

Overview of corporate income tax

SGP ¶3-200 Introduction

Taxable entities

In the absence of tax incentives, Singapore-registered corporations and branches of foreign corporations are taxed at the prevailing corporate rate. Corporate members of a partnership are taxed at the same rate on their share of the partnership's profits.

Tax rate

Singapore has been gradually lowering its corporate tax rate in an attempt to attract and stimulate investment. From the year of assessment 2005, both resident and non-resident corporate taxpayers pay tax at a rate of 20% on their corporate profits, unless they qualify for tax exemption or a concessionary tax rate (usually 5% or 10%). In addition, with effect from year of assessment 2002, a new partial exemption regime was introduced, whereby the following chargeable income of a company is exempt from tax:

- three-quarters of the first S\$10,000; and
- one half of the next S\$90,000.

In addition, to help entrepreneurs in their new ventures, a full exemption scheme is introduced for an initial period of five years from year of assessment 2005 to year of assessment 2009. A newly incorporated company will have its first S\$100,000 of chargeable income fully exempt from tax for its first three years of assessment that fall within the said period.

The above partial and full exemptions do not apply to income from Singapore taxable dividends.

Tax treatment of corporate dividends

Imputation system

Up until 31 December 2002, Singapore applied an imputation system in relation to dividends paid by corporate entities. Under such a system, tax paid by a Singapore resident company represents a prepayment of the tax ultimately payable by its shareholders on the profits it makes. This is known as a full imputation system, since all tax paid by the company is effectively imputed to the shareholder to the extent that dividends are paid to him out of its taxable profits. Such dividends are taxable in the hands of the shareholder; and to the extent that the personal tax payable by him on that dividend exceeds the corporate rate, he will pay a top-up of tax. To the extent it is lower, he will receive a credit to be set against his other tax liabilities for that year, or where his other liabilities are insufficient, he will earn a refund. Table 1 provides an example.

Table 1

Company level	S'000
Corporate profits	100.00
Tax @ 22%	<u>(22.00)</u>
Profit after tax (available for distribution)	<u>78.00</u>
<i>Shareholder</i>	
Dividend	78.00
Imputation credits	<u>22.00</u>
	<u>100.00</u>
Tax at (say) 18%	18.00
Tax credit	<u>(22.00)</u>
Refund/credit against other tax liabilities	<u>(4.00)</u>

Generally speaking, this is an equitable position as the corporate profits are only taxed once, initially at the corporate rate, but with an adjustment, ultimately, by reference to the shareholder's personal marginal rate. This is known as a two-tier or imputation system.

From a corporate perspective however, the system is stodgy and hampers the flow of dividends back to shareholders. This is because corporate profits have to be taxed first before the necessary tax credits are created to enable a dividend payment. Alternatively, corporate tax liabilities are accelerated, through a franking deficits mechanism (known as a section 44 charge), to enable the payments. Dividends flowing through a corporate chain are particularly hampered by this feature, since the dividends have to be taxed at each corporate level, a process which takes a year at a time, before they can be passed on without the section 44 charge.

One-tier system introduced from 1 January 2003

With effect from 1 January 2003, the existing imputation system is to be scrapped and replaced by a "one-tier" system, under which profits are taxed at the corporate level only. Dividends are therefore exempt from further tax when paid out to shareholders. This is the model currently adopted by Hong Kong.

Reasons for the change

In their earlier recommendations to the Minister, the Taxation Sub-Committee of the Economic Review Committee gave three primary reasons why they believed a change was required. The first was that it will facilitate Singapore's use as a holding company location, as it allows an efficient flow of dividends up through the corporate chain. The second was that the imputation system as currently configured is simply adding complexity and potentially tax avoidance opportunities in an increasingly complex business environment. And finally, because the interaction with exempt dividend provisions under the tax incentives legislation causes an unnecessary compliance burden on companies.

It is not entirely clear that a move to a one-tier system is the only means of easing the dividend flow through corporate chains. This can be achieved quite simply and effectively by allowing tax credits attaching to dividends to go immediately into the recipient's franking account, so that a dividend can pass-up through the chain almost instantaneously, as is the case in Malaysia.

Given also the extremely complex tracking requirements under the transitional provisions (see below), it would appear that what has been created is significantly more complex and burdensome than what it replaces.

