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IRAS e-Tax Guide

Certainty of Non-taxation of Companies' Gains
on Disposal of Equity Investments
(Third Edition)



Certainty of Non-taxation of Companies' Gains on Disposal of Equity Investments

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1 Aim

- 1.1 This e-Tax Guide provides details on the tax measure to give upfront certainty of non-taxation to companies which derive gains from disposal of equity investments.
- 1.2 It is relevant to a company ("divesting company") that disposes of investments in ordinary shares of another company ("investee company") on or after 1 Jun 2012.

2 At a glance

- 2.1 A scheme to provide upfront certainty of non-taxation to divesting companies ("the scheme") was introduced in Budget 2012. Under the scheme, the gains derived by a divesting company from its disposal of ordinary shares in an investee company are not taxable, subject to conditions. The scheme is applicable to share disposals made during the period of 1 Jun 2012 to 31 Dec 2027.
- 2.2 To qualify for the tax treatment, the divesting company must have held at least 20% of the ordinary shares in the investee company for a continuous period of at least 24 months prior to the date of share disposal. Exclusions apply if the divesting company is subject to certain tax rules or if the investee company engages in certain types of activity.
- 2.3 Where the scheme is not applicable or availed of, the determination of whether gains or losses from a disposal of equity investments are income or capital in nature will continue to be based on the badges of trade and the facts and circumstances of each case. Normal tax rules apply to such gains or losses.

3 Background

- 3.1 In Budget 2012, Deputy Prime Minister and Minister for Finance announced that certainty of non-taxation will be given on gains derived by a company from disposal of equity investments that meet the specified conditions.
- 3.2 The certainty of non-taxation scheme is intended to facilitate companies' restructuring for growth and consolidation¹, enhance Singapore's attractiveness as a business location and minimise compliance costs for taxpayers.

4 Current Tax Treatment

- 4.1 Singapore does not tax capital gains. Therefore, only gains or losses of an income nature derived by a company from disposal of equity investments in another company are taxable or deductible for tax purposes.
- 4.2 The determination of whether a gain or loss from disposal of equity investments in a company is income or capital in nature is based on a consideration of the facts and circumstances of each case. The factors considered are drawn from established case law principles². They include motive of the seller when it acquired the shares, length of period of ownership of the shares disposed, frequency of similar transactions, reasons for the disposal and means of financing the acquisition of the shares.

5 Certainty of non-taxation scheme

- 5.1 The scheme is provided in Section 13Z of the Income Tax Act. It is applicable to disposals of ordinary shares in an investee company made during the period 1 Jun 2012 to 31 Dec 2027 (both dates inclusive).³ It is applicable regardless of whether the investee company is –
- (a) incorporated in Singapore or elsewhere;
 - (b) listed⁴ or non-listed.

¹ The restructuring of companies often involves the acquisition and disposal of equity investments in their associates and subsidiaries.

² The factors considered are commonly referred to as the badges of trade.

³ It was announced in Budget 2020 that the scheme which was originally effective for the period 1 Jun 2012 to 31 May 2022 is to be extended till 31 Dec 2027.

⁴ Listed on the Singapore Exchange (SGX) or an exchange elsewhere

5.2 Condition for the scheme

5.2.1 In line with the policy objectives stated in paragraph 3.2, the scheme is only applicable to a divesting company that owns a sizeable level of ordinary share capital⁵ of an investee company for a reasonable length of time. It is not applicable to a disposal of shares of a preferential nature or shares with redeemable or convertible features.

5.2.2 Under the scheme, gains⁶ derived by a divesting company from its disposal of ordinary shares in an investee company are not taxable if immediately prior to the date of share disposal –

the divesting company had held at least 20%⁷ of the ordinary shares in the investee company for a continuous period of at least 24 months⁸.

5.2.3 The example in **Annex A** illustrates the application of the condition.

6 Exclusions from the scheme

6.1 Besides the condition mentioned in paragraph 5.2.2, the divesting company needs to ensure that it is not an 'excluded divesting company' (paragraph 6.3) and the shares disposed are not those in an 'excluded investee company' (paragraph 6.4).

