

## SINGAPORE CA QUALIFICATION (FOUNDATION) EXAMINER'S REPORT

**MODULE:** Singapore Taxation (TXF)

**EXAMINATION DATE:** 11 June 2021

### **Section 1**

#### **General comments**

The examination continues to be conducted online, and Candidates seem to have adapted well to online examinations. The current examination format remained unchanged, a restricted open- book format with an Appendix containing information relating to tax rates, rebates, personal reliefs, and allowances provided. In addition, Candidates were allowed to bring in one (1) A4-sized double-sided cheat sheet and a blank scratch paper to the examination.

The following were noted from the performance of the current cohort:

- Most Candidates attempted all four (4) questions, although some Candidates did not submit their answers to the qualitative type questions. Candidate's performance on the computational (Question 1(a), 2(a) and 4(b)) and GST question (Question 3(a)) were mostly competent, although many answers still showed gaps in Candidates' basic tax knowledge.
- The answers to the qualitative questions (Question 2(b) and 4(c)) continue to be poor, showing clearly that Candidates' knowledge and understanding of the subject areas tested were superficial or muddled. Consequently, there was a lack of depth and completeness in the answers given, apart from regurgitating rules and conditions.
- Many Candidates have incorporated workings in their answers, making it easier for markers to award marks for correct application as many Candidates continue to commit careless computational or transposition errors.
- Topics tested were those required under the TXF syllabus, but it appears that many Candidates did not study sufficiently. This is exhibited in Question 1(a) as Candidates could not work out the capital allowance claim under Section 19.
- Question 4(c) was the worst-performing question for many Candidates. This stemmed from the Candidates' failure to see how one of the conditions for group relief should be applied to the information given in the question.

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 of understanding 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 corporate tax rebate was claimed when none was given for Year of Assessment 2021 ("YA"). (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 their understanding. Please avoid rote learning as much as possible. Past examination questions should preferably be attempted on their own 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 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 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 at <https://elearn.iras.gov.sg/iraslearning/content/iras/startpage/index.aspx#>.

## **Section 2**

### **Analysis of individual questions**

#### **Question 1**

For **Part (a)**, almost all 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 although this distinction (between deduction as part of adjusted profits or capital allowances) continues to challenge some Candidates. To reiterate, where deductions are allowed under Section 14 (which includes special and further deductions under Section 14) or disallowed under Section 15, such adjustments would determine the adjusted trade profit.

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 given in the question, many faltered on the following adjustments:

### **Non-trade and non-taxable receipts to be removed from net profit**

- The interest on late settlement of accounts is trade-related as it arose from outstanding trade invoices owing by customers. It is also a revenue receipt. Therefore, there is no tax adjustment required.
- The insurance compensation is non-trade related and not taxable as the insurance payout enables the company to make extensive repairs to an area that is not being used in the production of income. The costs relating to this area (Warehouse 1) will not be deductible (see below under **Expenses**).

### **Expenses**

- Some Candidates treated the cash allowance of \$190,000 as part of staff remuneration in determining the quantum of medical expenses allowable. This is incorrect. Cash allowance for staff medical and dental treatments and the staff hospitalisation insurance are treated as medical expenses to be subjected to cap limits.
- Private hire car expenses for cars used in Singapore are not tax-deductible unless such cars are hired together with the driver (i.e. chauffeured private hire cars). Chauffeured private hire cars (i.e. Grab, Gojek and similar such cars) are being used like public modes of transportation. In the current paper, only the car is hired, and thus, the car hire charges are to be disallowed as required under Section 15. This is so even where the car is hired for business usage only. Most Candidates disallowed the car hire charges for the car used by the family members of Mr Hero Wong, but that for the car used by Mr Wong was not. This is incorrect.
- Interest expense is deductible where the loan is used for a purpose that acquires income. Thus, for the loan that was used to purchase the company van, the interest expense is deductible as the van is being used in the company's business of trading in medical supplies. It is used to generate trade sourced income, and thus, no tax adjustment is required. Some Candidates treated it as a capital expense; this is incorrect.

