IRAS e-Tax Guide

Income Tax: Concession for Enterprise Development – Deduction of Certain Expenses Incurred Before Business Revenue is Earned

(Second Edition)

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Income Tax: Concession for Enterprise Development – Deduction of Certain Expenses Incurred before Business Revenue is Earned

1 Aim

1.1 This e-tax guide[1] explains the concession for enterprise development, which was first implemented in 2003, and enhanced in Budget 2011. The concession allows tax deduction on certain expenses incurred before a business begins to generate revenue.

2 Glossary

2.1 **Deemed date of commencement**

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

2.2 **Revenue expenses**

All outgoings and expenses that would have been allowable under section 14 and are not denied deduction under section 15 of the Income Tax Act (ITA) if the business had commenced when the expenses are incurred.

3 Background

3.1 The concession for enterprise development was introduced in Budget 2003 and took effect from Year of Assessment (YA) 2004.

3.2 Under the concession, a person[2] who conducts business activities[3] is treated as having commenced his business on the deemed date of commencement. The concession seeks to promote entrepreneurship by providing businesses with greater certainty regarding tax matters. It also helps to partially relieve businesses of the costs incurred when starting out.

3.3 To facilitate business start-ups further, the Minister for Finance has announced in Budget 2011 that businesses may claim tax deduction on revenue expenses incurred in the accounting year immediately

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[1] This e-tax guide replaces the IRAS e-tax guide on "Concession for enterprise development – tax deduction allowable for certain expenses incurred prior to commencement of business" issued on 14 Mar 2003.

[2] For the purpose of this guide, a person includes a partnership.

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

before the deemed date of commencement. This enhancement takes effect from YA 2012. The enhancement provides further relief to business start-ups which take a longer time to generate revenue.

3.4 This e-Tax Guide supersedes IRAS's e-Tax Guide issued on 14 March 2003 on "Concession for Enterprise Development – Tax Deduction Allowable for Certain Expenses incurred prior to Commencement of Business" and provides details on the 2011 enhancement.

4 Tax Treatment before YA 2004

4.1 Sections 14 and 15 of the ITA govern the deductibility of outgoings and expenses of a business. 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 ITA also lists certain allowable deductions[4] and non-allowable expenses[5].

4.2 Outgoings and expenses incurred before a business commences operation are not wholly and exclusively incurred in the production of income. Hence, they are not allowable for tax purposes[6]. Consequently, for every new business that is established, it is necessary to determine the date on which the business commences its operations. This may pose tax uncertainty to some businesses.

5 Concession for Enterprise Development 2003

5.1 Under the 2003 concession for enterprise development, a business is, unless paragraph 7.1 below applies, treated as having commenced its operations on the deemed date of commencement. This means revenue expenses incurred in an accounting year, including those incurred prior to the day on which the business earns its first dollar of business receipt, are deductible for income tax purposes.

5.2 Any excess of the revenue expenses over the business income in the basis period for a YA is treated as a trade loss for that YA. Thus, the trade loss may be available for:

(i) offset against other income in the same YA;

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[4] Sections 14(1)(a) to (h), and sections 14A to 14T of the ITA (2008 Revised Edition).

[5] Section 15(1)(a) to (q) of the ITA.

[6] In addition, outgoings and expenses may be incurred prior to the date on which a business commences operation to set up the business by creating the permanent organisation or structure through which income is produced. These expenses are disallowed on the basis that they are capital in nature.

(ii) offset against income for future YAs[7],

(iii) transfer to a related company under the group relief system[8],

(iv) transfer to spouse[9], and

(v) carry-back relief to preceding YA[10].

6 Enhancement to the Concession Announced in Budget 2011

6.1 In Budget 2011, the 2003 concession is enhanced to allow tax deduction for revenue expenses incurred in the accounting year immediately preceding the deemed date of commencement. Such revenue expenses are treated as incurred on the deemed date of commencement. They are deductible against the business income derived during the basis period in which the business derives its first dollar of business receipt[11]. Similarly, any excess of the revenue expenses over the business income for a YA is treated as a trade loss. The usual rules for utilisation of the trade loss apply (see paragraph 5.2).

