Singapore Budget 2002 Synopsis

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Introduction

In December 2001, the Singapore Government set up an Economic Review Committee ("ERC") to review various aspects of the country's development strategies. One of the Sub-Committees of the ERC was charged with the responsibility for studying the impact of key Government policies on business costs, entrepreneurship and resource allocation. This ERC Sub-Committee released its Report to Deputy Prime Minister and Minister for Finance Lee Hsien Loong on 11 April 2002.

Just over three weeks later, on 3 May 2002, the Minister delivered his 2002 Budget Statement to Parliament, and in that Budget Statement adopted most of the key recommendations of the ERC Sub-Committee for the re-shaping of the Singapore tax system. In particular, the Minister has acted on the ERC Sub-Committee's recommendations to substantially cut both corporate and personal income tax rates, and somewhat increase the Goods and Services Tax rate to partially recover the income tax revenues foregone.

The Minister has also accepted the ERC Sub-Committee's recommendations for other substantive changes in the Singapore tax system including the introduction of group relief, the introduction of a one-tier corporate taxation system, the rationalisation and expansion of a number of tax incentive schemes, and a general shift away from taxes on income to taxes on consumption. The underlying intention behind all of these changes is to increase entrepreneurship, make Singapore a more attractive location for foreign inward investment, attract foreign talent, grow the economy and create more and better job opportunities for the Singaporean workforce.

The Minister mentioned in his Budget Statement a number of other ERC Sub-Committee recommendations that are being studied with a view to their possible future implementation. There are other recommendations that were not mentioned, and may therefore not be under active consideration at the present time. Nonetheless, the Minister has already acted decisively in relation to the largest and most important of the Sub-Committee's recommendations, and his 2002 Budget Statement may well be seen as a watershed in Singapore's economic development.

Budget Day
3 May 2002

Corporate Income Tax Reduction

Current

The standard corporate tax rate applicable to taxable income in excess of $100,000 is 24.5%. For lower levels of taxable income, the effective rates are 6.125% on the first $10,000 and 12.25% on the next $90,000. For Year of Assessment 2002, most corporate taxpayers are entitled to a one-off rebate of 5% on tax payable, giving a reduced effective standard tax rate of 23.275% on taxable income in excess of $100,000 and correspondingly reduced effective rates on lower income bands.

Proposed

With effect from the Year of Assessment 2003, the standard corporate tax rate will be reduced by 2.5% points to 22%. The effective rates on the first $10,000 and the next $90,000 of taxable income will be correspondingly reduced to 5.5% and 11% respectively.

Because of the preceding year basis of tax assessment, the reduced tax rates for Year of Assessment 2003 will apply to business income of accounting years that end in calendar year 2002 and to investment income of the calendar year 2002.

Barring any major change in the current economic and political climate, the standard corporate tax rate will be further reduced over the next two years to reach 20% by the Financial Year 2004 Budget.

Comments

- The further reduction in the corporate tax rate to 20% by Financial Year 2004 seems almost certain to be implemented. This rate cut will translate into a reduction in the deduction value of tax-deductible expenditures. It may therefore be advantageous for companies to consider accelerating their controllable business expenditures.

- Companies with foreign source income that is taxable on a remittance basis in Singapore may similarly want to consider deferring the remittance of that income into Singapore so as to maximise the benefit from the further reduction in corporate tax rate.

- Companies with overseas operations may need to review the structure of those operations with a focus on reducing foreign tax liabilities in line with the reduction in Singapore corporate tax rate, so as to avoid creating excess foreign tax credits.

- Groups whose parent companies are based in countries with Controlled Foreign Corporation ("CFC") or accruals taxation regimes will need to consider the home country impact of the reduced corporate tax rate and the extent (if any) to which their Singapore operations may have to be re-organised. This is particularly relevant to countries (such as the United Kingdom and France) with a "minimum tax rate" threshold of above 22% in their CFC regimes.

- For companies with deferred tax liabilities calculated under the "liabilities method", the cut in the corporate tax rate will result in an immediate reduction in their deferred tax liabilities and hence an improvement in their net asset position.

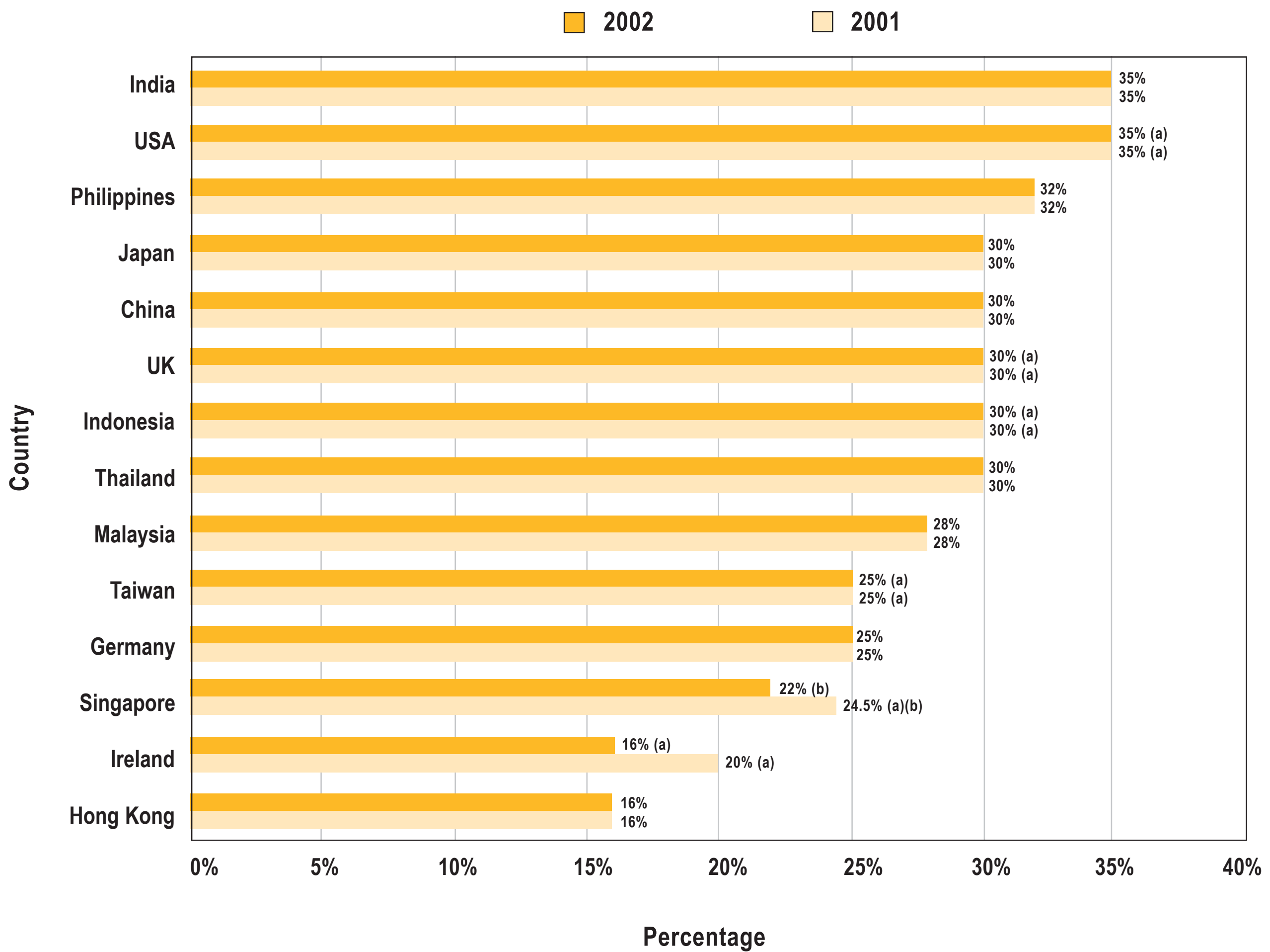
- While not specifically mentioned in the Budget, the following tax rates which are traditionally pegged to the corporate tax rate are almost certain to be correspondingly reduced to 22%:

  - the rate of tax credit on franked dividends paid by companies on or after 1 January 2002;

  - the flat rate of tax payable by certain non-resident individuals and by trustees and executors, with effect from the Year of Assessment 2003; and

  - the maximum effective rate of tax payable by clubs, trade associations, unincorporated societies and management corporations, with effect from the Year of Assessment 2003.

Corporate Income Tax Rates In Selected Countries



The rates above exclude local taxes, surcharges and state taxes where applicable.

(a) Progressive corporate tax rates are applicable for lower income bands in these countries.

(b) For Singapore, the rates indicated are for incomes earned in calendar and/or accounts years 2001 and 2002, which are taxed in the Years of Assessment 2002 and 2003 respectively. The 2001 rate does not take account of a one-off 5% tax rebate granted for Year of Assessment 2002.

One-Tier Corporate Taxation System

Current

Singapore currently adopts a full imputation tax system. Under this system, the taxes paid at the standard corporate tax rate on corporate profits may be used to frank the taxes otherwise due on dividend payments. Under Section 44 of the Income Tax Act, when a Singapore resident company pays a dividend, the corporate tax it has paid is imputed as a credit (more technically described as tax deducted at source) which may be used to offset the tax payable by the shareholder. Distributed corporate income is therefore effectively subject to tax only once and at the marginal income tax rate of the shareholder.

Where the available franking credits are insufficient to frank the full amount of the dividends paid, the company needs to make a cash payment known as a Section 44 charge. This charge is essentially an advance payment of corporate tax on future profits. It can be set off against the future tax liabilities of the company but will not be refunded if it exceeds the future tax liabilities.

The franking credit rules do not apply to tax-exempt dividends paid out of income which is exempt or taxed at concessionary tax rates. Instead, separate rules govern such dividends that are tax-exempt in the hands of the shareholders.

Proposed

To simplify Singapore's tax code, reduce the cost of compliance and administration for companies as well as to make more profits available for distribution as dividends, the Minister has accepted the ERC Sub-Committee's recommendation to move to a "one-tier" corporate tax system with effect from 1 January 2003. Under this system, the tax collected from corporate profits is final and Singapore dividends are exempt.

