

IRAS' AUDIT ON MOTOR VEHICLE RETAIL SECTOR

1. Overview of the Motor Vehicle Retail Sector

The motor vehicle retail sector comprises new and second-hand car dealers. The new car dealers may include authorised car distributors, retailers, agents, and parallel importers.

Motor car dealers may deploy the cars for various purposes. Table (1) below summarises the common categories of cars held by motor car dealers and their purposes:

Table (1): Common categories of cars

S/N	Categories	Purpose of car
1	Test-drive cars	For test-driving by potential customers and journalists
2	Display cars	For display in showrooms and marketing events
3	Events cars	For use in sponsorship of events and marketing events
4	Courtesy cars	For loan to customers while customers await the servicing or repair of their cars
5	Management cars	Provided to staff including directors for their use (business and/or private purpose)

2. Audit Review

As part of IRAS' regular compliance reviews on taxpayers' Income Tax returns, reviews on 18 motor vehicle retail companies were conducted. Beside desk review, pre-arranged on-site visits were also made by IRAS auditors to selected motor vehicle retail companies. Information and documentation on their business operations, record keeping practices and accounting systems were gathered during the visits for IRAS auditors to ascertain the accuracy of the taxpayers' Income Tax reporting. Our auditors discovered errors including wrongful claims of private expenses, general provision in inventory, and provisions for contingent expenses.

In total, the taxes and penalties recovered by IRAS amounted to \$1.4 million.

3. Audit Outcomes, Observations and Common Mistakes made by Taxpayers

From the audits conducted, the following are the common mistakes observed by IRAS:

a. Sale or purchase transactions with related car dealers not at market value

We observed that some car dealers set up different entities for different segments of their business. For example, an entity may be set up solely to buy and sell cars, while another entity

provides repair and maintenance services. Some cases also involve another entity providing loan financing to the customers. Our compliance reviews showed that some of these related party transactions had not been transacted at market value. This is inconsistent with the arm's length principle which requires transactions with related parties to be conducted at market prices. For more information on the arm's length principle and application, please refer to [Transfer Pricing](#).

b. Wrongful claims on general provision for inventory

Some companies have made claims on general provision for inventory. For income tax purposes, companies should only claim deduction for expenses where there is a definite legal liability to pay. General provision for expenses which are merely anticipatory and set aside to meet a contingent liability does not qualify for tax deduction.

c. Claiming of private expenses

Another common mistake made by car dealers is wrongful claims of private expenses incurred by the directors for themselves and/or their family members. These included prayer expenses, petrol costs in respect of the director's private car, and medical expenses incurred by director's family members.

d. Claiming of expenses without maintaining sufficient supporting documents

Very often, claims were made by companies without sufficient records and supporting invoices. During our reviews, we have observed cases where reimbursements for travelling and entertainments were made to directors without proper records and invoices to support the claim. As a result, we were unable to ascertain the existence and validity of the transactions.

Company should keep proper documentation and records to substantiate their purchases and expenses. They should also ensure that such claims are with economic substance and justified on a commercial basis. More information on good record keeping standards can be found in the IRAS e-Tax Guides¹:

- Record Keeping Guide for GST-registered Businesses; and
- Record Keeping Guide for Non GST-registered Businesses.

4. Framework on Tax Treatments relating to Motor Car Dealers

To close the gaps in the application of tax law by car dealers and to ensure consistency in tax treatment adopted by different car dealers, IRAS issued a clarification framework on "[Tax Treatments relating to Motor Car Dealers](#)" which was shared with members of the motor vehicle associations² on 3 Sep 2020. A summary of the tax treatments in the framework is provided below.

¹ Please refer to related content under [Record Keeping Requirements](#).

² Singapore Vehicle Traders Associations (SVTA), Automobile Importer and Exporter Association (AIEA), and Motor Traders Association of Singapore (MTA).

A. Inventory Tax Treatment

For motor cars that are inventories, the company can apply the inventory tax treatment. Under the inventory tax treatment, motor car expenses incurred are deductible. Profit or loss on disposal of the cars is taxable or deductible.

