KPMG

Tax alert

Issue 16 | November 2023

Updates on tax treatment of front-end fees

Recently, the Inland Revenue Authority of Singapore (IRAS) has updated its e-Tax Guide on Tax Deduction for Borrowing Costs Other Than Interest Expenses (Fourth Edition) to provide a more detailed guidance on deductibility of front-end fees (FEF).

Under Section 14(1)(a)(ii) of the Income Tax Act 1947, borrowing costs (other than interest expenses), which are incurred as a substitute for interest expenses or to reduce interest costs, are deductible if they are prescribed under the stipulated regulations. To qualify for deduction under Section 14(1)(a), the expense must be payable 'upon any money borrowed' and the Comptroller of Income Tax must be satisfied that such sum is payable on 'capital employed in acquiring the income'. In 2014, the list of prescribed borrowing costs was expanded to include amendment fees, FEF and back-end fees[1].

As there was an increasing number of disputes on the FEF claim to substantiate that it was equivalent to interest otherwise payable, the IRAS has conducted a policy review and updated the e-Tax Guide to provide certainty and address taxpayers' concerns.

In this tax alert, we summarise the key features of the different types of loans for which FEF is incurred and the qualifying conditions on claiming tax deduction on the FEF and provide our insights on them.

Tax treatment of FEF and administrative procedures

The IRAS has set out the conditions and tax treatment of FEF:

	Type of loan	Main features of the loan on which FEF is payable	Tax treatment of FEF
1	**Bilateral loans**	• Provided by a single lender dealing directly with a borrower • No coordination, arrangement or underwriting services are involved	FEF is treated as equivalent to interest and hence tax deductible, subject to meeting the conditions*
2	**Club loans**	• Provided by a small group of lenders to a borrower • Generally, no coordination, arrangement or underwriting services are involved	
3	**Syndicated loans**	• Provided by a group of lenders (a syndicate) to one or more borrower(s) • One or more lenders would act as arranger(s) and obtain a mandate letter from the borrower(s) to allow the arranger(s) to invite other lenders to participate in the provision of the loan • FEF paid to arranger(s) covers both provision of loan/credit facility **and** provision of services (e.g. loan arrangement/underwriting)	Where no breakdown on the FEF between interest and service components is available, the IRAS is prepared to allow deduction on 55% of the FEF paid, subject to meeting the conditions* (1), (2) and (4)

[1]Front-end fees/back-end fees are defined in the Income Tax (Deductible Borrowing Costs) (Amendment) Regulations 2014 as any amount payable to the lender, either at the beginning or at the end of the term of borrowing, which is equivalent to the interest which the borrower would otherwise be required to pay to the lender under the loan agreement.

***Conditions for deduction:**

1. The taxpayer must have made a draw-down on the loan facility by the end of the basis period of the Year of Assessment (YA) in which the FEF was incurred. There is a relaxation of this condition — where the loan agreement is signed within 3 months from the financial year end (e.g. on or after 1 October for an entity with a 31 December financial year end), the taxpayer will have until the end of the next financial year to make a draw-down on the loan[2].

2. The FEF was incurred in the basis period for the YA in which the tax deduction was claimed (i.e. deduction is granted on an incurred and not an amortised basis).

3. The loan agreement and other loan documentation must not indicate any intention by the bank to sell down the loan or include a provision of underwriting services.

4. The deductible amount of FEF should not include any fees for services (e.g. facility agent fee, security agent fee, coordination fee, etc.).

The above tax treatment takes effect from YA 2023.

The IRAS has highlighted that in claiming the deduction, taxpayers are to declare in their tax computations which loan type the FEF relates to and that the relevant conditions stated above are met.

For syndicated loans, taxpayers are to declare if they are availing themselves of the tax deduction on 55% of the FEF incurred on the syndicated loans.

Taxpayers should continue to maintain supporting documents to substantiate their deduction of FEF and submit them to the IRAS upon request. Where the loan documentations include terms and clauses indicating syndication, arrangement, sell-down intention or underwriting, the loan will be regarded as a syndicated loan.

KPMG commentary

This update follows a series of clarifications made between the IRAS and various banks, including the Association of Banks in Singapore (ABS) on the commercially practicable documentation available for taxpayers to substantiate a tax deduction claim on FEF. The update demonstrates the IRAS' commitment to maintain an equitable playing field for smaller taxpayers who are unlikely to have the same leverage as large multinational corporations (MNCs) over their lenders or banks to customise their loan document(s) in alignment with the IRAS' previous documentation requirements.

Taxpayers who have undertaken loans as a borrower under which they incur FEF should revisit the clauses set out in their relevant loan document(s) and assess their respective features to validly identify the loan type for determination of the appropriate tax treatment on any FEF incurred.

[2] To claim deduction on the FEF, the draw-down of the loan agreement must be made before the filing deadline of the tax return for the YA. If the draw-down is made after the filing deadline of the tax return but before the next financial year end, taxpayers can submit a revised tax computation following the draw-down to claim deduction on the FEF.

