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CHINA

CHINA GOVERNMENT EXTENDS FAVORABLE POLICIES OF IIT.

The Chinese government has taken steps to ease the burden on taxpayers by issuing important announcements regarding various aspects, especially the Individual Income Tax (IIT) policies.

On August 28th, the Ministry of Finance and the State Taxation Administration issued the "Announcement on Extending the Implementation of the Annual One-time Bonus Individual Income Tax Policy." The announcement states that if a resident individual receives an annual one-time bonus that meets the provisions of the "Notice of the State Taxation Administration on Adjusting the Calculation and Collection of Individual Income Tax for Annual One-time Bonuses" (Guoshui Fa [2005] No. 9), it will not be included in the comprehensive income of the current year. Instead, the annual one-time bonus income will be divided by 12 months. The applicable tax rate and quick deduction amount will be determined based on the monthly converted comprehensive income tax rate table attached to this announcement. The tax will be calculated separately.

Furthermore, recognizing the importance of supporting international businesses and foreigners, the government has also unveiled an announcement concerning income tax policies on subsidies specifically aimed at this group. Foreign individuals meeting the criteria of resident individuals have the option to choose either the special additional deduction for individual income tax or to follow the provisions outlined in previous notices, including exemptions and reductions on subsidies for housing, language training fees, children's education expenses, and other allowances. However, simultaneous enjoyment of these benefits is prohibited, and once a choice is made, it cannot be changed within a tax year.

These policies will remain in effect until **December 31, 2027**, providing stability and predictability for taxpayers and foreign individuals alike. If you require assistance with navigating these tax policies and maximizing their benefits, Acclime is always available to guide you through the process smoothly.

Pre-tax additional deduction for R&D expenses

In order to further encourage enterprises to increase investment in research and development (R&D) activities, and to better support technological innovation, the Ministry of Finance and the State Tax Administration jointly issued the latest announcement about the pre-tax additional deduction for R&D expenses in March 2023. According to this announcement, enterprises are allowed to deduct an additional 100% of R&D expenses on top of actual expenses incurred if the R&D has not formed intangible assets. If intangible assets are formed, the enterprises are allowed to use 200% of the cost of intangible assets as the amortizing basis. Compared to the previous policies, this announcement extends the scope of enterprises that can enjoy the highest deduction rates to most enterprises. In the past, the highest additional deduction was only limited to certain industries or certain types of enterprises.

Even though the scope has been extended, the industries that are excluded from additional R&D deductions have not been changed. These industries include the tobacco manufacturing industry, accommodation and catering industry, wholesale and retail industry, real estate industry, leasing and business services industry, and entertainment industry. In addition, this additional R&D deduction policy can only be applied to resident enterprises that have a sound accounting system, calculate and pay tax based on accounting books, and are able to trace and bookkeeping R&D expenses correctly.

To better trace and bookkeep qualified R&D expenses, it must first know what R&D expenses cover. Below is a summary of the most common R&D expenses:

- **Personnel expenses**

Qualified R&D personnel expenses are only limited to personnel who are directly engaged in R&D activities. If the personnel also conduct non-R&D activities, the enterprise should make necessary records and adopt reasonable methods to allocate expenses between R&D activities and non-R&D activities.

- **Direct expenses**

These expenses mainly include materials, fuel, and power that are directly invested and consumed in R&D activities, and include rent, repair, and maintenance fees for the equipment and instruments participating in R&D activities. Like the above, if the equipment and instruments are used in both R&D and non-R&D activities, records and allocation are also needed.

- **Depreciation expenses**

As the name implies, depreciation expenses incurred by equipment used for R&D activities can also be treated as qualified R&D expenses. Still, records and allocation should also be done if the equipment is not purely used in R&D activities.

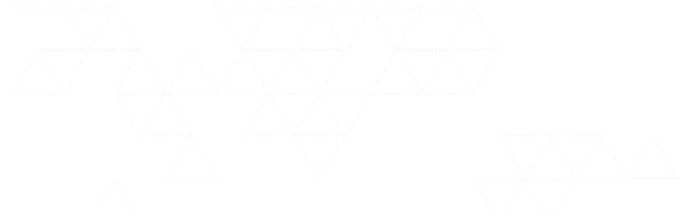
- **Amortization expenses**

While conducting R&D activities, intangible assets such as software, patents, and non-patented technology always play an important role. The amortization expenses on these intangible assets (the portion contributed to R&D activities) can also be treated as qualified R&D expenses.

- New product design fees, new procedure formulation fees, clinical trial fees for new drug development, and field test fees for exploration and development technology.

- Other related expenses. This category refers to miscellaneous expenses directly related to R&D activities, such as book and material fees, translation fees, export consulting fees, appraisal, and evaluation fees, etc.

The handling method of enjoying additional R&D deduction is unchanged, which is still "based on actual R&D expenses, making an independent judgment, declaring for enjoyment, and retaining the relevant materials for future reference". When the enterprises file their Corporate Income Tax (CIT) returns for the third quarter (quarterly filing enterprises) or September (monthly filing enterprises), the enterprises are allowed to choose if they will include additional deductions calculated based on R&D expenses incurred in the first three quarters in this filing and adjust it to the whole year amount while doing CIT annual filing, or just simply wait until annual filing to declare the whole year additional deductions all at once.



Compiled by Mandy Liu on 15 December 2023

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SINGAPORE

SINGAPORE ENACTS SECTION 10L ON TAXATION OF GAINS FROM THE SALE OF FOREIGN ASSETS

To align with European Union laws and comply with international standards the following section 10L of the Singapore Income Tax Act has been introduced that will become effective from 1 Jan 2024. It allows the taxation of foreign disposal gains that are received in Singapore in the absence of real economic activities.

