

Strategic Professional – Options

Advanced Taxation – Malaysia (ATX – MYS)

Tuesday 8 December 2020



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.

Please note that you are not expected to make any reference to Covid 19 or the global economic crisis as a result of this pandemic in your exams. None of the temporary financial or legislative measures implemented as a result of Covid are examinable.

ATX – MYS

Think Ahead

ACCA

The Association of
Chartered Certified
Accountants

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, and for fertility treatment, 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)	2,000
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)

Category of disposal	Companies incorporated in Malaysia; Trustee of a Trust	A disposer who is not a citizen and not a permanent resident or an executor of the estate of a deceased person who is not a citizen and not a permanent resident, or a company not incorporated in Malaysia	All other persons
	Rate %	Rate %	Rate %
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	RM3

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Question 1 begins on page 6.**

Section A – BOTH questions are compulsory and MUST be attempted

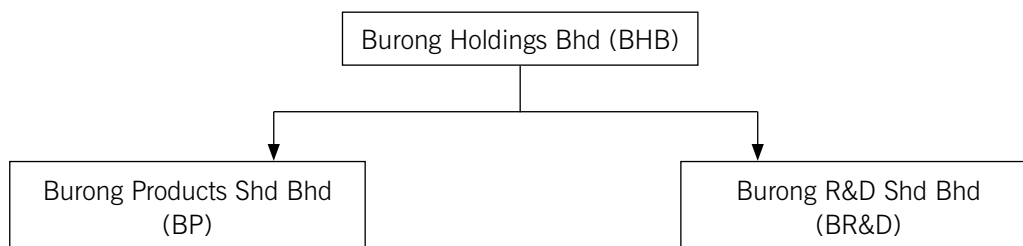
1 Assume today's date is 1 December 2020.

You are a tax associate of Tax Firm and one of the firm's clients, Burong Products Sdn Bhd (BP), requires Tax Firm's assistance with its corporate plans. The relevant details made available to your tax partner by Ms Long, BP's chief financial officer, are as follows:

Corporate exercise information

1. BP, incorporated and tax resident in Malaysia, is wholly owned by the Lee family who are citizens of Malaysia.
2. BP processes raw birds' nests into highly prized ready-to-consume bottled birds' nest essence and related birds' nest products. The tax authorities have confirmed that the activity constitutes 'manufacturing' for tax purposes.
3. BP has been exporting its products to China since 2019. Recent market surveys have indicated significant potential increase in demand in China. BP expects to register annual increases of 60% to 80% in exports for the financial years ending September 2021 to 2023. The value of the increased exports is estimated to be about RM50 million each year.
4. An initial public offer (IPO) will be launched by listing at the Bursa Malaysia in October 2023. The listed vehicle will be an investment holding company, Burong Holdings Bhd (BHB). BHB will acquire 100% of BP and incorporate a new company to carry out research and development (R&D) on birds' nest products. All three companies will be resident in Malaysia and close their accounts annually to 30 September.

5. The corporate structure will be as follows:



6. The IPO is expected to raise RM80 million for BHB and the proposed utilisation is as follows:

	RM'000
Acquisition of 100% shareholding in BP	20,000
Loan to BP	23,000
Acquisition of 100% shareholding in BR&D	7,000
Other investments and reserves	26,000
Operating expenditure	4,000
	80,000

7. Of the RM23 million loan, BP will use RM18 million in October 2023 to build birds' hotels to produce its own birds' nests so that it will not have to heavily depend on raw birds' nests from external suppliers. Birds' hotels are concrete buildings with small windows with a conducive interior environment to attract migratory swift birds to build and maintain their nests therein. These birds' nests are periodically harvested and processed into essence and other products. The tax authorities have confirmed that the production and harvesting of birds' nests constitute a 'manufacturing' activity for income tax purposes.
8. BP will use the remaining RM5 million for R&D services to be provided by BR&D for innovation and improvement of its products over the years of assessment (YAs) 2024, 2025 and 2026.
9. BR&D will utilise RM6 million from its share capital to acquire and install research equipment. Initially it will only provide R&D services to BP.
10. BHB's income will solely consist of dividend and interest from its subsidiaries.
11. Ms Long would like Tax Firm to provide a comprehensive analysis of all the relevant tax issues pertaining to the Burong Group of companies as a result of the proposed plans.

