THE PITFALLS OF PIC

SMEs should make full use of the Productivity and Innovation Credit scheme, but care must be taken to ensure that any expenditure is legitimate

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THE Productivity and Innovation Credit (PIC) scheme was introduced in the 2010 Budget to encourage businesses to spend on activities which would boost their productivity. Small and medium-sized enterprises (SMEs) have and will continue to benefit hugely from the scheme, which has paid out S$1.5 billion in cash and tax savings as at February 2014.

Under the PIC Scheme, businesses which invest on specified activities will receive enhanced deductions and/or allowances amounting to 400 per cent per dollar of qualifying expenditure up to a cap. The combined cap for each activity is (i) S$1,200,000 over three years of assessment (YA) 2013 to YA 2015; and (ii) S$1,200,000 over three years of assessment YA 2016 to YA 2018. The six activities currently covered under the PIC Scheme are:

- *Acquisition or leasing of PIC information technology (IT) and automation equipment;*
- *Acquisition or licensing of intellectual property rights (IPRs);*
- *Registration of certain IPRs;*
- *Research and development;*
- *Training provided to employees so as to upgrade skills and capabilities; and*
- *Approved industrial or product design projects conducted primarily in Singapore.*

TAX SAVINGS AND/OR CASH PAYOUTS

A business which spends S$100,000 on a qualifying activity would be able to receive enhanced deductions and/or allowances amounting to S$400,000. As Singapore's corporate tax rate is 17 per cent, this could translate into tax savings of up to S$68,000.

Alternatively, in lieu of a deduction, businesses may opt to convert qualifying expenditure of up to S$100,000 for each YA into cash. The conversion rate is 60 per cent for YA 2013 to YA 2018. In addition, the cash payout application is irrevocable and once the qualifying expenditure is converted into cash, the same amount would be unavailable for further tax deduction or allowance. The cash payout is exempt from tax in Singapore. This may be the preferred option for SMEs that require more liquidity for their operations expenses.

NEW IMPROVED FEATURES

In Budget 2013, an additional cash bonus (known as PIC Bonus) was announced as part of a three-year transition support package. For YA 2013 to YA 2015, businesses that invest a minimum of S$5,000 per YA in qualifying PIC activities will receive a dollar-for-dollar matching cash bonus (PIC Bonus) of up to S$15,000, subject to certain conditions. The PIC Bonus will be paid over and above the existing PIC benefits.

This means that for an expenditure of S$10,000 on a qualifying activity (which does not exceed the combined cap for that activity), a business could receive: (i) a tax deduction of S$40,000 and a PIC Bonus of S$10,000 in cash (up to S$15,000 a year); or (ii) a cash payout of S$6,000 and a PIC Bonus of S$10,000 in cash (up to S$15,000 a year).

Furthermore, in Budget 2014, a PIC+ scheme was introduced to provide support to SMEs that are making more substantial investments to transform their businesses. For qualifying SMEs, the combined expenditure cap for each activity is increased to (i) S$1,400,000 over YA 2013 to YA 2015 (with a limit of $800,000 over YA 2013 and YA 2014) and (ii) S$1,800,000 over YA 2016 to YA 2018. SMEs should capitalise on these substantial tax incentives to invest in the six activities, with the aim of increasing their productivity to offset against the labour crunch.

AVOID ABUSING THE SCHEME

With the huge incentives given by the government, there will undoubtedly be businesses that attempt to abuse this scheme. In 2014, it was reported that since the PIC scheme was introduced in 2010, the Inland Revenue Authority of Singapore (IRAS) has probed 158 cases. It has also set up a nine-man task force to focus on investigating PIC abuse. In its last five financial years, IRAS has investigated 691 cases involving all types of tax fraud and recovered about S$248 million in taxes and penalties. Common examples of abusive schemes are as follows:

- *Claiming PIC using false records or documents when no such expenditure was incurred or where the actual amount incurred was lower*
- *Creating a shell company to make PIC claims on purchase of equipment from a related company when no such purchase was made and where the equipment continued to be owned and used by the related company*
- *Claiming PIC based on collusion with a third party to purchase automation equipment, when the selling party is not the legal owner of the equipment and was merely renting or leasing it*
- *Using phantom employees to meet the PIC qualifying condition of having made CPF contributions for three or more local employees*
- *Engaging in arrangements that seek to artificially inflate PIC claims such as purchase/lease arrangements bundled with non-qualifying costs (for example, offering a high cash back for trade-in of an old asset)*
- *Inflating the staff cost allocated to software development*
- *Inflating the cost of goods or services to an amount which exceeds the open market value of those goods or services.*

Businesses that list relatives and friends as staff when they actually do not work for the company would be brought to task. Similarly, businesses that send their employees for a training course for an inflated course fee (which includes not just the training fees but also costs for a "door gift" given to the employees) will also be penalised.

The repercussions for providing false information to IRAS and/or making a fraudulent claim are severe, and perpetrators could be jailed. For multiple offences, there may be mandatory imprisonment of not less than six months.

For example, in September 2013, a director of an IT company was sentenced to eight weeks' imprisonment for willfully assisting the company to claim a PIC cash payout of S$58,143.60 which the company was not entitled to. In February 2014, another director of a company that manufactured machine tools accessories was fined and sentenced to five weeks' jail for the same offence.

Promoters of such schemes could be similarly charged and convicted for assisting a business to obtain a cash payout or bonus that the business was not entitled to.

SMEs should make full use of the PIC scheme and capitalise on the substantial incentives which are being offered to them. However, care must be taken to ensure that any expenditure is legitimate as the repercussions for providing false information or making fraudulent claims are severe. ■

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