Strategic Professional – Options

Advanced Taxation – Malaysia (ATX – MYS)

September/December 2018 – Sample Questions

ATX MYS ACCA

Time allowed: 3 hours 15 minutes

This question paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – BOTH questions are compulsory and MUST be attempted

Tax rates and allowances are on pages 2–4

Do NOT open this question paper until instructed by the supervisor.

This question paper must not be removed from the examination hall.

ATX – MYS

Think Ahead ACCA

The Association of Chartered Certified Accountants

SUPPLEMENTARY INSTRUCTIONS

1. You should assume that the tax rates and allowances shown below will continue to apply for the foreseeable future.
2. Calculations and workings should be made to the nearest RM.
3. All apportionments should be made to the nearest whole month.
4. All workings should be shown.

TAX RATES AND ALLOWANCES

The following tax rates, allowances and values are to be used in answering the questions.

Income tax rates

Resident individual

Chargeable income	RM	RM	Rate %	Cumulative tax RM
First	5,000	(0 – 5,000)	0	0
Next	15,000	(5,001 – 20,000)	1	150
Next	15,000	(20,001 – 35,000)	3	600
Next	15,000	(35,001 – 50,000)	8	1,800
Next	20,000	(50,001 – 70,000)	14	4,600
Next	30,000	(70,001 – 100,000)	21	10,900
Next	150,000	(100,001 – 250,000)	24	46,900
Next	150,000	(250,001 – 400,000)	24·5	83,650
Next	200,000	(400,001 – 600,000)	25	133,650
Next	400,000	(600,001 – 1,000,000)	26	237,650
Exceeding	1,000,000		28	

Resident company

Paid up ordinary share capital	First RM500,000	Excess over RM500,000
RM2,500,000 or less	18%	24%
More than RM2,500,000	24%	24%

Non-residents	
Company	24%
Individual	28%

Labuan entity – income from a Labuan trading activity	
All chargeable profits	3%

Trust body – resident or non-resident	
All chargeable income	24%

Personal reliefs

		RM
Self		9,000
Disabled self, additional		6,000
Medical expenses expended on parents	(maximum)	5,000
Medical expenses expended on self, spouse or child with serious disease, including up to RM500 for medical examination	(maximum)	6,000
Parental care	(each)	1,500
Basic supporting equipment for disabled self, spouse, child or parent	(maximum)	6,000
Study course fees for skills or qualifications	(maximum)	7,000
Lifestyle allowance		2,500
Spouse relief		4,000
Disabled spouse, additional		3,500
Child – basic rate	(each)	2,000
Child – higher rate	(each)	8,000
Disabled child	(each)	6,000
Disabled child, additional	(each)	8,000
Childcare (below six years old)	(maximum)	1,000
Breastfeeding equipment	(maximum)	1,000
Life insurance premiums and contributions to approved funds	(maximum)	6,000
Private retirement scheme contributions, deferred annuity premiums	(maximum)	3,000
Medical and/or education insurance premiums for self, spouse or child	(maximum)	3,000
Deposit for a child into the National Education Savings Scheme	(maximum)	6,000
Contribution to Social Security Organisation (SOCSO)	(maximum)	250

Rebates

Chargeable income not exceeding RM35,000	**RM**
Individual – basic rate	400
Individual entitled to a deduction in respect of a spouse or a former wife	800

Capital allowances

	Initial allowance (IA) Rate %	**Annual allowance (AA) Rate %**
Industrial buildings	10	3
Plant and machinery – general	20	14
Motor vehicles and heavy machinery	20	20
Office equipment, furniture and fittings	20	10
Agriculture allowance		
Buildings for the welfare of or as living accommodation for farm employees	Nil	20
Other buildings used in the business	Nil	10
All other qualifying agricultural expenditure	Nil	50

Real property gains tax (RPGT)

	Companies	Individuals – non-citizens and non-permanent residents	All other persons
	Rate %	Rate %	Rate %
Category of disposal			
Disposal within three years after the date of acquisition	30	30	30
Disposal in the fourth year after the date of acquisition	20	30	20
Disposal in the fifth year after the date of acquisition	15	30	15
Disposal in the sixth year after the date of acquisition or thereafter	5	5	0

Goods and services tax (GST)

Standard rate	6%

Stamp duty

Rates of duty under the First Schedule
Conveyance, assignment, transfer or absolute bill of sale

	Rate %
Sale of property	
For every RM100 or fractional part thereof:	
On the first RM100,000	1
On the next RM400,000	2
On the excess over RM500,000	3
Sale of company shares	
On every RM1,000 or fractional part thereof	0·3

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Question 1 begins on page 6.

