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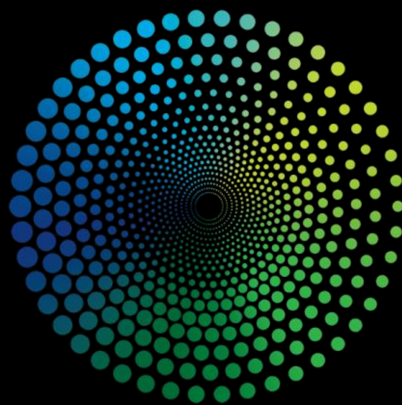

Singapore Business Tax developments

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Greetings from your Tax & Legal team at Deloitte Singapore. We hope that you and your loved ones are staying safe and healthy despite these challenging times. As we navigate ourselves through this trying period, we are committed to giving you the support you need.

We are pleased to share the following with you.

GCN v Comptroller of Income Tax [2020] SGITBR 2

The decision of *GCN v Comptroller of Income* [2020] SGITBR 2 was issued on 27 April 2020. The dispute concerns the calculation of notional section 19 capital allowances for the purpose of determining the residue of expenditure (RoE) under section 13A(11) of the Income Tax Act (ITA).

Broadly, companies operating Singapore-registered ships will enjoy tax exemption on qualifying shipping income under section 13A of the ITA. However, where the ship ceases to be a Singapore ship, the RoE has to be determined under section 13A(11) of ITA for such ship for that Year of Assessment (YA) and subsequent years. RoE is essentially the cost of the ship less any notional capital allowances that would have been claimed in the YAs that the ship continues to derive exempt income.

Background

GCN is a company incorporated in Singapore in August 2003 and claimed exemption of qualifying shipping income under section 13A of the ITA. In 2010, GCN was found to engage in activities that was disallowed under the Merchant Shipping Act and it had to de-register two of its ships from the Singapore Registry of Ships by 26 August 2010.

Given the de-registration, the exemption of shipping income under section 13A of the ITA could no longer apply and hence the RoE under section 13A(11) had to be determined for each of the ships for tax purposes in YA 2011 and subsequent years.

In computing the RoE, GCN, and the Comptroller of Income Tax used the following basis:

Party	Position taken
GCN	Took into account only the annual allowances (AA) claimable under section 19(2) of the ITA as the notional capital allowances.
Comptroller of Income Tax	Took into account both the initial allowance (IA) and AA claimable under sections 19(1) and 19(2) of the ITA as the notional capital allowances.

Relevant provisions in the ITA are as follows:

Provisions	Details
Section 13A(11)	"Where in the basis period for any year of assessment a ship ceases to be a Singapore ship the income derived from the operation of which is exempt under this section, the capital allowances in respect of that ship for that year of assessment and subsequent years shall be calculated on the residue of expenditure or reducing value of the assets after taking into account the capital allowances provided for in sections 16, 17, 18, 18B, 18C, 19, 19A, 20, 21, and 22 for those years of assessment during which income derived from the operation of the ship was exempt from tax **notwithstanding that no claim for such allowances was made**." (emphasis added)
Section 13A(12)	Section 13A(11) "shall have effect notwithstanding any other provisions of this Act.
Section 19(1)	"Where a person carrying on a trade, profession or business incurs capital expenditure on the provision of machinery or plant for the purposes of that trade, profession or business, there shall be made to him, <u>on due claim</u> for the year of assessment in the basis period for which the expenditure is incurred an allowance, to be known as an "initial allowance", equal to one-fifth of that expenditure or such other allowance as may be prescribed either generally or for any person or class of persons in respect of any machinery or plant or class of machinery or plant." (emphasis added)

Due to the difference in the basis of computing the RoE (which resulted in lower RoE under the position adopted by the Comptroller and hence lower capital allowance claimable against non-exempt shipping income), there was an increase in tax liability for GCN of about $1,215,559 for YAs 2011 to 2013 and there would be an increase in future tax liability in excess of $800,000 for the rest of the tax life for the two ships.

Salient Arguments

The salient arguments adopted by the parties are as follows:

Party	Arguments
GCN	Taxpayer should have the option of deciding whether to take into account only AA or both IA and AA when computing the RoE. This is because section 19(1) provides that IA shall be granted to a taxpayer only on "due claim" and there was no such claim made by GCN at the material time. Even though section 13A(11) provides "notwithstanding that no claim for such allowances was made", this should not result in a situation where a taxpayer is deprived of his option of claiming IA only "on due claim" as provided in section 19(1) which is available to taxpayers ordinarily. The normal operation of the provision in section 19(1) should not be changed simply because it is invoked for purposes of fulfilling the requirements under section 13A(11).
Comptroller of Income Tax	Section 13A(11) needs to be applied based on a literal reading of the provision "notwithstanding that no claim for such allowances was made". For this reason, both IA and AA under sections 19(1) and 19(2) respectively needs to be taken account in determining the RoE of the ships.

Decision

The Board held that section 13A(11) of the ITA is to be applied based on a literal reading of the provision. The provision "notwithstanding that no claim for such allowances was made" should be interpreted to mean that all capital allowances under section 19 should be included for purposes of calculating the RoE of the ships, including the IA under section 19(1). Furthermore, the Board held the view that section 13A(12) is relevant for this case, and in effect negated the "due claim" basis under section 19(1), such that section 13A(11) has its intended effect.

In this regard, GCN lost the appeal.

Deloitte Singapore's views

The Board's decision provides more clarity on a perennial issue in computing the RoE under section 13A(11) of the ITA, subject to any further appeals by the taxpayer. This is a common issue faced by shipping enterprises when the Singapore-flagged vessels have been re-flagged.

The main argument of the decision appears to surround the interpretation of the phrase “notwithstanding that no claim for such allowances was made” under section 13A(11) of the ITA. The Board, which endorsed the Comptroller’s arguments, seems to adopt a narrower interpretation in which the computation of RoE would encompass all capital allowances claimable under section 19 of the ITA, thereby reducing the RoE and hence the amount of capital allowances actually claimable in later years. This is counter-intuitive to the normal application of section 19(1), which operates on a due claim basis and is only available in the year that the expenditure is incurred.

The Board’s decision is likely to have a wider implication on companies with tax incentives. Broadly, capital allowance claims are mandatory for companies with certain concessionary tax rates. For such companies that are claiming Section 19 (i.e., non-accelerated) capital allowances, the decision may support the position that both the initial and annual allowances should be claimed, given that the similar wordings of “notwithstanding that no claim for such/those allowances has been made” are also found in the tax provisions relating to such tax incentive schemes. Examples of such schemes include the Maritime Sector Incentive (MSI)-Approved International Shipping Enterprise, MSI-Maritime Leasing and MSI-Shipping-related Support Services schemes, the Pioneer and Development & Expansion Incentive schemes, Aircraft Leasing Scheme, etc. Companies that have adopted a different position, i.e., only claimed AA to effectively “slow down” the capital allowance claim, may wish to review their position and determine if such position remains supportable. This could either be from a cash tax perspective or from a tax provisioning/deferred tax perspective.

Contacts

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