Tax exemption granted in respect of vessel disposal gains

(Note: Last updated in January 2022)

1. What is the tax exemption granted in respect of vessel disposal gains about?

Answer: In Budget 2012, it was announced that revenue gains from the disposals of vessels derived by qualifying ship operators and ship lessors on or after 1 June 2011 will be treated as income qualifying for tax exemption, subject to conditions.

The exemption will be an added tax benefit under the following Maritime Sector Incentive (**MSI**) awards:

- MSI-Shipping Enterprise (Singapore Registry of Ships) **(MSI-SRS)** award[1];
- MSI-Approved International Shipping Enterprise **(MSI-AIS)** award; and
- MSI-Maritime Leasing (Ship) **[MSI-ML(Ship)]** award[2].

2. What are the qualifying conditions for the tax exemption?

Answer: The tax exemption only applies if the revenue gains:

- fall within the qualifying scope as listed in FAQ no. 3; and
- are derived by an eligible entity as described in FAQ no. 4.

In addition, losses incurred on the sale of vessels and wholly-owned vessel-owning special purpose companies (SPC) will be disregarded for income tax purposes. The losses cannot be offset against other streams of income, carried forward to future Years of Assessment (YAs), carried back to earlier YAs or transferred out under the loss transfer system of group relief.

3. What is the scope of the tax exemption?

Answer: The tax exemption is applicable to:

(a) <u>Gains on the sale of vessels</u>

[1] An MSI-SRS entity is an entity which owns or operates Singapore ships and is in the business of ship operations.

[2] This refers to entities awarded the MSI–Approved Shipping Investment Enterprise **(MSI-ASIE)** / MSI-ASIE (Local ASPV) statuses, but excludes entities awarded the MSI-Approved Shipping Investment Manager **(MSI-ASIM)** status, as the latter do not own or operate ships directly.

Revenue gains derived from the sale of vessels registered[3] or to be registered[4] under the SRS or vessels owned or operated under the MSI-AIS / MSI-ML(Ship) awards. The exemption will include gains derived:

- from the sale of vessels under a sale and lease-back transaction; and
- from the sale of vessels under construction (including newbuilding contracts)[5].

(b) *Dividend income, share of partnership profits and/or branch profits*

- An MSI-AIS company's dividend income, share of partnership profits and/or branch profits* paid out from gains from vessel sales derived by the MSI-AIS company's Approved Network Company **[MSI – AIS(ANC)]** under the MSI-AIS award; or
- An MSI-ASIE's dividend income and/or share of partnership profits paid out from gains from vessel sales derived by the MSI-ASIE's foreign Approved Special Purpose Vehicle **[MSI–ASPV]** under the MSI-ML(Ship) award.

* In Budget 2015, it was announced that qualifying profits remitted from approved foreign branches by MSI-AIS entities will enjoy exemption under the MSI-AIS award with effect from 24 February 2015. Pursuant to this announcement, branch profits paid out of gains from vessel sales derived by the MSI-AIS(ANC) on or after 24 February 2015 will be treated as income qualifying for tax exemption.

(c) *Gains on the sale of shares in a wholly-owned vessel-owning SPC*

Revenue gains derived from the sale of 100% of shareholding in a wholly-owned **SPC** that, at the time of sale:

- Owns vessel(s) registered[3] or to be registered[4] under the SRS. The SPC must only be in the business of ship operations[6];
- owns vessel(s) under the MSI-AIS award[7]. The SPC must only be in the business of ship operations[6]; or

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[3] This includes vessels under provisional registration.

[4] Depending on the stage of the construction of the vessel, the vessel may or may not have obtained a registration (including provisional registration) with the SRS at the time of sale. For such cases, the tax exemption will only apply if the company can prove that it had intended to register the vessel with the SRS had it not been sold.

[5] Depending on the stage of the construction of the vessel, the vessel may or may not have obtained a registration (including provisional registration) with any shipping registry at the time of sale.

[6] "Ship operations" in relation to a Singapore or foreign ship refers to the shipping activities specified under S13A(16) or S13E(1) of the Singapore Income Tax Act 1947.

[7] The SPC does not need to be approved under the MSI-AIS/MSI-ML(Ship) award. The vessel(s) owned by the SPC may be registered under any shipping registry at the time of the sale of shares by the MSI-AIS / MSI-ML(Ship) entity.

