INLAND REVENUE
AUTHORITY
OF SINGAPORE

IRAS e-Tax Guide

Income Tax: Treatment of Certain Expenses Incurred Prior to the Commencement of a Business Activity (Second Edition)

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1 Aim

1.1 This e-Tax Guide provides guidance on the tax treatment of certain expenses incurred before a person commences his business activity[1] or earns revenue from his business.

1.2 This e-Tax Guide is relevant to you if you derive income from a business activity that is subject to tax at different tax rates[2] in the Year of Assessment relating to the basis period in which the business activity commences or is deemed to have commenced (referred to as "first YA").

2 At a glance

2.1 Qualifying expenditure relating to intellectual property protection, research and development, renovation or refurbishment ("R&R") and design incurred before the business activity commences (collectively, "pre-commencement expenses") are deemed to be incurred on the first day on which the business activity commences ("actual date of commencement")[3]. As such, the pre-commencement expenses are tax- deductible in the basis period in which the business activity commences.

2.2 Under section 14R of the Income Tax Act 1947 (2020 Revised Edition) ("ITA"), a person is treated as having commenced his business on the first day of the accounting year in which the business earns its first dollar of business receipt ("deemed date of commencement"). The person may claim tax deduction on revenue expenses incurred before the first dollar of business receipt is derived as well as revenue expenses incurred up to 12 months prior to the deemed date of commencement (collectively, "s14R expenses")[4].

2.3 If you derive income from a business activity that is subject to tax at different tax rates in the first YA, the pre-commencement and s14R expenses that are directly attributable to normal income, concessionary income and tax-exempt income will be allowed deduction against the respective income streams. The remaining pre-commencement and s14R expenses will be apportioned among the different streams of income based on the proportion of the income to the total income and allowed deduction against the respective streams of income accordingly. This takes effect for pre-commencement and s14R expenses incurred on or after 25 Mar 2016.

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[1] This refers to activities that generate income assessable to tax under section 10(1)(a) of the ITA.

[2] Income that is subject to tax at different tax rates includes income that is exempt from tax.

[3] The relevant provisions are sections 14A(3), 14C(2), 14N(4) and 14P(5) of the ITA respectively.

[4] Please refer to IRAS e-Tax Guide "Deduction for Expenses Incurred Before First Dollar of Income is Earned", published on 23 Mar 2022.

2.4 However, if you derive only concessionary income or tax-exempt income in the first YA, all pre-commencement and s14R expenses incurred on or after 25 Mar 2016 will be allowed deduction against the concessionary income or tax-exempt income.

3 Glossary

3.1 Actual date of commencement

First day on which business activity commences. Please refer to IRAS e-Tax Guide “Determination of the Date of Commencement of Business” for the guidance and examples on the determination of the date of commencement of a business.

3.2 Concessionary income

Income that is subject to tax at a concessionary rate of tax.

3.3 Deemed date of commencement

The first day of the accounting year in which a business earns its first dollar of business receipt.

3.4 Normal income

Income that is subject to tax at the rate of tax in section 42(1) or 43(1) of the ITA, as the case may be.

3.5 Pre-commencement expenses

Qualifying expenditure relating to intellectual property protection, research and development, R&R and design incurred before the business activity commences that are deemed to be incurred on the first day on which the business activity commences under sections 14A(3), 14C(2), 14N(4) and 14P(5) of the ITA respectively.

3.6 Revenue expenses

All outgoings and expenses that would have been allowable under Part V of the ITA and are not denied deduction under section 15 of the ITA if the business had commenced when the expenses are incurred.

3.7 S14R expenses

Revenue expenses incurred on or after the deemed date of commencement but before the first dollar of business receipt is derived as well as revenue expenses incurred up to 12 months prior to the deemed date of commencement.

4 Background

4.1 The following pre-commencement expenses are deemed to be incurred by a person on the actual date of commencement of the business activity:

a. Costs for protecting Intellectual Property under section 14A(3) of ITA;
b. Expenditure on research and development under section 14C(2) of ITA;
c. R&R expenditure under section 14N(4) of ITA; and
d. Design expenditure under section 14P(5) of ITA.

