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Singapore Publishes Tax Guide on Enterprise Innovation Scheme

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On 30 June 2023, the Inland Revenue Authority of Singapore (IRAS) published an e-Tax Guide on the Enterprise Innovation Scheme (EIS).

Background

Introduced by the Finance Minister in the 2023 Budget, the EIS allows businesses engaging in research and development (R&D), innovation and capability development to:

- claim enhanced/new tax deductions and/or allowances (Collectively referred to as “enhanced deductions”) on qualifying expenditure incurred, or
- convert up to $100,000 of the total qualifying expenditure incurred for each Year of Assessment (YA) into cash at a conversion rate of 20%, in lieu of tax deductions/allowances.

The EIS is available from YA 2024 to YA 2028.

Qualifying Activities and Expenditure Caps

Enhanced deductions are available for qualifying expenditure incurred on the following five (5) activities:

Qualifying EIS Activities	Enhanced EIS Deductions/ Allowances	Existing Deductions/Allowances under the Income Tax Act 1947 (ITA)
Qualifying R&D activities undertaken in Singapore	400% for the first $400,000 of staff costs and consumables incurred on qualifying R&D projects conducted in Singapore	250% tax deduction for staff costs and consumables incurred on qualifying R&D projects conducted in Singapore (sections 14C and 14D)
Registration of intellectual property (IPs)	400% for the first $400,000 of qualifying IP registration costs incurred	200% tax deduction for the first $100,000 (and 100% for amounts exceeding $100,000) of qualifying IP registration costs (section 14A)
Acquisition and licensing of IP rights (IPRs)	400% for the first $400,000 (combined cap) of qualifying expenditure incurred on the acquisition and licensing of IPRs	• 100% writing-down allowance (WDA) over a period of 5, 10 or 15 years on acquisition cost of qualifying IPRs (section 19B), or • 200% tax deduction for the first $100,000 (and 100% for amounts exceeding $100,000) of qualifying IPRs licensing expenditure (sections 14 or 14C, and 14U)

Qualifying EIS Activities	Enhanced EIS Deductions/ Allowances	Existing Deductions/Allowances under the Income Tax Act 1947 (ITA)
Training	400% for the first $400,000 of qualifying training expenditure incurred on qualifying courses	100% tax deduction (section 14)
Innovation projects carried out with polytechnics, the Institute of Technical Education (ITE) or other qualified partners	400% tax deduction for up to $50,000 of qualifying innovation expenditure incurred	Not allowable unless the projects meet the definition of R&D under section 2 of the ITA

Qualifying R&D Activities

Qualifying R&D expenditure refers to the following expenditure that is attributable to qualifying R&D activities undertaken in Singapore:

- staff costs (excluding directors' fees)
- consumables, or
- such other item of expenditure which the Minister for Finance may prescribe by regulations.

A business that contracts with a R&D organisation to undertake qualifying R&D activities in Singapore on its behalf may also claim enhanced deduction on the fees payable to the R&D organisation to the extent the fees relate to qualifying R&D expenditure. For this purpose, up to 60% of all fees payable to the R&D organisation may be claimed as qualifying R&D expenditure. However, if the actual qualifying expenditure incurred exceeds 60% and can be substantiated, a higher percentage can be claimed.

Similarly, 60% of the payments made under a R&D cost-sharing agreement is deemed as qualifying R&D expenditure for the purpose of claiming the enhanced deduction.

In line with existing rules for R&D claims, the R&D claims under the EIS need not be related to the business' existing trade or business since the qualifying R&D activity has to be undertaken in Singapore.

Registration of IPs

Qualifying IP registration costs refer to expenditure incurred by any person carrying on a trade or business in registering patents, trade marks, designs and plant varieties for the purposes of that trade or business. Registration costs that qualify for tax deduction are official fees and professional fees. The legal and economic ownership of the qualifying IPRs must belong to the business entity in Singapore.

The enhanced deduction is granted regardless of the outcome of the application of the registration of qualifying IPR. This means that even if an application for registration is rejected, the related registration costs incurred are still eligible for the enhanced deduction.

Businesses must own the related IPRs registered (or, where applicable, ensure the application for registration or grant of the related IPR is not assigned to another person) for a minimum period of one year failing which, claw-back provisions apply.

Acquisition and Licensing of Qualifying IPRs

Under this qualifying activity of the EIS, businesses can either claim:

- enhanced WDA on qualifying IPRs acquisition expenditure incurred over a period of 5, 10 or 15 years, and/or
- enhanced deduction on qualifying IPRs licensing expenditure incurred.

The list of qualifying IPRs is defined under Section 19B(11) of the ITA.

The enhanced WDA is applicable only where the qualifying IPRs are legally and economically owned by a company or partnership in Singapore.

To claim the enhanced WDA and/or deduction, the business must carry on a trade or business and:

- if the business is not part of a group: derive less than $500 million in revenue in the basis period for the relevant YA
- if the business is part of a group: the group derives less than $500 million in revenue in the basis period for the relevant YA.

The amount of qualifying IPR acquisition costs and qualifying IPR licensing expenditure eligible for the enhanced WDA and deduction is subject to a combined cap of $400,000 for each YA.

Enhanced deductions will not be given under the EIS if the qualifying IPR is licensed from a licensor which is a related party:

- who carries on a trade or business in Singapore, and
- the qualifying IPR is acquired or developed (in whole or in part) by the related party.

