# Suggested solution

## Section A

### Question 1

Report to Summer (HK) Ltd

To: CEO, Summer (HK) Ltd

Date: 1 December 2026

Subject: Tax advice on proposed cash-generating measures

We refer to your discussion with our manager, Jenny Ko, discussing the various cash-generating measures proposed by the Company's senior management and their respective Hong Kong tax implications. We provide our advice on the respective issues as follows.

**(a) Mrs Chao's proposal to provide additional funding to the Company**

The major shareholder of the Company, Mrs Chao, intends to inject additional funding into Summer (HK) Ltd (the Company), either in the form of an interest-bearing loan or equity. Given that the funding will be financed by Mrs Chao's personal bank loan, she will seek to secure an interest rate which is comparable to market rate if the funding is injected by way of a loan. The Hong Kong tax implications to both the Company and Mrs Chao are as follows:

**Interest-bearing loan**

Under this option, the Company would incur interest expenses payable to Mrs Chao, and Mrs Chao would earn interest income from the Company.
From the perspective of Mrs Chao, the interest income would likely not be assessable to profits tax in Hong Kong, unless the loan is provided in the course of a money-lending business carried on by Mrs Chao. In the absence of information indicating that Mrs Chao is carrying on a business as a moneylender, the interest income represents an income from personal investment and therefore is not assessable to profits tax of Mrs Chao in Hong Kong.

From the Company's perspective, the major concern is whether the interest expense is Hong Kong deductible in computing its profits assessable to profits tax. The tax deductibility of the interest expense depends on:

1. Whether the loan interest is incurred in the production of assessable profits (s.16(1)): and


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2. Whether the borrowing, being a loan from Mrs Chao who is a person other than a financial institution, generates interest income which is assessable in Hong Kong in the hands of Mrs Chao (s.16(2)(c)); or if this condition fails,
3. Whether the borrowing is used to acquire machinery or plant or trading stock for use by the Company, but the lender is not associated with the Company (s.16(2)(e)).

Assuming that the additional funding from Mrs Chao is applied by the Company in its operations for the purpose of producing assessable profits in Hong Kong, condition (1) is satisfied. However, condition (2) may not be satisfied for the reason that Mrs Chao would not be assessed on the interest income received unless she lends the funds to the Company in the course of carrying on a money-lending business. Whether she could be carrying on a business in extending the loan to the Company is a matter of fact to be decided on the merits of each case. There is no simple rule for deciding on such an issue. We do not have sufficient information for this purpose. If necessary, we would be glad to discuss the matter with Mrs Chao. Condition (3) is also not satisfied as Mrs Chao, the lender, is the shareholder of the Company and thus she is an associate to the Company. In conclusion, the interest expense incurred on the shareholder's loan would not be eligible for tax deduction for profits tax purposes.

It is worth noting that the company should have sufficient assessable profits to offset the interest expense, if it is deductible, in order to obtain current tax savings. Otherwise, the interest expense is a deferred tax deduction to the extent it is not offset by the Company's assessable profits.

**Equity**

Under this option, the potential return to Mrs Chao is dividend income from the Company, if so distributed. Under this scenario, the Company does not incur any regular expense, instead it may declare a dividend as and when the Company becomes profitable.
From the perspective of Mrs Chao, dividend income is not taxable in Hong Kong on the basis that it arises from personal investment which does not fall within any of the tax regimes in Hong Kong.

From the perspective of the Company, dividend payment is neither an expense nor an outgoing, but rather it is an appropriation of profits. As a result, no tax deduction would be secured. Therefore, the Company is not able to claim any tax deduction for the dividend distribution.

In conclusion, under either option of additional funding, the lender, Mrs Chao, is expected not to be taxed on the related income and the borrower, the Company, would not be eligible for claiming any tax deduction.


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Taking into consideration the Company's current problem of a shortage of cash, as well as the neutral tax implications for either option, it would be advisable, from a tax perspective, to proceed with the equity injection such that the Company is not subject to any interest payment or accrual.