To enable companies to make full use of their unutilised dividend franking credits in their Section 44 accounts as at 31 December 2002, the Minister will introduce a 5-year transition period from 1 January 2003 to 31 December 2007 for such companies to pay franked dividends out of any unutilised dividend franking credits. During this period, the shareholders will continue to receive these dividends with credits attached.

Under the imputation system, a company may not be able to flow exempt dividends to all tiers of shareholders, regardless of shareholding level. As a concession, the Minister will allow companies that are still on the imputation system during the 5-year transition period to flow exempt dividends paid out of concessionary income to all tiers of shareholders without restriction on shareholding level.

Comments

- The one-tier tax system should simplify the procedures for effecting dividend distributions, capital reductions, share buy-backs, share redemptions and share borrowing and lending. The one-tier system will also facilitate the onward payment of dividends received by intermediate Singapore holding companies to their own shareholders, free of the procedural and timing constraints that exist under the current tax system.

- Currently, companies with capital gains and other non-taxable income may lack sufficient franking credits to distribute dividends out of such income or gains without incurring a Section 44 charge. Under the one-tier tax system, such companies will be able to distribute dividends free of such Singapore tax constraints.

- Currently, the Section 44 rules do not apply to Singapore incorporated companies which are not tax residents (i.e. which are not managed and controlled) in Singapore. Under the one-tier system, the main continuing constraint on the payment of dividends for both resident and non-resident companies would be the Companies Act requirement that dividends be paid out of profits.

- Given the 5-year transition period, companies with substantial accumulated dividend franking credits should consider the timing of the payment of franked dividends to its shareholders so as to enable their shareholders to derive maximum benefit from the franking credits.

- It remains to be seen whether companies which have incurred the Section 44 charge will continue to be able to offset this charge against their tax liabilities incurred during the 5-year transition period and perhaps beyond this period.

- The holding company of a Singapore group of companies may have borrowing costs that are attributable to the financing of its investments in subsidiaries and affiliates. These borrowing costs can currently be set off against the taxable dividends that it receives from its subsidiaries and/or affiliates. No such relief will be possible once these dividends become tax-exempt and corporate groups with this type of funding model would need to restructure their borrowing arrangements. It remains to be seen whether interest expense incurred after 1 January 2003 can be deducted against franked dividends paid during the 5-year transition period.

- Similarly, individuals whose marginal tax rates are lower than the corporate tax rate will no longer receive tax refunds. In the ERC Sub-Committee's report, a mitigation factor for the loss of tax refunds was the proposed exemption of interest income. However, the exemption of interest income has not been included in this year's Budget.

- Issuers and holders of fixed rate preferential shares will need to determine whether the dividend rate is specified as a gross or a net of tax rate. If the specified rate is the gross dividend rate, the proposed removal of the tax deducted at source may result in additional (non-tax deductible and non-taxable) cash payments by the company to the preference shareholder(s).

Unlimited Flow Through Of Exempt Dividends

Current

Companies which distribute dividends out of income which are taxed at a concessionary rate or are exempted from tax, are allowed to flow such exempt dividends to their own (immediate) shareholders. In general, a corporate shareholder receiving these tax-exempt dividends can pass on such tax-exempt dividends to its own shareholders provided the shareholder is a holding company which owns at least 50% of the beneficial interest in the issued capital of the company distributing the tax-exempt dividends. The current rules generally limit the flow through of the tax-exempt dividends to two tiers of shareholders, even when the minimum shareholding requirement is satisfied.

Proposed

In recognition of the trend towards more complex corporate structures and the prevalence of joint ventures as a means of spreading risks in new business undertakings, the Minister has proposed that with effect from 1 January 2003, dividends distributed by companies out of income which has been exempted from tax or taxed at concessionary rates under tax incentive schemes will be allowed to flow tax-free to all tiers of shareholders, regardless of shareholding level. This unlimited flow through of exempt dividends will apply to all credit balances in the exempt dividend income accounts as at 1 January 2003.

Comments

- The retention of the existing restrictions on the flow through of these types of exempt dividends would be out of line with the introduction of the one-tier corporate taxation system.

- Notwithstanding the introduction of the one-tier corporate taxation system and the unlimited flow through of exempt dividends, it may still be beneficial for certain companies with foreign shareholders to separately identify and keep track of dividends which qualify for tax sparing credits under relevant double taxation treaties in order to assist their shareholders in making the available tax sparing relief claims in their home countries.

Group Relief For Losses

Current

There is currently no provision for group relief in Singapore. Losses of one company in a group cannot be offset against profits of another.

Proposed

A loss transfer model of group relief, under which losses of one company may be utilised for tax purposes by another company in the same group, will be introduced with effect from Year of Assessment 2003.

For group relief purposes, a group is to consist of a Singapore incorporated parent company and all its Singapore incorporated subsidiaries. Two Singapore incorporated companies will also be members of the same group if one is 75% owned by the other, or if both are 75% owned by another Singapore incorporated company.

Group companies will be able to transfer their current year unutilised capital allowances and losses. Investment allowances and foreign losses may not be transferred.

The ERC Sub-Committee's recommendation to introduce consortium relief is to be studied further before any decision is taken regarding its introduction.

Comments

- The absence of group relief is one of the key causes of some Singapore groups having very high effective tax rates in their consolidated accounts. The introduction of group relief will help to mitigate both this and the related (tax settlement) cash flow problems experienced by many such groups.

- Similarly, the introduction of group relief will remove the anomaly in the current tax regime that favours structuring diverse operations as divisions of a single Singapore company rather than as separate subsidiaries.

- Under the proposed definition of a group, it will be necessary to have a Singapore parent or holding company. For example, if two Singapore companies are each owned directly by a foreign parent, they will not be in a group for group relief purposes. Furthermore, only Singapore incorporated companies can be in a group. Singapore branches of foreign companies, and companies incorporated overseas but tax resident in Singapore, are not included in the group definition. Some groups may therefore need to consider restructuring to obtain the benefits of group relief.

- The creation or loss of a group relationship for tax purposes will be a factor that companies will in future need to consider in relation to any corporate reorganisations, partial divestments and/or new share issues that they wish to effect.

- Group relief is to be restricted to current year unutilised capital allowances and losses, which is in line with the UK model for group relief. Unutilised capital allowances and losses brought forward from prior years will not be transferable for group relief purposes.

- When losses in one company are surrendered to another company, the surrendering company may require the claimant company to pay for the value of the transferred losses, especially where the two companies do not have 100% common ownership and it is necessary to protect the interest of minority shareholders. Under the UK group relief model, payments for group relief are accounted for in the profit and loss account as a separately disclosed category of tax charge or credit, and such payments are disregarded for tax purposes. It remains to be seen whether a similar or a different approach will be taken in the Singapore model.

- Other areas which will need to be addressed during the implementation process, and which companies will need to consider once the legislative details are available, include:

    - whether a parity adjustment is to be required for the transfer of losses between companies that have different tax rates;
    - group entry and exit rules;
    - whether group relief can extend beyond trading losses, for example to include the unrelieved interest costs of an investment holding company, especially as these will cease to be effectively relieved by set-off against dividend income under the one-tier corporate taxation system.

Unilateral Foreign Tax Credits For Services

Current

Unilateral tax credit ("UTC") is granted only in respect of foreign tax suffered on income from certain specified categories of services performed in certain specified non-treaty countries. There are currently 13 different categories of qualifying services and 19 eligible countries.

Proposed

To further support regionalisation, with effect from the Year of Assessment 2003, UTC will be extended to cover all services income remitted from all non-treaty countries.

Comments

- The proposed change goes beyond the ERC Sub-Committee's recommendation of expanding or abolishing the existing list of prescribed services as it not only removes the list of prescribed services but also removes the list of non-treaty countries.

- The current UTC scheme also covers certain categories of dividend income, employment income and profits derived from outside Singapore by an overseas branch of a Singapore resident company. It does not cover royalties, rental and interest income and it would seem that these will continue to be excluded from the UTC scheme.

R&D Expense Deductions

Current

R&D expenses incurred by companies engaged in manufacturing or in certain stipulated service activities are allowed as deductions if the R&D activities are either undertaken in-house or outsourced to approved R&D organisations that conduct their research activities in Singapore. Additional, or further deductions premised on similar qualifying criteria, are allowed for certain approved R&D expenses.

Separately, if certain conditions are satisfied, writing down allowances are granted over a five-year period or such shorter period as may be approved, on expenditures incurred under any approved cost-sharing agreement in respect of R&D activities undertaken for the purposes of a trade or business.

Proposed

With effect from the Year of Assessment 2003, the single tax deduction for expenses incurred for R&D that leads to ownership of intellectual property ("IP") in Singapore will be liberalised to include R&D outsourced to any R&D organisation, whether local or overseas.

In addition, the scope of the further tax deduction for R&D expenses will be extended to all service companies.

Further details of the proposed Enhanced Deduction for R&D Expenses are to be released by the Economic Development Board ("EDB") within one month from the date of the Budget Statement i.e. by 3 June 2002.

Comments

- The proposed liberalisation to allow a single tax deduction for expenses incurred for R&D that leads to ownership of IP will be of benefit to those companies who engage unapproved local or foreign R&D organisations, including their affiliates, to perform R&D activities for them.
- Although the Budget Statement referred only to extending the scope of the further tax deduction to all service companies, it would seem likely that the single tax deduction will also be extended to all categories of service companies since currently it is restricted to companies providing specified services.
- It is uncertain whether the proposed liberalisation of tax deductions for R&D expenses will benefit companies whose R&D projects are abandoned before any identifiable (or registrable) IP is created.

Financial Sector Incentives

(A) Fund Management Industry Incentives

Current

Currently, Approved Fund Managers ("AFM") enjoy the following tax incentives:

- a 10% concessionary rate of tax on fees and commissions derived from managing the funds of foreign investors invested in designated investments, provision of investment advisory services to a foreign investor in relation to any designated investments and arranging on behalf of foreign investors any loan of designated securities; and
- tax exemption on the above qualifying income where the average size of funds managed is at least S$5 billion throughout the incentive period.

Specified income from designated investments derived by foreign investors whose funds are managed by AFMs is exempt from tax. Such income is also exempt from tax if the funds are managed by Approved Boutique Fund Managers ("ABFM").

Proposed

The present tax exemption available to foreign investors is to be extended to qualifying income derived by foreign investors from funds managed by all fund managers in Singapore.