The interest in respect for the repayment of interest-free shareholder's loan should be deductible if the original shareholder's loan was used for income-generating purposes. In this instance, it was used to purchase shares in another company and on-lent to another party. If the shares produced dividend income and the loan was interest-bearing, the interest expense on the refinancing loan would be deductible against the related dividend and interest income.

- As pointed out earlier, the expenses relating to Warehouse 1 are not deductible as the expenses are not incurred in the production of income; Warehouse 1 has been left idle since 1 April 2019, the beginning of the basis period for YA 2021. Whilst many Candidates disallowed the rental and maintenance expense of \$95,000, the repairs and rectification expenses of \$106,000 were subjected to varying adjustments. Some disallowed the cleaning and repainting expenses of \$23,000 only, while others claimed Section 14Q deduction on the replacement of the fire sprinkler system and non-structural electrical and flooring/tiling works. The entire amount of \$106,000 is not deductible, and none of it qualifies for Section 14Q deduction as the area was not used for business purposes.

### Special and further deductions

- Given the foregoing, only the non-structural renovation costs of \$96,000 incurred on the re-configuration of business premises will qualify for special deduction under Section 14Q. In addition, for costs incurred in YA 2021 (and YA 2022), the qualifying Section 14Q compliant costs can be deducted over 1 year instead of 3 years. The 1-year write-off should be opted for in this case as the company is in a tax-paying position.

### Capital allowances

- Many Candidates did not seem to know how to work out the capital allowance claim under Section 19. There were two (2) allowances to be claimed under Section 19 – initial allowance at 20% of the **cost incurred during the basis period** and annual allowance on the remaining 80% of **qualifying cost to be claimed over the prescribed useful life under the Sixth Schedule** (i.e. 6 years in this case). As the van was purchased under hire purchase term, the capital repayment during the year would qualify for an initial allowance of 20%. This would be equivalent to 12 months of monthly capital repayment of \$6,400 (\$160,000/25 instalments). However, the actual qualifying cost of the van is \$190,000. Thus, an annual allowance of 80% of \$190,000 (i.e. \$152,000) should be deducted over each of the 6 years of useful life the van is in use at the end of each year. Many Candidates omitted the initial allowance claim, while others claimed an annual allowance based on the total qualifying cost of \$190,000 over 6 years. Nothing in the question suggested that the company did not wish to claim the initial allowance.
- The tables and chairs acquired in the financial year 2019 would qualify for a 1-year write-off as the cost of each set is not more than \$5,000. This would mean that a 1-year write-off on 8 sets costing \$28,800 would have been claimed in YA 2020. The remaining cost of \$7,200 can be claimed over 3 years (i.e. \$2,400) in YA 2020. Since the remaining unclaimed cost (i.e. tax written down value) carried forward to YA 2021 still relates to low-value assets where the unit cost does not exceed \$5,000, the remaining cost of \$4,800 (\$7,200 - \$2,400) may still qualify for 1-year write-off in YA 2021 but the acquisitions of similar assets in the basis period for YA 2021 must be taken into consideration to ensure the total claim under Section 19A(10A) stays within the maximum allowed of \$30,000. Many

Candidates claimed the one-off claim of \$28,800 in YA 2021, which is incorrect and created a consequential error for low-value assets acquired in the basis period for YA 2021.

- Many Candidates omitted to claim capital allowances on the sprinkler system installed in the office premises. The system qualifies as plant and machinery as it serves a specific function –to put out fires. For qualifying costs incurred in YA 2021, companies have the option to claim capital allowances over 2 years at the rate of 75% in YA 2021 and 25% in YA 2022. As the company is in a tax-paying position, it should opt for a 2-year write-off instead of a 3-year write-off.
- The chairs and cabinets acquired in YA 2021 would qualify for a 1-year write-off subject to a maximum claim of \$30,000. Any remaining costs would qualify for a 2-year write-off. It was noted that most Candidates could make a claim correctly under the rules of Section 19A(10A), although the combinations opted for may not be the most tax-efficient.