It is the second reason, however, which raises some interesting questions as there is clearly a concern, presumably from the Inland Revenue Authority of Singapore's side, that tax credits can be effectively sold, thereby causing the IRAS to make refund payments to entities who had bought the credits at a discount. It is not clear however that this abuse is so widespread as to merit a complete revamping of the system. On the other hand, there is little doubt that the changes, taken in isolation, will be revenue positive as a result of the denial of tax credits to individuals, and, in certain cases, to companies (see below).

On the other hand, one point touched upon in the Committee's report, but not developed or mentioned by the Minister, is the interaction of this proposal with the introduction of a group relief system (see below). An imputation system does not fit particularly well into a group relief or consolidated filing environment, since the availability of the relief may mean that companies with distributable profits will have

paid no tax, and will thus have created no franking credits. The one-tier system solves this issue at a stroke.

Implications for shareholders

As noted above, there are a number of issues worth mentioning in the context of a one-tier system. These are discussed below:

(1) Individual shareholders

Overall, the migration to the new system will be revenue positive for the Inland Revenue Authority of Singapore. This is because from year of assessment 2003, the highest marginal personal tax rate is the same as the corporate rate (22%). An imputation system would therefore result in one-way traffic, namely a tax credit coming back to all individual resident shareholders across the board. Under a one-tier system, no rebates or credits are given.

This feature will give rise to an issue for small businesses. This is because the one-tier system will mean that all shareholders effectively get taxed at the corporate tax rate on profits made by companies whose shares they own, irrespective of their marginal rates of personal tax. In particular, a small entrepreneur who has decided to incorporate his business, will be taxed as if he was a comparatively high rate taxpayer, even though his earnings may remain modest for some time. His options therefore are to consider not incorporating, or to ensure that he pays himself by way of salary and bonus rather than dividend, to ensure he converts corporate profits into income taxable on him directly.

(2) Retirement savings

There may also be an impact on retirement savings from two perspectives. The first is when the retiree earns income from Singapore shares, and where his level of income allows him to pay tax at modest rates. The proposed system will suddenly cause him to be taxed at the corporate tax rate, which may have a massive impact on his savings.

The second is in relation to the Supplementary Retirement Scheme ('SRS') which was introduced in 2001. Currently, Singapore dividends paid into the SRS are taxable on receipt, to allow a claim for tax credit. If the dividends are to be exempt, there will be no tax credit available. In addition, one half of the dividends will be taxed on retirement. This is an anomaly that needs to be resolved.

(3) Life insurance products

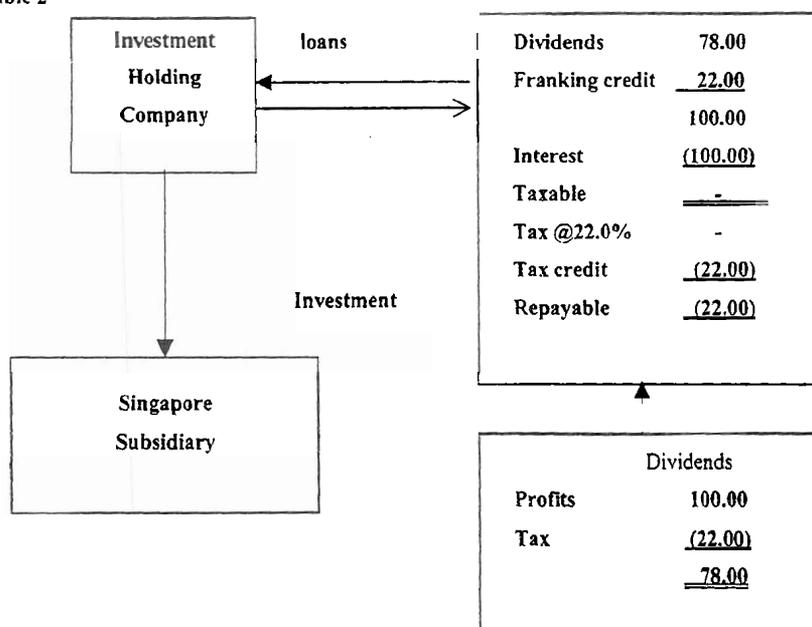
The income of the life insurance fund of an insurance company that is attributable to policyholders is taxed currently at a rate of 10%, which includes Singapore dividends. The changes to the dividend system raise the question as to whether changes may be needed also in this area so as not to disadvantage the life insurance industry.

(4) Investment holding companies

The exemption for dividends may also have a serious impact on investment holding structures under which an investment holding company has borrowed to acquire shares in a Singapore resident subsidiary. Currently, interest expense on the borrowings can be used to set off against the (taxable) dividend income from the

subsidiary, and a refund of the franking credit attaching to the dividend obtained. See Table 2.

