

CA



THE INSTITUTE OF
CHARTERED ACCOUNTANTS
OF SRI LANKA

SUGGESTED SOLUTIONS

15304–Advanced Taxation and Strategic Tax Planning

CA Professional (Strategic Level I) Examination
June 2013

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

Answer No. 01**Part (a) (i)**AIT Agribusiness PLCComputation of Statutory/Assessable/Taxable Income and Tax Payable

			Rs. '000	
Adjusted Profit from Agriculture			40,152	
Tourism-Disposal of F/A			10	
Seeds-Disposal of F/A			<u>130</u>	
Total Statutory Income			40,292	
Less: Trade Losses				
Trade Loss B/F		18,000		
Loss from Seeds (Exempt Income /hence loss is not allowed)		-		
Loss from Tourism(Exempt Income /hence loss is not allowed)		<u> </u>		
		18,000		
Limited to 35% of statutory income		14,102	<u>(14,102)</u>	
Assessable Income			26,190	
Less: Q/P	Building & Hotel Equipment -Rs. 80 M			
	Cannot claim it as it is not for expansion		-	
			<u> </u>	
Taxable Income			<u>26,190</u>	
Tax Payable				
	Agriculture	26,050	10%	2,605
	Disposal of F/A	<u>140</u>	28%	<u>39</u>
	Income tax payable	<u>26,190</u>		2,644
	Dividend Tax	22,000	10%	<u>2,200</u>
TOTAL TAX PAYABLE				<u>4,844</u>

Schedule-01**Computation of adjusted Profit From Trade from Trade ,Business**

Rs.000

	Agriculture	Seeds	Tourism
	Liabe	Exempt	Exempt
Net profit Before tax	90,000	(3,420)	4,010
Preparation of Land-Allowed	-	-	-
Stamp Duty paid			3,900
Foreign Travelling	3,200		1,850
Foreign Travelling Limited to 2% of 30,000	(600)	-	
Foreign Travelling Allowed 100% as for Tourism			(1,850)
Depreciation	8,200	1,200	8,500
Share Issue Expenses	16,200	-	-
Share Issue Expenses Limitation (1% Of 500M)	(5,000)	-	-
Provision for Gratuity Note-01	850	250	190
Gratuity Paid Note-01	(340)	-	-
Capital Allowances			
2nd Year (2011/12)			
Computers (25%) 750 x (1/3)	-	(250)	-
Agri Equip (33.33%) 4,500 x(1/2)	-	(2,250)	-
Tractor (20%) 2,700 x (1/4)	-	(675)	-
4th Year (2009/10)			
Computers (25%)	(2,000)	-	-
Agri Equi (12.5%) 6,000 x(1/5)	(1,200)	-	-
Lorry (20%) 12,000 x (1/2)	(6,000)	-	-
1st Year(2012/13)			
Cont'n Building (10%) 50,000x10%	-	-	(5,000)
Equipment (30-18) x 33.33%	-	-	(4,000)
High Tech Equipment 18 x 50%	-	-	(9,000)
Tank & Ponds-Fully Allowed			
Agriculture 3000+ 158	(3,158)	-	-
Seeds 7500+395	-	(7,895)	-
Management Fees Note -02	-	-	1,350
Book Profit On Disposal of Fixed Assets	-	(80)	(10)
Adjusted Profit on Disposal of Fixed Assets Note -03	-	130	10
	100,152	(12,990)	(50)
Less: Profit on Disposal Of F/A-(Liable)		(130)	(10)
Deemed sale as per Section 16B (3)			
30,000 packets @ Rs.2 per packet	(60,000)	60,000	
Statutory income from business - liable	40,152		
Tax Exempt Profit /(Loss)		46,880	(60)

Note-01

Gratuity

Balance as at 01.04.12	4,850
Add: Provision for the year	<u>1,290</u>
	6,140
Less: Payments made during the year	<u>(340)</u>
Balance as at 31.03.13	<u>5,800</u>

Note -02

Management Fees

Actual Expense	3,700
Limited to 5% of Gross Profit of Rs. 47,000	<u>2,350</u>
Disallowed	<u>1,350</u>

