Factors Of Trade

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Residential property prices in Singapore grew an average of 31% in 2007[1] amid strong economic growth and local demand fuelled by an abundance of collective sales over the past two years. With property prices soaring aggressively over a short one-year period, many owners and investors have been keen to take advantage of the market by selling their properties and crystallising their gain from increased property values. It was not uncommon, especially in 2007, to hear of people buying a condominium unit at a soft launch and selling it for a quick profit a few months later.

While there is no capital gains tax in Singapore, any profits of a trade are subject to taxation[2] at prevailing rates. If the Inland Revenue of Singapore ("IRAS") looks at a particular transaction and deems the seller to be a property trader, that seller's profits will be treated as part of his chargeable income and subject to tax.

What are the factors governing the decision of IRAS in each case? Although the terms "trade" or "trader" are not defined in the Income Tax Act (Cap 134, 2004 Rev Ed), there are judicial discussions in decided cases in Singapore. In applying the objective test to determine if a particular transaction is a trade or merely an investment, the Courts take the following factors into account:-

- the motive of the taxpayer;
- the nature of the subject matter;
- the method of financing (of the purchase);
- whether there has been a multiplicity of similar transactions;
- the duration of ownership;
- the application of special skill or supplementary work to the subject matter; and
- the reasons for the sale/realisation.

Broadly speaking, there is no single factor that will determine whether the activities of a taxpayer in the property transaction amount to the carrying on of a trade or business.3 The Courts will have to assess all the facts of the case, taking into account the factors of trade mentioned above, to make that determination.

The Courts will look at the whole evidence to discern the taxpayer's primary reason for the sale. It was decided in a recent case that the reason of bad feng shui affecting the property could be accepted as the primary reason for the sale, thereby negating the other factors of trade of the case.[4]

It would be interesting to see how the Courts would assess a reason for sale being an Order for Sale by the Strata Titles Board for collective sale where the seller is a minority owner who did not agree to the collective sale. Perhaps the Courts should also look at other factors closely in a collective sale case, such as the motive of the seller in buying the property in the first place and the multiplicity of similar transactions, if any.

Clearly, the multiplicity of similar transactions is an important factor. For example, if a person sells a few properties within a short one-year period, that would suggest a trade as opposed to an investment.[5]

Similarly, the factor of the duration of ownership is very relevant. In one case, it was held that the period of two years was not unduly short in the context of the residential property market in Singapore and, as such, a neutral factor.[6]

As for the method of financing, the fact that the sale proceeds are reinvested in another purchase helps negate the effect of a short duration of ownership and also the motivation for quick profit.[7]

The key question here is whether the seller possessed an intention to trade. Normally, this intention is to be discerned at the time the asset is acquired. But the Courts believe that intentions may change, and therefore what was initially bought for investment may subsequently become a trading item or vice-versa.[8] At the end of the day, all the evidence adduced should be considered and weighed to determine whether the transaction is a trading activity or not.

In view of these considerations, anyone buying property for a "quick flip" should closely take note of the factors of trade as he may well be classified a property trader and be taxed on the sale profits. In appropriate cases, it is advisable for monies to be set aside for possible taxes, which may be imposed up to six years after the relevant sale.

On a related note, if a person is not a tax resident in Singapore and assessed to be trading in properties in Singapore, withholding tax will be applicable if such person sells a property.[9] In each such case, the purchaser's lawyers shall withhold 15% of the sale price to account for the withholding tax.

1 Statistics from the Business Times on 3 January 2008 and also available from URA's Release of 4th Quarter 2007 Real Estate Statistics; extracted from http://www.ura.gov.sg/pr/text/2008/pr08-12.htm

2 Income Tax Act (Cap 134, 2004 Rev Ed) s 10(1)(a).

3 Teo, Keang Sood, Badges of Trade Revisited, [1996] Sing J.L.S. 43.

4 NP and Another v Comproller of Income Tax [2007] 4 SLR 599.

5 [2007] 4 SLR 599 at page 612.

6 [2007] 4 SLR 599 at page 612.

7 LKC v Comproller-General of Inland Revenue [1973] 2 MLJ 17.

8 [2007] 4 SLR 599 at page 611.

9 Income Tax Act (Cap 134, 2004 Rev Ed) s 45.

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