



Examiners' report

P6 Advanced Taxation (HKG)

December 2008

As in the previous diets under the new syllabus, the questions in this paper are practically set and case-oriented, with the requirements of the questions broken up as specific as possible. An average and 'well-prepared' candidate should be able to follow and obtain a pass. Section A covered a very broad scope of the syllabus including Question 1 on corporation profits tax issues and Question 2 on individual income tax. Questions 1 and 2 were for a total mark of 68. Section B comprises 3 questions of 16 marks each, and candidates had to choose two of these to answer. These 3 questions are comparatively shorter and more straightforward. Total marks awarded for Section B are 32 only and thus candidates need to score good marks from Section A in order to get a pass. Candidates should also note that very few marks are awarded to computations or numbers included as part of the answers. 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 that this trend would be followed in subsequent diets.

Performance of this paper was not as satisfactory as expected. Given that the style of questioning and the coverage of syllabus are not inconsistent with prior papers, better performance was expected. Question 4 was the least attempted and poorly answered question probably because the topic of change of accounting date was not too often examined. 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, better performance was observed for this diet, indicated by most candidates who attempted four questions. Candidates are advised to make use of the pre-exam 15 minutes reading and planning time to finish reading all the questions, develop a full picture of the facts in Questions 1 and 2, understand what exactly 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 answers by allocating sufficient time to each question.

Specific Comments

Question 1

This question contained a scenario whereby a taxpayer attempts to achieve tax results by altering the accounts. Candidates should learn the integrated relationship between accounting treatment and tax treatment. Weak answers were found in parts (b), (c) and (d), but recommendations in part (e) given by most candidates have been found reasonably addressed. The question on interest deductibility is a hot topic and thus, most candidates are able to obtain high marks here. Before highlighting the common errors below, examiners have found that quite a few candidates at this level are still confused between 'taxable' and 'non-deductible' (or 'non-taxable' and 'deductible'). At this level of examination, it is not acceptable to find statements like: income is deductible (instead of non-taxable) or expense is taxable (instead of non-deductible).

Other common errors found were:

- many candidates simply repeated the facts (especially the accounting treatments) given in the question but gave no answers which are tax-related;
- mixed up 'badges of trade' with 'totality of facts'
- only mentioning the 6 headings under badges of trade without elaborating the meaning or application to the case
- most candidates provided overly simple answers to part (b), by stating that the revaluation gain is capital in nature and thus not taxable. Detailed explanation of the rationale was absent. Candidates should have noted that 9 marks have been allocated to this part and should have elaborated their answers to justify these marks.
- part (e)(ii) re funding by interest-free loan, most candidates simply answered no interest was paid. Strictly speaking, this is not a tax answer.
- most answers on part (e)(ii) have focused on the tax impacts on Smart Ltd only, but failed to address the tax impacts on Mr Smart.

- a lot of answers started well with the with report format but were found to have no ending or conclusion, thus missing professional marks
- part (d) was found to be weak in answering s61B impact on carrying forward the tax loss

Question 2

This question was another scenario-based question on individual income tax, covering salaries tax, property tax and personal assessment. Tax compliance obligations were examined. In general, performance was comparatively better than Question 1.

Common errors found were:

- candidates still used ‘deductible’ to mean ‘non-taxable’; or ‘taxable’ to mean ‘non-deductible’, which is conceptually wrong;
- as in Q1, a lot of candidates forgot to give ending to the letter;
- most candidates correctly answered HK sourced employment but surprisingly, they applied time-apportionment – indicating that they are wrong in basic concept
- Goepfert principles are used for determining the source of ‘employment’ NOT source of ‘income’
- personal assessment should not include Diana Ltd’s profit
- no rental value was calculated because residence was not located in HK – wrong concept
- personal assessment was confused with joint assessment
- stamp duty on leasing property was ignored
- some candidates have mistaken that the letter only applied to part (a)
- for tax compliance obligations, only s51(2) was mentioned
- some answered that tax returns must be submitted 18 months after commencement of business, which was not correct

Question 3

This question examined the concept of contract processing as opposed to import processing, in the context of HK taxation regime. However, it was found that most candidates were not able to distinguish the two, or explain correctly the rationale for the difference. Most candidates discussed in length the source of trading profits instead of manufacturing profits, whilst some other candidates simply stated all the different source rules for markers to pick. The overall performance of this question was not satisfactory.

Question 4

This question was the least attempted and poorly answered. Change of accounting date is indeed not often examined, but it is in reality one of the common tax issues encountered in the tax practice. Candidates who chose to attempt this question were mostly found to have performed poorly in other questions. Candidates were unable to state the year of change and preceding year correctly. Application for advance ruling is a new topic, but it is by no means a new practice. Moreover, there are no difficult technical provisions to be learnt. .

Question 5

This question examined the tax treatments of various common termination payments. Principles examined are straightforward and common, but disappointingly, performance was not as good as expected. S11D(b) was ignored by most candidates, as a result of which, most recommended the taxpayer to receive the bonus after 31 March of that year. Housing benefit received after cessation of employment was not taxable, because no income was derived during that period to enable rental value to be calculated; NOT because the taxpayer was no longer the employee. Interesting but unrealistic recommendations were found, e.g. advising the taxpayer to change the nature of payment (from housing to compensation for loss of office; or from bonus to share option). Ethical issues should be considered by candidates. The tax treatment for the second batch of share options was not well explained.