SINGAPORE CA QUALIFICATION (FOUNDATION) EXAMINER'S REPORT

MODULE: Singapore Taxation (TXF)

EXAMINATION DATE: 10 December 2020

Section 1
General comments

This is the second examination conducted remotely and generally, and Candidates seem to have adapted well to the examination software. Otherwise, the current examination format remained mostly similar, a restricted open-book format with an Appendix containing information relating to tax rates, rebates, personal reliefs and allowances provided.

The performance of the current cohort is lower than the previous cohort.
The following were noted:

- Time management remains an issue. Although most Candidates could complete all four (4) questions, Question 4 was the least well attempted. Candidate's performance on the computational (Question 1(b) and 3(a)) and GST questions (Question 2a) were mostly competent although many answers showed gaps in Candidates' basic tax knowledge. There were a handful of Candidates who did not attempt the corporate tax computation question.

- The answers to the qualitative questions (Question 2(b) and 4(b)) continued to be poor showing clearly that Candidates' knowledge and understanding of the subject areas tested were very superficial or very muddled. Consequently, there was a lack of depth and completeness in the answers given apart from regurgitating rules and conditions.

- Careless computational or transposition errors were noted, but many Candidates have now incorporated workings in their answers, making it easier for markers to award marks for the correct application.

- Topics tested were those required under the TXF syllabus, but it appears that many Candidates did not study sufficiently. This is apparent in Question 3(a) as many Candidates did not address the claim under Section 14A - special and further deduction for intellectual property right and Question 4 where many Candidates do not seem to know the restrictions applicable to Section 10E companies.

- Question 4 was the worst-performing question for the majority of Candidates. This stems from Candidates' lack of understanding of the rules on the utilisation of loss items under the carry forward/carry back relief provisions and group relief provisions and their unfamiliarity with Section 10E companies. Nonetheless, it was noted that some Candidates made a valiant attempt to go beyond stating

the conditions and instead applied the conditions to the circumstances applicable to the respective entities.

Candidates must 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 related regulations, and iii) the Inland Revenue Authority of Singapore (IRAS) e-Tax guides.

There is a lot of tax information in the public domain (for example, the IRAS website). 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 alleviate some of the stress from trying to understand this information and bridge any gaps in your tax knowledge. If the self-study route is taken, please ensure that your tax knowledge is up to date by checking to IRAS website. A handful of answers were submitted where personal tax rebate was claimed when none was given for Year of Assessment 2020 ("YA"), or the wrong rate of corporate tax rebate was used. (The information on these rebates can be found in the Appendix to the question paper.)

Candidates must put in enough time and effort to reinforce and clarify your understanding. Please avoid rote learning as much as possible. Past examination questions should preferably be attempted before cross-checking to the suggested solutions. 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. We should strive to understand the principles of what we are doing instead of merely carrying out our tasks mechanically and by rote.

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 https://elearn.iras.gov.sg/iraslearning/content/iras/startpage/index.aspx# .

Section 2
Analysis of individual questions

Question 1

Question 1 centred on a female individual, Ms Claire Soon, who switched from deriving business income as an active partner in medical practice to employment income after her division was acquired. There were two parts to Question 1.

Part (a) required Candidates to work out the partnership's capital allowances available to the individual after her resignation as a partner. Many Candidates very poorly attempted this part largely due to their lack of understanding/knowledge of the tax consequences on capital allowances claim upon the resignation of a partner. It should be noted that whenever qualifying assets are no longer in use for business or trade, it will trigger a balancing adjustment whereby the tax written down value of the asset no longer in use will be compared to the sales proceeds or the relevant market value when the asset ceased to be in use. In the case of a partnership, the resignation of a partner results in the cessation of business.

A new business comprising the remaining partners will commence after that. In this case, there was a cessation of partnership business on 31 March 2019 as the subject taxpayer ceased to be a partner in the business effective from 1 April 2019. A new business comprising the remaining two partners commenced on 1 April 2019. Thus, balancing adjustment will be required of the assets that are sold and those that will be transferred to the new partnership for use in the new business commencing on 1 April 2019.

For the assets that were transferred to the new partnership, we should consider if Section 24 can be elected. Since the remaining partners held at least 50% of the profit-share in the old partnership (70%) as well as in the new partnership (100%), Section 24 can be elected on the assets that will continue to be used by the partnership on 1 April 2019. Almost all Candidates failed to consider Section 24 election on this lot of assets. As for those assets that were sold to the buyer of the weight-loss business, there is no need to pro-rate the balancing allowance based on the actual number of months the asset was in use in the old partnership business. Capital allowances are given based on the total costs incurred in any basis period regardless of the actual number of days used.

