SINGAPORE CA QUALIFICATION (FOUNDATION) EXAMINER’S REPORT

MODULE: Singapore Taxation (TXF)

EXAMINATION DATE: 12 December 2017

Section 1
General comments

The performance of the second centralised Taxation module (TXF) examination of 2017 showed a slight deterioration in the pass rate. The examination format 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. Despite no change to the format and the release of the suggested solutions to the mock examination paper and the June 2017 examination, the quality of the answers submitted were not significantly better than the previous two examination sessions.

While most Candidates demonstrated sufficient technical competency to succeed in the current examination, a significant number were still not able to do so and failed the examination.

It is essential that Candidates prepare well for the examination through reading, comprehending, and applying the relevant sections from the i) 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, as well as the financial press in relation to emerging trends and current issues.

It is recognised that 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 strongly encouraged not to spot questions. Neither should Candidates make a mockery of the examination by doing away with proper analysis of the information given in the questions. It was observed that a number of Candidates took a chance that they would score some marks by including every item of income and expense in their answer to Question 1. Candidates should 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 making inferior decisions.

Section 2
Analysis of individual questions

Question 1

The corporate tax question centred on a company incorporated in Singapore, which continued to be at least 50% owned by the founding shareholders after the sale of part of their shareholding to another company. However, after the divestment, the principal activities of the company changed from product distribution to manufacturing.

For Part (a), Candidates were required to ascertain if the unabsorbed capital allowances from the Year of Assessment 2015 (YA) could be deducted from the taxable profits derived in YA 2017. Every Candidate could comment on the need to pass the shareholdings test which requires the common ultimate individual shareholders to continue to hold at least 50% of the shares on the relevant comparison dates. Most Candidates could identify the comparison dates by narrating the basis of arriving at the dates but the actual dates of 31/12/2015 and 1/1/2017 were not stated in the answer. This raises questions on whether Candidates could actually apply their ‘knowledge’ or were regurgitating information in their ‘cheat sheets’. The need to satisfy the business continuity test was not raised by many Candidates and of those who raised it, quite a number stated that the business continuity test was satisfied because by 31/12/2015, the claimant company had already switched to the manufacturing business. This was an incorrect conclusion. The unabsorbed capital allowances arose from the product distribution business. Since the business in the YA the unabsorbed allowances were to be deducted is manufacturing, the test is thus not satisfied.

Part (b) required Candidates to compute the minimum tax liability of the Singapore-based manufacturing company for the YA 2017. 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 was still 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/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. The question also required Candidates to digest the information given and be able to relate information from varied sources to a particular tax adjustment, where necessary. Thus, in the current examination, Candidates had to be able to identify that some of
the expenses related to the non-trade sources of income from dividends, interest, and rental and not the manufacturing source. These expenses (interest expense, lease renewal, maintenance, and utilities expenses) had to be removed from net profit first as these expenses were not incurred in the production of trade sourced income. Deduction thereof is subsequently claimed directly from the related non-trade income. A significant number of Candidates did not make this connection. For those few Candidates who did make the correct claim for rental source expenses, most only claimed the maintenance and utilities expense as direct expense and ignored the lease renewal expense.

Candidates could largely determine the taxability of the various receipts and deductibility of most expenses, but many faltered on the following:

- Almost all Candidates could identify that the dividend income from Crystal Clear did not qualify for tax exemption but a few Candidates proceeded to claim relief for the underlying tax suffered in Country B. This relief was not available as the shareholdings in Crystal Clear did not meet the condition required for unilateral relief under Section 50A.

- Excluding the interest expense pertaining to non-trade assets held in fixed deposit (principal amount of $500,000) and investment in Crystal Clear Inc. ($400,000). No Candidate made the interest adjustment using the total assets basis. Some Candidates merely disallowed the entire interest expense.

- The income tax expense of the ex-General Manager was not deductible as the tax was not borne by the company but by the former employee. This was thus not a staff benefit given to the individual but a loan extended which was not recoverable.

- Many Candidates could identify that the engineering fee for site supervision was not deductible being capital in nature but then failed to include it with the underlying cost of the same machine purchased during the year ($900,000) for capital allowances claim.