6.2 The 2011 enhancement, which will be given legal effect in the Income Tax Act, takes effect from YA 2012. This means businesses can claim revenue expenses incurred in an accounting year ending in 2010 (YA 2011) if the first dollar of business receipt is earned during accounting year ending in 2011 (YA 2012) and so on. The examples in Annex A illustrate the application of the 2003 concession and the 2011 enhancement.

7 Actual Date of Commencement

7.1 As with the 2003 concession, the implementation of the 2011 enhancement does not preclude businesses from providing relevant details to the Comptroller of Income Tax (CIT) to substantiate that their business operations have commenced earlier than the deemed date of commencement. If the actual date of commencement is established to be earlier than the deemed date of commencement, all expenses incurred wholly and exclusively in the production of income from the

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[7] 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 (‘shareholding test’).

[8] Subject to the provisions of section 37C.

[9] Subject to the provisions of section 37D.

[10] Subject to the provisions of sections 37E and 37F.

[11] In the case where a person has ceased his business for some time but subsequently recommences the same business or another business, the concession also applies in determining the revenue expenses deductible in relation to the subsequent business.

actual date of commencement are tax deductible, subject to the provisions of section 15. In this regard, please refer to the e-Tax Guide on "Determination of the Date of Commencement of Business" for the guiding principles and examples.

8 Administrative Procedure

8.1 Any person who wishes to claim tax deduction of revenue expenses under the 2011 enhancement is required to provide the amounts and description of such expenses incurred during the basis period for the preceding YA in the tax computation for the current YA in which the first dollar of business receipt is earned. For example, if a business earns its first dollar of business receipt during the basis period for YA 2012, it must include the revenue expenses incurred during the basis period for YA 2011 in its YA 2012 tax computation.

8.2 For partnerships and sole-proprietorships, the amount of expenses claimed under the 2011 enhancement must be included in the line "allowable business expenses" of the 4-line statement for the year of claim.

8.3 Businesses are required to maintain the relevant supporting documents relating to the expenses claimed but they <u>need not submit those documents to IRAS unless we ask for them.</u>

8.4 The accounting period before the deemed date of commencement may exceed 12 months. In such a scenario, only revenue expenses relating to the 12-month period immediately before the deemed date of commencement may qualify for tax deduction under the 2011 enhancement. Where a business is unable to identify the relevant expenses, the CIT may apply time apportionment to arrive at the amount of expenses for the 12-month period.

8.5 The example in Annex B illustrates the application of the 2011 enhancement to a company with its first set of accounts prepared for a period exceeding 12 months.

9 Income subject to the provisions of section 10E

9.1 As with the 2003 concession, the 2011 enhancement is not applicable to the income of entities to which the provisions of section 10E of the ITA applies.

9.2 Section 10E of the ITA provides rules for determining the taxable income of entities that carry on the business of the making of investments. Among other things, the provisions disallow tax deduction of revenue expenses incurred by such an entity in relation to non-income producing investments. As the Government has decided to maintain the current tax treatment of section 10E, the concessions remain not applicable to income which is subject to the provisions of section 10E.

10 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).

11 Updates and Amendments

	Date of amendment	Amendments made
1	03 Sept 2014	Paragraph 7.1 amended to make reference to e-Tax Guide "Determination of the Date of Commencement of Business".

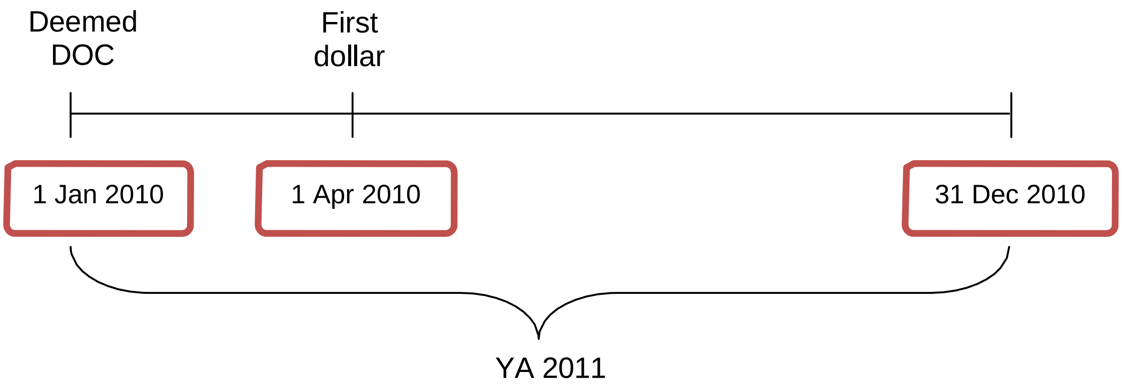
Annex A

Examples Illustrating the Effect of the 2003 Concession and the 2011 Enhancement

Example 1 (2003 Concession)

A sole proprietor registered its business on 1 December 2009 and has December year end.