Section A – BOTH questions are compulsory and MUST be attempted

1 You are a tax assistant in Tax Firm which has the ABC group as one of its clients.

The holding company, ABC Sdn Bhd (ABC), operates an established oil palm plantation, milling the fresh fruit bunches into crude palm oil. ABC sells its entire crude palm oil output to its wholly-owned subsidiary, DEF Sdn Bhd (DEF), to be refined into speciality oils for the Malaysian food industry. Both ABC and DEF are very profitable companies, close their accounts annually to 30 September, and have no unabsorbed losses or unabsorbed capital allowances brought forward.

A few days ago, your tax partner met with the group managing director of the ABC group and learned that the group is planning to carry out research and development (R&D) to enable them to process and recycle the waste products from the mill into high grade poultry feed. The production of poultry feed in Malaysia is encouraged by the Malaysian Investment Development Authority (MIDA), and it is therefore listed as a promoted product.

If this proves to be successful, the ABC group sees scope for further R&D activities for both ABC and DEF arising from other plantation by-products (such as fronds and timber) and speciality oils.

The ABC group intends to spend RM20 million in total on the first project in year one as follows:

		RM'000
R&D business	– purchase of research equipment and facility	3,000
	– manpower and fees to carry out the R&D	4,000
Poultry feed business	– New factory premises and plant and machinery for production of the poultry feed	13,000

ABC is seeking advice from Tax Firm regarding how best to carry out the project within the ABC group, and also the impact of this choice on a future disposal of the R&D and/or poultry feed business.

This morning, you received an email from your tax partner regarding the ABC group.

Extract from your tax partner's email

Please draft a report to the chairman of the ABC board of directors addressing the following issues:

(a) R&D activity

Explain the relevant tax incentives available if the R&D is carried out:

– by ABC itself; or

– by a new Company X incorporated solely to carry out R&D work to cater for the research needs of ABC initially, and subsequently DEF as well. Company X would be a 100% subsidiary of ABC.

For this part (a), assume that Company X will:

– charge an R&D fee of RM4 million to ABC; and
– will be profitable after 12 months of operation.

(b) Production of poultry feed

Explain the relevant tax incentives available if the production of poultry feed is undertaken:

– by DEF as a diversification project under the Income Tax Act; or

– by another new Company Y incorporated as a 100% subsidiary of ABC, which intends to apply for incentives under the Income Tax Act or the Promotion of Investments Act.

– For this part (b), assume the poultry feed business will take 36 months of operation to become profitable.

(c) Tax savings

Illustrate the tax impact of the R&D activity and the poultry feed production by computing the potential tax savings for the ABC group in year one of the project under each of the alternative strategies in parts (a) and (b).

You should assume that all companies in the ABC group pay tax at a rate of 24%.

Extract from your tax partner's email (continued)

> **(d)** Recommendations
>
> Recommend, based on the relative tax treatment and tax savings identified in parts (a), (b) and (c), which company should undertake the R&D work and which company should undertake the production of poultry feed.
>
> **(e)** Future disposal of R&D business and/or poultry feed business
>
> Advise whether your recommendations would change if ABC were planning to dispose of the R&D business and/or the poultry feed business in the fifth year of operation.

Required:

Prepare the draft report to the chairman of the ABC Sdn Bhd board of directors as instructed by your tax partner.

The following marks are available:

(a) The tax incentives for the R&D activity; (7 marks)

(b) The tax incentives for the production of the new product of poultry feed; (6 marks)

(c) Computation of potential tax savings for parts (a) and (b); (8 marks)

(d) Recommendations of which ABC group company should undertake the R&D activity and which should undertake the poultry feed business; (6 marks)

(e) Changes to your recommendations if an exit is planned for the fifth year of operation. (4 marks)

Professional marks will be awarded in question 1 for adopting a logical approach, the appropriateness of the format and presentation of the report, and the effectiveness with which the information is communicated. (4 marks)

(35 marks)

2 The tax manager of Tax Firm received a telephone call on 2 December 2018 from Ms Dei, who is seeking confirmation of the correct tax treatment for several property disposals and also income generated from the provision of design services.