- A number of Candidates did not seem to understand or were unaware of the tax treatment of private hire cars in Singapore. Generally, such cars are viewed like an S-plated car and the car hire charges should be disallowed. However, IRAS has clarified that where the hirer does not have possession of the hired car and such cars are used as a mode of transport similar to taxis, the car hire charges will be deductible. Hence, the Uber transport charges were deductible whilst the cars hired to ferry overseas visitors were not as the company would have possession of the car for a large part of the day or the week.

- As the interest on late payment was a financial deterrent imposed by trading partners, as opposed to a penalty for breach of any legal requirements, it was a deductible expense. A number of Candidates disallowed the outlay.
A significant number of Candidates could not identify the correct amount of external training costs that qualified for Productivity and Innovation Credit (PIC) enhanced deduction. Most Candidates neglected to take into account the grant received of $6,000.

Many Candidates did not claim the deductible donation correctly. Either the amount qualifying for deduction was computed incorrectly or the rate applied was incorrect (2.5 times instead of 3 times). On this point, Candidates are reminded that the ‘Examination Tips’ email from the SAC should not be ignored.

The struggle to identify expenses qualifying for claim under Section 14Q or capital allowances claim under Section 19 continued in the current examination. A significant number of Candidates included the fire sprinkler system as qualifying expenditure for Section 14Q deduction. Generally, standalone and mechanical equipment which serves a specific function should qualify for capital allowances at the accelerated rate of 33 1/3% unless the question states that such equipment will qualify for the rate of 100% claim. Many Candidates also do not seem to know that the 3-year blocking to determine the qualifying costs deductible under Section 14Q is fixed by the first YA when Section 14Q compliant costs were first claimed. As a result, the 3-year blocking started from YA 2015 for many Candidates instead of YA 2011. This resulted in the unnecessary restriction of the qualifying renovation costs for YA 2017.

Many Candidates were still unsure of how to claim the total allowances on PIC qualifying assets. Quite a few Candidates did not seem to be aware that the base capital allowances should be calculated based on actual costs incurred and it is only the enhanced claim that is subject to the cap limits of $1.2 million for qualifying assets acquired in YAs 2016 to 2018.

The following errors were noted in the land intensification allowances (LIA) computed:

- The land cost was included in the computation;
- The cost of the administrative office was excluded; and
- The total cost qualifying for LIA was restricted to 85%.

The corporate tax rebate was restricted by some Candidates to $20,000 instead of $25,000.

**Question 2**

An individual tax computation was to be prepared for a 45-year-old female taxpayer who holds Singapore Permanent Resident status. She was married to a Singapore citizen male whose taxable income for the same YA was $22,000.

**Part (a)** required Candidates to determine if the training expense incurred under the taxpayer’s sole proprietorship business qualified for PIC cash payout. Most Candidates could answer this question reasonably well although there were a few
Candidates who claimed that the rate of the payout would be 40% when it should have been 60%.

**Part (b)** required Candidates to compute the taxpayer’s tax liability for YA 2017. 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, rental income, 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 and deduct qualifying expenses from the respective income.

The following errors were noted in the determination of net taxable employment income:

- A number of Candidates subjected to tax only 20% of the cost of the air tickets for the taxpayer to fly to Penang to visit her mother. The concession given to home leave passage is not extended to Singapore citizens or Singapore permanent residents. Candidates should also bear in mind that this concession will be withdrawn from YA 2018 onwards.

- It is not clear why some Candidates determined that the taxpayer had a taxable benefit arising from Central Provident Fund (CPF) contributions in excess of the statutory limits. The question clearly states that CPF contributions by the taxpayer and her employer were within the statutory limits. Is this a result of extreme rote learning?

- A number of Candidates omitted to claim deduction of employment related expenses in transport and entertainment.

For the trade sourced income, a number of Candidates did not seem aware that medical expenses (including dental expenses) of the sole proprietor are not viewed as part of staff medical expense. It is treated as part of personal drawings. Hence, it is not a tax-deductible expense. Some claimed deduction to the extent of the medical expense cap limit of 1% of staff remuneration.

Some Candidates did not bring to tax the interest income from the loan extended to the taxpayer’s friend. As interest on the loan was earned on a daily basis (accrued), the interest for the basis period ended 31 December 2016 is taxable even if the interest is not received yet.

