

# **IRAS CIRCULAR**

**CONCESSION FOR  
ENTERPRISE DEVELOPMENT  
- TAX DEDUCTION ALLOWABLE  
FOR CERTAIN EXPENSES INCURRED PRIOR  
TO COMMENCEMENT OF BUSINESS**



**INLAND REVENUE  
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# **IRAS CIRCULAR**

## **CONCESSION FOR ENTERPRISE DEVELOPMENT**

### **- TAX DEDUCTION ALLOWABLE FOR CERTAIN EXPENSES INCURRED PRIOR TO COMMENCEMENT OF BUSINESS**

#### **INTRODUCTION**

1 In his Budget Statement 2003, DPM and Minister for Finance announced the introduction of the concession for enterprise development. Under this concession, any person who carries on a business<sup>1</sup> will be treated as having commenced the business operation on the first day of the accounting year in which it earns its first dollar of business receipt.

2 The concession seeks to promote entrepreneurship by providing businesses with greater certainty regarding tax matters. It will also help to partially relieve businesses of the costs that they have to incur when starting out.

3 This circular provides details of the concession.

#### **EFFECTIVE DATE OF CONCESSION**

4 The concession will take effect from Year of Assessment (YA) 2004.

#### **CURRENT TAX TREATMENT OF OUTGOINGS AND EXPENSES INCURRED PRIOR TO COMMENCEMENT OF BUSINESS**

5 The deductibility of outgoings and expenses of a business is governed by the provisions under sections 14 and 15 of the Singapore Income Tax Act (SITA). Under section 14(1), only outgoings and expenses that are wholly and exclusively incurred in the production of income are tax deductible. Besides this general deduction rule, the SITA also provides a list of allowable deductions<sup>2</sup> and a separate list of non-allowable expenses<sup>3</sup>.

6 As 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, they are not allowable for tax purposes<sup>4</sup>. Consequently, for every new

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<sup>1</sup> 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.

<sup>2</sup> Section 14(1)(a) to (h), and sections 14A to 14O of the SITA

<sup>3</sup> Section 15(1)(a) to (q) of the SITA

<sup>4</sup> Furthermore, where any outgoings and expenses, incurred prior to the date on which a business commences operation, are incurred to set up the business by creating the permanent organisation or

business that is established, it is necessary to determine, based on the facts in each case, the date on which the business commences its operation in order to determine whether or not any of the outgoings or expenses incurred can qualify for tax deduction. This may pose some tax uncertainty to some businesses.

## **DETAILS OF THE CONCESSION**

7 Under the concession, a business will, unless paragraph 10 below applies, be treated as having commenced operation on the first day of the accounting year in which it earns its first dollar of business receipt. The effect of the concession is that all outgoings and expenses that are not capital in nature or are not denied deduction under section 15 of the SITA (hereinafter referred to as “revenue expenses”) incurred in that accounting year, including those incurred prior to the day on which the business earns its first dollar of business receipt, will be deductible for income tax purposes. The Annex contains examples that illustrate the effect of this concession in various situations.

8 Any loss incurred by any person carrying on a business for any YA due to such revenue expenses, not fully absorbed by other sources of income of that person for the same YA, will be available for set-off against his income for future YAs<sup>5</sup>. Such loss may also be transferred to a related company if the conditions under section 37C of the SITA (i.e. the provisions governing group relief for Singapore companies) are met.

9 The concession will be applied automatically to all businesses unless an earlier date has been established in accordance with paragraph 10 below. In other words, there is no requirement for any business to make an election to be accorded the concession.

10 The implementation of the concession does not preclude a business from providing the relevant details to the Comptroller of Income Tax (CIT) to substantiate that it has commenced operation before the accounting year in which it earns its first dollar of business receipt. Once it is established, based on facts, that the business has actually commenced its operation earlier, all revenue expenses incurred from the actual date of commencement of business will qualify for tax deduction.

