RELEVANT TO ACCA QUALIFICATION PAPER P6 (SGP)

Three new tax schemes in Singapore

This article explains three new tax initiatives that were introduced in Singapore in Budget 2010 and Budget 2011. Although the first two initiatives were introduced and took effect from the year of assessment (YA) 2011, there were important refinements made which affect the YA 2012. As for the second and third new initiatives, they apply from the YA 2012

1 Productivity and Innovation Credit (PIC) scheme

The Productivity and Innovation Credit (PIC) was first introduced in Budget 2010 to help businesses restructure, upgrade the skills of their workers and generate better-quality jobs for their employees. To help businesses defray the costs incurred for these projects, the tax benefits under the PIC provide for enhanced deductions or allowances of the amount of expenditure incurred (subject to an annual ceiling) on each of the following six categories of qualifying activities along the innovation value chain for the YAs 2011 to 2015:

- Registration of intellectual property rights (Section 14A)
- Research and development (Section 14D)
- Training of employees (Section 14R)
- Approved design projects (Section 14S)
- Leasing or acquisition of prescribed automation equipment (Section 14T/19A)
- Acquisition of intellectual property rights (Section 19B).

After the introduction of PIC, businesses were able to claim enhanced tax deductions (or allowances) of 250% of the amount of qualifying expenditure incurred in each of the six categories of activities, up to a maximum of $300,000 of qualifying expenditure in each category for each YA. Normal tax deductions or allowances are available for any balance expenditure in excess of $300,000 for each category in each year of assessment (ie 100%/150% tax deduction (or allowances) for any balance expenditure in excess of $300,000).

In addition, to help businesses (including sole proprietorships, partnerships, companies and business trusts) which pay little or no taxes to invest in productivity, they may convert the tax deductions (or allowances) under the PIC Credit scheme into a non-taxable cash grant equal to 7% of the amount of tax deductions (or allowances) allowed – ie up to a maximum cash grant of $21,000 per year of assessment. They can do so if they have:

- incurred qualifying expenditure and are entitled to PIC during the basis period for the qualifying YA
- active business operations in Singapore and

- at least three local employees (Singapore citizens or permanent residents with CPF contributions excluding sole proprietors, partners under contract for service and shareholders who are directors of the company). A business is considered to have met this three-local-employees eligibility if it contributes CPF on the payrolls of at least three local employees in the last month of its basis period for the qualifying YA.

Any unused PIC shall form part of the taxpayer's unutilised tax losses/capital allowances (whichever is applicable) available for future claim or carry-back, subjecting to the satisfaction of the shareholding continuity and/or same trade tests as at certain relevant dates. Taxpayers are also allowed to transfer their unused PIC to be offset against the taxable income of their Singapore related companies under the Group Relief System.

Budget 2011 enhancements

The PIC scheme was enhanced and simplified in Budget 2011 in the following ways:

- Instead of 250% of the first $300,000 of qualifying deduction, the PIC scheme provides for enhanced tax deductions (or allowances) of 400% of the amount of qualifying expenditure incurred in each of the six categories of activities, up to a maximum of $400,000 of qualifying expenditure in each category for each year of assessment. Businesses can combine the annual expenditure cap and claim up to $800,000 expenditure per category for YA2011 and YA2012 combined; and up to $1,200,000 expenditure per category for YA2013 to YA2015 combined.
- Instead of $21,000, the maximum cash payout is increased to $30,000 for the first $100,000 of qualifying expenditure for the years of assessment 2011 to 2013 for all six qualifying activities. For amount below $100,000, the cash payout is based on a conversion ratio of 30% of qualifying expenditure (subject to a minimum of $400). Businesses are also allowed to claim a combined cash payout cap of $60,000 based on the combined cap of $200,000 of total qualifying expenditure incurred for the years of assessment 2011 to 2012.
- To help smaller businesses with their cashflows and investments in productivity and innovation, a tax deferral option was introduced to allow businesses to defer the payment of current year tax for every dollar of PIC qualifying expenditure incurred for the current financial year, up to a cap of $100,000. This election is available for tax payable for the years of assessment 2011 to 2014 based on expenditure incurred in the corresponding financial years 2011 to 2014.

Below is a broad overview of the PIC scheme for each of the six qualifying PIC activities.

Qualifying activities	**Nature of qualifying expenditures**	**Tax benefits under the enhanced PIC scheme**	**Examples of qualifying expenditures**
Registration of IPRs**	Costs incurred to register patents, trademarks, designs and plant variety. Renewal costs do not qualify for enhanced deduction. Enhanced deduction is granted regardless of the outcome of the application.	• 400% tax deduction for the first $400,000* of qualifying expenditures and • 100% tax deduction for the remaining expenditures.	• Fees paid to Intellectual Property Office of Singapore to register trademark. • Payments made to an agent to prepare specifications or other documents for the purposes of the Patents Act.
R&D	Staff costs and costs of consumables incurred on qualifying R&D conducted in Singapore or overseas (overseas R&D must be related to the taxpayer's Singapore trade or business).	• 400% tax deduction for the first $400,000* of qualifying expenditures • 150% tax deduction for the remaining qualifying expenditures for R&D done in Singapore and/or • 100% tax deduction for all other qualifying expenditures (including expenditures for R&D done outside Singapore, subject to conditions).	Salaries for R&D personnel and purchase costs of laboratory chemicals relating to the R&D activities.