The AFM and ABFM schemes are to be merged into a single AFM scheme. Under the new scheme, ABFMs will enjoy the 10% concessionary tax rate currently enjoyed by the AFMs on their qualifying fee and commission income. The new scheme will also cover more types of investments.

Both changes are to take effect from the Year of Assessment 2003.

Comments

- The merger of the AFM and ABFM schemes should help to streamline and simplify the current tax incentive regime for the fund management industry. It also puts the ABFMs on a level playing field with the AFMs.

- The Budget Statement does not make clear whether in order for the tax exemption to apply, the funds must be managed by a fund manager with an investment adviser licence. Currently, a company may operate an investment advisory business without holding an investment advisor licence if its investment advisory business is confined to no more than 30 accredited investors. An accredited investor is defined in the Securities Industry Regulations as an individual with net personal assets exceeding S$5 million or a corporation with net assets exceeding S$10 million.

- The Monetary Authority of Singapore ("MAS") is to announce more details of the proposed changes within two months from the Budget Statement, i.e. by 3 July 2002.

(B) Enhanced Approved Trustee Company Scheme

Current

Income derived by an Approved Trustee Company ("ATC") from the provision of certain trustee or custodian services is taxed at a concessionary rate of tax of 10%. The qualifying trustee or custodian services include such services provided to foreign trusts, foreign unit trusts, for foreign bond or loan stock issues, and for foreign currency stocks and shares of foreign companies. The 10% tax rate does not apply to any payment made to an ATC, which is borne directly or indirectly, by a person resident in Singapore or a permanent establishment in Singapore. In addition, specified income derived from designated investments by a foreign trust administered by an ATC is currently exempt from tax.

Proposed

The scope of the qualifying trustee or custodian services for the purpose of the 10% concessionary rate of tax is to be expanded to include:

- custodian services provided to mutual fund corporations; and
- substantial trust management or administrative services provided to a foreign trust of which the ATC is not the trustee.

In addition, the current tax exemption available to a foreign trust is to be extended to the following:-

- income derived by the foreign trust through an eligible investment holding company; and
- qualifying income derived by the foreign trust if substantial trust management or administrative services are provided by an ATC who is not the trustee of the trust.

Both changes are to take effect from the Year of Assessment 2003.

Comments

- Payments to an ATC that are borne directly or indirectly by a Singapore resident person or a permanent establishment in Singapore will continue to be taxed at the normal corporate tax rate of 22%.

- The MAS is to announce more details on the above enhancements within two months of the Budget Statement, i.e. by 3 July 2002.

(C) Concessionary Tax Rates for Equity Capital Market and Treasury Industry

Current

At present, Asian Currency Units ("ACUs") and Approved Securities Companies ("ASCs") are granted:

- a 10% concessionary rate of tax on income derived from certain specified activities, including:
    - a. arranging, underwriting, managing and placing Initial Public Offerings ("IPOs") of foreign currency shares; and
    - trading of foreign currency shares and services for acting as brokers, nominees or custodians for specified securities.

- tax exemption for income derived from arranging, underwriting, managing and placing IPOs of foreign currency shares and trading in foreign currency shares listed on the Singapore Exchange Limited ("SGX"). This incentive was granted for a specified initial period of 5 years from the Year of Assessment 1998 to the Year of Assessment 2002.

In addition, ACUs also enjoy:

- a 5% concessionary rate of tax on incremental income from all qualifying offshore ACU activities. This incentive was granted for a limited period, from the Year of Assessment 1998 to the Year of Assessment 2002; and

- a 10% concessionary rate of tax on income derived from offshore financial derivative transactions with qualifying parties. This incentive was granted for the period from the Year of Assessment 2001 to the Year of Assessment 2005.

Proposed

Subject to certain (not yet specified) conditions, the 10% concessionary rate of tax will be extended to income derived by ASCs from the provision of financial advisory services to persons outside Singapore.

The income derived by ACUs and ASCs from managing IPOs of securities of foreign companies for listing on the Singapore Exchange and from the sale of such foreign securities, including related brokerage and custodian services, will be taxed at a concessionary rate of 5%. The securities can be placed with any investor and denominated in any currency.

Both of the above changes are to have effect for the period from the Year of Assessment 2003 to the Year of Assessment 2007. The MAS is to provide further details of these incentives within two months from the Budget Statement, i.e. by 3 July 2002.

In addition, ACUs and ASCs with substantial (but not yet specified) commitments will enjoy a 5% concessionary rate of tax on income derived from transacting with qualifying parties in over-the-counter financial derivatives denominated in any foreign currency. This scheme is to take effect from 20 May 2002 and will last for 5 years. Payments to non-residents on such derivative transactions will be exempted from withholding tax during the qualifying period. The MAS is to provide further details before the 20 May implementation date.

Comments

- With some degree of consolidation occurring across different business segments within the financial services industry, many companies in the industry are increasingly going beyond their traditional businesses to undertake new activities. The extension of the 10% tax concession to the provision of financial advisory services by ASCs is therefore timely.

- Offering the extended incentive for managing IPOs should assist ACUs and ASCs to offer more competitive terms to foreign companies to list their securities in Singapore. Whilst the present incentive grants tax exemption for income derived from managing IPOs and trading in foreign currency shares only, the extended incentive in the form of a 5% tax concession applies to securities denominated in any currency.

- Over-the-counter financial derivatives have come to play an important role in the financial system. Financial and non-financial institutions have begun to embrace derivatives as an integral part of their risk capital allocation, profit maximisation and hedging strategies. The enhanced incentive will help to grow this area of treasury business and further bolster Singapore's position as Asia's treasury hub outside Japan. The enhanced incentive will be given to ACUs and ASCs with substantial commitments. It is unclear at this moment what types or levels of commitment will be required, but this information will no doubt be included in the details that are to be announced in the near future.

- It may be noted that under the new scheme, the larger ACUs will be paying tax at the reduced rate of 5% on income derived from qualifying over-the-counter financial derivatives, while income derived

from other offshore financial derivative transactions will continue to be taxed at 10% up to the Year of Assessment 2005.

(D) Concessionary Tax Rate for Corporate Futures Members of the Singapore Exchange Limited

Current

Eligible corporate futures members of the SGX enjoy a 5% concessionary tax rate on incremental trading and broking income derived from any designated transactions in new financial, petroleum or gold futures which are launched and traded on the SGX. The eligibility criteria are:

- the company has been a corporate futures member of the SGX for at least 3 prior years of assessment; and
- the company is among the top 20 corporate futures members as determined by the SGX in terms of total volume of transactions on the exchange during the year before the introduction of new contracts.

For each new contract, the tax benefit is given for 5 years of assessment and on the incremental qualifying chargeable income. The incremental portion is determined as the current qualifying chargeable income less the previous qualifying chargeable income subject to tax at the rate of 5%.

Proposed

The above tax incentive will be replaced by a new scheme which provides for the 5% concessionary tax rate on all income derived by top 20 corporate futures members on approved new derivative products launched and traded on the SGX during the period from 1 January 2002 to 31 December 2006.

In terms of ranking the top 20 corporate futures members, the measurement criterion will in future be focused on annual trading volume generated for each approved new derivative product.

It is indicated in the Budget Statement that further details on the new scheme will be released by the MAS within two months of the Budget Statement, i.e. by 3 July 2002.

Comments

- The current 5% concessionary tax rate is intended to encourage corporate futures members to support, promote and trade in new futures contracts launched on the SGX. However, because of the complex mathematical formula for determining incremental taxable profits, members who meet the eligibility

criteria may end up with little or no taxable benefit. The current scheme is therefore not as attractive as it might be.

- The new scheme, which applies to all income, removes from the formula the incremental income component. It therefore provides a clearer indication to corporate futures members of the tax benefit to be derived if they were to participate in the new derivative products launched on the SGX.

(E) Consolidation of Existing Schemes

Current

There are presently some eleven separate financial sector incentives, as follows:

- Asian Currency Unit ("ACU") – qualifying income derived by an ACU of a financial institution is generally taxed at the concessionary rate of 10%, if certain specified criteria on the types of transactions, the currency the transaction is denominated in and the counterparties to the transactions are satisfied. Certain types of income derived by the ACU are taxed at 5% or are exempt from tax, if other specified conditions are satisfied.

- Approved Boutique Fund Manager ("ABFM") – qualifying investment income derived by foreign investors from funds managed by an ABFM is exempt from tax. The fee income derived by an ABFM is taxed at the normal tax rate (but it is proposed in the current Budget Statement that the ABFM scheme is to be merged with the AFM scheme).

- Approved Fund Manager ("AFM") – in addition to the exemption for foreign investors under the ABFM incentive, qualifying fund management, advisory and securities lending fee income derived by an AFM is subject to tax at the concessionary rate of 10%, if certain conditions are satisfied.

- Enhanced Fund Manager ("EFM") – in addition to the exemption for foreign investors under the ABFM incentive, qualifying fund management, advisory and securities lending fee income derived by an EFM is exempt from tax for up to 10 years if certain additional conditions are satisfied.

- Approved Trustee Company ("ATC") – qualifying trustee and custodian fee income of an ATC is subject to tax at the concessionary rate of 10%, if certain conditions are satisfied.

- Approved Bond Intermediary ("ABI") – qualifying fee income earned by approved financial institutions in Singapore from arranging, underwriting or distributing qualifying debt securities in Singapore is exempt from tax, if certain conditions are satisfied. Interest income earned by non-residents from such qualifying debt securities are exempt from tax and interest income earned by financial institutions and corporations in Singapore from qualifying debt securities are taxed at the concessionary rate of

10%, if relevant conditions are satisfied.

In addition, income derived by any financial institution from trading in any debt securities during the specified period is taxed at the concessionary rate of 10%. Notwithstanding the above, income derived by a primary dealer from trading in Singapore Government Securities during the specified period is exempt from tax if certain conditions are satisfied.

- Approved Securities Companies ("ASC") – qualifying commission and securities trading income derived by an ASC is taxed at the concessionary rate of 10%, if specified criteria on the types of transactions, the currency the transaction is denominated in and the counterparties to the transactions are satisfied. Certain types of income derived by an ASC are taxed at 5% or exempt from tax, if relevant conditions are satisfied.

