# LEGISLATION COMMENT

## MORE TAX CHANGES
## INCOME TAX (AMENDMENT) ACT, 1982 (ACT No. 1 OF 1982)

### *Introduction*

The 1981 Income Tax (Amendment) Bill[1] was introduced in Parliament on the 2nd day of December, 1981 and as expected, has been passed without controversy as the 1982 Income Tax (Amendment) Act (hereafter the Act) on 3rd March, 1982.[2] This Act, apart from making various amendments to the Income Tax Act[3] (hereafter "ITA"), is noteworthy for its implementation of the Government's 1981 Budget Proposals.[4] The tax changes proposed in the 1981 Budget were described as a "continuation of the liberalisation of the tax system begun in fiscal year 1978"[5] when tax rates for personal income were substantially reduced by an average of 14.8%[6] Two years later, in 1980, Part A of the Second Schedule to the ITA was again completely revised to give another major across-the-board reduction in tax rates averaging 16.1%.[7] For the year of assessment 1981, although 1980 tax rates were retained, tax relief came in the form of a one-time tax-rebate of 10% to every resident taxpayer on his total tax liability. In his Budget Speech, the Minister of Trade and Industry (hereafter "the Minister") noted that inflation has pushed many wage-earners into higher income tax brackets and thus the 10% tax-rebate was necessary "to take account of the pernicious effect of inflation on tax burdens."[8] This phenomenon of "bracket-creep" is well-known as a structural problem of the progressive system of income tax[9] and unless the Government proposes to index[10] income taxes for inflation, the only way to deal with the problem of bracket-creep is to adopt a policy of increasing personal exemptions to keep pace with inflation and occasionally reducing tax rates. The revision of tax rates in 1978, 1980 and now in 1982 clearly shows that the Government prefers to pursue the latter alternative. The following examines some of the more noteworthy changes wrought by the Act.

1 Bill No. 30 of 1981.
2 Act No. 1 of 1982. The Act was assented to by the President on 10th March, 1982.
3 Cap. 141, Singapore Statutes, Rev. Ed. 1970.
4 See 1981 Annual Budget Statement in Singapore Parliamentary Debates, Vol. 40, No. 6 Cols. 329-355, 357-380.
5 *Ibid,* at Col. 352.
6 See "A Year of Tax 'Handouts' (1981) 23 Mal. L.R. 156 at 165, n. 51.
7 This revision has been noted by the writer in the legislation comment on the two 1980 amendment acts to the ITA. See "A Year of Tax 'Handouts' ", *supra,* n. 6 at 165.
8 *Supra,* n. 4 at Col. 350.
9 See generally Goode, *The Individual Income Tax,* Chap. 11 on Stabilisation Aspects esp. at 287-289.
10 See Goode, *op. cit.* at 288-290 and Pechman, Federal Tax Policy (3rd Ed.) at 103-105.

### *The 1982 Revised Tax Rates: New Part A to the Second Schedule,*[11] *IT A*

The average reduction in tax-rates as implemented by the new Part A of the Second Schedule to the ITA works out to be 13% and the loss of revenue to the Government has been estimated at $78 million.[12] The taxpayers who will benefit most from this revision are those with chargeable incomes within the $5,000 and $75,000 bracket, enjoying reduction ranging from 17.8% to 25.9%.[13] Taxpayers within these brackets largely comprised "senior clerical, supervisory and skilled grades and the middle-income group" and were accorded special attention. These categories of taxpayers are apparently regarded as the "core" taxpayers, representing the largest segment of the tax base, whose incentive to work should not be undermined by onerous tax rates.

It is interesting to compare the revision of rates at both ends of the scale. At the bottom of the rate structure, the lowest two brackets [14] (the first $2,500 at 4% and the next $2,500 at 7%) have been merged to a common bracket: the first $5,000 at 7%. This means that taxpayers with chargeable income of $1 - $2,500 did not benefit at all from the 1982 revised rates and those in the $2,501 - $5,000 bracket enjoy a mere 3% reduction in tax rate. By way of contrast, the tax reduction at the top end of the rate structure may only be described as over-generous! In the 1980 revised rates, every dollar in excess of the first $200,000 was taxed at 45%, every dollar in excess of the first $400,000 at 50% and every dollar in excess of $600,000 at 55%. With the 1982 revised rates, the top marginal rate of 55% saw a substantial reduction of 10% to 45% and becomes applicable only on chargeable income in excess of $750,000. This means that taxpayer with chargeable income ranging from $200,000 - $600,000 benefited by a tax reduction of 12% - 13%, a very substantial saving in terms of tax dollars. Certainly, in contrast with the savings at the bottom-end of the scale, the top-end reduction seems regressive. The Minister has rationalised the meagre-to-non-existent reduction of the lowest two brackets on the ground that the average tax assessed on taxpayers with $1 - $2,500 income was about $45, which is not "onerous". And in any case, most of the taxpayers in the lowest bracket are young workers whom the Minister thinks "should quickly move up to higher income levels and benefit from tax reduction."[15] It is not clear whether this statement reflects the Minister's *prediction* of the taxpayer's inevitable rise to a higher income level or his *prescription* to these taxpayers to generate more income so that they may rise to higher brackets in order to enjoy the tax reduction.