4.2 Under section 14R of the ITA, any person who carries on a business activity is considered to have commenced business on the deemed date of commencement[5]. Revenue expenses incurred on or after the deemed date of commencement but before the person derives the first dollar of business receipt as well as revenue expenses incurred up to 12 months prior to the deemed date of commencement (collectively, "s14R expenses") are deductible for income tax purposes[6].

5 Tax treatment before Budget 2016

5.1 Where a person's income from a business activity is subject to tax at different rates of tax[7] in the first YA, the person is not required to allocate the pre-commencement expenses and s14R expenses to normal income, concessionary income and tax-exempt income.

5.2 The examples in Annex A illustrate the application of sections 14A and 14R prior to the Budget 2016 announcement.

6 New tax treatment for pre-commencement expenses and s14R expenses

6.1 To ensure fair allocation of the pre-commencement expenses and s14R expenses to income derived from the business activity that is subject to tax at different tax rates in the first YA and to provide certainty on the allocation method to be used, the pre-commencement and s14R expenses will be allowed as follows:

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[5] Section 14R(2)(b) of the ITA
[6] In the case where a person has ceased his business for some time but subsequently recommences the same business or another business, section 14R also applies in determining the revenue expenses deductible in relation to the subsequent business.
[7] For example, a person may enjoy tax incentives under the ITA or the Economic Expansion Incentives (Relief from Income Tax) Act ("EEIA"), which accord tax exemption or concessionary tax rates on the incentivised income.

a. Pre-commencement expenses and s14R expenses that are directly attributable to the normal income, concessionary income and tax-exempt income will be offset against the respective income streams; and

b. The remaining pre-commencement expenses and s14R expenses will be allocated to the respective income streams based on income apportionment. Examples of income-apportionment basis include "turnover", "gross profit" or "ratio B" for banks.

6.2 The above change applies to pre-commencement expenses and s14R expenses incurred on or after 25 Mar 2016. The examples in Annex B illustrate the application of sections 14A and 14R to a company claiming such expenses.

6.3 Where the person carries on more than one trade, business, profession or vocation (as the case may be), the pre-commencement expenses and s14R expenses incurred in respect of each trade, business, profession or vocation should be separately tracked and attributed to income of the respective trade, business, profession or vocation, before applying the above treatment.

6.4 All other conditions governing the claim of expenses under sections 14A, 14C[8], 14N[9], 14P and 14R of the ITA remain the same.

6.5 Any excess of the pre-commencement expenses or s14R expenses over the respective income streams would form part of the trade losses and such trade losses may be available for:

(i) offset against other sources of income in the same YA[10];
(ii) offset against income for future YAs[11];
(iii) transfer to a related company under the group relief system[12]; and
(iv) carry back to the immediate preceding YA[13].

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[8] For more details, please refer to the e-Tax Guide on "Research and Development Tax Measures (Sixth Edition)".
[9] For more details, please refer to the e-Tax Guide on "Deduction for Expenses incurred on Renovation or Refurbishment Works Done to Your Business Premises".
[10] Subject to the section 37A adjustment factor, if applicable. Section 37A provides for an adjustment factor to be applied when offsetting any unabsorbed capital allowances ("CA"), losses or donations in respect of income that is taxed at one rate against income taxed at another rate. The adjustment factor is the ratio which the tax rate of the activity giving rise to the loss or CA bears to the tax rate of the income against which the loss or CA is to be offset.
[11] In the case of a company or registered business trust, the availability of offset is subject to the shareholding test under section 37(12) of the ITA.
[12] Subject to the provisions of section 37B.
[13] Subject to the provisions of sections 37D.

