



Examiners' report

P6 Advanced Taxation (HKG)

June 2008

This examination was the second diet of Paper P6 (HKG) under the new syllabus. As in the last diet, the format and style of the questions have changed to be more practical and case-oriented; however the requirements of the questions have been structured to be more specific so that an average and 'well-prepared' candidate should be able to follow them.

Section A covered a very broad scope of the syllabus including question 1 on corporation profits tax issues surrounding different modes of business operation, different licensing structures, and alternative financing options. Question 2 was on individual income tax including property tax, salaries tax, personal assessment and stamp duty. Questions 1 and 2 were for a total of 68 marks. Section B comprised 3 questions, of which candidates were to answer 2. These 3 questions were comparatively shorter and more straightforward. Total marks awarded for Section B were 32 and thus candidates need to score average marks from Section A in order to achieve a pass. Candidates should also note that very few marks were allocated to computations or numbers included as part of the answers. This is following one of the objectives of the professional level of examination that candidates are expected to demonstrate their abilities in analysing the questions and presenting their answers with logics and principles, rather than detailed calculations. Candidates should expect this trend to be followed in subsequent diets.

Performance of this paper was not satisfactory. Examiners found that not only for Section A, but performance for Section B was not up to standard. Candidates are advised to be well-prepared for all topics, and should equip themselves with the ability to analyse facts and present findings clearly. In terms of time management, some candidates were found not to have time left to attempt the other two optional questions after answering questions 1 and 2. Candidates are advised to make use of the pre-exam 15 minutes reading and planning time to finish reading all the questions, get a full picture of the facts in questions 1 and 2, understand exactly what the requirements are, identify which 2 optional questions are to be attempted, decide on the priority of the questions to be attempted, and finally, plan their answers and roughly allocate the time to each question.

Specific Comments

Question 1

This question contained a scenario that involved HK and PRC. Candidates should be aware that all the PRC tax information was already given in the question. That said, candidates were not required to give answers on the PRC tax. Suggested answers however have to include both HK and PRC tax aspects for educational purposes. As the case was long, candidates should have focused articulately on the specific requirements of the questions and followed what was being asked.

The average mark scored for this question was very low. Common errors found were:

- quite a lot of candidates simply repeated the facts given in the question but gave no answer;
- very weak discussion on the source rule;
- very few candidates correctly mentioned about dividends to be received by the subsidiary, however rather a lot of candidates focused on capital or stamp duty;
- not many candidates discussed the s.16 deductibility issue of the HK company making royalty payment to the US;
- for the interest-free loan, a lot of candidates only mentioned 'no HK tax impact';
- s.61B was mentioned under item (d);
- a lot of candidates agreed that the losses from the PRC branch could be aggregated with the HK profits and thus net taxable profits would be reduced;
- some candidates considered that due to the 2 years' loss making positions, a branch is considered better than a subsidiary because a branch loss can be offset against profits of the head office; and
- some candidates commented on the accounting differences between a branch and a subsidiary rather than the tax implications.

Question 2

This question was another scenario-based question on individual income tax, covering salaries tax, property tax and personal assessment. In general, performance was comparatively better than question 1. Common errors found were:

- quite a lot of candidates still used 'deductible' to mean 'non-taxable'; or 'taxable' to mean 'non-deductible', which is conceptually incorrect;
- a lot of candidates forgot to give ending to the memorandum;
- property loan interest was mistaken as home loan interest;
- utilities are not taxable because receipts are submitted;
- interest can be deducted only if paid to bank, not to relatives;
- a lot of candidates could state the Goepfert principles very well, but made the wrong assumption for HK employment;
- few mentioned the 180 days rule;
- stamp duty on property purchased was ignored;
- quite messy discussion of the source of employment;
- some concluded that it was a HK employment because there was office in HK and MPF was joined; and
- very few candidates were able to mention the nominal/deemed exercise rule upon departure for share options.

Question 3

This question provided a briefing on the outcome of a due diligence report, concerning a potential acquisition of a company, and candidates were required to address the potential tax risks in terms of tax compliance, and address whether clauses in the Share and Purchase Agreement were effective. This question was not attempted by a lot of candidates. The possible reason was that candidates were not sure about what needed to be answered. The aspects on s.70 and s.60 were well-answered, however indemnity was not correctly or properly addressed.

Question 4

This question was split into two parts: the first part on shipping business and the second part on stamp duty. The second part on stamp duty was almost the best answered part of the whole paper. Quite a number of candidates scored full marks on stamp duty. However, performance for part (a) was very disappointing. Section 14 instead of s.23B was mentioned as the charging section. This demonstrated that a lot of candidates simply ignored the special types of business. Candidates are advised that they should at least obtain a basic understanding of the tax position of the special businesses even if they choose not to study the details.

Question 5

This question required the candidates to make a comparison of the tax implications of running a business through an incorporated company with that as a sole proprietor. This question was attempted by most candidates, and the average performance was satisfactory. However, some candidates focused too much on interest deductibility and very few candidates mentioned the difference for profit repatriation. Moreover, quite a lot of candidates incorrectly perceived that the s16 deduction rule only applied to company, but not sole proprietor.