Your tax partner has requested that you prepare a report to Ms Long, addressing the following issues:

(a) Tax incentives available to BP

(i) Explain why BP is eligible for the following incentives and how each incentive measure operates:

- Allowance for significant increase in exports (ASIE) of 30%; and
- Reinvestment allowance.

Remember to highlight the ownership requirement for ASIE.

(ii) As the two incentives are mutually exclusive, explain the importance to BP of timing claims for each incentive measure.

(b) Birds' hotels

Given that the production and harvesting of the birds' nests constitute 'manufacturing', present your arguments for the birds' hotels qualifying as industrial buildings (IBs) and as plant. Explain the difference in capital allowances available for IBs and plant, and recommend the appropriate treatment for BP.

(c) Deductibility of expenditure for BHB

Explain the tax deductibility of the following expenditure to BHB:

- (i) IPO expenditure of RM1.8 million;
- (ii) Annual operating expenses of RM750,000 in maintaining the corporate headquarters for the Burong Group of companies.

(d) Preferred company to claim for R&D incentive

(i) Explain why BR&D is potentially eligible for the status of R&D company, and compute the tax savings for BP and BR&D if BR&D obtains approval for investment tax allowance (ITA) under the Promotion of Investments Act.

(ii) Assuming BR&D qualifies as an R&D company, assess BP's eligibility for the double deduction incentive in respect of the R&D fees it incurs over the three years of assessment, and compute the tax savings.

(iii) Based on the computation of tax savings, recommend which company should claim the R&D incentive. Attach your computations as an appendix to the report.

Required:

Draft the report to Ms Long as instructed by your tax partner.

The following marks are available:

- (a) (i) **Reinvestment allowance and allowance for significant increase in exports.** (8 marks)
- (ii) **Timing of each incentive.** (3 marks)
- (b) **Arguments for industrial buildings and plant, with recommendation.** (5 marks)
- (c) (i) **IPO expenditure.** (1 mark)
- (ii) **Annual operating expenses.** (3 marks)
- (d) (i) **R&D company status.** (4 marks)
- (ii) **R&D fees.** (4 marks)
- (iii) **Recommendation.** (3 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 Assume today's date is 1 December 2020.

You are a tax associate of Tax Firm. Yesterday, your tax director brought you along to attend a meeting with a client, Mr Dinlamza (Din), the chief financial officer of Harimau Sdn Bhd (Harimau). Below are the notes of the meeting.

Notes of meeting

1. Harimau, with an ordinary share capital of RM4 million, operates 23 retail outlets in Malaysia. Harimau closes its accounts annually to 31 March.
2. In the last nine months, revenue has consistently dropped due to competition from online shopping. To remain competitive, Harimau has decided to close five retail outlets by 31 March 2021. The major costs of these closures are estimated to be as follows:

	RM
Loss on sale of store furniture and equipment	1.1 million
Compensation for:	
– retrenched employees	2.2 million
– premature termination of store tenancy contracts	1.8 million
Total	<u>5.1 million</u>

Additional information has been provided in relation to the above costs, as follows:

- All the assets disposed of were acquired and put in use when each of the five outlets were opened, on or after 1 July 2019;
 - The employees retrenched have served with Harimau for less than two years. Compensation of three months' salary will be paid to each of them;
 - There are five separate tenancy contracts terminated, out of a total of 23 tenancy agreements, with duration ranging from three to five years.
3. Harimau had furnished an estimated tax of RM30 million for the year of assessment (YA) 2021 on 28 February 2020. Estimated tax for YA 2022 is expected to be RM20 million because of falling revenue.
 4. Harimau plans to launch its own online sales department. The start-up cost of RM4.9 million will be incurred by 31 March 2021 so that online sales will commence by 1 May 2021.
 5. To drive the online selling activity, Harimau will recruit four software engineers, two from Hong Kong and two locally. The two Malaysian engineers are freelancers with their own practice in Malaysia who will come in for two days a week, while the two from Hong Kong will work full time for Harimau under a two-year employment contract. All four will be Malaysian tax residents.
 6. Din requests Tax Firm to explain all the tax issues relating to the closure of the outlets and the establishment of the online selling activity.