Table 2



The net effect is a form of group relief, in that the tax paid by the subsidiary is recovered by the parent. Net group profits are therefore \$nil.

Where such dividends are exempt, as is the case under the one-tier system, then technically, there is nothing to deduct the interest expense from, and it is wasted. In this context, it has been suggested to the IRAS that the group relieving provisions (see SGP ¶21-500 "Group relief system") may allow a direct set off of the interest expense against the corporate profits of the subsidiary, as is the case in other jurisdictions (United Kingdom, New Zealand). They have confirmed, however, that this will not be allowed.

Without group relief, the only means of acquiring an interest in a subsidiary in a tax efficient manner is either for the holding company to borrow to buy the business and undertaking of the subsidiary, or by forming another subsidiary who borrows to do so. Buying shares with borrowed money will no longer be an option, or at least not an attractive one. New subsidiaries can only be financed effectively by debt, if the parent company has to borrow to set them up.

If this deductibility restriction is not intended, then there will need to be a re-thinking of the current IRAS practice in relation to investment holding companies and in particular the implications for companies falling under sec 10E of the ITA.

Singapore groups of companies therefore will need to take a close look at their group structures in this context. This is an area of extreme importance not only for groups with existing investment holding company structures, but also groups with complex financing arrangements, where investments had hitherto been regarded as “income producing” for interest deductibility purposes. It also changes the entire landscape of acquisition structures where significant investment is to be made in other companies or businesses.

(5) Capital reduction and share buy-back provisions

The proposed changes will also have an impact on the capital reduction and share buy-back provisions found in the ITA. These provisions deem payments made to shareholders under these arrangements to be dividends in certain cases. This legislation will therefore become largely redundant under the proposed system. If nothing else, this will make the whole process more straightforward, even if, again, it denies shareholders otherwise valuable tax credits.

(6) Capital gains

One interesting feature of the proposed one-tier system is in relation to capital gains. Currently, gains of a capital nature are not subject to tax in Singapore. However, they can be effectively taxed under an imputation system if they are paid out to shareholders by way of a dividend. This is because capital gains by definition do not create franking credits. However, all dividends need to be franked (or exempted under specific legislation). A distribution of capital gains will thus lead to a franking deficit charge under sec 44 of the *Income Tax Act* or will involve a utilisation of franking credits created by other taxable income (which then becomes short of franking credits itself).

It has been confirmed that the one-tier system allows the tax neutrality of capital gains to be preserved all the way through to the shareholder. However, in this case, additional attention may be paid by the IRAS as to whether, in their view, the gains are truly capital in the first place.

(7) Preference dividends

Under existing tax law, a company cannot use any of its exempt dividend balances for the purposes of paying dividends of a “preferential nature” (see SGP ¶6-400 “Salient features of incentives”). The move to a one-tier system would, on its own, have made this restriction redundant. However, under the provisions of the *Income Tax (Amendment) Act 2002*, preference dividends paid out of exempt balances were treated as interest income in the shareholder’s hands, and if it so elected, as interest expense of the company. This would have had the effect of restricting the ability of companies to stream their different types of income to different taxpayers. It did however create some interesting complications in the system, and seemed certain to perpetuate the need to track exempt income or income which had been the subject of tax at reduced rates. It is likely for this very reason that these deeming provisions were removed by the *Income Tax (Amendment) Act 2003*.

Section 44 transitional rules

To help resident companies move into the new taxation system smoothly, transitional provisions will operate between 1 January 2003 and 31 December 2007 to allow companies time to use up their residual franking balances. All companies will migrate automatically to the new system from 1 January 2008. Any company wishing to go straight onto the one-tier system can opt to do so however, at any time, by abandoning its existing section 44 franking balances.

During this transitional period, section 44 franking credits accumulated by a company as at 31 December 2002 can be passed on to its shareholders until 31 December 2007. However, corporate shareholders cannot use the attaching franking credits to pay franked dividends onto their own shareholders. Accordingly, franking credits stranded at second-tier subsidiaries at 31 December 2002 will be of no value going forward unless the parent company has excess expenses which can be set off against the taxable dividend income.

In relation to foreign shareholders, the new system is unlikely to make any difference, since the extent to which a dividend has been franked for Singapore tax purposes (or not) should have no effect on the level of underlying tax, if any, that is available. Section 44 balances are already therefore of no use.

