

SINGAPORE CA QUALIFICATION (FOUNDATION) EXAMINER'S REPORT

MODULE: Singapore Taxation (TXF)

EXAMINATION DATE: 12 December 2018

Section 1

General comments

December 2018 exam session was the first time Candidates used e-Exam software, with each of them recording their answers using their personal laptop (in full lockdown mode – no internet/network connectivity or hard drive access) instead of traditional pen and paper. Notwithstanding the use of laptops, all SCAQ Foundation Module examinations continue to be a restricted open-book format with Candidates being able to bring in a double-sided A4 page of personal notes for reference. An appendix with relevant tax rates, reliefs, and allowances was also attached to the question paper. There was also no change made to the format of the question paper and the suggested solutions to past examination papers continue to be released.

While the performance of December 2018 exam was significantly better than previous cohorts, which is commendable, the following shortcomings were also noted:

- The computational and Goods and Services Tax (GST) questions were quite well answered but attempts at the qualitative questions were not so well done. In fact, a fair number of Candidates did not attempt the lower weightage qualitative questions. The answers that were given to the qualitative questions also shows up gaps in the Candidates' knowledge and understanding of Singapore tax law generally.
- Incorrect application of tax law.
- Lack of depth and completeness in answering qualitative type questions. It is insufficient to just regurgitate rules and conditions. Candidates also need to explain why those rules and conditions are not met. For example, it is better to state that an expense is not deductible because it is capital in nature since the outlay was used to acquire an investment or fixed asset that is to be used for the long-term benefit of the business instead of just stating that the expense is not deductible as it is capital in nature.
- Careless computational errors.

It is essential that Candidates prepare well for the examination through reading, comprehending and applying the relevant sections from i) the *Income Tax Act* (ITA) and associated regulations applicable to the TXF syllabus, ii) the *Goods and Services Tax Act* (GSTA) and associated regulations, and iii) the IRAS e-Tax guides.

There is a lot of tax information in the public domain (e.g. the IRAS website) and it can be overwhelming to sieve through all the information available especially when taxation of any kind is not part of the daily work routine. Attending tax courses will help to alleviate some of the stresses from trying to understand this information, as well as bridge any gaps in your tax knowledge.

Candidates are therefore strongly encouraged to explore the IRAS website and make good use of the resources available. For instance, Candidates can improve their knowledge by undertaking the free online courses offered by IRAS at <https://elearn.iras.gov.sg/iraslearning/content/iras/startpage/index.aspx#>.

Candidates must put in enough time and effort to reinforce and clarify their understanding. This is especially important for those Candidates who are switching from a non-accounting background.

Candidates are also reminded to seek to learn and understand all areas of taxation that are covered in the syllabus. The TXF examination tests Candidates' understanding and ability to **apply** their tax knowledge. In our bid to be good tax preparers, professional accountants, consultants, or key business decision makers, a solid foundation and clear understanding of the rules will help us to avoid costly mistakes or make inferior decisions. We should strive to understand the principles of what we are doing instead of merely carrying out our tasks mechanically and by rote.

Section 2

Analysis of individual questions

Question 1

Question 1 comprised two parts and **Part (a)** required Candidates to calculate the minimum tax liability of a Singapore incorporated company that was in the business of selling wines and related accessories. It was a relatively newly incorporated entity with 80% of the shares held by an individual and the remaining 20% of the shares held by a foreign owned company. Hence, one of the key areas to consider was whether the company qualified for the full tax exemption scheme (also referred to as start-up tax scheme). Surprisingly, a fair number of Candidates did not claim tax exemption under the start-up scheme but utilised only the partial tax exemption scheme. It appears that quite a number of Candidates were not familiar with the tax exemption scheme that was introduced to support entrepreneurship in Singapore. This observation is also borne out by the fact that a fair number of Candidates did not answer or gave a totally wrong answer to **Part (a)** despite this part clearly stating that the company would like to maximise the benefits under the full tax exemption scheme.

