CHARTERED TAX INSTITUTE OF MALAYSIA (225750 T)
(Institut Percukaian Malaysia)

PROFESSIONAL EXAMINATIONS

FINAL LEVEL

ADVANCE TAXATION 2

DECEMBER 2017

Student Registration No.		**Date**	
Desk No.		**Examination Centre**	

Time allowed: 3 hours

INSTRUCTIONS TO CANDIDATES

1. You may answer this paper **EITHER** in English **OR** in Bahasa Malaysia. Only **ONE** language is to be used.
2. This paper consists of **SIX** questions. **Candidates are ONLY REQUIRED TO ANSWER FIVE QUESTIONS.**
3. The Income Tax Act 1967 (as amended) is referred to as ITA.
4. Each answer should begin on a separate answer booklet.
5. All workings **MUST** be shown as marks will be awarded.
6. Answers should be written in either black or blue ink.
7. No question paper or answer booklets are to be removed from the examination hall.

DO NOT TURN OVER THIS PAGE UNTIL INSTRUCTED BY THE INVIGILATOR

Question 1

(a) Ravi Manufacturing Sdn Bhd ('Ravi') is a Malaysian resident company carrying on the business of manufacturing thumb-drives. Forty percent of the company's shares are owned by an American company which is a pioneer in digital recording and storing devices. In early 2017, Ravi acquired the proprietary rights to a patented design of a digital storing device from a British company with a view to expanding its product range. The cost of the acquisition, including incidental and related costs, is as follows:

Particulars	Cost (RM)
Cost of two trips to London and return to Malaysia to negotiate the acquisition deal by two of Ravi's executive directors	15,000
Consultancy fees paid to a consultant in London for advice on the acquisition	45,000
Consultancy fees paid to a local management firm for advice on the acquisition, including its market potential in the South East Asia region	55,000
Legal fees on the acquisition and local registration of the said design, including stamp duty on the execution of the agreement	27,000
Cost of the patented design	400,000
Total costs	**542,000**

Ravi's accountant has informed you that for the year of assessment 2017, the adjusted income (prior to any adjustments for the acquisition of the proprietary rights) was RM2.6 million; and the capital allowance due for the current year of assessment was RM380,000. It had an unabsorbed capital allowance of RM220,000 brought forward from year of assessment 2016.

Required:

Compute the statutory income of Ravi Manufacturing Sdn Bhd for the year of assessment 2017 taking into account any deduction due on the acquisition of the proprietary rights to the patented design of the digital storing device from the British company.

(5 marks)

(b) Anusha Manufacturing Sdn Bhd is a company incorporated on 1 May 2017. The company wants to ensure the availability of skilled production and maintenance staff in order to commence operations as soon as the plant and machinery are installed at its factory in Nilai. It is expected that the company would commence operations sometime in December 2017 to fill in orders. The company is therefore incurring recruitment and training expenses.

The company's accountant seeks your advice on the deductibility of the recruitment and training expenses for income tax purposes; and in addition whether any special incentives are available in respect of these expenses.

Required:

(i) **Quote the applicable legislation for the above scenario.**

(ii) **State the conditions for the deductions as set out in the legislation.**

(iii) **State the expenses in the scenario which are deductible pursuant to the legislation.**

(5 marks)

(c) Miss Dharshini is an accounts executive at Malaysian Mangoes International Sdn Bhd, a locally incorporated resident company. Japanese entrepreneurs holds 30% of the paid up capital and the balance is held by Malaysian shareholders. The company specializes in preserved mangoes that are canned and exported to Japan and South Korea. The company hopes to gain a foothold in these two countries. About 20% of the output is for Malaysian consumption.

Miss Dharshini has made an appointment with you to discuss incentives that may be available in respect of expenditure incurred from the export of the mango products to Japan, with a view to reducing the company's income tax liability for the year of assessment 2017.

In the course of her discussion with you, she provided the following information:

1. The company incurred a sum of RM100,000 on advertisements that are printed and distributed in Malaysia. It spent another RM300,000 on printed advertising materials in Japan – these adertisements were printed and distributed exclusively in Japan.

2. Samples of the canned mangoes were given free of charge to prospective customers in Japan and South Korea with a view to secure sales and dealerships. In 2017, the company spent RM150,000 on such samples, and incurred air freight of RM3,000.

