



ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

AA3 EXAMINATION - JULY 2017

(AA35) CORPORATE AND PERSONAL TAXATION

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

(1) **Time Allowed:** Reading : 15 minutes

Writing : 03 hours

(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.**

16-07-2017
Afternoon
[1.45 – 5.00]

No. of Pages : 08
No. of Questions : 09

SECTION A

Four (04) compulsory questions

(Total 20 marks)

Question 01

Tac (Pvt) Ltd. was incorporated on 1st January 2016 under the Companies Act No. 07 of 2007 and commenced the business operations on the same date.

You are required to:

(a) **Explain** the rule applicable to a company in Sri Lanka in the determination of tax residency status. (03 marks)

(b) **State** the due date to submit the return of income of **Tac (Pvt) Ltd.** for the year of assessment 2015/16. (02 marks)

(Total 05 marks)

Question 02

Aloka (Pvt) Ltd. is a company engaged in the business of selling electronic equipments.

The following information was extracted from the books of the company for the quarter ended 31st March 2016:

- (1) Turnover of the company is as follows:

	Rs.
Sale of products imported by the company	4,600,000
Sale of products locally purchased by the company	2,340,000
	6,940,000

(2) The amounts of Nation Building Tax (NBT) paid by the company are as follows:

	Rs.
On imported goods	32,800
On local purchases of goods	12,500

(3) Rs.20,000/- has been paid as monthly installments of NBT for the quarter ended 31st March 2016.

You are required to:

Assess the balance amount of Nation Building Tax payable for the quarter ended 31st March 2016.

(05 marks)

Question 03

Suwa Divi Foundation is a Non-Governmental Organization (NGO). It is conducting public awareness programmes on health with the objective of improving life conditions of the rural community.

Extract of financial statements for the year ended 31st March 2016 is given below:

	Rs.
Grants received from foreign donors	1,440,000
Interest income received on fixed deposits (WHT deducted at 8%)	46,000
Fees for Resource persons	(840,000)
Administration expenses	(570,000)
Surplus for the year	76,000

You are required to:

Assess the income tax liability of **Suwa Divi Foundation** for the year of assessment 2015/16.

(05 marks)

Question 04

AA partners is engaged in wholesale and retail sale of hardware items in Colombo and **Ahamed** is a Partner of **AA partners**. He is evaluating few methods for minimizing his income tax liability. **Ahamed** was advised by his friend to enter into an agreement with his five sons to share his profit share from **AA partners**.

You are required to:

Explain whether whole of the profit share would be considered as the income of **Ahamed** for tax purposes referring to the decision given in the case of *Davoodbhoy Vs Commissioner General of Inland Revenue*.

(05 marks)

End of Section A

SECTION B

Three (03) compulsory questions

(Total 30 marks)

Question 05

Rosy (Pvt) Ltd. is a Value Added Tax (VAT) registered company engaged in the business of manufacturing soft toys. The following information for the quarter ended 31st March 2017 were extracted from the books of the company:

- (1) Sales (**exclusive** of VAT):

Direct Exports (USD 1 = Rs.150/-)	USD 14,500/-
Sales to local customers	Rs.5,325,000/-

- (2) Sale proceeds from disposal of computers were Rs.300,000/-.

- (3) Input VAT paid:

	Rs.
On imported raw materials	636,000
On local purchases	244,000
On Insurance premium of motor car used by CEO	42,000

- (4) The excess input VAT brought forward from the previous quarter amounts to Rs.24,000/-.

You are required to:

Assess the balance payable / (overpaid) of Value Added Tax (VAT) for the quarter ended 31st March 2017. (10 marks)

Question 06

You are provided with the following information of **Sayuru Products (Pvt) Ltd.**, which is engaged in the business of manufacturing and selling of canned fish:

- (1) Details of Property, Plant and Equipment:

	Carrying Value (Net Book Value) as at 01.04.2014 (Rs.)	Additions during the year (Rs.)	Depreciation for the year (Rs.)	Carrying Value (Net Book Value) as at 31.03.2015 (Rs.)
Land	-	1,000,000	-	1,000,000
Buildings	2,650,000	-	265,000	2,385,000
Computers	525,000	345,400	131,250	739,150
Equipment	236,000	155,000	35,400	355,600
Machinery	2,430,000	-	303,750	2,126,250
Motor Cars	-	1,600,000	-	1,600,000
	5,841,000	3,100,400	735,400	8,206,000

As per the policy of the company, no depreciation is charged in the year of purchase of assets.