The substantial reduction at the top-end of the scale was justified on the ground that the Government's objective is "to encourage, not to smother, individual drive and enterprise."[16] In fact, the Minister observed that with the newly revised rates, very few individuals will

[11] See s. 13 of the amending Act, *supra,* n. 2.
[12] *Supra,* n. 4 at Col, 351.
[13] *Supra,* n. 4 at Col. 350.
[14] See Part A, Second Schedule, ITA as amended by the Income Tax (Amendment No. 2) Act 1980, Act No. 28 of 1980.
[15] *Supra,* n. 4 at Col. 351.
[16] *Ibid.*

be paying tax at more than 40% effectively on their chargeable income. One may be led to speculate whether this is, in effect, a move to equalise the maximum effective rate for individual taxpayers with the tax on corporate taxpayers levied at a flat-rate of 40%.[17] Whether that is in fact the intention, the result could mean that for those taxpayers with large incomes, there is now very little incentive to divert their income to a corporate shell merely to escape higher individual tax rates.

### *Separate Assessment for the Unearned Income of a Married Woman: Section 51, ITA Amended*

Prior to 1963, the income of a married woman living with her husband was, for the purposes of the ITA, deemed to be income of her husband and she could not be assessed separately in her own name.[18] This was undoubtedly a perpetuation of the old common law position that a husband and wife were one person and a married woman was legally incapable of acquiring, holding and disposing of property in her own name. It was not until 1962 that the ITA was amended to give the option for separate assessment to married women.[19] This recognition of the married women as a taxpayer in her own right was however extended to her "earned income" only. Her "earned income" was identified under the ITA[20] as income from any "trade, business, profession or vocation carried on by her separately from her husband," *i.e.,* any income that is attributable to a section 10(1) source[21] which is unconnected with the husband. This clearly addressed the problem of "assignment of income" by a higher-bracket taxpayer to a lower-bracket taxpayer and reflects a stereotyped sexist situation: the husband is assumed to be the higher-bracket income earner who will seek to "attribute" or "assign" part of his income to his wife who, naturally, has a lower tax bracket.[22]

The need to police loss of revenue through the assignment of income from a higher-bracket taxpayer to a lower-bracket taxpayer is not disputed. However, the statute would be more effective if it does not assume that the lower-bracket taxpayer is always the wife. This assumption is implicit in deeming the married woman's unearned income to be that of her husband.

The new amendment to section 51 which allows separate assessment on the unearned incomes of married women represents a step in the right direction. As the Minister observed in his Budget statement,[23] it is clear that many married women are capable of deriving

[17] See s. 43(a), ITA, *supra,* n. 3.

[18] This is the effect of s. 51(1) prior to amendment by Act No. 15 of 1962, making this provision subject to the new sub-s. (4) to s. 51.

[19] S. 51(4) as introduced by Am. 15 of 1962 and subsequently modified by M. 2 of 1965 and Act No. 29 of 1965.

[20] S. 51(5), ITA, *supra,* n. 3.

[21] Arguably, it also includes income from a s. 10(1)(b) source although sub-s. (5) to s. 51 does not talk of income derived from employment. The wording of sub-s. (5), *i.e.* the use of the word 'include', indicates that it is not meant to be exhaustive in enumerating the sources of eligible 'earned income'.

[22] The married woman who earns more and is therefore in a higher lax bracket than her husband is obviously regarded as a mythical creature by tax legislators, who were undoubtedly all men, and sexist.