Note -03

Adjusted Profit on Disposal of F/A

	Seeds <u>Tractor</u>	Tourism <u>Air Conditioner</u>
Sale Proceeds	880	60
Tax WDV	<u>(750)</u>	<u>(50)</u>
Adjusted Profit	<u>130</u>	<u>10</u>

Note -04

Details of Property Plant and Equipment, Tax written Down Value, Book Written Down Value, additions and disposals are follows:

Computers

	Agriculture	Seeds
Year of purchase	2009/10	2011/12
Rate	25%	25%
Remaining years to claim	1	3
Remaining Tax written Down Value at the beginning	<u>2,000</u>	<u>750</u>
Claim for the year	<u>2,000</u>	<u>250</u>

Agricultural Equipment

Year of purchase	2009/10	2011/12
Rate	12.50%	33.33%
Remaining years to claim	5	2
Remaining Tax written Down Value at the beginning	<u>6,000</u>	<u>4,500</u>
Claim for the year	<u>1,200</u>	<u>2,250</u>

Tractors and lorries

Year of purchase	2009/10	2011/12
Rate	20%	20%
Remaining years to claim	2	4
Remaining Tax written Down Value at the beginning	<u>12,000</u>	<u>2,700</u>
Claim for the year	<u>6,000</u>	<u>675</u>

Part (a) (ii) Computation of Deemed Dividend Based on 2012/13 Profit

			Rs
Profit/(Loss) before Tax			90,590
Income Tax			<u>(2,644)</u>
Profit /(Loss) after Tax			87,946
Add: Depreciation on Assets acquired during the year			
Tank & Ponds	10,500	(100/95)x 5%	553
Building	50,000	x 5%	2,500
Hotel Equip	30,000	x 20%	<u>6,000</u>
			<u>9,053</u>
			96,999
Less: Capital assets acquired during the year			
9,053			
<u>82,000</u>			
<u>91,053</u>			(91,053)
Distributable Profit/(Loss)			<u>5,946</u>
Minimum 10% Distribution to be made			<u>595</u>
Actual Distribution			<u>22,000</u>
Hence no deemed dividend tax arises.			NIL
10% Dividend Tax on Actual Distribution			<u>2,200</u>

(25 marks)

(Part b)

Yes. At present company has invested an amount less than Rs. 100 million. Therefore company is entitling to a tax holiday of 4 years. However if the company invested further Rs. 50 million, the total investment of the company will be more than Rs. 100 million but less than Rs. 200 million. Therefore company is entitling to income tax exemption for a period of 5 years.

(5 marks)

(Total 30 marks)

Answer No. 02

Part (a)

**Mr. Siripala
Computation of Taxable Profit Y/A 2012/13**

<u>Employment Income</u>				
Non executive Director Fees	Net	PAYE	Gross	
ABC Plc	504,000	96,000	600,000	
PQR Plc	252,000	28,000	280,000	
XYZ (Pvt) Ltd	336,000	<u>64,000</u>	<u>400,000</u>	1,280,000
(PAYE tax @ 10% & 16%)		<u>188,000</u>		
Less: Employment tax credit is not applicable since non executive director fees				-
<u>Sale of Car-Rs. 6.5 M</u>				
Not a source of Income				-
<u>Rent Income & NAV</u>				
Rent				
Gross Rent 20,000 x 12=			240,000	
Less: Rates(350,000 @ 20%)			<u>(70,000)</u>	
			170,000	
Less: Repairs 25%			<u>(42,500)</u>	
Net Rent			<u>127,500</u>	
NAV				
Rating assessment			350,000	
Less: Repairs 25%			<u>(87,500)</u>	
NAV			<u>262,500</u>	
Whichever is Higher			262,500	
Occupiers Income(262,500-240,000)			<u>(22,500)</u>	
Exempted for 2007/08 + 6 Years as it does not exceed Sq.Ft. 1500 and constructed before 1.4.2008			<u>240,000</u>	Exempt
Agency Commission –US \$ 9,500/- Foreign Commission is Liable				1,200,000
<u>Share of Profit-Manufacture of Leather Slippers</u>				
<u>Adjusted Profit/Divisible Profit</u>				
Net Profit as per Accounts			350,000	
Add: Partners Drawings				
Depreciation			150,000	
Partners Salary			700,000	
Less: Rent Income			<u>(300,000)</u>	
Divisible Profit			<u>900,000</u>	