While the identification of a bilateral loan should be generally straightforward, taxpayers are expected to face difficulties differentiating between club loans and syndicated loans, given their seemingly synonymous features (e.g. presence of multiple lenders, sharing of credit risks, etc.). In addition, it should be noted that some banks or lenders may label club loans as syndicated loans for industrial prestige and give themselves the title of an 'arranger', despite no actual arrangement services being rendered. Hence, regardless of the form in which the loan is presented, taxpayers should stay mindful of its actual substance, using relevant documentation to corroborate their assertion on the loan type and corresponding claim for tax deduction.

Given the more 'generous' tax deduction granted to FEF incurred under a club loan (i.e. full deduction), there might be an increased scrutiny from the IRAS in respect of such deductions. Moreover, the onus would lie on taxpayers to demonstrate that there is no element of service component embedded within the asserted club loan, which would indicate syndication and accordingly a lower allowable tax deduction. In the updated e-Tax Guide, the IRAS has provided guidance on key differentiating factors between a club loan and a syndicated loan, which taxpayers should find helpful.

For banks or lenders issuing loans where FEF is involved, it may be worthwhile to review the loan's standard terms and clauses to minimise ambiguity on the loan type they are issuing to borrowers.

For syndicated loans, banks or lenders may also consider transparentising the breakdown of the FEF into interest and service components for borrowers, where commercially possible.

With the additional disclosure requirements for claiming a tax deduction on the FEF, there could be an increase in occurrence of the IRAS requesting for the necessary supporting evidence for verification of the disclosed loan type. The perusal of such supporting evidence by the IRAS may hint at other features of the loan and whether taxpayers have complied with the relevant Singapore tax obligations (e.g. withholding tax where lenders are non-resident companies, appropriate transfer pricing arrangements for related party loans, etc.). Taxpayers should therefore ensure that the relevant tax considerations have been taken into account and appropriately complied with in a timely manner.

Nonetheless, it should be noted that any consideration on deductibility of FEF should, at the outset, be dependent on the purpose of the underlying loan (i.e. whether specifically undertaken to finance income-producing assets), keeping in mind any interest expense restriction required on the deductible FEF.

How we can help

As a committed tax advisor to our clients, we welcome any opportunity to discuss the relevance of the above matters to your business.

Author

Alan Lau
Partner
Head of Financial Services, Tax
T: +65 6213 2027
E: alanlau@kpmg.com.sg

Contact us

Ajay K Sanganeria
Partner
Head of Tax
T: +65 6213 2292
E: asanganeria@kpmg.com.sg

BANKING & INSURANCE

Alan Lau
Partner
Head of Financial Services, Tax
T: +65 6213 2027
E: alanlau@kpmg.com.sg

ENERGY & NATURAL RESOURCES, TELECOMMUNICATIONS, MEDIA & TECHNOLOGY

Gordon Lawson
Partner
Head of Energy & Natural Resources, Tax
T: +65 6213 2864
E: glawson1@kpmg.com.sg

Harvey Koenig
Partner
T: +65 6213 7383
E: harveykoenig@kpmg.com.sg

Mark Addy
Partner
T: +65 6508 5502
E: markaddy@kpmg.com.sg

INFRASTRUCTURE, GOVERNMENT & HEALTHCARE AND MANUFACTURING

Chiu Wu Hong
Partner
Head of IGH & Manufacturing, Tax
T: +65 6213 2569
E: wchiu@kpmg.com.sg

Pauline Koh
Partner
T: +65 6213 2815
E: paulinekoh@kpmg.com.sg

Yong Jiahao
Partner
T: +65 6213 3777
E: jiahaoyong@kpmg.com.sg

Toh Boon Ngee
Partner
T: +65 6213 2052
E: btoh@kpmg.com.sg

REAL ESTATE & ASSET MANAGEMENT

Teo Wee Hwee
Partner
Co-Head of Real Estate, Tax, and Head of Asset Management & Family Office
T: +65 6213 2166
E: weehweeteo@kpmg.com.sg

Anulekha Samant
Partner
Co-Head of Real Estate & Asset Management, Tax
T: +65 6213 3595
E: asamant@kpmg.com.sg

Agnes Lo
Partner
T: +65 6213 2976
E: agneslo1@kpmg.com.sg

Andy Baik
Partner
T: +65 6213 3050
E: andybaik1@kpmg.com.sg

Pearlyn Chew
Partner
T: +65 6213 2282
E: pchew@kpmg.com.sg

Evangeline Hu
Partner
T: +65 6213 2597
E: evangelinehu@kpmg.com.sg

Contact us

TRANSFER PRICING

Felicia Chia
Partner
Head of Transfer Pricing, Tax
T: +65 6213 2525
E: fchia@kpmg.com.sg