- The Singapore Exchange Limited ("SGX") Derivatives Trading ("DT") and Derivatives Clearing ("DC") members – qualifying commission and trading income derived by a futures member of the SGX from relevant transactions are taxed at the concessionary rate of 10%. The top 20 corporate futures members are taxed on their incremental qualifying income at the lower concessionary rate of 5%, if specified conditions are satisfied.

- Offshore Insurance business – qualifying underwriting and investment income derived by an approved insurance company in respect of its offshore insurance business is taxed at the concessionary rate of 10%, if certain conditions are satisfied.

- Offshore Marine Hull and Liability business – qualifying underwriting and investment income derived by an approved marine hull and liability insurer is exempt from tax, if certain conditions are satisfied.

- Tax Exemption Scheme for Syndicated Facilities – qualifying fee and interest income derived by a financial institution or an ASC from approved syndicated offshore credit facility, syndicated offshore underwriting facility or syndicated guarantee facility is exempt from tax, if certain conditions are satisfied.

Proposed

To rationalise and consolidate existing financial sector incentives, it is proposed that several of the above eleven existing financial sector incentives be merged into a single FSI scheme from Year of Assessment 2004. The FSI scheme will offer a concessionary tax rate of 5% for qualifying high growth and high value-added activities and 10% for mature but tax sensitive activities. The MAS is to announce more details in 6 months.

Comments

- The proposed FSI scheme should reduce the compliance costs arising from the current need to keep separate accounts for each financial sector incentive, in particular for those non-bank financial institutions

which are not eligible for the ACU licence but who conduct a range of financial activities which qualify for a number of different financial sector incentives.

- Some of the above tax incentives exempt income from certain activities from tax. It remains to be seen whether there will be a transition period for companies that are currently enjoying tax exemption or lower concessionary tax rates to continue to enjoy such benefits and to join the new FSI scheme upon expiry of the existing schemes.

- Currently, some of the financial sector incentives (for example, the ACU and AFM incentives) are based on particular licence or status and do not contain a sunset clause while other incentives (for example, the EFM and ABI incentives) are for specified periods. It remains to be seen whether the proposed FSI scheme will include a sunset clause.

(F) Extension of Concessionary Rate for Interest Income from Qualifying Debt Securities

Current

Interest income received by a financial institution or a company in Singapore from qualifying debt securities is taxed at the concessionary rate of 10%.

Proposed

With effect from the Year of Assessment 2003, this incentive will be extended to bodies of persons such as management corporations, town councils, trade and industry associations, and clubs.

Comment

- The extension of the 10% concessionary tax treatment to these bodies of persons should widen the pool of potential investors in qualifying debt securities and reinforces the Government's commitment to continue to promote the Singapore debt market.

(G) Tax Deduction for Special Reserves of General Insurance Companies

Current

General insurance companies can claim tax deduction on specific reserves for reported claims and provisions for incurred but not reported ("IBNR") claims if such IBNR provisions are determined using approved statistical methods.

Proposed

With effect from the Year of Assessment 2003, general insurance companies can claim tax deduction on special reserves set aside for certain offshore risks. MAS is to release further details at a later date.

Comment

- It remains to be seen what types of offshore risks will be included in this scheme, and in particular whether provisions for catastrophic losses arising from (say) natural disasters will be included in the definition of "special reserves".

Other Incentives

(A) Improved Development and Expansion Incentive

Current

Under the Development and Expansion Incentive (“DEI”), expansion income derived from qualifying activities by a development and expansion company is taxed at a concessionary rate of tax of not less than 10%.

Proposed

The minimum tax rate under the DEI will be reduced from 10% to 5% with effect from 3 May 2002.

Some companies may currently enjoy the Pioneer Incentive on some activities and DEI on other activities. Under the Pioneer Incentive, income derived from qualifying activities is exempt from tax. These companies may apply to the EDB for a flat tax rate to be applied to all qualifying activities.

Comments

- Given that the standard corporate tax rate is now only 22%, and is expected to reduce further to 20% over the next two years, a DEI incentive tax rate of (not less than) 10% starts to look high by comparison. Hence, the reduction to 5% (minimum) is timely.

- Using a single flat rate of tax can significantly reduce compliance costs as it eliminates the need for companies to separately track incomes and expenditures related to different tax incentives granted for different projects.

(B) Approved International Shipping (AIS) Enterprise Scheme

Current

The AIS scheme accords a 10-year renewable exemption to income from the operation and charter of non-Singapore flag vessels and approved floating production storage offloading ships (FPSOs) or approved floating storage offloading ships (FSOs) used outside of Singapore.

There are certain basic minimum qualifying criteria which have to be met. These relate to the size of the operation, the place of control and management of the operations, the level of business spending in Singapore, the minimum ownership threshold of Singapore flagged ships (either 10% of the total fleet or one ship, whichever is the higher) including the use of Singapore's trade infrastructure.

For operators of FPSOs and FSOs, there is an added requirement to employ a Singapore-based team of professional experts.

Proposed

With effect from Year of Assessment 2003, the qualifying income for exemption will be extended to include income from the operation and charter of the following types of vessels:

- Towage vessels
- Salvage ships
- Dredgers
- Seismic vessels
- Semi-submersible oil rigs

With immediate effect, the qualifying criterion based on the minimum ownership threshold of Singapore flagged ships will be removed, so that AIS can be granted to companies which do not own any Singapore flagged ship as long as the other conditions are met.

In addition, the requirement for a Singapore-based team of professional experts applicable to operators of FPSOs and FSOs will be removed with effect from the Year of Assessment 2003.

Further details of the proposals are to be released by International Enterprise Singapore (formerly known as Singapore Trade Development Board).

Comment

- The AIS, when originally introduced in 1991, was intended for the carriage of passengers, mails, livestock or goods from outside the limits of the port of Singapore. The incentive was extended in the Year of Assessment 2000 to FPSO and FSO vessels. The extension now to other vessels such as towage vessels, savage ships, etc and the removal of some of the qualifying criteria seeks to enhance the attractiveness of the incentive and of Singapore as a transport and logistics centre.

Withholding Taxes on Professional Services

Current

Fees paid to non-resident individual professionals in respect of services performed in Singapore are currently subject to tax withholding at source of 24.5% of the gross amounts paid.

Under current rules, the 24.5% tax withheld at source is not a final tax. The non-resident professionals can file a tax return at the year-end if they wish to claim deductions for the relevant expenses incurred in earning the income and pay tax at 24.5% on the net amount. Any excess tax withheld may then be reclaimed from the Inland Revenue Authority of Singapore ("IRAS"). In practice however not many professionals choose to file a tax return at year-end to reclaim the excess tax paid unless the deductible expenses in question are very material, especially if they are able to secure a credit for the Singapore withholding tax suffered against their home country tax on the same income.

Proposed

With immediate effect (i.e. as from 3 May 2002), payments made to non-resident professionals are to be subject to a final withholding tax at 15% whilst payments made to international arbitrators are to be exempt from withholding tax.

Comments

- The reduction of withholding tax on fee payments to professionals from 24.5% (which is not a final tax) to a 15% (final tax) should be a welcome move as this is a substantial rate reduction. In situations where the withholding tax incidence is borne by the fee payer, the overall cost to him of engaging a non-resident professional will be significantly reduced as payments will now be re-grossed at a reduced rate of 15% rather than 24.5%.

- The withholding tax rate change will not in any way impact a situation where the professionals concerned can qualify for tax exemption under relevant Tax Treaty provisions.

- The tax exemption for fee payments to international arbitrators is in line with the Government's aim to promote Singapore as an international arbitration and dispute resolution centre and to put Singapore in line with other jurisdictions where arbitrators are only taxed in their country of residence.

- It is unclear at this juncture whether the reference to international arbitration services implies that one or both parties to the dispute must be from a country other than Singapore and that the disputes concerned must relate to cross-border trade or business disputes and involve certain specified areas of international law. It is also unclear whether the intention is to exempt non-resident international arbitrators from all forms of Singapore income tax, or only from the cash flow effects of suffering up-front withholding tax deductions. The Budget Statement specifically refers only to exemption from withholding tax.

Reductions In Personal Income Tax Rates

Current

The income tax rates for Singapore residents currently range from 0% for the first S$7,500 of chargeable income to 26% for chargeable income exceeding S$400,000. All resident individuals are entitled to a personal relief deduction of S$3,000 and to a deduction (or rebate) of S$250 from the tax they would otherwise be due to pay. (This S$250 is the remaining balance of a S$500 rebate first granted when GST was introduced in 1994. Half of the original rebate was incorporated into the personal income tax rate structure in the Year of Assessment 2002).

Proposed

With effect from the Year of Assessment 2003, the tax rates for all income bands are to be reduced. In particular, the top marginal tax rate is to be reduced by 4% points from the current 26% to 22%. Corresponding reductions are to be made in the lower rates and the number of separate rate bands reduced from ten to seven.

The remaining S$250 of the S$500 GST-related income tax rebate and the S$3,000 personal relief are to be incorporated into the personal income tax structure for the Year of Assessment 2003.

Comments

- In view of the reduction in the top marginal tax rate and the corresponding adjustment in other income bands, all individual taxpayers will pay less tax.
- Lower personal income taxes are seen as important to attracting and retaining talent, encouraging entrepreneurship and strengthening Singapore's competitiveness as a regional hub.
- The top rate of personal tax of 22% is the same as the proposed corporate tax rate for the Year of Assessment 2003. The government expects to lower both these rates to 20% by the Financial Year 2004 Budget.
- A comparison of the tax payable on equivalent income levels for the Years of Assessment 2002 and 2003 is set out on the facing page.

Personal Income Tax Rates

Comparison of Years of Assessment 2002 and 2003

YA 2003

	S$	Rates	Tax Payable S$	Tax Payable based on YA 2002 Tax Rates * S$	Tax Savings
On the first	20,000	0%	-	6.50	6.50
On the next	10,000	4%	400.00	459.00	59.00
On the first	30,000		400.00	465.50	65.50
On the next	10,000	6%	600.00	594.00	(6.00)
On the first	40,000		1,000.00	1,059.50	59.50
On the next	40,000	9%	3,600.00	4,023.00	423.00
On the first	80,000		4,600.00	5,082.50	482.50
On the next	80,000	15%	12,000.00	12,528.00	528.00
On the first	160,000		16,600.00	17,610.50	1,010.50
On the next	160,000	19%	30,400.00	33,399.00	2,999.00
On the first	320,000		47,000.00	51,009.50	4,009.50
Above	320,000	22%	varies		

* To take into account the proposed incorporation of the personal relief of S$3,000 into the tax bands with effect from YA 2003, for comparison purposes, the comparative tax payable for YA 2002 is computed after deducting S$3,000 from the corresponding YA 2003 taxable income figures. The comparative tax payable also takes into account the 10% and S$250 tax rebates.

