MHC & ASSOCIATES, DFK
CERTIFIED PUBLIC ACCOUNTANTS

AROUND US

VOL.3
ISSUE 5
DECEMBER 2003

UPDATES OF TAX CHANGES

Introduction

We summarise some changes to taxation as a result of recent changes in the Income Tax treatment of foreign exchange gains or losses for businesses, Goods and Services Tax ("GST") rate and Central Provident Fund ("CPF") contributions below.

Income Tax Treatment of Foreign Exchange Gains or Losses

On 28 November 2003, IRAS issued a guideline on the income tax treatment of foreign exchange gains or losses for businesses.

We summarise in brief the existing and new income tax treatment below:

<u>Existing income tax treatment</u>

For Singapore income tax purpose, unrealised gains are not taxable and unrealised losses are not tax deductible until they are realised. Furthermore, businesses have to ascertain whether the gains or losses are revenue or capital in nature. Any exchange gains or losses of a capital nature are not taxable or tax deductible respectively.

<u>New income tax treatment</u>

The IRAS has reviewed the income tax treatment of foreign exchange gains or losses. With effect from Year of Assessment 2004, businesses are no longer required, for income tax purposes, to distinguish between realised and unrealised foreign exchange differences. Hence, all foreign exchange gains or losses recognised in the profit and loss account which are revenue in nature, will be taxable or tax deductible respectively in the same accounting period even if they are not realised yet. For your information, this treatment has been accorded to banks since 1993. Foreign exchange gains or losses of a capital nature remain not taxable or tax deductible as in the past.

The above concession will be granted to businesses automatically unless they wish to opt out. The opt out can be done when submitting their Year of Assessment 2004 income tax return. The decision to opt out of this concession will be irrevocable. Once the company opts out, the new tax treatment will not be applicable and the company will continue with the existing tax treatment.

GST Rate

The GST rate will be increased to 5% from 1 January 2004. The IRAS has issued a guideline for GST-registered businesses in November 2003 to prepare them for the rate change. The IRAS has also compiled a list of frequently asked questions to help businesses further understand the application of the transitional rules.

Please click www.iras.gov.sg/data/etax/faq_gst_rate_change.htm to read the details.

CPF Wage Ceiling

Ordinary Wages

With effect from 1 January 2004, the CPF contributions on monthly ordinary wages will be capped at $5,500 for both employers and employees.

Employees who are earning above $5,500 per month will have a higher take home pay. However, in view of the reduction in their CPF tax relief, their personal income tax will increase. Overall income to employees will also be lowered as a result of reduced CPF contributions from employers.

Additional Wages

Current additional wage ceiling for CPF contributions is:

Total Ordinary Wages for the year	Additional Wage Ceiling
≤ $72,000	$100,000 – Total Ordinary Wages
> $72,000	40% of Total Ordinary Wages

The new additional wage ceiling for CPF contributions with effect from 1 January 2004 will be as follows:

Additional Wage Ceiling	$93,500 – Total Ordinary Wages subject to CPF contributions in the year

The scope to optimise remuneration package by maximising the CPF relief is now reduced in view of the new ceiling limit. For employees whose monthly ordinary wages exceeds $5,500, the maximum CPF relief is capped at $18,700 (i.e. $93,500 @ 20%) for the Year of Assessment 2005, assuming no further CPF changes in 2004. Their personal income tax will increase with the corresponding reduction in CPF relief.

CPF Contribution Rates

The changes to the CPF contribution rates are as follows:

	Total	Employer	Employee
Prior to 1 October 2003	36%	16%	20%
With effect from 1 October 2003	33%	13%	20%

The reduced employer CPF contribution rates together with the reduction in salary ceiling represent cost savings to employers. The overall income of employees are reduced accordingly.

The reduced employee CPF contribution rates will provide a higher take home pay for employees but result in a higher personal tax burden due to reduction in the CPF relief claimable.

Tax Relief for CPF Contributions for Self-Employed

With the reduced CPF contribution rates and salary ceiling, the tax relief for CPF contributions from self-employed individuals will be lowered from $25,920 to $25,380 (i.e. [$6,000 X 9 X 36%] + [$6,000 X 3 X 33%]) for 2003. The CPF tax relief will be further lowered in 2004 to $21,780 due to the lower CPF salary ceilings (i.e. $5,500 X 12 X 33%), assuming no further CPF changes in 2004.

Limit on Voluntary CPF Contributions

With the reduction in CPF contribution rates and salary ceiling, the limit on voluntary CPF contributions will be lowered with effect from 1 January 2004. The new limit will be $23,760 (i.e. $5,500 X 36% X 12 months) for 2004 as compared to $28,800 for 2003. Please see table below. Foreigners are not allowed to contribute CPF since 1 January 2003.

Mandatory Contributions ("MC")	Maximum Voluntary Contributions ("VC")
MC < $23,760	Maximum VC = $23,760 – MC
MC ≥ $23,760	VC = $0

Although voluntary CPF contributions are allowed up to the limit specified above, tax deductions/reliefs are given only for mandatory contributions. Employers that are compensating their employees for the shortfall in CPF via the additional 3% voluntary contribution will not get a tax deduction for the 3% voluntary contribution whereas the same amount will be treated as additional income of the employees.

Conclusion

The changes mentioned above will take effect in their respective effective dates. Businesses must be aware and ready for these changes to ensure compliance and prepare for the impact to their bottom line and cash flows.