Your tax manager made the following notes during the call:

Notes from telephone call with Miss Dei on 2 December 2018

Ms Dei, a Malaysian citizen and resident, is an architect employed by a firm in Kuala Lumpur. Since 1 January 2016, she has been working three days a week for the firm, devoting the remaining days of each week to her other interests.

Property disposals

Ms Dei purchased her first residential property, a terraced house in Petaling Jaya, in 2009. She redesigned it, furnished it, and lived in it before selling the property in 2016 for twice the price she purchased it for. A real property gains tax (RPGT) return was duly submitted.

In January 2017, Ms Dei reinvested the proceeds from the disposal of the terraced house by purchasing a condominium unit in Kuala Lumpur. Ms Dei has similarly redesigned, furnished the property and has been residing in it. After putting the condominium on the market, Ms Dei has accepted an offer for the property which is RM400,000 more than she paid for it.

In 2010, Ms Dei inherited five acres of agricultural land in Pahang. She has since fenced up the area, built roads, planted 'musang king' durian trees, and enjoyed 'back-to-nature' weekends at the '*Durian Haven*'. A Chinese businessman, who heard about *Durian Haven* through a mutual friend, has recently made a generous offer to buy it. Ms Dei is considering whether to accept this offer.

Ms Dei is unsure how these three property gains should be treated for tax purposes.

Design services

When not working for her employer, Ms Dei designs private residential houses for friends and acquaintances, all from within Malaysia. She maintains a duly-equipped studio-office at her home in Kuala Lumpur for this purpose. She considers the activity to be a hobby which she does by herself, and therefore does not report the amounts received for these designs in her annual tax return. She received gross fees of RM70,000 in YA 2017 and expects that the gross fees in YA 2018 will be RM150,000.

In September 2018, in response to a request for her design services, she made a visit to Singapore to assess the site, receive instructions and agree to the terms of the assignment. She worked on the designs from her studio-office at home in Malaysia. In November 2018, she visited Singapore again to present and hand over the architectural plans, after which she was paid the agreed fee of RM50,000.

Note from your tax manager

I have arranged a meeting with Ms Dei next week, and in preparation for that meeting, I would like you to carry out the following work:

(a) Treatment of property gains

Based on the information provided by Ms Dei on her property acquisitions and disposals:

(i) Present arguments for and against the treatment of the RM400,000 gain on the disposal of the Kuala Lumpur condominium as income from an adventure in the nature of trade. State your conclusion regarding the correct treatment.

(ii) Explain both the capital and revenue arguments in respect of the potential gain from the proposed disposal of *Durian Haven*. State your conclusion regarding the correct treatment.

(iii) In light of the disposals in parts (a)(i) and (a)(ii), reassess the treatment of the gain on the disposal of the terraced house in Petaling Jaya in the year of assessment 2016.

(b) Design service income

(i) Explain how you would support classifying the RM70,000 received by Ms Dei for design services in the year of assessment 2017 as business income.

(ii) Explain why the RM50,000 fee Miss Dei receives for the Singapore work should be treated as part of her business income derived from Malaysia for the year of assessment 2018.

State the expenses incurred by Miss Dei which would likely qualify as tax deductions in arriving at the adjusted income from the business.

(c) With reference to the non-disclosure of her design service income, state the potential offence, if any, committed by Ms Dei for the years of assessment 2017 and 2018, and any action Ms Dei should take to rectify the situation.

Required:

Prepare notes for your manager addressing the work he has asked you to perform.

The following marks are available:

(a) (i) Treatment of the gain on disposal of the Kuala Lumpur condominium. (6 marks)

(ii) Treatment of the potential gain on the planned disposal of *Durian Haven*. (4 marks)

(iii) Treatment of the gain on disposal of the terraced house. (2 marks)

(b) (i) YA 2017 design service income. (3 marks)

(ii) YA 2018 Singapore design service income. (6 marks)

(c) Non-disclosure of income for YA 2017 and YA 2018. (4 marks)

(25 marks)

Section B – BOTH questions are compulsory and MUST be attempted

3 Welcome Hospitality College Sdn Bhd (WHC), based in Penang, specialises in providing hospitality training courses. WHC has a wholly-owned subsidiary, Tanah Sdn Bhd (Tanah), which provides residential accommodation to the students. WHC is registered for goods and services tax (GST) whilst Tanah is NOT a GST registrant.