1 Dec 2009	Date of registration
1 Apr 2010	Earns its first dollar of business receipt
1 Jan 2010	Deemed date of commencement (DOC)
1 Jan 2010 to 31 Dec 2010	Accounting year in which the sole proprietor earns first dollar

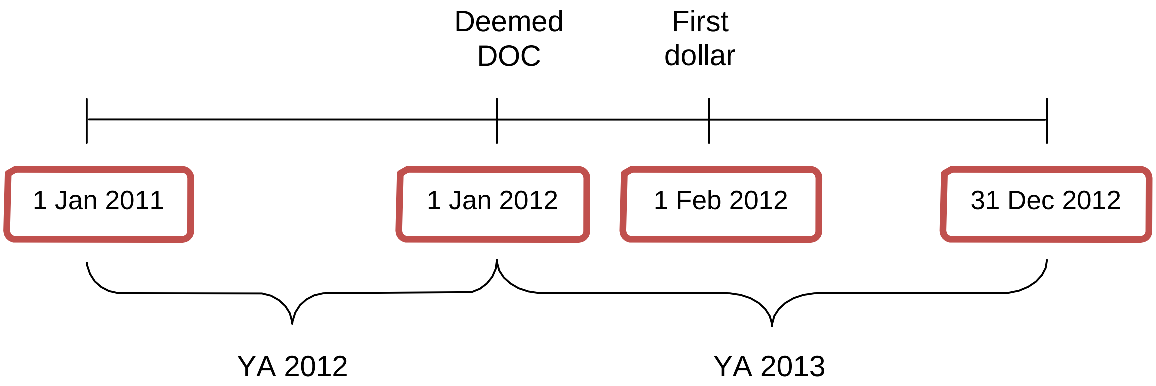


Under the 2003 concession, revenue expenses incurred during the basis period for YA 2011, including those incurred prior to the day on which the business earns its first dollar of business receipt, are deductible.

Example 2 (2011 Enhancement)

A partnership is registered on 1 July 2010 and has December year end.

1 July 2010	Date of registration
1 Feb 2012	Earns its first dollar of business receipt
1 Jan 2012	Deemed date of commencement (DOC)
1 Jan 2012 to 31 Dec 2012	Accounting year in which the partnership earns first dollar



Under the 2011 enhancement, revenue expenses incurred during the basis period for YA 2012 are deemed incurred on 1 January 2012 (first day of the accounting year in which first dollar of business receipt is earned) and deductible in YA 2013.

(Note: The revenue expenses incurred during the period from 1 January 2012 to 31 January 2012 would also be allowable under the 2003 concession.)

Example 3

A company is incorporated on 6 May 2011 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	2012	2013	2014
Basis period	6 May 11 to 31 Dec 11	1 Jan 12 to 31 Dec 12	1 Jan 13 to 31 Dec 13
Sales income	0	0	25,762
Interest income	0	2,074	3,384
	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	(873)	(885)	(1,854)
Net profit/ (loss)	(10,992)	(17,166)	(6,234)

The company earns its first dollar of business receipt on 1 June 2013 (YA 2014).

The table below compares the effect of the concession for enterprise development.

