

ANNEX B-2: Research and Development (R&D) Tax Measures

1) Liberalisation of R&D Tax Deduction

a) Enhanced deduction for R&D expenses

Existing Tax Treatment

- Currently, taxpayers carrying on a manufacturing trade or business or a trade or business for the provision of any services enjoy tax deduction, under section 14D of the Income Tax Act (ITA), for expenses they incur on R&D⁴. The deduction is available for expenses on R&D, irrespective of whether the R&D is done in-house by the taxpayer itself or by a R&D organisation on behalf of the taxpayer, whether done in Singapore or abroad⁵.
- The tax deduction under section 14D is equal to 100% of the amount of qualifying R&D expenditure.

New Tax Treatment

- With effect from YA2009, taxpayers that incur expenses in respect of R&D activities carried out in Singapore will qualify for a tax deduction of 150% of the amount of R&D expenses incurred. The 150% tax deduction will be granted to R&D which the company itself does in Singapore, or outsources to an R&D organisation in Singapore. This higher tax deduction will be available for the years of assessment from YA2009 to YA2013.
- R&D expenditure incurred in respect of R&D activities that the taxpayer has outsourced to an R&D organisation outside of Singapore will continue to qualify for deduction under section 14D. The tax deduction will, however, remain unchanged at 100% of the qualifying R&D expenditure incurred.

b) Removal of “related to that trade or business” requirement under Section 14D and Section 14E of the Income Tax Act (ITA)

Existing Tax Treatment

- Besides the 100% tax deduction available under section 14D of the ITA, taxpayers carrying on a manufacturing trade or business or a trade or business for the provision of any services can also be granted a further tax deduction under section 14E on approval

⁴ Section 2 of the Income Tax Act defines R&D as any systematic or intensive study carried out in the field of science or technology with the object of using the results of the study for the production or improvement of materials, devices, products, produce, or processes, but does not include —

(a) quality control or routine testing of materials, devices or products;

(b) research in the social sciences or the humanities;

(c) routine data collection;

(d) efficiency surveys or management studies; or

(e) market research or sales promotion.

⁵ Where a taxpayer pays an R&D organisation overseas to do R&D on its behalf, the taxpayer is granted the tax deduction under section 14D of the ITA only if the taxpayer undertakes that the benefit of the R&D to be done accrues to itself.

basis for R&D done in Singapore either by the taxpayer itself or by a R&D organisation in Singapore on its behalf. Tax deductions under section 14D and section 14E of the ITA are granted on the condition that the R&D done is *related to the trade or business of the taxpayer*.

New Tax Treatment

- With effect from YA2009, taxpayers carrying on a manufacturing trade or business or a trade or business for the provision of services will be allowed to claim deductions for R&D expenses that are not incurred in respect of their existing trade or business. These claims will, however, be subject to the condition that the R&D expenses are incurred in respect of R&D activities done in Singapore either by the taxpayer itself or by a R&D organisation in Singapore on its behalf. The change applies to both section 14D and section 14E deductions, and will be effective for years of assessment from YA2009 to YA2013.
- Expenses incurred on R&D that is outsourced to an R&D organisation outside Singapore will continue to be granted the 100% deduction under section 14D, only if the R&D done is related to the trade or business of the taxpayer.

2) R&D Tax Allowance

- The R&D tax allowance is a new incentive available to companies in Singapore that have chargeable income. Under the incentive, companies with chargeable income will be granted an R&D allowance for each year of assessment falling within the period from YA2009 to YA2013, at a prescribed rate based on the chargeable income for the year of assessment. The R&D allowance granted can be used to offset chargeable income for the next three years of assessment provided the qualifying conditions are met.
- The prescribed rate at which R&D tax allowance is granted shall be 50% of the first \$300,000 of a company's chargeable income⁶ or such lower amount where the company's chargeable income⁶ is less than \$300,000, for each year of assessment from YA2009 to YA2013. The maximum R&D tax allowance granted for each qualifying year of assessment is therefore \$150,000 (i.e. 50% of \$300,000).
- The R&D tax allowance can be utilised to offset chargeable income for the next three years of assessment (following the year of assessment that it is granted), if the company incurs, in the basis periods of those three years of assessment of utilisation, qualifying R&D expenditure in excess of a base amount (i.e. incremental qualifying R&D expenditure). Any R&D tax allowance that remains unutilised as at the end of the three years of assessment will be disregarded.
- Qualifying R&D expenditure refers to R&D expenditure that:
 - qualifies for deduction under section 14D of the Income Tax Act; and
 - the company incurs in respect of R&D activities undertaken directly (i.e. in-house) by the company in Singapore

⁶ Chargeable income after R&D tax allowance utilised (if any), start-up exemption (where applicable) and partial tax exemption (PTE).

For the purpose of computing the amount of qualifying R&D expenditure, government grants (if any) and R&D expenses which the company incurs for all outsourced R&D (whether outsourced to an R&D organisation in Singapore or abroad) will not be considered as part of the qualifying R&D expenditure.

