



**ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA**

**AA3 EXAMINATION - JANUARY 2016**

**(AA35) CORPORATE AND PERSONAL TAXATION**

• **Instructions to candidates** (Please Read Carefully):

- (1) **Time Allowed:** Reading : 15 minutes  
Writing : 03 hours

31-01-2016  
Afternoon  
[1.45 – 5.00]

No. of Pages : 09  
No. of Questions : 09

- (2) **All questions should be answered.**
- (3) **Answers should be in one language, in the medium applied for, in the booklets provided.**
- (4) **Submit all workings and calculations. State clearly assumptions made by you, if any.**
- (5) **Use of Non-programmable calculators is only permitted.**
- (6) **Action Verb Check List with definitions is attached. Each question will begin with an action verb. Candidates should answer the questions based on the definition of the verb given in the Action Verb Check List.**
- (7) **100 Marks.**

**SECTION A**

Four (04) compulsory questions

(Total 20 marks)

**Question 01**

**Supertec (Pvt) Ltd.** is an overseas company registered in Sri Lanka under Companies Act No. 07 of 2007. **Jayasooriya**, a citizen of Sri Lanka, is the Country Head of **Supertec (Pvt) Ltd.** He has travelled abroad several times during the year and details are given below:

Departure from Sri Lanka	Arrival to Sri Lanka
23.03.2014	08.05.2014
27.07.2014	16.09.2014
10.11.2014	07.01.2015
02.03.2015	28.04.2015

**You are required to,**

**Identify** the resident status of:

- (a) **Supertec (Pvt) Ltd.** and, (03 marks)
- (b) **Jayasooriya**, (02 marks)

for taxation purposes in Sri Lanka in relation to year of assessment 2014/15. (Total 05 marks)

## Question 02

**Mr. Soysa** was divorced from his wife in June 2014. His daughter **Nethmi** who is 15 years old lives with her mother, **Mrs. Soysa** from that date, and all her expenses are borne by **Mrs. Soysa**.

You are the tax consultant of **Mr. Soysa**.

**You are required to,**

**Explain** him on the following:

- (a) Who is a "Child" for the purposes of the Inland Revenue Act No. 10 of 2006? (03 marks)
- (b) To whom is **Nethmi's** income aggregated? (02 marks)

(Total 05 marks)

## Question 03

**Perera**, a long standing employee of **AB Ltd.** who had to undergo a heart surgery in January 2015, was paid a special payment of Rs.100,000/- for this purpose by the company. This payment was referred to as a bonus payment by the company.

**You are required to,**

**Explain** the chargeability of this payment for income tax of **Perera** based on the provisions of the Inland Revenue Act. (Refer to any case law in Sri Lanka to substantiate your explanation)

(05 marks)

## Question 04

**State** the activities chargeable with Nation Building Tax (NBT), according to the provisions of the Nation Building Tax Act.

(05 marks)

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*End of Section A*

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## SECTION B

Three (03) compulsory questions

(Total 30 marks)

### Question 05

**Sudath** is an attorney-at-law and he commenced his practice in the year 2012. **Jagath**, a friend of **Sudath**, joined as a partner of **Sudath's** firm and started a Partnership in the year 2013. Name of the new business is **SJ Associates**. **Sudath** and **Jagath** agreed to share profits in the ratio of 2:1 respectively. **Sudath** is entitled for a salary of Rs.50,000/- per month.