Your tax director has requested you to carry out the following work:

(a) Closure of five retail outlets

(i) Sale of store furniture and equipment

Explain the tax treatment of the loss on sale of store furniture and equipment.

(ii) Retrenchment of employees

Explain the tax treatment of the compensation payable to the employees from the perspectives of Harimau and the retrenched staff.

(iii) Cancellation of store tenancy contracts

Present your arguments for both the capital and revenue nature of the compensation payable.

(b) Starting online selling

Briefly outline the arguments for the start-up costs being treated as capital or revenue in nature.

(c) Estimate of tax

Explain the compliance requirement for YA 2022 with regard to the original tax estimate, the revised tax estimate and their respective timelines and amounts of tax instalment.

(d) Software engineers

Explain the differences between 'contract of service' and 'contract for service', and the respective income tax treatment of the remuneration or fees payable under each category from the perspective of the Malaysian and Hong Kong software engineers.

In addition, state the compliance requirements relevant to Harimau with respect to both categories of engineers.

Required:

Carry out the work as instructed by your tax director.

The following marks are available:

(a) The cost of closing retail outlets

(i) **Loss on sale of store furniture and equipment.** (3 marks)

(ii) **Retrenchment of employees.** (4 marks)

(iii) **Cancellation of store tenancy contracts.** (4 marks)

(b) Online selling start-up costs. (4 marks)

(c) Estimate of tax. (4 marks)

(d) Software engineers. (6 marks)

(25 marks)

Section B – BOTH questions are compulsory and MUST be attempted

- 3 (a)** Margaret and Ben, both Malaysian citizens, incorporated a new company, MB Sdn Bhd (MB), on 2 January 2010. The initial paid-up ordinary share capital of 2 million shares, with a cash subscription price of RM0.50 per share, is shared equally between Margaret and Ben.

MB signed an agreement on 4 March 2010 to acquire industrial land in Klang, Malaysia for RM5 million. The agreement is conditional upon the approval from the State Government as well as the approval of the vendor's shareholders. Approval from the State Government and the vendor's shareholders were obtained on 1 July 2011 and 3 September 2011 respectively. The agreement was completed upon the full payment of the consideration on 1 October 2011.

On 1 August 2011, four million new ordinary shares at a subscription price of RM1 per share were issued to Jeremy, a mutual friend of both Margaret and Ben. The share proceeds were used to partly finance the construction of a factory.

The market value of the factory property as at 1 January 2013 was RM25 million and the other tangible asset of the company was RM10 million.

On 15 June 2019, the company had a one for one bonus issue of ordinary shares.

On 1 November 2020, due to a cash flow problem, Jeremy sold his entire shareholding in the company to Margaret for RM12 million.

Required:

- (i) Explain when MB Sdn Bhd (MB) became a real property company (RPC). Determine the date of acquisition and acquisition price of the RPC shares to each shareholder.**

Your answer should also consider the significance of the market valuation as at 1 January 2013.

(7 marks)

- (ii) Compute the real property gains tax (RPGT) payable in relation to the disposal of MB's shares by Jeremy to Margaret.**

(3 marks)

- (b)** Rasa Sdn Bhd (Rasa) is an engineering company with three wholly owned Malaysian subsidiary companies and one associated Malaysian company with a 25% shareholding. Rasa can nominate one director representation out of four directors in the associated company.

Rasa is a service tax registrant by virtue of it providing engineering services. The revenue from the engineering services is expected to exceed RM5 million annually. The group is looking at centralising its support function whereby Rasa will commence providing group management services to its subsidiary and associated companies. The expected revenue from the management services for the first two years is RM450,000 and RM600,000 respectively and the estimated fee to be charged to the associated company is fixed at RM25,000 annually.