3. In addition, during a trade fair held in Malaysia in late September 2017, RM20,000 worth of samples were given to trade representatives from Taiwan, Hong Kong, China and Europe who attended the Fair.

4. In November 2017, three company executives from the marketing division travelled to South Korea to discuss and negotiate a deal with a potential customer for specially prepared mango products to suit Korean tastes. If the deal was successful, it would boost the company's turnover by another 30%. Miss Dharshini informs you that the company incurred considerable travelling expenses for the three company executives to go to South Korea.

5. The company participated in a tender exercise for the supply of preserved mango products to a company in Japan and South Korea in the middle of 2017. The tender for the Japanese company was prepared by the company's appointed agent in Japan and submitted accordingly by them. The other tender was prepared locally and handed over to the Korean company when the company's representative was at the Korean embassy in Malaysia on an official visit.

Required:

Miss Dharshini requires you to identify any expenses from (i) to (v) above which would be eligible for a favourable tax deduction pursuant to a tax incentive.

*Where applicable, you are required to provide details of the available tax incentive for the expenses***.**

(10 marks)

[Total: 20 marks]

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Question 2

(a) Goods and Services Tax (GST) is a multi stage, broad consumption tax, based on value added concept introduced in Malaysia on 1 April 2015 to replace Sales & Service Tax:

In the context of GST you are required to:

(i) **Define zero-rate supply.**

(2 marks)

(ii) **Explain when services are deemed to be made in:**

a. **Malaysia**

b. **Another country**

(2 marks)

(iii) **Name six (6) types of supplies that are excluded in determining the taxable turnover for registration purpose.**

(6 marks)

(b) Jade Sdn Bhd (Jade) is a GST registered manufacturer that made some mixed supplies in October 2016 (taxable period is on a monthly basis), and incurred residual input tax of RM 30,000. The breakdown of supplies are as follows:-

	RM
Value of all supplies including capital goods	380,000
Value of all taxable supplies excluding Capital goods	300,000
Value of capital goods	50,000
Value of exempt supplies	30,000
Residual input tax incurred	30,000
Input Tax attributable to taxable supply	20,000
Input Tax attributable to Exempt supply	500

(i) **Compute the input tax that can be claimed for the month of October 2016.**

(5 marks)

(ii) **State the two (2) de-minimis rules.**

(2 marks)

(c) In November 2016, Jade made the following supplies:

	RM
Residual input tax incurred	10,000
Taxable supplies	79,500
Exempt supplies	4,950

Determine whether Jade fulfilled the de-minimis rule and how much was the input tax claimable.

(3 marks)

[Total: 20 marks]

Question 3

In September 2017, the Inland Revenue Board (IRB) commenced a tax audit on Cekap Sdn Bhd (Cekap) for years of assessment (YAs) 2012-2015. Cekap is a manufacturer of rubber gloves. Since YA 2010, Cekap has undertaken a qualifying expansion project. Cekap acquired some new machinery for the project in order to increase the productivity in its manufacturing activity. Accordingly, Cekap claimed reinvestment allowance (RA) in respect of qualifying assets in its tax returns submitted to the IRB.

Based on the tax audit findings, the IRB disallowed the RA claim. The following are the cost of the qualifying assets for YAs 2012 to 2015 that were disallowed:

YA	Cost of qualifying assets disallowed by IRB (RM)
2015	500,000
2014	750,000
2013	1,000,000
2012	750,000

In addition, the following tax issues were raised by the IRB:

1. Cekap's director, Madam Ooi regularly took rubber gloves for her household use and also gave away rubber gloves to charitable organisations. This withdrawal of stock was never recorded either for accounting or stock count purposes. At the end of each accounting year, the discrepancy in stock quantity between the book records and the physical stock count was expensed off to the Profit and Loss account at cost.

   The IRB viewed that the withdrawn stock for own use, be treated as gross income, and be valued at market value and subjected to tax. The IRB estimated the value of stock withdrawn by Madam Ooi for YAs 2012 – 2015 to be at RM5,000 per month as additional gross income.

2. In YA 2013, a bad debt written off amounting to RM125,680, was claimed in Cekaps's tax return. The bad debt was subsequently recovered in YA 2015 and this amount was subjected to tax. However, the accountant failed to support the bad debt claim in YA 2013, i.e. to prove that the debt was irrecoverable and that reasonable actions had been taken to recover it. As a result, the IRB disallowed the bad debt written off in YA 2013.