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structure through which income is produced, they will also be disallowed on the basis that they are capital in nature.

<sup>5</sup> In the case of a company, the availability for set-off is subject to the shareholding test under section 37(5) of the SITA.

## **SECTION 10E COMPANIES**

11 The above concession is however not extended to companies to which the provisions of section 10E of the SITA apply.

12 Section 10E of the SITA currently provides rules for the determination of the taxable income of companies which have demonstrated or are able to demonstrate that they are carrying on the business of the making of investments (hereinafter referred to as “section 10E companies”)<sup>6</sup>. Among other things, it provides that any revenue expenses incurred by a section 10E company in respect of investments of that business that do not produce any income shall not be allowed as a deduction under section 14 of the SITA. As the Government has decided to maintain the current tax treatment of section 10E companies, this concession shall not apply to such companies.

## **ENQUIRIES**

13 For any enquiries or clarification on this circular, please call 1800-3568622 (Corporate) or 1800-3568611 (Individual).

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<sup>6</sup> Please refer to Income Tax Practice Note 24 of Vol. 4 No. 1, Practice Note 26 of Vol 5 No. 1 and Practice Note 28 of Vol 5 No 2 for more details on the application of the provisions of section 10E.

## ILLUSTRATION OF THE EFFECT OF THE CONCESSION FOR ENTERPRISE DEVELOPMENT

### Example 1

A partnership was registered on 1 Feb 2002 to carry on a business. Its accounting year ends on 31 Jul. Its first set of accounts is for the period from 1 Feb 2002 to 31 Jul 2003 (i.e. 18 months) during which it earns its first dollar of business receipt.

Based on this set of accounts, the basis periods for the relevant YAs are as follows:

- a) YA 2003: 1 Feb 2002 to 31 Jul 2002 (6 months).
- b) YA 2004: 1 Aug 2002 to 31 Jul 2003 (12 months).

- (i) Suppose the first dollar of business receipt is earned on 6 Jun 2002 (i.e. during the period from 1 Feb 2002 to 31 Jul 2002 – YA 2003)

Effect of concession:

⇒ Nil, since the concession is not applicable as it takes effect only from YA 2004.

- (ii) Suppose the first dollar of business receipt is earned on 15 Jul 2003 (i.e. during the period from 1 Aug 2002 to 31 Jul 2003 – YA 2004)

Effect of concession:

⇒ Revenue expenses incurred from 1 Aug 2002 to 14 Jul 2003 are tax deductible.

## ILLUSTRATION OF THE EFFECT OF THE CONCESSION FOR ENTERPRISE DEVELOPMENT

### Example 2

A company is incorporated on 6 May 2003 to carry on a business. Its accounting year ends on 31 December. Its accounts for the first 3 years since incorporation are as follows:

| Year of Assessment        | <u>2004</u>              | <u>2005</u>              | <u>2006</u>              |
|---------------------------|--------------------------|--------------------------|--------------------------|
| Basis period              | 6 May 03 to<br>31 Dec 03 | 1 Jan 04 to<br>31 Dec 04 | 1 Jan 05 to<br>31 Dec 05 |
|                           | \$                       | \$                       | \$                       |
| Sales income              | 0                        | 0                        | 25,762                   |
| Interest income           | <u>0</u>                 | <u>2,074</u>             | <u>3,384</u>             |
|                           | 0                        | 2,074                    | 29,146                   |
| Less: expenses            |                          |                          |                          |
| Advertisement/promotion   | (81)                     | (145)                    | (2,514)                  |
| Audit fee                 | (500)                    | (600)                    | (1,200)                  |
| Depreciation              | (326)                    | (524)                    | (856)                    |
| Fixed assets expensed off | 0                        | (294)                    | (281)                    |
| Penalties and fines       | (70)                     | (50)                     | (120)                    |
| Printing & stationery     | (48)                     | (154)                    | (234)                    |
| Private car expenses      | (343)                    | (2,725)                  | (3,079)                  |
| Rental                    | (3,200)                  | (4,800)                  | (6,000)                  |
| Repairs & maintenance     | (284)                    | (277)                    | (1,560)                  |
| Secretarial fee           | (200)                    | (200)                    | (300)                    |
| Staff salaries            | (4,376)                  | (7,542)                  | (12,588)                 |
| Telephone                 | (419)                    | (623)                    | (1,950)                  |
| Travelling and transport  | (272)                    | (421)                    | (2,844)                  |
| Water and electricity     | <u>(873)</u>             | <u>(885)</u>             | <u>(1,854)</u>           |
| Net profit/(loss)         | <u>(10,992)</u>          | <u>(17,166)</u>          | <u>(6,234)</u>           |

