

IRAS CIRCULAR

Determination of the Date of Commencement of Business



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DETERMINATION OF THE DATE OF COMMENCEMENT OF BUSINESS

INTRODUCTION

- 1 On 14 March 2003, IRAS issued a Circular on “Concession For Enterprise Development – Tax Deduction Allowable for Certain Expenses Incurred Prior to Commencement of Business”. Under the concession, any person who carries on a business¹ will be treated as having commenced its operation on the first day of the accounting year in which it earns its first dollar of business receipt.
- 2 The concession does not, however, preclude a business from substantiating that it has commenced operation earlier than the accounting year in which it earns its first dollar of business receipt. Certain businesses may have commenced operation before the first dollar of business receipt is earned.
- 3 Generally, a business may be regarded as having commenced operation when it opens its doors to receive its first customer. All outgoings and expenses incurred from the actual date of commencement of business that are not capital in nature or are not denied deduction under Section 15 of the Singapore Income Tax Act (“SITA”), herein referred to as “revenue expenses”, will qualify for tax deduction.
- 4 This circular provides some guiding principles and examples on the determination of date of commencement of a business. It is not intended to provide an exhaustive list of situations and conditions for the determination of the date of commencement of a business, given that businesses differ and therefore will require different considerations for this purpose.

CURRENT TAX TREATMENT

- 5 The deductibility of outgoings and expenses of a business is governed by the provisions under Sections 14 and 15 of the SITA. Under Section 14(1), only outgoings and expenses that are wholly and exclusively incurred in the production of income are tax deductible.
- 6 All outgoings and expenses incurred prior to the date on which a business commences operation are not wholly and exclusively incurred in the production of income. Such pre-commencement or pre-operating expenses are not allowable for tax purposes.

¹ This refers to a person who carries on a trade, business, profession or vocation, the income from which is assessable to tax under section 10(1)(a) of the SITA. For tax purposes, a person includes a company.

CONSIDERATIONS FOR DETERMINING THE DATE OF COMMENCEMENT OF BUSINESS

- 7 The SITA does not provide specific definition on when a business is regarded as having commenced its operation. Based on case laws, the primary tax considerations are to ascertain the actual regular activities carried on by a business and the presence of the profit-making structure of the business that enable it to commence its day-to-day operation. It is only when the business has established its profit-making structure and started its first commercial activity that it can be regarded as having commenced operation. There is, however, no singular test provided in case laws on what constitutes the profit-making structure of a business.
- 8 What constitutes “a profit-making structure” will differ from business to business. The type of essential activities a business primarily engages in will determine its profit-making structure and the operational readiness of such structure. For example, in businesses like hotel operations, the profit-making structure can be said to be in place when the licence to operate is obtained. Generally, in determining the date of commencement of business by a taxpayer, the Comptroller of Income Tax (“CIT”) requires the following facts for examination:
- (i) description of the taxpayer’s main business;
 - (ii) profit-making structure of the identified business; and
 - (iii) chronological list of key events leading up to the profit-making structure being operationally ready and the time when the taxpayer starts its ordinary business activities.
- 9 In the course of evaluating the facts, the CIT will distinguish activities that are merely preparatory or preliminary in nature² from those conducted by the business on a day-to-day basis. Once the date of commencement of business is ascertained, all expenses incurred prior to this date, being pre-commencement or pre-operating expenses, would not qualify for tax deduction under Section 14(1).

EXAMPLES

- 10 The examples below illustrate CIT’s determination of the date of commencement of business for certain businesses.

² Preparatory or preliminary activities may include signing a business contract, obtaining a loan to build infrastructure for the business, construction/ building of the infrastructure, etc.

Wholesale and Retail

- 11 Generally, a trading business in the wholesale and retail industries is considered to have commenced its business when it opens its door to the public.

Example (Supermarket)

<u>Dates</u>	<u>Events</u>
1/1/2008	Incorporation of company
1/2/2008	Signed tenancy agreement for business premises, purchased office equipment, recruited staff, placed orders for products to be sold
1/4/2008	Retail stock arrived and arranged on shelves
9/4/2008	Supermarket opened to the public
1/6/2008	Opening ceremony

A supermarket commences business when it opens its door and offers its goods for sale to the public. Thus, the date of commencement would be 9/4/2008. The opening ceremony is merely ceremonial and does not alter the actual date of commencement.

Manufacturing

- 12 A manufacturing business is considered to have commenced operation only when a profit-making structure enabling the manufacturing operations capable of commercial production has been put in place. CIT considers the profit-making structure of a manufacturer to be in place when the manufacturer is capable of supplying goods/services to the customers in its ordinary course of business. Generally, the date of commercial production is taken as the date of commencement of a manufacturing business.