**(b) Disposal of warehouse complex**

According to the Inland Revenue Ordinance (IRO), profits arising from the sale of capital assets are excluded from assessment to profits tax. As the complex has been occupied by the Company for its own use since 2008 and the disposal is not driven by a profit-making motive in the absence of evidence proving otherwise, it is reasonable to claim that any profit arising from the disposal is capital in nature and therefore not taxable.

Given that the complex has been used for income-generating purposes, the Company should have been claiming commercial buildings allowance (CBA) during the years in which the complex was in use. For the year of assessment during the basis period of which the complex is sold, a balancing adjustment (either a balancing charge or balancing allowance) would arise. A balancing charge represents the excess of the sale proceeds over the tax written down value and is taxable for the Company. A balancing allowance represents the excess of the tax written down value over the sale proceeds and is tax deductible. For the purposes of calculating the balancing adjustment, only the portion of sale proceeds as attributable to the building element is taken into account. The portion attributable to the land is not eligible for adjustment. Therefore, when the complex is sold as 'land and building together', the sale proceeds need to be apportioned, usually based on the ratio adopted in allocating the qualifying expenditure in the year the complex was acquired. In the event that there is an excess of sale proceeds (as attributable to the building) over the tax written down value leading to a balancing charge, the taxable amount of balancing charge is restricted to the total amount of the tax depreciation allowance (that is, either industrial buildings allowance (IBA) or commercial building allowance (CBA) in this case) which has been claimed by the Company previously. Any further excess is treated as a capital gain which is not assessable under the Hong Kong tax regime.

In the event that the building is demolished before the land is sold, the Company would not receive any proceeds for the building, and thus no balancing charge will arise. On the other hand, even if the Company has a tax written down value for the building but no proceeds, a balancing allowance would not be eligible in this case because the demolition of the building for sale is clearly unconnected with and not in the ordinary course of the conduct of the Company’s trading business. As a result, the Company would not be able to claim any deduction for the balance of tax written down value. In addition, any costs of demolition, if expensed to the income statement, would not be

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eligible for tax deduction for the reason that they are unrelated to the business and are capital in nature.

**(c) Change of accounting date**

When the Company changes its forthcoming accounting date from 31 March 2027 to 31 December 2026, the year of change is 2026/27 on the basis that it fails to make up accounts based on the corresponding day in the year (s.18E), i.e., it fails to make up accounts to 31 March 2027 for the year of assessment 2026/27. The year preceding the year of change is 2025/26. The year 2026/27 is the first assessment year which adopts accounts made up to the new accounting date of 31 December.

The Commissioner will usually take the new accounting year end date, i.e., 31 December 2026, as the ending date of the basis period for the year of change 2026/27. As the Company was incorporated in 2002, it must have commenced business after 1974, and thus it is a 'new' business for this purpose. Therefore, any basis period to be adopted for the year of change should ensure that no profits arising during the life of the business fall out of the profits tax net. However, if the accounts based on the new accounting date cover a period less than 12 months, which is the case of the Company, the IRD should ensure fairness and would only be prepared to adopt a basis period of less than 12 months if the change of accounting date is driven by a compelling reason which is not at the discretion of the taxpayer (e.g. due to a change of shareholding). In the event that the change is driven by other reasons, the IRD is likely to follow a period of 12 months ending on the new accounting date for the year of change. This might result in a duplication of profits being assessed.

It is therefore necessary to check the reasons to justify the Company changing the accounting date. If the change is driven by the intention to drop out a substantial profit from assessment for the year of change, it is unlikely to be accepted as a compelling reason. Based on the information given, it appears obvious that the reason for pushing forward the accounting date from 31 March 2027 to 31 December 2026 is to enable the project profit to fall out of the new basis period for the year of change. In the circumstances, the IRD will likely disagree with the adoption of the 9-month basis period but choose to adopt a 12-month basis period for the year of change, i.e., year of assessment 2026/27, covering the 12 months from 1 January 2026 to 31 December 2026. Since the three-month period from 1 January 2026 to 31 March 2026 has been assessed for the year of assessment 2025/26, the profits arising from this 3-month period would be duplicated for assessment leading to double taxation.

