

EXAMINER'S REPORT**AA3 EXAMINATION - JANUARY 2018****(AA35) CORPORATE AND PERSONAL TAXATION**

Question No. 01 (05 marks)

What was tested?

It was required to state the sources of income according to the Inland Revenue Act No.10 of 2006.

Observations:

Majority of candidates got high marks for the above question. But few has misunderstood and wrote about PAYE, Stamp duty and other taxes though sources of income has been tested. Though this was a very simple question, performance for the question was not that satisfactory.

The performance for this question was at an average level.

Question No. 02 (05 marks)

What was tested?

It was required to state three conditions required to be satisfied to make a valid appeal against the assessment.

Observations:

Some candidates wrote about late appeal procedure instead of valid appeal, though the question was very clear. Therefore they mentioned reasons for late appeal such as sickness of the tax payer, been overseas at the time of submission of the assessment. It was noted from the answers that candidates have skipped these areas when studying the subject.

The performance for this question was at an average level.

Question No. 03 (05 marks)

What was tested?

It was required to assess the Economic Service Charge (ESC) payable for the quarter ended 31st March 2017.

Observations:

Only a very few candidates applied the correct rate of ESC effective from 1.01.2016 which is 0.5%. Most candidates have applied the incorrect rate of 0.25% which was applicable prior to 01.01.2016. Further items of a commercial grower which are not liable for ESC such as disposal of office furniture and interest income was not deducted from the total turnover thus arriving at incorrectly computed liability.

The performance for this question was not satisfactory due to not up-to date with the current changes to the ESC Act.

Question No. 04 (05 marks)

What was tested?

It was required to identify whether the given Sports Club can be deemed to have carried out a business for the year of assessment 2016/2017.

Observations:

Most of the answers given by candidates were very poor and not up to the level of a final student. It was noted from most of the answers that candidates were unaware of the fact that if $\frac{3}{4}$ th of Sports Club's gross receipts are received from its members, that club cannot be considered as carrying out a business for the purpose of tax. To identify this, the proportion or percentage of receipts from members from the gross receipts should be computed and decided accordingly. However, most of the candidates failed to identify this percentage correctly.

The performance for this question was at a very poor level.

Question No. 05 (10 marks)

What was tested?

It was required to assess the balance payable / (overpaid) of Value Added Tax (VAT) for the quarter ended 31st March 2017. Further, it was required to state the due date for submitting Value Added Tax return for the quarter ended 31st March 2017.

Observations:

Though the correct VAT rate applicable for the quarter ended 31st March 2017 was 15%, some candidates stated it as 11%. Further, most of the candidates not showed the following adjustment correctly.

*Total claimable input VAT = (Direct exports + SVAT value) / total supplies * claimable input tax = Rs.195,219/-.*

Balance input VAT limited to lower of 100% of the output VAT or amount incurred = Rs.414,781/-.

Therefore, Total claimable input vat incurred was Rs.610,000/-.

Under tax credits, considerable number of candidates not deducted the installment payment of Rs.10,000/- and SVAT credit voucher amounting to Rs.113,760/-. Further, some candidates showed SVAT credit vouchers amount under input VAT thus not considered the VAT return format in arriving at the balance tax payable.

Though the date of submitting the VAT return for the quarter ended 31st March 2017 was on or before 30th of April 2017, most of the candidates stated it as 20th April 2017 incorrectly.

The performance for this question was at an average level.

Question No. 06 (10 marks)

What was tested?

It was required to compute the divisible profit of the partnership for the year of assessment 2016/17 and the income tax payable by the partnership for the year of assessment 2016/17.

Observations:

Though the allowance applicable for partnership was Rs.1,000,000/- some candidates considered the allowance as Rs.500,000/-. Though the tax rate applicable for y/a 2016/2017 was 8%, some candidates incorrectly applied 10%. Though ½ of the rates should be considered in the computation of divisible profit, considerable number of candidates considered the entire Rs.30,000/- as rates.

The performance for this question was at a satisfactory level.

Question No. 07 (10 marks)

What was tested?

It was required to compute the withholding tax deducted at each of the given sources of income of the given person for the year of assessment 2016/17. Further, two conditions that should be satisfied for an individual to be considered as a child under the Inland Revenue Act.

Observations:

Most of the candidates applied incorrect WHT rates for each of the below sources of income. The correct WHT rates that should have been applied are as follows:

- That person has received director fee of Rs.369,600/- after deducting WHT amounting to Rs.70,400/- at the rate of 16%.
- That person has received Interest income from Fixed Deposit amounting to Rs.92,000/- after deducting WHT amounting to Rs.2,359/- at the rate of 2.5%.
- That person has received the cash prize of Rs.720,000/- from the lottery after deducting WHT amounting to Rs.8,000/- at the rate of 10%.

