

Explanatory Notes to Annex 7 of Circular on the New One-tier Corporate Tax System released on 15 Aug 2002

- 1 The purpose of these explanation notes is to provide further clarification on the following items during the 5-year transitional period for the one-tier corporate tax system:
 - a the types of downward adjustment to the S44 balance as at 31 Dec 2002,
 - b the corresponding upward adjustment to the S44 balance as at 31 Dec 2002, and
 - c the effect of interim discharge order (IDO) and interim recharge order (IRO) on the S44 balance as at 31 Dec 2002.

2 Downward and upward adjustment against the S44 balance

2.1 Downward adjustment

Where the tax discharge is relating to tax assessed previously included in the S44 balance as at 31 Dec 2002, this amount of tax discharge would need to be adjusted downwards against the S44 balance.

There are 2 types of downward adjustment:

- a amount debited directly against the S44 balance, and
- b amount which cannot be debited directly against the S44 balance due to insufficient balance but resulted in S44 charge.

2.2. Upward adjustment

Where any additional tax raised subsequently is relating to tax discharge which has been adjusted downwards against the S44 balance, this amount of the additional tax would need to be adjusted upwards against the S44 balance.

The amount of upward adjustment is the lower of:

- a the downward adjustment less any S44 charge utilised, or
- b the tax payable.

3 We would illustrate using the example in Annex 7 to the circular on one-tier corporate tax system:

Date of asst	YA	Type of asst	Tax assessed/ (discharge)	S44 statement			S44 charge (Tax discharge not refunded but available for offset)		Tax refundable	Tax payable	Downward adjustment via					
				Dr	Cr	Bal	Amt	Bal			Direct debit (YA 2001)		S44 charge (YA 2001)		S44 charge (YA 2003)	
											Amt	Bal	Amt	Bal	Amt	Bal
Balance @ 31/12/02					20,000											
30/1/03	2001	Amended	(50,000)	20,000	0	0	30,000	30,000	20,000		20,000	20,000	30,000	30,000		
15/2/03	2003	Original	40,000	0	10,000	10,000	(30,000)	0	10,000		0	20,000	0	30,000		
18/10/03	2001	Amended	(60,000)	10,000	0	0	50,000	50,000	10,000		10,000	30,000	50,000	80,000		
30/11/03	2003	Amended	(15,000)	0	0	0	15,000	65,000	0		0	30,000	0	80,000	15,000	15,000
15/12/03	2003	Additional	10,000	0	0	0	(10,000)	55,000		0	0	30,000	0	80,000	(10,000)	5,000
28/12/03	2001	Additional	65,000	0	10,000	10,000	(55,000)	0	10,000		0	30,000	(65,000)	15,000	0	5,000

3.1 The columns under “Downward adjustment via” have been added to track the amount of downward and upward adjustments to be made for each YA.

3.2 Tax discharge for YA 2001: \$110,000¹

As the tax discharge is relating to tax assessed previously included in the S44 balance as at 31 Dec 2002, this amount of tax discharge would need to be adjusted downwards against the S44 balance. The amount of downward adjustment is:

YA 2001	Tax discharge	Amount debited directly against the S44 balance	Amount which cannot be debited directly against the S44 balance due to insufficient balance but resulted in S44 charge
Amended asst dated 30/1/03	50,000	20,000	30,000
Amended asst dated 18/10/03	60,000	10,000	50,000
Total	<u>110,000</u>	<u>30,000</u>	<u>80,000</u>

3.3 Original assessment for YA 2003: \$40,000²

As the ECI for YA 2003 is submitted prior to 31/3/03, the tax of \$40,000 is to be included in the S44 balance. As there is a S44 charge of \$30,000 available for set-off, the amount of tax payable is \$10,000 (40,000 – 30,000). Hence, only this amount is credited into the S44 statement.

If not for utilising the S44 charge of \$30,000, the amount of tax for YA 2003 that can be credited into the S44 balance is \$40,000. Hence, although the charge of \$30,000 is utilised, it is not deducted from the S44 charge (YA 2001) balance as it remains to be reinstated.