Section 10L(1) of the Singapore Income Tax Act stipulates -

"Despite anything in this Act, gains from the sale or disposal by an entity (called in this section the seller entity) of a relevant group of any movable or immovable property situated outside Singapore at the time of such sale or disposal or any rights or interest thereof (called in this section a foreign asset), that are received in Singapore from outside Singapore, are treated as income chargeable to tax under section 10(1)(g) for the year of assessment relating to the basis period in which the gains are received in Singapore."

The Singapore government has passed the above section 10L legislation to apply from 1 Jan 2024 relating to the gains from the sale or disposal of a foreign asset.

The above law applies to a relevant entity which is part of a relevant group in which entities in the group are not all incorporated or established within a single jurisdiction, that is, in Singapore or any entity of the group has a place of business outside of Singapore. In other words, if one of the entities of the group has a place of business, such as a branch or a permanent establishment outside of Singapore, the group is considered a relevant group for the application of s10L purposes.

Please note that the section 10L provision does not apply to the following:

a. Prescribed financial institutions
b. Entities deriving income that is exempt under section 13A, 13E, 43C,43E,43I,43L,43N,43Q,43R or 43U
c. Entities deriving income that is exempt or taxed as a concessionary tax rate under the Economic Expansion Incentive (Relief from Income Tax) Act 1967
d. Entity that is an excluded entity.

With reference to (d), an excluded entity refers to either a pure equity-holding entity **("PEHE")** or an entity that is not a pure-equity-holding entity **("NPEHE").** A PEHE means an entity whose function is to hold shares or equity interest in any other entity, and that has no other income other than dividends, gains on the sale or disposal of shares or equity interests or income incidental to its activities of holding shares or equity interest in any other entity.

A PEHE is an excluded entity if -

- It submits statutory returns that are required under Singapore laws on a regular basis;

- Its operations are managed and performed in Singapore subject to the direct and effective control of the entity, whether by its employees or by other persons, and
- It has adequate human resources and premises in Singapore to carry out the above operations.

An NPEHE is an excluded entity if –

- Its operations are managed and performed in Singapore subject to the direct and effective control of the entity, whether by its employees or by other persons;
- It has **adequate economic substance** in Singapore, taking into account the following considerations:
- The number of full-time employees of the entity or other persons managing or performing the entity's operations in Singapore;
- The qualifications and experience of such employees or other persons;
- The amount of business expenditure incurred by the entity in relation to its operations in Singapore and
- Whether key business decisions of the entity are made by persons in Singapore.

Impact of section 10L on Singapore as a holding company jurisdiction

Singapore has been an attractive holding company jurisdiction on many fronts, including having a relatively low tax jurisdiction that only imposes tax on income, whereby capital gains are exempt from tax. The tax imposed on income is on a territorial basis; in other words, on income accrued in or derived from Singapore or received from outside Singapore. Capital gains were never subject to any tax, regardless of whether such gains were received in Singapore or not.

However, with the introduction of s10L, capital gains derived from the disposal or sale of foreign assets by a Singapore entity, which is part of a relevant multinational group, may potentially suffer capital gains tax if it does not qualify as an excluded entity.

The s10L may adversely impact a PEHE if it is set up in Singapore as a holding company having entities in the region if it does not qualify to be an excluded entity. One of the criteria to be an excluded entity requires some economic substance, which has been defined to include its operations carried out in Singapore, including premises more than a registered office address provided by a professional corporate secretarial firm.

A PEHE should meet the adequate premises criterion if –

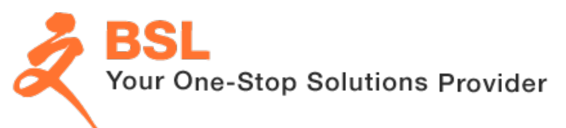
- It has an office in Singapore for the use of its employees (including rented premises or co-working office space.
- It shares a premise with an associated entity for the use of its employee(s) or
- The outsourced service provider performing the PEHE's core income-generating activity has an office in Singapore.

The economic substance as laid out above should be met in the year of disposal of the foreign asset. Therefore, a PEHE should maintain a Singapore premise and have employee(s) working in Singapore or outsource its business activities to a service provider to prove economic substance to qualify to be an excluded entity, to exempt from tax its capital gain that is received in Singapore from the disposal of foreign assets.

To provide certainty, in anticipation of a proposed sale of foreign assets, the taxpayer can apply for an advance ruling on the adequacy of its economic substance. The advance ruling application must be made, provided the disposal of the foreign assets is to take place within one year from the date of application.

As this is relatively new legislation, there should be further clarity, guidance and assistance provided by the Inland Revenue Authority of Singapore as they continue to fine-tune and implement s10L.

Compiled by N Vimala Devi 15 December 2023



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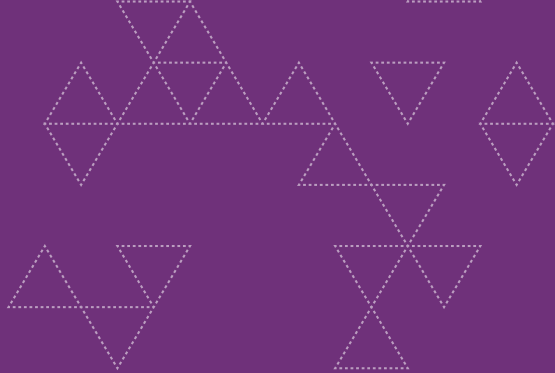

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