3. Since YA 2012, Cekap rented a passenger vehicle from a related party, The rental payments for the passenger vehicle are stated below:

YA 2012	YA 2013	YA 2014	YA 2015
RM35,800	RM40,000	RM40,000	RM30,000

   The IRB restricted the rental payments on the basis that the payments were in respect of a non-commercial vehicle.

   The accountant accordingly informed the IRB that the above rented vehicle was not used prior to this rental and the original cost of the vehicle was RM149,880.

4. Cekap engaged a foreign technician to assist in the installation of machinery at its factory. A service fee was paid to the foreign technician (a non-tax resident) for RM68,580 in YA 2015. The detailed breakdown of the fee is as follows:

	RM
Installation charges	60,000
Travelling (air tickets)	5,000
Accommodation	3,580
	68,580

Cekap made the gross payment to the foreign technician in YA 2015. The IRB disputed the deductions of the service fee on the grounds that it was subject to withholding tax pursuant to Section 4A of the ITA.

Required:

(i) Cekap wishes to lodge an appeal against the disallowed RA claim by IRB. Cekap is of the view that since it had undertaken a qualifying project which increased its production capacity and turnover, it should be entitled to the RA incentive.

Assuming you are Cekap's tax advisor, suggest the relevant supporting documents the company should provide to the IRB for lodging the appeal.

(2 marks)

(ii) The following information was extracted from the tax files:

YA	**Original chargeable income (RM)**	**Original tax paid (RM)**
2015	3,850,000	962,500
2014	3,500,000	875,000
2013	2,800,000	700,000
2012	2,150,000	537,500

Cekap is not a SME for tax purposes. The rate of Reinvestment Allowance claim is 70% on the cost of qualifying assets.

Re-compute Cekap's chargeable income, tax liability together with the imposition of a penalty for YAs 2012 to 2015.

Your computation should take into account the disallowances raised by the IRB. The penalty rate imposed by IRB is 45%.

(15 marks)

(iii) Currently, Cekap has submitted its tax returns up to YA 2017 to the IRB. The Company's directors have approached you as tax advisor for the following**:**

a. **To advise on the Notices of Additional Assessment, in the context of time bar.**
b. **To explain to them under what circumstance the IRB is empowered to issue Notices of Additional Assessment/s beyond the time bar period, and the retention period for record keeping.**

(3 marks)

[Total: 20 marks]

Question 4

A Bhd (A) is an investment holding company. A owns directly 100% of the shares in B Sdn Bhd (B) and 10% of shares in C Sdn Bhd (C). B owns directly 100% of the shares in D Sdn Bhd (D).

A, intends to undertake a corporate restructuring exercise for the whole group including C.

(i) Mr. Nick, the Managing Director of A is considering to sell a factory currently owned by D to C at its market value of RM10 million. The factory was acquired by D,10 years ago to be used for its manufacturing activities. There are no other significant assets and liabilities in the books of D.

Required:

Highlight to Mr. Nick the potential income tax and stamp duty implications for D and C from the sale of the factory.

(8 marks)

(ii) Mr. Nick informs you that C has the option to buy the factory directly from D or to buy the shares in D.

Required:

Advise Mr. Nick of the income tax and stamp duty implications of the two options.

(4 marks)

(iii) Mr. Nick tells you that A intends to acquire an additional 80% of the shares in C before D sells the factory to C. Further, Mr. Nick confirms that the group structure will remain unchanged thereafter.

Required:

Highlight to Mr. Nick the income tax and stamp duty implications of the two options for C of the sale of factory after the acquisition of the additional 80% of shares in C by A.

(8 marks)

[Total: 20 marks]

Question 5

Qlab Sdn Bhd (Qlab-M) is a company incorporated in Malaysia in 2010 and is a member of the Qlab group. Qlab-M is principally in the business of the manufacturing and trading of smartphone accessories. Qlab-M's paid up capital as of today is RM5 million and is wholly owned by Qlab Pte Ltd (a company incorporated in Singapore). Qlab-M's annual turnover is RM500 million as at 31 December 2016.

Qlab-M has related companies in Thailand, Laos and Vietnam.

With effect from 1 January 2018, the intention of the Qlab Group is to use Malaysia as a hub for conducting its regional business and operations to manage, control, and support its key functions including management of risks, decision making, strategic business activities, trading, finance, management and human resources.

