

Preparing Taxation Computations

(Hong Kong)

ACCA CERTIFIED ACCOUNTING TECHNICIAN EXAMINATION

ADVANCED LEVEL

TUESDAY 13 JUNE 2006

QUESTION PAPER

Time allowed **3 hours**

ALL FOUR questions are compulsory and **MUST** be answered

Tax rates and allowances are on page 3

Do not open this paper until instructed by the supervisor

This question paper must not be removed from the examination hall

The Association of Chartered Certified Accountants

Paper T9(HKKG)



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The question paper begins on page 3.**

ALL FOUR questions are compulsory and MUST be attempted

- 1 (a)** Until 31 March 2005, Mr Chan was employed by an American company in New York as sales manager for the Far East region at an annual salary equivalent to \$730,000. During the year ended 31 March 2005, Mr Chan visited Hong Kong on duty for 120 days. During this period he stayed in a hotel (one room) for which the American company was billed for \$30,000.

As from 1 April 2005, the American company set up a subsidiary company in Hong Kong to take charge of its Hong Kong activities called American (HK) Ltd. Effective from 1 April 2005, Mr Chan was appointed as Vice-President of American (HK) Ltd. His annual salary was increased to \$912,500. Since 1 April 2005, Mr Chan has been living in a flat at Happy Valley at a monthly rental of \$24,000. American (HK) Ltd agreed to bear the cost of the rent but limited to \$20,000 per month.

On 1 May 2005 Mr Chan got married. The couple had a honeymoon holiday in Tianjin, China for one month, after which Mr Chan immediately worked in American (HK) Ltd's Beijing office for 100 days. During this period, he stayed in a hotel paid for by the company.

Mr Chan suffered tax of a similar nature to Hong Kong salaries tax for his work in Beijing amounting to \$14,400.

On her marriage, Mrs Chan resigned from her job as a secretary earning a monthly salary of \$12,000 with effect from 1 May 2005. On 1 March 2006 a child was born to the Chan family.

Required:

Compute Mr Chan's salaries tax payable for each of the years of assessment 2004/05 and 2005/06 assuming that both Mr and Mrs Chan have elected for joint assessment if applicable. Ignore provisional salaries tax. Show all workings. (13 marks)

- (b) State under what conditions an individual may be granted child allowance for salaries tax and personal assessment purposes. Your answer should include a definition of a "child" for this purpose.** (6 marks)
- (c) State the circumstances under which a non-resident person will be liable for Hong Kong profits tax.** (5 marks)
- (d) Describe the assessment procedures applicable to a non-resident person under the Inland Revenue Ordinance (including the position of persons chargeable on behalf of the non-resident person).** (6 marks)
(30 marks)

- 2 State, giving reasons, whether or not the following items are chargeable to salaries tax:
- (a) A \$200 cash coupon given by an employer to an employee as a wedding gift. (3 marks)
 - (b) An ex gratia payment made by an employer in the form of a gold coin in recognition of a job well done by an employee. The coin had a face value of \$1,000 but a market value of \$2,000 at the date of payment. (3 marks)
 - (c) A gas bill settled directly by an employer for quarters occupied by an employee, in circumstances where the contract with the gas company had been entered into by the employee personally. (3 marks)
 - (d) Payment in lieu of notice made by an employer for the early termination of employment of an unsatisfactory employee. (2 marks)
 - (e) Payment to a retiring employee for entering into a covenant whereby the employee agreed not to compete in future with the employer in the same field. (2 marks)
 - (f) Tips given to a waiter in a restaurant by customers. (4 marks)
 - (g) Sums withdrawn from a recognised occupational retirement scheme by an employee upon the implementation of a mandatory provident fund. (4 marks)
 - (h) A long service payment payable under the Employment Ordinance by an employer. (3 marks)
- (24 marks)**

- 3 Eric, Edwin and Reality Ltd are in partnership as insurance brokers, sharing profits and losses in the ratio of 25%, 25% and 50% respectively. The trading results of the partnership were as follows:

Year to 31 December	2003 \$	2004 \$	2005 \$
Commission income	1,400,000	1,900,000	2,600,000
Less: Salary to Edwin	200,000	200,000	200,000
Rent to Reality Ltd	1,200,000	1,200,000	1,200,000
Provision for depreciation	100,000	100,000	100,000
Profits tax paid	88,000	–	–
Other revenue expenses (all allowable)	540,000	360,000	640,000
	<u>2,128,000</u>	<u>1,860,000</u>	<u>2,140,000</u>
Net profit (loss) for the year	<u>(728,000)</u>	<u>40,000</u>	<u>460,000</u>

Depreciation allowances have been agreed by the Assessor to be \$50,000 for each of the years of assessment 2003/04 to 2005/06 inclusive.