Training of employees	Costs incurred for all employees on: • All external training; or • In-house training certified by Singapore Workforce Development Agency, Institute of Technical Education or other prescribed courses. There is no restriction on where the training is conducted.	• 400% tax deduction for the first $400,000* of qualifying expenditures; and • 100% tax deduction for the remaining expenditures.	• External training: training fees payable to external trainer, examination and tuition fees. • In-house training: rental of external training premises, salary of in-house trainers, training materials/ stationery, meals and refreshments provided during the courses.
Approved design projects	Costs incurred to create approved new products and industrial designs where the activities are primarily conducted in Singapore.	• 400% tax deduction for the first $400,000* of qualifying expenditures; and • 100% tax deduction for the remaining expenditures.	• Remuneration of qualified in-house designer relating to approved in-house design projects. • A certain percentage of fees payable to external design service providers on approved design projects.

Acquisition or leasing of prescribed automation equipment**	Costs incurred for the acquisition or leasing of prescribed automation equipment that enhances the productivity of businesses by automating core work processes or reducing man-hours.	• 400% tax deduction/ allowance for the first $400,000* of qualifying expenditures; and • 100% tax deduction/ allowance for the remaining expenditures.	• Purchase costs for computers. • Rental costs for fax machines, scanners, etc.
Acquisition of IPRs**	Costs incurred to acquire IPRs for use in a trade or business (exclude EDB approved IPRs and IPRs relating to media and digital entertainment contents)	• 400% tax allowance for the first $400,000* of qualifying expenditures; and • 100% tax allowance for the remaining expenditures.	Price paid for acquiring a trademark or patented technology.

* Total combined expenditure cap for the YAs 2011 and 2012 – $800,000
Total combined expenditure cap for the YAs 2013 to 2015 – $1,200,000 for each of the six qualifying activities

** Minimum ownership period requirement applicable. Taxpayers failing to meet the ownership requirement will be subject to claw-back provisions which apply to both the deductions (or allowances) and/or cash payout, unless waived in the case of prescribed automation equipment under certain circumstances.

2 New Merger and Acquisition (M&A) scheme
The costs incurred by companies in mergers and acquisitions (M&As) have traditionally been treated as capital in nature and not deductible for tax purposes in Singapore. But this has changed with the introduction of the M&A Scheme. More guidelines were released by the Inland Revenue Authority of Singapore on 27 June 2011.

The M&A scheme only applies to qualifying acquisitions of ordinary shares in an active target company (local or foreign) made during the period 1 April 2010 to 31 March 2015 – ie asset deals are excluded. The scheme does not apply to internal restructuring or reorganisations, the incorporation of new subsidiaries to carry on business activities, or trading transactions.
Under this scheme, an M&A Allowance (based on 5% of the cash consideration paid for the acquisition and/or the value of any shares issued as consideration) is granted to the acquiring company who acquires the ordinary shares in the

target company directly or through a wholly-owned acquiring subsidiary. The allowance is capped at $5m for acquisitions made in each year of assessment and claimed over five years on a straight-line basis.

The qualifying conditions for the acquiring company under the M&A Scheme are:

- The acquiring company and its ultimate holding company (if any) must be incorporated and tax resident in Singapore.
- It must carry on a trade or business on the acquisition date.
- It must have at least three local employees (excluding company directors) throughout the period of 12 months preceding the acquisition date.
- It must not be connected to the target company for at least two years prior to the acquisition date.

In addition, a qualifying acquisition is a share acquisition that results in the acquiring company or its acquiring subsidiary:

- owning more than 50% of the ordinary shares in the target company (where 50% or less of the ordinary shares in the target company was owned before the acquisition date); or
- owning at least 75% of the ordinary shares in the target company (where more than 50% but less than 75% of the ordinary shares in the target company was owned before the acquisition date)

Any unabsorbed M&A Allowance may be carried forward provided there is no substantial change in the shareholders of the acquiring company, but cannot be carried back nor available for transfer under the group relief system.

In addition to the M&A allowance, there is also stamp duty relief available to an acquiring company under the scheme but is capped at $200,000 per financial year.

