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# Answers

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Cases are given in the answers for educational purposes. Unless specifically requested, candidates are not required to quote specific case names to obtain the marks. Only the general principles involved are required.

**Section A**

1 A  $10,000 \times 12 \times 80\% \times 15\% = 14,400$

2 C

3 D

4 A	A	B	C	Total
Salary	14,000	10,000	–	24,000
Balance	(17,000)	(17,000)	(17,000)	(51,000)
Loss	(3,000)	(7,000)	(17,000)	(27,000)
Transfer to PA	3,000	–	–	3,000
Loss c/f	<u>–</u>	<u>(7,000)</u>	<u>(17,000)</u>	<u>(24,000)</u>

5 B

6 A  $(200,000 + 10,000 - 40,000) \times 10\% = 17,000$

7 C

8 C  $1,500,000 \times 0.5\% = 7,500$

9 A

10 B  $150,000 \times 3/15 = 30,000$

11 C

12 B

13 D	2013/14	HP 30%
	Cost	100,000
	IA $(20,000 + 5,000 \times 6) \times 60\%$	(30,000)
		70,000
	AA	(21,000)
		49,000
	2014/15	
	IA $(5,000 \times 10) \times 60\%$	(30,000)
		19,000
	AA	(5,700)
	WDV	13,300

14 D

15 B  $RV = (800,000 - 2,700) * 10\% = 79,730$   
 $800,000 + 79,370 - 2,700 = 877,030$

2 marks each

30

Section B

Marks

1 Alex and Annie

Personal assessment computation 2014/15

	Alex \$	Annie \$	
Salary	–	192,000	0·5
Net assessable value from leased property	–	504,800	0·5
Proprietorship profits (net of ACD limited to 35%) (320,000 – 112,000)	208,000	–	1
Share of partnership profits	<u>300,000</u>	–	0·5
	508,000	696,800	
Less: Mortgage interest	–	<u>(280,000)</u>	0·5
		416,800	
Approved charitable donations transferred from spouse 260,000 – 112,000 = 148,000, limited to 35% of 416,800	–	(145,880)	1·5
Contributions to mandatory provident fund (maximum)	–	<u>(17,500)</u>	0·5
		253,420	
Loss from property trading	–	(253,420)	1
Loss transferred from spouse (330,000 – 253,420)	<u>(76,580)</u>	–	1
Reduced total income	<u>431,420</u>	<u>0</u>	
Joint total income		431,420	0·5
Married person's allowance		<u>(240,000)</u>	0·5
Net chargeable income		<u>191,420</u>	
Tax payable by Alex		<u>20,541</u>	0·5
Tax payable by Annie		<u>0</u>	0·5
Correct treatment of items which require no adjustment: dividend of \$1,000 and AA Ltd's profits of \$40,000.		<i>0·5 mark each</i>	<u>1</u>
			<b><u>10</u></b>

2 Watch Manufacturers Recreational Club

- (a) A club is deemed to be carrying on a business if less than half of its gross receipts on revenue accounts (including entrance fees and subscriptions) are received from members who are entitled to vote in general meetings (24(1)). Only if a club is deemed to be carrying on a business will it be subject to profits tax. 2
- In the case of Watch Manufacturers Recreational Club for the year ended 31 March 2015:
- Total receipts = \$1,998,075 + \$780,900 + \$456,675 = \$3,235,650
- Receipts from voting member = \$1,998,075, i.e. 61·75% of total receipts 1
- As the Club received more than half of its gross revenues from voting members, it is deemed not to be carrying on a business and is therefore not chargeable to profits tax. 1
- 4
- (b) Although the Club is not chargeable to profits tax, it is still liable to property tax in respect of rental income from non-members. 0·5
- Property tax payable = \$386,175 x 80% x 15% = \$46,341 1·5
- 2
- (c) A trade association is a body of persons which is formed for the purpose of furthering the trade interests of its members. 0·5
- A trade association is deemed to be carrying on a business if more than half of its receipts from subscriptions are from persons who either claim or would be entitled to claim their subscriptions deductible under s.16(1) (s.24(2)). A trade association which is deemed to be carrying on a business is subject to profits tax on the whole of its income, including entrance fees and subscriptions. For this purpose 'subscription' refers only to recurrent payments and does not include founders' contributions and entrance fees (*CIR v Far East Exchange Ltd*). 3

**Marks**

A trade association which is not deemed to be carrying on a business will be subject to property tax on any rental income received.

