Strategic Professional – Options

Advanced Taxation – Malaysia (ATX – MYS)

September/December 2019 – Sample Questions

ATX MYS ACCA EN

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 individuals
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	17%	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	(maximum)	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	(maximum)	3,000
Contributions to approved funds	(maximum)	4,000
Life insurance (public service)	(maximum)	7,000
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)	8,000
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
Computers	20	20
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 agriculture 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	10	10	5

Sales and service tax

Sales tax rate	5%/10%
Service tax 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 next RM500,000	3
On the excess over RM1,000,000	4
Sale of company shares	
On every RM1,000 or fractional part thereof	0·3

Section A – BOTH questions are compulsory and MUST be attempted

1 Assume today's date is 3 December 2019.

You are a tax associate of Tax Firm and one of your clients is Agri-Bijak Bhd (ABB), a Malaysian tax resident plantation company with a large bank of land. ABB has a paid-up ordinary share capital of RM42 million.

On 29 November 2019, your tax manager attended a meeting with Mr Akaun Tan, the newly-appointed finance director of ABB, and took the following notes:

ABB closes its accounts to 30 September each year.

New plantation land

On 8 October 2018, ABB substantially increased its large land bank by acquiring a sizeable plot of land adjacent to existing land they owned.

As a result of the acquisition, ABB incurred the following capital agriculture expenditure during the year ended 30 September 2019:

	RM'000
New planting	4,800
Roads and bridges	1,200
Workers' accommodation	560
Storage buildings	930

Mr Tan has asked whether ABB qualifies for any tax deduction for the above expenditure.

Railway system

The increased acreage made it economically viable to install a railway system to move the agricultural produce within the plantation more efficiently. ABB completed the construction of the railway system at a cost of RM6 million and started to use it for the purposes of the trade on 1 September 2019.

Research and development (R&D)

The R&D department of ABB has been working to develop high yielding seedlings for their own planting. A total of RM1,450,000 (non-capital expenditure) was spent on the R&D in the year ended 30 September 2019.

The expenditure was capitalised and will be amortised over the five-year period from 2019 to 2023. ABB does not intend to apply for any R&D incentives.

Mr Tan would like to know the tax impact of the railway system and R&D expenditure and has requested a draft tax computation for the year of assessment (YA) 2019.

Projections

Mr Tan anticipates that the additional land will lead to an increase in chargeable income in YA 2020 which he has estimated to be approximately RM30 million. On 29 August 2019, ABB had estimated the tax for YA 2020 to be RM18 million.

Mr Tan is seeking advice on the minimum additional tax estimate ABB may report and the deadlines for revising the tax estimate.

Freight charges

As ABB incurs more than RM10 million a year in freight charges, it is planning to establish a shipping company to handle the transportation of produce to its overseas markets.

Mr Tan has heard that there is some preferential tax treatment for Labuan companies. He would like to know the tax treatment of a Labuan shipping company.

Notes (continued)

Replanting expenditure

ABB's board of directors has decided to replant approximately 20% of its total plantation acreage over the next two years. The replanting project will be outsourced to a subsidiary which will charge a fee which is 15% above the prevailing market rate.

The aim of the board of directors is to boost the subsidiary's profitability, and to build its track record, as ABB plans to sell its shares in the subsidiary in five years' time.

Mr Tan believes that the replanting costs are capital in nature, but would like Tax Firm's advice on whether these costs are tax deductible.

Following the meeting, your manager obtained a copy of the draft financial statements for the year ended 30 September 2019, and she has sent you the following extracts:

	Note	RM'000	RM'000
Gross revenue			125,000
Gain on disposal of non-current assets	1		380
Less Expenditure:			
Amortised research expenditure	2	290	
Depreciation	3	469	
Legal and professional fees	4	1,051	
Donations	5	5,800	
Other expenses (all tax deductible)		80,770	
			(88,380)
Profit before tax			37,000

Notes:

1. A balancing charge of RM920,000 has been calculated in respect of the disposal of business assets.
2. The amortised research expenditure represents a 20% amortisation of ABB's R&D expenditure incurred in the year.
3. Capital allowances (excluding the railway tracks and agriculture expenditure) have been computed to be RM475,000.
4. Of the legal and professional fees incurred, RM451,000 related to the acquisition of the additional plantation land. The remainder all relate to trading operations.
5. Of the donations made, RM800,000 was for the provision of free meals to the homeless. The remainder represents cash donations to approved institutions.

Your manager has asked you to write a report to Mr Tan, addressing the following issues:

(a) New plantation land and railway system

(i) Explain why ABB is eligible for agriculture allowances and compute the agriculture allowances for YA 2019.

(ii) Support the case for treating the railway tracks as 'plant', and assuming it is classified as plant, compute the capital allowances available for YA 2019.

(b) R&D expenditure

As ABB will not be applying for a tax incentive for the R&D expenditure, explain the deductibility of the R&D expenditure for income tax purposes, and advise Mr Tan of the adjustments required in view of the accounting treatment.

(c) Tax computation for YA 2019

Produce a draft computation of tax chargeable for YA 2019 incorporating the above items. Remember to start the tax computation with the 'profit before taxation' amount.

