

**EXAMINER'S REPORT****Level III EXAMINATION - JULY 2021****(304) CORPORATE & PERSONAL TAXATION**

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**Question No. 01****What was tested?**

This question was required to apply the residency rule in terms of Section 69 (1) (b) of the Inland Revenue Act No. 24 of 2017 (hereafter referred to as the Act) to an individual taxpayer who was in overseas for job purpose in 2020/2021 year of assessment.

Accordingly, an individual shall be a resident in Sri Lanka for any year of assessment if, he or she 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 months period that commences or ends during the year.

**Observations:**

- (1) The majority has correctly identified the given facts of the question, and applied the 183 days residency rule and concluded that the individual is a non-resident for tax purpose in Sri Lanka.
- (2) Some candidates have decided that the taxpayer is a resident due to citizen in Sri Lanka without applying residency rule. Such candidates lost the marks allocated for the question.
- (3) Some candidates have just wrote number of days stayed in Sri Lanka or overseas without providing proper calculation with their workings, and concluded that taxpayer is a non-resident person for tax purpose.
- (4) Some students have written long paragraph and question repeatedly. But the important point, which should be included in the answer was completely missing. This resulted in losing marks as well as wasting time too.

**Performance: The overall knowledge of candidates in applying residency rule for a given scenario was satisfactory level.**

**Question No. 02****Part (a)****What was tested?**

The knowledge on the Stamp Duty with regard to salary payment in terms of Stamp Duty (Special Provisions) Act No. 12 of 2006 (as amended) was tested by this particular question.

The facts of the question was crystal clear and very simple. According to the Stamp Duty Act, the Stamp Duty is charged at Rs.25/- if the monthly salary payment per employee is exceeded Rs.25,000/-. The simple answer was Rs.25/- is multiplied by number of employees, and then multiplied by 3 to obtain answer for the quarter (Rs.25/- x 120 x 3 = Rs.9,000/-).

**Observations:**

- (1) The majority of candidates do not have a proper knowledge on the Stamp Duty.
- (2) A very few students has answered correctly and obtained the marks allotted for this.
- (3) Around 90% of total candidates have lost full marks, which could have been easily earned.
- (4) The most of candidates were incorrectly calculated Stamp Duty payable by applying incorrect amount Rs.50/- instead of Rs.25/- per employee.
- (5) A majority of candidates have applied irrelevant amount to calculate Stamp Duty on the total salary.
- (6) Some candidates were correctly calculated the liability for one month only instead of 3 months liability.
- (7) Some candidates have just wrote the incorrect amount without showing calculations in their workings.

**Performance: The overall performance was not at satisfactory level.**

**Part (b)****What was tested?**

This part of the question was tested the specific instruments, which are liable for the Stamp Duty in terms of Section 4 of the Stamp Duty (Special Provisions) Act No. 12 of 2006.

**Observations:**

- (1) Examiners expected to state about affidavit, policy of insurance, warrant to act as Notary Public, share certificate, bond or mortgage, promissory note, lease or hire of any property, and receipt or discharge given for any money or other property. Further the allocated two marks were awarded for any two correct answers.
- (2) Almost all candidates were completely unaware about those instruments.
- (3) Majority of candidates has provided completely irrelevant answers such normal post, registered post, etc.

**Performance: The overall performance was not at satisfactory level.**

### **Question No. 03**

#### **What was tested?**

This question was tested the knowledge on Capital Gain Tax, which is charged under the Income Tax Act.

#### **Observations:**

- (1) Some of candidates have taken Rs.5,000,000/- as the cost of the land when calculating the value for capital gain, instead of Rs.6,800,000/- the market value as at 30.09.2017.
- (2) The majority of candidates correctly identified the broker fees Rs.50,000/- as allowable deduction when arriving at value for capital gain. However, some candidates have considered the broker fee as income instead of expenses.
- (3) Some candidates have stated that unlisted company shares are exempted from Capital Gain Tax, same as listed company shares.
- (4) Some candidates have applied incorrect tax rates instead 10% for capital gain.
- (5) Some students did not show the proper workings to support their figures, which they have computed.

