



Association of Accounting Technicians of Sri Lanka

July 2016 Examination - AA3 Level

**Questions and Suggested Answers
Subject No : AA35**

**CORPORATE AND PERSONAL TAXATION
(CPT)**

Association of Accounting Technicians of Sri Lanka
No. 540, Ven. Muruththettuve Ananda Nahimi Mawatha,
Narahenpita, Colombo 05.

Tel : 011-2-559 669

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THE ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

EDUCATION AND TRAINING DIVISION

AA3 Examination - July 2016
(35) Corporate and Personal Taxation

SUGGESTED ANSWERS

SECTION – A

Four (04) compulsory Questions
(Total 20 marks)

Suggested Answers to Question One:

- **Equity**
All the people have to bear the public expenses based on their ability to pay.
- **Progressivity**
Higher income group has to be paid proportionally more tax than the lower income group.
- **Economy**
The minimum possible amounts have to be spent to collect the tax revenue.
- **Certainty**
Time of payment, the manner of payment and the amount payable have to be clear and plain to the contributors as well as to every other person.
- **Adequacy**
Tax revenue has to be sufficient to cover the expected portion of the Government expenses.
- **Simplify**
Tax system should be simple, easy and understandable to the public.
- **Broad base**
The tax system should be spread over to cover more and more tax payers.

Note:

Explanations regarding the five principles are enough to take entire marks

(05 Marks)

Suggested Answers to Question Two:

Following activities can be identified as taxable activities which are liable to VAT

- a. Any activity carried on as business (Trade, Business, Profession or Vocation or every adventure or concern the nature of a trade).
- b. Provision of facilities to its member or others for a consideration and payment of subscription in the case of a club, association or organization.
- c. Any activity is done in connection with commencement or cessation of business institution or other institution (club, association or organization).
- d. The hiring or leasing of any movable or immovable property or administration of any property.
- e. The exploitation of any intangible property such a patents, copyright or other similar assets (Such asset is registered in Sri Lanka or the owner of such asset is in Sri Lanka)

(05 Marks)

Suggested Answers to Question Three:

As provisions of Economic Service Charge (ESC) Act, relevant to the quarter ended March 31, 2015, if any business which is available an adjusted tax loss in the previous year of assessment or Full or Part of the Income which is exempted from Income tax at current period and exceed the turnover is more than 50 million for relevant quarter, is liable to pay ESC.

Agri Seed (Pvt) Ltd is available an adjusted tax loss in the previous year of assessment, profit from production of seed is also exempted from Income tax and turnover has exceeded more than 50 million Therefore, company is liable to pay ESC.

Total Turnover of the Quarter	-	70,275,000
Less: Turnover not liable to ESC		
Sale proceeds on Office Equipment	-	(2,225,000)
Interest Income	-	(750,000)
Turnover liable to ESC*	-	<u>67,300,000</u>

*** due to available adjusted tax loss on previous year of assessment, both income tax liable and exempted income are liable to ESC.**

ESC Liability = 67,300,000 * 0.25%

168,250/-

(05 Marks)

Suggested Answers to Question Four:

Goods worth of Rs.500,000/- were damaged due to flood. Damaged good was contained on working capital (paper Stock) and flooding is a natural disaster and it is an involuntary incident. Loss was reduced up to Rs. 200,000/- by the insurance claim of Rs. 300,000/-.

According to the decision given on decided tax case Law, “Hayley Company Vs. CIR, Outgoing is included the losses. Such outgoing should be incurred for the production of income and loss have to be represented the working capital and not for fixed capital. Further noted, as General rule of the Inland Revenue Act regarding the calculation of adjusted business profit, it has allowed deducting the involuntary outgoing that incurred for the production of income.

As per matters related to the Paper (Pvt) Ltd, loss related to paper stock (working Capital) and it has happen due to flood (Involuntary outgoing). Therefore, we can decide assessor’s decision was not correct in term of decided case law and the provision of the Inland Revenue Act.