0.5  
4  
10

**3 Andrew**

**(a) Property tax computation for the year of assessment 2014/15**

	\$	
Rental (\$45,000*12)	540,000	1
Premium (\$180,000*12/24)	90,000	1
Repairs borne by tenant	25,000	1
Assessable value	<u>655,000</u>	
Less: Rates paid by landlord (\$6,000*2 + \$7,500*2)	(27,000)	1
	<u>628,000</u>	
Less: 20% statutory deduction	(125,600)	0.5
Net assessable value	<u>502,400</u>	
Property tax at 15%	<u>75,360</u>	0.5

Correct treatment of items which require no adjustment: rental deposit of \$90,000; government rent of \$9,600; management fees of \$36,000 and bank interest of \$280,000.

*0.5 mark each*  
2  
7

**(b) Explanations:**

- (1) The property agency fee for handling the lease is deemed to be covered by the 20% statutory deduction and thus is not separately allowed as a deduction. 0.5
- (2) Repairs relating to the property are regarded as the liability of the landlord. In this case, the repair cost was shared by Andrew and the tenant. The part shared and paid by the tenant is deemed additional consideration earned by the landlord and assessable to property tax. 1
- (3) Although the tenant has defaulted in rental payment since January 2015, no bad debt deduction will be allowed to Andrew for the year 2014/15 on the basis that the property was still under lease and the outstanding rental payment remained as 'consideration payable' to Andrew. Therefore, the rental in arrears is still part of the assessable value, until the debt has been proved as bad and irrecoverable. 1
- (4) The fact that the tenant has sub-let the property for a rental does not affect the property tax liability of Andrew. The implications of sub-letting the property rests with the tenant, not with Andrew. 0.5

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**4 Alan and HKC Ltd**

HKC Ltd as Alan's existing employer is required to fulfil the following compliance reporting obligations in respect of Alan's resignation from his employment:

- (1) An employer is required to notify the Commissioner of Inland Revenue (CIR) in writing of the cessation of employment of an employee at least one month before the cessation (s.52(5)). A shorter period of notice may be accepted if the employer is not aware of the date of cessation at least one month before it occurs. 1

The official cessation date of Alan's employment is 30 June 2015. His last date in the office being 5 June 2015 is not relevant. Strictly speaking, HKC Ltd is therefore obliged to inform the CIR of the cessation of Alan's employment by 31 May 2015, which is the date that Alan submitted his resignation. As it would not be possible for HKC Ltd to anticipate Alan's resignation in advance and file the cessation notice on the same date as the resignation, the IRD is likely to be prepared to accept a shorter period of notice from HKC Ltd, provided that the cessation notice is filed within a reasonable and practical timeframe. HKC Ltd is advised to file the cessation notice in respect of Alan's employment as soon as practicable. 2

- (2) When an employee is about to leave Hong Kong after the cessation of employment for a period longer than one month and the employer is aware of such intended departure, the employer is required to notify the CIR in writing of the departure and the expected date of departure at least one month before the intended departure (s.52(6)). A shorter notice period may be accepted if the CIR deems it reasonable.

1

Since HKC Ltd is aware of Alan's intention of leaving Hong Kong for more than one month, it is obliged to report Alan's intended departure and the expected date of that departure to the IRD. This report should be filed at least one month before Alan's intended departure date. In practice, HKC Ltd may include this departure information in the cessation notice, which (as stated in (1) above) should be filed as soon as practicable after receiving Alan's resignation. However, given that Alan's last date in the office is 5 June and his intended departure date is unknown, there is a risk that the cessation notice may not be filed in time prior to Alan's departure from Hong Kong. HKC Ltd is therefore advised to seek clarification from Alan as to the date of his departure from Hong Kong, and to report that information to the IRD as soon as possible. Failure to report the departure of an employee without a justifiable reason may be subject to challenge by the IRD and a penalty may be imposed.

3

- (3) When an employer has given notice of the expected departure of an employee (under s.52(6)), the employer must not pay to or on behalf of the employee any money or money's worth, without the CIR's written consent, within one month of giving the notice (s.52(7)).