#### **Income from non-trade sources**

- The interest income from the loan to the Singapore subsidiary was correctly brought to tax by most Candidates. However, many Candidates omitted to claim the interest expense incurred on the refinancing loan related to the financing of the loan extended to the subsidiary. Where the deduction was claimed, many Candidates did not realise or failed to bar the deduction of the net interest deficit from other income. The net interest deficit is not deductible as it is not a trade loss.
- Likewise, many Candidates failed to claim the deduction of the interest expense related to financing the acquisition of shares in LMC, which produced dividend income during the year. However, the dividend, being foreign-sourced, was not remitted to Singapore during the basis period. Thus, the net dividend surplus would not be subjected to Singapore tax, although many Candidates indicated that the dividend was exempted from Singapore tax. It will be exempted only when the dividend is remitted to Singapore, and the conditions for tax exemption are met in the basis period when the dividend is actually remitted.

#### **Chargeable Income**

- The company qualifies for tax-exempt income under the start-up tax exemption scheme as 20% of the shares in the company were held by Hero Wong, an individual, and YA 2021 is the last of the company's first three Years of Assessment (YA). As a result, some Candidates claimed exempt income under the partial tax exemption scheme.

For **Part (b)**, almost all Candidates could explain that the fall in the headline tax rate to 14% would result in the dividend no longer qualifying for tax exemption. However, very few Candidates addressed the ways to mitigate the adverse tax impact.

## Question 2

Question 2 is a 2-part question centred on Nigel and Sunshine Quek. Nigel is a Singaporean and just returned to Singapore from Shanghai. He is tasked to head a regional office based in Singapore.

**Part (a)** required Candidates to work out the income tax liability of Nigel for YA 2021, showing clearly the net taxable income from his employment and rental source. This part was answered competently by many Candidates, although the following errors were noted in many of their answers:

### Employment source

- Some Candidates were not able to work out correctly the number of months of employment income/benefit derived. It is 7 months for salary, rental car benefit and the cash allowance for the hired car running expenses. The accommodation in the rental apartment was only 6 months as Nigel and his family were put up in a serviced apartment for the first month.
- A cash allowance of \$10,000 was given to Nigel to help defray his expenses in relocating to his home country to commence employment. The cash allowance is taxable in full. However, quite a few Candidates' answers did not bring it to tax, and likely may have mistaken it with relocation passage; the latter is not subjected to tax. This extended to expatriate employees only.
- Only the children's medical and dental coverage by Nigel's employer is a taxable benefit. The coverage for Nigel is not taxable as all employees were provided with similar benefits. As Nigel contributed \$4,000 to the children's medical and dental coverage provided by his employer, the taxable benefit should exclude the employee's contribution.
- The car benefit provided to Nigel comprised 2 components. Whilst the car hire charges and monthly office car park charges (component 1) were paid for by the employer, all other running expenses like petrol and ERP charges will be borne by Nigel, with the monthly cash allowance (component 2) of \$150, which the employer was providing. Hence, the charges borne by the employer will be taxable on Nigel using the formula prescribed by Inland Revenue (IR), and the cash allowance of \$150 for 7 months will be taxable in full. In addition, although Nigel can claim a deduction of his out-of-pocket expenses incurred on transportation in the discharge of his employment duties, none of the \$490 can be deducted as it was incurred on a private hire car which is prohibited under Section 15.
- The school fees are taxable in full based on the actual fees paid during the basis period; there is no need to pro-rate the fees as Nigel's child remained a student throughout the basis period, and there is no information provided that the fees are refundable.

### Rental source

- The question clearly stated that Nigel would like to claim expenses relating to his rental source using the simplified basis prescribed by IR. The majority of Candidates could work out the deductible expenses under the said basis, but a small number of Candidates did not seem to be aware of it. Under the simplified basis of the claim, landlords who are individuals and are not carrying on a rental business can claim deductible expenses at 15% of gross rental income and the actual interest expense incurred.