(05 Marks)



End of Section A

Three (03) compulsory questions
(Total 30 marks)

Suggested Answers to Question Five:

(a) **Calculation of the Divisible Profit**

Suresh and Naresh Partnership

Year of Assessment 2015/2016

Calculation of the Divisible Profit

	+	-
Net Profit As Accounts	846,000	
Removed – Other sources of Income -Interest Income received on Savings Account		8,000
Rent paid to the Naresh for building Rs.120,000 allowed Related with business	0	
Accounting Depreciation - Disallowed	20,000	
Depreciation Allowance for Equipment 90,000/ * 33 1/3%		30,000
Salaries to partners - Disallowed Suresh Naresh	192,000 192,000	
Other expenses- allowed for tax Purpose	0	
	1,250,000	38,000
Divisible Profit	<u>1,212,000</u>	

(b) Calculation of the Partnership Tax Liability

Divisible Profit	1,212,000
<u>Other Sources of Income</u>	
Gross Interest Income	<u>8,000</u>
	1,220,000
Partnership Tax free Allowance	<u>(1,000,000)</u>
Taxable Income	<u>220,000</u>
Partnership Tax Liability	220,000/- * 8%
	<u>17,600</u>

(c) Distribution of Profit and Income among the Partners

	Suresh	Naresh	Total
Salaries	192,000	192,000	384,000
Share of Profit	414,000	414,000	<u>828,000</u>
			1,212,000
Other Source of Income			
Gross Interest Income	4,000	4,000	8,000
Rent	-	120,000	120,000
	610,000	730,000	1,340,000

(10 marks)

Suggested Answers to Question Six:

Spicy World (Pvt) Ltd

Quarter ended March 31, 2015

Calculation of VAT payable

Out Put Tax			
Sales to Local Market	2,850,000 * 11%	313,500	
Suspended Supply (SVAT)	845,000 * 11%	92,950	
Direct Exports (12,500*130)	1,625,000 * 0%	<u>0</u>	406,450
Input Tax			
Importation		0	
Local Purchases (Note 1)		<u>128,100</u>	
Input for the Period		128,100	
Disallowed Input tax		<u>0</u>	
Allowed Input for the Period		128,100	
B/F Unabsorbed Input Tax		<u>74,000</u>	
Total Input tax available to deduct		202,100	
Deductible Input Tax			
Related to Export and SVAT (Note 2)	59,475		
Related to other (Note 3)	<u>142, 625</u>	(202,100)	(202,100)
C/F Input tax		0	
Gross VAT Payable			204,350
Tax Credit			
SVAT Vouchers		(92,950)	
Installment Payment		(80,000)	(172,950)
Balance VAT Payable			31,400

(10 Marks)

Note 01: Input from Local Purchases

Input for local Purchases	-	144,600
Less : input adjustment to tax credit note from supplier	-	<u>(16,500)</u>
		<u>128,100</u>

Note 02: Deductible Input tax for Export and SVAT

Export and SVAT supplies * allowable Input tax for the period

$$\begin{array}{rcl} & \text{Total Supply} & \\ 2,470,000 * 128,100 & = & \underline{\underline{59,475}} \\ 5,320,000 & & \end{array}$$

Note 03: Deductible Input tax for other supplies

-	Remaining Input Tax	- 142,625/-	} whichever is lower
	(Total allowable Input tax – deducted for exports) (202,100 - 59,475)		
-	100% of Output tax (other than SVAT)	- 313,500/-	} 142,625/-
	(313,500* 100%)		

Suggested Answers to Question Seven:

- (a) Return of Income for year of Assessment 2014/15 have to be submitted on or before November 30, 2015
- (b) Benefits of submitting the Return of Income on or before due date can be mentioned as follows,
- No any possibility to impose the penalties due to non-submission of Return of Income.
 - No any possibility to issue the estimated assessment due to non-submission of the Return of Income.
 - Time bar period is limited to 18th months from date on which return of Income is due (from November 30th). If there is a delay or non-submission it will be extended up to 4 years.
- (c) Following action can be taken by Commissioner General of Inland Revenue on failure to furnished the Return of Income,
- Maximum Rs. 50,000/- penalty can be imposed.
 - Estimated assessment can be issued.
 - Legal case can be filled before the majestic court.
- (d) Proves to the satisfaction of the Commissioner-General regarding the failure to furnish a return for following circumstances,
- Was due to circumstances beyond his control and he has furnished such return later.
 - Has complied with such requirement at the point of imposed the penalty.

(10 marks)

End of Section B

Two (02) compulsory questions.