Part (b) required the preparation of tax computation for the married Singaporean female with two children. The individual derived income from three (3) sources – business, employment and rental. Candidates were required to show clearly the net taxable income from each of these three (3) sources separately before deducting the relevant personal reliefs. Most answers submitted showed a clear distinction between the various sources, but there were answers that were somewhat jumbled.

Business source

Candidates needed to ascertain the adjusted profit attributable to the subject taxpayer before she ceased to be a partner. As the divisible profit is the residual adjusted profit after deducting partners' appropriation, the adjusted profit attributable to Claire Soon is arrived at by adding back Claire's appropriations (drawings for her salary and interest on capital contribution) to her share of the divisible profits. Against the adjusted profit derived, the order of set-off after that should be her share of capital allowances from the partnership business (i.e. answer from part (a)) followed by the unabsorbed trade loss brought forward from YA 2019.

The following were noted:

- Many Candidates could not arrive at the adjusted profit.

- Many Candidates did not adopt the correct order of set-off.

- Some Candidates further pro-rated the divisible profit as well as salary and interest to the period from 1 July 2018 to 31 March 2019. This is inexplicable. It is stated clearly that the divisible profit, salary and interest from the partnership were for the aforementioned period. There was no need for the further adjustment.

Employment source

The following errors were noted:

- As her employment commenced on 1 May 2019, only 8 months' salary needs to be brought to tax. There were various errors in the number of months used to compute the total salary to be brought to tax, including the use of 12 months.

- The bonus was not taxable in YA 2020 as she has not earned it let alone received the bonus. It was stated that the bonus is payable upon completion of one (1) year's employment; she needs to remain an employee till 30 April 2020. The bonus will be taxable in YA 2021 if the condition is met.

- The taxable car benefit should be pro-rated to the actual number of days used by Claire in year 2019 (from 1 May to 31 December 2019). Many Candidates failed to do so.

- The taxable benefit arising from the provision of the car running expenses by the employer relates to the personal usage by Claire. Thus, the factor of 3/7 needs to be applied to the expenses borne by the employer. Many Candidates subjected to tax the entire expenses borne by the employer.

Rental source

- As this was Claire's first time deriving rental income, the deductible expenses were restricted to property tax, maintenance expense and interest expense. The remaining two expenses are capital in nature and not deductible as they were incurred to enable Claire to access rental source for the first time.

  These deductible expenses related to a 12-month period while her rental income was derived for a 7-month period. Thus, the deductible expenses had to be further restricted to a 7-month period. Many Candidates failed to do so.

- As the rental property was a joint venture purchase with her siblings, Claire's taxable rental income should relate to her ownership share of 25%. A small number of Candidates did not restrict her taxable rental income to her ownership share.

Personal relief

The following errors were noted:

- The subject taxpayer's husband was suffering from a debilitating medical condition certified by a doctor. She is entitled to handicapped spouse relief. A few Candidates failed to do so.

- Qualifying child relief is available even if the child is above 16 years old so long as the child is studying full time in any university, college or the educational institution at any time in the basis period and the child did not derive income above $4,000 in the same period. As her son was studying during part of 2019 before his graduation, Claire is still entitled to claim qualifying child relief on her son. Many Candidates failed to make the claim. Since her children are Singapore citizens, she is also entitled to Working Mothers' Child Relief ("WMCR") on both children. In this regard, the relief is calculated based on the prescribed % for the relevant child, according to their birth order, which is to be applied to the mother's earned income. Earned income relates to net taxable income from both the business as well as an employment source. A number of Candidates did not compute the earned income correctly. Further, the total child relief QCR + WMCR) for each child is restricted to $50,000. Thus, the WMCR on the second child needed to be limited to $46,000. Many Candidates failed to do so.

- Parent relief can be claimed on Claire's mother even though she passed away during the basis period. A fair number of Candidates failed to do so. Quite a few also claimed Grandparent Caregiver relief. This is unavailable as the qualifying child needs to be below 12 years of age.

- Since Claire is a Singapore citizen, the CPF relief should be determined on her salary derived from her employment source. Many Candidates failed to do so.

  Salary derived from the partnership business is not subject to employment CPF as this is not viewed as employment income since she is one of the business owners. CPF on self-employed income is only payable if it is determined that the self-employed have assessable net trade income in excess of $6,000. There is no CPF relief for Claire's self-employed income in YA 2020 as it was not stated that Claire had made any CPF contribution on her partnership income during the basis period. Furthermore, it is unlikely that there would be CPF payable in the basis year 2019 on self-employed income as it is stated that she had unabsorbed trade loss brought forward from YA 2019.