(d) Tax estimate for YA 2020

Explain to ABB why it needs to revise its tax estimate for YA 2020, the amount of the adjustment required, the relevant deadlines for making the revised estimate, and the deadline ABB should select.

Assuming the final tax liability is RM30 million, calculate the minimum amount by which ABB must revise its estimate to avoid incurring a penalty.

(e) Freight charges

(i) Explain the tax treatment (all taxes) of how the Labuan shipping company will be treated for tax purposes.

(ii) Advise whether the potential freight payments made from ABB to the Labuan company will be tax deductible.

(f) Replanting expenditure

(i) Describe the income tax treatment of the replanting expenditure.

(ii) Explain the potential issue(s) regarding the proposed replanting contract with ABB's subsidiary, and suggest a best-practice course of action.

Required:

Draft the report to Mr Tan as instructed by your manager.

The following marks are available:

(a) New plantation land and railway system:

(i) Agriculture allowances. (4 marks)

(ii) Why the railway tracks constitute 'plant'. (4 marks)

(b) Income tax treatment of the research and development expenditure. (4 marks)

(c) Draft tax computation for YA 2019. (8 marks)

(d) Tax estimate for YA 2020. (3 marks)

(e) Freight charges:

(i) Tax treatment of the Labuan company. (4 marks)

(ii) Deductibility of freight payments. (1 mark)

(f) Replanting expenditure:

(i) Income tax treatment. (1 mark)

(ii) Potential issues with the contract; and recommendation. (2 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 You are a tax associate of Tax Firm and yesterday a client, Ms Leemah (Leemah), visited Tax Firm's office to meet with you and your tax manager.

The following information was gathered during the meeting:

Leemah resides in Malaysia under the 'Malaysia My Second Home' programme. She has spent nine months in Malaysia in each of 2018 and 2019. She solely supports her only child who became 19 years of age in 2019.

Leemah's investment portfolio comprises the following:

– a rental property in Australia;
– a fixed deposit account with a UK bank;
– units in listed real estate investment trusts (REITs) resident in Malaysia and approved by the Securities Commission;
– shares in companies listed on the Bursa Malaysia; and
– a 50% share in a limited liability partnership (LLP) in Malaysia.

During the basis period for the year of assessment 2019 (YA 2019), Leemah derived the following income and gains:

– rental income from the rental property in Australia, of which RM61,000 was remitted to Malaysia.
– interest equivalent to RM5,000 earned on the deposit account in the UK, which was not remitted to Malaysia. She had deposited her savings in a bank in the UK to defray her child's tertiary education expenses.
– cash distributions from the REITs of RM7,200 (after the deduction of tax at source).
– a gain of RM25,000 on the sale of one of her share investments.
– dividends of RM14,600 from the remaining share investments she has in ten listed companies.
– a share of income from the LLP, whose principal activity is the supply of cheese in the domestic market. As provided for in the partnership agreement, Leemah will be paid a basic salary of RM4,000 a month for her expertise in this field. For 2019, Leemah received a salary of RM48,000 and in 2019 her share of the distribution of profits was RM30,800.

Leemah is currently negotiating to take over a very successful cafe business in Kuala Lumpur, Malaysia, at a cost of RM5 million, funded with a bank loan.

The assets of the business are valued as follows:

	RM'000
Commercial shop lot for the cafe premises	3,000
Plant, equipment and fittings	800
Goodwill	1,200
Total value	5,000

Leemah is unsure whether she should:

– buy the assets and the goodwill, and run the business as a sole proprietorship; or
– acquire the shares of the company which owns the cafe business.

She has asked for Tax Firm's advice on how best to proceed with the acquisition.

After the meeting, your tax manager requested you to carry out the following work:

(a) Investment income

Prepare detailed notes to explain how the income and gains are treated for tax purposes in Malaysia:

(i) Rental income from the property in Australia.
(ii) Interest on the deposit with a UK bank.
(iii) Cash distributions from the REITs.
(iv) Gain and dividends from the shares in companies listed on the Bursa Malaysia.
(v) Salary and distribution of profit from the LLP.

Your notes should include scope of charge, derivation, specific taxing provisions and any other relevant issues relating to the tax treatment of each source.

(b) Computation of tax payable for YA 2019

Based on the information available, prepare Ms Leemah's computation of tax payable for YA 2019.

Your computation should commence with 'gross income' and should indicate by the use of '0' any items which are not taxable.

(c) Acquisition of the cafe business

Compare the tax treatment of acquiring the cafe business under an asset deal with the share deal. For each option, consider the:

(i) classification of the income which arises;
(ii) tax deductibility of the interest expense on the RM5 million bank loan against the respective class of income;
(iii) real property gains tax (RPGT) implications relating to the shop lot;
(iv) capital allowance implication on plant, equipment and furniture.

Required:

Carry out the work as instructed by your tax manager.