YA 2002

	S$	Rates	Tax Payable after 10% & $250 Rebate S$
On the first	7,500	0%	NIL
On the next	12,500	3%	87.50
On the first	20,000		87.50
On the next	15,000	6%	810.00
On the first	35,000		897.50
On the next	15,000	9%	1,215.00
On the first	50,000		2,112.50
On the next	25,000	12%	2,700.00
On the first	75,000		4,812.50
On the next	25,000	15%	3,375.00
On the first	100,000		8,187.50
On the next	50,000	18%	8,100.00
On the first	150,000		16,287.50
On the next	50,000	21%	9,450.00
On the first	200,000		25,737.50
On the next	200,000	24%	43,200.00
On the first	400,000		68,937.50
Above	400,000	26%	varies

Not Ordinarily Resident (NOR) Taxpayer Scheme

Current

Time Apportionment of Income:

- Currently, an individual exercising an employment in Singapore is liable to tax on his full employment income. The current tax rules allow for time apportionment of employment income on a very limited basis, for employees of non-resident companies based in Singapore performing duties in Singapore and other regional countries.

- Under the current basis of taxation, with the exception noted above, employees of Singapore companies with regional/global duties are currently subject to tax on their full employment income, and the work they do when overseas is generally treated as incidental to their Singapore employment by the IRAS.

Remittances of Pre-assignment Income:

- Individuals who are tax residents are currently liable to tax on the foreign source income they remit, transmit or bring into Singapore even if that income was earned prior to their relocation to Singapore.

- As an administrative concession, foreign income received in Singapore by individuals who migrate to Singapore will not be subject to tax, where it can be shown that the foreign income received after such individuals take up residence in Singapore was earned prior to their relocation to Singapore.

Employer's Contributions to Overseas Private Pension Funds:

- In general, contributions by employers to a pension or provident fund constituted outside Singapore are tax deductible for the employer but form part of the employee's taxable employment income.

- Under an administrative concession, such contributions are not taxed on the employees if they are made under a compulsory government social security scheme in the employee's home country and the Singapore employer does not claim a tax deduction for these contributions. Contributions which do not fall under the category of compulsory government social security schemes remain taxable on the employee regardless of the tax treatment adopted by the employer.

Proposed

In line with the ERC Sub-Committee's recommendations, the Minister announced that a new class of taxpayers called "Not Ordinarily Resident" ("NOR") taxpayers will be created. This NOR Taxpayer Scheme will take effect from the Year of Assessment 2003 and will be extended to qualifying individuals for a period of 5 years of assessment.

An NOR taxpayer must meet the following criteria:

(1) He must not have been a Singapore tax resident in the 3 years of assessment before the year he first qualifies for the NOR scheme; and
(2) He must be a tax resident for the year of assessment in which he wishes to qualify for the NOR scheme.

An NOR taxpayer will enjoy the benefit of time apportionment of income only if he meets additional conditions:

(1) He must spend more than 90 days outside Singapore for business; and
(2) He must pay at least a floor tax rate of 10% on his total employment income.

The time apportionment incentive means he pays income tax only on his employment income attributable to the number of days he spends in Singapore per calendar year.

In addition, an NOR taxpayer will enjoy the following benefits:

(1) The remittance of pre-assignment income will be exempt from tax; and
(2) Subject to a limit equivalent to the cap on the employer's contribution to CPF for Singaporeans, the employer's contributions to overseas pension funds on behalf of a non-citizen NOR taxpayer will be exempt from income tax in the hands of the employee.

Comments

- This recommendation would reduce the current disadvantage faced by Singapore previously when compared with Hong Kong, help to attract talent to Singapore and encourage senior management of companies to use Singapore as their base for regional activities.

- Present law permits an effectively quite similar personal tax exemption for income earned outside of Singapore by individuals who are separately employed by non-Singapore employers to perform their non-Singapore duties, provided that the offshore employment income is not claimed as a Singapore tax deduction by the employing entity(ies). The proposal is silent on whether the Singapore employer can claim a corporate tax deduction for the cost of the (tax-exempt) offshore employment income although it appears to be so since the individual must pay at least a floor tax rate of 10% on his total employment income.

- It is not obvious why the NOR Taxpayer Scheme should be available only to individuals who have not been resident in Singapore for the previous 3 years of assessment, or why the scheme should be limited to a maximum period of 5 years.

- The criterion that the individual must not have been a Singapore tax resident in the 3 years of assessment before the year he first qualifies for the NOR scheme disadvantages locals with similar overseas responsibilities as they would be subject to tax on their full Singapore employment income.

- Detailed travel schedules, including overseas trips for business/vacation are likely to be needed to substantiate the number of days outside Singapore. Currently, it is unclear as to how the number of days outside Singapore for business (i.e. work days or calendar days) is computed.

- The NOR scheme appears to be restricted to new expatriates relocating to Singapore or Singapore citizens / Permanent Resident (PR) returning to Singapore after at least three years of absence. For the NOR scheme to apply, the following tax planning points may be considered:

  - An expatriate with overseas responsibilities who arrived in Singapore in Year 2001 and spent less than 183 days in Singapore should not accede to be treated as a tax resident for the Year of Assessment 2002 (under the IRAS' administrative practice of treating an individual as a tax resident if employed in Singapore is at least 3 consecutive years). This may allow him to be covered by the NOR scheme in the Year of Assessment 2003, subject to the IRAS's agreement.

  - A Singapore citizen / PR who exercises employment outside Singapore for more than 6 months in each calendar year may wish to consider making an election to be treated as a non-resident in the years (at least three years) before his overseas assignment ends to avail himself of this NOR scheme if such scheme is more tax beneficial to him.

- The ERC Sub-Committee had recommended that the exemption for remittances of foreign-source income to Singapore be extended also to resident individuals. In addition, the ERC Sub-Committee recommended that expatriates be exempted from tax on their employers' contribution into overseas pension funds. These recommendations have only been partially adopted by the Minister in the form of remittance of pre-assignment income and employer's contributions to overseas pension funds for NOR taxpayers (subject to a cap).

- If the CPF equivalent limits are exceeded, it remains to be seen whether the administrative concession on not taxing the employer's contribution to overseas pension / provident fund under certain circumstances will apply to individuals within the NOR scheme.

- The NOR scheme would effectively reduce the tax equalisation costs for employers who have to bear the tax liabilities of their employees who are relocated to Singapore.

- Illustrations of the NOR scheme are set out on the facing page. It would appear that the 10% floor rate on total employment income would generally apply due to our low personal tax rates unless the individual is a high wage earner. Indeed, at lower income levels, the 10% floor tax rate can exceed the tax payable on all income at the regular personal income tax rates for a resident individual.

Not Ordinarily Resident Taxpayer Scheme Singapore - Year Of Assessment 2003

	Resident	Not Ordinarily Resident	
		75% of time in S'pore	60% of time in S'pore
	S$	S$	S$
Employment income	100,000	75,000	60,000
Employer's contribution to overseas pension fund	20,000	3,960*	3,168*
Total taxable employment income	120,000	78,960	63,168
Less: Personal reliefs:			
Earned Income	(1,000)	(1,000)	(1,000)
Wife	(2,000)	(2,000)	(2,000)
Child	(4,000)	(4,000)	(4,000)
Chargeable Income	113,000	71,960	56,168
Tax payable based on			
- Tax rate table (a)	9,550	3,876	2,455
- 10% of total income (b)	NA	10,528**	10,528**
Tax payable [higher of (a) or (b)]	**9,550**	**10,528**	**10,528**

Assumptions:

1) He is less than 55 years old
2) Married with 2 children
3) Wife has no taxable income
4) Base salary of S$80,000 and bonus of S$20,000
5) He is a foreigner

* Assumption: Actual employer's contribution to overseas pension fund is S$20,000. However, under Singapore CPF capping rules, the statutory contributions are capped at S$14,720. Therefore, the excess of S$5,280 is taxable. His total employment income is S$105,280.

** Floor rate of 10% on total employment income assumed to be calculated as follows:
= 10% x S$105,280
= S$10,528

Not Ordinarily Resident Taxpayer Scheme Singapore - Year Of Assessment 2003

	Resident	Not Ordinarily Resident	
	S$	75% of time in S'pore S$	60% of time in S'pore S$
Employment income	200,000	150,000	120,000
Employer's contribution to overseas pension fund	28,000	6,360*	5,088*
Total taxable employment income	228,000	156,360	125,088
Less: Personal reliefs:			
Earned Income	(1,000)	(1,000)	(1,000)
Wife	(2,000)	(2,000)	(2,000)
Child	(4,000)	(4,000)	(4,000)
Chargeable Income	221,000	149,360	118,088
Tax payable based on			
- Tax rate table (a)	28,190	15,004	10,313
- 10% of total income (b)	NA	20,848**	20,848**
Tax payable [higher of (a) or (b)]	**28,190**	**20,848**	**20,848**

Assumptions:

1) He is less than 55 years old
2) Married with 2 children
3) Wife has no taxable income
4) Base salary of S$150,000 and bonus of S$50,000
5) He is a foreigner

* Assumption: Actual employer's contribution to overseas pension fund is S$28,000. However, under Singapore CPF capping rules, the statutory contributions are capped at S$19,520. Therefore the excess of S$8,480, is taxable. His total employment income is S$208,480.

** Floor rate of 10% on total employment income assumed to be calculated as follows:
= 10% x S$208,480
= S$20,848

Changes To The Tax Treatment Of Stock Options

Current

Under current legislation, the gains derived from the exercise of any stock options granted to an employee by reason of any office or employment are taxable to the employee at the time of exercise of the stock options, for so long as the individual remains employed in Singapore. This is regardless of where the individual is physically located at the time of the exercise or where he was when the options were granted. In general, the gains that are subject to tax are calculated as the difference between the market value of the shares at the date of exercise and the price that is paid for them.