Subject to the prevailing rules, the related party licensor will be able to claim:

- enhanced WDA on qualifying costs incurred on the acquisition of qualifying IPRs
- enhanced deductions on qualifying R&D expenditure or qualifying IP registration costs incurred on the development and/or registration of IPs, or
- enhanced deduction on licensing expenditure on qualifying IPRs licensed from a third party.

If a business had been granted a WDA under section 19B of the ITA on a qualifying IPR previously, it cannot claim any enhanced deduction under the EIS for expenditure incurred on the licensing of the same IPR.

The qualifying companies or partnerships must own the qualifying IPRs for a minimum period of one year failing which, claw-back provisions will apply.

Qualifying Training Expenditure

Businesses may claim enhanced deduction on qualifying training expenditure incurred on courses that are eligible for SkillsFuture Singapore (SSG) funding and aligned with the Skills Framework. Qualifying training expenditure refers to course fees, assessment fees and certification fees paid by the employer to training providers which are registered with the SSG.

Businesses may also claim EIS benefits on qualifying training expenditure incurred on individuals deployed under centralised hiring arrangements or secondment arrangements, subject to conditions.

Innovation Projects carried out with Polytechnics, ITE or other Qualified Partners (collectively referred to as "partner institutions")

To qualify for this tax deduction, the business must collaborate directly with the partner institutions on the qualifying innovation project and must be the beneficiary of the project.

Qualifying innovation projects with partner institutions refer to projects that predominantly involve one or more of the following innovation activities:

- research and experimental development activities
- engineering, design, and other creative work activities
- IP-related activities, and
- software development and database activities.

The relevant partner institutions will validate the project as a qualifying innovation project and issue the innovation project invoice. Expenditure incurred outside of the collaboration with the partner institution will not qualify for this tax deduction.

Businesses will not be allowed to claim tax deduction under this qualifying activity if they have already claimed tax deductions or allowances on the same amount of qualifying innovation expenditure under other sections of the ITA.

Where an innovation project that is certified by the partner institution as a qualifying innovation project also meets the definition of R&D under section 2 of the ITA and the business chooses to claim tax deduction under this qualifying activity, any qualifying innovation expenditure incurred in excess of the $50,000 cap will not be eligible for R&D tax deduction under sections 14C and/or 14D of the ITA.

Deduction Rules

The qualifying expenditure cap for each qualifying activity is applied on a per YA basis and cannot be combined across YAs. The deductions/allowances granted under the EIS are in addition to the deductions/allowances allowable under prevailing income tax rules.

Where the qualifying expenditure is subsidised by a grant or subsidy from the Government, only the amount of expenditure that is net of the grant or subsidy is eligible for an enhanced deduction under the EIS.

Enhanced deductions that cannot be fully offset against the income of a business are treated as unutilised trade losses or allowances to be carried forward, transferred to a group company or carried back to be set off against the business' taxable income in the immediate preceding YA.

Cash Payout

In lieu of tax deductions/allowances, eligible businesses may opt to convert up to $100,000 of the total qualifying expenditure across all the qualifying activities for each YA into cash at a conversion rate of 20%. The cash payout is capped at $20,000 per YA. Each cash payout application is subject to a minimum expenditure of $400. The cash payout is not taxable. The cash conversion cap of $100,000 cannot be combined across YAs.

An eligible business refers to any company, registered business trust, partnership or sole-proprietorship that carries on business in Singapore and has at least three (3) full-time local employees (Singapore citizens or permanent residents with Central Provident Fund (CPF) contributions) earning a gross monthly salary of at least $1,400, in employment for six (6) months or more in the relevant YA.

Once an amount of qualifying expenditure is converted into cash, the same amount is no longer available for tax deduction/allowance.

Similar to the rules for enhanced deductions, the amount of qualifying expenditure that is eligible for cash payout is net of grant or subsidy from the Government.

To receive the cash payout, the eligible business must be carrying on a trade or business and not have ceased business at the time of disbursement of the cash payout.

Partial cash conversion is allowed for qualifying R&D undertaken in Singapore, licensing of IPRs, training and qualifying innovation projects. However, it is not allowed for registration of IPs and acquisition of IPRs. This means that the option to convert qualifying IP registration costs into cash payout is on a per IP registration or IPR basis. Any amount in excess of the expenditure cap for cash payout is forfeited and deduction or WDA cannot be claimed.

Our Observations

The qualifying activities, enhanced deduction/allowance limits and cash payout option under the EIS are largely similar to a previous scheme (Productivity and Innovation Credit (PIC) scheme) that was introduced in the 2010 Budget. The PIC was a broad-based tax incentive available to all businesses from YA 2011 to YA 2018. Unlike the EIS, the PIC did not cover innovation projects; instead, it provided enhanced deductions/allowances for two (2) additional activities: investments in design and investments in automation.

As can be inferred from the naming of the EIS, the Government seems to be shifting its focus away from productivity to innovation. It should also be noted that the transformation of enterprises sometimes starts with routine process improvements that may not be seen as innovation. Nevertheless, maintaining the EIS as a broad-based scheme allows smaller businesses to avail of the benefits.

Final Thoughts

Businesses planning to make substantial investments to transform, innovate and upgrade their capabilities through R&D, IP-related activities and innovation projects can benefit from the EIS. A business looking to claim EIS benefits should study the qualifying conditions, rules and examples detailed in the IRAS e-Tax Guide to avoid erroneous claims, penalties and claw backs. Care should also be taken to ensure that relevant records are maintained, any option for cash payout is exercised on a timely basis, and the IRAS is notified promptly of any cessation or disposal of IPRs.

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