The following marks are available:

(a) Tax treatment of each investment source:

(i) Rental income from the property in Australia; (2 marks)

(ii) Interest on the deposit with a UK bank; (2 marks)

(iii) Cash distributions from the REITs; (3 marks)

(iv) Gain and dividends from the shares in companies listed on the Bursa Malaysia; (3 marks)

(v) Salary and distribution of profit from the LLP. (2 marks)

(b) Computation of Ms Leemah's income tax payable for YA 2019. (7 marks)

(c) Comparison of the two options to acquire the cafe business. (6 marks)

(25 marks)

Section B – BOTH questions are compulsory and MUST be attempted

3 **(a)** On 2 January 2019, Azlan, a Malaysian citizen, gifted an apartment to his son, Nazrin, when its market value was RM300,000.

On 13 March 2019, Azlan died and in his will he left a four-acre coconut plantation to Nazrin. The plantation was transferred to Nazrin on 3 June 2019.

The market value of the land on 13 March 2019 and 3 June 2019 was RM1,500,000 and RM1,600,000 respectively.

The acquisition details of the properties which were owned by Azlan are as follows:

Property	Acquisition date	Cost RM'000
Apartment (Note)		
Original purchase price	14 January 1995	100,000
Renovation cost	13 June 2008	30,000
Coconut plantation	5 December 2012	900,000

Note: The market value of the apartment as at 1 January 2000 was RM500,000.

Nazrin replanted the coconut trees on the plantation at a cost of RM71,000 and built a store for RM80,000. On 2 December 2019, Nazrin disposed of two acres of the plantation land together with the store for RM950,000. Prior to the disposal, Nazrin incurred a valuation fee of RM60,000 relating to the valuation of the whole plantation.

Required:

(i) **For the purposes of real property gains tax (RPGT), explain how Nazrin will determine the acquisition dates and deemed cost of the apartment and coconut plantation he acquired from Azlan.** (5 marks)

(ii) **Compute the RPGT liability arising on the part disposal of the coconut plantation by Nazrin.** (5 marks)

(b) Mamak Sdn Bhd (Mamak), a manufacturing company, is planning to construct a new factory in Pahang, Malaysia. The costs of constructing the factory are expected to be as follows:

	RM'000
Design fees payable to a Singapore architect firm (services to be rendered in Singapore)	1,000
Construction cost to a local construction company	10,000
Project management fee payable to its holding company, Rojak Sdn Bhd (Rojak) (Note)	1,500
	12,500

Note: The principal activities of Rojak are investment holding and the provision of management services solely to its wholly-owned subsidiaries.

Mamak has also successfully obtained a grant from the Malaysian Investment Development Authority (MIDA) for the following:

– RM3 million to subsidise the construction of the new factory;
– Up to RM2 million to cover training expenses to upskill the employees.

In addition, Rojak has provided a subsidy of RM200,000 to Mamak to cover its high raw material costs of manufacturing.

Mamak is registered for sales tax but not for service tax.

Required:

(i) Explain the service tax implications arising from the potential costs which Mamak Sdn Bhd (Mamak) will incur on the construction of the new factory. (5 marks)

(ii) State the income tax treatment in relation to the grant and subsidy income received by Mamak. (5 marks)

(20 marks)

4 **(a)** Palm Sdn Bhd, a software development company, closes its accounts to 31 December every year. In relation to the company's tax return for the year of assessment 2016, the following claims for a tax deduction were NOT made:

– a claim for an accrued royalty as no withholding tax had been paid. The royalty was subsequently paid on 15 January 2019 and the relevant withholding tax amount was remitted to the Inland Revenue Board (IRB) on 31 January 2019.

– a claim for the interest expense in respect of a loan from its holding company to finance business operations because the interest only became due for payment on 30 June 2019.

Required:

Explain the actions to be taken by Palm Sdn Bhd to make the appropriate adjustments to correct and update its tax position for the year of assessment 2016. You should also explain the timeframe allowed under the respective provisions to make these adjustments. (6 marks)

(b) Dai Wan Sdn Bhd (DW) manufactures personal computers, and its wholly-owned subsidiary, Siao Wan Sdn Bhd (SW), manufactures electronic notebooks. Both companies have paid-up ordinary share capital of RM10 million.

SW was originally set up to undertake the notebook manufacture following advice from the Malaysian Investment Development Authority (MIDA), to help facilitate its application for pioneer status. SW's pioneer status ended in the year of assessment (YA) 2019.

The tax position of the two companies for YA2019 is as follows:

	DW	SW
	RM'000	RM'000
Unabsorbed tax losses carried forward	15,000	0
Unabsorbed pioneer losses carried forward	0	500
Unabsorbed capital allowances carried forward	5,000	0

DW and SW are projected to have annual adjusted income of RM1 million and RM4 million respectively for the next eight years.

To achieve overall tax efficiency, the group plans to merge SW's notebook manufacturing business with DW. Thereafter, SW is expected to be a dormant company.

Required:

(i) **Explain how the proposed merger of the notebook business with Dai Wan Sdn Bhd (DW) will improve the tax position of the group. Support your explanation with calculations of the tax position before and after the merger.** (9 marks)

(ii) **Consider whether the proposal to merge the business under DW could be regarded as a tax avoidance scheme by the Inland Revenue Board (IRB).** (5 marks)

(20 marks)

End of Question Paper