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TAX ALERT

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With the Year of Assessment (YA) 2025 corporate tax filing deadline fast approaching, it is essential for companies to ensure their tax returns are prepared accurately and in full compliance. While our July's Tax Alert highlighted common pitfalls such as common non-deductible expenses, inadequate record-keeping requirements, updates on foreign income reporting and reimbursement of transport expenses, our August's edition takes a deeper look at two areas that often pose challenges to taxpayers - **foreign exchange differences and interest adjustments.**



[A] Foreign exchange differences

In general, the tax treatment of foreign exchange ("FX") differences can be summarised as shown in the table below:

Nature of FX differences	Tax treatment
Capital FX differences	Not taxable or deductible
Revenue FX differences	All exchange differences recognised in the profit and loss account are taxable or deductible, regardless of whether they are realised or unrealised. Examples are FX arising from settlement of sales/purchases transactions, and revaluation of trade receivables, trade payables.
Translation FX differences	Arise when financial statements are converted from its functional to another currency for presentation purposes – purely notional and are not taxable or deductible. Examples are FX arising from arising from investments, loans, fixed assets purchases, and revaluation of bank accounts and other non-trade balances.

Designated bank account

A common area of confusion for businesses is the tax treatment of FX differences arising from foreign currency bank accounts, particularly in distinguishing between capital and revenue nature. Generally, FX differences from revaluating standard business bank accounts are treated as capital in nature and are not taxable or deductible, as they reflect the cost of holding foreign currency[1] to meet both capital and revenue requirements, rather than actual revenue transactions.

However, some business may designate a specific foreign currency bank account (referred to as "designated bank account") that are maintained **solely** for receiving trade receipts and paying revenue expenses in a specific foreign currency. In such cases, FX differences arising from the revaluation of the bank account balance into the business's functional currency may be regarded as revenue in nature, making them taxable or deductible, provided that documentary evidences e.g. monthly bank statements are available to support the above tax position.

To ease compliance, the Comptroller of Income Tax ("CIT") allows businesses which maintain a designated bank account primarily for revenue purposes to adopt a de-minimis approach.



[1] Foreign currency refers to a currency that is different from a business's functional currency.

Under this approach, the FX differences can still be treated as revenue in nature provided that both the conditions below are met:

a. the total number of capital transactions does not exceed 12 per year; and
b. the total value of capital transactions does not exceed S$500,000.



Notwithstanding the application of the de-minimis limit, the CIT reserves the right to examine the transactions within the bank account. In the event that the total number or value of capital transactions exceeds the de-minimis limit, the tax treatment for the designated bank account will not apply.

To help clarify the practical application of the rules relating to tax treatment of FX differences and the designated bank account, we highlight some frequently asked questions as follows:

1. Do businesses need to elect for the de-minimis limit every year?

   There is no requirement to make an annual election. The designated bank account treatment will only cease from the YA in which the business either discontinues the treatment, adopts the de-minimis limit for the first time but fails the thresholds, or the account fails to meet the de-minimis limits.

2. Are GST and corporate tax payments treated as capital transactions?

   Payments of corporate income tax, including Singapore tax or foreign withholding taxes, are not considered purchases of goods or services and are thus classified as capital transactions for de-minimis computation.

   Conversely, GST or withholding taxes related to business expenses (e.g., interest, royalties, technical fees) may be treated as revenue transactions if they are incurred as part of payments for goods or services.

3. What exchange rate should businesses use to convert transactions to Singapore Dollar for computing the total value of capital transactions?

   Businesses may use either the spot rate or the MAS average month-end exchange rate for the basis period to convert capital transactions into Singapore Dollars for de-minimis computation. It is important to apply the same rate consistently across all transactions. If a business decides to change the exchange rate method, the change should be clearly declared in the tax computations.



[B] Interest Adjustments

Interest expenses are commonly incurred on debt liabilities, such as loans or borrowings. While interest on loans used to finance income-producing assets is generally tax-deductible, interest attributable to non-income producing assets is not deductible. In such cases, businesses must make interest adjustments in their tax computations to reflect the correct deductible amount.

Examples of non-income producing assets are vacant properties held for long-term investment, investments in shares or securities that have not generated income, interest-free loans owning by non-trade debtors etc.

It is worth noting that interest adjustments are not required for interest-free loans provided to directors or employees. The interest-free benefit in such cases is treated as taxable employment income and should be reported in Form IR8A. The taxable benefit can be calculated by multiplying the interest-free loan outstanding at the balance sheet date by the average prime lending rate, which can be obtained from the Monetary Authority of Singapore's website.

Method for computing interest adjustments

If a company wishes to claim tax deduction on interest expense but cannot identify and track the use of an interest-bearing loan to specific assets financed by the loan and not all the assets are income-producing, the **Total Asset Method ("TAM")** is the default method to be applied to attribute the common interest expense to the assets.

Under the TAM, the disallowable interest expense is computed as:

$$\textit{Disallowable Interest Expense} = \frac{\text{Cost of non income producing assets X Common interest expenses}}{\text{Cost of total assets}}$$

Similarly, we have also compiled a set of frequently asked questions on interest adjustments and the TAM computation, which address common areas of uncertainty for businesses:

1. Can TAM be used if a loan can be directly linked to a specific asset?

   No. TAM should not be applied to loans whose use can be directly identified. The method is meant as a proxy for attributing common interest expenses when direct allocation is not feasible.

2. Do interest expenses and borrowing costs need to be attributed to investments which derive one-tier dividends or foreign-sourced dividends?

   Yes. Interest and qualifying borrowing costs must be allocated to the cost of these investments and are to be deducted against the dividend income.

3. Can foreign exchange losses arising from interest expense be included as part of total interest expense when applying TAM?

   Yes. Total interest expense under TAM includes any foreign exchange differences arising from the interest incurred. For example, S$10,000 of interest with a S$500 FX loss would result in a total interest expense of S$10,500 for TAM computation purposes.

4. What are some costs that are excluded from TAM's denominator?

   The total asset base includes all current and non-current assets reflected in the balance sheet. However, it excludes the cost of assets financed by specific interest-bearing loans, ROU assets treated as sale agreements, and ROU assets with deductible lease payments.

5. Are asset movements during the year (e.g., acquisitions or disposals) adjusted in TAM?

   No. TAM is a proxy formula based on the financial statements at year-end. Movements during the year are not separately adjusted.

How We Can Help?

Accurate corporate tax filing is essential to avoid unnecessary penalties and to ensure a seamless tax assessment process. If you have any uncertainties regarding your tax filings or would like your tax computations reviewed before submission, please reach out to us.

Our team of tax professionals is well-equipped to conduct thorough reviews, identify potential issues, and provide practical guidance to optimise your tax position. Engaging us early helps minimise last-minute surprises and provides greater confidence as the filing deadline approaches.



If you require any clarification on the updates shared in this newsletter or would like to discuss how these developments may impact your business, please feel free to reach out to us. Our team is ready to assist you with your tax compliance and advisory needs.



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