1

Given that HKC Ltd is aware of Alan's intended departure from Hong Kong for more than one month, HKC Ltd is also obliged to retain any payment to be made to Alan until he has cleared all his Hong Kong tax liabilities and the CIR has given consent to the release of the money. The maximum period of money retention is one month. In complying with the retention requirement, HKC Ltd is protected from any action which may be brought against it by Alan for non-payment. Failure to comply with these obligations would cause HKC Ltd to be subject to a fine at level 3, i.e. \$10,000.

2

10

5 George

Salaries tax assessment  
Year of assessment 2014/15

	\$	
Salary (80,000*12)	960,000	0.5
Travelling allowance (5,000*12)	60,000	0.5
Reimbursement of removal expenses	12,000	1
Passage allowance	20,000	0.5
	<u>1,052,000</u>	
Time apportionment:		
HK: $(100 + 91 - 16) \text{ days} + 16 * 175 / (365 - 16) \text{ days} = 183 \text{ days}$		3
Taxable: $1,052,000 * 183 / 365$	527,441	1
Rental value at 10%	52,744	0.5
Less: Rent paid (1,000 *12)	<u>(12,000)</u>	1
	568,185	
Gain on share option		
- On sale $(9,000 - 8,000 * 2 / 10)$	7,400	1
- On exercise $[8,000 * (19 - 15) - 8,000 * 8 / 10]$	<u>25,600</u>	1
	<u>33,000</u>	
Apportioned on time basis $(33,000 * 183 / 365)$	16,545	1
Assessable income	584,730	
Less: Part V allowances		
Married person's allowance	(240,000)	0.5
Child allowance	<u>(70,000)</u>	0.5
Net chargeable income	<u>274,730</u>	
Tax at progressive rates	<u>34,704</u>	0.5
Tax at standard rate $(\$584,730 * 15\%)$	<u>87,709</u>	0.5
Tax payable	<u>34,704</u>	0.5

Correct treatment of items which require no adjustment: reimbursement of medical expenses of \$38,000 from insurance company, \$2,000 paid and borne by George, and annual premium of \$5,000 paid by Hopewell.

*0.5 mark each*      1.5

15

## 6 Digital Technology Ltd

## Profits tax computation for the year of assessment 2014/15

Basis period: 1 February to 31 December 2014

0.5

	\$	\$	
Loss for the year		(41,880)	0.5
<i>Add:</i> Donation	188,000		0.5
Depreciation	331,000		0.5
Loss on sale of China listed shares	30,000		0.5
Incorporation fee	4,000		0.5
Legal fee on setting up the company	40,000	593,000	0.5
		<u>551,120</u>	
<i>Less:</i> Depreciation allowance for machinery and plant	186,760		0.5
Commercial building allowance	100,000		0.5
Dividend from HK listed shares	20,000		0.5
Interest income – HK\$ deposit	19,000		0.5
Prescribed fixed assets – computer laptops	176,000		0.5
Energy-saving lighting (123,000*20%)	24,600	(526,360)	1
		24,760	
<i>Less:</i> Approved charitable donation (limited to 24,760*35%)		(8,666)	1
Net assessable profits		<u>16,094</u>	
Profits tax at 16.5%		<u>2,655</u>	0.5

Correct treatment of items which require no adjustment (candidates are NOT required to prepare the following table in their answers). Marks will be awarded if they are not adjusted in the tax computation.

Taxable/non-deductible items	\$	Deductible/non-taxable items	\$	
Fee from China customer	1,400,000	Utilities for director's apartment	60,000	
Gain from HK shares	690,120	Regular contributions to pension	64,000	
Loan interest from director	38,000	Rent, rates and utilities for apartment	408,000	
		Interest on bank loan	39,000	
			<b>0.5 mark each (max)</b>	2.5

## Depreciation allowance schedule

	20%	30%	Allowance	
	\$	\$	\$	
Additions:				
Microwave and distilled water dispensers	29,000			0.5
Motor vehicle		232,000		0.5
Initial allowance at 60%	(17,400)	(139,200)	156,600	1
	<u>11,600</u>	<u>92,800</u>		
Annual allowance	(2,320)	(27,840)	30,160	1
WDV carried forward	<u>9,280</u>	<u>64,960</u>		
			<u>186,760</u>	

## Commercial building allowance

	Allowance	
	\$	
Additions – office (\$5m*50%)	2,500,000	0.5
Annual allowance at 4%	(100,000)	0.5
WDV carried forward	<u>2,400,000</u>	

15