6.2 The flowchart in **Annex B** illustrates the application of the scheme to a divesting company.

⁵ Ordinary shares typically carry voting rights and entitle their holders to variable rates of dividends unlike preference shares.

⁶ On the other hand, the determination of income or capital nature of any losses incurred by a divesting company from disposal of ordinary shares under similar circumstances (i.e. as set out in paragraph 5.2.2) will continue to be made based on consideration of the facts and circumstances surrounding the disposal of shares. Please refer to paragraph 7.1(a) for more details.

⁷ A shareholding of at least 20% is considered a reasonably sizeable ownership and may be a proxy indicator that the investment is not a portfolio investment. In addition, a similar 20% threshold is also used as an indication of significant influence for "associate companies" under the Singapore Financial Reporting Standards and associate companies are usually acquired for long-term strategic purposes.

⁸ Under the scheme, this means that for every day of the 24 months, the divesting company must maintain a minimum ordinary shareholding level of at least 20% in the investee company whose ordinary shares are being disposed of.

6.3 Excluded divesting company

6.3.1 The scheme does not apply to a divesting company whose gains or profits from the disposal of shares are included as part of its income based on the provisions of section 26 of the Income Tax Act.

6.4 Excluded investee company

Disposals of shares before 1 Jun 2022

6.4.1 The scheme does not apply to disposals of non-listed shares, before 1 Jun 2022, in an investee company if –

- (a) the investee company is in the business of trading Singapore immovable properties; or
- (b) the investee company's principal activity is that of holding Singapore immovable properties, whereby passive or no income is derived.

6.4.2 However, an investee company that is in the business of property development is not excluded from the scheme. The scheme also remains applicable in respect of an investee company that is in the business of letting immovable properties and thus subject to the provisions of section 10E of the Income Tax Act.

Disposals of shares on or after 1 Jun 2022

6.4.3 As announced in Budget 2020, a refinement in the scope of exclusion is made to ensure consistency in the tax treatment for property-related businesses. For disposals of shares on or after 1 Jun 2022, the scheme does not apply to disposals of non-listed shares in an investee company if –

- (a) the investee company is in the business of trading immovable properties (situated in Singapore or elsewhere);
- (b) the investee company's principal activity is that of holding immovable properties (situated in Singapore or elsewhere), whereby passive or no income is derived; or

- (c) the investee company has undertaken property development activities (in Singapore or elsewhere). An exception to this exclusion is where both of the following conditions are satisfied:-
 - (i) the immovable property developed is used by the investee company to carry on its own business⁹ to derive trade income¹⁰. Such a business includes the business of letting immovable properties; and
 - (ii) the investee company did not undertake any property development activity in the past 60 months before the disposal of shares.

For example, an investee company that uses a self-developed immovable property entirely to derive passive rental income (not assessed as a trade income) is excluded from the scheme.

On the other hand, the scheme remains applicable to an investee company that uses a self-developed immovable property as a factory to carry on its manufacturing business. This is provided that, on the date of share disposal, the investee company did not undertake any property development activity in the past 60 months.

6.4.4 **Annex C** provides more examples to illustrate the application of the scheme to an investee company that has undertaken property development activities.

6.4.5 Property development activities in paragraph 6.4.3(c) refer to the construction or causing the construction of any building (or part of a building), including the acquisition of land or building for such construction.¹¹ Particularly for additions and alternations, only structural changes made to a building are considered as construction of a building. Therefore, so long as the building works do not require an approval from the Commissioner of Building Control under the Building Control Act, the building works would not constitute property development activities for the purpose of this scheme. Where building works are done overseas, whether the building works constitute "construction" would be determined based on whether the building works would have required an approval from the Commissioner of Building Control if such building works were done in Singapore.

⁹ To avoid doubt, immovable properties that constitute the trading stock of an investee company are not used by the investee company to carry on its own business.

¹⁰ Trade income refers to an income that is chargeable to tax under section 10(1)(a) of the Income Tax Act.

¹¹ Property development activities are not confined to those undertaken by property developers who develop immovable properties for sale.

6.4.6 An investee company is considered to have completed its property development activities upon the issuance of a Certificate of Statutory Completion (“CSC”) by the Commissioner of Building Control in respect of the property development activities. This means that shares in an investee company disposed more than 60 months after the investee company is issued with a CSC (in respect of all property development activities it has undertaken) would satisfy the condition at paragraph 6.4.3(c)(ii), i.e. the investee company did not undertake any property development activity in the past 60 months before the disposal of shares.