(Total = 50 marks)

Suggested Answers to Question Eight:

				+	-
Net Profit before Tax				17,489,450	
Book Depreciation				1,602,840	
Depreciation allowance					
Land	2,000,000	-	-		
Buildings	12,000,000	6 2/3	-		
Furniture	860,000	20	172,000		
Plant and Machinery	7,290,000	12 1/2	911,250		
Computers	435,000	25	fully claimed		
Office equipment - 10/11	236,000	12 1/2	29,500		
Office equipment - 14/15	42,000	50	21,000		1,133,750
Profit from Disposal of Machine					180,000
Cost			1,250,000		
Depreciation allowance claimed	12.5% x 4 x 1,250,000		625,000		
Tax written down value			625,000		
Sale Proceeds			430,000		
Tax loss on disposal					195,000
Replaced Machine					
Depreciations allowance for new asset - Export company	2,400,000	50%			1,200,000
	Disposal of Machine				
Cost	1,250,000	Acc. Depre- ciation	1,000,000		
Profit	180,000	Cash	430,000		
	1,430,000		1,430,000		
Export Development Rebate - exempted (sec. 13 (qqqq))					500,000
Interest Income - Separate source					265,000
Advertising					
- To sale of Machine*	Disallowed			15,000	
- Foreign media	100% Allowed for expert promotion outside SL				
Royalty Paid	Allowed			-	
Foreign Travelling - Production Manager 2% of business profit of previous year			250,000	15,000	
Trade fair - allowed					
Research Expenses	300%			-	2,000,000
Donation				600,000	
				19,722,290	5,473,750
				(5,473,750)	
Adjusted Trade Profit				14,248,540	

Computation of Income Tax					
Income from Trade, business				14,248,540	
Interest Income			exempt	-	
Total Statutory Income				14,248,540	
Less - Deductions under Sec. 32					
Losses brought forward	limited to 35% of TSI	5,024,439		(2,435,000)	
Assessable Income				11,813,540	
Less - Allowance for Qualifying Payments					
Donation to Government (sd. State)				(600,000)	
Taxable Income				11,213,540	
Income tax on profits from business		11,213,540	12%	1,345,625	
Gross tax liability				1,345,625	
Less -					
Self-Assessment payments				750,000	
Balance Income Tax payable				595,625	

(25 marks)

Suggested Answers to Question Nine:

<u>Income from Employment</u>			
Salary (100,000 x 12)			1,200,000
Production Incentive			100,000
Residence allowance (50,000 x 12)			600,000
Value of conveyance	420,000		
(exempted lower of value of one vehicle or Rs. 50,000p.m.)			
Gift	not taxable		
			1,900,000
<u>Rent Income - Income from properties</u>			
Gross rent (20,000 x 12)	240,000		
- rates paid	(18,000)		
	222,000		
- 25% of allowance	(55,500)		
Net rent	166,500		
<u>Comparison</u>			
Annual Value	90,000		
-25% of allowance	(22,500)		
	67,500		
Net rent > NAV			
Rent Income			166,500
Sale on Shares	Exempt		

<u>Interest Income</u>			
Fixed Deposit - WHT is deducted (69,000 / 92) x 100			75,000
Dividend Income			
Paid out of dividend received		18,000	
Paid out of profits and income		7,000	25,000
Statutory Income			2,166,500
Child's Income			3,000
Total Statutory Income			2,169,500
Less - Income which does not form part of Assessable Income			
Dividend Income		25,000	
Interest Income		75,000	(100,000)
			2,069,500
Less - Deductions under Sec. 32			
Interest Paid (on personal loan) (not allowed)			-
Assessable Income			2,069,500
Less - Allowance for Qualifying Payments			
Donation to Api Wenuwen Api Fund		(100,000)	
Donation to an approved charity	(20,000)		
Limited to lower of 1/3 of AI or Rs. 750,000/- or actual		(20,000)	
QP on employment income		(100,000)	
Tax free allowance		(500,000)	(720,000)
Taxable Income			1,349,500
Tax Liability			
On first Rs. 500,000/- @ 4%		20,000	
On next Rs. 500,000/- @ 8%		40,000	
On balance Rs. 349,500/- @ 12%		41,940	
		101,940	
Less - Tax Credits			
Self-Assessment Payments		(10,000)	
PAYE		(96,000)	
Balance Payable / (Refund receivable)		(4,060)	

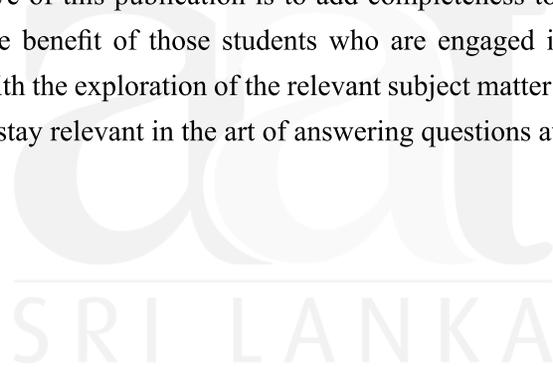
(25 marks)

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