### Personal relief

The following errors were noted:

- Qualifying child relief (QCR) 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 educational institution at **any time** in the basis period and the child did not derive income in excess of \$4,000 in the same period. As his son was studying full time during part of 2020 prior to his National Service enlistment, Nigel is still entitled to claim qualifying child relief on his son. A number of Candidates claimed QCR on either 1 or 2 children.
- Surprisingly, quite a few Candidates did not claim relief for Nigel's contribution under the Supplementary Retirement Scheme. However, as his contribution was within the cap of \$15,300, it was fully relieved.
- Parent relief can be claimed on up to 2 parents. Further, as the relief is shared equally with his sibling, Nigel can only claim 50% of the total Parent relief on both his parents. A number of Candidates claimed relief at 50% of only one parent.
- As Nigel used part of his upfront bonus to top-up his mother's Central Provident Fund (CPF) Special Account, he is entitled to CPF top-up relief capped at \$7,000.

**Part (b)** relates to Nigel's wife, Sunshine Li, who returned to Singapore in July 2020 together with the couple's youngest child. Sunshine continued to work for her employer in China remotely from Singapore. The question required Candidates to explain the Singapore tax implications of her employment duties towards her overseas employer being exercised in Singapore and the Covid-19 rules pertaining to such an arrangement. Almost all Candidates could narrate the Covid-19 rules but almost none addressed the actual tax implications of Sunshine exercising employment in Singapore.

### Question 3

This question comprises two parts. The GST analysis of transactions given in **part (a)** was well attempted. All Candidates could answer in the format required. Nonetheless, the following errors were noted:

- The interest charged on the loan to the Malaysian subsidiary is a zero-rated supply; most Candidates identified it as exempt supply. The financial service was provided to a company that belongs outside Singapore. Only prescribed financial services provided to a person who belongs to Singapore will be exempted from GST.
- Many Candidates could identify the conversion of the refundable cash deposit received of \$20,000 to an advanced payment as a standard-rated supply. However, many faltered when working out the output GST. As it was stated that no further payment will be required of the buyer until completion of the sale in April or May, the \$20,000 collected is inclusive of 7% GST. The output GST should be determined on a re-grossed basis.
- The purchase of supplies from non-GST registered suppliers should be denoted as out-of-scope as one of the conditions before GST can be imposed was not satisfied. Several Candidates denoted it as standard-rated supply.
- The purchase of furniture for the staff accommodation is a standard-rated supply as the furniture was bought from GST-registered traders. However, as the purchase was for the employee's private consumption, the close nexus test was not met, so the input tax credit was blocked. Many Candidates did not seem to be aware of this.
- All Candidates could correctly identify the GST implications of the cash donation. However, the part on the donation of goods was fraught with errors. Firstly, the two sets of goods donated were purchased in a previous quarter. Thus, the input tax considerations would be taken care of in the previous quarter. In the current quarter ended 31 March 2020, the GST consideration would be on the output tax implication arising from the deemed supply of goods at no consideration. For the goods purchased from non-GST registered suppliers, since no input tax claimed, no output GST needs to be accounted for on the deemed supply. As for the donation of imported goods, output GST on the deemed supply will arise, and the value of supply is based on the original purchase price. The market price of the goods donated has not changed significantly from the purchase price.

Candidates' attempts on **part (b)** were largely reasonable, although some Candidates did not submit their answers. 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 is deemed sourced in Singapore under the said provisions **and** if the income is paid to non-residents of Singapore. In the light of the foregoing, the following conditions required under Section 12(6) will be expected in the answer:

- As the interest amount was income in nature, Candidates need to confirm that the interest was payable on an indebtedness (whether by way of a bank loan or instalment repayment to the supplier) in respect of the purchase of kitchen equipment by the Singapore company.