Division	Others	Siripala	Total	
Salary- 3/5 X 700,000	280,000	420,000	700,000	
Share of profit 1:1	<u>100,000</u>	<u>100,000</u>	<u>200,000</u>	
	380,000	520,000	900,000	exempt
Other Income-Rent				
Gross Rent	300,000			
Less: Repairs 25%	<u>(75,000)</u>			
Net Rent	225,000	112,500	112,500	<u>225,000</u>
				Liable
			225,000	112,500
Less: Tax Free Allowance			<u>(600,000)</u>	
Taxable Partnership Profit			NIL	
TOTAL STATUTORY INCOME				2,592,500
Less: HOUSING Loan Interest				(132,000)
ASSESSABLE INCOME				2,460,500
Less: Qualifying Payments				
Repayment of Loan capital- Rs. 47,000 (Not a Qualifying Payment)				-
Approved Charity-Sick & Needy				(10,000)
Approved Charity-Social Research-Rs.15,000 (Not a Qualifying Payment)				-
Personal Allowance				(500,000)
TAXABLE INCOME				1,950,500
Income Tax Payable				
First	500,000	@ 4%		20,000
Second	500,000	@ 8%		40,000
Balance	<u>950,500</u>	@ 10%		95,050
	<u>1,950,500</u>			155,050
Less: Tax Paid				
PAYE				<u>(188,000)</u>
Tax Over Paid-Can not be refunded or C/F				<u>(32,950)</u>
Self Assessment Payment				<u>(30,000)</u>
Refund Due				<u>30,000</u>

(15 marks)

Part (b)

Under the Section 3 of the Inland Revenue Act, the sources of income has been enumerated. Accordingly income from any other source whatsoever but excluding **profit from casual or non recurring nature will be liable to tax.** In this instance **it has to be clear whether he is doing a business or not.** If there is evidence that he is doing a business then the income will falling to business income. However in this instance it is clear that he is not carrying a business. Therefore **the income received is from casual or non recurring nature.** Profit on sale of Car imported with the financial assistance **is not liable to Income tax** on the basis that the income received from such sale is falling to the category of casual and non recurring nature.

(5 marks)

(Total 20 marks)

Answer No. 03**Part (a)**

Gunasekera Trust
Computation of Taxable Profit Y/A 2012/13

Rent Income			
Rent			
Gross Rent		2,400,000	
Less: Rates		<u>(80,000)</u>	
		2,320,000	
Less: Repairs 25%		<u>(580,000)</u>	
Net Rent		<u>1,740,000</u>	1,740,000
Interest Income			
Interest Income (Becomes Final tax since WHT is Paid)			
Not form part of Assessable Income	540,000		-
Interest on Treasury Bills- Tax Paid			
Not form part of Assessable Income	1,000,000		-
Dividend Income			
Since WHT Paid- Not form part of Statutory Income			
Donations from Public			
Tax exempt	600,000		-
NAV			
Office Building	150,000	Exempt	
TOTAL STATUTORY INCOME			
			1,740,000
Less: Statutory Deductions			
			-
ASSESSABLE INCOME			
			1,740,000
Less: Qualifying Payments			
Tax Free Allowance			
			<u>(500,000)</u>
TAXABLE INCOME			
			<u>1,240,000</u>
Income Tax Payable	1,240,000	@ 10%	124,000

(6 marks)

Part (b)

“charitable purpose” means a purpose for the benefit of the public or any section of the public in & outside Sri Lanka, of any of the following categories.