3.4 Tax discharge for YA 2003: \$15,000³

As the tax discharge is relating to tax assessed for YA 2003 which has been included in the S44 balance, this amount of tax discharge would need to be adjusted downwards against the S44 balance. The amount of downward adjustment is:

<u>YA 2001</u>	<u>Tax discharge</u>	<u>Amount debited directly against the S44 balance</u>	<u>Amount which cannot be debited directly against the S44 balance due to insufficient balance but resulted in S44 charge</u>
Amended asst dated 30/11/03	15,000	0	15,000

3.5 Additional tax for YA 2003: \$10,000⁴

As the additional tax is relating to the tax discharge of \$15,000 for YA 2003 that has been adjusted downwards against the S44 balance, this amount would need to be adjusted upwards against the S44 balance. The amount of upward adjustment is the lower of:

- a \$5,000 [downward adjustment for YA 2003 of \$15,000 – S44 charge utilised of \$10,000], or
- b \$0 [tax payable = additional tax of \$10,000 – S44 charge utilised of \$10,000]

Hence, the amount of upward adjustment is nil. The S44 charge (YA 2003) balance is reduced by \$10,000.

3.6 Additional tax for YA 2001: \$65,000⁵

As the additional tax is relating to the tax discharge of \$110,000 for YA 2001 that has been adjusted downwards against the S44 balance, this amount would need to be adjusted upwards against the S44 balance. The amount of upward adjustment is the lower of:

- a \$55,000 [downward adjustment for YA 2001 of \$110,000 (30,000 + 80,000) – S44 charge utilised of \$55,000], or
- b \$10,000 [tax payable = additional tax of \$65,000 – S44 charge utilised of \$55,000]

Hence, the amount of upward adjustment is \$10,000. The S44 charge (YA 2001) balance is reduced by \$65,000.

3.7 Maximum amount of upward adjustment

The maximum amount of upward adjustment that can be made in this example is \$60,000. This is made up of the S44 opening balance of \$20,000 that is adjusted downward by the amended assessment for YA 2001 and the tax assessed of \$40,000 for YA 2003.

4 Contrast the above example with the one below if the ECI for YA 2003 is submitted after 31/3/03 (all other transactions are the same):

Date of asst	YA	Type of asst	Tax assessed/ (discharge)	S44 statement			S44 charge (Tax discharge not refunded but available for offset)		Tax refundable	Tax payable	Downward adjustment via					
				Dr	Cr	Bal	Amt	Bal			Direct debit (YA 2001)		S44 charge (YA 2001)		S44 charge (YA 2003)	
											Amt	Bal	Amt	Bal	Amt	Bal
Balance @ 31/12/02						20,000										
30/1/03	2001	Amended	(50,000)	20,000	0	0	30,000	30,000	20,000		20,000	20,000	30,000	30,000		
15/6/03	2003	Original	40,000	0	0	0	(30,000)	0		10,000	0	20,000	(30,000)	0		
18/10/03	2001	Amended	(60,000)	0	0	0	60,000	60,000	0		0	20,000	60,000	60,000		
30/11/03	2003	Amended	(15,000)	0	0	0	0	60,000	15,000		0	20,000	0	60,000	0	0
15/12/03	2003	Additional	10,000	0	0	0	(10,000)	50,000		0	0	20,000	(10,000)	50,000	0	0
28/12/03	2001	Additional	65,000	0	15,000	15,000	(50,000)	0		15,000	(15,000)	5,000	(50,000)	0	0	0

4.1 Tax discharge for YA 2001: \$110,000¹

As the tax discharge is relating to tax assessed previously included in the S44 balance as at 31 Dec 2002, this amount of tax discharge would need to be adjusted downwards against the S44 balance. The amount of downward adjustment is:

<u>YA 2001</u>	<u>Tax discharge</u>	<u>Amount debited directly against the S44 balance</u>	<u>Amount which cannot be debited directly against the S44 balance due to insufficient balance but resulted in S44 charge</u>
Amended asst dated 30/1/03	50,000	20,000	30,000
Amended asst dated 18/10/03	<u>60,000</u>	<u>0</u>	<u>60,000</u>
Total	<u>110,000</u>	<u>20,000</u>	<u>90,000</u>

4.2 Original assessment for YA 2003: \$40,000²

As the ECI for YA 2003 is submitted after 31/3/03, the tax of \$40,000 would not be included in the S44 balance. But the S44 charge utilised of \$30,000 is deducted from the S44 charge (YA 2001) balance as it would not be reinstated.

4.3 Tax discharge for YA 2003: \$15,000³

As the tax discharge is relating to tax assessed for YA 2003 which is not included in the S44 balance, this amount of tax discharge would not be adjusted downwards against the S44 balance.

4.4 Additional tax for YA 2003: \$10,000⁴

As the additional tax is relating to the tax discharge of \$15,000 for YA 2003 that has not been adjusted downwards against the S44 balance, this amount would not be adjusted upwards against the S44 balance. But the S44 charge utilised of \$10,000 is deducted from the S44 charge (YA 2001) balance as it would not be reinstated.