WHC provides a cafeteria for students to use on its existing campus. Due to the danger arising from several leakages in the gas pipe system in the cafeteria's kitchen, WHC needed to carry out repair work promptly. The contractor whom WHC engaged to do the work informed the company that it would be faster and cheaper to encase the entire gas pipe system in new larger pipes rather than to repair the individual leakages in the system.

As part of WHC's expansion plan, a new campus is being built on land owned by Tanah. Upon completion of the campus property, it will be let out to WHC.

The managing director of WHC has been informed by a friend that the proposed arrangement whereby Tanah will own and let out the new campus property to WHC is not tax efficient. The friend has suggested that WHC should immediately acquire the campus property, and when it is ready, the property will be used for its own college operations, rather than being leased from Tanah. The value of the new campus property is RM20 million.

WHC is unsure how this suggested course of action could improve its tax position, and is concerned that if that were the case, whether this could be viewed as a tax avoidance scheme by the Inland Revenue Board (IRB).

Required:

(a) Justify how the gas pipe system qualifies as 'plant'. Identify whether the encasement of the pipes is capital or revenue in nature and the corresponding appropriate tax treatment. (5 marks)

(b) Explain how Welcome Hospitality College Sdn Bhd (WHC) purchasing the new campus property from Tanah Sdn Bhd (Tanah) could improve the tax position of the group, and whether the proposal could be regarded as a tax avoidance scheme by the Inland Revenue Board (IRB). (9 marks)

(c) Advise the management of WHC of the goods and services tax (GST) implications of the proposed transfer of the new campus property from Tanah to WHC. You should consider whether any reliefs may be applicable. (6 marks)

(20 marks)

4 (a) Mas and her daughter, Linda, are the only shareholders of Selamat Datang Sdn Bhd (SD). The company is engaged in the business of property letting and management in Malaysia.

To expand SD's property portfolio, Mas is proposing to transfer an office block which she owns personally to the company for consideration of RM10 million. Mas acquired the office block eight years ago for RM6 million. The transfer consideration will be wholly satisfied in the form of shares in SD.

Required:

(i) Advise Mas of the real property gains tax (RPGT) implications of the proposed transfer of the office block from Mas to Selamat Datang Sdn Bhd (SD), and a subsequent disposal of the office block by SD. You should consider the applicability of any reliefs and the conditions which apply. (7 marks)

(ii) Suggest how the proposed transfer of the office block from Mas to SD could be altered to achieve a greater tax efficiency on a future disposal of the property by SD. (3 marks)

(b) World Best Berhad (WBB), a listed company on Bursa Malaysia, decided to use its available cash to repurchase its own shares from Bursa Malaysia as the prevailing market price of the shares is below its net asset value. By reducing the number of shares in the market, WBB hopes to improve the market price of the shares. Depending on the market conditions, the repurchased shares may be subsequently resold or cancelled.

Required:

Explain the income tax treatment of the repurchase of World Best Berhad's shares and its subsequent resale or cancellation. (4 marks)

(c) Siew Mai Sdn Bhd (SM) is a trading company which manufactures materials used in the building trade. SM normally prepares its accounts annually to 31 March. The company submitted an original tax estimate of RM120,000 for the year of assessment 2019. On 2 September 2018, before paying the fifth instalment, SM submitted a revised tax estimate of RM180,000.

Earthquakes in other parts of the world have resulted in markedly increased orders for SM's products since September 2018. This will lead to a further higher tax estimate of RM350,000.

Required:

(i) Compute the monthly revised tax instalments for the year of assessment 2019 following the submission of the revised tax estimate in September 2018. (2 marks)

(ii) State the course of action which Siew Mai Sdn Bhd (SM) may take in respect of its revised tax estimate of RM350,000 in view of the unexpected increase in profits. (2 marks)

(iii) If no action is taken under (ii) above, and assuming the final tax liability of SM is RM400,000 for the year of assessment 2019, compute the amount of penalty which will be levied, if any. (2 marks)

(20 marks)

End of Question Paper