BDO CONNECT

MANAGING PARTNER'S MESSAGE

Frankie Chia
BDO Singapore

Time flies, and we already at the halfway mark of 2018. The first half was quite an interesting one with several notable events that took place. The obvious one is the ongoing trade wars between China and the US which is worrying. Even American allies are not spared either with President Trump insisting that the world play fair with America in trade. Then the twist of events in the Korean peninsula that caught many by surprise. For months, the DPRK Supreme Leader and the US President has been engaging in an intense war of words, and suddenly after the 2018 Winter Olympics, the tone changed. Both leaders met one-on-one in Singapore in June resulting in DPRK leader agreeing to denuclearise. The success of the summit seems to reduce tension here in Asia somewhat. Singapore also benefitted from this event putting this 'little red dot' at an important place in the world of politics, economy and human history.

In this issue, we are featuring an article on cybersecurity among other things. In fact, we will be featuring more such articles/pieces on a regular basis going forward hoping to raise awareness on the importance of cybersecurity with our clients and partners in light of the increase in cyber threats. In June, Cyber Security Agency of Singapore released the Singapore Cyber Landscape 2017 reporting an overall increase of cyber threats ranging from phishing attacks, website defacements and malware infections here in Singapore last year. And most recently, Singapore's health system was hit by cyber attack - a severe breach in Singapore's history.

I hope you will enjoy and benefit from the articles that we have for you on this issue. Have a good read and enjoy!

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Basis of Assessment for Service Companies

A service company refers to a company that provides services only to related companies. Services may include management services, technical support services, procurement, administrative support services and customer support services. It is essentially a cost centre rather than a profit-making entity, normally reimbursed by their related parties at cost or cost plus a certain margin.

Cost-plus mark-up basis of assessment

As an administrative concession to ease the compliance burden of such services companies, the Inland Revenue Authority of Singapore ("IRAS") has accepted a simple cost-plus mark-up basis of assessment ("CM basis").

The IRAS generally allows the chargeable income of a service company to be computed based on the mark-up on the total expenditure incurred by the service company, without any further tax adjustments.

The IRAS does not allow a service company adopting the CM basis to make the following claims:

- Double or further tax deductions;
- Productivity and Innovation Credit ("PIC") enhanced deduction and cash payout;
- Capital allowances and loss;
- Donations and deduction under the Business and IPC Partnership Scheme; Foreign tax credit.

Tax items	Tax treatment
Section 14Q deduction (renovation or refurbishment incurred prior to the transition YA)	If the expenditure has been capitalised in the accounts, Section 14Q may be computed based on the net book value ("NBV") at the transition YA
Capital allowances (qualifying plant & machinery acquired before the transition YA)	If the expenditure has been capitalised in the accounts, capital allowances may be computed based on the NBV at the transition YA
General provision made prior to the transitional YA	Provisions utilised may be allowed and provision written back may not be taxed
Specific provision made prior to the transitional YA	No adjustment will be required on provision utilised or provisions written back
PIC claim on expenditures incurred prior to the transitional YA	No PIC claim will be allowed

The IRAS has clarified that the CM basis will continue to be available as an administrative concession, to service companies on the premise that they fall within the following scenarios:

- The routine support services fall within Annex C of the IRAS e-Tax Guide entitled "Transfer Pricing Guidelines";
- The service provider does not offer the same routine support services to an unrelated party; and
- All costs, including direct, indirect and operating costs relating to the routine support services performed, are taken into account in computing the 5% mark-up.

From YA 2018 onwards, new service companies which do not qualify for the CM basis will need to adopt the NTC basis from inception.

Existing service companies that have adopted the CM basis but do not meet the above conditions for CM basis to apply, will be required to prepare their tax computations on a normal trading basis ("NTC basis") latest by Year of Assessment ("YA") 2020.

Normal Trading Company Basis

Under the NTC basis, a company's chargeable income is ascertained after detailed examination of its accounts and making tax adjustments in accordance with the provisions of the Income Tax Act, such as:

- Deducting non-taxable income (such as gain arising from sale of fixed assets, non-trade income, etc);
- Adding back disallowable expense (private car expenses, non-business expenses, etc);
- Claiming double and further deductions for qualifying expenditure;
- Claiming capital allowances and donations;
- Setting off brought forward loss, capital allowances and donations

Transitional adjustments from CM basis to NTC basis

The IRAS has recently issued guidelines for service companies that have adopted the CM basis and are required to be transited to the NTC basis. Briefly, these companies that are transiting to the NTC basis should apply the following rules in the YA of transition.