[23] *Supra,* n. 4 at Col. 347.

unearned income in their own right. Section 51 as amended recognises this by extending separate assessment to "investment income" of a married woman but only "if the Comptroller is satisfied that her investment income is attributable to assets and investments acquired by her from her earned income."[24]

On closer analysis, this amendment is not as liberal as it may seem. The unearned income in question is limited to investment income from assets and investments *acquired from earned income.* It rules out unearned income from assets and investments acquired by way of gift or inheritance. If a married male taxpayer is under no obligation to satisfy the Comptroller that his unearned income is attributable to assets and investments acquired from earned income, then it is difficult to find any compelling reason why his female counterpart should be. This requirement can only be rationalised if we revert to the original underlying sexist assumption that only husbands have higher income and hence the incentive to "assign" part of it to their wives who are invariably lower-bracket taxpayers. Again, if the problem to be addressed is the revenue loss through assignment of income, the tax statute would be more effective if it required either *spouse,* whether woman or man, to satisfy the Comptroller that her or his unearned income is derived from assets or investments acquired from her or his respective earned income, or from a source which is not connected with the other spouse. Thus, although the new amendment to section 51 is a step in the right direction, it is only good as far as it goes, which is not, unfortunately, very far.

### *New Category of Exempt Income: Section 13B As Amended*

One of the new tax concessions implemented in 1980[25] was the extension of the 10% concessionary tax-rate to income from off-shore gold transactions undertaken by an approved member of the Gold Exchange of Singapore. It has been elsewhere noted[26] that the concession was intended to foster the growth of the gold market in Singapore. Section 3 of the Act amends section 13B(1) to extend tax exemption to dividends declared by a company, which is a member of the Gold Exchange of Singapore, from income qualifying for the concessionary tax-rate under section 43D. Thus, the incentive for the development of the gold market is taken one step further. Not only do companies undertaking off-shore gold transactions enjoy a favourable rate of tax on their income, but shareholders in such companies derive tax-exempt dividends. In effect, the tax concession is no longer confined to the corporate level but extends down to the shareholder level. Hopefully, this would make investment in section 43D companies more attractive to investors. With this new amendment, the favourable treatment of section 43D companies is brought in line with that of section 43A companies (financial institutions operating Asian Currency Units) and section 43C companies (companies insuring and reinsuring off-shore risks), which have been enjoying tax-exemption on their dividends since 1979.[27]

[24] See s. 12 of the amending Act, *supra,* n. 2.
[25] See s. 43D introduced by the Income Tax (Amendment No. 2) Act 1980; Act No. 28 of 1980.
[26] See "A Year of Tax Handouts", *supra,* n. 6 at 164.
[27] S. 13B was introduced by Act No. 7 of 1979.

### *Enhanced Child Relief for Specially Qualified Women: Amended Fifth Schedule to the IT A*

As from the Year of Assessment 1974,[28] a married women who is a "specially qualified person"[29] and elects to be assessed separately becomes entitled to a special deduction for child relief.[30] Instead of a $750 deduction for each of her first 2 children,[31] she could deduct $2,000 or 5% of her earned income, whichever is the lesser. As for her third child, the special deduction is $2,000 or 3% of her earned income whichever is the lesser, as compared to the normal deduction of $500.[32] The policy in granting this special deduction is quite clear. It is to create an incentive for specially qualified women to enter the workforce rather than remaining at home to look after their children. Under the present tax regime, women who go to work cannot deduct expenses incurred in hiring a maid to look after the children or to do household chores in her place. This is simply because such expenses are regarded as personal or domestic expenses which section 15 of the ITA treats as a non-permissible deduction.[33]

Thus, a married woman engaged in gainful employment will increase the real family income only by the amount by which her earnings exceed the wages and keep of the servant, as well as other expenses attributable to her leaving home to work.[34] Where tax rates are high and no allowance is made in the income tax base for income of the working wife, or alternatively for her expenses attributable to going to work, tax may seriously inhibit the entrance of married women in the workforce.

If a married woman with special qualifications elects to remain at home and perform the tasks that can be done by a less qualified person, it is presumably regarded as a waste of human resources.[35] Of course, even with the possibility of enhanced child relief, some specially qualified women may still prefer to be full-time mothers and homemakers because they regard these roles as more important than being an income earner. The incentive only works in relation to those women taxpayers at the margin, where their decision to work is determined by the amount they can earn and the corresponding expenses incurred in hiring a substitute to look after the children and perform household chores.

[28] Inserted by Act No. 26 of 1973.