A circular has been prepared by the IRAS on the one-tier system, which is mainly devoted to the transitional rules, as they are by far the most complex part. To the disappointment of taxpayers, the circular not only confirms certain disadvantages of the new system (for example the attribution of expenses relating to dividends as discussed above) but also retains the administrative burden of section 44 by requiring the tracking of section 44 balances during the transitional period regardless of whether companies have opted for the new system or not.

A comprehensive analysis of the provisions is given at the IRAS website www.iras.gov.sg.

Law: sec 10E, 10I, 10J, 10K, 44, 44A and 46 of the *Income Tax Act*; *Income Tax (Amendment) Act 2002*; and *Income Tax (Amendment) Act 2003*.

SGP ¶3-205 Basis of liability to tax

The statutes that govern taxation of income in Singapore are:

- (1) the *Income Tax Act* ("ITA"); and
- (2) the *Economic Expansion Incentives (Relief from Income Tax) Act* ("EEIA").

These statutes are supplemented by rules, regulations, orders and notifications which are made or prescribed by the relevant authorities.

In Singapore, tax for each year of assessment is imposed on income earned in the preceding year. The year of assessment (ie the year in which tax is computed and assessed) coincides with the calendar year. Thus, the year of assessment 20X2 refers to the calendar year from 1 January 20X2 to 31 December 20X2. However, tax assessed in this year will be income earned in 20X1 (the basis period).

The basis period is the period of income that is subject to tax for the relevant year of assessment. This is normally the preceding calendar year. However, for trade or business

income, the accounting period ending in the preceding calendar year may be taken as the basis period if the accounting period is different from the calendar year.

Example:

Company A closes its accounts on 30 June. The basis period for trade profits and interest on fixed deposit (non-trade) derived by Company A for year of assessment 20X3 would be as follows:

Basis period

Trade profits	1 July 20X1 to 30 June 20X2
Interest	1 January 20X1 to 31 December 20X2

Where the accounting period for the first set of accounts exceeds 12 months, the income will be pro-rated.

As part of a series of measures introduced to simplify tax rules and procedures, the IRAS has granted a concession whereby taxpayers may elect to have their non-trade source income assessed to tax on an accounting period basis. This will be administered as a concession from year of assessment 2005 to year of assessment 2008, while legislative effect will be given to the change with effect from year of assessment 2009. Using the earlier example as an illustration, the basis periods for the trade profits and interest income will be aligned under the new treatment, ie the basis period will be 1 July 20X1 to 30 June 20X2 for both types of income.

Law: *Income Tax Act*; and *Economic Expansion Incentives (Relief from Income Tax) Act*.

SGP ¶3-210 The central charging section

Singapore adopts a semi-territorial basis of taxation. Section 10(1) of the ITA is the central charging section and provides for the imposition of tax as follows:

“Income tax shall . . . be payable. . . for each year of assessment upon the income of any person accruing in or derived from Singapore or received in Singapore from outside Singapore. . .”.

There are thus effectively two bases of taxation in Singapore, ie

- (1) the “territorial” basis which is reflected in the phrase “accruing in or derived from”; and
- (2) the “receipts” basis imposed on foreign income as reflected in the phrase “received in Singapore from outside Singapore”.

This is to be contrasted with the pure territorial basis applied in Hong Kong, where income sourced outside of the territory is not taxable at all, whether remitted or not.

There are provisions in the ITA governing the basis of treating foreign income as received in Singapore. Income derived from outside Singapore is regarded as received in Singapore, whether or not the source from which the income is derived has ceased, if it is:

- (a) remitted to, transmitted or brought into, Singapore;
- (b) applied in or towards satisfaction of any debt incurred in respect of a trade or business carried on in Singapore; or

(c) applied to purchase any movable property which is brought into Singapore.

Under sec 10(1), the words “any person” shows that this section does not distinguish between a resident or a non-resident person. Section 10(1) thus provides the basis of charge to Singapore income tax on the income of non-residents accruing in or derived from Singapore. However, this section must be read together with the specific provisions dealing with the taxation of non-residents in respect of specific categories of income. Where the non-resident is resident in a treaty country, it is necessary to consider the impact of the treaty provisions on his tax position.

Law: sec 10(1) of the *Income Tax Act*.

SGP ¶3-215 Income subject to tax

Income tax in Singapore is “schedular” in nature, ie only the income from one of the sources mentioned within sec 10(1) of the ITA is taxable. A taxpayer’s gains or profits will be subject to income tax if they are derived from one of the following sources:

- (1) trade, business, profession or vocation income;
- (2) dividends, interest or discounts;
- (3) income from any pension, charge or annuity;
- (4) rents, royalties, premiums and any other income arising from property; and
- (5) any other gains or income of an income nature.