- As her son had completed his National Service duties, Claire is entitled to claim NS parent relief. Many Candidates did not do so. She is not entitled to NS wife relief as her husband was exempted from National Service duties.

Question 2

This question comprises two parts. The GST analysis of transactions given in **part (a)** was well attempted. The majority could answer in the format required. However, there were sub-parts where more than one (1) transaction was required to be analysed. Even though the separate transactions were not annotated, Candidates could have provided separate answers to the individual transactions as some did. Many Candidates provided one linear solution.

The following errors were noted:

- As stated in the question, for all the transactions given, it should be indicated if the GST consideration was from the output tax ("O") or input tax ("I") perspective regardless if GST was chargeable.

  Where there was a supply of goods or services made in respect of the transaction given, Candidates were to indicate if the GST implication was from the output or input tax perspective. Thus, the use of "Not Applicable" should be carefully considered and not be indiscriminately used whenever there is no GST to be collected or paid.

  "Not Applicable" can be used if we are certain there is no actual supply of goods and services (e.g. cash donations) but for a zero-rated supply, the use of "Not applicable" would be marked wrong. Candidates lost marks on the incorrect use of this annotation.

- There is no supply of goods nor services in respect of dividend income received. Many incorrectly identified the type of supply as exempt supply.

- Service providers must charge 7% GST on services provided in respect of immovable properties located in Singapore regardless of the property is a residential or commercial property. However, whether the input tax credit can be claimed depends on whether the conditions for input tax credit were satisfied. The input GST paid on the legal fees regarding staff accommodation is blocked from input tax credit as the staff benefit did not meet the close nexus test. Many Candidates either identified the type of supply as exempt or claimed the input tax credit.

- As the medical equipment was imported into Singapore, it would be subject to GST by Customs and Excise Department and 7% GST would be levied on the purchase price as well as the insurance and freight charges. Some Candidates did not claim the input tax credit.

- Both the interest paid to the overseas supplier and the bank in Country Y should be identified as out of scope supply as the supplier belongs outside Singapore. Thus, the supply made would not be subject to GST in Singapore. Many identified it as Exempt Supply.

- As the bento lunch boxes given to staff represents business goods given away for no consideration, there is a need to address the output tax implications arising from the deemed supply. Only a few Candidates addressed the output tax implications.

Candidates' attempts on **part (b)** were mostly reasonable, but it did show that many Candidates had a very poor understanding of the topic on withholding tax. Sections 12(6) and (7) helps to determine if the source of income in the form of interest, royalty, rental, management fee, etc. was derived from Singapore. Withholding tax would be applicable if such income were deemed sourced in Singapore under the said provisions **and** if the income were paid to non-residents of Singapore.

In light of the foregoing, the following conditions required under Section 12(6) were expected to be addressed:

- As the nature of the income was interest, Candidates need to confirm that the interest was payable on indebtedness relating to the purchase of medical equipment by the Singapore company. Since the purchase of equipment is repayable by instalments, the instalment plan represented an indebtedness, and so, Section 12(6) would be applicable on the interest chargeable. Quite a few Candidates stated that the purchase of equipment does not equivalent to an indebtedness.

- The creditor is a company that is incorporated outside Singapore and which does not have a place of operations in Singapore, and thus, it is safe to point out that the recipient of the interest income is a non-resident of Singapore.

- The payment is borne by a company that is tax resident in Singapore.

- Only the payment relating to the purchase of equipment would be subject to withholding tax as the payment was for the benefit of a business conducted in Singapore. On the other hand, the interest on the working capital loan would not be subject to Singapore withholding tax even though the payment was borne by a Singapore tax resident company. This is because the proceeds of the loan were being used for a business conducted outside Singapore via the offshore branch. Just as importantly, the proceeds of the loan were not brought into or used in Singapore.

- The deductibility of the two (2) payments also impacts whether Singapore withholding tax would be applicable as this is one of the pre-requisites listed in Section 12(6) for specified income to be deemed sourced in Singapore. Only the interest in the purchase of the equipment is deductible as the equipment was used to acquire income sourced in Singapore (the equipment is the trading stock of the Singapore purchaser). On the other hand, the interest on the working capital loan is not deductible for Singapore tax purposes as the loan was used to acquire income sourced outside Singapore by the offshore branch.