3 Foreign Tax Credit (FTC) pooling system

Foreign income derived by a Singapore company that suffers taxation in a foreign country may still be subject to tax when the foreign income is remitted into Singapore. Where the foreign income does not qualify for exemption under current rules, foreign tax credit (FTC) may be granted by allowing the Singapore tax resident company to claim a credit for the tax paid in the foreign country against the Singapore tax that is payable on the same income.

To claim FTC, a company must satisfy all the following conditions:

- it must be a tax resident in Singapore for the relevant basis year
- tax has been paid or is payable on the same income in the foreign country and
- the income is subject to taxation in Singapore.

The amount of foreign sourced income must be re-grossed to include the foreign tax paid, and allowable expenses can be deducted from the foreign sourced income. The FTC is computed on a source-by-source and country-by-country basis, for each particular stream of foreign income remitted into Singapore. In other words, foreign tax paid on one stream of income cannot be used to set off against the Singapore tax payable on another stream of income even if both streams of income are derived from the same country.

The FTC granted is capped at the lower of the foreign tax paid and the Singapore tax payable on the particular stream of remitted foreign income. Any excess of foreign tax paid over the Singapore tax payable for the specific stream of income cannot be used to reduce the Singapore tax payable on other streams of remitted income. Neither can it be carried forward or backward.

With effect from the YA 2012, an FTC pooling system was introduced with the following objectives:

- give businesses greater flexibility in their claim of FTCs
- reduce the Singapore taxes payable on remitted foreign income
- simplify tax compliance.

Resident taxpayers can elect for the FTC pooling system if the following conditions are fulfilled:

- foreign income tax is paid on the foreign income in the foreign jurisdiction from which the foreign income is remitted
- the headline tax rate of the foreign jurisdiction from which the foreign income is remitted is at least 15% at the time the foreign income is received in Singapore
- there is Singapore tax payable on the foreign income and
- the taxpayer is entitled to claim for FTC under the Income Tax Act on that foreign income.

Without pooling, any FTC for a particular stream of foreign income that is in excess of Singapore tax payable is disregarded and cannot be used to offset the Singapore tax payable on another source of foreign income that is subject to tax in Singapore.

To the extent that the difference between the foreign tax suffered and the Singapore tax payable is large, the ‘wastage’ will be higher.

Such a restriction is lifted for qualifying foreign income under the FTC pooling system which allows FTC to be computed on a pooled basis, rather than on a source-by-source and country-by-country basis for each particular stream of income. The amount of FTC to be granted will be based on the lower of the pooled foreign taxes paid on the foreign income and the pooled Singapore tax payable on such foreign income.

It should be noted that FTC pooling is not applicable in the following situations:

- Foreign income which qualifies for tax sparing credit in Singapore, since it does not meet the 'subject to tax' condition.
- Foreign income which qualifies for exemption in Singapore, other than under Section 13(8)
- Singapore company suffers a net tax loss.

Example: how Foreign Tax Credit (FTC) pooling works
A Singapore Company received dividend income from Foreign Country X and royalty income from Foreign Country Y in August 2011. Both these incomes would be considered foreign income. The Company incurred foreign income taxes on these foreign incomes in Countries X and Y respectively where the headline tax rate of Countries X and Y in the year 2011 is at least 15%. The Company is entitled to claim for FTC on these foreign incomes under the Income Tax Act.

Foreign income taxes paid on the foreign income

	Foreign Country X $	**Foreign Country Y $**	**Total S$**
Foreign income remitted	20,000	40,000	60,000
Foreign income taxes paid	1,000	10,000	11,000

Comparison of the existing FTC system and the new FTC pooling system

	Existing FTC System			**New FTC pooling System**
	Foreign Country X $	**Foreign Country Y $**	**Total $**	**Total $**
1) Foreign income taxes paid	1,000	10,000	11,000	11,000
2) Singapore tax payable on the foreign income (based on prevailing corporate tax rate of 17% for illustrative purposes)	17% x 20,000 = 3,400	17% x 40,000 = 6,800	3,400 + 6,800 = 10,200	3,400 + 6,800 = 10,200
3) FTC available (capped at the lower of 1) foreign income taxes paid and 2) Singapore tax payable)	1,000	6,800	<u>(7,800)</u>	<u>(10,200)</u>

4) Net Singapore taxes payable on the foreign income after offsetting FTC [2) minus 3)]			2,400	0

Before the introduction of the FTC pooling system, the Company is only able to claim FTC of $7,800, based on the lower of the foreign taxes paid and Singapore tax payable on each particular stream of the remitted foreign income. With a FTC of $7,800, the company will have to pay $2,400 Singapore tax on the $60,000 remitted foreign income from Countries X and Y.

Under the new FTC pooling system, for the example above, the company will now be able to enjoy a higher FTC of $10,200 and pay $2,400 less Singapore tax on the remitted foreign income from Countries X and Y. This is because the FTC is computed on a pooled basis, based on the lower of the pooled foreign taxes paid on all qualifying remitted foreign income and total Singapore tax payable on such income.

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