Eric is single. He owns a flat which is 20% occupied by him and the remaining 80% is let at an annual rent of \$60,000. The flat was purchased through a mortgage loan and interest payments are calculated as \$83,000, \$74,000 and \$60,000 for the years of assessment 2003/04, 2004/05 and 2005/06 respectively. During the year 2003/04 he was also engaged in a freelance business from which he personally earned a profit of \$64,000. This source of income ceased on 31 March 2004. He has elected for personal assessment for each of the years of assessment 2003/04 to 2005/06 inclusive.

Edwin is married and has elected for personal assessment only for 2005/06. His wife is in employment and earned \$96,000 in the year ended 31 March 2006. She is also entitled to a 10% share of the assessable profits of a restaurant business which was formed by 22 partners. Her share of assessable profits from this restaurant business was \$180,000 for the year of assessment 2005/06. Edwin remitted \$30,000 each to his parents, who have been residing in Australia for the last three years and his two sons (aged 16 and 20) who are studying full-time at a college there. His parents were 60 years old on 31 March 2006.

Reality Ltd is a property investment company in Hong Kong. Apart from its rental income of \$1,200,000 per annum from the partnership, it has other net business income in the amount of \$550,000 per annum. All of this income is subject to profits tax.

Required:

- Compute the profits tax payable by the partnership of Eric, Edwin and Reality Ltd for each of the years of assessment 2003/04, 2004/05 and 2005/06. Ignore provisional profits tax. Show all workings.** (16 marks)
 - Compute the personal assessment tax payable by Eric as a result of electing for personal assessment for each of the years of assessment 2003/04, 2004/05 and 2005/06. Show all workings.** (7 marks)
 - Compute the personal assessment tax payable in total by Edwin and his wife for the year of assessment 2005/06. You are not required to apportion the tax liability between husband and wife. Show all workings.** (4 marks)
 - Compute the profits tax payable by Reality Ltd for each of the years of assessment 2003/04, 2004/05 and 2005/06. Ignore provisional profits tax. Show all workings.** (3 marks)
- (30 marks)**

- 4 Prestige Ltd owned a factory in Tai Po on leasehold land. The Government lease expired on 30 June 2003 when it was renewed for a further period of 20 years at a premium of \$2,500,000. During the two years ending on 31 March 2004 and 31 March 2005, Prestige Ltd demolished the existing factory and constructed a new one on the leasehold land at a cost of \$8,894,000. The breakdown of the cost was as shown below:

	Year ended 31 March 2004	Year ended 31 March 2005
	\$	\$
Demolition of old factory building	840,000	
Site investigation	74,000	
Architect fees	420,000	
Foundation work	790,000	
Construction cost		5,400,000
Sewers and water mains		670,000
Lifts		700,000
	2,124,000	6,770,000

The new factory building was completed on 31 January 2005 following which it was used in the following manner, according to the original building plan:

Usage	Percentage of the building area
Factory area	75%
Workers' canteen and amenity area	5%
Administrative office area	20%

One half of the factory area was leased to Perfect Metal Ltd from 1 February 2005. Perfect Metal Ltd carried on metal fabrication work in the leased area.

Prestige Ltd had acquired a mortgage loan from a bank to finance the construction cost of the new factory building. Interest paid up to 31 March 2005 was as follows:

Year ended 31 March 2004	\$240,000
Year ended 31 March 2005	
1 April 2004 to 31 January 2005	\$280,000
1 February 2005 to 31 March 2005	\$30,000

Required:

Calculate the depreciation allowances to which Prestige Ltd is entitled for each of the years of assessment 2003/04 and 2004/05. Show all workings.

(16 marks)

End of Question Paper