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Stamp duty traps to watch out for

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Stamp Duty Traps To Watch Out For

On 15 December 2021, the Ministry of Finance introduced a new package of measures designed to cool the residential property market. The measures include increases in Additional Buyer's Stamp Duty ("ABSD"), the tightening of the Total Debt Servicing Ratio, adjustments to the Loan to Valuation limit for loans from HDB and a planned increase of housing supply.

Notably, there were significant increases in the ABSD rates applicable to almost all categories of buyers. The ABSD rates only remained unchanged for Singapore Citizens and Permanent Residents purchasing their first residential property (0% and 5% respectively). This article focuses on the implications of the increase in ABSD rates arising from the property cooling measures.

Most of the ABSD rates increased by 5-15%, with the highest rate of about 44% applying to buyers who purchase equity interests in property-holding entities ("PHEs") (viz., shares in companies owning residential properties) under the Additional Conveyance Duty ("ACD") regime. (The ACD regime was introduced to ensure that buyers do not take advantage of the lower stamp duty on purchases of shares as opposed to residential properties by buying the shares of the company owning the property rather than the property itself.)

A few quick observations may be made about this round of measures. Firstly, the official announcement was made after office hours on the day before the measures were to take effect. This is common practice when raising stamp duty rates and prevents taxpayers from avoiding the rate increase by completing their property transactions before the new rates kick in. Secondly, the property market was actually given some hints that new property cooling measures might be on the cards, as early as January this year, when then Deputy Prime Minister and Finance Minister, Mr Heng Swee Keat and Minister for National Development, Mr Desmond Lee commented about the close attention that the government was paying to the local property market.

Thirdly, the maximum amount of stamp duty payable by a taxpayer purchasing and then selling a residential property has now crossed the psychologically-significant threshold of 50% of the price of the property. This can be computed by adding the ACD rate of about 44% borne by the buyer when purchasing shares in a company owning residential property, to the ACD rate of 12% (borne by the seller) when selling the property by selling the shares of the company.

Fourthly, these measures may help to cool the residential property market in a perhaps unexpected way. Property developers effectively pay an ABSD rate of 5% when they purchase residential properties for development. While their ABSD rate is actually 40%, a full 35% of the purchase price may be remitted should certain conditions be met. One of these conditions is that all units in the development must be sold within 5 years from when the developer made the initial purchase (certain limited exceptions apply). Should the developer be unable to sell even one unit at that point, it will have to pay an effective ABSD rate of 40%, since it would not qualify for the remission. This is likely to put quite some pressure on developers to sell their remaining units, even at a discount.

The considerable increase in ABSD rates has made stamp duty mis-steps even more costly and taxpayers should look out for the following "traps" in dealing with residential property if they do not want to incur an unexpected (and large) tax bill.

Firstly, unless there are very good reasons for indirectly purchasing a residential property by purchasing the shares of the company owning the residential property, taxpayers should aim to purchase the property directly and have it transferred into their own name. Note that the ACD payable on purchase and sale of shares in a company owning residential property are flat rates and apply regardless of the status of the taxpayer or the number of years which the shares in the company has been owned. This means that, in the most extreme case, there can be a difference of stamp duty liability of about 52% if a residential property is purchased and sold indirectly rather than directly from the seller. This would occur if a Singapore Citizen with no existing residential properties purchased one residential property and subsequently sold it after owning it for three years. Such a person would only pay about 4% in stamp duties if the purchase was done directly, but a whopping nearly 56% if the purchase was done indirectly through the purchase and sale of shares.

Secondly, married couples (at least one person must be a Singapore Citizen) who jointly purchase a second residential property may benefit from an ABSD remission provided that they sell the first residential property within 6 months of the date of purchase of the second property (other conditions may apply depending on whether the property has been completed). This scheme is intended to allow couples to smoothly “upgrade” to a new property without having to pay a hefty ABSD bill due to the time delay in selling their old house. Without this scheme, couples would have to sell their existing residential property first before purchasing the new one, forcing them to find an alternative place to stay in the interim.

However, the costs of being unable to meet the six-month deadline has become even higher with these new changes. Consider the case where one spouse is not a Singapore citizen. If a couple (one Singapore Citizen and one Foreigner) should fail to meet the deadline, they would not qualify for a remission, which would mean ABSD is payable at 30% of the purchase price (for purchases made jointly by two parties subject to different rates, the highest rate will apply).

The situation is marginally better if the non-Singapore Citizen spouse is a Permanent Resident (effective ABSD rate of 25%) or if the couple were both Singapore Citizens (effective ABSD rate of 17%). Thus, couples must be absolutely sure that they have secured a buyer for their existing residential property before purchasing the new one, so as to be able to meet the 6 month deadline.

Thirdly, property-owners who are likely to have at least one residential property in their estate when passing on are advised to draft their wills carefully. It is common for testators to direct that all of their assets be distributed to their beneficiaries in equal shares. However, this becomes a problem when the estate is comprised of at least one residential property. The beneficiaries will each receive a share of this property, which can have at least three major effects. The first (and most direct) effect is that each of these beneficiaries will be treated as having one more “property count” for ABSD purposes, even if they only own a miniscule share in the property. If any beneficiary wishes to purchase a second residential property, a higher rate of ABSD is likely to be payable. Second, if the beneficiaries do not agree to either all live together in the property, or own the property jointly, they are likely to want to consolidate the ownership of the property in the hands of one person. This will have ABSD implications.

For example, assuming a case where there are three beneficiaries, A, B and C, each with one third of a share in a residential property. If A wishes to continue staying in the property, he or she might well have to “buy out” B and C’s shares. The transfer of B and C’s shares in the property to A will attract both Buyer’s Stamp Duty and ABSD on the value of the transfer.

Thus, if there is any possibility of potential beneficiaries wanting to keep on staying in “the family home”, for stamp duty purposes it may be prudent for testators to leave the entirety of the property to one beneficiary outright, and adjust the inheritances of the other beneficiaries accordingly to reflect this (insofar as if possible).

Finally, there has been an increasing trend of parents purchasing residential property on trust for their (minor) children. This enables them to utilise the “property count” of the child, who as a minor, generally would not own any other properties at that time. Aside from the legal implications of a trustee-beneficiary arrangement that will arise when a trust is deployed, the recently announced increase in ABSD rates heightens the risk of a large tax bill if things are not properly planned. This is because, eventually when the child grows up and wishes to purchase his or her own property, there will already be one “property count”, pushing the child into a higher ABSD tax bracket.

It is also, from an ABSD perspective, a bad idea to arrange for one residential property to be held on trust for multiple children as beneficiaries, since that single property would result in an increase of one “property count” for each of the children, regardless of the size of their interest in it. Much like the previous point, while it is often the desire of parents to be “fair” and treat their children “equally,” the arrangement of making each child a beneficiary can result in adverse tax consequences. Under the current stamp duty regime, it is simply unwise to share the interest in a residential property amongst various parties. This has also given rise to other practices such as “decoupling” where a married couple jointly owning a residential property may decide that only one spouse should hold the entire interest in the property outright, leaving the other spouse free to purchase another property without already having one “property count”.

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