[29] Para. 10 of the Fifth Schedule defines a "specially qualified person" to mean a person who has obtained a degree from a University or equivalent institution or who is a member of a profession regulated by any written law otherwise approved by the Minister and notified in the *Gazette.*

[30] See para. 8 of Fifth Schedule, to the ITA, *supra,* n. 3.

[31] See para. 2 of the Fifth Schedule, ITA, *supra,* n. 3.

[32] *Ibid.*

[33] Even if a case may be made out that such expenses are "wholly and exclusively incurred in the production of income" within the scope of s. 14 of the ITA which allows deduction, after 1979 s. 14 is read subject to s. 15 as the amendment introduced by Act No. 9 of 1979 provides that s. 15 shall govern notwithstanding the provisions of the ITA, *supra,* n. 3.

[34] Alternatively expenditure on substitute services may take subtle forms, *e.g.* higher prices may be paid generally because of lack of time for leisurely shopping and meals may be eaten more often in restaurants. See generally the discussion of imputed income from the housework of wives in Vickery, *Agenda for Progressive Taxation* (1947) reproduced in the Bittker & Stone, *Federal Income Estate and Gift Taxation,* (4th Ed.) at 62-66.

[35] Her productivity will often be greater than that of the servant, or at least, than her contributions as a homemaker.

As implemented in 1973, the enhanced child relief was only available to taxpayers who on or after 1st August, 1973 had no more than three children. This was of course in keeping with the Government's concerted effort to promote population control. The policy was to create a "disincentive" for having more than three children by denying child relief for the fourth or subsequent child born on or after 1st August, 1973.[36]

However, paragraph 18 of the Fifth Schedule was worded such that its effect excluded married women, even though specially qualified within the meaning of the Act, from the enhanced child relief if they had more than three children *before* 1st August, 1973. This was obviously an unfair penalisation of these taxpayers because it disqualified them based on a situation already in existence *before* tax disincentives were created to limit family size to three or fewer children. This discrimination seems unintended because it could not be justified on policy grounds: the intended disincentive can only hope to affect *future* behaviour — it is powerless to alter existing fact and this should have been recognised.

Unfortunately, this inequitable position was allowed to persist until the present amendment which seeks to extend the enhanced child relief for specially qualified women to women who had more than three children before 1st August 1973. The enhanced relief is of course similarly confined to only the first three eligible children. This amendment takes effect from the year of assessment 1982, ending eight years of inequity for some unfortunate taxpayers.

### *What the Act Does Not Do*

In his Budget Statement, the Minister reported to Parliament that over the preceding year there had been an increase of 91,868 taxpayers.[37] He noted, however, that many self-employed income-earners and professionals paid by customers or clients who do not seek deductions for such payments still elude the tax net. The problem created by such tax evaders is not confined to the obvious loss of revenue to the Government. The more insidious effect is that it undermines one of the basic objects of the tax system — the equitable distribution of the tax burden. It is fundamental that the more narrow the tax base, the higher will be the tax rates required to raise the same amount of revenue. Thus, if a percentage of income-earners remains outside the tax base, the tax rates will continue to be higher than what they need to be if every income-earner bears his share of the tax burden.

This is naturally a matter of concern to tax administrators and the Minister reported that the Inland Revenue Department was then studying the possibility of presumptive taxation of hawkers, restauranteurs, taxi-drivers, property brokers and other free-lancing commercial intermediaries who do not keep proper accounts.[38] It was thus somewhat disappointing to note that the 1982 amending Act has not implemented any system for presumptive taxation. One wonders whether

[36] See para. 3, Fifth Schedule, ITA, *supra,* n. 3. The date is clearly arbitrary being the date that the amending act came into force.
[37] *Supra,* n. 4 at Col. 348.
[38] *Ibid.,* at Col. 349.

the restraint is occasioned by potential administrative difficulties. The infrastructure for identifying the various categories of potential tax-evaders is already in existence: hawkers, taxi-drivers and property-brokers are all subject to licensing regulations. This means that records are available to identify these potential taxpayers. Presumptive assessment based on an estimated average income will certainly compel those earning below the average figure to keep proper accounts. For those earning above the average figure no similar incentive will exist. This problem is probably met by using figures substantially higher than the estimated average. The "incentive" for these taxpayers to keep proper accounts to establish their true tax liability creates no extra burden for the taxpayer beyond what is already required by the Act,[39] *i.e.* that a person carrying on or exercising any trade, business, profession or vocation should keep sufficient records to enable his tax liability to be readily ascertained.

SHUE TILY

[39] See s. 67(1) ITA, *supra,* n. 3.