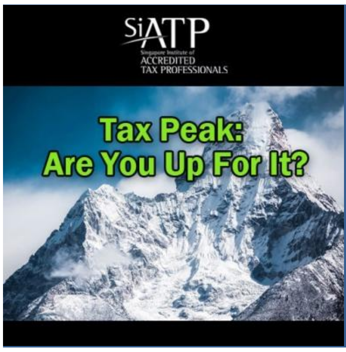

Tax Peak: Are You Up For It?

Journey through the Tax Peak Season Smoothly

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The peak season for corporate tax filing is here. Beyond the usual reminders for smaller businesses to ensure proper record keeping (especially for documents printed on thermal paper), reasonable remuneration to family members who are employees in family businesses, and accurate segregation of personal and private expenses, larger businesses also have a wide range of tax compliance issues to note as they get into the thick of it, amid a backdrop of greater scrutiny by tax authorities in the global marketplace.

The Singapore Institute of Accredited Tax Professionals (SIATP), working closely with officers from the Inland Revenue Authority of Singapore, has encapsulated some key Singapore corporate tax issues in the following article, for companies to note this tax season.

Classification of Income and Expenses for Incentive Companies

Companies on tax incentive schemes, such as the Development and Expansion Incentive (DEI), may enjoy concessionary income tax rates on their qualifying income. For such companies, it is essential to ensure that their income and expenses are classified into the correct tax categories in accordance with the relevant tax legislations and regulations. To allow for easy identification and proper classification into the various tax categories, companies are encouraged to assign distinct tax codes to each type of income and expenses.

In addition to segregating income and direct expenses (incurred to generate the income) to the correct tax categories, companies are also required to select an appropriate and reasonable allocation base to allocate the common expenses and capital allowances (CA) on the common fixed assets.

Once an allocation base is adopted, it is to be applied consistently unless there is a change in circumstances. As a good practice, companies should include a note in their tax schedules to justify the allocation base used.

Foreign Exchange Gains or Losses

Foreign exchange differences can arise from capital or revenue transactions. For income tax purposes, foreign exchange differences arising from capital transactions are capital in nature and hence, not taxable as income or deductible as an expense. On the other hand, foreign exchange differences arising from revenue transactions are revenue in nature and hence, taxable or deductible.

One common compliance error is the incorrect tax treatment applied on foreign exchange differences arising from revaluation of bank financing facility. Instead of simply assuming that all loans are capital in nature, companies need to know the actual usage of their banking facility when determining whether the foreign exchange differences arising from the banking facility or loan is capital or revenue in nature.

Motor Vehicle Expenses

Tax deduction claims on any expenses incurred directly or indirectly (in the form of reimbursement) in respect of private cars are strictly disallowed, even if they are incurred for business purposes. If, instead of a reimbursement, a company provides a monthly car allowance to its employee for using his private car for business purposes, such expense would be deductible for the company (but taxable in the hands of the employee as a benefit-in-kind).

It should be noted that while expenses incurred to rent a private car (with or without driver) in Singapore are non-deductible, reimbursements paid to employees for taking public transport (for example, MRT rides, taxi rides and Uber/ Grab ride-hailing services) for business purposes are tax deductible.

Group Insurance

With effect from Year of Assessment (YA) 2013, insurance premiums relating to group insurance (for example, group insurance policies covering life, personal accident or critical illness) are not taxed in the hands of an employee as a benefit-in-kind if the company elects not to claim a tax deduction on such premiums in its corporate tax returns. This administrative concession is not applicable to investment holding companies and service companies providing routine services to its related companies that are on the cost plus 5% mark-up basis of assessment.

It should be noted that once an election is made, the same treatment should be consistently applied for all employees covered under the policy.

If the company wishes to claim deduction on the insurance premiums incurred, it will have to ensure that the amounts have been reported as benefits-in-kind in the employees' Form IR8A.

Lee Woon Ling, Principal Tax Officer, Inland Revenue Authority of Singapore, highlighted on IRAS' assessment process and risk-based approach to tax assessment.

Interest Expense

Interest expenses attributable to non-income producing assets (such as vacant properties acquired for long-term investment) are not tax deductible. Where the company is unable to identify and track the use of an interest-bearing loan to specific assets, the "total asset method" should be applied to attribute the interest expense relating to the loan to the income-producing and non-income producing assets.