7 Administrative procedure

7.1 If you have incurred pre-commencement expenses and s14R expenses that are directly attributable to the normal income, concessionary income and tax-exempt income of your business, you should claim a deduction of such direct expenses against the respective income streams. In this regard, you are required to provide the description and amount of such expenses; and the basis to substantiate your claim that such expenses are directly attributable to the respective streams of income in your tax computation for the relevant YA. The remaining pre-commencement expenses and s14R expenses will be allocated to the respective income streams based on income apportionment.

7.2 You are required to maintain the relevant supporting documents relating to expenses claimed but you need not submit those documents to IRAS unless requested by IRAS to do so.

8 Contact information

For any enquiries or clarification on this e-Tax Guide, please call
(i) 1800 356 8622 (Corporate) or
(ii) 1800 356 8300 (Individual)

9 Updates and amendments

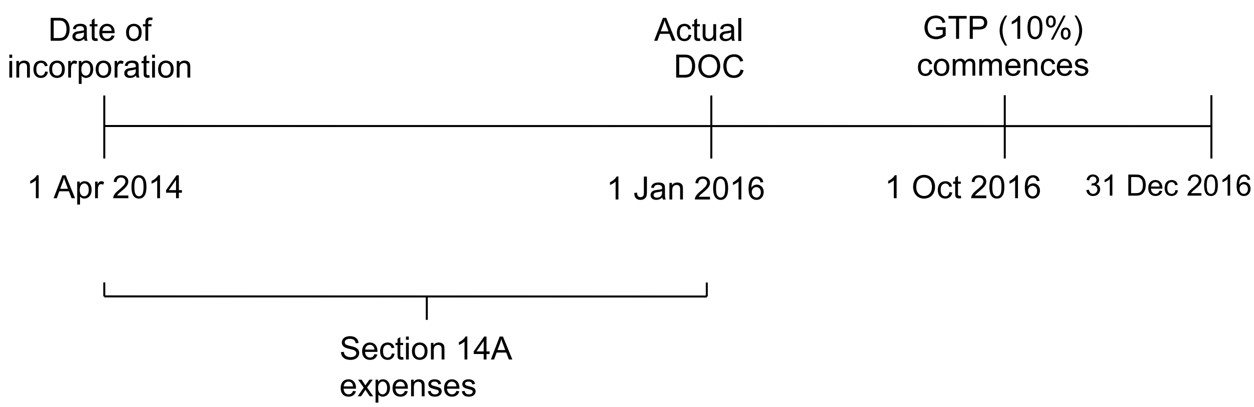
	Date of amendment	Amendments made
1	23 Mar 2022	The e-Tax Guide has been updated to make reference to the renumbered provisions in the Income Tax Act 1947 (2020 Revised Edition).

Annex A – Examples illustrating the application of sections 14A and 14R prior to the Budget 2016 announcement

Example 1: Application of section 14A

A company was incorporated on 1 Apr 2014 and commenced its trade on 1 Jan 2016. Its accounting year ends on 31 Dec. The company is awarded a 10% Global Trader Programme ("GTP") incentive, commencing on 1 Oct 2016.

1 Apr 2014	Date of incorporation
1 Jan 2016	Actual date of commencement ("Actual DOC")
1 Oct 2016	GTP incentive commences