These heads of charge embody four sources which give rise to income, with the last head being a “catch-all provision”. Unless the gains made by a taxpayer are from one of these sources, no tax can be imposed on what is received.

Law: sec 10(1) of the *Income Tax Act*.

SGP ¶3-220 Taxation of capital gains

There is no capital gains tax in Singapore. Neither are capital gains subject to income tax.

However, where a company derives gains of a recurring nature, it may be viewed as carrying on a business and the gains will be taxed as trading profits. Hence, the importance of the distinction between income and capital gains. In practice, such distinction is sometimes unclear, and this has led to various disputes between the taxpayers and the tax authorities. The IRAS takes an aggressive position on this generally, thus consideration should be given to this aspect in all disposals of shares and real estate.

While capital gains are not taxed, profits from short-term gains from the sale of real property were, until 13 October 2001, subject to income tax. This tax was introduced in 1996 to curb property speculation in Singapore. Generally, gains on property sold within three years of purchase were taxable as income. The proportion taxable decreased by a third with each year added to the holding period. Besides real property, the tax applied to short-term gains from the sale of shares in a private company that held 75% or more of its assets in the form of real property or shares in real property companies. As noted above, these provisions were made inoperative from 13 October 2001. Sections 10F and 10G were repealed in the *Income Tax (Amendment) Act 2002*.

Law: sec 10F and 10G of the *Income Tax Act*; and *Income Tax (Amendment) Act 2002*.

SGP ¶3-225 Exempt income

The following income/receipts of a company or other institutions are exempt from income tax in Singapore under the ITA:

- (1) income derived by institutions, authorities, funds and other entities listed in the First Schedule of the ITA;
- (2) income of approved *bona fide* friendly societies and co-operative societies registered under the *Co-operative Societies Act*;
- (3) receipts of an approved charitable institution (conditions apply);
- (4) non-business/trade income of a Singapore-registered union;
- (5) income of non-residents derived from trading in Singapore through consignees of specified commodities (rubber, copra, pepper, tin, tin-ore, gambia, sago flour and cloves) produced outside Singapore;
- (6) approved charter payments made to non-residents by an approved international shipping ("AIS") enterprise;
- (7) investment income of approved pension/provident funds or societies;
- (8) income derived by asian currency units ("ACU") of financial institutions and approved securities companies ("ASC") from approved syndicated offshore credit/underwriting facilities or syndicated guarantee facilities;
- (9) certain interest and related payments derived by non-residents (see SGP ¶3-275);
- (10) interest on government loan stocks listed in the Fourth Schedule of the ITA, provided that the interest does not form part of the trading receipts of the recipient, such as in the case of a bank or a finance company;
- (11) remittance of certain overseas income by residents (subject to approval);
- (12) income derived from the operation (including charter and towage/salvage operations) of Singapore ships outside the Singapore port limit;
- (13) income of an approved international ship-owner derived from the operation of foreign ships outside Singapore port limits;
- (14) prescribed income of non-residents arising from funds managed by any fund manager in Singapore;
- (15) certain income of approved foreign trusts (the exemption also extends to the beneficiaries of such trusts and to income derived by foreign trusts through an eligible holding company);
- (16) prescribed income of approved venture companies;
- (17) dividends paid out of exempt income of ACUs, AFMs and securities companies, companies insuring or re-insuring offshore risks, corporate futures members of the Singapore Exchange, approved headquarters companies, oil trading companies, FTCs, international commodity trading companies, offshore leasing companies, trustee companies, members of commodity futures exchange, art/antique dealing companies, cyber traders and global trading companies;

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- (18) dividends paid out of income from qualifying debt securities (“QDS”);
- (19) dividends paid out of exempt income of approved investment companies;
- (20) dividends paid out of exempt foreign income (including foreign income for which tax credit has been given);
- (21) dividends paid by a Singapore company that has moved to the one-tier system (see SGP ¶3-200); and
- (22) foreign-sourced dividends, branch profits and service income remitted to Singapore on or after 1 June 2003, where the foreign income has been taxed overseas and is received from a foreign jurisdiction with a headline tax rate of at least 15%.

Detailed provisions may specify conditions for the tax exemption of income listed above.

Income may also be exempt under the various tax incentives under the EEIA. These are discussed in more detail in SGP ¶6-200.