- Inventory tax treatment on new cars applies to:
 - a. Unregistered cars
 - b. Registered cars if the following conditions are met for each car:
 - i. Registration of the car is solely to facilitate the car to be used for test-driving by customers and/or journalists;
 - ii. Actual use of the car is for purposes of test-driving, display, and/or one-time participation in marketing event and there are documents and records to demonstrate the car is used for such purposes; and
 - iii. The car is held for two years or less from its registration date.

If any of the conditions in (i) to (iii) for a car is not met in the basis period of a YA, inventory tax treatment does not apply to the registered car in that YA. The expenses incurred on the car for that YA are not tax deductible. Any profit or loss on disposal of that car in that YA is not taxable or deductible.

- The inventory tax treatment also applies to second-hand cars acquired for resale. Second-hand cars are cars that are previously registered under the name of and driven by another owner. Expenses incurred on second-hand cars relating to test-driving or display are deductible. However, expenses relating to other uses (e.g. employee of company uses the car for his own private uses) are not tax deductible. Profit or loss on disposal of second-hand cars acquired for resale are taxable or deductible.

B. Business Use Tax Treatment

The business use tax treatment is applicable to registered cars deployed for business use purposes such as:

- Management cars provided to staff
- Courtesy cars for use by customers
- Cars held for more than two years from their registration dates

Under the business use tax treatment, motor car expenses incurred are not tax deductible. Profit or loss on disposal of the cars is not taxable or deductible. This tax treatment is no different from

the tax treatment for motor cars owned by businesses in other industries.

C. Effective YA

The tax treatments provided for in the framework are effective from YA 2021. However, IRAS is prepared to accept the claims and tax treatments adopted by car dealers in an earlier YA if car dealers have supporting documents to substantiate their claims.

D. Record Keeping

To facilitate the claiming of tax deductions, car dealers are strongly encouraged to use the record keeping [template for new cars](#) and [template for second-hand cars](#).

o New cars

The template for new cars is applicable if a registered car is used for purposes besides test-driving, display, and/or one-time participation in marketing event. It helps to keep track of usage and expenses incurred from the date of registration of each car for the purposes of ascertaining whether inventory tax treatment is applicable to that car in any given YA.

o Second-hand cars

The template for second-hand cars is applicable if a second-hand car acquired for resale will be used for purposes other than test-driving or display. It helps to keep track of usage and expenses incurred to ascertain the disallowable expenses to be added back in the tax computation in any given YA.

Please refer to Table (2) below for the circumstances under which car dealers are not required to use the templates:

Table (2): Circumstances under which car dealers are not required to use the template

New cars	Second-hand cars
which are - i) Unregistered cars. ii) Registered cars used/ to be used only for purposes of test-driving, display and/or one-time participation in marketing event. iii) Acquired for business use as courtesy cars and management cars.	which are - i) Acquired for resale to be used only for purposes of test-driving and/or display. ii) Acquired for business use as courtesy cars and management cars.

We encourage car dealers to use the template for proper record keeping but they are not precluded from adopting other ways of record keeping which are more expedient for them as long as there are proper internal controls and they are able to furnish the details in the format shown in the record keeping template upon request.

5. Voluntary Disclosures of Errors

IRAS will continue to conduct regular compliance reviews on various industries as part of our efforts to enhance voluntary compliance of our taxpayers.

Under Section 95 of the Income Tax Act 1947, any person who negligently or without reasonable excuse makes an incorrect Income Tax Return may be liable to a penalty as high as two times the amount of tax undercharged. Serious cases of omissions or errors may be subject to court prosecution.

Taxpayers are encouraged to voluntarily disclose errors made in their past Income Tax returns. Under the [IRAS Voluntary Disclosure Programme](#), IRAS will waive the penalty for voluntary disclosures of omissions or errors that meet the qualifying conditions and are made within the 'grace period' of 1 year from the statutory filing date of 30 November. For voluntary disclosures made after the 'grace period', IRAS will impose penalty at a reduced rate of 5% per annum.