Although the person under concern is a retired Government employee he was only 58 years .Under the Inland Revenue Act, the age should be over 59 years to qualify as a Senior Citizen in order to get qualify for the WHT exemption from FD interest for the year of assessment 2016/17. However, there were considerable number of candidates who exempted the interest income from FD from WHT.

Almost all the candidates correctly mentioned the conditions that should be satisfied to be considered as a child under the Inland Revenue Act correctly and scored full marks for this part of the question.

The performance for part (A) of the question was not that satisfactory.

However, the performance for part (B) was very satisfactory.

Question No. 08 (25 marks)

What was tested?

Computation of corporate income tax according to the Inland Revenue Act No. 10 of 2006 and subsequent amendments up to 31st March 2017 was tested. For the computation of the Total Statutory Income, Assessable Income, Taxable Income, Gross Income Tax Payable and Balance Tax Payable marks were allocated separately.

Observations:

Considerable number of candidates has applied correct formats in doing computations, while a fewer number of candidates have not applied the correct formats.

Common mistakes identified are given below:

- Some candidates applied the income tax rate as 28%, some other candidates applied personal income tax rates erroneously. Under Section 59B, a manufacturing undertaking in which the turnover does not exceed Rs.750M, and when there is no holding subsidiary company relationship, qualifies for the tax rate of 12% for the year of assessment 2016/17.
- Lease adjustment has also been erroneously done by several candidates, although it has been tested in previous examinations.

<i>Gross lease 160,000*9</i>	<i>Rs.1,440,000/-</i>
<i>Lease allowance 160,000*60*20%</i>	<i>Rs.2,400,000/-</i>
<i>Gross lease or lease allowance whichever is lower</i>	<i>Rs.1,440,000/-</i>

- A very few candidates applied the accepted formats in preparing the computation of income tax.
- Cost incurred for the building being constructed is not entitled for depreciation allowance for the year of assessment 2016/17 as the construction is not completed. Further, no depreciation allowance is applicable for furniture which was acquired to be used in the new building. Inter changing depreciation allowances rates were commonly seen from most of the answers.
- Most of the candidates did the advertising adjustment incorrectly, whereas the correct adjustment to be made as follows:

<i>Total Advertising cost</i>	<i>Rs.343,000/-</i>
<i>Recruitment staff advert.</i>	<i>(Rs.63,000)/- 100% allowed</i>
<i>Balance</i>	<i>Rs.280,000/-</i>
<i>¼ the disallowed ad.</i>	<i>Rs.70,000/- to be added back.</i>

The performance for this question was at a satisfactory level. However, it is recommend to understand the tax rates applicable to different undertakings.

Question No. 09 (25 marks)

What was tested?

Personal income tax computation for the year of assessment 2016/17 was tested.

Observations:

Most of the candidates have approached the question really well. However, they have lost marks due to not mentioning the reasons for exempting certain income such as value of conveyance, NAV of the apartment etc.

Common mistakes identified are as follows:

- Insurance premium of Rs.60,000/- was not taken as a non cash benefit under the employment income, by some candidates .
- Further the rental value of rent free house amounting to Rs.180,000/- was not considered by some candidates . Gross rent of the rent free residence was Rs.240,000/- per annum. Rental Value (Rating assessment + rates paid) of that residence was Rs.125,000/-. Whichever is higher from Gross Rent and Rental value is restricted to Rs.180,000/- if the aggregate employment income is more than Rs.1.8 million per annum.
- Considerable number of candidates did not do the NAV adjustment correctly. They failed to compare Net Rent and NAV correctly.
- Under qualifying payments, considerable number of candidates not considered the capital repayment of the housing loan amounting to Rs.200,000/- of a professional which is restricted to amount incurred or RS.600,000/- whichever is lower.
- Employment allowance of Rs.250,000/- has not been considered by some candidates .
- Employment income of a professional is taxable at the maximum rate of 16% progressively starting from 4%, 8% & 12% respectively. However, there were some candidates who have applied company tax rates also.

The performance for this question was at a satisfactory level.

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Hints to Improve Performance:

- (1) Time allocation must be considered before start answering the question. Most of the candidates have ignored the weightage of these questions according to the new syllabus.
- (2) In order to improve these skills candidates must practice more past papers, read the study Pack and practice past papers of the equal examinations before sitting the examination. This also assists candidates to be thorough with the subject area and the scope of the syllabus.
- (3) Candidates should practice a method to analyze a question to understand the question. Some candidates had done this analysis while they are reading the question. This will help them to properly understand the question and select the correct format to present the answer. For an example, if the question expects them to prepare adjusted profit for taxation, they need two columns for additions and deductions from net profit before tax. Selecting the correct format will assist candidates to produce a clear and complete answer and reduce mistakes. This will help marking examiner also to give allocated marks to each point without any ambiguity.