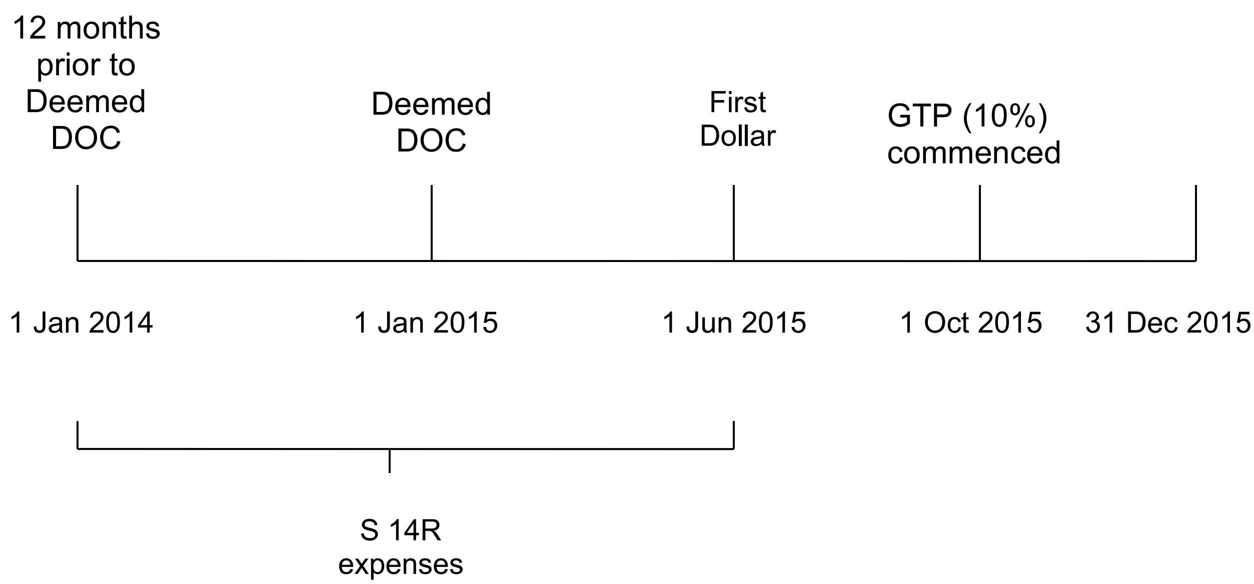


Under section 14A(3), any patenting costs and qualifying intellectual property registration costs incurred from 1 Apr 2014 to 31 Dec 2015 are deemed to be incurred on 1 Jan 2016. As the GTP incentive commences after the actual date of commencement of the business activity, the section 14A expenses would be allowed against income taxable at the normal tax rate ("NTR").

Example 2: Application of section 14R

A company was incorporated on 1 Dec 2013 and has a Dec accounting year end. The company was awarded a 10% GTP incentive which commenced on 1 Oct 2015.

1 Dec 2013	Date of incorporation
1 Jan 2015	Deemed date of commencement ("Deemed DOC")
1 Jun 2015	Earned its first dollar of receipt
1 Oct 2015	GTP incentive commenced
1 Jan 2015 to 31 Dec 2015	Accounting year in which the company earned its first dollar



Under section 14R, the revenue expenses incurred during the period from 1 Jan 2014 to 31 May 2015 are deductible in YA 2016. As the GTP incentive commenced after the date on which the first dollar was earned, the s14R expenses would be allowed against income taxable at the NTR.

Annex B – Examples illustrating the application of sections 14A and 14R before and after the change in tax treatment

Example 1: Application of section 14A

A company was incorporated on 1 Jun 2014 and commences its trade on 1 Jan 2017. Its accounting year ends on 31 Dec. The company is awarded a 10% GTP incentive, commencing on 1 Oct 2017.

1 Jun 2014	Date of incorporation
1 Jan 2017	Actual date of commencement
1 Oct 2017	GTP incentive commences
1 Jan 2017 to 30 Sep 2017	Sales income of $20m
1 Oct 2017 to 31 Dec 2017	Sales income of $5m (all the sales income qualify as GTP qualifying income)

The table below shows the difference in section 14A deduction before and after the change in tax treatment:

	Before the change	After the change
Section 14A expenses incurred from 1 Jun 2014 to 24 Mar 2016	Allowable in YA 2018 against income taxable at NTR, as any expenses incurred during this period are treated as incurred on 1 Jan 2017 and the Company's GTP incentive commences on a later day, 1 Oct 2017.	Same tax treatment as before the Budget 2016 change.

