

EXAMINER'S REPORT

Level III EXAMINATION - JANUARY 2025

(304) CORPORATE & PERSONAL TAXATION

Question No. 01**Part (a)****What was tested?**

This question was tested the residency status under Section 69 of the Inland Revenue Act No. 24 of 2017 (hereafter referred to as the act) (as amended) of individual who has migrated to Australia on 25.09.2023, and came back to Sri Lanka on 15.03.2024, and again departed on 25.03.2024.

Accordingly, in terms of Section 69 (1) of the act, an individual shall be a resident in Sri Lanka for a year of assessment if such individual,

- (1) resides in Sri Lanka;
- (2) is present in Sri Lanka during the year and that presence falls within a period or periods amounting in aggregate to 183 days or more in any 12 month period that commences or ends during the year;
- (3) is an employee or an official of the Government of Sri Lanka and his spouse is posted abroad during the year; or
- (4) is an individual who is employed on a Sri Lanka ship, within the meaning of the Merchant Shipping Act, during the period the individual is so employed.

Observations:

- (1) Almost all candidates have attempted the question.
- (2) Majority of candidates have correctly answered the question by referring to the residence rule.
- (3) Eventhough some candidates have decided that the said individual has a tax residency in Sri Lanka they failed to state 183 days rule.
- (4) Some candidates have lack of understanding on the residence rule as they have incorrectly mentioned the number of days required to be considered as a resident in Sri Lanka.

Performance: The performances were in a satisfactory level.

Question No. 02

Part (a)

What was tested?

This part was tested the fundamental knowledge of Social Security Contribution Levy (SSCL), which was payable under Social Security Contribution Levy Act No. 25 of 2022 by every taxable person. Accordingly, this question was required to calculate the SSCL for the quarter ended 31st March 2024.

Observations:

- (1) Majority of the candidates have calculated the SSCL on the total Turnover correctly.
- (2) Some candidates have failed to identify tax rate under SSCL Act.

Performance: The performances were in a satisfactory level.

Part (b)

What was tested?

This question was tested the fundamental knowledge of Share Transaction Levy (STL), which was imposed under the Finance Act No. 5 of 2005 to charge a levy on quoted public company share transactions, taking place in the Colombo Stock Exchange. Accordingly, the question was required to calculate STL on disposal of shares.

Observations:

- (1) The majority of candidates have failed to answer the question correctly.
- (2) Most of candidates incorrectly applied tax rate as 3% instead of 0.3%.

Performance: The performances were not in a satisfactory level.

Question No. 03

What was tested?

This case law question was based on the case law that emerged from the judgment of **Davoodbhoy Vs. CGIR (1979) 4 SLTC 122**. The question was required to provide the answer in line with the said case for a situation in which two partners carry out partnership to share profits and losses at 2.1 ratio. The important aspect was that one partner (**Sirisena**) has planned to enter into another agreement with his son to share his profit share of the main partnership.

The question was required to explain income tax application of the agreement between **Sirisena** and his son by referring to the case Vs CGR and the provisions of Inland Revenue Act No. 24 of 2017.

As per the facts of the above case, Abasbhoy Davoodbhoy was one of the five partners of Abdul Hassen Davoodbhoy partnership, and was entitled to receive a one fifth share of the partnership. He has entered into another agreement with his children to share his one fifth share of the said partnership. Under the agreement, the capital and goodwill in the partnership was a property of

appellant Davoodbhoy was to remain his separate assets. The only asset of that new agreement was the one fifth share of Abdul Hassen Davoodbhoy partnership. But this agreement was rejected by both the Commissioner General of Inland Revenue as well as the Board of Review.

First, it came to the Court of Appeal and decided that there cannot be a valid partnership if the agreement is merely sharing the profits and losses of one partnership in another partnership without anything more.

Finally, the case came to the Supreme Court by way of question of law, it was held that the agreement was not artificial and fictitious and it incorporates a family arrangement that was genuine and very common in our society.

However, Section 195 of the act does not allow the above type of sub partnership agreement by defining that a “partnership means an association of two or more individuals or corporations carrying on business jointly for the **purpose of making profit**, irrespective of whether the association is recorded in writing”.

Hence, as per the above definition, sub partnership formed among children is valid in law provided that if carrying on business jointly **for the purpose of making profit**.