7 Situations where normal tax rules continue to apply in determining nature of gains or losses from disposal of equity investments

7.1 The tax treatment of gains or losses from disposal of equity investments will continue to be determined based on normal tax rules¹² in the following situations –

- (a) where a divesting company had held at least 20% of the ordinary shares in an investee company for a continuous period of at least 24 months (i.e. it meets the condition mentioned in paragraph 5.2.2) and incurs losses from the disposal of ordinary shares in the investee company. In such a case, the losses are not immediately disregarded;
- (b) where a divesting company derives gains from the disposal of ordinary shares in an investee company and the disposal does not meet the condition in paragraph 5.2.2 or fall within the exclusions in paragraph 6. In such an instance, the gain is not automatically subject to tax;
- (c) where a divesting company makes gains or losses from the disposal of non-ordinary shares in an investee company.

7.2 In other words, whether the gains or losses from the disposal of equity investments in the above situations are income or capital in nature will continue to be determined based on the facts and circumstances of each case.

8 Administrative Procedure

8.1 To avail itself of the scheme, a company must provide the requisite information in its income tax return for the Year of Assessment (“YA”) relating to the basis period in which the disposal of ordinary shares is made. The

¹² For a divesting company that has been awarded any tax incentive that covers gains or losses from disposal of investments, the relevant governing rules under the tax incentive will apply where applicable.

company must keep sufficient documents to support that the specified condition in paragraph 5.2.2 is met and the share disposal does not fall within the exclusions in paragraph 6. The company need not submit the documents with its income tax return but must do so upon IRAS' request.

- 8.2 Where a company does not provide the requisite information in its income tax return, IRAS will continue to apply normal tax rules to establish the nature of gains or profits from the disposal of ordinary shares.

9 Frequently Asked Questions

9.1 Do companies have the choice to avail themselves or not to avail themselves of the scheme?

Yes, companies have the choice. Companies that wish to avail themselves of the scheme can do so by providing the requisite information in their income tax returns for the relevant YA relating to the basis period in which the disposal of ordinary shares is made.

9.2 Can my company avail itself of the scheme if it currently enjoys a tax incentive which provides for tax exemption or concessionary rate on gains or losses from the disposal of equity investments?

A company enjoying tax incentives is not precluded from availing itself of the scheme in respect of gains it derives from the disposal of ordinary shares, subject to the condition in paragraph 5.2.2 and the exclusions in paragraph 6. However, the relevant governing rules under the tax incentive awarded to the company continue to apply, where applicable, to:-

- (i) losses from disposals of equity investments; and
- (ii) gains from disposals of equity investments that do not meet the condition under the scheme.

9.3 Is the scheme applicable to a registered business trust that disposes of ordinary shares in an investee company?

Yes. This is because a registered business trust is taxed like a company for income tax purposes.

9.4 Does the scheme apply only to tax resident companies?

No. The scheme applies to all divesting companies regardless of tax residency (provided it is not an 'excluded divesting company' referred to in paragraph 6.3).

9.5 How does the scheme apply in a situation where ordinary shares are disposed of after they have been converted from hybrid instruments e.g. convertible bonds? Does the 24-month period include the period of holding of convertible bonds up to their conversion into ordinary shares?

In determining whether the condition in paragraph 5.2.2 is met, the holding period of ordinary shares starts on the date on which the bonds are converted into ordinary shares (i.e. the conversion date). The period of holding of convertible bonds up to their conversion into ordinary shares should not be taken into account in determining whether the 24-month period is met.

9.6 How does the scheme apply to an amalgamated company that has elected to come under the corporate amalgamation framework under section 34C of the ITA?

Under the section 34C corporate amalgamation tax framework, the amalgamated company is treated to have stepped into the shoes of the amalgamating companies. As such, ordinary shares that were originally acquired by an amalgamating company are treated as held by an amalgamated company since the date of acquisition by the amalgamating company.