Financial information of the partnership for the year of assessment 2014/15 is as follows:

	US \$	Rs.	Rs.
Professional fee:			
Local currency			10,000,000
Foreign currency	25,100		3,539,100
			13,539,100
Less:			
Salary		4,200,000	
Telephone		125,000	
Stationery		45,000	
Depreciation		36,800	
Electricity		55,000	
Interest		258,000	
Water		36,000	
Expenses incurred to earn foreign currency income		525,000	(5,280,800)
			8,258,300
Share of profit: <b>Sudath</b>		5,505,533	
<b>Jagath</b>		2,752,767	(8,258,300)
			-

**Notes:**

- (1) Depreciation allowance for tax purposes is Rs.60,000/-.
- (2) Salary includes Rs.600,000/- paid to **Sudath** as his salary.
- (3) Interest was paid to **Jagath** for the loan provided by him to **SJ Associates**.
- (4) Professional fee in foreign currency have been received for the services rendered in foreign countries and those earnings have been remitted to Sri Lanka.

**You are required to,**

- (a) **Calculate** the Divisible Profit of the Partnership. (03 marks)
- (b) **Prepare** Statement of Profit Distribution. (03 marks)
- (c) **Calculate** the tax payable by the Partnership. (04 marks)

**N.B:** State reasons, if any receipt is considered exempted from tax.

(Total 10 marks)

## Question 06

**Sharp Associates** is a firm of Chartered Accountants and is engaged in the business of providing professional accounting services. Following information for the quarter ended 30<sup>th</sup> June 2015 were extracted from the books of **Sharp Associates**:

(1)

Invoices Issued:	Value of Supplies
For services provided to local clients	Rs.4,250,000
For services provided to non-resident(foreign) clients for payment in USD (US \$ 1 = Rs.141)	US\$ 6,500

(2) Rs.166,500/- has been received from sale of a photocopy machine to a non-registered person for Value Added Tax (VAT).

(3)

Input VAT	Rs.
On office expenses	130,000
For repair of a vehicle used for travelling	11,000

(4) Unabsorbed input VAT brought forward from previous quarter is Rs.36,000/-.

(5) VAT of Rs.120,000/- has been paid in installments.

**You are required to,**

- (a) **Assess** the balance amount of VAT payable for the quarter ended 30<sup>th</sup> June 2015. (07 marks)
- (b) **State** the due dates for the payment of VAT for the quarter ended 30<sup>th</sup> June 2015. (03 marks)
- (Total 10 marks)

## Question 07

**Mathurata (Pvt) Ltd.** is a resident company engaged in the business of manufacturing rubber based products. The company has filed its return of Income for the Year of Assessment 2013/14 on time. The Deputy Commissioner has rejected the return and has issued an assessment. The company wishes to appeal against the assessment.

**You are required to,**

- (a) **State** the requirements of a valid Income tax appeal. (04 marks)
- (b) **State** instances where Commissioner General of Inland Revenue may entertain a late appeal. (03 marks)
- (c) **State** the next step on receipt of a valid appeal that will be taken by the Commissioner General of Inland Revenue in respect of such appeal. (03 marks)
- (Total 10 marks)

End of Section B

## SECTION C

Two (02) compulsory questions.

(Total 50 marks)

### Question 08

**Rajarata Importers (Pvt) Ltd.** was incorporated on 01<sup>st</sup> April 2014, and it is engaged in the business of importing agricultural equipment and selling in the local market. The following information has been extracted from the financial statements for the year ended 31<sup>st</sup> March 2015:

(1) Net profit before tax for the year ended 31<sup>st</sup> March 2015 is Rs.12,847,325/-.

(2)

Other Income	Rs.
Dividend income - net of withholding tax	90,000
Interest income received from Treasury Bills	243,000
<b>Total</b>	<b>333,000</b>

(3)

Expenses Charged when arriving at the Profit Before Tax	Note	Rs.
Administration Expenses	1	8,407,200
Selling and Distribution Expenses	2	1,050,000
Finance and Other Expenses	3	95,275
<b>Total</b>		<b>9,552,475</b>

(4) **Note 01 - Administration Expenses:**

	Note	Rs.
Salaries & wages		4,228,000
Employees' Provident and Trust Fund		634,200
Provision for gratuity		136,000
Depreciation		294,000
Entertainment		38,000
Local travelling		68,000
Foreign travelling	1.1	184,000
Company formation expenses	1.2	285,000
Donation	1.3	100,000
Legal expenses	1.4	128,000
Rent		420,000
Utilities		136,000
Other expenses		1,756,000
<b>Total</b>		<b>8,407,200</b>

#### **Note 1.1 – Foreign Travelling**

The Managing Director visited China to meet suppliers, and expenses incurred on his tour were recorded under foreign travelling.