Observations:

- (1) The most of candidates failed to understand how to apply the facts of a given question to a decided case law.
- (2) Even though the question was required to answer with reference to the decided case and provisions of the act, the most of candidates were failed to do so.
- (3) The majority of candidates have not adequately described the case given, and they simply repeated the question itself rather than providing the substantive answer.
- (4) Some candidates have concluded that there is a valid partnership without proper justification or explanation.
- (5) Only very few candidates have correctly identified the facts of the given case and provided the expected answer by referring to the both case law as well as provisions of the Act.
- (6) Some candidates have written lengthy paragraphs and question itself repeatedly, but the important points that should be included in the answer were completely omitted.

Performance: The case law knowledge of the candidates was not in a satisfactory level.

Question No. 04

Part (a)

What was tested?

This question was tested the fundamental knowledge of Advanced Income Tax (AIT), which was imposed under Division II of the Act to charge taxes that are payable by withholding. Accordingly, the candidates were required to calculate the AIT on;

- (1) Rent payment to a resident, and
- (2) Interim dividend paid out of current year's profit.

Observations:

- (1) Most of candidates have not attempted this part of the question.
- (2) The majority of candidates did not possess the knowledge at all on the relevant AIT rates those are applicable for the rent and dividend payment.

Performance: The knowledge of AIT was poor and therefore the performance was also not in a satisfactory level.

Part (b)

What was tested?

This question was required to state three obligations of employer under Advanced Personal Income Tax (APIT) scheme.

Observations:

- (1) The majority of candidates have correctly answered the question.
- (2) Some candidates provided answers which are not related to this question at all.

Performance: The performances were good.

Question No. 05

What was tested?

This question was required to calculate the balance payable / (overpaid) of Value Added Tax (VAT) for the quarter ended 31.03.2024 by an entity, which was engaged in the business of manufacturing and selling toys.

Observations:

- (1) Almost all candidates attempted the question.
- (2) Eventhough the applicable VAT rate has been given as 18% in the question itself, some candidates have applied 15% VAT rate in their computations.
- (3) Most of candidates incorrectly charged VAT on export sales that must be charged at zero rate.
- (4) Some candidates incorrectly claimed common office expenses as input credit in arriving at balance tax payable.
- (5) Considerable number of candidates failed to understand the difference between liable supply and zero rated supply.

- (6) The excess input tax brought forward from the previous quarter and installment payment were deducted by the majority of candidates.
- (7) Most of candidates failed to secure marks for relevant heading of the computations because of not mentioning what they have arrived through calculations.
- (8) Handful number of candidates have answered the question using ledger account mode by disregarding the correct format of the VAT return.
- (9) Few candidates have arrived at the correct answer without following all the steps outlined in the marking scheme. In such cases, Marking Examiners were unable to allocate full marks.
- (10) The knowledge pertaining to input-output mechanism of VAT was understood by the majority.

Performance: The knowledge of VAT was good.

Question No. 06

What was tested?

This question was tested the fundamental knowledge in relation to tax administration, which included return submission, quarterly installment payments, and authorized persons. Accordingly, candidates were required to state

- (1) Due date for filling Statement of Estimated Tax (SET) payable for Y/A 2023/24
- (2) Due dates for quarterly installment payments for Y/A 2023/24
- (3) Whether the taxpayer has to file a return of income when there is taxable loss.
- (4) Persons who can be "Authorized Persons".

Observations:

- (1) Majority of candidates have not attempted all four parts of the question.
- (2) Due date for filling SET was not known by the majority.
- (3) The most of candidate failed to answer the question of quarterly installments payment dates that can be considered as an important knowledge of taxation.
- (4) The correct status of filling a return of income when there is a taxable loss was not known by almost all candidates.
- (5) Persons who can act as an authorized persons have been recognised by many candidates. However, certain candidates have provided irrelevant answers such as names of politicians.

Performance: The performances in relation to tax administration was very poor.

Question No. 07

What was tested?

This question was tested the fundamental knowledge on partnership taxation in terms of Section 53 to 56 of the Act. The question was required to calculate the Income Tax payable by a partnership for the Y/A 2023/24, which included,

- (1) Partners' salaries.
- (2) Rates for the building.
- (3) Accounting depreciation.
- (4) Donation.
- (5) Other income.