Lee Jingyi
Partner
T: +65 6213 3785
E: jingyilee@kpmg.com.sg

Denis Philippov
Partner
T: +65 6213 2866
E: denisphilippov@kpmg.com.sg

Yong Sing Yuan
Partner
T: +65 6213 2050
E: singyuanyong@kpmg.com.sg

INDIRECT TAX

Elaine Koh
Partner
T: +65 6213 2300
E: elainekoh@kpmg.com.sg

Sharon Cheong
Partner
T: +65 6213 2399
E: sharoncheong@kpmg.com.sg

Gan Hwee Leng
Principal Consultant
T: +65 6213 2813
E: hweelenggan@kpmg.com.sg

CORPORATE TAX PLANNING & COMPLIANCE

Mak Oi Leng
Partner
Head of Corporate Tax
Planning & Compliance, Tax
T: +65 6213 7319
E: omak@kpmg.com.sg

Audrey Wong
Partner
T: +65 6213 2010
E: audreywong@kpmg.com.sg

Lim Geok Fong
Principal Advisor
T: +65 8118 1129
E: geokfonglim@kpmg.com.sg

TAX GOVERNANCE

Pauline Koh
Partner
T: +65 6213 2815
E: paulinekoh@kpmg.com.sg

TAX TECHNOLOGY & TRANSFORMATION

Catherine Light
Partner
T: +65 6213 2913
E: catherinelight@kpmg.com.sg

GLOBAL COMPLIANCE MANAGEMENT SERVICES

Cristina Alvarez-Ossorio
Partner
T: +65 6213 2688
E: cristinaalvarez@kpmg.com.sg

PERSONAL TAX & GLOBAL MOBILITY SERVICES

Murray Sarelius
Partner
Head of Personal Tax &
Global Mobility Services, Tax
T: +65 6213 2043
E: murraysarelius1@kpmg.com.sg

Barbara Kinle
Partner
T: +65 6213 2033
E: bkinle@kpmg.com.sg

Garren Lam
Principal Advisor
T: +65 9728 1502
E: garrenlam@kpmg.com.sg

FAMILY OFFICE & PRIVATE CLIENTS

Teo Wee Hwee
Partner
Head of Asset Management
& Family Office
T: +65 6213 2166
E: weehweeteo@kpmg.com.sg

Pearlyn Chew
Partner
T: +65 6213 2282
E: pchew@kpmg.com.sg

MANAGED SERVICES

Larry Sim
Partner
Head of Managed Services, Tax
T: +65 6213 2261
E: larrysim@kpmg.com.sg

Contact us

PROPERTY TAX & DISPUTE RESOLUTION

See Wei Hwa
Partner
T: +65 6213 3845
E: wsee@kpmg.com.sg

Leung Yew Kwong
Principal Advisor
T: +65 6213 2877
E: yewkwongleung@kpmg.com.sg

R&D AND INCENTIVES ADVISORY

Lee Bo Han
Partner
T: +65 6508 5801
E: bohanlee@kpmg.com.sg

TAX – DEALS, M&A

Adam Rees
Partner
T: +65 6213 2961
E: adamrees@kpmg.com.sg

BASE EROSION AND PROFIT SHIFTING (BEPS)

Harvey Koenig
Partner
T: +65 6213 7383
E: harveykoenig@kpmg.com.sg

Andy Baik
Partner
T: +65 6213 3050
E: andybaik1@kpmg.com.sg

INDIA TAX SERVICES

Bipin Balakrishnan
Partner
T: +65 6213 2272
E: bipinbalakrishnan@kpmg.com.sg

US TAX SERVICES

Andy Baik
Partner
Head of US Tax Desk
T: +65 6213 3050
E: andybaik1@kpmg.com.sg

Joon Choi
Principal Advisor
T: +65 6508 5636
E: joonchoi1@kpmg.com.sg

Nicole Li
Principal Advisor
T: +65 6213 3388
E: nicoleli4@kpmg.com.sg

About our tax alerts

KPMG's tax alerts highlight the latest tax developments, impending change to laws or regulations, current practices and potential problem areas that may impact your company. As certain issues discussed herein are time-sensitive, it is advisable to make plans accordingly.

Tax alerts are issued exclusively for the information of clients and staff of KPMG Services Pte. Ltd. and should not be used or relied upon as a substitute for detailed advice or a basis for formulating business decisions. Read more of KPMG in Singapore's insights and perspectives here.

KPMG
12 Marina View, #15-01
Asia Square Tower 2
Singapore 018961
T: +65 6213 3388
F: +65 6225 0984
E: tax@kpmg.com.sg

- Singapore Tax Firm of the Year – International Tax Review Asia-Pacific Tax Awards 2022, 2023
- Singapore Tax Disputes Firm of the Year – International Tax Review Asia-Pacific Tax Awards 2021, 2022, 2023
- Singapore Tax Policy Firm of the Year – International Tax Review Asia-Pacific Tax Awards 2023
- Regional Tax Compliance and Reporting Firm of the Year – International Tax Review Asia-Pacific Tax Awards 2023
- Diversity & Inclusion Firm of the Year – International Tax Review Asia-Pacific Tax Awards 2023

For more details on our tax services, please click here.