(2) Summary of income tax computation for the year of assessment 2014/15:

	Rs.
Profit Before Tax	15,678,000
Add: Disallowable Expenses	6,520,000
Less: Allowable Expenses	4,563,000
Adjusted profit for tax purposes	17,635,000
Gross Income Tax Payable	4,937,800

(3) The company has paid an interim dividend of Rs.500,000/- on 31st January 2015 from the profit for the year of assessment 2014/15.

You are required to:

Compute the following:

- Distributable profit of the company for the year of assessment 2014/15. (05 marks)
 - Minimum amount of dividends to be distributed to avoid the tax on distributable profits (Deemed Dividend Tax) for the year of assessment 2015/16. (02 marks)
 - Tax on distributable profits (Deemed Dividend Tax) for the year of assessment 2015/16. (03 marks)
- (Total 10 marks)

Question 07

Modern Look, a partnership engaged in the business of importing and selling of garment items. **David** and **Edward** who are the partners of **Modern Look** agreed to share the profit and loss equally and to receive 5% interest for funds provided by partners to the business in addition to the capital. Income statement of the partnership for the year ended 31st March 2016 is given below:

	Rs.
Turnover	12,380,940
Cost of Sales	(7,780,000)
Gross Profit	4,600,940
Salaries to the staff	(540,000)
Depreciation on assets	(236,000)
Utility bills	(45,000)
Interest on loan provided by David	(56,000)
Stationery	(12,000)
Net Profit	3,711,940

The following additional information is also provided:

- David's** wife **Rose** works as the administration officer of **Modern Look** and **Rose's** monthly salary is Rs.20,000/-. Staff salaries include salary paid to **Rose** amounting to Rs.240,000/-.
- Depreciation allowance on assets for tax purposes for the year of assessment 2015/16 was Rs.96,000/-.

You are required to:

- Calculate** the divisible profit of the partnership. (05 marks)
 - Calculate** the income tax liability of the partnership. (02 marks)
 - Prepare** a statement of distribution of profits and other income of the partners arising from the partnership. (03 marks)
- (Total 10 marks)

End of Section B

SECTION C

Two (02) compulsory questions.

(Total 50 marks)

Question 08

Rich Food (Pvt) Ltd., which is a resident company incorporated in 2000, is engaged in the business of manufacturing and selling of cookies for the local market. The company is a subsidiary of **Star PLC**. The following information has been extracted from the financial statements of **Rich Food (Pvt) Ltd.** for the year ended 31st March 2016.

(1) Summarized Income Statement for the year ended 31st March 2016 is as follows:

	Rs.
Turnover - Local Sales	538,310,000
Cost of Sales	(290,687,200)
Gross Profit	247,622,800
Other Income:	
Profit on disposal of machinery	340,000
Dividend received - net	108,000
Administration expenses	(94,776,000)
Distribution expenses	(24,650,000)
Finance expenses	(8,549,000)
Profit Before Tax	120,095,800

(2) Administration expenses include the following:

- Management fee paid to **Star PLC** was Rs.4,036,000/-.
- Cash donation of Rs.1,000,000/- made to an approved charity which was established for the provision of institutionalized care for displaced elders.
- Receivable balance of Rs.75,000/- from an employee has been written off. In addition to that, the company has made a general provision of Rs.25,000/- for doubtful debts from debtors.
- Gratuity provision for the year was Rs.543,000/-.
- The company entered into a rent agreement for a period of five years from 01st July 2014. Monthly rent is Rs.26,000/- and rent for the year has been charged to the income statement.

(3) Distribution expenses include the following:

- The total advertising cost was Rs.760,000/-. Out of that, Rs.500,000/- has been spent outside Sri Lanka to attract foreign customers.
- Entertainment expenses were Rs.265,500/- and it was spent to entertain customers who had come for business negotiations.

(4) Economic Service Charge written off due to lapse of claimable period for tax credit which was included under finance expenses was Rs.4,000,000/-.

(5) All other expenses are allowable for income tax purposes.