Action required

Service companies which have prepared and filed their tax returns on the CM basis should start to review the scope of services they provide to ensure that they will continue to qualify to apply this basis. In the event that they do not, and a change to the NTC basis is required, the company should start to prepare for the transition, including:

- Review and enhance its accounting records and documentation to provide more transactional details so that tax adjustments (e.g. private car expenses, capital items, exchange differences) can be made.
- Revisit its business plans and commercial activities to explore possible tax concessions, e.g. double deductions for expenses incurred for internationalisation of its business.
- Review its capital expenditure budget for capital allowance claims, although service companies generally are not expected to require significant fixed assets.
- Consider the need to engage a tax agent to prepare the tax computation since there is an increase in complexity of the tax compliance work.

While there is some increase in tax compliance burden, with careful attention to additional data collation and analysis, there could be benefits that the service companies may enjoy under the NTC basis. Early review of business plans and accounting systems will help to ensure a smooth transition and also position the company to benefit from the availability of the various deduction schemes.

For further information or clarifications, kindly contact:

Evelyn Lim
Executive Director
evelynlim@bdo.com.sg
+65 6828 9629

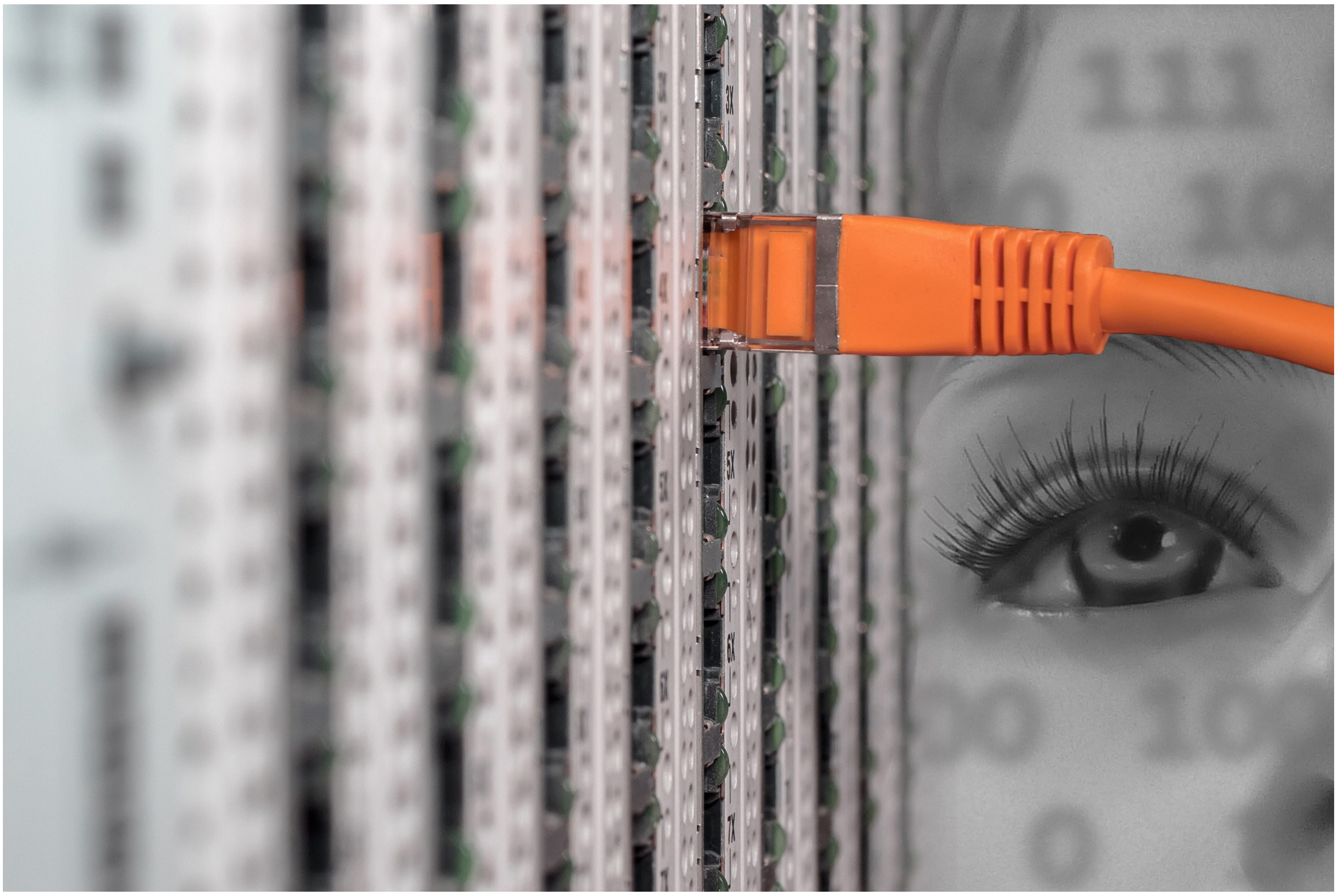
Eu Chin Sien
Executive Director
chinsien@bdo.com.sg
+65 6828 9186