Candidates could claim most of the relevant personal reliefs except for the following:

- The foreign maid levy relief was either omitted or the relief was calculated based on one month’s levy or it was not claimed at the rate of two times.
Parent relief in respect of both in-laws living with the taxpayer was not claimed by many Candidates. Instead parent relief was claimed in respect of the taxpayer’s own parent. The latter dependent did not qualify for relief as she did not live in Singapore.

Handicapped sibling relief for the sister-in-law was not claimed.

As the eldest child was above the age of 16 years old and had not commenced full-time studies in the basis period, the dependent child did not qualify for child relief (neither qualifying child relief (QCR) nor working mothers’ child relief (WMCR)). Thus, child relief could only be claimed for the second to fifth order children. For WMCR, the rates of claim were to be at 20% and 25% and subject to an overall cap per child of $50,000.

- Most Candidates did not include the trade source in the determination of the taxpayer’s earned income or the WMCR was calculated based on statutory income.
- Some Candidates did not include the QCR claim under the taxpayer and instead indicated that the relief would be made under the husband’s tax return. As the husband’s taxable income was only $22,000, it would be more tax efficient for the wife to claim maximum reliefs.

Question 3

There were two parts to the GST question. **Part (a)** required Candidates to complete the GST return for the quarter ended 31 December 2016 for a GST registered company carrying on a business of selling jewellery and providing jewellery repair services. In this respect, a template was provided to help Candidates work out the values of taxable (standard and zero-rated) and exempt supplies as well as the value of taxable purchases before transferring the values to the return.

Many Candidates did not identify the value of the zero-rated supply arising from repair services carried out overseas correctly. The value of $5,000 was used instead of $6,500. The cost of the air ticket was a taxable purchase except that the supply was zero-rated and thus there was no input tax to be claimed. On the other hand, the overseas accommodation cost was an out-of-scope supply.

Many Candidates could not determine correctly the input tax payable on the import of non-investment grade gold and semi-precious stones. Some Candidates excluded the cost of the materials imported or claimed input tax on the insurance and freight only.

Many Candidates did not determine the value of the exempt supply from the residential property lease based on the annual value of the property. Others forgot to calculate the exempt value on a 3-month basis.
As the washing machine was used by an employee and such staff benefit is viewed by IRAS as not for business purposes, no input tax credit would be allowed in respect of the washing machine acquired.

There was no supply made in respect of the late payment interest paid for the CPF Board as this was a penalty imposed for breaching a legal obligation. A number of Candidates indicated that this was an exempt supply made by the company.

The donation of jewellery resulted in business goods being given away for no consideration. Hence a deemed supply arose especially since input tax was paid and claimed on the costs of the jewellery given away. A number of Candidates did not address this transaction.

**Part (b)** was not well attempted. Many Candidates mentioned the $200 GST exemption threshold in respect of goods given away for free but few Candidates could state the basis for input tax claim and far fewer made any reference to IRAS' current view on staff benefits (close nexus test). Candidates are advised to read section 3.5 of the IRAS e-Tax Guide: *Fringe Benefits (2nd edition)* for application of the close nexus test.

**Question 4**

This question tested Candidate’s knowledge and application of rules pertaining to carry back and group relief. **Part (a)** required Candidates to determine if the aforementioned reliefs could be utilised and **Part (b)** required the tax computations to be done using the said reliefs in specified entities. Both parts of this question were poorly attempted by most Candidates as they either did not have sufficient time to attempt the question or they let themselves down by their poor understanding of the reliefs being tested.

Although it was clearly stated under **Part (a)** that Candidates need only comment on the utilisation of Adventure Outdoor’s loss, a number of Candidates included the parent company’s loss in their answer. As the parent company was an investment holding company, its loss is a non-trade loss that cannot qualify for group relief. Some Candidates did not have a good understanding of the ‘shareholdings test’ under group relief using the Common Parent route.

The tax computations required under **Part (b)** were done poorly due to the following:

- Candidates seem unable to prepare the tax computation when it does not start with the net accounting profit. They seem not to understand or recall how the adjusted profit is arrived at. Their order of set-offs was haphazard. Thus, instead of deducting the current year’s capital allowances first from adjusted profits, the loss items from previous years or loss items transferred under group relief provisions were deducted first.

- The order of set-off between group relief and carry back was not done correctly.
| Many Candidates did not seem to know that the loss company could transfer its available loss items to multiple companies. Many transferred to only one entity. |