Deloitte Tax Challenge 2010

Team Category
Preliminary Stage Case Study - New Kid

New Kid Sdn Bhd was recently incorporated to operate a supermarket chain in Malaysia. It proposes to have a grand opening on 1 January 2011 by the Prime Minister of Malaysia after which, the supermarkets will be open. New Kid will begin with five 100%-owned subsidiaries, each of which will be profitable but none of them are expected to pay tax for 3 years.

As New Kid Sdn Bhd has limited technical experience in the supermarket business, it contacted a famous American supermarket operator for expertise to be provided in the USA and short visits to Malaysia not exceeding 60 days a year. Since the American entity has little knowledge of Malaysian taxation, it requires that any Malaysian taxes it may have to suffer be borne by New Kid Sdn Bhd. The fee payable each year for this service is RM3 million.

New Kid Sdn Bhd also intends to acquire a new America brand, XMart, for RM3 million and to operate its supermarket business under that brand. It aims to gain business from tourists and locals by using that brand.

In order to fund its operations, New Kid borrowed RM20 million which it in turn invested each of the subsidiaries by way of subscribing for their shares. Each of its 5 subsidiaries will incur operating costs like rental, staff costs, electricity and purchases of goods for resale and some of these costs will arise from 1 September 2010. Most of the premises to be rented require much repair as the previous tenants had not maintained the premises well. They will also require much outfitting e.g. brighter lighting, floor tiling, mirrors, etc before they can be used as supermarket premises.

Given that the supermarket business is a cash business, the 5 subsidiaries are expected to be cash rich and will pool their cash surplus at their holding company, New Kid, by way of loans to that company which it will invest in various instruments available in the money market. Once or twice a year, the subsidiaries will declare dividends to the holding company, possibly about equal to the loans made.

New Kid will itself provide management services to its subsidiaries for a fee. It also intends to provide such services to supermarkets owned by an unrelated supermarket chain operating in rural areas.

Being a forward looking company, New Kid has approached your team to advise them on how they can be tax efficient, restricted to the proposals and facts highlighted above. They require your advice in the form of a letter addressed to their Managing Director and have asked that the deduction of incorporation costs be excluded from your advice as their company secretary has given them the legislation on that matter.

Note: Any general advice like employment of disabled persons, double deduction in respect of insurance premiums and the like are regarded as extraneous to the proposals and facts highlighted above and should be excluded.