- owns vessels under the MSI-ML(Ship) award[7]. The SPC must only be in the business of ship leasing[8].

Please note that the tax exemption is **<u>not</u>** granted to the following:

(a) Revenue gains on the sale of vessels derived by the lessor under a finance lease treated as sale[9] under Section 10C of the Singapore Income Tax Act 1947 and the Income Tax (Income from Finance Leases) Regulations.

For example, in a sale and lease-back arrangement, if the lease-back is in the form of a finance lease and the vessel in the sale and lease-back transaction has been previously used by the lessee or any other person (i.e. the lease-back is a finance lease treated as sale), the tax exemption will not apply to the lessor.

The above exclusion applies to gains derived under the:
(i) MSI-SRS and MSI-AIS award before 12 December 2018;
(ii) MSI-ML (Ship) award before 24 February 2015.

(b) Income derived by award recipient from carrying on a business of trading in ships or of constructing ships for sale.

Examples of scenarios where the exemption will and will not apply are set out in **Appendix 1** for further clarity.

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[8] "Ship leasing" refers to the activities specified under S13P(1) of the Singapore Income Tax Act 1947. Prior to 24 February 2015, "ship leasing" excludes the finance leasing of a sea-going ship which has been treated as though it had been sold[9] pursuant to Section 10C of the Singapore Income Tax Act 1947 and the Income Tax (Income from Finance Leases) Regulations for an MSI-ML(Ship) entity approved on or after 1st March 2011.

[9] Under Section 10C of the Singapore Income Tax Act 1947 and the Income Tax (Income from Finance Leases) Regulations, a finance lease will be treated as a sale agreement if:

a. the lessee has an option to purchase the vessel during the term of the lease including any extension or renewal thereof or upon its expiry;
b. the vessel which is leased is a limited use vessel;
c. the vessel in a sale and lease-back transaction has been previously used by the lessee or any other person;
d. the lessor and the lessee are related to each other and –
   i. the lessee or any other person related to the lessee lends to the lessor any of the funds necessary to acquire the leased vessel or guarantees any debt of the lessor incurred in connection with the lease;
   ii. the terms of the lease are determined otherwise than on the basis that there is no such relationship between the lessor and the lessee; or
   iii. the total value of the rentals or hire received or receivable for the term of those finance leases entered into by the lessor with lessees, who are related to the lessor, at any time during the basis period for any YA exceeds half of the total value of the rentals or hire received or receivable for the term of all finance leases entered into by the lessor in that basis period; or
e. the lease is a leveraged lease, unless the Comptroller determines that it shall be treated otherwise.

4. Who is eligible for the tax exemption?

Answer: An eligible entity is one that:

(a) Owns a vessel under the MSI-AIS award or owns a vessel that is registered[3] or to be registered4 under the SRS **and** is in the business of ship operations[6]; or
(b) Owns a vessel under the MSI-ML(Ship) award **and** is in the business of ship leasing[8].

In the case of qualifying foreign-sourced dividend income / partnership profits / branch profits and gains on sale of shares derived, the SPC, MSI-AIS(ANC) or MSI-ASPV, instead of the parent company should be the party that satisfies the above conditions.

In addition, for gains on sale of shares,

(a)the SPC should **only** be in the business of ship operations[6] or ship leasing[8], as the case may be;
(b)where the gains are derived by an MSI-AIS or MSI-ML(Ship) entity, the SPC does not need to be approved under the MSI-AIS/MSI-ML(Ship) award. The vessel(s) owned by the SPC may be registered under any shipping registry at the time of the sale of shares by the MSI-AIS / MSI-ML(Ship) entity; and
(c)where the gains are derived by a non MSI-AIS or non MSI-ML(Ship) entity, the entity has to be in the business of ship operations[6] and the SPC must not own any vessels registered under a foreign registry at the time of sale of the shares by the entity.

The tax exemption does **not** apply to an entity that buys and sells vessels as its main business (e.g. a vessel trader, a ship builder etc).