9.7 My company made two disposals of ordinary shares in the same investee company in the same financial year. The first disposal results in a gain of \$500,000 and the second disposal results in a loss of \$200,000. The net gain in the financial statements is \$300,000. How do I apply the scheme to the disposals if my company satisfies the condition in paragraph 5.2.2?

The gain of \$500,000 made on the first disposal of ordinary shares is treated as not taxable as the condition in paragraph 5.2.2 is met. Normal tax rules will however continue to apply to determine the tax treatment of the loss made on the second disposal of ordinary shares.

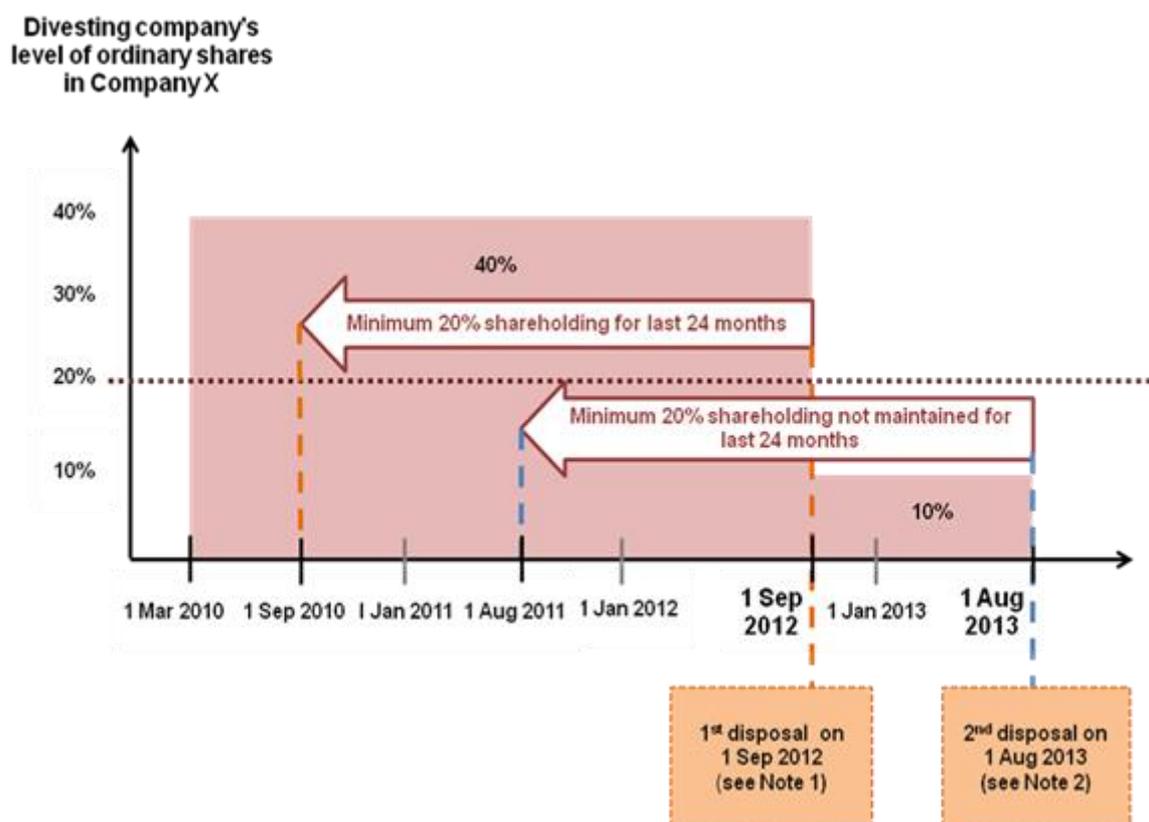
10 Contact Information

10.1 For any general enquiries or clarification on this e-Tax Guide, please call 1800 356 8622 (Corporate Income Tax).

11 Updates and Amendments

	Date of amendment	Amendments made
1	10 Dec 2020	<ul style="list-style-type: none">• Inserted paragraph 2 to provide the tax treatment at a glance• Amended paragraph 5.1 and footnote 3 to reflect the extension of the scheme announced in Budget 2020• Inserted paragraph 6 and Annex C to reflect refinements in the scope of exclusion and provide details of the tax change announced in Budget 2020• Renumbered the Annexes• Made conforming edits to other paragraphs and Annex B, such as to update the references to new and renumbered paragraphs

Annex A – Example on application of condition to be met by a divesting company



A company acquired 40% of the ordinary shares in Company X on 1 March 2010. On 1 September 2012, it disposes of 30% of the ordinary shares in Company X and on 1 August 2013 it disposes of the remaining 10% of ordinary shares in Company X. Gains are derived by the divesting company from both disposals.