The IRAS has previously issued on 30 June 1997 an Income Tax Interpretation and Practice Note to state their interpretation and application of the existing tax legislation. The IRAS takes the view that where a person was granted a share option prior to his posting to Singapore but exercises the option while he is in Singapore, he is liable to tax in Singapore on the full amount of gains or profits derived from the exercise of the option. Similarly, where a person was granted a share option prior to his posting overseas and who exercises the option while he is employed overseas, the person will not, in general, be subject to tax in Singapore on any gains or profits derived when he exercises the option.

In recent years, the Government has introduced a number of incentive schemes which focus primarily on partial tax exemption for stock option gains, namely the Entrepreneurial Employee Stock Option (EESOP) scheme and the Company Stock Option (CSOP) scheme, as well as the Qualified Employee Stock Option (QSOP) scheme to alleviate the cashflow problems faced by employees who do not sell their shares after exercising their options.

Proposed

As stock options are effective in encouraging entrepreneurship, more companies are using stock options to recruit, motivate and retain talent. Although the Government has already granted favourable tax treatment for some types of stock options, the ERC Sub-Committee had proposed further improvements. In response to these proposals, the Minister has decided to introduce the following changes with effect from the Year of Assessment 2003:

- Exempt from tax stock options granted for non-Singapore employment even if they are exercised in Singapore. To be consistent, gains from stock options granted for Singapore employment will be taxed no matter where they are exercised.

- Tax stock options and restricted share awards at the end of their moratoriums. Where there is a moratorium on the shares, such stock options will be taxed only after the moratorium ends. The taxable gain will be the difference between the market price of the share at the end of the moratorium and the exercise price. Restricted share awards would be treated in a similar way.

- Extend the scope of existing stock option incentive schemes, such as the CSOP scheme, to include other forms of employee share ownership plans. Employee share ownership schemes will now qualify for concessionary tax treatment granted under the current incentive schemes, so long as there is a holding period that achieves similar effect as the vesting period requirement in the current stock option incentive schemes. This will also make it easier for companies to meet the 50% participation rate requirement under the CSOP scheme, as recommended by the ERC Sub-Committee.

- Require Singapore companies to collect the taxes on gains from employees who exercise their stock options after leaving Singapore. These companies will have to track their employees, including ex-employees, and collect the taxes when the employees exercise their stock options, if the employees are allowed to exercise the stock options even after leaving Singapore. Thus, employers who grant stock options should be responsible for declaring the stock option gains when the gains are realised. The IRAS is to release details within three months from the Budget Statement, i.e. by 3 August 2002.

Comments

- The proposal to exempt from tax stock options granted in respect of non-Singapore employment appears to be a reversal of the view taken by the IRAS as stated in the 30 June 1997 Income Tax Interpretation and Practice Note. Individuals who have previously been subject to tax based on current practice on stock options granted during their non-Singapore employment will be at a disadvantage if they also have stock options granted during their Singapore employment and they exercise these stock options after they are employed overseas.

- A relief for double taxation by way of Ministerial remission was previously announced to alleviate double taxation of the gains from stock options granted in respect of non-Singapore employment. As gains from stock options granted for non-Singapore employment are now tax exempt, the remission is no longer applicable. However, if the stock options that were granted in respect of Singapore employment are exercised while employed overseas, double taxation may now occur. It then depends on the overseas country's tax legislation as to whether the individual is able to claim a foreign tax credit or other relief for the Singapore tax suffered.

- This proposal to tax stock options and restricted share awards at the end of their moratorium brings certainty to the timing on the taxation of restricted share awards. It also proposes a departure from the current timing of taxation of stock options where there is a moratorium on the shares, from the point of exercise to the point where the moratorium ends.

- Whilst this proposal serves to alleviate cashflow problems, using the market price at the end of the moratorium period as opposed to the market price at the date of exercise might in practice result in an increase or decrease in the tax payable, depending on the movement in the share prices.

- The proposal to extend concessionary tax treatment granted under the current incentive schemes (which focus primarily on stock option schemes) to other employee share ownership plans, such as employee share purchase plan, will enable more individuals to enjoy beneficial tax treatments. This is in line with the ERC Sub-Committee's call to extend current concessionary tax treatment to other share schemes.

- The ERC Sub-Committee recommended that departing expatriates should settle their taxes on unexercised stock options on a "deemed exercise" basis at the point of departure, but this requirement may be waived if the employer is willing to be accountable for tracking its employees upon their departure from Singapore. While the "deemed exercise" basis has not been accepted (note that the "deemed exercise" basis would create cashflow problems for the employees), the Minister announced the requirement for Singapore companies to track their employees and collect the taxes when the employees exercise their stock options after they leave Singapore.

- It remains to be seen how companies will be able to collect the taxes due on stock option gains from employees who have left Singapore. Prima facie, they could only do so out of money that the individual is due to pay to them in order to exercise the options, and where the options relate to shares in some other group company (such as the group's overseas parent company), there may not be any such money due to the Singapore company.

Donations

Current

Tax deductions for cash donations made by any person are allowed if they are made either to the Government or any institution of a public character ("IPC") in Singapore approved by the Minister on application by the institution concerned.

A deduction is also allowed (under the Computer Donation Scheme) for the value of a computer (including computer software and peripherals), approved by the Minister and donated to a prescribed educational, research or other institution in Singapore. However, this deduction is allowed only to corporate donors.

Artefact donations to Approved Museums are also allowed. The deduction available is an amount not exceeding twice the value of the approved gift, both the amount and value of which are to be determined by the Minister.

With effect from January 2001, deductions are (under the Shares Donation Scheme) also available to individuals who donate to any IPC in Singapore, which is approved by the Minister, gifts of shares in a company listed on the SGX or units in unit trusts traded in Singapore.

No carryforward of the value of the donation is however allowed if there are insufficient profits/income to offset the donation.

In addition, for estate duty purposes, only donations to IPCs specified in a will are exempted from estate duty.

Proposed

To promote the spirit of philanthropy in individuals and corporations, particularly in the current uncertain economic environment where voluntary organisations face some difficulties in raising funds, the Government has decided to introduce the following measures:

- Allow a double tax deduction for all cash donations made to IPCs on or after 1 January 2002. A double tax deduction will also be granted for donations of computers and related peripherals, artefact donations to Approved Museums, and approved shares and unit trusts.

- Individuals and corporations will be allowed to carry forward for 5 years all "unutilised" deductions granted for donations made to IPCs on or after 1 January 2002.

- Some IPCs name their buildings or scholarships after their donors in return for their generous financial

support. A single tax deduction will be granted to such donations made on or after 1 January 2002.

- With effect from 1 January 2002, all donations made from estates will be exempted from estate duty.

- All qualifying charitable private foundations that benefit the local community at large will with immediate effect, enjoy IPC status to help them raise funds for their charitable activities.

Comments

- The decision to grant IPC status to qualifying charitable private foundations and to allow double tax deduction for donations to IPCs is in line with the announcement made by the Prime Minister previously. In his National Day Rally address in August 2001, the Prime Minister indicated that the Government would grant IPC status to private foundations that support charitable activities, to encourage volunteerism and charity work. In addition, the Government will consider giving double tax deductions for donations to these organisations.

- The 5-year carry-forward of any “unutilised” deductions granted for donations would in all likelihood benefit mainly corporate taxpayers. This could well be the Government’s deliberate attempt to encourage corporate donors to be more supportive of charitable organisations.

- As donations with naming opportunities will now be tax-deductible, albeit a single deduction only, charities may attempt to be more innovative in raising funds through naming buildings or scholarships after their benefactors.

- As regards the estate duty exemption for all donations made from estates, it is unclear at this stage as to the circumstances under which a donation made from an estate would be tax exempt. However, it seems clear that the administrator or executor of the estate would have to have the necessary degree of discretion over the distribution of the assets of the estate, and that, in all likelihood, this discretion would need to be made available under the terms of the will.

Personal Reliefs

(A) Handicapped Parent Relief

Current

The current parent relief available to resident individuals is as follows:

■ If the dependent is living in the same household as the taxpayer	S$5,000 per dependent
■ If otherwise and the taxpayer has incurred at least S$2,000 a year for the maintenance of the dependent	S$3,500 per dependent

Proposed

With effect from the Year of Assessment 2003, a handicapped parent relief of S$3,000 is to be introduced. This is on top of the normal parent relief. The total relief granted to taxpayers who take care of their handicapped parents will be S$8,000 if the taxpayers are living with the parents and S$6,500 if otherwise.

Comments

The additional relief is in line with the Government's policy of encouraging families to look after their aged and handicapped parents.

(B) National Service Reliefs

Current

Operationally ready NSmen are entitled to the following reliefs:

■ Those who have performed operationally ready national service	S$2,000
■ Those who have not performed operationally ready national service	S$1,000

In addition, wives, widows and parents of operationally ready NSmen who are Singapore citizens are entitled to a relief of S$500. Each parent will receive the relief regardless of the number of children who have undergone national service.

Proposed

With effect from the Year of Assessment 2003, the reliefs are to be increased as follows:

NSmen who have performed operationally ready national service	S$3,000
NSmen who have not performed operationally ready national service	S$1,500
Wives and widows of operationally ready NSmen	S$ 750
Each parent of operationally ready NSmen	S$ 750

Comment

- The increase in reliefs is in recognition of the commitment and contributions made by the NSmen, especially during an economic downturn.

(C) Personal Allowance

Current

All resident individuals are entitled to an allowance of S$3,000.

Proposed

This allowance is to be withdrawn with effect from the Year of Assessment 2003, and replaced by an extension in the lowest band of income on which no tax is paid.

Comment

- With effect from the Year of Assessment 2003 resident individuals pay no tax on the first S$20,000 of chargeable income, as against S$7,500 in the Year of Assessment 2002. This increase of S$12,500 reflects a combination of the withdrawal of the above personal allowance and of a $250 tax rebate, as well as the generally lower tax rates at all income levels for the Year of Assessment 2003.

(D) Double Child Relief for Children Studying Overseas

Current

This relief is available where an unmarried child is receiving full-time education in a university or equivalent institution outside Singapore after being unable to gain admission to a similar institution in Singapore or is pursuing a course of study not available in Singapore. The deduction is double the normal child relief.

Proposed

With effect from the Year of Assessment 2003, the relief is withdrawn.