Example (Manufacturer of electronic components)

<u>Dates</u>	<u>Events</u>
2/1/2007	Incorporation of the company
1/12/2007	Completion of construction of manufacturing plant
5/12/2007	Relevant licences to manufacture components obtained
8/12/2007	Recruited staff
15/12/2007	Installed plant and machinery
20/12/2007	Engineers and technical specialist sent for training
15/1/2008	Purchased raw materials
30/1/2008	Trial run to test out product before commercial production
15/2/2008	Commenced commercial production
25/2/2008	First sale made

The business of manufacturing commences when the company is in a position to start its first commercial production, that is, on 15/2/2008. As with other manufacturing companies, there were expenses related to licences and approval permits that are required before operation of the plant. These and other expenses, including the construction of plant, installation of plant and machinery, recruitment and training of staff, purchase of raw materials and trial runs incurred prior to its commercial production are treated as pre-commencement expenses as these relate to preliminary work done in preparation for the commencement of business and hence not tax deductible.

Hoteliers

- 13 Under the Hotels Act, a hotel operator is required to register the premises with the Hotel Licensing Board (“HLB”) before it can operate a hotel. Typically, when an application to HLB is made, the hotel premises should be fully constructed and the internal fittings installed. Otherwise, it will not be able to meet the conditions for registration as a hotel. Only upon the successful registration is the hotel allowed to receive its first guest. CIT therefore considers a hotel to have commenced its business on the date of certificate of registration issued by HLB. This is because the hotel is unable to operate legally before this date.

Example

<u>Dates</u>	<u>Events</u>
6/1/2007	Purchased land to construct hotel premises
1/3/2007	Began construction of hotel premises
16/3/2008	Recruited staff
2/6/2008	Conducted training for staff
1/7/2008	Applied for hotel registration certificate
2/8/2008	Obtained certificate of hotel registration

The activities carried out by the company prior to 2/8/2008 were not the ordinary business of an hotelier but were merely preparatory in nature. The business would be regarded as having commenced on 2/8/2008, which is the earliest date it could operate as a hotelier and receive its first guest.

Property Developer

- 14 A newly incorporated property development company which develops properties for sale can be regarded as having commenced business when it acquires land/building for development for sale. All expenses incurred prior to the date of acquisition of land/building for development do not qualify for

tax deduction. Expenses such as property tax and interest that are directly attributable to the property and are incurred in the course of the property development would be capitalized as part of the development costs and qualify for tax deduction as cost of sale upon TOP.

Proprietary Club³

- 15 The main business of a proprietary club involves the sale of club memberships and that of the running a club. The main source of income for such business is usually from the sale of its club memberships. Thus, the proprietary club is generally regarded as having commenced business on the date it first launches its membership drive. All revenue expenses incurred on or after the date of first launch of membership are tax deductible.

Example

<u>Dates</u>	<u>Events</u>
16/10/2006	Purchased land to build clubhouse
12/11/2006	Conducted recruitment and staff training exercises
15/12/2006	Launched advertisement and promotional campaigns to market club membership
3/1/2007	Began construction of clubhouse
3/2/2007	Received first club membership fees from new members
13/3/2008	Completed the construction of clubhouse

The proprietary club would be regarded as having commenced its business on 15/12/2006 when it launched the club membership, although the club only received its first membership fees on 3/2/2007. It is through its advertisement and marketing efforts that the business would be able to derive its earnings. All activities carried out prior to 15/12/2006 were preparatory work to put the club in a position to sell its club membership. Thus, expenses that were incurred prior to 15/12/2006 are pre-commencement expenses that are not tax deductible.

Professional Services

- 16 A business which provides professional services such as fund management services is considered to have commenced operation when the necessary set-up for the activities that enables it to conduct its day-to-day operation is in place. Generally, this is when the business is ready to market its services and conclude contracts with its potential clients.

³ In a proprietary club, the club together with the premises and assets are owned by the proprietor. Members of the club do not own the club, and have no say in the management of the club.

Example (Fund management services)

<u>Dates</u>	<u>Events</u>
10/1/2006	Incorporation of the company
15/11/2006	Establishment of office
30/11/2006	Recruited fund managers and other office staff
15/3/2007	Commenced to market its fund management products/services
4/1/2008	Commenced to derive income

The business of fund management commenced on 15/3/2007 when the company was able to market its products and services, although the company only first started earning income on 4/1/2008. In the context of the fund management business, the marketing activities appear to be the company's regular business activities and an integral part of its day-to-day operations. The necessary set-up was in place on 15/3/2007 for marketing activities to be conducted. Expenses such as establishment of an office, hiring of fund managers and other office staff incurred prior to 15/3/2007 were preparatory in nature and therefore pre-commencement expenses which are not tax deductible.

ENQUIRIES

- 17 If you wish to seek clarification on the contents of this circular, please contact IRAS at 1800-3568622.

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