

SINGAPORE CA QUALIFICATION (FOUNDATION) EXAMINER'S REPORT

MODULE: Singapore Taxation (TXF)

EXAMINATION DATE: 18 June 2018

Section 1

General comments

The examination continues 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 no change to the format and the suggested solutions to past examination papers continue to be released.

While all Candidates could complete the paper indicating better time management, they let themselves down through:

- Not reading and processing the information given properly and adequately;
- 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; and
- Careless computational errors.

It is that Candidates prepare well for the examination through reading, comprehending, and applying the relevant sections from i) the *Income Tax Act* and associated regulations applicable to the TXF syllabus, ii) the *Goods and Services Tax Act* and associated regulations, and iii) the Inland Revenue Authority of Singapore (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.

However, Candidates must also 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 reminded to seek to learn and understand all areas of taxation that are covered in the syllabus. The 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.

Candidates are 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#>.

Section 2

Analysis of individual questions

Question 1

The corporate tax question centred on a plastics product manufacturing company incorporated in Singapore, which was privately owned by two brothers.

For **Part (a)**, Candidates were required to ascertain deductible medical expenses. Although the company had not implemented any Portable Medical Benefits Scheme or Transferable Medical Insurance Scheme, it did voluntarily make contributions to the Medisave accounts of its Singaporean employees. So, while the deductibility of medical expenses and insurance premiums continue to be restricted to 1% of staff remuneration, the ad-hoc Medisave contributions could enjoy tax deduction up to the overall medical expenses tax deduction limit of 2% of staff remuneration. However, the ad-hoc Medisave contributions must first be subject to an overall cap of \$1,500 per employee per year. Many Candidates did not seem aware of the Medisave deductible cap limit of \$1,500.

Part (b) required Candidates to compute the minimum tax liability of the client company for the YA 2018. To do well in this question part, Candidates needed to work quickly and accurately to identify the line items that needed adjustment to arrive at adjusted profit, statutory income, assessable income, chargeable income, and net tax payable. Almost all Candidates could prepare the computation in the correct format although there continues to be some confusion among the 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 or disallowed under Sections 14 and 15 (including special and further deductions under Section 14), such adjustments would go towards forming part of adjusted trade profit.

The tax computation tested Candidates' understanding of tax principles and current rules relating to taxation of income from various sources (trade vs non-trade sources), deductibility of expenses, and capital allowances claims. In the current examination, Candidates were tested on balancing adjustments arising out of plant and machinery and a building that were no longer in use for the company's business as a result of a fire in its warehouse.

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

- The insurance compensation with respect to losses suffered on the automated warehousing equipment and warehouse building were not taxable as they related to the recoupment of cost relating to capital expenditure. However, the compensation must be taken into consideration in the balancing adjustment relating to these two fixed assets. Some Candidates also included the accounting net book value written off in the balancing adjustment. This was incorrect.

No adjustment was required in respect of the compensation relating to the loss suffered on trading stock as the compensation was taxable.

- The profit from sale of Singapore shares was a capital gain and thus not taxable. While most Candidates correctly treated it as a non-trade gain, they also subsequently brought it back to tax as income from non-trade sources. This was incorrect.
- Many Candidates failed to identify the surveyors' fees relating to the warehouse as capital expenditure. As this expenditure related to reconstruction of a fixed asset, it was capital in nature and thus not deductible.
- The gifts to business associates were deductible as gifts are generally given with the view of cultivating and/or maintaining business relationships that help in the generation of sales or to ensure a smooth supply chain. However, with respect to the input GST of \$1,500, this was not deductible. The input GST would qualify for input tax credit as it was incurred to generate taxable supplies but where the value of the gift exceeds \$200, output tax will have to be accounted for based on the value of the gift since business goods were given away for no consideration. However, to avoid accounting for the deemed output GST, the GST-registered company can opt to give up the input tax credit but Section 15 prohibits the deduction of the input tax so written off. Not many Candidates seemed to be aware of this prohibition.
- Many Candidates omitted to disallow the mileage claims by staff of \$18,000 even though this related to private car expenses. Instead, a number of Candidates disallowed the private car hire charges incurred on overseas business trips. Since Year of Assessment 2014, expenses on foreign rental cars used exclusively outside Singapore are fully deductible where the cars are used for business purposes. Expenses on private cars used in Singapore continue to be not deductible even where such expenses are business-related.
- The hire purchase interest on the delivery vans acquired was deductible as the hire purchase loan was used to acquire assets that produce trade-related income. Generally, any expense relating to the purchase of fixed assets or investments would not qualify for tax deduction as it is viewed as capital

expenditure. However, interest expense is an allowed deduction under Section 14(1)(a) so long as the loan is used to generate income.