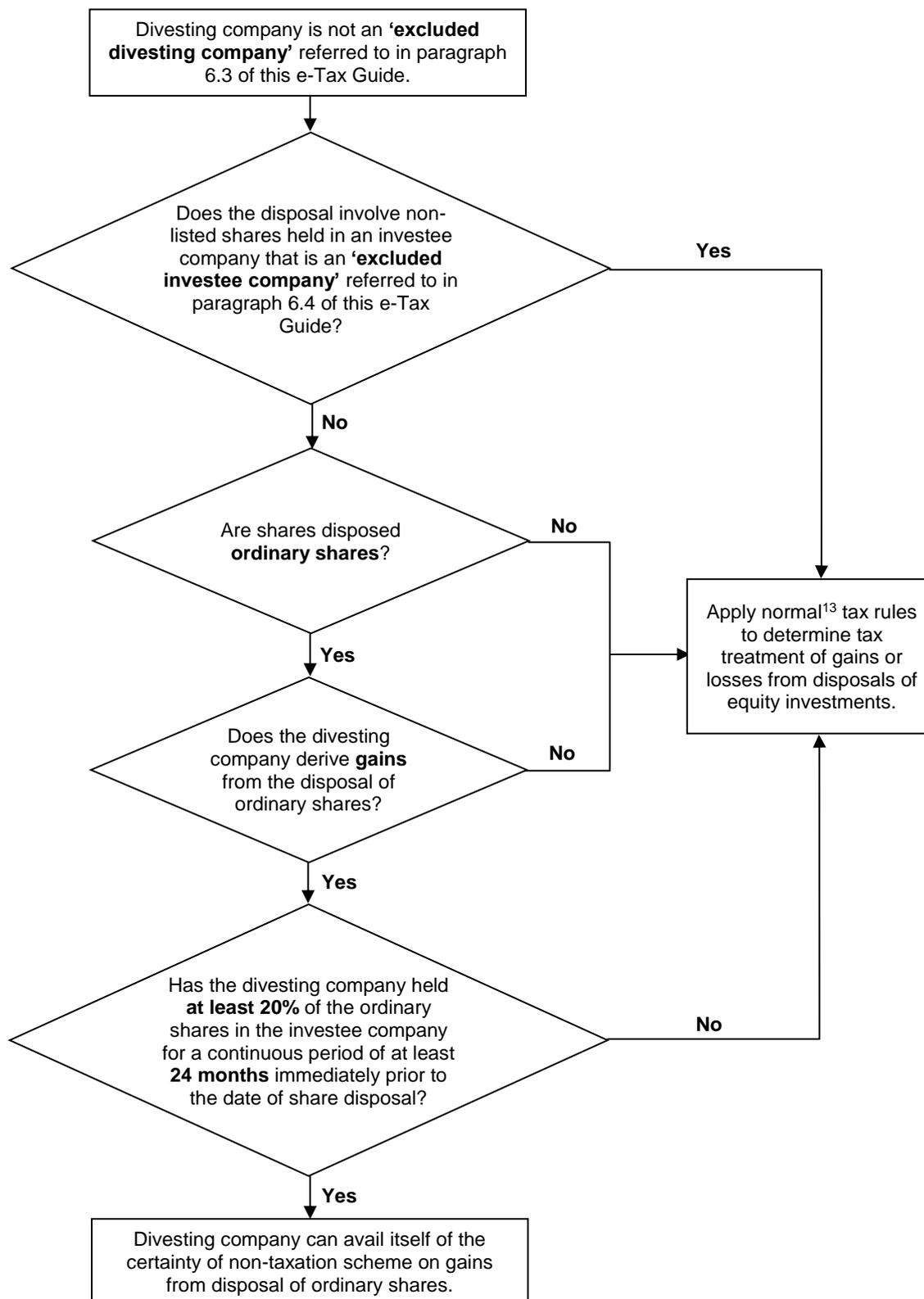
Note 1

The gains from the 1st disposal on 1 September 2012 of 30% of the ordinary shares of Company X qualifies for certainty of non-taxation as immediately before the date of disposal, the divesting company has a minimum level of 20% of ordinary shares in Company X for a continuous period of at least 24 months. In this case, the divesting company has held a minimum level of 20% ordinary shares in Company X from 1 March 2010 to 31 August 2012 (i.e. 30 months).