4.5 Additional tax for YA 2001: \$65,000⁵

As the additional tax is relating to the tax discharge of \$110,000 for YA 2001 that has been adjusted downwards against the S44 balance, this amount would need to be adjusted upwards against the S44 balance. The amount of upward adjustment is the lower of:

- a \$20,000 [downward adjustment for YA 2001 of \$70,000 (20,000 + 50,000) – S44 charge utilised of \$50,000], or
- b \$15,000 [tax payable = additional tax of \$65,000 – S44 charge utilised of \$50,000]

Hence, the amount of upward adjustment is \$15,000. The downward adjustment for YA 2001 is reduced by \$65,000.

4.6 Maximum amount of upward adjustment

The maximum amount of upward adjustment that can be made in this example is \$20,000 which is the S44 opening balance of \$20,000 that is adjusted downward by the amended assessment for YA 2001.

- 5 Suppose the additional tax for YA 2003 dated 15/12/03 and YA 2001 dated 28/12/03 is \$75,000 and \$300,000 respectively in the example in Annex 7 (all other transactions are the same):

Date of asst	YA	Type of asst	Tax assessed/ (discharge)	S44 statement			S44 charge (Tax discharge not refunded but available for offset)		Tax refund-able	Tax payable	Downward adjustment via					
				Dr	Cr	Bal	Amt	Bal			Direct debit (YA 2001)		S44 charge (YA 2001)		S44 charge (YA 2003)	
											Amt	Bal	Amt	Bal	Amt	Bal
Balance @ 31/12/02					20,000											
30/1/03	2001	Amended	(50,000)	20,000	0	0	30,000	30,000	20,000		20,000	20,000	30,000	30,000		
15/2/03	2003	Original	40,000	0	10,000	10,000	(30,000)	0		10,000	0	20,000	0	30,000		
18/10/03	2001	Amended	(60,000)	10,000	0	0	50,000	50,000	10,000		10,000	30,000	50,000	80,000		
30/11/03	2003	Amended	(15,000)	0	0	0	15,000	65,000	0		0	30,000	0	80,000	15,000	15,000
¹ 15/12/03	2003	Additional	75,000	0	0	0	(65,000)	0		10,000	0	30,000	(50,000)	30,000	(15,000)	0
² 28/12/03	2001	Additional	300,000	0	60,000	60,000	0	0		300,000	(30,000)	0	(30,000)	0	0	0

5.1 For the first 4 transactions, please refer to para 3.2 to 3.4 above.

5.2 Additional tax for YA 2003: \$75,000¹

As the tax discharge of \$15,000 for YA 2003 has been adjusted downwards against the S44 balance, the additional tax would need to be adjusted upwards against the S44 balance. The amount of upward adjustment is the lower of:

- a \$0 [downward adjustment for YA 2003 of \$15,000 – S44 charge utilised up to the downward adjustment for YA 2003 of 15,000],
or
- b \$10,000 [tax payable = additional tax of \$75,000 – S44 charge utilised of \$65,000]

Hence, the amount of upward adjustment is nil.

Of the additional tax of \$75,000, \$15,000 is relating to tax discharge which has been adjusted downwards against the S44 balance while \$60,000 is relating to tax raised after 31/3/03 which is not to be included in the S44 balance. Of the S44 charge utilised of \$65,000, \$15,000 is attributable to the additional tax of \$15,000 while \$50,000 to the additional tax of \$60,000. Hence, the S44 charge (YA 2003) and (YA 2001) balance is reduced by \$15,000 and \$50,000 respectively.

5.3 Additional tax for YA 2001: \$300,000²

As the additional tax is relating to the tax discharge of \$110,000 for YA 2001 that has been adjusted downwards against the S44 balance, this amount would need to be adjusted upwards against the S44 balance. The amount of upward adjustment is the lower of:

- a \$60,000 [downward adjustment for YA 2001 of 60,000 (30,000 + 30,000)], or
- b \$300,000 [tax payable]

Hence, the amount of upward adjustment is \$60,000. The downward adjustment for YA 2001 is reduced by \$60,000.

5.4 Maximum amount of upward adjustment

The maximum amount of upward adjustment that can be made in this example is \$60,000. This is made up of the S44 opening balance of \$20,000 that is adjusted downward by the amended assessment for YA 2001 and the tax assessed of \$40,000 for YA 2003.

6 Interim discharge order (IDO) or interim recharge order (IRO)

Under the current S44 mechanism,

- a when an assessment is raised, the S44 balance is increased by the amount of tax assessed.
- b when this tax assessed is withheld from collection (IDO), the S44 balance is reduced by the same amount of tax.
- c upon reviewing the assessment, CIT would first reinstate the amount of IDO (IRO) and either maintain the assessment, amend the assessment or raise additional assessment. The S44 balance would then be increased by the amount of IDO reinstated and at the same time reduced by the tax discharge or increased by the additional tax.

