., awards approved before 1 July 2018 that are therefore grandfathered), which extend beyond 30 June 2018 should review their income streams to consider whether such income will fall within the scope of IP income after 30 June 2018, as the PC-S or DEI will no longer cover IP income derived from New IP Rights after 30 June 2018, and IP Income derived from Existing IP Rights after 30 June 2021, notwithstanding any agreement with the EDB.
- (b) Companies that are currently recipients of the PC-S or DEI awards and derive IP income from IP rights that it owns will need to consider its compliance obligations in relation to the tracking of IP income derived from Existing IP Rights and New IP Rights. This applies equally to companies that are undergoing restructuring of their business structures and operations, but will not be able to complete such restructurings before 1 July 2018.
- (c) Companies which are intending to apply for the PC-S or DEI, or are currently in discussions with the EDB on applying for an extension of such incentives will need to consider the timing implications of signing the PC-S or DEI. Where the PC-S or DEI is approved before 1 July 2018, the IP income derived by the companies from Existing IP Rights will be grandfathered till 30 June 2021.

www.bakermckenzie.com

Baker McKenzie Wong & Leow
8 Marina Boulevard
#05-01 Marina Bay Financial Centre
Tower 1
Singapore 018981

Tel: +65 6338 1888
Fax: +65 6337 5100

Companies may also wish to consider whether they will want to apply for the IDI, once the details of the IDI are released. We will provide further updates on the IDI, when the details become available.

Please feel free to reach out to us if you have any questions on the above.

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