As for the year preceding the year of change, i.e., year of assessment 2025/26, the original basis period ending on the previous accounting date was 12 months from 1 April 2025 to 31 March 2026. Assessment for this year should have already been issued. When


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considered necessary, the IRD is empowered to amend the basis period for this preceding year to the new accounting date if this gives a higher profit for assessment. Therefore, for the preceding year 2025/26, the IRD may recompute the Company's assessable profits for the 12-month period from 1 January 2025 to 31 December 2025 and compare this with the original assessable profits assessed based on the old accounting date. If the recomputed profit is higher, the IRD is empowered to revise the assessment for 2025/26 and seek to impose tax accordingly. Additional assessment may be issued for the additional profits recalculated.

Moreover, we do not agree with the opinion of the finance director that no challenge from the IRD is anticipated. Apart from the risk of certain profits being doubly assessed as explained above, there is also a risk that the IRD may apply the general anti-avoidance provision under s.61A if it considers that the change of accounting date was not for a bona fide commercial reason but for the sole or dominant purpose of obtaining a tax benefit arising from the exclusion of certain profits and deferring such profit to a later year. For this purpose, 'tax benefit' includes deferral of tax liability. It is also worth noting that the onus of proof rests on the Company to justify the change.

Given the above analyses, it is not advisable for the Company to pursue the change of accounting date as a measure to relieve its cash flow problem. Instead, the Company could consider applying for a holding over of its provisional profits tax for 2026/27 if conditions are satisfied.

**(d) Termination of senior manager**

From the facts, the Company has the intention of terminating the employment of a senior manager, Brian, in January 2027, after serving sufficient notice. On top of the last month's salary, the Company would make the final payment representing (i) payment for leave not taken and (ii) bonus entitlement in respect of 2026.

**Deductibility to the Company of the final payment**

From the perspective of the Company, whether the costs incurred on the final payment are deductible for profits tax purposes depends on whether the general deductibility rule under s.16(1) is satisfied and not precluded by s.17 such as capital expenditure. In the case of the final payment made to the departing member of staff, Brian, it is generally deductible to the Company if Brian has been deployed for services rendered for the benefit of the Company with a view to producing the Company's profits assessable to profits tax in Hong Kong. The fact that this is the final payment made upon the termination of the staff member is irrelevant as long as the intention of the payment represents a reward for the staff member's services, which is the case of Brian. This is valid for both payment for leave not taken and the bonus. However, if the payment, or part thereof,

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genuinely carries the nature of a compensation for a loss or damage caused to the staff member, instead of an income from employment or a reward for services, the payment or part thereof would potentially be capital in nature and non-deductible to the Company.

**Taxability of final payment to the employee**

From the perspective of Brian, given that his employment with the Company is a Hong Kong employment, the whole of his income from the employment is chargeable to salaries tax provided that it represents an award for services under the employment. This is the case regardless of whether it comes from the employer or from some other person. Based on the Company's intention to terminate Brian's employment in January 2027, the taxability of each item of the final payments receivable by Brian is analysed as follows:

**1. Payment for leave not taken amounting to $50,000**

Compensation for leave not taken is regarded as income from employment and is assessable for the year of assessment 2026/27. The fact that some leave days being compensated were brought forward from the previous year is not relevant since the amount is not received by Brian until 2026/27, and thus the payment will be assessed in the year 2026/27.

**2. Estimated bonus of $150,000 and potential top-up in April 2027**

A bonus paid for services rendered is a contractual entitlement and is an assessable remuneration under s.9(1)(a). This is the case regardless of the fact that the amount is estimated or may only be quantified and paid at a later date *(D46/98)*. Provided that the amount of $150,000 is paid to Brian during the year of assessment 2026/27, the amount would be included in his assessable income for the captioned year.

As regards the potential receipt of the top-up amount in April 2027, any amount received represents part of the bonus and carries the same nature of assessable remuneration and should be assessable. When income relating to employment is only paid by the employer after the taxpayer has ceased that employment, the income is deemed to have accrued to the taxpayer on the last day of that employment (s.11D(b)(ii)) and is accordingly assessed for that year of assessment in which the employment ceased. As a result, the top-up amount would become part of Brian's taxable income, if there is any and paid to him in April 2027, for the year of assessment 2026/27. Should the notice for salaries tax assessment for 2026/27 have been issued, an additional assessment would be raised under s.60 bringing the top-up amount back into the tax net.