Note 2

The gains from the 2nd disposal on 1 August 2013 of 10% of the ordinary shares of Company X does not qualify for certainty of non-taxation. This is because in the 24 months immediately before the date of disposal (i.e. period from 1 August 2011 to 31 July 2013), the divesting company held less than 20% of ordinary shares in Company X. The taxability of the gain from the 2nd disposal will be determined based on facts and circumstances of the case.

Annex B – Flowchart illustrating the application of the certainty of non-taxation scheme to a divesting company



¹³ If the divesting company has been awarded any tax incentive that covers gains or losses from disposal of investments, the relevant governing rules under the tax incentive will apply where applicable.

Annex C – Examples on the application of the certainty of non-taxation scheme to an investee company that has undertaken property development activities (for disposals of shares on or after 1 Jun 2022)

Company A holds 100% of the ordinary shares in Company X since the incorporation of Company X. On 1 Jan 2023, Company A (the divesting company) disposes ordinary shares in Company X (the investee company) and derives gains from the disposal.

Company X has undertaken property development activities¹⁴ to develop an immovable property. The property development activities were completed with a Certificate of Statutory Completion issued on 1 Jan 2017. Company X did not undertake any other property development activities thereafter. Since the property development activities were completed more than 60 months before the disposal of shares by Company A, the condition at paragraph 6.4.3(c)(ii) is satisfied.

Examples

	How Company X uses the immovable property developed	Does the scheme apply to the gains derived by Company A from its disposal of shares in Company X?
1	Company X carries on a manufacturing business from which it derives trade income. Company X uses the immovable property developed as its premises (factory and office) to carry on the manufacturing business.	Yes. The immovable property developed is used by Company X to carry on its manufacturing business to derive trade income.
2	Company X carries on a manufacturing business from which it derives trade income. Company X developed an industrial building. It rents out two floors of the building to another company and derives passive rental income. Other parts of the industrial building are used by Company X as its premises (factory and office) to carry on its manufacturing business.	Yes. The immovable property developed is used by Company X to carry on its manufacturing business to derive trade income.
3	The immovable property is developed into a hotel. Company X carries on a business of operating the hotel. Trade income is derived from operating the hotel.	Yes. The immovable property developed is used by Company X to carry on its hotel operation business to derive trade income.

	How Company X uses the immovable property developed	Does the scheme apply to the gains derived by Company A from its disposal of shares in Company X?
4	The immovable property is developed into a commercial building. Company X carries on a business of letting out units of that commercial building. Income derived from the business is trade income that is subject to the provisions of section 10E of the Income Tax Act.	Yes. The immovable property developed is used by Company X to carry on its business of letting out immovable properties to derive trade income.
5	Company X developed the immovable property into residential units for sale. Trade income is derived from the selling the residential units.	No. Company X is in the business of trading immovable properties, thus an 'excluded investee company' referred to in paragraph 6.4.3(a). The immovable property developed is the trading stock of Company X.

If the property development activities undertaken by Company X is still ongoing on the date of share disposal or have occurred during the past 60 months before the date of share disposal, the scheme does not apply to the gains derived by Company A from its disposal of shares in Company X. This is regardless of how the immovable property developed is used or will be used. In this instance, IRAS will examine the facts and circumstances to determine whether the disposal gains are capital or revenue in nature and apply normal tax rules.

¹⁴ Property development activities refer to the construction or causing the construction of any building (or part of a building), including the acquisition of land or building for such construction. For the purpose of the scheme, only building works that require an approval from the Commissioner of Building Control under the Building Control Act (or would have required such approval if the building works are done in Singapore) are considered as construction of a building.