(6) Details of Property, Plant and Equipment are as follows:

Cost

Particulars	Balance as at 01 st April 2015 (Rs.)	Additions (Rs.)	Disposals (Rs.)	Balance as at 31 st March 2016 (Rs.)
Building	15,000,000	-	-	15,000,000
Machinery	21,500,000	4,675,000	(3,850,000)	22,325,000
Computers	1,450,000	320,000	-	1,770,000
Motor vehicles	5,650,000	2,600,000	-	8,250,000
Furniture	1,240,000	124,000	-	1,364,000
Total	44,840,000	7,719,000	(3,850,000)	48,709,000

Depreciation

Particulars	Balance as at 01 st April 2015 (Rs.)	Charge for the year (Rs.)	Disposals (Rs.)	Balance as at 31 st March 2016 (Rs.)
Building	6,750,000	750,000	-	7,500,000
Machinery	10,750,000	2,232,500	(1,540,000)	11,442,500
Computers	1,015,000	354,000	-	1,369,000
Motor vehicles	2,542,500	1,237,500	-	3,780,000
Furniture	1,116,000	136,400	-	1,252,400
Total	22,173,500	4,710,400	(1,540,000)	25,343,900

- (7) During the year, the company has sold a machinery used in the manufacturing process. This machinery was purchased for Rs.3,850,000/- in May 2011. Entire sale proceeds were used to purchase a new machinery for the replacement of the old machinery.
- (8) Additions to motor vehicles represent a car purchased for the use of the Managing Director.
- (9) Except the building and disposed machinery, the allowance for depreciation for tax purposes on assets as at 01st April 2015 were fully claimed. The building was constructed in May 2005.
- (10) No payments have been made as gratuity during the year.
- (11) The self-assessment payment of income tax for the year of assessment 2015/16 was Rs.12,000,000/-.

You are required to:

Assess the following for the year of assessment 2015/16:

- 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

Ramya, a resident individual is employed as the chief Legal Officer of a finance company. She is divorced from her husband in the year 2012 and their daughter **Sanuthi**, born on 29th June 2006 is living with her and looked after by her. The following information relating to **Ramya** is provided in respect of the year of assessment 2015/16 (hereinafter referred to as the 'year').

- (1) She has received a gross salary of Rs.200,000/- per month.
- (2) She was provided with a motor car (1,300 CC) with a driver and fuel for her official and private use and she did not pay the employer for the private use. The company does not maintain running records for this car.
- (3) The company bears her mobile phone bills and has reimbursed Rs.32,000/- during the year.
- (4) The company has a medical scheme and the company has reimbursed an amount of Rs. 140,000/- during the year in respect of the medical expenses of her daughter.
- (5) PAYE deducted for the year was Rs.168,960/-.
- (6) She lives with her daughter in an apartment purchased by her. The rating assessment of that apartment is Rs.240,000/- and rates are paid at 30%.
- (7) **Ramya** has rented out her house which was received as a gift from her late father at a monthly rent of Rs.35,000/-. The cost of repairs borne by **Ramya** during the year was Rs. 265,000/-. Rating assessment of the house is Rs.160,000/- and rates are paid at 20%.
- (8) Interest received for the year on a fixed deposit was Rs.250,000/- and withholding tax has been deducted on the interest at the rate of 2.5%.
- (9) **Sanuthi** has a minor's savings account and she has received a gross interest income of Rs.18,000/- for the year.
- (10) **Ramya** has given a loan of Rs.100,000/- to a friend and she has received Rs.120,000/- as the repayment of loan during the year.
- (11) She won a cash prize of Rs.400,000/- from a lottery during the year. Rs.50,000/- from the lottery prize has been donated to "Api Wenuwen Api" fund.
- (12) **Ramya** has obtained a loan of Rs.200,000/- from her bank to repair the house given on rent. She has paid Rs.22,250/- and Rs.75,750/- during the year as interest and capital repayments respectively for the loan.
- (13) She has donated Rs.50,000/- worth of paint to re-paint a ward of the National Hospital, Colombo.
- (14) Tax paid on self-assessment basis was Rs.20,000/-.

From the foregoing information,

You are required to:

Assess the following for **Ramya** for the year of assessment 2015/16.

- (a) Taxable income,
- (b) Gross income tax payable,
- (c) Balance tax payable, and,
- (d) Exempt Income, if any.

(25 marks)

End of Section C

ACTION VERB CHECK LIST

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

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

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