A typical mistake involves companies claiming a tax deduction on interest expense relating to investment in shares and securities that yielded tax-exempt dividends. As such dividends are tax exempt, interest expense attributable to them will have no deduction value and should be added back.

Demolition or Dismantling Costs

Demolition or dismantling costs (incurred to remove existing assets which are installed at the business premises during the course of or prior to renovating the premises) are generally capital expenditure disallowed under section 15(1)(c) the Income Tax Act (ITA), and hence non-deductible for tax purposes.

However, if the costs are incidental to the provision of specific assets or other categories of expenditure under sections 14(1)(c), 14Q, 19 or 19A of the ITA ("categories of expenditure"), such cost may be claimed as part of the expenditure in that particular category of asset or expenditure if they can be specifically identified. Otherwise, it may be apportioned to the various categories of expenditure using a reasonable and consistent allocation method (for example, the total cost method).

Yap Zhi Hui, Tax Specialist, Inland Revenue Authority of Singapore, shared insights on ways to improve tax compliance by enhancing internal controls, record keeping and other areas.

Capital Allowance for Plant and Machinery Acquired Under Hire Purchase

In computing CA for plant and machinery acquired under hire purchase, companies should not claim CA based on the full cost of the plant and machinery.

Instead, CA should be claimed based on the principal repayments and deposits paid for that YA. Hire purchase interest and GST amount paid (if the company is GST-registered) should be excluded in the computation of the CA.

Tax Exemption for Foreign-Sourced Income

Singapore tax resident companies are subject to tax on foreign income received in Singapore unless the foreign income qualifies for tax exemption under the Foreign-Sourced Income Exemption (FSIE) regime pursuant to section 13(8) of the ITA. The qualifying conditions for FSIE are:

- i. foreign headline tax rate is at least 15%;
- ii. the foreign-sourced income has been subject to tax in the foreign jurisdiction, and
- iii. the tax exemption is beneficial to the Singapore resident company.

In determining whether a foreign income qualifies for the FSIE scheme, special care should be taken to ascertain whether the "headline tax rate" condition is met. Headline tax rate refers to the highest corporate tax rate of the foreign jurisdiction from which the foreign income is received. Dividend is considered to be sourced in the jurisdiction where the company paying the dividend is tax resident in. For example, dividends received from a company that is incorporated in the Cayman Islands (a tax haven country) but listed on the Hong Kong Stock Exchange (Hong Kong has a headline tax rate of more than 15%) may give the wrong impression that the dividends meet the headline tax rate condition.

In addition, companies should also ensure that sufficient documentation is maintained to substantiate that the "subject to tax" condition has been met.

Foreign Tax Credit

Foreign income earned by a Singapore resident company may be subject to tax in the foreign tax jurisdiction from which it is derived. The Singapore resident company may claim foreign tax credit (FTC) against the Singapore tax payable on the same income, either in the form of Double Tax Relief (DTR) or Unilateral Tax Credit (UTC). Claim of the FTC should be restricted to the lower of the foreign tax paid and the Singapore tax payable on the foreign income (net of expenses).

A "very useful session" and an appreciation of the clear explanations especially during the Q&A session were just two of many positive comments received from participants after the tax compliance session.

For companies with permanent establishment (PE) overseas, FTC can be claimed (against the Singapore tax payable on the same income) if the trade income is derived through the PE in the foreign jurisdiction and the foreign tax has been paid in accordance with the relevant Avoidance of Double Taxation Agreement (DTA).

In situations where a company is subject to tax in the foreign jurisdiction even though it does not have a PE in the foreign jurisdiction, FTC may still be claimed if the company is subject to tax in the foreign jurisdiction based on the relevant Article(s) in the DTA. For example, Article 13 of the Singapore-Malaysia DTA states that technical fees derived from Malaysia by a Singapore tax resident may be taxed in Malaysia if the services are performed in Malaysia (notwithstanding that the Singapore tax resident may not have a PE in Malaysia).

For passive income (such as interest and dividend) derived from outside Singapore, FTC may be claimed in the year of remittance (when the income is taxed in Singapore).

To improve tax compliance and avoid unnecessary tax penalties, companies need to put in place good internal controls and a robust record-keeping system to enable its income and expenses to be correctly computed for tax purposes. It is also good practice for companies to conduct periodic reviews of their tax matters and voluntarily disclose any errors in a timely manner.

With the right procedures in place, tax compliance does not have to be taxing.

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