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**Compensation for loss of office**

Brian has made a request that the above final payments are to be aggregated into one lump sum payment and packaged as a 'compensation for loss of office' pursuant to a termination agreement to be signed with the Company. He believed that this would render the final payment to be non-taxable.

Compensation for loss of office was traditionally arguable as not assessable on the grounds that it is a payment for breach of contract rather than a payment for services rendered. For this to be valid, the 'breach' must be a real and identifiable breach, and not a pre-arranged term under the employment contract or represent a payment for past services or a substitute for a reward-type of payment such as a bonus. Based on the Fuch's case (2019), if the 'compensation' is paid pursuant to a term stipulated in the employment contract, the payment becomes an entitlement under the contract rather than compensation for the loss of something and thus would be assessable as income from employment.

It is likely that the IRD is entitled to look beyond the description and ascertain whether it is merely window-dressing to disguise the true arrangements which have been agreed.
In the case of Brian, it is given that the termination of his employment was driven by his age and decreasing productivity rather than by the extinction of Brian's job position. If the Company already served sufficient notice to Brian and cleared the outstanding obligations by making leave payment and bonus entitlement, Brian does not suffer any loss for which compensation should be sought. Unless there is sufficient evidence to prove otherwise, it is likely that the payment, in whatever name, would still be regarded as income from employment and taxable to Brian. Brian's suggestion is considered not effective.

We trust the above has addressed all the related tax concerns. Should there be any questions, please let us know.

Tax Firm


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# Section B

## Question 2

### Eddie

### (a) Exercise of share option

Eddie is entitled to exercise the share option for the remaining 5,000 shares. Upon exercising the option, a deemed gain will be calculated and will be assessable based on the market value of the shares on the date of exercise. If the exercise is effected on 1 January 2027, the deemed gain will be aggregated with his other employment income and assessed for 2026/27. With a salary of $840,000, a share option gain of $35,000 ([5,000 x ($12 – $5)], contributions to the mandatory provident fund of $18,000 and a married person's allowance of $264,000, Eddie will have a net chargeable income of $593,000 ($840,000 + $35,000 – $18,000 – $264,000), and the share option gain will be assessed at the highest progressive tax rate of 17%.

However, if the exercise is effected in April 2027, the deemed gain from exercising the share option will be brought into assessment for the year of assessment in which the exercise takes place, i.e., for 2027/28. Section 11D, which deems post-employment receipts as accruing on the last day of employment, does not apply to share option gains. Given that Eddie has no other employment income, he will have no net chargeable income and the share option gain will be exempt from salaries tax for 2027/28.

In the circumstances, it will be more tax effective for Eddie to exercise the share option in the year following the retirement year, as the deemed share option gain will be absorbed by the Part 4A concessionary deductions and Part 5 allowances and exempt from tax.

### (b) Consultancy fees and gratuity received after retirement

After his retirement, Eddie will sign a consultancy agreement with Brilliant Ltd (Brilliant) and act as its consultant on a fee basis. *Prima facie,* this appointment is self-employment such that Eddie will be assessable to profits tax instead of salaries tax in respect of the fees received. Under s.14(1), profits arising in or derived from Hong Kong from a trade, profession or business carried on in Hong Kong would be chargeable to profits tax. Any expenses incurred in the production of such assessable profits would be deductible against the assessable profits (s.16(1)). The net assessable profits after deduction would be subject to tax at 7·5% on assessable profits up to $2 million and at 15% on any part of the assessable profits over $2 million. Therefore, the estimated profits tax payable by Eddie for the year of assessment 2027/28 will be $12,750 [($200,000 – $30,000) x 7.5%]. Under the profits tax regime, Eddie is not entitled to any concessionary deductions or allowances. Therefore, it is advisable for Eddie to elect for personal assessment, so that

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Eddie's consultancy fees would be aggregated with other income, if any, and, where appropriate, full year Part 4A concessionary deductions as well as Part 5 allowances can be deducted. If personal assessment is elected for 2027/28, Eddie will have no net chargeable income ($170,000 + $35,000 – $264,000), and the assessable profits as well as the share option gain will be exempt from tax.