- Many Candidates could not identify correctly the training expenses that qualified for enhanced deduction under the Productivity and Innovation Credit (PIC) Scheme.
- The exchange gain arising from the purchase of artwork that was kept by the company was capital in nature and thus not taxable as it was related to the acquisition of a fixed asset. The gain relating to the purchase of artwork that was gifted to a customer was a taxable gain as it relates to a business expense incurred in the production of trade income. Not many Candidates made the distinction.
- Only the cash donation of \$16,000 qualified for deduction and the rate of relief was at 2.5 times although there were some Candidates that claimed deduction at 3 times, a rate that was granted only for qualifying donations given in calendar year 2015. Future Candidates should note that the Minister for Finance, Mr Heng Swee Keat, announced in the 2018 Budget that the 250% tax deduction for donations made to Institutions of a Public Character (IPCs) would be extended for another three years, until 31 December 2021.
- The non-structural renovations carried out during the year should be claimed for deduction under Section 14Q even though the works may also qualify for deduction under Section 14H. As the maximum claim allowed under Section 14H is \$100,000 and it had been fully claimed previously, the additional costs incurred during the year should be claimed under Section 14Q instead.
- Despite the hint given, there were still some Candidates who claimed accelerated capital allowances in respect of the new delivery vans acquired. Many Candidates also did not seem to know how to claim capital allowances on qualifying plant and machinery bought on hire purchase terms. Under hire purchase arrangements, costs are treated as incurred based on capital repayments made during the year. Thus, initial allowance under Section 19 as well as accelerated allowances under Section 19A are to be claimed based on capital repayments in the year while Section 19 annual allowance continues to be claimed based on 80% of the total qualifying costs over the prescribed tax useful life under the Sixth Schedule. This is also why for non S-plate motor vehicles bought under hire purchase, it may be more tax efficient to claim normal allowances under Section 19 instead of accelerated allowances under Section 19A.
- Land Intensification Allowance (LIA) requires prior approval to be granted by the Economic Development Board (EDB). Since the question did not state that prior approval for LIA had been sought from the EDB, Candidates should not assume that the building qualified for LIA. A number of Candidates made the claim.

- Artwork is generally not viewed as plant and machinery for capital allowances claim purpose unless it is an apparatus that is necessary for carrying out the trade activities of the taxpayer. Artwork generally has no use apart from decorative purposes and, as such, would not qualify for capital allowances. But for businesses like those in the hospitality industry, artworks are necessary to project a certain image as well as to create the appropriate ambience to draw in the desired customers. This is not the case for Enviro Plastics Ltd.

Hardly any Candidate could answer **Part (c)** adequately. Firstly, not many Candidates seemed to know the courses of action that can be taken in the case of errors discovered in tax returns already submitted. Of those who did, not many Candidates made the distinction between errors that resulted in tax overpaid and errors that resulted in tax underpaid to IRAS. This distinction is important as there is a deadline by which time errors resulting in tax overpaid can be requested for review. As for errors resulting in tax under-collected by IRAS, such errors should be voluntarily disclosed as quickly as possible to mitigate the imposition of penalties. There were also some Candidates who stated that objections should be lodged against the Notices of Assessment previously issued by Comptroller of Income Tax. This is incorrect as the time frame to lodge an objection is 30 days from the date of issue of the Notice although as a concession to corporate taxpayers, this time frame has been extended to two months since 1 January 2014.

Question 2

The case facts described a widow with two children who commenced employment in Singapore during the year 2017. Question 2 tested Candidates on their understanding and application of tax residence rules as well as claiming of relevant personal reliefs besides the taxation of various benefits given to foreign employees.

Part (a) required Candidates to establish the individual's tax residence status. While many Candidates stated that the individual failed the qualitative test, not many Candidates could explain that it was because the individual's **normal place of residence** was not Singapore. Instead, Candidates quoted citizenship as the reason why the qualitative test was not met. Citizenship is just one of the factors used to determine where an individual normally resides.