Law: sec 13, First Schedule of the *Income Tax Act*; *Co-operative Societies Act*; and *Economic Expansion Incentives (Relief from Income Tax) Act*.

SGP ¶3-230 Deductions

Expenses are tax deductible only if they:

- (1) are incurred (need not be paid out) by the taxpayer during the basis period;
- (2) are wholly and exclusively incurred in the production of income (although income - need not necessarily be produced when these expenses are incurred);
- (3) meet the conditions for deductibility under the ITA; and
- (4) are not specifically disallowed under the ITA.

Section 14 of the ITA deals generally with the deductibility of expenses whilst sec 15 of the ITA deals with expenses which are specifically not deductible. Once an expense is denied under sec 15, it will not be deductible even if the expenditure satisfies the conditions stipulated in sec 14. In other words, in a conflict between these two sections, sec 15 would prevail.

Non-deductible expenses

Generally, these include the following:

- domestic or private expenses;
- expenses not wholly and exclusively incurred in the production of income; capital expenditure and capital losses;
- capital employed on improvements to assets; losses recoverable under an insurance or indemnity contract;
- rent or costs of repairs to premises not incurred in the production of income;
- income taxes paid or payable;
- GST input tax — when there is a failure to register for GST (where required to) or to claim the input tax (if entitled to do so);
- GST output tax borne by a GST-registered person;

- contributions to unapproved pension or provident funds;
- contributions in excess of statutory limits to approved pension funds;
- interest paid to non-residents by a person out of Singapore where withholding tax has not been paid;
- expenses incurred (directly or in the form of reimbursement) on motor cars; and
- rental and operating expenses of private hire cars.

Deductible expenses

Besides the general rules for deduction as mentioned above, there are specific deductions allowed under sec 14 of the ITA, which include:

- interest paid on moneys used to generate or acquire income;
- rent paid for business premises;
- cost of repairs to plant, machinery or premises and the cost of replacing implements and utensils;
- bad and doubtful debts arising from trading receipts of the company; and
- contributions to approved pension or provident funds (including the Central Provident Fund).

A more detailed discussion of tax deductions is provided in SGP ¶10-100.

Law: sec 14 and 15 of the *Income Tax Act*.

SGP ¶3-235 Tax depreciation

Initial and annual allowances

Depreciation charged to the accounts in arriving at the accounting profits is a capital expense not deductible for tax purposes. However, the ITA provides for a claim for tax depreciation (known as “capital allowances”) on certain assets as described below.

(1) Industrial buildings

Industrial buildings allowance may be claimed for qualifying capital expenditure incurred on the construction of an industrial building. An industrial building is defined in the ITA as a building or structure that is used in a qualifying trade as defined in the ITA.

The allowances given are as follows:

- initial allowance of 25% of the cost of construction (excluding the cost of land) in the year of assessment relating to the basis period in which the expenditure was incurred; and
- annual allowance of 3% of the cost, until the total cost has been allowed (normally 25 years).

Buildings that qualify for industrial buildings allowance are mainly factories, mills or similar premises. Certain warehouses qualify, as do buildings used by certain service industries and research and development organisations. Hotels (except for an approved hotel on the island of Sentosa) and commercial, residential or office buildings do not qualify.

(1a) Newly-constructed buildings

Where a new industrial building is not constructed by the taxpayer but purchased ready-built, the base amount on which the allowance is calculated is the original construction cost or the net purchase price, whichever is the lower.

(1b) Second-hand industrial buildings

An annual allowance based on the residue of expenditure (ie residue of qualifying expenditure over the tax depreciation claimed or deemed to have been claimed by the previous owner) is given so that the amount allowed is either:

- (a) equally spread over the balance remaining of a term of 50 years from the date of first use; or
- (b) at an annual rate of 3% on a straight-line basis, whichever produces the higher allowance annually.

A second-hand purchaser is not entitled to an initial allowance.

(2) Plant and machinery

Capital allowances on plant and machinery are granted only to persons carrying on a trade, business or profession. "Plant and machinery" may be defined as the fixed assets employed in the company's business which fulfil a functional role in the business activity and which are not merely part of the setting of a business or trade.

The allowances given, on due claim, are as follows:

- initial allowance of 20% of the cost of the asset; and
- annual allowances for the remaining cost after deducting the initial allowance, on a straight-line basis over the working life of the asset as specified in the Sixth Schedule to the ITA. The specific working life varies from five to 16 years, depending on the nature of the asset.