At the expiry of the consultancy agreement, Eddie may be awarded a gratuity of $40,000. This payment has direct association with the consultancy services performed by Eddie during the period and thus should be regarded as part of his business income assessable to profits tax. In terms of timing of assessment, although the benefit starts to be contingent from the commencement of the agreement, it is only payable at the discretion of Brilliant. More importantly, it will only be brought into Eddie's assessable income as and when it becomes payable to him, and the amount is accounted for as business income of his consultancy business. Hence if it is paid on 31 December 2028, it is assessable for the year of assessment the basis period of which includes 31 December 2028.

**(c) Stamp duty cost - Option one - acquiring all the assets of Anara Ltd**

Conveyances on the sale or transfer of the shop premises, a non-residential property in Hong Kong, are chargeable to stamp duty under Head 1 of the Stamp Duty Ordinance (SDO). The chargeable document is the agreement for sale and purchase (AFS), and it is chargeable to *ad valorem* duty (AVD) at Scale 2 rates ranging from $100 (for a value not exceeding $2 million) to 4.25% (for a value exceeding $20 million) for non-residential properties. The dutiable value is usually based on the transaction price or consideration, unless the consideration is below the market price, in which case the property market value would be used for stamping purposes. Therefore, the stamp duty payable will be $2.125 million (4.25% on $50 million). Where the AFS is stamped, the subsequent formal assignment or conveyance executed in conformity with the stamped AFS will be liable to a fixed duty of $100. The law stipulates that parties to the transaction, the buyer, and the seller, are jointly and severally liable to pay the stamp duty, but in market practice, the purchaser is normally the person to pay.

No stamp duty is payable on the acquisition of other assets.

**Stamp duty cost - Option two - acquiring all the shares in Anara Ltd**

The register of members (i.e., shareholders) of a company incorporated in Hong Kong is required by the Companies Ordinance to be kept in Hong Kong. Hence shares in a company incorporated in Hong Kong are Hong Kong stock as defined in s.2(1) of the SDO. Therefore, the parties effecting the sale and purchase thereof must prepare and stamp contract notes for the sale and purchase and an instrument of transfer: s.19(1) and

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Heads 2(1) and 2(4) respectively. Duty on the contract notes under Head 2(1) is 0·2% of the consideration or market value if applicable; and duty under Head 2(4) on the instrument of transfer is $5.

Stamp duty should be paid on the total consideration of $55 million including the $5 million shareholder's loan assigned (s.24(1)). The fact that a separate assignment deed is executed for the loan assignment is not relevant to reduce the stamp duty payable. The SDO stipulates that all the facts and circumstances affecting the liability of any instrument to stamp duty must be fully and truly set forth in the instrument (s.11l).

Total duty on the contract notes under Head 2(1) is $110,000 ($55 million x 0·2%); and the duty for the instrument of transfer is $5, which is much lower than the amount payable ($2.125 million) if the property, not the shares, were acquired. It is the usual practice that the vendor and purchaser are each liable to pay one-half of the duty.


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## Question 3

### Pearl (HK) Ltd and Pearl (China) Ltd

### (a) Transfer pricing risk to Pearl (HK) Ltd (PHK) in Hong Kong

Based on the Inland Revenue Ordinance (IRO) (Rule 1 under s.50AAF), a transfer pricing risk arises if all of the following circumstances exist:

(i) There is an actual provision between two 'affected persons';
(ii) Participation conditions as defined in s.50AAG apply to the 'affected persons', i.e., the 'affected persons' are associated in terms of management, control or capital;
(iii) The pricing for the provision between the 'affected persons' is not at arm's length; and
(iv) The actual provision confers a potential advantage in relation to Hong Kong tax on an 'affected person', the so-called 'advantaged person'. Based on s.50AAJ, a potential advantage exists if, in general, profit is understated, or a loss is overclaimed.