	Before the change	After the change
Section 14A expenses incurred from 25 Mar 2016 to 31 Dec 2016	Allowable in YA 2018 against income taxable at NTR, as any expenses incurred during this period are treated as incurred on 1 Jan 2017 and the Company's GTP incentive commences on a later day, 1 Oct 2017. **(Note: this tax treatment is no longer applicable with the change announced in Budget 2016)**	Expenses that are directly attributable to the pre-GTP and GTP income would be offset against the respective income streams. The remaining section 14A expenses that cannot be directly identified to the respective income streams will be apportioned to the pre- GTP and GTP income based on income proportion, as follows: <u>Pre-GTP income</u> S$20m/S$25m x remaining section 14A expenses <u>GTP income</u> S$5m/S$25m x remaining section 14A

In this example, any section 14A expenses incurred during the period from 1 Jun 2014 to 24 Mar 2016 are allowable in YA 2018 against income at NTR while any section 14A expenses incurred during the period from 25 Mar 2016 to 31 Dec 2016 are allowable in YA 2018 against income taxable at NTR or concessionary tax rate ("CTR") as stated in the table above. If there is insufficient chargeable income at NTR in that YA, the excess of such expenses over income may be offset against the company's GTP income after the application of the section 37A adjustment factor.

Example 2: Application of section 14R

A company was incorporated on 1 Jul 2014 to carry on a business. Its accounting year ends on 31 Dec. Other details are as follows:

1 Jul 2014	Date of incorporation
1 Jul 2014	Company first incurred revenue expenses such as rental, utilities, etc.
1 Jan 2016	Deemed date of commencement
1 Jun 2016	Company earned its first dollar of business receipt
1 Oct 2016	Company's GTP incentive commences
1 Jun 2016 to 30 Sep 2016	Sales income of $12m
1 Oct 2016 to 31 Dec 2016	Sales income of $3m (of which S$2m qualify as GTP qualifying income)

The table below shows the difference in revenue expenses deduction before and after the change in tax treatment:

	Before the change	**After the change**
Revenue expenses incurred from 1 Jul 2014 to 31 Dec 2014.	Not allowable. The expenses were not incurred within 12 months prior to the deemed date of commencement, which is 1 Jan 2016.	Same tax treatment as before the Budget 2016 change.
Revenue expenses incurred during the period from 1 Jan 2015[14] to 31 Dec 2015.	Allowable in YA 2017 against income taxable at NTR, as any expenses incurred during this period are treated as incurred on 1 Jan 2016 and the Company's GTP incentive commences on a later day, 1 Oct 2016.	Same tax treatment as before the Budget 2016 change.
Revenue expenses incurred during the period from 1 Jan 2016 to 24 Mar 2016.	Allowable in YA 2017 against income taxable at NTR, as the Company's GTP incentive commences on a later day, 1 Oct 2016.	Same tax treatment as before the Budget 2016 change.

[14] 12 months prior to the deemed date of commencement

	Before the change	After the change
Revenue expenses incurred from 25 Mar 2016 to 31 May 2016	Allowable in YA 2017 against income taxable at NTR as the Company's GTP incentive commences on a later day, 1 Oct 2016. **(Note: this tax treatment is no longer applicable with the change announced in Budget 2016)**	Expenses that are directly incurred to derive the pre-GTP, GTP and non-GTP qualifying income would be offset against the respective income streams and remaining expenses that cannot be directly identified to the respective income streams will be apportioned to the pre-GTP, GTP and non-GTP qualifying income based on income proportion, as follows: <u>Pre-GTP income</u> S$12m/S$15m x remaining s14R expenses <u>GTP income</u> S$2m/S$15m x remaining s14R expenses <u>Non-GTP qualifying income</u> S$1m/S$15m x remaining s14R expenses

In this example, any s14R expenses incurred during the period from 1 Jan 2015 to 24 Mar 2016 are allowable in YA 2017 against income taxable at NTR while any s14R expenses incurred during the period from 25 Mar 2016 to 31 May 2016 are allowable in YA 2017 against income taxable at NTR or CTR as stated in the table above. If there is insufficient chargeable income at NTR in that YA, the excess of such expenses over income may be offset against the company's GTP income after application of the section 37A adjustment factor.