Observation:

- (1) Almost all candidates attempted the question, and the majority of them secured average marks for the question.
- (2) Correct treatment for book depreciation, claiming capital allowance for the same, partners' salaries, and donation have properly adjusted by the majority of candidates.
- (3) However, some candidates have erroneously added back the total rates, which is disallowed only 50% in arriving at the partnership income.
- (4) Some candidates have not properly calculated the investment income and WHT claim on the same.
- (5) Many candidates have consistently confused with adjustments of business profit. Some candidates have added income that should be deducted and deducted expenses that should be added back to the profit.
- (6) Some candidates have not added back donations to the accounting profit but incorrectly deducted them as qualifying payments, and some have ignored donation under qualifying payments.
- (7) Taxing first Rs.1,000,000/- at 0% and balance at 6% have correctly done by many candidates. It was noticed that some candidates have not updated their knowledge about tax rates. Some candidates have used progressive rates and company tax rate 30% to tax the partnership.
- (8) Some candidates have incorrectly claimed Rs.1,000,000/- as partnership allowance without taxing at 0%.

Performance: The knowledge of partnership taxation was good.

Question No. 08

What was tested?

The fundamental knowledge on corporate taxation for the Y/A 2023/24 was tested by this question. Accordingly, the question was required to,

- (1) Compute the Assessable Income, Taxable Income, gross Income Tax payable, and balance tax payable / (overpayment) by a resident company.
- (2) To decide the Income Tax rate when the company is engaged in the business of publishing.
- (3) To evaluate the practical aspect of applying general deductions under Section 10, main deductions under Section 11, and specific deductions under Section 12 to 19 of the Act in ascertaining the business profit.

Observations:

(1) **Average marks secured:**

Almost all candidates attempted the question, and the majority have secured average marks for this question.

(2) **Presentation format:**

The presentation and identification of statutory contents of the corporate Income Tax computation have been understood by the most of candidates. However, few candidates who are still experiencing difficulties to keep up with statutory contents and presentation of corporate Income Tax computation.

(3) **Other income:**

Most of candidates have eliminated the interest and dividend income as separate sources of income from accounting profit when arriving at the business income.

(4) **Book depreciation, asset disposal and capital allowances:**

Book depreciation has been added back to the accounting profit by almost all candidates. Further, the majority have applied the correct rates of 5 years to claim capital allowances for building, plant and machinery, office equipment, and computers, which were purchased in the Y/A 2020/21.

The accounting loss on machinery disposal was not added back to the accounting profit by many candidates. Also, the assessable charges on machinery disposal was not computed by majority of candidates. Even though, some candidates have correctly calculated the assessable charge on machinery, but the same amount was not added to the accounting profit in arriving at the Assessable Income from business.

(5) **Disallowable expenses:**

Provision for gratuity and donation correctly added back to the accounting profit by the majority of candidates. But, most of the candidates failed to make correct treatment for sponsorship for LPL Cricket Series, director's participation fees, ticket fees for a conference in America on digital communication technologies and free of charge publishing advertisement of SOS children's village.

(6) **Allowable expenses:**

Payment of gratuity was claimed by the majority.

(7) **Investment income:**

Interest from fixed deposit was correctly treated as investment income by many candidates. Further, some candidates have erroneously taken in to account the dividend income for which WHT has been deducted as an investment income.

(8) **Qualifying payments and reliefs:**

The donation made to the government properly claimed by many candidates. But, donation to an approved charity, which has a limitation of lower of 1/5 of the Taxable Income or Rs.500,000/- was not understood by many candidates.

(9) **Identification of tax rate:**

Identifying the correct tax rate as 30% was done by the majority. However, few candidates have still applied the individual progressive rates (6% to 36%) to tax the company.

(10) **Identification of tax credit:**

Quarterly installment payment was claimed as a tax credit by the majority. However, withholding tax on interest was not claimed by many candidates.

Performance: The overall performances were good.

Question No. 09

What was tested?

This question was required to ascertain personal Income Tax for the Y/A 2023/24 of a resident individual who worked as a Software Engineer. The sources of income included income from employment, business, and investment.

Observations:

The question was attempted by almost all candidates, and the fundamental knowledge of candidates performing to the individual taxation was in a satisfactory level. Most of the candidates secured average marks out of allocated marks.

The observations are listed below:

(a) Employment income:

- (1) The majority of candidates have included the gross salary in the employment income. However, some candidates have considered only monthly salary for their computation.
- (2) Bonus paid in the previous year has been correctly included in employment income in the current year by many candidates.
- (3) Travelling allowance and vehicle allowance were correctly treated as employment income by many candidates.
- (4) APIT was deducted from employment income by considerable number of candidates.