If the transfer pricing risk is successfully challenged, a transfer pricing adjustment may be made by the Inland Revenue Department (IRD) to re-compute the profit or loss of the 'advantaged person' (circumstance (iv) above) based on the arm's length value for the transaction.

In the case of PHK, the sale of goods made to Pearl (China) Ltd (PCL) (which is its wholly owned subsidiary) (i.e., $120 million) would fall within circumstances (i) and (ii) above. As the sale is priced at 20% above market price, the pricing would be regarded as not at arm's length, meeting circumstance (iii) above. However, instead of conferring a potential tax advantage, the overstated pricing of sale would actually give rise to higher assessable profits to PHK. Taking the 2024 figures as an example, if the sale of $120 million is overstated by 20%, the gross profit of $40 million is overstated by $20 million leading to taxable income being overstated by $20 million too. This should cause PHK to be charged with an excessive profits tax. There is no Hong Kong tax advantage being enjoyed by PHK. As a result, circumstance (iv) above is not met, and PHK is not an 'advantaged person'. Hence, the pricing cannot be challenged by the IRD under the transfer pricing rule and no tax adjustment can be made by the IRD for Hong Kong tax purposes.

While this is a common commercial strategy to shift profits from a high-tax jurisdiction (e.g., China at 25%) to a low-tax jurisdiction (e.g., Hong Kong at 16.5%), it is anticipated that a transfer pricing challenge would be raised by the China tax authority which suffers from an understated tax collected from PCL.

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**(b) Double tax position of the group and relief for Pearl (HK) Ltd (PHK)**

Based on the information provided, PCL will be issued an additional assessment to China corporate income tax of $5 million as a result of a downward adjustment made to the cost base of its purchase from PHK in 2024 from $120 million to $100 million. This is generally referred to as a transfer pricing adjustment. Despite the adjustment only being made to PCL, there is a corresponding effect to PHK as well as the group (PHK and PCL). Given that PHK is being taxed in Hong Kong on the basis of invoiced value for the sale to PCL (i.e., $120 million) whereas the same transaction was only deducted by PCL in China on the basis of adjusted value of $100 million, double taxation arises from the group's perspective. In general, this is 'economic double taxation' (as per DIPN 45) where the profits of one enterprise are adjusted upwards increasing the tax charged on that enterprise in one state (i.e., a primary transfer pricing adjustment), without a corresponding downward adjustment to the tax payable of the associated enterprise in the other state.

Pursuant to the Associated Enterprises article (Article 9} of the PRC-HK double taxation arrangement (DTA), where the commercial or financial relations between two associates residing in each side of the DTA are different from those between independent enterprises, any profits which would have accrued to one of the enterprises but by reason of those relations have not so accrued may be included in the profits of that enterprise and taxed as such. This justifies the tax adjustment made by the China tax authority on PCL. Relating to the position of the other side (i.e., PHK) Article 9 of DTA clarifies that the other side shall make an appropriate adjustment to the amount of tax charged making reference to the other provisions under the DTA and the consultation between the tax authorities of two sides. Therefore, this requires the IRD in Hong Kong to make an appropriate adjustment of PHK's tax and to consult with the China tax authority on the related issue.

Making reference to the Hong Kong domestic tax law (s.50AAN: Corresponding relief involving foreign tax: disadvantaged person), where a Hong Kong taxpayer transacts with a foreign associate residing in a DTA territory, and the foreign associate is an advantaged person such that its income is re-computed based on arm's length basis, the Hong Kong taxpayer is a disadvantaged person who is eligible to be assessed in Hong Kong as if the arm's length basis of the corresponding territory had been adopted instead of the actual transaction value. In the case of PHK, it is empowered by s.50AAN to make a claim to the IRD for a corresponding tax adjustment to its sales value based on the arm's length value adopted by PCL (i.e., $100 million) instead of the actual transaction value of $120 million. As a result, PHK's assessable profit could be revised downward, with an aim to eliminate or reduce the double taxation burden of the group.