**Note 1.2 – Company Formation Expenses**

Company formation expenses include the following:

	<b>Rs.</b>
Legal charges incurred in connection with the formation of the Company	235,000
Share issue expenses	50,000
<b>Total</b>	<b>285,000</b>

**Note 1.3 – Donation**

During the year, the company has donated Rs.100,000/- to "Api Wenuwen Api Fund".

**Note 1.4 – Legal Expenses**

During the year, the company has been sued by the Customs due to manipulation of custom duty. Rs.128,000/- has been paid to a lawyer to defend the company.

**(5) Note 2 – Selling and Distribution Expenses**

	<b>Rs.</b>
Advertising Note 2.1	475,000
Sales commission	575,000
<b>Total</b>	<b>1,050,000</b>

**Note 2.1 - Advertising**

The company has incurred the following expenses for advertising:

	<b>Rs.</b>
Paper advertisement to recruit workers	25,000
Advertisement on electronic media	450,000
<b>Total</b>	<b>475,000</b>

**(6) Note 3 – Finance and Other Expenses**

	<b>Rs.</b>
Lease interest Note 3.1	14,325
Loan interest Note 3.2	68,200
Bank charges	12,750
<b>Total</b>	<b>95,275</b>

**Note 3.1 - Lease Interest**

On 01<sup>st</sup> July 2014, two laptop computers were obtained under a finance lease agreement for a period of 24 months. Monthly installment of the lease was Rs.7,600/-. The company has paid 9 installments during the year.

**Note 3.2 - Loan Interest**

The company purchased a plot of land to build a warehouse. For this purpose, a loan was obtained from a commercial bank. Interest paid on that loan was charged to income statement.

(7) The following additional information relating to Property, Plant and Equipment is also provided.

➤ Details of Property, Plant and Equipment as at 31<sup>st</sup> March 2015 are as follows:

Type of Asset	Cost (Rs.)
Land	1,000,000
Office Equipment	78,000
Lorry	2,500,000
Furniture	26,000
Computer equipment	280,000
Computer Software - Developed in Sri Lanka	65,000
Laptop Computers - leased assets	160,000
<b>Total</b>	<b>4,109,000</b>

➤ All the assets, except leased assets have been purchased at the time of incorporation of the company.

(8) The company has paid income tax of Rs.1,500,000/- on the self-assessment basis.

**You are required to,**

**Assess** the following for the year of assessment 2014/15:

- Total Statutory Income,
- Assessable Income,
- Taxable Income,
- Gross Income Tax Payable and
- Balance Tax Payable.

**N.B:** The reasons for allowing or disallowing any expenses should be clearly stated. (25 marks)

### Question 09

**Rathnayake** is a resident individual, working as the Marketing Manager of a Micro Finance Company. Following information relating to **Rathnayake** is provided in respect of the year of assessment 2014/15 (hereinafter referred to as the 'year').

- He has received a salary of Rs.80,000/- per month. One month salary was paid to him in December 2014 as bonus, based on the profits for the year ended 31<sup>st</sup> March 2014.
- Further he received Rs.15,000/- per month as an entertainment allowance.