- The base amount of qualifying R&D expenditure is set at the level of the company's qualifying R&D expenditure incurred for the base year. The fixed base year for existing companies is the basis period for Year of Assessment 2008.
- R&D tax allowances cannot be transferred among related companies under group relief.
- Example: Mechanics of R&D Tax Allowance Scheme

	YA2009	YA2010	YA2011	YA2012
TAX COMPUTATION				
Chargeable income (before Partial Tax Exemption (PTE))	500,000	300,000	250,000	400,000
Less: R&D Tax Allowance utilised (A) = lower of (B-C) or D	0	100,000	98,750	36,563
Adjusted chargeable income before PTE	500,000	200,000	151,250	363,437
Adjusted chargeable income after PTE	347,500	97,500	73,125	210,937
R&D Expenses (B)	100,000	200,000	300,000	400,000
Base Year R&D (C)	100,000	100,000	100,000	100,000
Incremental R&D Exp (B-C)	NA	100,000	200,000	300,000
R&D Tax Allowance Account				
R&D Tax Allowance b/f:				
YA2009	0	150,000	50,000	0
YA2010	0	0	48,750	0
YA2011	0	0	0	36,563
Total R/D Tax Allowance b/f (D)		150,000	98,750	36,563
Less: R&D Tax Allowance utilised (A)	0	-100,000	-98,750	-36,563
Add: Current year R&D Tax Allowance (E) = 50% * adjusted chargeable income after PTE	150,000	48,750	36,563	105,469
R&D Tax Allowance c/f = D-A+E	150,000	98,750	36,563	105,469

Note:

A = Utilisation of R&D tax allowance is capped at the lower of incremental R&D expenses or the R&D tax allowance brought forward (i.e. excluding R&D tax allowance earned in current YA).

B = This refers to the actual amount of R&D expenses incurred, and not the quantum of the tax deduction.

C = R&D expenses incurred in basis period for YA2008 i.e. financial year 2007.

D = Unutilised R&D Tax Allowance brought forward from up to the preceding 3 YAs.

E = Capped at 50% of the first \$300,000 chargeable income (after R&D tax allowance utilised (if any), start-up exemption (where applicable) and partial tax exemption (PTE)), or such lower amount where the chargeable income (after R&D tax allowance utilised (if any), start-up exemption (where applicable) and PTE) is less than \$300,000

3) **R&D Incentive for Start-up Enterprises (RISE)**

- This is a new incentive which provides government grants to R&D-intensive start-ups that do not generate taxable profits in their first three years of assessment, subject to qualifying conditions.
- R&D-intensive start-ups invest a significant amount of R&D into developing their products. It often takes time for these products to generate profits, so the start-ups may not have chargeable income in the initial years. For start-ups who do not yet have chargeable income, they are unable to benefit from R&D tax incentives such as the R&D tax allowance. For tax purposes, these start-up companies are allowed to carry forward their losses currently. Nonetheless, this carry-forward of losses may not be of immediate assistance to ease the cashflow challenges these R&D-intensive start-ups may face in their initial years.
- To make Singapore more attractive for R&D-intensive start-ups and to encourage start-up companies to invest more in building up their in-house R&D capabilities in Singapore, the *R&D Incentive for Start-up Enterprises (RISE)* will be introduced.
- Under RISE, a qualifying start-up company is allowed to convert up to \$225,000⁷ of tax losses into cash computed at a prescribed rate, if it spends at least \$150,000 expenses on ongoing R&D done in Singapore in the basis period for the year of assessment of claim.
- The start-up can therefore choose either to convert its losses in exchange for cash under the RISE scheme, or carry forward the losses for offset against its subsequent chargeable income in future years of assessment. If the start-up company chooses to convert its losses under RISE into cash instead of carrying forward the losses, the losses of the start-up company to be carried forward will be correspondingly reduced by the amount of the converted losses.
- Qualifying start-up companies can claim for cash grants under RISE for the years of assessment from YA2009 to YA2013.
- To qualify for RISE, the start-up company needs to meet all of the following conditions:
 - a) It satisfies the criteria for the general start-up corporate tax exemption, that is, it is a company that:
 - (i) is incorporated in Singapore;
 - (ii) is tax resident of Singapore;
 - (iii) has total share capital which is beneficially held, directly or indirectly, by no more than 20 persons –
 - (1) all of whom are individuals, or

⁷ This is 150% of \$150,000 of R&D expenditure, in view of the concession to allow deduction of 150% of expenses incurred on R&D carried out in Singapore.

(2) of which at least one is an individual shareholder holding at least 10% of total number of issued ordinary shares throughout the basis period relating to the years of assessment of claim.

- b) Its first three years of assessment fall within the period of YA2009 to YA2013;
- c) It does not have taxable profits or chargeable income in all preceding years prior to the year of assessment of claim;
- d) It incurs at least \$150,000 qualifying expenditure on R&D in the basis period for the year of assessment of claim.