Qlab-M was informed that Malaysia has a wide range of tax incentives to encourage investment and reinvestment, by foreign direct investors and domestic investors. Qlab-M has enquired of its eligibility for the Principal Hub incentive and was informed of the following:

1. Under the Principal Hub incentive, the company is eligible for a 3 tiered corporate taxation rate as follows:

	Tier 3		**Tier 2**		**Tier 1**	
Blocks (years)	5	+5	5	+5	5	+5
Tax rate	10%		5%		0%	

2. Employment requirements and annual business spending are as follows:

	Tier 3	**Tier 2**	**Tier 1**
High value jobs	15 positions	30 positions	50 positions
Key strategic/ Management positions	3 positions	4 positions	5 positions
Annual business spending	RM3 million	RM5 million	RM10 million

Required:

(i) **Qlab-M believes that it has met the eligibility criteria for the the Principal Hub incentive. List the conditions Qlab-M has met based on the scenario above.**

(4 marks)

(ii) **Other than the 3 tiered corporate taxation rate, what other benefits does an approved Principal Hub company enjoy?**

(2 marks)

(iii) **Prepare a computation of the tax savings for Qlab-M arising from the Principal Hub incentive for YA 2018 to YA 2022.**

Assume Qlab-M is eligible for Tier 3 of the Principal Hub incentive from YA 2018 and the prevailing corporate tax rate for YA 2018 and onwards is 24%.

For the purpose of this computation, use the following information:

	YA 2018 (RM'000)	**YA 2019 (RM'000)**	**YA 2020 (RM'000)**	**YA 2021 (RM'000)**	**YA 2022 (RM'000)**
Profit before tax	18,000	19,500	20,000	22,500	25,000
Depreciation	1,000	1,250	1,500	2,000	2,500
Unrealised foreign exchange loss, trade	700	850	900	1,000	1,200
Capital allowance	900	1,000	1,250	1,500	1,800

(12 marks)

(iv) Upon expiry of the first 5 years, each tier can be considered for an extension of a further 5 years subject to the fulfilment of all previous conditions and 2 additional conditions in relation to employment requirements and annual business spending.

Qlab-M has now been awarded the Principal Hub incentive with the first 5 years to commence on 1st January 2018. Qlab-M intends to apply for an extension of the Principal Hub incentives, when the first five years of the incentives have expired.

What are the additional criteria it needs to fulfil to qualify for the extension?

(2 marks)

[Total: 20 marks]

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Question 6

Gideon Sdn Bhd (Gideon) holds 70% of the shares in Enoch Sdn Bhd (Enoch) and 100% of the shares in David Sdn Bhd (David). Enoch holds 100% of the shares in each of Farok Sdn Bhd (Farok), Horay Sdn Bhd (Horay) and Joshua Sdn Bhd (Joshua). Gideon acquired the shares in all the above companies in 2015 except David's shares which were acquired on 1 January 2016.

All the companies close their accounts to a 30 June year end.

Farok has been incurring losses in its business and the Gideon Group is keen to explore utilizing group relief to reduce its group tax liability.

You are the tax advisor to Gideon Group and the management of Gideon has provided you with the following details for the year ended 30 June 2017:

1. Enoch is a pioneer status company, with an exemption rate of 70%

2. All companies have a paid-up ordinary share capital of RM5million. However, Joshua had a paid up ordinary share capital of RM2million and increased it's paid up ordinary share capital to RM5million on 1 January 2017.

3. Financial results for all companies are given as follows:

	Gideon RM '000	**Enoch RM '000**	**David RM '000**	**Farok RM '000**	**Horay RM '000**	**Joshua RM '000**
Business adjusted income/(loss)	4,100	2,700	1,600	(7,200)	(200)	500
Capital allowances	800	700	200	400	100	200
Fixed deposit interest	24	10			15	
Rental income				200	195	250
Cash donation to approved institution	104	100			40	

Required:

(i) One of the conditions for participating in the group relief is that both surrendering and claimant companies must be related.
Explain the meaning of "related" in the context of group relief.

(3 marks)

(ii) **Explain the conditions for the two related companies to participate in the group relief and give the reason(s) if the companies in Gideon group of companies are eligible OR ineligible for the group relief.**

(4 marks)

(iii) **Compute the income tax payable by all the companies in the Gideon Group, for the year of assessment 2017. In your computation, show the different stages of income clearly.**

(13 marks)

[Total: 20 marks]

(END OF QUESTION PAPER)