Comment

- In view of the opening of the Singapore Management University (SMU) and the Singapore Institute of Management (SIM) open-university, there are now more opportunities for Singaporeans and foreigners alike to pursue tertiary education in Singapore, thus reducing the need to go overseas for further education. In consequence, it is no longer considered necessary for the Government to subsidise overseas education.

(E) Procreation Tax Rebate

Current

The procreation tax rebates granted to parents who have a second, third or fourth child cease to be available for future utilisation if the parents divorce within nine years of the birth of the second, third or fourth child. The rebate will not be given for any year of assessment following the year in which such event takes place.

Proposed

The Government has decided to allow the divorcees to continue to claim their procreation tax rebates with effect from the Year of Assessment 2003. Divorcees whose procreation tax rebates have already been terminated may apply to the IRAS for reinstatement of their rebates if their claim periods have not expired.

Comment

- The procreation tax rebate was granted to encourage parents to bring up their children in an intact family. Although the Government continues to uphold the value of maintaining strong families, nonetheless it recognises that withdrawing the rebate from divorcees can add to an already difficult financial burden. In this respect, the Government has decided not to withdraw the rebate from divorcees.

Tax on Parliamentary Allowances

Current

Members of Parliament (MPs) currently enjoy a tax remission on their allowance as MPs.

Proposed

The tax remission for the MP allowance is withdrawn with effect from the Year of Assessment 2003.

Comment

- As the MP's allowance is regularly revised in step with a private sector salary benchmark, this remission is no longer considered necessary.

Goods and Services Tax Rate Increase

Current

Goods and Services Tax ("GST") was first introduced in Singapore on 1 April 1994 at a single low rate of 3%, as part of the Government's effort to broaden Singapore's tax base and reduce the country's reliance on direct taxes.

Proposed

In order to make up for at least part of the future revenue loss from the recommended corporate and personal income tax cuts, the Minister has proposed that the GST rate be increased from 3% to 5% with effect from 1 January 2003, in line with the recommendations of the ERC Sub-Committee.

The GST system in Singapore is to continue to be applied at a single rate and across-the-board on all goods and services, with as few exemptions as possible. The Government has however announced a very comprehensive GST offset package to help Singaporeans adjust to the rate increase.

Comments

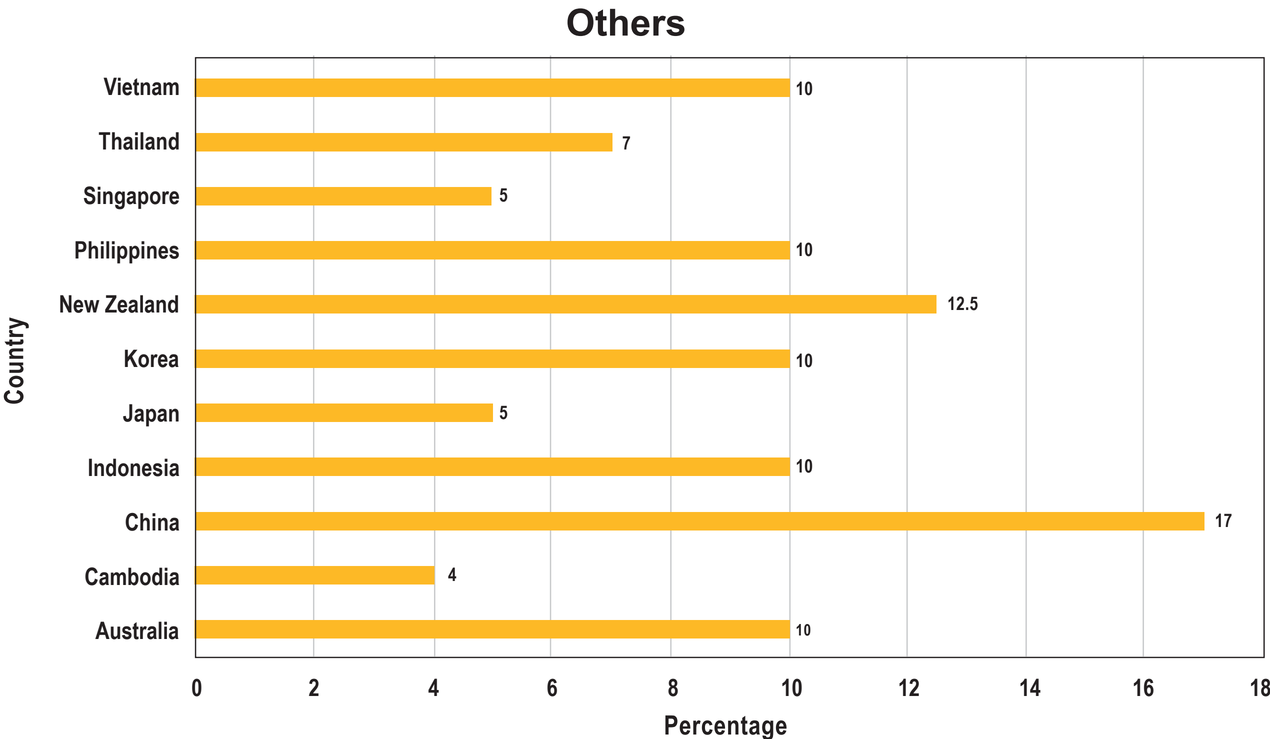
- Although not primarily a tax on businesses, the increase in GST will adversely affect three business sectors:
  - businesses which are not registered for GST, who will incur an additional 2 percent on their purchases from GST registered suppliers, and will have to either absorb the cost or raise their prices;
  - property developers, with projects relating to residential properties, who will suffer additional GST which will flow through as increased costs because these businesses cannot recover input tax relating to these exempt activities; and
  - the financial services industry, due to the inability to fully recover the input tax.
- There will be transitional issues resulting from the change in the rate. For example, unless expressly determined otherwise, contracts which span the change date, will attract the increased rate on subsequent payments.

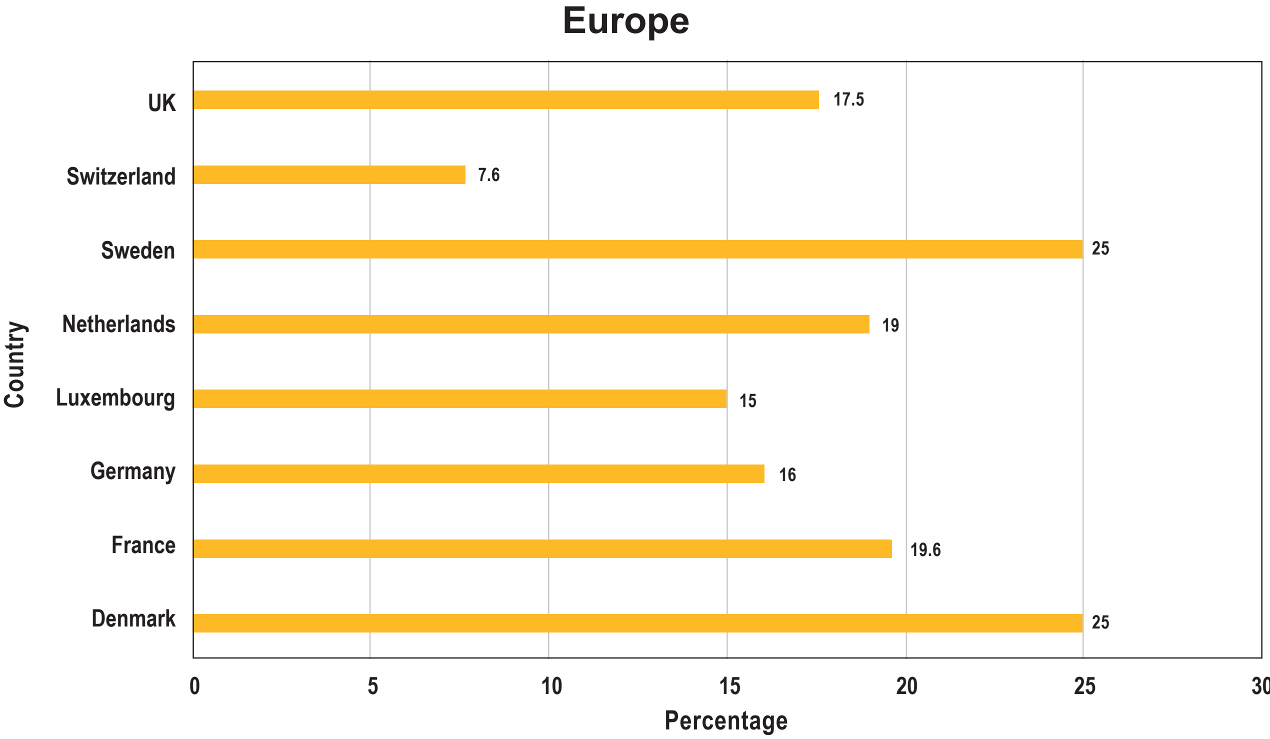
- From a time of supply perspective, a supplier can elect to account for tax on the basic tax point. The effect of the election is that GST may be charged at the old rate on goods removed or services performed before the change, even though a tax point normally would be triggered by the issue of a tax invoice after the change.

- Given the increase in the GST rate, businesses may wish to re-examine their GST systems and procedures to ensure that they are not suffering unnecessary tax or cashflow costs.

- Notwithstanding the proposed increase in GST, the Singapore rate of GST remains low by comparison with VAT and GST rates elsewhere in the world, as indicated in the tables of comparative rates on page 47.

GST Rates In Selected Countries





GST Offset Package

Proposed

To offset the increase in the GST rate, the Government will introduce a comprehensive package of measures to cover the increase in the GST rate for most households, and for all lower income households, for at least 5 years. These comprise:

- **Healthcare**

  Increasing the direct grants to restructured hospitals and polyclinics to ensure that charges for subsidised medical care will not be affected at all by the increase in the GST rate.

- **Education**

  Increasing the subsidy to the state education system to absorb the GST payable on education.

- **Service and Conservancy Charges**

  Increasing the subvention to Town Councils to offset the GST payable on Service and Conservancy charges ("S&CC").

- **Public Transport**

  The transport operators have accepted the recommendation of the Public Transport Council that there is no need to increase the public transport fares for next year.