If an eligible entity (as defined above) has a separate and distinct ship trading / ship building division housed within the same entity and derives relevant vessel disposal gains, the entity will need to substantiate that the vessel was used or is intended to be used by its ship operating or ship leasing division in its business of ship operations[6] or ship leasing[8], as the case may be, and that the gains do not form part of the ship trading / ship building gains which remain taxable.

5. What benefits is each class of eligible entities entitled to?

Answer: The tax exemption applies as follows:

Eligible entity	Scope of tax exemption includes:				
	Gain on disposal of vessels		Gain on disposal of vessels under construction (including newbuilding contract)	Gain on disposal of wholly-owned vessel owning SPC	Foreign sourced dividend income, share of partnership profits and/or branch profits attributable to vessel disposal gains
	Singapore flagged vessel	Foreign flagged vessel			
MSI-SRS	Yes	NA	Yes, provided that the entity can substantiate that it intended to flag the vessel with SRS	Yes, provided that the SPC only owns Singapore flagged vessels and is **only** in the business of ship operations[6].	NA
MSI-AIS Entity	Yes	Yes	Yes	Yes. The SPC may own Singapore and / or foreign flagged vessels and should **only** be in the business of ship operations[6].	Yes, but only for dividends / partnership profits/ branch profits received from MSI-AIS(ANC)
MSI-ML(Ship) Entity	Yes	Yes	Yes	Yes. The SPC may own Singapore and / or foreign flagged vessels and should **only** be in the business of ship leasing[8].	Yes, but only on dividends / partnership profits received from overseas MSI-ASPV

6. Is there any requirement on the minimum length of ownership of vessels or shares in vessel-owning SPCs?

Answer: No, there is no requirement on the minimum length of ownership of vessels or shares in vessel-owning SPCs.

7. Is there any requirement for the vessel to be used for ship operations[6] before it is sold?

Answer: No, there is no requirement for the eligible entity to operate the vessel before it is sold. The exemption is also available to gains derived from the sale of vessels under construction (including newbuilding contracts).

8. How do we apply for the tax exemption?

Answer: There is no need to make a separate application for this tax exemption. If a taxpayer ascertains that it meets the conditions listed in FAQ no. 2 above, it can report the vessel disposal gains / qualifying dividend income / qualifying partnership profits / qualifying gains from sale of SPCs derived on or after 1 June 2011 and qualifying branch profits derived on or after 24 February 2015, as income to be exempt under Sections 13A, 13E, 13P or 13(12) of the Singapore Income Tax Act 1947 accordingly when filing its income tax returns.

9. Are all gains on vessel disposal to be assessed under this tax exemption?

Answer: No, the tax exemption would not apply to capital gains since Singapore does not tax capital gains.

Appendix 1

Application of the Exemption: Sample scenarios

The table below sets out a list of sample scenarios under which the exemption will or will not apply to the gains derived by an eligible entity from the disposal of vessels. An eligible entity is one that:

(a) Owns a vessel under the MSI-AIS award or owns a vessel that is registered (provisionally or otherwise) or to be registered* under the SRS **and** is in the business of ship operations [i.e. shipping activities specified under Section 13A(16) or Section 13E(1) of the Singapore Income Tax Act 1947]; or

(b) Owns a vessel under the MSI-ML(Ship) award **and** is in the business of ship leasing [i.e. activities specified under Section 13P(1) of the Singapore Income Tax Act 1947#].

* Depending on the stage of the construction of the vessel, the vessel may or may not have obtained a registration (including provisional registration) with the SRS at the time of sale. For such cases, the tax exemption will only apply if the company can prove that it had intended to register the vessel with the SRS had it not been sold.

Prior to 24 February 2015, "ship leasing" excludes the finance leasing of a sea-going ship which has been treated as though it had been sold pursuant to Section 10C of the Singapore Income Tax Act 1947 and the Income Tax (Income from Finance Leases) Regulations for an MSI-ML(Ship) entity approved on or after 1st March 2011.

Scenario		Covered under tax exemption?
1	SRS vessel or vessel owned by an MSI-AIS / MSI-ML(Ship) entity is sold on the same day or within a few days from delivery.	Yes.
2	Fully constructed / purchased SRS vessel or vessel owned by an MSI-AIS / MSI-ML(Ship) entity is sold before delivery (i.e. did not use vessel at all).	Yes.
3	Vessel under construction is sold before delivery (i.e. did not use vessel at all).	Yes.
4	Sale of newbuilding contract(s). [i.e. a contract for a vessel under construction where the vessel does	Yes.