Pleasingly, almost all Candidates could prepare the computation in the correct format, although there continues to be confusion among some Candidates between treating Section 14Q deductions on renovations as part of adjusted trade profit or as part of capital allowances claim (it should be the former). As a guide, where deductions are allowed under Section 14 of the ITA (including special and further

deductions under Section 14) or disallowed under Section 15 of the ITA, such adjustments should go towards forming part of adjusted trade profit. Please also refer to further comments on Section 14Q of the ITA adjustment below.

The tax computation part of Question 1 also tested Candidates' understanding of the tax principles and current rules relating to taxation of income from various sources (trade viz non-trade sources), deductibility of expenses and capital allowances claims. In the current examination, Candidates were tested again on balancing adjustment but this time arising out of machinery that previously qualified for the Productivity and Innovation Credit (PIC).

Whilst Candidates could generally determine the taxability of the various receipts and deductibility of most expenses, many faltered on the following adjustments:

- Generally, any subsidy received to help cushion high operating expenses of a business should be viewed as a trading receipt and thus taxable as part of trade-sourced income. Thus, the special employment credit received of \$28,650 was a taxable trade receipt and required no adjustment. Some Candidates brought it to tax as part of the receipts from non-trade sources.
- All Candidates were aware of the limits placed on medical expense deduction. However, what felled many Candidates was the determination of staff remuneration for medical expense claim restriction. Many Candidates did not include the transport allowance paid to directors. As allowances are cash remuneration paid to staff, the transport allowance paid to directors should form part of staff remuneration against which the deductible percentage should be applied.
- Quite a number of Candidates treated the transport allowance as not tax deductible because it was stated that it was used by members of staff to upkeep their privately-owned cars. Fixed sum allowances form part of cash remuneration paid to staff to enable them to discharge their employment duties and are therefore deductible. How the allowances are utilised by staff does not have an effect on its deductibility to the employer.
- Many Candidates did not seem to be aware that where GST paid is accounted for in the Profit and Loss Account, it does not qualify for tax deduction if the input GST qualified for input tax credit. If the GST amount expensed relates to a blocked input GST credit, then the deductibility of the GST paid is dependent on the underlying expenditure. The GST in respect of the taxi booking charge qualified for input tax credit and thus the amount expensed was not deductible. Not many Candidates correctly made this tax adjustment. On the other hand, the GST in respect of medical and dental insurance premiums is blocked from input tax credit claim. Hence, it should be included as part of the underlying medical costs and subject to the medical expense restriction.
- The reserve for upkeep of premises was a general provision and not deductible. A number of Candidates did not disallow the provision. The amount utilised from

the reserve for additional tiling works qualified for tax deduction under Section 14Q but not many Candidates claimed one-third deduction thereof.

- The identification of capital expenditure that qualified for Section 14Q deduction or qualified as plant and machinery for capital allowances has always posed a problem for Candidates and it remains so in the current paper. Generally, where the cost relates to fixed premises – flooring, tiling, plumbing, sanitary and electrical works (these works are usually carried out to make the building or fixed premises functional), the costs should qualify for Section 14Q deduction unless the building qualifies for Land Intensification Allowance. Where the costs relate to mechanical equipment (air-conditioners for instance) and furniture (e.g. demountable partitions), the costs should qualify as plant and machinery for capital allowances claim.
- The interest incurred on the property loan was deductible as the property generated taxable income from the trade activity. A small number of Candidates did not allow this tax deduction.
- Many Candidates could determine the amount of interest expense payable on the loan that was not used for purposes of the trade activity (it was used to finance the loan to the shareholder). However, just as many Candidates also failed to claim a deduction of the said interest expense incurred from the gross interest income earned on the loan to the shareholder.
- It is inexplicable why some Candidates claimed capital allowances on the motor car. It is also inexplicable why a number of Candidates claimed allowances on the retail shop. Both of these items do not qualify for capital allowances.
- PIC enhanced allowances were previously claimed on the computerised Point of Sale system (POS) that was disposed. As the holding period was less than a year, the enhanced allowance claimed previously will be clawed back. Some Candidates omitted to adjust for the clawback while others calculated the clawback based on the sale proceeds when it should have been based on the original purchase price.
- As the cost of each counter did not exceed \$5,000, many Candidates were aware that the counters would qualify for accelerated claim of one year, subject to the maximum limit of \$30,000. However, not many Candidates seemed aware that under Section 19A(10A(b)) of the ITA, the tax written down value of such assets can be claimed over one year, subject to the maximum limit of \$30,000. As the tax written down value of the counters bought in the previous year was \$21,333, the entire amount could be claimed in full in YA 2018 (since it was within the limit of \$30,000).
- Finally, the dividend income was deemed remitted to Singapore under Section 10(25)b of the ITA since the foreign income was used to settle debts relating to the Singapore business.