- (a) the relief of poverty;
- (b) the advancement of education or knowledge other than by any institution established for business purposes or by any institution established under the Companies Act;
- (c) activities for the protection of the environment or eco-friendly activities
- (d) the advancement of religion or the maintenance of religious rites and practices or the administration of a place of public worship;
- (e) any other purpose beneficial or of interest to mankind, not falling within any of the preceding categories;

(4 marks)

(Total 10 marks)

Answer No. 04

Part (a)

Jayland Enterprises Ltd
VAT Computation for the Q/E 31/03/2013

Output VAT	EXEMPT	LIABLE	RATE	OUTPUT VAT
Sale of Cosmetics		10,000,000	12%	1,200,000
Sale of Pharmaceuticals (Exempt)	30,000,000		-	-
Sale of delivery Van (1M x 100/112)	-	892,857	12%	107,143
Commission-India	-	600,000	0%	
Insurance Receipt-Cosmetics (200,000 X 100/112)		178,571	12%	21,429
Insurance Receipt-Pharmaceuticals (Exempt)	600,000	-		-
Commission in Foreign Currency		500,000	0%	-
	30,600,000	12,171,428		1,328,571

Less: Input VAT

VAT on Import of Cosmetics		600,000	
Others(Both Cosmetics & pharmaceuticals)	(200,000 x 10/40)	<u>50,000</u>	(650,000)
			678,571
Less: Unabsorbed VAT B/F from Previous Quarter			<u>(50,000)</u>
VAT Payable			628,571
Less:			
Unclaimed VAT B/F-Limited to 10% per month (100,000 x10%x3)			<u>(30,000)</u>
Balance VAT Payable			<u>598,571</u>

(10 marks)

- (b) The rules which govern the issue of a valid tax invoice are;
- i) A valid tax invoice can be issued only by a registered person to another registered person.
 - ii) A valid tax invoice can be issued only within a period of 28 days from the date of the supply

The Tax Invoice shall set out,

- i) The name, address & the registration number of the supplier.
- ii) The name, address & the registration number of the person to whom the supply was made.
- iii) The date on which the tax invoice issued and the serial number
- v) The date of supply and description of the goods & services.
- vi) The quantity or volume of the supply
- vii) The value of the supply ,the tax charges and the consideration for the supply
- viii) The words " TAX INVOICE" at a conspicuous place in such invoice.

(3 marks)

(Total 13 marks)

Answer No. 05

- (a) The assessor is not right. Mr. Seneviratne has no right or entitlement to receive the car. It is given to him as a matter of discretion of the company. It is not something given for services rendered. For it to be treated as part of employment income it should have been for services rendered. For these reasons it is not liable to tax. (Authority O Craib Vs CLT or J De Fonseka Vs CIR or Canagasabapathy Vs CIR)
- (5 marks)
- (b) The company is not doing any business in Sri Lanka because the contracts relating to the sales made to local buyers are not made in Sri Lanka (Anglo Persian Oil company Ltd Vs CIT) but the company would have been liable to tax in Sri Lanka due to the operation of Section 80 (instrumentality) (Chivers Sons Ltd Vs CIT) but in the absence of a permanent establishment under the treaty provision the company is not liable to tax in respect of the profits.
- (5 marks)
- (c) Under section 25 of the Inland Revenue Act only expenditure incurred in the production of income is deductible. Expenditure incurred in the production of income means expenditure directly related to the production of income. It is not sufficient that it is remotely connected with the production of income (Ward & company Ltd Vs CIT New Zealand or David Appuhamy Vs CIR). The expenditure in question does not fall into this category therefore it is not deductible. It is deductible under the wider rule of deduction in the U.K.

(5 marks)

(Total 15 marks)

Answer No.06

- (a) Foreign tax credit mean credit given against the tax payable in one country for tax paid in another country.

Credit is given by the country of residence (where the tax payer is resident)

The credit is allowed subject to the condition that it cannot exceed the amount of tax payable on similar income in the country of residence.

(7 marks)

- (b) What is not a permanent establishment

1. Use of facilities solely for storage, display of delivery of goods.
2. Maintenance of a stock for stock storage, display of delivery.
3. Maintenance of a stock of goods for processing by another enterprise.
Having a fixed place of business for the purpose of purchasing goods or collecting information
4. Maintenance of affixed place of business for the purpose of advertising, supply of information etc. if the activity is of a preparatory nature.

(5 marks)

(Total 12 marks)