

CAPITAL ALLOWANCES FOR A PIONEER ENTERPRISE UPON EXPIRY OF ITS TAX RELIEF PERIOD

INTRODUCTION

- 1 A company engaged in the production of a pioneer product and approved as a pioneer enterprise under Part II of the Economic Expansion Incentives (Relief from Income Tax) Act (EEIA) is granted exemption from tax for a period of 5 to 10 years¹ on its pioneer trade profits.
- 2 Subsection 10(1A)² of the EEIA stipulates that the capital allowances provided for in Sections 16, 17, 18, 19³, 20, 21 and 22 of the Income Tax Act (ITA) shall be taken into account in determining the exempt income of the pioneer enterprise even though no claim for the allowances has been made.
- 3 Under Section 7 of the EEIA the “old” trade or business of the pioneer enterprise is deemed to have permanently ceased at the end of the tax relief period and the pioneer enterprise is deemed to have set up a “new” trade or business on the day immediately following the end of its tax relief period.
- 4 Based on the concept of a deemed cessation of the “old” trade or business and commencement of a “new” trade or business, where the tax relief period of a pioneer enterprise expired during the basis period for a year of assessment, capital allowances for two years of assessment were previously computed for that basis period; one for each of the “old” and “new” trade/business periods falling within that basis period. This resulted in two years of capital allowances being given on some assets for that basis period.
- 5 The above treatment no longer applies from year of assessment 1993 with the enactment of Section 10(1B)⁴ of the EEIA. This section provides for capital allowances to be computed as if the “old” trade or business had not been deemed to have permanently ceased at the end of the tax relief period i.e., capital allowances for only one year of assessment are to be computed on all assets for that basis period. It also provides for the capital allowances to be apportioned between the “old” trade or business and the “new” trade or business in a manner which appears to the Comptroller to be reasonable.
- 6 The purpose of this practice note is to spell out the manner of apportioning capital allowances under Section 10(1B)⁴ of the EEIA.

¹ The incentive period has been extended to 15 years following the enactment of Economic Expansion Incentives (Amendment No.2) Act [EEIA (Amendment No. 2)] 2004.

² The original proviso to section 10(1) has been renumbered as subsection (1A) by EEIA (Amendment) Act 1993.

³ EEIA (Amendment No.2)] 2004 provides for mandatory deduction of capital allowances under sections 19A and 19B of the Income Tax Act.

⁴ Subsection renumbered as (1B) by EEIA (Amendment) Act 1993.

ADMINISTRATIVE PRACTICE

7 Where the tax relief period of a pioneer enterprise expires during the basis period for any year of assessment, capital allowances for that year of assessment are to be apportioned between the “old” trade or business and “new” trade or business of the pioneer enterprise in the following manner.

(a) Capital expenditure incurred before the expiry of the tax relief period

Initial allowances under Sections 16 and 19 of the ITA on capital expenditure incurred before the date of expiry of the tax relief period are to be allocated to the “old” trade or business.

(b) Assets in use at the end of both the tax relief period and the basis period

Where the assets are in use at the end of both the tax relief period and the basis period, annual allowances (AA) for the assets under Sections 16, 19 and 19A of the ITA are to be apportioned to the “old” trade or business and the “new” trade or business as follows:

Amount apportioned to the “old” trade or business:

Number of days in the basis period
relating to the “old” trade or business x AA
Number of days in the basis period

Amount apportioned to the “new” trade or business:

Number of days in the basis period
relating to the “new” trade or business x AA
Number of days in the basis period

(c) Capital expenditure incurred after the expiry of the tax relief period

Initial and annual allowances under Sections 16, 19 and 19A of the ITA on capital expenditure incurred after the expiry of the tax relief period are to be allocated to the “new” trade or business.

(d) Assets disposed before the expiry of the tax relief period

Balancing allowances or balancing charges under Section 20 of the ITA on assets disposed before the date of expiry of the tax relief period are to be allocated to the “old” trade or business.

(e) Assets disposed after the expiry of the tax relief period

Balancing allowances or balancing charges under Section 20 of the ITA on assets disposed after the date of expiry of the tax relief period are to be allocated to the “new” trade or business.

- 8 Unabsorbed capital allowances brought forward from the basis period preceding the basis period during which the tax relief expires are to be allocated to the “old” trade or business.