In lieu of the initial and annual allowances, an accelerated capital allowance of 33.33% per annum is available for a consecutive period of three years on all machinery and equipment except motor cars, motorcycles and light-goods vehicles.

Further, an immediate 100% allowance claim is also available for certain assets such as computers, prescribed automation equipment, robots, standby office and factory generators, highly efficient pollution-control (including noise and chemical control) equipment and energy-efficient equipment.

The *Income Tax (Amendment) Act No 37/2002* amends the ITA to deem a website as plant or machinery. Where such a website is used for the purposes of a trade, business or profession carried on by a taxpayer, he may claim 100% capital allowances in respect of the capital expenditure incurred by him on the provision of that website. This takes effect from 3 May 2002.

As yet another part of a series of measures introduced to simplify tax rules and procedures, the IRAS issued a circular on 14 September 2004 announcing that an immediate 100% write-off will be allowed for assets costing not more than S\$1,000 each, subject to a maximum aggregate claim of \$30,000 annually. This takes effect from year of assessment 2005. A copy of the circular is available on the IRAS website at www.iras.gov.sg.

Carry-forward of unutilised capital allowance

Capital allowances that are not fully utilised against the current income may be carried forward for deduction against future income from all sources, provided:

- (1) the trade for which the assets were acquired has not ceased; and
- (2) the continuity of beneficial ownership test is satisfied (see SGP ¶3-255 “Tax losses”).

The continuity-of-trade test is not required for carry-forward of unabsorbed industrial building allowances, but the relevant source of income must not cease to exist. This is on the basis that a receipt of rental income may not constitute the carrying on of a trade or business.

Balancing adjustments

When an asset in respect of which tax depreciation has been granted ceases to be used in the trade, a balancing adjustment is made. The balancing adjustment is computed as the difference between the sales proceeds and the tax depreciated (written down) value of the assets. The gain (balancing charge) on realising depreciable assets is taxable as ordinary income, but only to the extent of any allowances previously given (depreciation recapture). To the extent that the sales proceeds exceeds the original cost, the profit is a capital gain and therefore outside the scope of tax.

Conversely, a balancing allowance (tax deduction) will be granted to the taxpayer when the tax written down value of the asset exceeds the disposal value.

Controlled sales

When there is a sale or transfer of plant or machinery between related parties, the parties may elect for the transfer to be made at tax written down value. No balancing allowance or charge arises for the seller. No initial allowance is given to the buyer. Annual allowances are given to the buyer as if no sale or transfer had taken place.

Intangible assets

Capital expenditure incurred on the acquisition of approved intellectual property rights for use in a trade or business may be written down over five years for tax purposes. These rights include patents, copyright, trademarks, registered designs, geographical indications and valuable trade secrets or information.

For acquisitions of intellectual property between 1 November 2003 and 31 October 2008, the claim for writing down allowances for capital expenditure incurred has been made broad-based. Prior approval is no longer required, though the claimant is required to submit a declaration form to the IRAS, with a copy to the Economic Development Board of Singapore. The claim for the writing down allowances is subject to the condition that the taxpayer retains the legal and economic ownership of the intellectual property. Third party independent valuation reports for acquisitions above certain values must also be submitted to the tax authorities.

Telecommunication submarine cable systems

Capital expenditure incurred on the acquisition of indefeasible rights to use telecommunication submarine cable systems may be written down over a period of five years. This applies with effect from year of assessment 2004.

Leased assets

Accounting convention differentiates between a finance lease and an operating lease. A finance lease is a lease that transfers substantially all the risks (eg technological obsolescence) and rewards (eg gain from appreciation in value) incidental to ownership of an asset to the lessee, whether or not title is eventually transferred. A lease that is not a finance lease is an operating lease. Whether a lease is a finance lease depends on the substance of the transaction rather than the form of the contract.

Finance leases are normally non-cancellable and secure for lessors the recovery of their capital outlay plus a return for the funds invested.

For the lessee, an asset under a finance lease is reflected in the financial statements in the same way as depreciable assets that are owned. For the lessor, the asset is recorded as a receivable. On the other hand, an asset under an operating lease is not reflected as an asset in the financial statements of the lessee; instead, the rental is a charge to income. The asset is recorded as property, plant or equipment by the lessor.