6.1 During the 5-year transitional period, CIT would adopt this approach for IDO and IRO:

- a Assessment and IDO raised prior to 31/12/02 and IRO raised after 31/12/02
 - i If CIT maintains the assessment, the amount of IRO (subject to the S44 charge available for set-off) will be credited to the S44 balance as at 31/12/02.

- ii If CIT amends the assessment, the amount of IRO (subject to the S44 charge available for set-off) will be credited to the S44 balance as at 31/12/02 and at the same time the amount of tax discharge will be adjusted downwards against the S44 balance.
- iii If CIT raises additional assessment, the amount of IRO (subject to the S44 charge available for set-off) will be credited to the S44 balance as at 31/12/02 but the additional tax will not be credited to the S44 balance as the additional assessment is raised after 31/12/02.

b Assessment raised prior to 31/12/02 and IDO and IRO raised after 31/12/02

- i The amount of IDO will be adjusted downwards against the S44 balance as at 31/12/02. If CIT maintains the assessment, the amount of IRO (subject to the S44 charge available for set-off) will be credited to the S44 balance as at 31/12/02.
- ii The amount of IDO will be adjusted downwards against the S44 balance as at 31/12/02. If CIT amends the assessment, the amount of IRO (subject to the S44 charge available for set-off) will be credited to the S44 balance as at 31/12/02 and at the same time the amount of tax discharge will be adjusted downwards against the S44 balance.
- iii The amount of IDO will be adjusted downwards against the S44 balance as at 31/12/02. If CIT raises additional assessment, the amount of IRO (subject to the S44 charge available for set-off) will be credited to the S44 balance as at 31/12/02 but the additional tax will not be included in the S44 balance as the additional assessment is raised after 31/12/02.

c Assessment, IDO and IRO raised after 31/12/02

No adjustment will be made to the S44 balance as at 31/12/02 as the assessment is raised after 31/12/02.

6.2 We would illustrate the above approach for IDO and IRO in the following examples:

Example 1: Assessment and IDO for YA 2000 raised prior to 31/12/02 and IRO raised after 31/12/02. Assessment amended subsequently.

Date of asst	YA	Type of asst	Tax assessed/ (discharge)	S44 statement			S44 charge (Tax discharge not refunded but available for offset)		Tax refundable	Tax payable	Downward adjustment via					
											Direct debit (YA 2001)		S44 charge (YA 2001)		Direct debit (YA 2000)	
				Dr	Cr	Bal	Amt	Bal			Amt	Bal	Amt	Bal	Amt	Bal
Balance @ 31/12/02						20,000										
30/1/03	2001	Amended	(22,000)	20,000	0	0	2,000	2,000	20,000		20,000	20,000	2,000	2,000		
18/10/03	2000	IRO	5,000	0	3,000	3,000	(2,000)	0		3,000	0	20,000	0	2,000		
18/10/03	2000	Amended	(2,000)	2,000	0	1,000	0	0	2,000		0	20,000	0	2,000	2,000	2,000

Maximum upward adjustment in this example = 20,000 [S44 balance @ 31/12/02] + 5,000 [IRO] = 25,000

Example 2: Assessment for YA 2000 raised prior to 31/12/02 and IDO and IRO raised after 31/12/02. Additional assessment raised subsequently.

Date of asst	YA	Type of asst	Tax assessed/ (discharge)	S44 statement			S44 charge (Tax discharge not refunded but available for offset)		Tax refundable	Tax payable
				Dr	Cr	Bal	Amt	Bal		
Balance @ 31/12/02						20,000				
28/2/03	2000	IDO	(5,000)	5,000	0	15,000				
18/10/03	2000	IRO	5,000	0	5,000	20,000				5,000
18/10/03	2000	Additional	3,000	0	0	20,000				3,000

Example 3: Assessment, IDO and IRO raised after 31/12/02. Assessment amended subsequently.

Date of asst	YA	Type of asst	Tax assessed/ (discharge)	S44 statement			S44 charge (Tax discharge not refunded but available for offset)		Tax refundable	Tax payable
				Dr	Cr	Bal	Amt	Bal		
Balance @ 31/12/02						20,000				
15/5/03	2003	Original	10,000	0	0	20,000				10,000
28/5/03	2003	IDO	(5,000)	0	0	20,000				(5,000)
18/10/03	2003	IRO	5,000	0	0	20,000				5,000
18/10/03	2003	Amended	(2,000)	0	0	20,000			2,000	