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PHK is required to make a claim for double taxation relief pursuant to the Methods for Elimination of Double Taxation article (Article 23) of the DTA. The tax authorities of Hong Kong and China are required by the Mutual Agreement Procedure article (Article 25) of the DTA to consult each other in order to reach an agreement to resolve the double taxation problem. The application for adjustment should be made before the end of two years from the time when the advantaged person's (i.e., PCL's) foreign tax-related adjustment is made, or before the expiry of the time limit for making an assessment/additional assessment under the IRO (i.e. before the expiry of the six-year statutory limit under s.60), whichever is the later. If the transfer pricing adjustment made by the China tax authority was accepted as being correct both in principle and in amount, an appropriate downward adjustment would be made to PHK's income for profits tax purposes under s.50AAN.


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# Mark scheme

## Question 1

### (a) Additional funding

| | |
|---|---|
| Interest-bearing loan | 7 |
| Equity | 3 |

**Maximum 8 marks**

### (b) Disposal of warehouse complex

| | |
|---|---|
| Commercial buildings allowance | 7 |
| Impact of demolition before sale | 3 |

**Maximum 8 marks**

### (c)

### Change of accounting date

| | |
|---|---|
| Basis periods | 2 |
| Possibility of IRD adopting 12-month period | 4 |
| Implications | 4 |
| General anti-avoidance rule risk | 3 |
| Advice | 2 |

**Maximum 12 marks**

### (d) Termination of senior manager

| | |
|---|---|
| Company | 3 |
| Employee | 6 |
| Compensation for loss of office | 4 |

**Maximum 12 marks**


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**Professional skills marks:**

**Communication**

General report format and structure (use of headings, sub-headings and an introduction)

Style, language and clarity (tone of report response, presentation of calculations, appropriate use of the tools, easy to follow and substantive amount of content)

**Analysis and Evaluation**

Clear and logical approach taken to the evaluation of the different forms of additional funding under consideration

Comprehensive evaluation of the taxability and deductibility of each item of Brian's termination package from the perspective of both Brian and the Company

**Commercial Acumen**

Advice on the tax implications of the disposal of the warehouse complex is appropriate and raises valid commercial points

**Scepticism**

Reasons for the IRD's position are explored and the Finance director's opinion re no expectation of IRD challenge to change of accounting date is challenged appropriately

**Maximum 10 marks**

**Total 50 marks**


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**Question 2**

**(a) Exercise of share option**

| | |
|---|---|
| Treatment on exercise | 3 |
| Conclusion | 2 |

**Maximum 4 marks**

**(b) Consultancy fees and gratuity**

| | |
|---|---|
| Profits tax implications | 4 |
| Personal assessment | 5 |

**Maximum 8 marks**

**(c) Stamp duty cost**

| | |
|---|---|
| Option 1 | 7 |
| Option 2 | 3 |

**Maximum 8 marks**

**Professional skills marks:**

**Analysis and Evaluation**

Comprehensive evaluation of whether bringing forward the date of exercise of his share options is beneficial

Clear, logical and systematic approach to calculations which support advice given in respect of the stamp duty cost of each option for acquisition of Anara Ltd

**Commercial Acumen**

Advice offered to Eddie is appropriate to his situation and logically flows from the analysis provided

**Maximum 5 marks**

**Total 25 marks**


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**Question 3**

**(a) Transfer pricing risk**

| | |
|---|---|
| Transfer pricing risk factors | 4 |
| Implications for Pearl (HK) Ltd | 4 |
| Challenge by IRD/China tax authorities | 2 |

**Maximum 9 marks**

**(b) Double tax position and relief**

| | |
|---|---|
| Double tax position of group | 3 |
| DTA and Hong Kong domestic law | 4 |
| Actions | 5 |

**Maximum 11 marks**

**Professional skills marks:**

**Analysis and Evaluation**

Clear and logical approach taken to the evaluation of transfer pricing risk

Comprehensive assessment of the impact of the tax adjustment made to Pearl (China) Ltd on the tax position of the group

**Commercial Acumen**

Recommendation of actions to be taken by Pearl (HK) Ltd to release double tax burden are appropriate and valid commercial points

**Maximum 5 marks**

**Total 25 marks**


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