All Candidates were familiar with the quantitative test but commented on the individual's tax residence status under the test only with respect to Year of Assessment 2018 and did not address her tax residence status for the rest of her employment period (i.e. Years of Assessment 2019 and 2020). As a result, marks were lost for incomplete answers.

Almost all Candidates were influenced by the fact that the individual was employed under a 2-year contract and thus went on to apply the 2-year administrative concession. Very few Candidates seemed aware that the 2-year employment contract stretched over three years and thus the 3-year administrative concession should be applied instead.

It is inexplicable that a number of Candidates went on to address the tax treatment of a non-resident employee under the provisions of Section 40B and adopted this stance when answering Part (b) as well. This most likely stems from Candidates' conclusion that the individual was non-resident under the quantitative test for Year of Assessment 2018 without considering their conclusions drawn under whichever administrative concession the Candidate chose to adopt. Section 40B was not relevant as the taxpayer was clearly tax resident in Singapore under the 3-year administrative concession.

Part (b) required Candidates to compute the taxpayer's tax liability for YA 2018. Again, to do well in this question, Candidates needed to work quickly and accurately to recognise the line items to correctly identify total employment income, income from other sources, statutory and assessable income, relevant reliefs, chargeable income, and net tax payable. Most Candidates could prepare the tax computation detailing the taxable income from the employment source viz other sources.

The errors noted in the tax computations prepared stem largely from failure to understand or process the information provided. Many Candidates also did not seem to understand what expenses can be claimed for deduction from employment income. In this regard, only expenses incurred by the employee in the discharge of employment duties will be allowed as a deduction. These expenses must be paid out of the employee's own pocket and not reimbursed by the employer.

- As a rule, any benefit, whether payable in cash or in kind, provided by an employer that relates to personal expenses or personal consumption will be a taxable benefit of the employee unless it is exempted by law or by way of administrative concession. As accommodation is a private expense, the provision of accommodation by the employer is a taxable benefit as follows:
 - The hotel bill borne by the employer was fully taxable. The amount borne by Fiona (the employee) could not be deducted from this benefit as this was a personal expense.
 - The taxable benefit arising from the fully furnished rental accommodation provided by the employer should be calculated based on the annual value of the accommodation instead of the monthly rental paid by employer.
 - All fixed cash allowances are fully taxable and the relocation allowance given to Fiona was no exception. However, expenses incurred to relocate to Singapore to commence employment would be allowed as a deduction. Thus, relocation expenses, like the air ticket to move to Singapore, the freight charges, settling-in expenses like the bed and temporary accommodation, would be deductible. Storage expenses to keep personal belongings are personal expenses and not deductible. Some Candidates inexplicably subjected to tax the relocation expenses borne by the employee.
- Some Candidates could not distinguish between expenses borne by the employer and the employee, Fiona. Consequently, private expense like the taxi fare for daily commutes borne by the employer were not treated as a taxable

benefit. Instead, some Candidates claimed deduction of the aforementioned taxi fares as well as taxi fares for client visits from Fiona's employment income.

- The formula pertaining to the taxable benefit of a leased car provided by an employer should be applied only to the leasing charge and not the running expenses. The taxable rate to be applied in relation to the provision of petrol for private travel should be \$0.10 and not \$0.55.
- Some Candidates subjected to tax 20% of the cost of Fiona's son's return air ticket. Firstly, this concession was removed with effect from Year of Assessment 2018. Even if the concession was still available, it would not be applicable in this case as the concession was only applicable to air passage taken by the foreign employee to go back to their home country for home leave.
- Some Candidates subjected the foreign rental income brought into Singapore to tax. Foreign income received by individuals in Singapore is generally exempt from Singapore tax except where such income is received through a partnership arrangement.
- Many Candidates seemed unaware of the conditions to be satisfied in respect of the following personal reliefs:
 - The claim for child relief is not dependent on whether the child is living in Singapore or not. Thus, qualifying child relief was available on both children as both children were not married and were below 16 years of age.
 - A number of Candidates claimed Working Mother's Child Relief. This relief is only available if the children are also Singapore citizens.
 - Parent relief and Grandparent Caregiver relief are available only if the dependent parent and grandparent caregiver are living in Singapore, a key condition amongst other conditions.
 - Only Singapore citizens and permanent residents are required to contribute to the Central Provident Fund (CPF). CPF relief is thus not relevant in this instance.
 - Spouse relief was claimed despite it being mentioned that Fiona's husband had passed away.
 - Foreign maid levy relief was incorrectly calculated based on the full monthly rate of \$265 instead of the concessionary rate given in the question of \$60.