(b) Business income:

- (1) The business income derived from agriculture from coconut estate in Kurunegala is an exempt income. However, this exemption has not recognized by the majority of candidates.
- (2) The time consumption to compute the business income from agriculture was a loss for the candidates.
- (3) Ad hoc service income from IT services was not clearly identified separately as business Income, and the most of the candidates have classified it under Investment Income included as a point in business income.

(c) Investment income:

- (1) Interest of fixed deposit has been taken into account as an investment income after grossing up by many candidates.
- (2) Many candidates have failed to identify quoted company share dividend as exempt income.
- (3) Identification of gross rent income as an investment income was in a satisfactory level.

(d) Common omissions and mistakes:

- (1) Rs.1,200,000/- was not claimed as personal relief by considerable number of candidates.
- (2) Certain candidates incorrectly claimed tax credits from Taxable Income directly without computing the tax liability.
- (3) Certain candidates have applied progressive rate ranging from 6% to 36%, and some candidates have combined progressive rates with 30% for business profit.
- (4) WHT on interest was not considered by many candidates.

- (5) Some candidates have not applied the correct flow of the individual return of income when reaching total Assessable Income, qualifying payment and relief, Taxable Income, gross tax liability, tax credits, and balance tax payable. For example, qualifying payments and quarterly installments payments have been claimed prior to the Assessable Income.
- (6) Some candidates have stopped tax computation at Taxable Income without completing the rest of the answer.
- (7) Most of the candidates have tried to make the entire answer on a single page. This resulted in difficulties for the Marking Examiner to provide marks as some of the workings were not clear.

Performance: The performances were good.

The Overall Performance:

The majority of candidates have secured satisfactory marks the question related for VAT, partnership taxation, corporate taxation, and individual taxation. However, certain poor performances have been displayed in the areas of case law, and tax administration. Particularly, the knowledge pertaining to return submission and installment payments were in extremely poor position.

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Common Reasons for Certain Poor Performances:

- (1) Devoting too much attention on arithmetical calculation rather than fundamental principles in taxation and respective taxing laws.
- (2) Lack of awareness on relevant taxing laws and its subsequent amendments.
- (3) Poor attention to read the question paper properly before starting to answer the questions. This resulted to forget certain important requirements of the question due to misunderstanding.
- (4) Not devoting enough attention to past question papers and model answers that help to improve the examination skills.
- (5) Less attention on the study pack in which the most of fundamental principles and taxing laws have been properly explained.
- (6) Poor time management in answering the question paper, and some candidates have written lengthy answers for small marks.
- (7) Certain realistic assumptions were missing while unrealistic assumptions were made.
- (8) Failing to understand the actual requirement of each question properly that permits candidate to organize the answer including the format and presentation.
- (9) Illegible handwriting that created difficulties for Examiners to understand the facts of answers. Sometime, answers were impossible or almost impossible to read because of being very untidy or not clear.

- (10) Lack of relevant workings for answers or workings were not properly linked with the computations, resulting Examiners were not able to grant full marks allocated for the questions.
- (11) Some candidates did not show the proper workings to support their figures, which they have arrived in the process of calculation.

Suggestions for Improvements:

- (1) Paying attention on time management before answering to the question paper, which allows candidates to understand the certain important requirements of the questions. It is utmost important to summarize the answer as much as possible based on the requirement of the questions and marks allocated.
- (2) Answering the past question papers and check with model answers in order to improve the examination skills.
- (3) Devoting full attention to the study pack because of all areas in the question paper are covered by the study pack. It is important to bear in mind that there is a possibility of testing different areas in the study pack.
- (4) Stating clear and realistic assumptions, which are useful in granting certain marks for answers. It is important to remind that candidates are not allowed to make unrealistic assumption to alter the given facts of the questions itself.
- (5) Focusing on basic fundamental principles of taxation rather than arithmetical accuracy of calculations.
- (6) Providing appropriate workings for each and every calculations whenever necessary and link them properly with relevant answers.
- (7) Answering the question paper with legible handwriting that allows the Examiners to understand the facts clearly.
- (8) Answering a new question on a new page of the answer booklet.
- (9) Candidates are advised to read the question paper more than once to understand the requirement clearly and avoid writing irrelevant answers and calculations that will save time.
- (10) Always use the reading time 15 minutes to read the question paper fully and then start to answer questions based on the confident level of each question.

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