Question 2

The tax computation required to be prepared under **Part (a)** was for a Singaporean male who was married to a citizen of the Philippines (a foreigner). Most Candidates could prepare the tax computation competently, detailing the taxable income from employment source viz other sources. The following errors were noted:

- Not many Candidates seemed aware that per diem allowances are taxable based on the amount of the allowance **in excess** of the IRAS prescribed rate for the respective countries. Quite a number of Candidates brought the full allowance paid to the employee (the taxpayer) to tax.
- The amount spent by the taxpayer on warm clothing was reimbursed by his employer. Hence, the tax consideration was whether this amount reimbursed should be brought to tax or not. Some Candidates incorrectly claimed a tax deduction for the expense.
- Most Candidates correctly calculated the accommodation benefit. Some Candidates chose to pro-rate the benefit utilised in the year based on the number of months while others used the number of days. Both methods are acceptable.
- Most Candidates correctly subjected the one-off cash allowance of \$20,000 (to assist the family to manage their property loss after the tax payer's residence suffered extensive damage in a fire) to tax although a small number of Candidates also claimed deduction for personal expenses purchased out of the allowance. This was not correct. Since this was a one-time allowance, it constituted additional wages for Central Provident Fund (CPF) contribution purposes. A number of Candidates did not work out the CPF relief on this additional wage amount.
- The rental income was derived from a **commercial property** and so the simplified basis of expense deduction was not applicable (a few Candidates considered this basis to claim rental expenses). Quite a number of Candidates did not claim a deduction for the cleaning expense nor the estate agent's fee. Since these two expenses were incurred to ensure continuity of rental source they were deductible.
- Any foreign income received in Singapore by an individual through a partnership does not automatically qualify for tax exemption. The tax exemption of such foreign income received is subject to the provisions under Sections 13(8) and (9) of the ITA.
- Many Candidates were not fully aware of the conditions to be satisfied in respect of the following personal reliefs:
 - Both children still qualified for child relief as there is no requirement that the child must receive full-time education throughout the basis period; and

- The full parent relief was still available even though the dependant parent passed away during the basis period.

Part (b) of Question 2 related to the tax clearance procedure. As the spouse was not a Singapore citizen nor a Singapore permanent resident, tax clearance was required when the individual terminated his/her Singapore employment contract. Only a small minority of Candidates were aware of this administrative requirement.

Question 3

Comprising three parts, the GST analysis of the transactions given in **Part (a)** was one of the better answered questions. Although there was a change in the answer format with the introduction of e-Exams, almost all Candidates could follow the instructions given correctly. It is pointed out that for all the transactions given, the answer should indicate if GST consideration is either output tax ("O") or input tax ("I"). In other words, would there be GST chargeable (output tax consideration) or GST payable (input tax credit consideration).

Some Candidates indicated "NA" for some transactions where there was no supply involved (e.g. cash donation). In this case, for GST purposes, the GST consideration is classified as an input tax claim. (Remember, sales and gifts generally entail an output tax consideration whereas purchases/imports and losses generally entail an input tax consideration.) Although well attempted, the common errors noted for **Part (a)** of Question 3 are as follows:

- For retail sales to non-GST registered customers, it was stated in the description that the GST was absorbed by the company. Perhaps this point was not taken note of as many Candidates did not calculate the GST chargeable correctly.
- For the donation of old inventory, the GST consideration was on the deemed supply arising from business goods given away to the charitable organisation at no consideration. Some Candidates stated that no supply arose from this donation.
- A number of Candidates could not identify the type of supply with respect to late payment interest paid on suppliers' invoices. This was a financial charge by the suppliers on late settlement of the debts due. This is an input tax consideration on a financing transaction which is thus an exempt supply.
- A number of Candidates did not know that bad debt relief should be claimed as part of input tax.
- The purchase of the sofa and wine fridge was a standard rated supply and so there should be input tax credit consideration. Since the provision of the furniture and equipment was for the employee's personal use, it did not satisfy the close nexus test and thus there should be no input tax claimed.