Kylie Luo Jia Li
Executive Director
kylieluo@bdo.com.sg
+65 6828 9123

Wong Sook Ling
Executive Director
sookling@bdo.com.sg
+65 6828 9145

Wu Soo Mee
Executive Director
soomee@bdo.com.sg
+65 6829 9125

Cybersecurity In An Evolving Landscape



The emergence of new technologies and their impact on private and public agencies is hard to ignore and overemphasise. These technologies are enabling a new platform of data-ingested, inter-connected and automated services that will drive new levels of convenience and efficiency. Similarly, they require a new approach to the workforce and a new set of skills – particularly when it comes to securing these new services.

To innovate and differentiate, multinational organisations cannot afford to stand still. They need to take on risk, but they face constraints regarding investment capacity, the organisation's risk appetite and their ability to manage change; not just within the organisation but also across the extended enterprise across the ecosystem that includes third-party suppliers, channels and customers. Organisations that can manage that proactively, as opposed to being reactive, will have a better chance of staying ahead. This depends on the strength of leadership, their resolve and the organisation's ability to navigate through complex change.

The observation is that some organisations are starting to use risk management as a strategic tool and as an enabler of business performance rather than just a check-the-box compliance exercise. The concern is that the risk management capabilities are lagging behind the ability of companies to take on more opportunities and that there are still gaps to be addressed. On the positive side, it is not often that organisations make decisions to invest in areas they think will help them do a better job of managing risk, such as in the areas of cyber and reputation risk. There are progressive executives who recognise that better risk management helps to differentiate and drive performance, rather than just being on the defence.

In essence, there is a diverse spectrum of risks, which are often inter-related, and they are continually expanding. In most cases, all pose a risk to brand and reputation. As an example, with the digitisation of businesses, disruptive innovation is occurring across vertical industries. Also, other external risks created by the complexity of supply chains and third-party involvement in business operations and further exacerbated by social media.

One other layer of risk relates to employees' conduct and actions, and insider threats are a crucial dimension of that, particularly in large organizations that operate in different businesses and different jurisdictions besides those in the government sector. There are instances in organisations where top leadership tries to foster a culture of integrity and compliance, growth can bring new challenges and expectations, and that can create a culture where some people inadvertently create new risks and at other times take liberties. Legal frameworks for governing cyberspace have been slow to develop but are beginning to take shape. These new frameworks will have a significant impact on the cybersecurity landscape both here and abroad.

Clinching the initiative on cybersecurity: The 3-point checklist

With large amounts of money in play and cyber-resiliency affecting a growing range of business issues—business continuity, customer privacy, and the pace of innovation, to name just a few—it is clear that current operating models for combating attacks are not up to the task. More often than not, they are compliance driven, technology-centric and grounded in collaboration across business functions. It is imperative that active engagement by the CEO and other senior leaders who understand the broad strategic risks of inaction can catalyse change. We have developed a checklist of practices that can help organisations as they re-map the boundaries of their cybersecurity operating models:

1. **Prioritise information assets by business risks**. Most companies lack sufficient insight into the precise information assets they need to protect—for example, the damage that might result from losing the intellectual property behind a new manufacturing process. Business leaders need to work with cybersecurity teams to assess and rank business risks across the value chain.

2. **Differentiate protection by the importance of assets.** Assigning levels of controls, such as encryption and more rigorous passwords for lower-value assets, will allow management to invest time and resources in protecting the most strategic information.

3. **Integrate security deeply into the technology environment to achieve scale**. Executives need to instil the mindset that security is not something bolted onto projects. Instead, every facet of the growing technology environment— from developing social-network applications to replacing hardware—needs to be shaped by the awareness of new vulnerabilities.