Scenario		Covered under tax exemption?
	not have a registration (including provisional registration) with any shipping registry at the time of sale.]	
5	▪ Entity has both a ship operating / ship leasing and a ship building division within the same entity; ▪ Vessel is built by the ship building division for use by its ship operating / leasing division; ▪ Vessel is subsequently sold by the ship operating / leasing division.	Yes, however the entity has to substantiate that the vessel was used / intended to be used by its ship operating / leasing division in its business of ship operations / leasing and that the gains do not form part of the entity's shipbuilding gains.
6	▪ Entity has both a ship operating / leasing and a ship trading division within the same entity; ▪ Vessel was used / intended to be used by its ship operating / leasing division; ▪ Vessel is subsequently sold by the ship operating / leasing division.	Yes, however the entity has to substantiate that the vessel was used / intended to be used by its ship operating / leasing division in its business of ship operations / leasing and that the gains do not form part of the entity's ship trading gains.
7	SRS vessel or vessel owned by an MSI-AIS / MSI-ML(Ship) entity is sold under a sale and lease-back transaction.	Yes.
8	Gains derived under a finance lease treated as sale.	No, if the gain is derived under the: (i) MSI-SRS or MSI-AIS award before 12 December 2018; and (ii) MSI-ML(Ship) award before 24 February 2015.
9	Company disposes of 100% of its shares in its wholly-owned SPC, which owns 100% of a vessel.	Yes, provided that the Company and the SPC is an eligible entity as defined in question 4 above.
10	A foreign entity of MSI-AIS company is approved as an Approved Network Company [MSI-AIS(ANC)] with effect from 1 April 2015. The MSI-AIS(ANC) disposes of vessel and pays	Yes, dividends or share of partnership profits paid out of vessel disposal gains derived by the MSI-AIS(ANC) on or after 1 June 2011 will be treated as income qualifying for tax

Scenario		Covered under tax exemption?
	dividends or share of partnership profits to the MSI-AIS company out of vessel disposal gains.	exemption, provided the MSI-AIS(ANC) is an eligible entity as defined in question 4 above. However, as the foreign entity is only approved as an MSI-AIS(ANC) with effect from 1 April 2015, only dividends or share of partnership profits paid out of vessel disposal gains derived on or after 1 April 2015 would be exempt. Note: For this scenario, the MSI-AIS(ANC) instead of the MSI-AIS company should satisfy the conditions of an eligible entity.
11	A foreign branch of MSI-AIS company is approved as an Approved Network Company [MSI-AIS(ANC)] with effect from 1 April 2015. The MSI-AIS(ANC) disposes of vessel and pays branch profits to the MSI-AIS company out of vessel disposal gains.	Yes, branch profits paid out of vessel disposal gains derived by the MSI-AIS(ANC) on or after 24 February 2015 will be treated as income qualifying for tax exemption, provided the MSI-AIS(ANC) is an eligible entity as defined in question 4 above. However, as the foreign branch is only approved as an MSI-AIS(ANC) with effect from 1 April 2015, only branch profits paid out of vessel disposal gains derived on or after 1 April 2015 would be exempt. Note: For this scenario, the MSI-AIS(ANC) instead of the MSI-AIS company should satisfy the conditions of an eligible entity.
12	A foreign entity of MSI-ASIE is approved as an Approved Special Purpose Vehicle (MSI-ASPV) with effect from 1 April 2015. The MSI-ASPV disposes of vessel and pays dividends or share of partnership profits to the MSI-ASIE out of vessels disposal gains.	Yes, dividends or share of partnership profits paid out of vessel disposal gains derived by the MSI-ASPV on or after 1 June 2011 will be treated as income qualifying for tax exemption, provided the MSI-ASPV is an eligible entity as defined in question 4 above.

Scenario		Covered under tax exemption?
		However, as the foreign entity is only approved as an MSI-ASPV with effect from 1 April 2015, only dividends or share of partnership profits paid out of vessel disposal gains derived on or after 1 April 2015 would be exempt. Note: For this scenario, the MSI-ASPV instead of the MSI-ASIE should satisfy the conditions of an eligible entity.