For **Part (b)**, most Candidates stumbled on the determination of the amount of GST to be repaid to IRAS. Since only \$30,000 in total was recovered from the receivers, the amount recovered should be treated as being inclusive of GST.

Part (c) was quite poorly attempted as the answers submitted were not complete or out of context, showing clearly that the Candidates' understanding of tax deduction and capital allowance claim was not complete. Many Candidates also only addressed the capital allowance claim and did not address if the cost was tax deductible in the first instance.

Question 4

There were three parts to Question 4 and all three parts were attempted to varying degrees of success, but largely quite poorly.

Part (a) was a test on utilisation of past and present loss items under carry forward provisions and group relief provisions. A number of Candidates could not make the distinction that some of the loss items were derived through an unincorporated entity (so the shareholders' test was irrelevant since the business and its owner were one and the same entity) as well as through an incorporated entity (so the only way to utilise the loss items was through group relief, if it was applicable).

On the use of the carry forward provisions, many Candidates indicated that there was a **change in business activity** thus resulting in the unabsorbed capital allowances brought forward from YA 2011 and 2012 being forfeited since the business continuity test was not satisfied. The change in business however had no effect on the utilisation of unabsorbed losses from the same YAs.

As for donations, quite a few Candidates failed to highlight that unabsorbed donations can only be carried forward for a maximum of five years. As for the loss items arising in the incorporated entity, many Candidates could state that the loss items could only be deducted under the group relief provisions and narrated the conditions for group relief. However, it somehow escaped their notice that the claimant was an individual and not a company incorporated in Singapore. As such, there was no follow-through connection made which resulted in an incorrect conclusion being made regarding transferability (and therefore deductibility).

Part (b) required a tax computation to be prepared for the owner of the sole proprietorship business incorporating income from the proprietor's other sources. This part was fairly done although the order of set-off of loss items was largely incorrect. Under Section 37(4) and subject to Section 37(5) of the ITA, the unabsorbed loss from any business should be deducted from the statutory income from the same trade or business first, before deducting from statutory income from any other trade or business and lastly against statutory income from any other sources. Consequently, the unabsorbed trade loss brought forward from YA 2011 and 2012 should be deducted from the statutory income of Faux Teak before the proprietor's income from non-trade sources were incorporated to arrive at her overall statutory income.

Some Candidates were not aware that the salary paid to the proprietor under a self-employment arrangement should be ignored for tax purposes. Therefore, the aforementioned salary was not deductible and should be taxed as part of business sourced income. On the other hand, the salary from the incorporated entity should be viewed as employment sourced income as the receipt was from a separate legal entity and prima facie it was for employment services rendered.

In **Part (c)**, Candidates were assessed on their understanding and knowledge of withholding tax implications in relation to interest payments. A number of Candidates did not submit any answer or submitted answers that were not very coherent or were incomplete. It points to either their poor understanding of the topic or poor time manage to complete question. Withholding tax is applicable only if the income is paid to non-residents and the income falls within the ambits of Sections 12(6) and (7) of the ITA. In other words, the income must be deemed sourced in Singapore under the provisions of these Sections. Generally, the relevant income is deemed sourced in Singapore if the payment is borne by a person resident in Singapore or a permanent establishment in Singapore or the payment is claimed for tax deduction against any income derived from Singapore. For interest, where funds from the loan provided are brought into or used in Singapore, the interest payment is also deemed sourced in Singapore. There are exceptions to this general rule and they should be highlighted where applicable. In **Part (c)**, two exceptions were applicable:

- A general waiver by IRAS under an administrative concession on all payments made to Singapore branches of non-resident companies (this took effect from 21 February 2014); and
- Interest payments made to non-residents where the proceeds from the loan are used to acquire immoveable property located outside Singapore.

As this was a new topic being tested, the attempts made by most Candidates were commendable.