- **Public Assistance and Singapore Allowance**

  Increasing the Public Assistance rates and the Singapore Allowance paid to government pensioners to further help the very low-income Singaporeans cope with the GST rate increase. The proposals are currently being reviewed and are expected to be implemented in time for the increase in the GST rate next year.

- **Committee to Combat Profiteering**

  Establishing a Committee to Combat Profiteering to deal with any complaints of profiteering or unjustified price increases.

- **Rebates for Service & Conservancy Charges and Rent**

  Extending the S&CC and rental rebates for Housing and Development Board ("HDB") households for 5 more years, from 1 April 2003 to 31 March 2008. The rebates will be maintained at their present levels in the first year, and will thereafter taper off gradually.

- **Economic Restructuring Shares**

  Recognising that the tax cuts over the last decade have resulted in the majority of Singaporeans paying no income tax at all, the Government has decided, as the major part of the GST offset package, to provide all Singaporeans with Economic Restructuring Shares (ERS).

  The key features of the ERS:

  - The value of each share is $1.
  - The shares will yield a guaranteed minimum dividend of 3% per annum.
  - Annual dividends in the form of bonus shares will be distributed over 5 years from 2004 to 2008. The dividends will be paid each year on 1 March.
  - Annual bonus dividends equal to the real GDP growth rate (if positive) of the preceding year will be declared.
  - There is no minimum holding period and the recipient may cash all the ERS at any time, even as soon as they are issued.

  The ERS will be given out in three lots, with one lot each year starting from 1 January 2003. To qualify for each lot, the individual must satisfy the following conditions:

  - Be a Singapore citizen as at 1 December of the year before;
  - Be at least 21 years old on 1 December of the year before; and
  - Put at least $50 into the CPF Account the year before.

- **Citizens' Consultative Committee Assistance Scheme**

  Introducing a Citizens' Consultative Committee ("CCC") Assistance Scheme to further assist households that may find the offset package insufficient to cover the increase in the GST. Under this scheme, any household with an income below the median household income of $3,600 can apply to their CCC for further assistance.

Comment

- As promised, the Government has introduced a very comprehensive GST offset package that is sufficient to offset the net increase in taxes a household will pay over the next 5 years, at least. In fact, based on the Government's analysis, the S&CC rebates, the rental rebates and the ERS shares should cover those living in one-or two-room HDB flats for the next 10 years.

Taxes on Motor Vehicles

Proposed

In line with the ERC Sub-Committee's recommendations to gradually reduce car ownership taxes and shift towards a system based on usage charges so as to strike a better balance between the ownership and usage costs of a car and to rationalise the various fees and charges, the Minister has proposed the following changes on motor vehicle taxes:

- **ARF and Excise Duty for Cars and Taxis**

	Cars		Taxis	
	2001	2002	2001	2002
ARF (% OMV)	140	130	140	130
Excise Duty (% OMV)	31	20	7	10
Total up-front taxes (% OMV)	171	150	147	140

ARF : Additional Registration Fee
OMV: Open Market Value

The proposed changes to the ARF will apply to Certificates of Entitlement ("COEs") obtained with effect from the May 2002 bidding exercise. The proposed changes to the Excise Duty rates will be effective from 4 May 2002.

As the Government is of the view that taxis should be treated like cars, it is the Government's eventual aim to raise the Excise Duty rate for taxis to 20%, to be in line with that for cars.

- **Pegging PARF to ARF**

	Age of Car/Taxi* at De-Registration					
	<5	5 to <6	6 to <7	7 to <8	8 to <9	9 to 10
Current Rate (% OMV)	130	120	110	100	90	80
New Rate (% ARF)	75	70	65	60	55	50

* Taxis have a mandatory life span of 7 years. Their PARF rebates are linked to those of cars.

The Preferential Additional Registration Fee ("PARF") rebate will be pegged to the ARF actually paid on each car, instead of the current practice of pegging the rebate to the OMV. This will allow the PARF to be automatically and proportionately reduced whenever the ARF is lowered.

The proposed change to the PARF will apply to COEs obtained with effect from the May 2002 bidding exercise.

- **Road Tax**

Engine Capacity (cc)	Current Road Tax	New Road Tax
EC ≤ 600	S$500	S$400
600 < EC ≤ 1,000	S$500 + 0.25 (EC – 600) (Max. $600)	S$400 + 0.25 (EC – 600) (Max. $500)
1,000 < EC ≤ 1,600	S$600 + 1.0 (EC – 1,000) (Max. $1,200)	S$500 + 0.75 (EC – 1000) (Max. $950)
1,600 < EC ≤ 3,000	S$1,200 + 1.8 (EC – 1,600) (Max. $3,720)	S$950 + 1.5 (EC – 1,600) (Max. $3,050)
EC > 3,000	S$3,720 + 2.5 (EC – 3,000) (No specific limit)	S$3,050 + 2.0 (EC – 3,000) (No specific limit)

The reduced road tax rates will take effect from September 2002. There will however be no road tax changes for taxis.

- **Certificate of Entitlement**

To further reduce the cost of owning a car, the Government will be releasing an additional 5,000 COEs in Quota Year 2002/2003.

- **Car Parking Charges**

As there is a need to rationalise car parking charges progressively in order to eliminate the current subsidies on car parking costs for motorists, the HDB and the Urban Redevelopment Authority will be announcing details on revision to car parking charges in due course.

- **Electronic Road Pricing ("ERP")**

As the ERP has proven to be an efficient and precise instrument in controlling congestion, with the expected increase in Singaporeans owning cars, the ERP system is to be further expanded to keep the roads in Singapore free flowing.

Comments

- The above measures are intended to allow wide ownership of cars while at the same time keeping congestion at an acceptable level with the expansion of the ERP system.

- Further reductions in ownership taxes (such as excise duty, ARF and road tax) coupled with increases in usage charges (such as ERP charges and perhaps also fuel costs) can be expected in future.

Excise Duties on Alcohol and Tobacco Products

To discourage consumption, and also to iron out some existing anomalies in liquor taxes, excise duties on a range of liquor and tobacco products were raised with effect from Budget Day, 3 May 2002. The increase in the duty rates on liquors range from 10% to 90% and on tobacco products from 17% to 100%.

Estate Duty Relief for Non-Domiciliaries

Current

For individuals not domiciled in Singapore, estate duty is currently charged on both “movable” and “immovable” assets located in Singapore.

Proposed

The “movable” assets, which are essentially all assets other than interests in land and buildings, of non-domiciled individuals will be exempt from estate duty irrespective of where they are located.

Comment

- The exclusion of the “movable” assets of individuals who are not domiciled in Singapore from any liability to estate duty should remove any disincentive for foreigners to hold Singapore dollar denominated investments in Singapore, and help to boost Singapore’s position as a private banking centre.

Foreign Worker Levy

Current

The Foreign Worker Levy ("FWL") is payable by employers in respect of their foreign workers. Currently it is levied at reduced rates which range from $30 to $470 per month, depending on the category of the foreign worker.

These FWL rates were first introduced in 1999 to help employers through the 1998 economic downturn, and were later extended to July 2002 due to the current economic recession.

Proposed

The reduced rates will now be extended for a further 6 months until December 2002.

Comment

- The Government has indicated that it will review the position again towards the end of the current calendar year. Unless the current economic downturn persists, it seems likely that these rates will be raised at that time.

Office

Ernst & Young Singapore

10 Collyer Quay
#21-01 Ocean Building
Singapore 049315

Tel: 6535 7777
Fax: 6532 7662
Email: contact.eys@sg.eyi.com
Website: www.ey.com/sg

Tax Partners And Directors

Ang Siew Lian — 6428 6607
Email: siew-lian.ang@sg.eyi.com

William Chua — 6428 6635
Email: william.chua@sg.eyi.com

Robert Lee — 6428 6688
Email: robert.lee@sg.eyi.com

Cindy L H Lim — 6428 6677
Email: cindy.lim@sg.eyi.com

Low Weng Keong — 6428 6686
Email: weng-keong.low@sg.eyi.com

Latha Mathew — 6428 6609
Email: latha.mathew@sg.eyi.com

Florence Ng — 6428 6632
Email: florence.ng@sg.eyi.com

Peter Arnett — 6428 6270
Email: peter.arnett@sg.eyi.com

Pok Soy Yoong — 6428 6616
Email: soy-yoong.pok@sg.eyi.com

Jean de Souza — 6428 6636
Email: jean.de-souza@sg.eyi.com

Tan Lee Khoon — 6428 6679
Email: lee-khoon.tan@sg.eyi.com

Steven M Timms — 6428 6668
Email: steven.timms@sg.eyi.com

Steven Yap — 6428 6778
Email: steven.yap@sg.eyi.com

Lisa Lim — 6428 6643
Email: lisa.lim@sg.eyi.com

Stephen Daas — 6428 6600
(US Personal Tax Division)
Email: stephen.daas@sg.eyi.com

Jeffrey Teong — 6428 6610
Email: jeffrey.teong@sg.eyi.com

Mike Vaughan — 6428 6739
Email: mike.vaughan@sg.eyi.com

Office

Arthur Andersen Singapore

10 Hoe Chiang Road
#18-00
Keppel Towers
Singapore 089315

Tel: 62204377
Fax: 62234795
Website: www.andersen.com.sg

Tax Partners And Directors

If you would like to know more about the issues discussed and our services, please contact your tax engagement partner or manager or any of the following:

Winnie Liew 64218225
Email: winnie.liew@sg.andersen.com

Cheong Choy Wai 64218226
Email: choy.wai.cheong@sg.andersen.com

Chong Lee Siang 64218202
Email: lee.siang.chong@sg.andersen.com

Juliana Ng 64218207
Email: juliana.ng@sg.andersen.com

Kang Choon Pin 64218204
Email: choon.pin.kang@sg.andersen.com

Choo Eng Chuan 64218212
Email: eng.chuan.choo@sg.andersen.com

Nurhajati Zainol 64218218
Email: nurhajati.zainol@sg.andersen.com

Chung Siew Moon 64218219
Email: siew.moon.chung@sg.andersen.com

Jacinta Loi 64218214
Email: jacinta.loi@sg.andersen.com

Soh Pui Ming 64218215
Email: pui.ming.soh@sg.andersen.com

Lim Lee Ching 64218285
Email: lee.ching.lim@sg.andersen.com

Yeo Kai Eng 64218208
Email: kai.eng.yeo@sg.andersen.com

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