

Tax Alert

SINGAPORE

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In this issue, KPMG Tax Services highlights the enhancements made to the Research and Development (R&D) incentive schemes, as detailed in the Inland Revenue Authority of Singapore (IRAS) circular which was revised on 12 December 2008. This circular follows the Singapore Budget 2008 announcement by the Minister for Finance on 15 February 2008. These new measures take effect from the Year of Assessment (YA) 2009.



New and Enhanced R&D Tax Incentives

The new and enhanced R&D tax incentives aim to encourage businesses to build up R&D capabilities in Singapore. The measures comprise liberalised R&D tax deductions, a new R&D Tax Allowance scheme, and a new R&D Incentive for Start-up Enterprises.

Some highlights of the new and enhanced tax incentives are:

- **The measures present immediate substantive income tax-saving opportunities** for businesses, as the measures take effect from YA2009.
- **The measures are not just targeted at high-end R&D work, but also for developmental work** and most other types of innovation-related activities. This supports the Government's objective to encourage enterprise innovation at big and small businesses.
- **There is no requirement to apply for the incentive.** Unlike many other types of incentives, these new incentives are claimed by submitting relevant documents together with the filing of the income tax return, and the claims would be allowed if the stated conditions are satisfied.
- **The R&D must benefit the applying company and this company should not merely be an R&D service provider.**

The salient features of the new R&D measures and administrative procedures are summarised in the following sections.

A. Liberalised R&D Tax Deductions

A tax deduction on expenditure incurred for R&D activities is available for R&D projects undertaken in-house or outsourced to an external R&D organisation.

Where it is outsourced to an R&D organisation outside Singapore, the deduction is available where the benefits from the R&D project accrue to the Singapore entity.

With effect from the YA2009, the following broad-based enhancements would apply:

- **Additional income tax deduction equal to 50 percent of qualifying R&D expenditure**, for a total tax deduction of 150 percent of such R&D expenses, for R&D undertaken within Singapore. This is for the basis periods for YA2009 to YA2013. R&D activities may be undertaken directly or outsourced to an R&D organisation that undertakes R&D activities in Singapore.
- **Where the R&D is outsourced to an external R&D organisation, the additional income tax deduction of 50 percent is claimed on the sum payable to the R&D organisation.** Where a breakdown of the external R&D organisation's expenditure is not available, the further deduction would be based on 30 percent of the sums payable to the R&D organisation
- **R&D activities that are not related to a company's existing trade or business** will also be eligible if the R&D is carried out in Singapore
- **Qualifying expenditure relating to the R&D activities** are staff costs, consumables, or other items as prescribed by the Minister for Finance

As an example, if a company incurs \$1m of qualifying R&D expenditure, the potential tax savings for YA2009 from the additional 50 percent deduction would be S\$90,000 ($\$1\text{m} \times 50\text{percent} \times 18\text{percent}$).

How to Claim the Liberalised R&D Tax Deductions

- **The incentives are given on due claim** (no pre-approval application is required), subject to agreement with the IRAS.
- **The company must file the following documents** with the IRAS to be eligible for the liberalised R&D tax deductions.
 - R&D Claim Form together with the company's Form C
 - A breakdown of the items that qualify as R&D expenditure together with the company's tax computation
 - A detailed project description of the R&D project if the R&D expenditure is \$150,000 or more (net of Government grants or subsidies)
- **For R&D expenditure below S\$150,000**, while there is no requirement to submit a detailed project description of the R&D project, adequate supporting documentation of the R&D project must be maintained and provided to IRAS upon request.

B. R&D Tax Allowance (RDA) Scheme

The RDA has been introduced to encourage profitable businesses, particularly Small and Medium-sized Enterprises (SMEs), to engage in qualifying R&D activities in Singapore.

- **The tax concession provides for an RDA of 50 percent** on the first S\$300,000 of chargeable income, i.e. a maximum of S\$150,000 can be credited per YA (a new module in myTaxportal will be set up for this purpose)
- **Companies may accumulate up to \$450,000 of RDA**, and the excess will be forfeited. The RDA may be used to offset taxable income in subsequent YAs up to YA2016, if companies incur incremental R&D
- **YA2009 would be the first YA** for which an RDA can be accumulated, and YA2010 would be the first YA for which the RDA can be utilised

How to Claim the R&D Tax Allowance

Maintenance of R&D Account

- **Provide a detailed project description of the R&D project to the IRAS** together with the company's income tax returns if the R&D expenditure is \$150,000 or more (net of Government grants or subsidies). Please note that adequate supporting documentation of the R&D projects must be maintained where the R&D project expenditure is less than \$150,000 and provided to IRAS upon request.
- **Companies must maintain records of the RDA claimable** and provide supporting documentation when utilising RDA
- **Companies will be able to view their R&D account balances** via myTaxPortal. The amount of RDA credited into the R&D account will be based on the finalised or provisionally finalised chargeable income for YA 2009 to YA 2013