- **Qualifying Expenditure on R&D means:**

- (a) Expenditure which the company incurs on R&D that the company undertakes directly (in-house) in Singapore. Expenditure on R&D that is funded by government grants (if any) or expenditure that the company incurs for R&D outsourced to a R&D organisation (whether in Singapore or abroad) will not be considered as part of qualifying expenditure on R&D (i.e. will be netted off from the total R&D expenditure incurred); and
- (b) The R&D concerned must still be ongoing at the time of claim

- **The amount of cash grant that a qualifying start-up company can claim for a year of assessment (during Years of Assessment 2009 to 2013) will be computed based on the prescribed rate as follows:**

- **Amount of tax losses that can be converted is the lower of -**
 - (a) the actual losses for the year of assessment of claim; or
 - (b) the tax deduction for up to \$150,000 qualifying R&D expenditure incurred in the basis period for the year of assessment of claim.Hence, the maximum amount of losses that can be converted is \$225,000 for each year of assessment of claim.
- **Amount of cash grant equals 9% of the amount of losses to be converted. The maximum amount of cash grant is thus \$20,250 for each year of assessment of claim.**

The 9% rate is equivalent to the effective marginal tax rate for companies with chargeable income between \$10,000 - \$300,000 (taking into account the prevailing partial tax exemption of 50% for this chargeable income range).

IRAS will release further implementation details (including anti-avoidance measures) for the above R&D tax changes by September 2008.

WORKED EXAMPLES OF THE R&D TAX ALLOWANCE AND 150% TAX DEDUCTION

Example 1

Company has accounting profits of \$300,000 in Year 1. It did not do any R&D.

In Year 2, it incurred incremental R&D spending of \$150,000, and its accounting profit is \$150,000. The R&D expenditure relates to R&D that the company itself carried out in Singapore.

Tax Computation:

	Year 1	Year 2	
Net profit per accounts (A)	300,000	150,000	
Add: R&D expenditure	0	150,000	
	300,000	300,000	
Less: R&D deductions	0	(225,000)	Note 1
Less: R&D Tax Allowance utilised		(73,750)	
Chargeable Income	300,000	1,250	
Less: Partial Tax Exemption	(152,500)	(938)	Note 2
Adjusted chargeable income	147,500	312	
Tax payable @ 18% (B)	26,550	56	
Effective tax rate (B)/(A)	8.85%	0.04%	
Current YA's R&D Tax Allowance c/f	73,750	156	Note 3
Tax savings from R&D incentives		26,494	Note 4

Note 1: 150% of expenditure incurred for R&D done in Singapore.

Note 2: 75 % of the first \$10,000 and 50% of up to the next \$290,000 of the company's chargeable income is tax exempt.

Note 3: Current year of assessment's R&D Tax Allowance is computed at 50% of the chargeable income after partial tax exemption (i.e. adjusted chargeable income in the table above), up to a maximum of \$150,000 of R&D Tax Allowance per year of assessment

Note 4: The tax savings is the difference between the taxes it would have paid without the R&D tax deductions and R&D Tax Allowance (\$26,550) and the tax payable for Year 2 (\$56).

Example 2

Company has accounting profits of \$1,000,000 in Year 1. It did not do any R&D.

In Year 2, it incurred incremental R&D spending of \$150,000, and its accounting profit is \$850,000. The R&D expenditure relates to R&D that the company carried out in Singapore.

Tax Computation:

	Year 1	Year 2	
Net profit per accounts (A)	1,000,000	850,000	
Add: R&D expenditure	0	150,000	
	<u>1,000,000</u>	<u>1,000,000</u>	
Less: R&D deductions	0	(225,000)	Note 1
Less: R&D Tax Allowance		<u>(150,000)</u>	
Chargeable Income	1,000,000	625,000	
Less: Partial Tax Exemption	<u>(152,500)</u>	<u>(152,500)</u>	Note 2
Adjusted chargeable income	<u>847,500</u>	<u>472,500</u>	
Tax payable @ 18% (B)	152,550	85,050	
Effective tax rate (B)/(A)	<u>15.26%</u>	<u>10.01%</u>	
Current YA's R&D Tax Allowance c/f	150,000	150,000	Note 3
Value of savings from R&D incentives		<u>67,500</u>	Note 4

Note 1: 150% of expenditure incurred for R&D done in Singapore.

Note 2: 75 % of the first \$10,000 and 50% of up to the next \$290,000 of the company's chargeable income is tax exempt.

Note 3: Current year of assessment's R&D Tax Allowance is computed at 50% of the chargeable income after partial tax exemption (i.e. adjusted chargeable income in the table above), up to a maximum of \$150,000 of R&D Tax Allowance per year of assessment

Note 4: The tax savings is the difference between the taxes it would have paid without the R&D tax deductions and R&D Tax Allowance (\$152,550) and the tax payable for Year 2 (\$85,050).