



Examiners' report

F6 Taxation (HKG)

December 2007

This is the first diet of examination under the new syllabus of Paper F6(HKG). In general, the syllabus and coverage of examination are largely similar to those of Paper 2.3H except that all five questions are compulsory. Questions 1 & 2 are for a total of 55 marks and three further questions are 20, 15 and 10 marks respectively, with an approximate 6:4 split requirement for computation and narrative respectively.

Most candidates attempted all five questions although there was some evidence of poor time management. Question 5 was found the worst answered as well as the most omitted by those who did not attempt all questions.

As expected, satisfactory performance was found in Questions 1 and 2, in particular the computational parts.

Common errors include the fact that workings to computations were at times difficult to follow. This was due to either the poor display of the logics, or lack of clear labeling of which part of questions the answers were relating to. Many candidates still failed to start a question on a new page and 'tick' the question numbers correctly on the covers of the answer books. Using confusing terminologies are still common in this paper, e.g. 'non-taxable income' was wrongly termed as 'deductible income' and 'non-deductible expense' was wrongly termed as 'taxable expense'.

Question 1

This 25-mark question examined an individual's salaries tax. Most candidates managed to score high marks for this question. Many candidates did score full mark on the tax computation for YA2005/06 in part (c). However, some candidates combined their answers to (a) and (b) together by applying Goepfert principles to the case. This may in some cases cause some marks to be lost if the candidates did not present the fundamental general principles as required under (a). Candidates are therefore strongly advised to read the requirements of the questions carefully. Other common errors were found. For example:

- failure to distinguish 'office' from 'employment';
- failure to address the principles applying to source of 'office' at all;
- out of the 3 Goepfert principles, the most important factor of place of residency of the employer was mistaken as 'the least important';
- failure to exclude share option and director fee from the time apportionment formula in the tax computation.

Question 2

This question is on the subject of profits tax and the majority of the marks are attributable to profits tax computation. However, the performance on this question is less satisfactory than expected. On the depreciation allowance calculation, some candidates listed out different categories of assets instead of 20% or 30% pools of assets. This is an error of fundamental concept and is not acceptable. Other common errors found in the tax computation are as follows:

- compensation income was either wrongly treated as non-taxable or wrongly spread over 5 years
- brought forward losses were offset against tax payable rather than assessable profits
- brought forward loss of \$630,000 was wrongly used rather than \$1,180,000.
- no breakdown or workings were shown for interest income added back
- tax treatments for exchange gain/loss were messy

Performance in part (b) was not good, and performance was particularly poor in part (c). A lot of candidates obviously have not read the requirements carefully and wrongly assumed that the question asked for record-keeping requirements. Some candidates repeated the requirements for preparing audited financial statements which have no relevance in tax regime. In some cases where candidates did correctly present a profitable position in the tax computation under (a), they still could not give a correct answer under (c). For those who did correctly mention the notification obligation of chargeability, the answer was too short to score higher marks under this part. As there were 4 marks available for this part, some elaboration of the answer was required.

Question 3

This question was on the subjects of partnership and personal assessment; and the whole question required computations. These topics have been frequently examined before, and so examiners did expect a very good performance on this question. However, the outcome was a bit disappointing. Some did score full or nearly full marks, but some others did make certain errors or mistakes which are fundamentally unacceptable. This included the inability to do the allocation of profit/loss amongst partners. Not all candidates managed to show that loss of a partner would lapse upon his withdrawal from the partnership.

For part (b), the salary of \$120,000 from partnership was wrongly included in the computation. Virtually none of the candidates could get the calculation of approved charitable donations perfectly right. Some candidates split the married personal allowance into two ie \$100,000 for each of husband and wife. This indicates that the fundamental concept of a personal assessment for a couple was not sufficiently well known.

Question 4

This question comprised two parts, one on the topic of interest expense deductibility and the other on the topic of non-resident receiving HK sourced royalty income. In general, the performance of this question was satisfactory. Examiners believed that the major reason was that these two topics were common topics in nearly every diet, and thus candidates did spend enough effort in studying these areas. One of the common errors found was that for interest payable to banks, candidates answered that interest was deductible because banks were taxable on the interests. Whilst this statement can't be incorrect in the context of Hong Kong, this is not the correct rationale for the bank interest to be deductible. Candidates confused all the conditions under s16(2) and did not get their logic clear.

For part (b), it was found that some candidates did not read the requirements carefully, and wasted time discussing the tax implications of the HK company paying the royalty expense, and the tax consequences of selling the patent.

Question 5

Question 5 was on the topic of tax depreciation covering the very fundamental principles surrounding building, plant and machinery, and items on replacement basis. Despite the fact that these are the fundamental aspects of the topic on tax depreciation, the performance on this question was extremely unsatisfactory. This question was the worst answered, and was the one omitted by those who did not attempt all the questions. The apparent reason was that candidates for this paper tend to avoid studying theories or fundamental principles or concept. With the change in the examination requirement that all questions now become compulsory, candidates are strongly urged to cover every topic of the syllabus. Given that Paper F6H is at fundamental level, it is to the advantage of the candidates to study all the aspects of the syllabus so as to prepare themselves for advancing to the professional level.