Question 3

Almost all the Candidates could prepare the computation in the correct format. Most candidates correctly treated Section 14Q deductions on renovations as part of adjusted trade profit instead of capital allowances claim. To reiterate, where deductions are allowed under Section 14 (including special and further deductions under Section 14) or disallowed under Section 15, such adjustments would go towards the determination of adjusted trade profit.

A handful of Candidates did not attempt the question, and there were a few incomplete answers submitted. Quite a few answers resulted in an overall net trade loss, and this is mainly due to carelessness like subtracting instead of adding amounts. Further, many Candidates also omitted to work out the balancing adjustment arising from the sale of an investment property even though it was stated clearly that the property qualified for industrial building allowances.

The tax computation question tested Candidates' understanding of tax principles and rules relating to the taxation of income from various sources (trade vs non-trade sources), deductibility of expenses (in general and against the respective income source) including special deductions and capital allowances claims.

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

Expenses

- Apart from the cash allowance and insurance premium, which will be addressed further on, all other expenses listed under "Staff costs" were deductible.

  Various Candidates have erroneously treated the following as not deductible:
  - The foreign workers' levy is a statutory fee payable when foreign workers are hired to work in Singapore.
  - The retrenchment payment is deductible as the representative office is an extension of the Singapore company in Country X. The closure of this office is a business decision and not due to a permanent cessation of its business.

- Some Candidates treated the cash allowance as part of staff remuneration in determining the quantum of medical expenses allowable, which is incorrect. Cash allowance for staff medical and dental treatments, and the staff hospitalisation insurance are treated as medical expenses to be subject to cap limits if applicable. In determining the quantum of medical expenses allowable, only cash remuneration for employment services will be considered. In this case, only staff salaries and the entertainment allowances (classified under Marketing expenses") should be considered.

- Private hire car expenses for cars used in Singapore are not tax-deductible unless such cars are hired together with the driver (chauffeured private hire

cars). Chauffeured private hire cars are thus the Grab, Gojek and similar such cars which are being used like public modes of transportation.

- Although the ceiling works are repair works in nature, it is a cost incurred to derive rental income. Thus, it will be deductible against rental income only. Most Candidates correctly identified it as part of non-deductible expenses for the business source but failed to claim the deduction against rental income.

Special and further deductions

- Fees and expenses incurred on the registration of intellectual property, although capital in nature, are allowed a special deduction under Section 14A. The same costs would also qualify for further deduction up to the maximum amount of $100,000. Very few Candidates seem to be aware of this adjustment.

- Of the two non-structural renovation costs incurred during the year, only the amount incurred to improve the office area and restrooms will qualify for special deduction under Section 14Q. Any such costs incurred on upgrading staff accommodation no longer qualifies for Section 14Q deduction. Many Candidates included the costs as mentioned earlier as part of Section 14Q deductions.

  With the introduction of Section 14Q, taxpayers are now given another option (in addition to Section 14H) to claim a deduction of capital expenditure incurred to improve premises for the benefit of their physically handicapped employees. While Section 14H allows a deduction of a maximum amount of $100,000 and requires prior approval, Section 14Q allows a deduction of up to $300,000 incurred over a 3-year block period and no prior approval is required. Past deductions made under Section 14H have no impact on the amount claimed for a deduction on subsequent similar costs under Section 14Q.

Capital allowances

- Many Candidates did not seem to be aware that computer hardware and software qualify for 100% capital allowances claim. They chose to claim a deduction over 3 years. As it is stated clearly that capital allowances claim was to be maximised, marks were docked for claiming at the lower rate. As for the computer modelling software that was purchased under an instalment scheme, capital allowances should be claimed based on the costs repaid during the basis period.

- Many Candidates did not seem aware that the acquisition costs of Intellectual Property Rights can only be claimed over 5, 10 or 15 years. Thus, despite stating that the cost of the Intellectual Property Right acquired during the year was to be claimed over 15 years, Candidates claimed deduction over 3 years.

Income from non-trade sources

- Interest on fixed deposit is taxable only upon maturity of the deposit. It should be noted that if the deposit was terminated prematurely, the bank or finance company would only repay the principal sum. Thus, the amount taxable should be $32,400. Not many Candidates seem to be aware of this.

- The foreign interest derived in Country X is deemed remitted to Singapore when the foreign income was used to finance the retrenchment pay-out to employees stationed in Country X. As the total foreign interest earned to-date was $30,000 and the retrenchment pay-out was many times that amount, the total foreign interest income deemed remitted and to be brought to tax should be $30,000, not just $6,000 as many Candidates subjected to tax.