- (3) The company has provided him a Motor bike with fuel and no records were maintained for usage.
- (4) PAYE deducted for the year was Rs.29,596/-.
- (5) He is living in a house inherited from his parents. Net Annual Value of this house is Rs.120,000/-.
- (6) **Rathnayake** has another house at Piliyandala and it was rented for Rs.50,000/- per month from April 2014. Rating assessment of this house is Rs.135,000/- and rates are paid at 20%.
- (7) During the year, he has sold a land for Rs.1,250,000/-. His grandmother has gifted this land in the year 2000 and on that date market value of the same was Rs.500,000/-.
- (8) During the year, he has received an Interest of Rs.82,800/- (net of WHT of 8%) on fixed deposits.
- (9) He received a dividend from **Magic Holding PLC**. The particulars on the dividend warrant counterfoil are as follows:

	<b>Gross Dividend (Rs.)</b>	<b>Withholding Tax (Rs.)</b>	<b>Net Dividend (Rs.)</b>
Paid out of dividend received from other companies	40,000	4,000	36,000
Paid out of profits and income	20,000	2,000	18,000
<b>Total</b>	<b>60,000</b>	<b>6,000</b>	<b>54,000</b>

- (10) **Rathnayake** has obtained a housing loan from National Savings Bank to construct the house at Piliyandala. During the year, he has paid Rs.64,000/- and Rs.82,000/- as interest on this loan and capital repayments respectively.
- (11) He has donated Rs.25,000/- to an approved charity which is established for the provision of institutionalized care for displaced children.
- (12) He has paid Rs.53,400/- for his annual life Insurance premium. It is a policy for which the premia are payable annually over a period of ten years.

From the foregoing information,

**You are required to,**

**Assess** the following for **Rathnayake** for the year of assessment 2014/15.

- (a) Taxable income,
- (b) Gross income tax payable, and,
- (c) Balance tax payable.

**N.B:** The reasons for allowing or disallowing any expenses should be clearly stated.

(25 marks)

End of Section C



## **ACTION VERB CHECK LIST**

Knowledge Process	Verb List	Verb Definitions
<b>Level 01 Comprehension</b>  Recall & explain important information	<b>Define</b>	Describe exactly the nature, scope, or meaning.
	<b>Draw</b>	Produce (a picture or diagram).
	<b>Identify</b>	Recognize, establish or select after consideration.
	<b>List</b>	Write the connected items one below the other.
	<b>Relate</b>	To establish logical or causal connections.
	<b>State</b>	Express something definitely or clearly.
	<b>Calculate/Compute</b>	Make a mathematical computation
	<b>Discuss</b>	Examine in detail by argument showing different aspects, for the purpose of arriving at a conclusion.
	<b>Explain</b>	Make a clear description in detail revealing relevant facts.
	<b>Interpret</b>	Present in an understandable terms.
	<b>Recognize</b>	To show validity or otherwise, using knowledge or contextual experience.
	<b>Record</b>	Enter relevant entries in detail.
<b>Summarize</b>	Give a brief statement of the main points (in facts or figures).	

Knowledge Process	Verb List	Verb Definitions
<b>Level 02 Application</b>  Use knowledge in a setting other than the one in which it was learned / Solve closed-ended problems	<b>Apply</b>	Put to practical use.
	<b>Assess</b>	Determine the value, nature, ability, or quality.
	<b>Demonstrate</b>	Prove, especially with examples.
	<b>Graph</b>	Represent by means of a graph.
	<b>Prepare</b>	Make ready for a particular purpose.
	<b>Prioritize</b>	Arrange or do in order of importance.
	<b>Reconcile</b>	Make consistent with another.
	<b>Solve</b>	To find a solution through calculations and/or explanation.

Knowledge Process	Verb List	Verb Definitions
<b>Level 03 Analysis</b>  Draw relations among ideas and compare and contrast / Solve open-ended problems.	<b>Analyze</b>	Examine in detail in order to determine the solution or outcome.
	<b>Compare</b>	Examine for the purpose of discovering similarities.
	<b>Contrast</b>	Examine in order to show unlikeness or differences.
	<b>Differentiate</b>	Constitute a difference that distinguishes something.
	<b>Outline</b>	Make a summary of significant features.