Suppose its first dollar of business receipt is earned on 1 Nov 2005 (YA 2006), the effect of the concession on the company is as follows:

- YA 2004 ⇒ Not applicable since the company did not earn its first dollar of business receipt.
- YA 2005 ⇒ Not applicable since the company did not earn its first dollar of business receipt.
- YA 2006 ⇒ Revenue expenses incurred from 1 Jan 2005 to 31 Oct 2005 are also tax deductible.

### Elaboration on the tax assessment for YA 2006

If the company does not provide any relevant details to CIT to show that it has commenced business operation at a date earlier than 1 Nov 2005, CIT will apply the concession automatically to the company for YA 2006.

The difference between the company's chargeable income (CI), with and without the concession for the YA 2006 is as follows:

|                                    | Without<br>concession <sup>7</sup> | With<br>concession <sup>8</sup> |
|------------------------------------|------------------------------------|---------------------------------|
|                                    | \$                                 | \$                              |
| Sales income                       | 25,762                             | 25,762                          |
| Less: Expenses                     |                                    |                                 |
| Advertisement/promotion            | (419)                              | (2,514)                         |
| Audit fee                          | (200)                              | (1,200)                         |
| Printing & stationery              | (39)                               | (234)                           |
| Rental                             | (1,000)                            | (6,000)                         |
| Repairs & maintenance              | (260)                              | (1,560)                         |
| Secretarial fee                    | (50)                               | (300)                           |
| Staff salaries                     | (2,098)                            | (12,588)                        |
| Telephone                          | (325)                              | (1,950)                         |
| Travelling and transport           | (474)                              | (2,844)                         |
| Water and electricity              | <u>(309)</u>                       | <u>(1,854)</u>                  |
| Adjusted profit/(loss)             | 20,588                             | (5,282)                         |
| Add: Interest income               | <u>3,384</u>                       | <u>3,384</u>                    |
| Unabsorbed loss c/f (note 1)       |                                    | <u>(1,898)</u>                  |
| CI (before exempt amount)          | 23,972                             |                                 |
| Less exempt amount (note 2)        | <u>14,486</u>                      |                                 |
| CI (after deducting exempt amount) | <u>9,486</u>                       | <u>Nil</u>                      |

#### Note 1

This amount is available for set-off against income of future YAs [subject to the shareholding test under section 37(5) of the SITA], or can be transferred to a related company if the conditions under section 37C (i.e. the provisions governing group relief for Singapore companies) of the SITA are met.

#### Note 2

Computed according to section 43(5) of the SITA.  
i.e. \$14,486 = (75% x \$10,000) + (50% x 13,972).

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<sup>7</sup> Without the concession, all expenses from 1 Jan 2005 to 30 Oct 2005 are not allowable for tax purposes for YA 2006. In other words, only revenue expense from 1 Nov 2005 to 31 Dec 2005 can be deducted. For the purpose of this illustration, it is assumed that all expenses are incurred evenly throughout the year.

<sup>8</sup> With the concession, the company is treated as having commenced business operations on the first day of the accounting year, i.e. 1 Jan 2005. All revenue expenses for the whole year (from 1 Jan 2005 to 31 Dec 2005) would be allowable for tax purposes for YA 2006.