<table>
<tr><th>Expenses incurred for period / year</th><th>Without concession</th><th>With 2003 concession</th><th>With 2011 enhancement</th></tr>
<tr><td>6 May 2011 to 31 Dec 2011</td><td rowspan="3">All expenses incurred may not be tax deductible</td><td rowspan="2">All expenses incurred may not be tax deductible</td><td>All expenses incurred may not be tax deductible</td></tr>
<tr><td>1 Jan 2012 to 31 Dec 2012</td><td>Revenue expenses incurred are tax deductible for YA 2014 (2011 enhancement)[12]</td></tr>
<tr><td>1 Jan 2013 to 31 May 2013</td><td>Revenue expenses incurred are tax deductible for YA 2014 (2003 concession)</td><td>Revenue expenses incurred are tax deductible for YA 2014 (2003 concession)</td></tr>
<tr><td>1 Jun 2013 to 31 Dec 2013</td><td>Revenue expenses incurred are tax deductible for YA 2014</td><td>Revenue expenses incurred are tax deductible for YA 2014</td><td>Revenue expenses incurred are tax deductible for YA 2014</td></tr>
</table>

[12] To benefit from the 2011 enhancement, the company has to provide the amounts and description of revenue expenses incurred during the year ending 31 December 2012 in its tax computation for YA 2014.

Tax computation for YA 2014[13]

The effect of the 2011 enhancement to the company for YA 2014 is shown in the tax computation below.

	Without Concession	With 2003 Concession	With 2011 Enhancement
Net profit/ (loss)	(6,234)	(6,234)	(6,234)
Add/(less):			
Interest income	(3,384)	(3,384)	(3,384)
Depreciation	856	856	856
Fixed assets expensed off	281	281	281
Penalties and fines	120	120	120
Private car expenses	3,079	3,079	3,079
Disallowable expenses incurred between 1 Jan 13 & 31 May 13 *[note 1]*	12,935	-	-
	7,653	(5,282)	(5,282)
(Less):			
Deductible revenue expenses incurred in the basis period for YA 2013 *[note 2]*	-	-	(15,647)
Adjusted profit/ (loss)	7,653	(5,282)	(20,929)
Add: Interest income	3,384	3,384	3,384
Unabsorbed losses c/f *[note 3]*		(1,898)	(17,545)
Chargeable income before partial tax exemption	11,037		

[13] CIT applies the 2011 enhancement to the company for YA 2014, unless the company provides relevant details to CIT to show that it has commenced business operation before 1 January 2013.

Notes :

1. Assumption: all expenses are incurred evenly throughout the year.

Computation of disallowable expenses for period 1 Jan 13 to 31 May 13 (5 months)

Expenses as per accounts:	
Advertisement/ promotion	2,514
Audit fee	1,200
Printing & stationery	234
Rental	6,000
Repairs & maintenance	1,560
Secretarial fee	300
Staff salaries	12,588
Telephone	1,950
Travelling and transport	2,844
Water and electricity	1,854
Total	31,044
Disallowable expenses = 5/12 x 31,044	12,935

2. **Deductible revenue expenses incurred during basis period from 1 Jan 2012 to 31 Dec 2012**

Advertisement/ promotion	145
Audit fee	600
Printing & stationery	154
Rental	4,800
Repairs & maintenance	277
Secretarial fee	200
Staff salaries	7,542
Telephone	623
Travelling and transport	421
Water and electricity	885
Deductible revenue expenses	15,647

3. The unabsorbed loss is available for carry back to YA 2013 to offset interest income of $2,074, subject to the provisions of section 37E.

Example of Company with Accounts Prepared for a Period Exceeding 12 Months

Example 4

A company was incorporated in Singapore on 15 September 2010. The financial year end of the company is 31 December. The Company's first set of accounts is prepared for the period from 15 September 2010 to 31 December 2011. The Company earns its first dollar on 1 February 2012 (i.e. in YA 2013).

As the first set of accounts covered a period of more than 12 months, there are 2 relevant YAs as follows:

YA	Basis period
2011 (1^{st} YA)	15 Sep 2010 – 31 Dec 2010
2012 (2^{nd} YA)	1 Jan 2011 – 31 Dec 2011

Under the 2011 enhancement, revenue expenses incurred during the accounting year 1 January 2011 to 31 December 2011 (YA 2012) are allowed tax deduction in YA 2013. The company should:

(a) identify the expenses applicable to each of the 2 periods (i.e. 15 September 2010 to 31 December 2010 and 1 January 2011 to 31 December 2011); and

(b) submit a claim only for revenue expenses incurred for YA 2012 together with its tax computation for YA 2013.

If specific identification of expenses to the 2 periods is not possible, the CIT may accept time-apportionment of expenses.