Evidently, cyber threats and attacks are growing and will continue to do so. With the pace at which businesses have been evolving, there is much more to be done to protect against cyber threats. Financial crime is also likely to be a continued challenge because of the connected economies, digital payment systems, e-commerce as well as other factors.

The primary step is building awareness at the C-suite and the board levels, and making cybersecurity risk part of a recurring agenda. Organisations have to get out of being just reactive to issues when cyberattacks occur and be better prepared. This step begins with corporate strategy and making cyber awareness part of that. Furthermore, it is critical to push awareness and preparedness down into operations and day-to-day business activities, with an emphasis on the people, processes and technology that permeate the organisation as they are part of its defence against cyber threats. The need to plan for cyberattacks and identifying what actions have to be taken, and by whom, are critical and so is developing the leadership and talent required to manage cyber risks. Furthermore, there is a need for greater awareness of industry norms, including culture and perception on issues such as third-party cyber risks.

A large number of organisations also need to think about incorporating cyber risk within a broader risk management framework—in particular for escalation around risk appetite, threshold reporting and related issues. Some may want to consider assessing their desired position on the maturity model continuum of low, moderate and high capability. Not every organisation may want to be at the highest level of maturity, however, because it could be infeasible or unaffordable. A framework that starts with strategy, builds out basic security measures, and then addresses vigilance and resilience capabilities is a model that many organizations can benefit from. It is a new world out there – one filled with opportunity but also with a new kind of threat – a threat more ubiquitous than any we have ever known and with repercussions we can only imagine. With that pervasive threat comes a new found responsibility for us all.

The ability to have the agility to react and proactively start to adapt based on trends is going to be crucial. In fact, many boards are beginning to do a commendable job (although a long way to go) now that they have been sensitised to that. Scenario planning has started to include things like cyber risks, third-party risks and other dimensions of the business. Many organisations are now integrated so tightly into their ecosystem that they cannot survive should a critical supplier go out of business or have a brand or delivery issue. It is heartening to know that scenario planning has changed dramatically from a purely financial management exercise to a more holistic look at nonfinancial measures, including brand, reputation and third-party risks.

It is fascinating to note that the same emerging technologies that are driving the need for cybersecurity skills also provide the means for developing engagement. Routine tasks such as analysing large volumes of security event logs can be automated by using digital labour and machine learning to increase accuracy, allowing cybersecurity professionals to focus on higher-level tasks, which are generally more exciting and rewarding.

For further information or clarifications, kindly contact:

Cecil Su
Director,
cecilsu@bdo.com.sg
+65 6829 9180

Three Strategic Approaches To Beat The Competition

Many a time, it is a zero-sum game in the business world. Your gains might be at the expense of others' loss, and vice versa. To be able to beat the competition is no longer simply a bonus, it is becoming more of a necessity for survival in the long run. Thus, how can a business beat the competition?

Go After Blue Ocean

The concept of Blue Ocean Strategy is familiar to many of us. Simply put, to create uncontested market space and make competition irrelevant. By breaking the value-cost trade off and reaching beyond existing demand and supply, companies would be able to avoid cutthroat competition in a bloody red ocean of competitors.
Take the circus industry, for example. Rise in alternative forms of entertainment such as video games, sporting events and increasing sentiment against the use of animals in circuses have resulted in a shrinking traditional circus industry. Under the situation, Cirque de Soleil did not take customers from the already shrinking industry that historically catered to children. Instead, it challenged the industry convention and created uncontested market for its own. It appealed to a whole new group of customers, i.e. adults and corporate clients who are prepared to pay a price several times as great as traditional circus. Cirque du Soleil nowadays has become a billion dollar business with more than 180 million spectators in more than 400 cities in over 60 countries.

Be Customer-Centric

The relationship between businesses and customers are constantly evolving, but there is one thing that doesn't change, that is customers' needs should always be put first and core of everything of what your business does.

Jeff Bezos, CEO of Amazon, often leaves a seat open at his conference tables to remind all people present

that the most important person in the conversation is the "customer". Also, from Kindle to drone delivery, all of Amazon's innovations are aimed at adding value to the customers. Furthermore, every manager at Amazon spends two days every two years at the customer service desk. This ensures that the company is listening to the customers and understanding their needs at every organizational level.

By understanding customers' needs and giving them what they need, your business is already on its way to beat the competition.