- Against the taxable rental income, deduction of the property maintenance expense and ceiling works should be taken, which not many Candidates did.

- The investment property which generated the rental income qualified for Industrial Building Allowances ("IBA"). As it was sold during the year, balancing adjustment has to be made as any allowances claimed previously may need to be clawed back (balancing charge) where the sales proceeds exceeded the building's tax written down value or further allowances to be claimed (balancing allowance) where the sales proceeds are less than the tax written down value.

  Although most Candidates could work out the balancing adjustment, the following errors were noted:

  - The building's actual purchase price qualifies wholly for IBA so long as not more than 10% of the building is used for non-qualifying purposes. As only 7% of the building was used for purposes other than manufacturing, it can be safely taken that the entire purchase price can be claimed for IBA. Some Candidates restricted the qualifying cost to 93%.

  - Annual IBA is granted only if the building is still in use on the last day of the basis period for YA 2020. Since it was sold during the year, no annual allowances ("AA") can be claimed in YA 2020. As such, to determine the tax written down value, only 11 years of AA have been claimed.

  - As mentioned previously, the balancing adjustment seeks to claw back any excess capital allowances claimed previously. In this case, the balancing adjustment resulted in a balancing charge, but the actual charge exceeded the total allowances claimed previously. Hence, the balancing charge will need to be restricted. Not many Candidates made the restriction.

  - As the building derived income from the non-trade source, the balancing charge should be included as part of non-trade income.

Corporate tax rebate

- A few Candidates calculated the corporate tax rebate based on chargeable income whilst some others used the rate of 15%.

Question 4

Both parts to Question 4 were poorly attempted. **Part (a)** required Candidates to work out the loss items for the parent company, Company K, which was in the business of making investments (i.e. a Section 10E company). For such companies, investment income like rental income would be treated as trade sourced income and the company is entitled to claim capital allowances (including on plant and machinery). Any unabsorbed trade loss or unabsorbed capital allowances will be forfeited as they do not qualify for carry back, carry forward nor group relief. Only unabsorbed donations can be utilised to carry forward for a maximum of 5 years or group relief. Very few Candidates seem familiar with the rules. Additionally, some Candidates omitted to claim a deduction of the qualifying donation at the rate of 2.5 times.

Part (b) required Candidates to address how the loss items of Company K, Company X and Z **arising from YA 2020** can be utilised. The options to be considered would be to carry forward to YA 2021 and then carry back to prior years and transfer to qualifying companies under the group relief scheme.

Those who attempted the question fumbled when trying to explain Company K's options, which is due to Candidates not knowing the rules applicable to Section 10E companies as described above. Although Section 10E companies cannot transfer out their unabsorbed capital allowances and trade losses, they can accept loss items from qualifying companies to reduce **any assessable income** the Section 10E company may have. Some Candidates had Company K absorb the loss items from other companies in the group even though it is clear that Company K could not take in any loss items since it had no assessable income for YA 2020.

For **Company X**, many Candidates focused on the carry forward of YA 2017 unabsorbed trade loss when their focus should be on YA 2020 unabsorbed trade loss. The options to be considered would be group relief and carry forward and carry back. Some Candidates could explain that group relief is not available due to the common parent company, Company K, not having a minimum shareholding of at least 75% in X. What was left out was when the condition needed to be met – the last day of the basis financial year.

For the carry-back option, not many seem to know that for YA 2020 unabsorbed capital allowances and trade losses, businesses were able to carry back to three (3) immediate preceding Years of Assessment (enhanced carry-back option). This enhancement was announced in Budget 2020.

Candidates are also expected to address the relevant conditions to be met and confirm if the conditions were indeed met. In this case, the minimum 50%

shareholdings test, identification of the common shareholder and how the said test is met needs to be included in the answer. The test essentially requires the shareholdings of the **ultimate individual shareholders** to remain at least 50% as at the relevant comparison dates. In the case of shareholders that are publicly listed companies, how do we ensure this condition is met given the practical difficulties? By ascertaining if the shareholder company was a subject of any merger or takeover exercise between (and including) the two relevant comparison dates. Most Candidates did not address this. Some Candidates also did not know that the shareholdings test required under group relief and carry forward/carry back are entirely separate and distinct. Very few Candidates addressed the carry forward option.

For **Company Z**, the only options available were group relief and carry forward. Hardly any Candidate discussed the carry forward option. Although group relief is available, the number of loss items available for transfer had to be compared to the claimant company's assessable income which had to be pro-rated. This is because Company Z's (transferor) basis period for YA 2020 was a shorter period than Company Y's (claimant company) basis period for the same YA.