Question 3

There were two parts to the GST question. **Part (a)** required Candidates to complete the GST return for the quarter ended 31 June 2017 for a GST-registered company in the food and beverage business. In this respect, a template was provided to help Candidates work out the values of the various taxable and exempt supplies and taxable purchases in order to complete the GST return. The following errors were noted:

- Many Candidates were unable to distinguish between output tax and input tax. This is a fundamental concept in accounting for GST. Future Candidates should

make good use of the free resources available from the IRAS website (<https://www.iras.gov.sg/IRASHome/GST/Non-GST-registered-businesses/Learning-the-basics/How-GST-Works/>).

- Some Candidates did not read the individual transactions completely and failed to correctly compute the value of the supply and the output tax where the charges given were inclusive of GST (i.e. the wine corkage charge and the ten dining vouchers).
- The output tax on the two dining vouchers consumed was not computed correctly by most Candidates.
- Many Candidates did not account for the output tax on the non-refundable deposit (payment in advance for goods and services to be supplied).
- Despite being sold at a larger than normal discount, the GST chargeable on the wine sold to the external accountant should be based on the actual sale price of \$50 per bottle.
- The invoice issued by the guest chef for his services, as well as the cost of his air ticket, should be stated as out of scope supplies. It should be noted that the services were provided by a person who does not belong in Singapore. Since this was the chef's first working assignment in Singapore, the chef would not have any business establishment or fixed establishment in Singapore.
- A number of Candidates could not correctly identify the late payment interest expense as a purchase exempted from GST (financial services).
- Many Candidates did not point out that there was no deemed supply arising from the cost of food supplies used in staff meals.

Part (b) required Candidates to address the time of supply in respect of a refundable deposit that was utilised against the value of food and services subsequently invoiced. While many Candidates could address the time of supply to varying degrees of accuracy, the vast majority could not calculate the GST chargeable correctly. This was because they failed to note that the deposit of \$2,000 was now a refundable deposit. Thus, when it was first received in the quarter ended 30 June 2017, no GST would have been collected on it. Hence, the GST to be accounted for in July when the reservation was confirmed should be calculated based on the \$2,000 deposit being inclusive of GST.

Question 4

This question tested Candidates' knowledge and application of deduction rules pertaining to interest expense and the adoption of appropriate financing options for tax efficiency. There were four parts to this question to guide Candidates to their final conclusion. While many Candidates drew the correct conclusions, the answers given were incomplete, lacking in details, or incorrect.

Part (a) required Candidates to explain the deduction of interest expense where debt financing was used to finance the purchase of real estate in Singapore or in China. Some Candidates stated that the interest expense was not deductible as it was capital in nature since the expense was incurred to acquire a fixed asset. This was incorrect. Interest expense deduction is generally dependent on whether income is derived or not. There were also quite a number of Candidates who mentioned that the interest expense in respect of the Singapore factory would qualify for LIA as part of qualifying building costs. It must be pointed out that if we can claim full deduction under Section 14(1)(a) as and when the interest expense is incurred, why would we want to consider claiming deduction over 15 years.

Of those who correctly stated that interest expense incurred to acquire the Singapore factory would be deductible as trade income was generated, many Candidates faltered when addressing the deduction of interest expense where the loan was used to acquire the investment property in China. The answers provided were mostly incomplete in that Candidates did not point out that the interest expense can only be deducted from rental income (not income from other sources) which is also foreign sourced. Thus, the benefit of tax deduction would be deferred until such time the foreign rental income was actually received in Singapore.

Part (b) required Candidates to address the tax treatment of the proceeds from the sale of shares that were held for a long time. Many Candidates treated the sale as being similar to a payment of foreign dividends and addressed the tax exemption scheme given under Section 13(7) and (8).

Part (c) was reasonably answered by many Candidates although not completely as many did not cover the circumstances under which foreign income is treated as received in Singapore or the availability of foreign tax credit if the foreign dividend was subject to Singapore tax. Although it is gratifying to note there were some Candidates who could identify that credit for the underlying tax suffered was not available as the minimum shareholding threshold was not met.

While Candidates could draw the correct conclusion for **Part (d)**, most Candidates did not explain the basis of their recommendations.