Focus on Quality

Could you image a muskmelon that costs $200 upwards a piece? It sounds insanely expensive for a piece of fruit, but this is how Sembikiya, a premium fruit store in Tokyo, beat the competition in traditional agricultural product space by making supreme quality their UVP. Muskmelons sold in Sembikiya are typically grown with the "one stalk on fruit" method, in which the superfluous fruits are removed so that they don't take away the nutrients. People know the extraordinary efforts that go into the making of a muskmelon, so they don't consider the price ridiculous. In this case, Sembikiya is no longer competing in the same league as the rest of the fruit sellers. Sembikiya's strong focus on supreme quality has made their success last for over 180 years since 1834.

Focusing on quality does not only work well on product, it works equally well on service. Richard Branson disrupted the airlines industry by launching Virgin Atlantic. At the time, major airlines, such as British Airways, were dominating the market. It made breaking into the airline industry extremely difficult. Virgin Atlantic differentiated itself by not only fulfilling customers' basic needs, but also introducing additional features such as hydrotherapy baths, in-flight messages, backseat video screens in every class, and free ice cream during movies. The launch of Virgin Atlantic proved to be a tremendous success for Virgin Group.

If your business has the right focus on market, customers and quality, no matter which industry you are in, it is possible to beat the competition, and be an industry disruptor and leader.

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For further information or clarifications, kindly contact:

Sonia Wang
Senior Consultant
soniawang@bdo.com.sg
+65 6828 9841

Goods And Services Tax Changes For The Fund Management Industry

Singapore has established itself as a leading global financial centre over the past few decades. To further strengthen Singapore's position as a hub for both fund management and domiciliation, the Monetary Authority of Singapore (MAS) is currently studying the regulatory framework for Singapore Variable Capital Companies (S-VACCs). S-VACCs are a new legal entity or structure designed for collective investment schemes that will accommodate a variety of traditional and alternative asset classes and investment strategies.

In the 2018 Singapore Budget, it was announced that a tax framework for S-VACCs will be introduced to complement the S-VACC regulatory framework and this includes extending the existing GST remission for funds to incentivise S-VACCs.

GST remission for funds

Generally, 7% GST is chargeable on fund management, custodian, and other services supplied by GST-registered suppliers to funds belonging in Singapore. Only GST-registered funds making taxable supplies are able to claim the GST incurred on its expenses. As some of the funds are not eligible for GST registration due to the type of investment activities made, the GST incurred on the fees charged would be an unrecoverable business cost to the funds.

A GST remission was introduced on 22 January 2009 to allow qualifying funds that are managed by a prescribed fund manager in Singapore to claim GST incurred on all expenses related to the fund's investment activities (except disallowed expenses) from 22 January 2009 to 31 March 2014 (both dates inclusive) at an annual recovery fixed rate. In the 2014 Singapore Budget, the GST remission was extended to 31 March 2019.

To qualify for the GST remission, the following conditions must be met:

- The fund must satisfy conditions for income tax concessions in Singapore as a Section 13C, 13G, 13R, 13X fund, of 13CA fund (with effect from 1 January 2014) or a designated unit trust or a unit trust included under the CPF[1] Investment Scheme (CPFIS) as at the last day of its preceding financial year.

- The fund must be managed or advised by a prescribed fund manager[2] in Singapore.

  Funds that meet the qualifying conditions are required to file a quarterly statement of claims to make the claims based on their financial year end. This allows funds that are not eligible for GST registration to mitigate the GST incurred while doing business in Singapore.

  With respect to S-VACCs, the above will take effect on or after the effective date of the S-VACC regulatory framework and MAS will release further details by October 2018.

How BDO in Singapore can assist

BDO in Singapore can help assess whether a fund is eligible for the GST remission (under the existing income tax concessions or under the S-VACC). BDO in Singapore can also assist funds with filing of the quarterly statement of claims for the purpose of making the GST claims.

For further information or clarifications, kindly contact:

Eu Chin Sien
Executive Director - GST
chinsien@bdo.com.sg
+65 6828 9186

Yvonne Chua
Director - GST
yvonnechua@bdo.com.sg
+65 6828 9623

[1] *Central Provident Fund – A mandatory social security savings scheme funded by contributions from employers and employees.*
[2] *One that holds a capital markets licence under the Securities and Futures Act (Cap. 289) for fund management or one that is exempt under the Act from holding such a licence .*

CONTACT US

BDO LLP
600 North Bridge Road
#23-01 Parkview Square
Singapore 188778
Tel: +65 6828 9118
Fax: +65 6828 9111
info@bdo.com.sg

www.bdo.com.sg

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