For tax purposes, a finance lease is treated as a purchase of a fixed assets by the lessee under a deferred payment arrangement if any one of the following conditions exists:

- (1) the lessee is given an option to purchase the leased asset;
- (2) the leased asset is limited-use property;
- (3) the asset in a sale-and-leaseback transaction had been previously used by the lessee;
- (4) lessor and lessee are related, and certain conditions are not satisfied; or
- (5) the lease is a leveraged lease.

The principal thrust of the legislation is that it is the lessee, rather than the lessor who is entitled to the capital allowances as if he had bought the assets under a hire purchase arrangement. Interestingly, such transactions are, in practice, treated as such for all purposes of the ITA, despite the fact that the legislation only refers to the treatment of capital allowances.

In determining the income of the lessor, the sales price and rental of a leased unit must be the open-market value. In addition, depreciation allowances claimed in respect of finance leases may be quarantined in certain cases, under complex rules. There are separate rules for deducting depreciation allowances and tax losses against lease income taxed at the reduced rate of 10% under certain fiscal incentives.

Overseas plant & machinery

An increasing form of business model used in Singapore is where the manufacturing arm of a company is situated in lower-cost areas in the region while the Singapore company undertakes high value-added or knowledge-intensive activities such as headquarters or marketing functions.

In recognition of the importance of the above model, an approved Singapore company may claim capital allowances on its plant & machinery that is being used by its wholly-owned subsidiaries outside Singapore. The plant & machinery must be used by the overseas subsidiary for manufacturing products that are sold to or through the Singapore company.

Law: sec 10 and 13A of the *Income Tax Act*.

SGP ¶3-250 Tax consolidation

Each company is taxed as a separate legal entity. Up until year of assessment 2003, there were no group taxation or group relief provisions in Singapore. However, a group relief system was introduced with effect from year of assessment 2003. This is dealt with in more details at SGP ¶21-500 “Group relief system”.

SGP ¶3-255 Tax losses

General principles

For a tax loss to be deductible, it must arise from the carrying on of a trade, business, profession or vocation. It must also be incurred on revenue account. Once these conditions are satisfied, the tax losses are deductible, not only against trade or business income, but also against income from other sources, eg dividends, interest and rents.

The loss relief is generally only due to the person who has incurred the tax loss. A tax loss may be carried forward in certain circumstances but it cannot be carried backwards. Tax losses cannot be surrendered to other entities in the same group (unless they qualify for group relief — see SGP ¶21-500 “Group relief system”), nor can they transfer with the business as they can in some countries.

Tax losses brought forward are claimed as a deduction on a first-in-first-out basis, with the earlier losses deemed to be utilised first.

Carry-forward of losses and capital allowances

The carry-forward and utilisation of tax losses and capital allowances are subject to the continuity of beneficial ownership test, ie the shareholders of the company are substantially the same as at the following relevant dates:

- For losses:
 - the last day of the year in which the loss was incurred (this is taken to be 31 December of the year in which the loss period ends even when a company’s accounting year ends on another date); and
 - the first day of the year of assessment in which the loss is sought to be utilised.
- For capital allowances:
 - the last day of the year in which the capital allowance arose (this is taken to be 31 December of the year of assessment in which the capital allowances arose); and
 - the first day of the year of assessment in which the capital allowance is sought to be utilised.

This means that the first date for capital allowances is always one year later than it is for tax losses.

Shareholders would be “substantially the same” if not less than 50% of the nominal value of allotted shares in the company was held by or on behalf of the same persons at the relevant dates. In practice, the tracing of the beneficial ownership has been known to extend to shareholders of the ultimate holding company, although it is not clear from the legislation that this should be the case.

Deduction for unutilised tax losses and capital allowances may be available even if there has been a substantial change in shareholdings, so long as the Minister of Finance is satisfied that the change is not for the purpose of obtaining a tax benefit or tax advantage. In such a situation, the tax losses and capital allowances can only be deducted against profits of the same trade or business. Historically, the waiver had been surprisingly difficult to obtain in practice, especially since the application for the waiver would only be processed when the tax losses and capital allowances were being utilised. However, in a bid to provide more certainty to taxpayers as well as reduce the administrative burden of having to extract old records to support the application, the IRAS announced in a Circular dated 7 August 2003, that the application for waiver of the shareholders' test will be processed even if the tax losses and capital allowances are yet to be utilised.

Law: sec 23, 23(4), 23(5), 37, 37(3), 37(12), 37(14) and 37(15) of the *Income Tax Act*.

ที่มา : David Sandison, Tax planning & Compliance in Asia Volume V., (The Netherlands:Kluwer law International,2005)pp.3-7,101 – 3-7,803.