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# **Examiner's Report**

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**Paper 5**  
**Hong Kong Taxation**

## **General Comments**

The paper consisted of three sections. Section A contained multiple choice questions. Section B contained one compulsory question on profits tax. Section C had five long questions and candidates were required to attempt any three. The questions tested the candidates' basic understanding of taxation concepts but the overall performance was not very good. As many questions concerned the year of assessment 2007/08 where tax relief was available in property tax, salaries tax and profits tax, but many candidates had omitted to specify such relief in their answers. Again, candidates avoided answering the essay-type parts which showed that they had not spent time on their written presentation techniques.

### **Section A – 15 Multiple Choice Questions**

Multiple choice questions can cover every part of the syllabus. The candidates' overall performance was not good. Many scored very low marks in this section which contained ten short and five computational questions. Their performance in computational questions was comparatively weaker. Candidates have to cover the whole syllabus in order to obtain good marks in this section.

### **Section B – 1 Question**

#### **Question B1**

This was a compulsory question on profits tax. Part (a) concerned the computation of profits tax liability of a sole proprietorship business. Most candidates possessed the basic understanding needed in preparing a profits tax computation. However, they should note the following:

- (a) rental income received by Mr Lee was chargeable to property tax and therefore should be excluded from the assessable profit;
- (b) Mr Lee's contribution to MPF scheme was deductible, subject to a maximum of \$12,000;
- (c) Mr T Lee was regarded as an employee of the business, the MPF contribution made by the business was deductible;
- (d) any private portion of expenses enjoyed by the proprietor was not deductible;
- (e) commission paid to overseas agent was expense incurred for the business and hence it was deductible;
- (f) many candidates had wrongly included the purchase of computer in the calculation of depreciation allowance, instead of wholly deducting from the assessable profit;
- (g) candidates were familiar with the calculation of the value of asset transferred into the business.

Part (b) required candidates to explain the treatment of certain items. Although they correctly treated the items in their computation, they could not explain the reasons for such treatment clearly.

### **Section C – 5 Questions**

#### **Question C1**

This was a question on salaries tax under a non-Hong Kong employment. Candidates' overall performance was satisfactory.

Many candidates wrongly stated in part (a) that one of the factors in determining the locality of employment was the place of service.

For part (b), many candidates had wrongly used the whole year (366 days) in calculating the leave days attributable to Hong Kong service instead of using the business days (336 days).

Part (c) concerned the computation of share option gain and many candidates were unable to compute the apportioned gain in case the option was granted subject to vesting period under a non-Hong Kong employment.

Candidates showed the following in the salaries tax computation under part (d):

- (a) apportionment was not applicable to the allowance for stays in Hong Kong;
- (b) share option gain should not have been included in the calculation of rental value;
- (c) dependent parent allowance should not have been allowed as the parent was not ordinarily resided in Hong Kong.

### **Question C2**

The question concerned personal assessment. In part (a), candidates failed to define the meaning of “permanent resident” and “temporary resident” under personal assessment. They wrongly applied the 60 days rule in defining “temporary resident”.

Part (b)(i) was concerned with the computation of tax payable under property tax and profits tax. Many candidates failed to apply tax relief to each tax computation.

For the computation of tax payable under personal assessment, many candidates demonstrated the following weaknesses:

- (a) failed to restrict the mortgage loan interest to net assessable value;
- (b) wrongly included the business loss in total income;
- (c) wrongly allowed both elderly residential care expense and dependent parent allowance.

### **Question C3**

Part (a) mainly concerned the computation of depreciation allowances on plant and machinery of a newly commenced business with first account more than 12 months. Candidates' weakness was that they did not know that the depreciation allowance allowed was based on the capital expenditure incurred during the relevant basis period. Therefore, the candidates should firstly know the basis period of the years of assessment concerned.

Part (b) concerned the computation of industrial building allowance and commercial building allowance and candidates showed that they had difficulty in segregating the qualifying expenditure for industrial building and commercial building respectively. They did not realise that no annual allowance was granted if the building was not in use at the end of the basis period.

### **Question C4**

Part (a) concerned the claim for exemption from property tax by a corporation and many candidates tried to avoid answering this part. Those who did, could not perform well.

Part (b) concerned the computation of the respective property tax and profits tax payable by a corporation which owned a property in Hong Kong. Candidates showed the following weaknesses:

- (a) wrongly stated that the basis period under property tax as the accounting date of the company;
- (b) computed rental income up to 31 December 2007 instead of 31 March 2008;
- (c) used the corporation profits tax rate instead of the standard rate to compute the property tax liability;
- (d) wrongly computed under profits tax, the premium to be included in the year of assessment 2007/08.

Part (c) concerned the computation of net assessable value of an individual under property tax and the performance in this question was on the good side. However, candidates wrongly deducted the rates paid by the owner for the vacant period.

**Question C5**

This was an essay-type question regarding the badges of trade, the requirements of a valid objection and an appeal to the Board of Review. As in the past, very few candidates attempted this question. Although the performance of most of the candidates who attempted this question was poor, there was one candidate who obtained full marks. This showed that candidates could get very good result if they prepare well on topics regarding tax administration.

**[ END OF EXAMINER'S REPORT ]**