Utilisation of Amounts in R&D Account

- **The amounts in the R&D account can be utilised from YA2010.** All amounts must be utilised by YA2016.
- **The R&D Claim Form together with its annual income tax return for the YA** must be submitted. The following must also be included in the tax computation submitted:
 - i. A breakdown of the R&D expenditure incurred during the basis period
 - ii. A computation of the RDA utilized against its assessable income.
- **To utilise the RDA**, there must be incremental R&D spending. The new R&D Allowance scheme would equate to additional tax deductions on incremental R&D

C. R&D Incentive for Start-Up Enterprise (RISE) Scheme

RISE provides cash flow assistance to new start-up companies that may not be deriving taxable profits and therefore cannot avail themselves of the RDA Scheme.

- **The RISE Scheme is available to start-ups** in their first three YAs of incorporation
- **Loss-making start-ups** that expend at least S\$150,000 a year on qualifying R&D activities in Singapore may convert their tax adjusted tax losses of up to S\$225,000 (i.e. based on 150 percent of S\$150,000) into a cash grant at the rate of 9 percent
- **Maximum cash grant** a start-up may obtain under the scheme is S\$20,250 (i.e. S\$150,000 x 150 percent X 9 percent)

How to Claim under RISE

The election to convert current year unutilised tax adjusted losses into R&D cash grant is final and irrevocable. Partial conversion of such losses is not allowed.

The following together with the company's annual income tax return for the YA should be submitted:

- R&D Claim Form
- Tax computation showing:
 - i. A breakdown of the R&D expenditure incurred during the basis period
 - ii. A computation of the R&D grant which it wishes to claim
- Detailed project description of the R&D project undertaken
- Audited accounts for the basis period relating to the relevant YA

What projects will qualify for the R&D tax incentives

To qualify for the tax incentives, the activities would have to fall within the definition of R&D under Section 2 of the Income Tax Act, which is briefly stated as follows:

Any systematic, investigative and experimental study that involves novelty or technical risk carried out in the field of science or technology with the object of acquiring new knowledge or using the results of the study for the production or improvement of materials, devices, products, produce or processes, but does not include —

- i. quality control or routine testing of materials, devices or products;
- ii. research in the social sciences or the humanities;
- iii. routine data collection;
- iv. efficiency surveys or management studies;
- v. market research or sales promotion;
- vi. routine modifications or changes to materials, devices, products, processes or production methods;
- vii. cosmetic modifications or stylistic changes to materials, devices, products, processes or production methods; or
- viii. development of a computer software that is not intended to be sold, rented, leased, licensed or hired to 2 or more persons who are not related parties to each other, and to the person who develops the software or on whose behalf the development of the software is undertaken

As illustrated in the guidelines of the IRAS circular, the targeted activities are not limited to high-end R&D, but would also include developmental work and most other types of innovative activities.

Some less obvious areas which could be regarded as R&D for the purpose of the concessions include:

- Improvements to manufacturing processes
- Adapting technologies for local or Asian customers
- Providing innovative solutions to customers
- Combining several existing technologies to achieve a particular outcome
- Adapting technologies used in one industry for use in another industry
- Materials substitution (e.g. using more environmentally-friendly materials in products)

What You Have To Do

The new and enhanced R&D measures present an immediate opportunity for you to realize potentially substantial tax savings. **As the new requirements take effect from YA2009, there is an immediate need for you to review your 2008 R&D expenditure so that the claims for R&D are filed in a timely manner.**

It is therefore important to review the business expenditure incurred in 2008 to (a) ensure qualifying R&D expenditure included therein is duly identified, and (b) to prepare relevant documentation to support the R&D claims.

The **typical steps** involved in reviewing your activities would include:

- Identify parts of the organisation where there may be qualifying R&D projects
- Identify qualifying R&D projects (in accordance with the R&D definition)
- Identify qualifying expenditure relating to each R&D project
- Prepare supporting documentation to support claims

Please note that failure to submit the requisite information / documents to support the R&D claims would lead to a disqualification of the company's claim.

Contact us

How KPMG Tax Services can help

We welcome the opportunity to discuss the relevance of the new and enhanced R&D tax incentives to your business.

In particular, we can help you to ascertain whether you are claiming your entitlement to the R&D incentives; advise on the criteria for qualifying R&D; identify potential qualifying R&D expenditure; identify and extract the relevant costs for your claim; produce relevant reports to support your claim to the R&D incentives; liaise with the IRAS regarding queries on the claim; and establish procedures for an ongoing review of your R&D expenditure.

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KPMG's Tax Alert highlights the latest tax developments, impending change to laws or regulations, current practices and potential problem areas that may have an impact on your business. As certain issues discussed herein are time sensitive, it is advisable to make plans accordingly.

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