- The creditor is a company that is incorporated outside Singapore, and which does not have a place of operations in Singapore. Thus, it is safe to point out that the recipient of the interest income is a non-resident of Singapore. Regarding the bank loan from the Singapore branch of a foreign bank, the branch is a non-resident of Singapore as its business is not managed and controlled in Singapore.
- The payment was borne by a company that is a tax resident in Singapore.
- Only the payment to the non-resident supplier will be subject to withholding tax at the final rate of 15%. The interest payment to the Singapore branch will not be subject to withholding tax as it was covered under a waiver granted by IR.
- The deductibility of the interest payments under both scenarios is the same. They are deductible as the interest is payable on loans/indebtedness used to acquire income from the trade source.

#### Question 4

This question was broken up into 3 parts with parts (a) and (b) requiring Candidates to compute the adjusted profit attributable to each partner and the assessable income of one of the partners. Part (c) relates to the utilisation of loss items using group relief.

It is clear from **Part (a)** that many Candidates do not understand the difference between divisible and adjusted profits. To determine the adjusted profit attributable to each of the 2 partners, only the overall divisible profit and some items of income and expenses were given in the question. Many answers given started from a notional net accounting profit number and then worked towards the divisible profit given in the question. Worse, some Candidates' answers did not attempt to reconcile to the stated divisible profit. The divisible profit is the tax-adjusted profit that can be allocated to partners according to the profit-sharing ratio. Thus, the divisible profit is the tax-adjusted profit stripped of partners' appropriations for personal usage (salary, allowances, etc.) and personal expenses. Therefore, by adding back the partners' appropriations to the divisible profits allocated to the respective partners according to the profit-sharing ratio, we can arrive at the adjusted profit attributable to the respective partners. Quite a few Candidates fared poorly for this question part.

Candidates performed much better in **part (b)** as this is more familiar and straightforward. Nonetheless, the following errors were noted:

- Ms Chow was paid an entertainment allowance of \$18,000, and this represents her appropriation from the partnership profits. However, her actual entertainment expenses incurred do not feature in the determination of the adjusted and divisible profits; the actual expenses of \$16,500 are her out-of-pocket expenses. Thus, in arriving at the adjusted profit attributed to Ms Chow, the actual allowance of \$18,000 should be added to her allocated divisible profits. The actual expenses incurred to enable Ms Chow to derive income from the business source

will then be deducted from the adjusted profit attributed to Ms Chow. Unfortunately, not many Candidates claimed the deduction in part (b).

- Very few Candidates brought to tax the partner's share of interest income from Country X that was derived through the partnership. The foreign income was deemed remitted to Singapore as it was used to settle business-related expenses in Country X and tax exemption under the Foreign-Sourced Income Exemption scheme is not available to foreign interest income.
- Many Candidates did not claim deduction of the qualifying cash donations completely. Two cash donations can be claimed by Ms Chow – the actual donation of \$ 3,000 made by the partner herself and her share of the cash donation of \$2,000 made through the partnership.

Many Candidates did very badly for **part (c)**. Partner Gwen currently has an 80% shareholding in JT Furnishings Pte Ltd, a Singapore incorporated company, which was projected to have an adjusted trade loss for YA 2022. Gwen intends to invest in another Singapore incorporated company, Natural Floors Pte Ltd, which was projected to be profitable in YA 2022. The investment in Natural Floors can be made by making JT Furnishings purchase the 100% shareholdings in Natural Floors or by Gwen buying the 100% shareholdings in Natural Floors herself. To enable Natural Floors to have access to JT Furnishings' adjusted trade loss for YA 2022, the investment in Natural Floors must be held by JT Furnishings. For group relief purposes, only Singapore incorporated companies can avail themselves of the relief, and this condition includes having the common shareholder being another Singapore incorporated company. Many Candidates either did not attempt this question or failed to see that by having Gwen hold shares directly in both companies, the group relief provisions are out of bounds even if Gwen's shareholdings in both companies are at least 75%.