To support one of its engineering contracts, Rasa has appointed a UK company to provide specialised engineering services worth RM800,000. In addition, the company has also appointed Rasa Group Ltd (RGL), a Singapore company, to provide information technology (IT) services to configure its management reporting system. RGL holds a 40% shareholding in Rasa and has the ability to appoint three out of the five directors in the company.

Required:

- (i) In relation to the services rendered and procured by Rasa Sdn Bhd (Rasa), explain whether the service provider and recipients are regarded as 'companies within the same group' for service tax purposes.**

(3 marks)

- (ii) Determine whether the management services to be provided by Rasa would be subject to service tax.**

(4 marks)

- (iii) Determine whether service tax is applicable on the specialised engineering service fee provided by the UK company and the IT services provided by Rasa Group Ltd.**

(3 marks)

(20 marks)

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Question 4 begins on page 12.**

- 4 (a) Badrul, a Malaysian citizen, graduated as an engineer from a local university in 2019 and took a year off before continuing his master's degree in the same university commencing in 2021.

During the calendar year 2020, Badrul has been involved in the following:

- He supports his university lecturer as a part-time tutor. On average, he tutors 20 hours per month, with a monthly fee of RM3,000.
- During his free time, as a hobby, he has developed a health monitor mobile application, which he uses both for his personal use and for sharing with his friends. The innovative application caught the eye of an entrepreneur who intends to commercialise the technology. It is agreed between Badrul and the entrepreneur that a company will be set up to commercialise the technology and Badrul will be given a 20% shareholding in the company.
- Badrul introduced his friend to a manufacturing company owned by his aunt to supply packaging materials. Badrul arranged for his friend to meet up with his aunt and acted as an intermediary to coordinate the deal. To show his appreciation, his friend has given him a luxury watch worth RM30,000.
- Based on the recommendations given by his friends, Badrul borrowed some money from his father to invest in shares listed on the local stock exchange. During the period, he bought three share counters, of which he has sold one share counter in December 2020 but suffered a loss of RM2,000. He continued to hold the other two share counters.

Required:

Explain how the various amounts received by Badrul will be taxed, and include the tax treatment of the loss arising from the sale of shares. (10 marks)

- (b) Cik Po, a Malaysian citizen and resident, created a trust, PoPo Trust (PTrust), for her sister, Pei, and nephews, Keong and Boon, aged 21 and 19 years old respectively. Cik Po's friend, Simon, a Malaysian citizen and resident, was appointed as a trustee of the trust fund. Both Keong and Boon are non-residents as they have been studying in Singapore since the age of 12 years old.

The relevant terms of the PTrust are as follows:

- Pei is to receive an annuity of RM300,000;
- Keong and Boon are to receive 80% of the distributable income in equal proportion while the remaining income is to be accumulated.

The statement of profit or loss of PTrust for the financial year ended 30 September 2020 indicates the following:

	RM'000	RM'000
Dividend income from local companies	1,000	
Interest income from Government bonds	200	
Interest income from fixed deposits	500	
Rental income from letting of shoplots	800	2,500
	8,000	
<i>Less: Expenditure</i>		
Depreciation of investment property	200	
Trustee remuneration	60	
Quit rent and assessments	40	
Accounting fee	100	
Annuity paid to Pei	300	
	(700)	
		1,800

For the financial year ended 30 September 2020, Keong and Boon received a trust distribution of RM720,000 each.

Required:

(i) **Determine whether PoPo Trust (PTrust) is a tax resident in Malaysia and give two examples of the significance of the residence status of the trust for tax purposes.** (3 marks)

(ii) **Compute the tax payable of PTrust for the year of assessment 2020.**

Note: Start your tax computation with the gross income figures, and indicate by the use of '0' any item shown in the statement of profit or loss for which no tax adjustments are necessary. (5 marks)

(iii) **Explain how the trust distribution received by Keong and Boon will be treated for tax purposes.** (2 marks)

(20 marks)

End of Question Paper