**Performance: Overall performance for this question is at satisfactory level.**

### **Question No. 04**

#### **What was tested?**

This case law question was based on the facts of decided case Crib vs. Commissioner of Income (1939) 1 CTC 156. This particular case can be still considered as one of a best landmark decision held by the Supreme Court of Sri Lanka in relation to past service rendered by an employee where the motive was the long service, but not the consideration for the payment.

Accordingly, the Supreme Court has held that the amount received by Mr. Crib for medical treatment was a gift and could not be treated as an income from employment. The court further held that the motive of the payment is long service rendered to the company, but not the consideration for the payment. The facts this case and the facts of the given question were almost identical and clear-cut. Hence, the special payment made to Mr. Silva can be considered as gift for his exceptional service to the company in considering his medical treatment. Accordingly, the opinion of Mr. Silva's tax consultant was not correct. The question was expected to give answer based on decided case.

#### **Observations:**

- (1) The most of candidates were given incorrect conclusion by referring to irrelevant cases.
- (2) Some candidates have referred to the correct case law, but conclusion was incorrect.

- (3) Most of candidates have misunderstood the question due to lack of attention to the requirements of the question.
- (4) Some candidates have written long paragraphs and question repeatedly, but the important points that should be included in the answer were missing by losing marks as well as time.
- (5) Considerable number of candidates are still struggling to apply the case law for a given scenario.
- (6) Few candidates stated that the benefit received by Mr. Silva is not taxable in terms of Crib vs. Commissioner of Income but taxable as per provisions of the act. This was an ideal answer in the context of argument ability for the given facts of the case, and full marks were awarded for that answers.

**Performance: Overall performance for this question is at average level.**

### **Question No. 05**

#### **What was tested?**

This question was based on furnishing of return of Income Tax due date for the year of assessment 2019/20. The taxpayer were able to file the Income Tax return till 10.03.2021 for year of assessment 2019/2020 but normal due date is 30<sup>th</sup> November. Tax payer failed to pay quarterly installment payments on due dates in given scenario. The Assistant Commissioner had assessed the taxpayer accordingly. Marks have given for the any one of the above dates.

The candidate were required to provide answers for penalties applicable for non-payment of quarterly payments, time bar for issuing an assessment, and four conditions that required to satisfy a valid appeal against the assessment.

#### **Observations:**

- (1) Majority was failed in answering all three parts of the question, and lost full marks allocated for the question.
- (2) The most candidates have provided completely irrelevant answers for all three parts of the question without any idea on assessments, penalty, time bar, and appeal procedure.
- (3) Majority did not know about penalties applicable for non-payments of quarterly installments, and statutory time bar for issuing assessments.
- (4) The knowledge on legal requirements that demand to satisfy a valid appeal against an assessment was absolutely poor.
- (5) It was very clear that the most of candidates have not gone through payment of Income Tax, furnishing of returns, assessment, appeals, tax in default, refunds, and penal provision (Chapter 5) of the study pack.

**Performance: Overall performance was not at satisfactory level.**

## **Question No. 06**

### **What was tested?**

This question was based on the partnership taxation in terms of Section 53 to 56 of the act. The question was required to calculate the Income Tax payable by partnership for the year of assessment 2020/2021 that include partners salaries, entertainment expense, interest paid to a loan provided by a partner, salary paid to a partner's wife, and donation made to an National Hospital (government).

### **Observations:**

- (1) The most candidates have secured a reasonable mark for this question.
- (2) The adjustments pertaining to partner's salary, interest paid to a partner's loan, entertainment expenses, and donation were properly adjusted by the most of candidates when arriving at business profit.
- (3) Some candidates did not consider the salary paid to a partner's wife correctly when calculating business profit.
- (4) Nearly half of candidates have forgot to deduct donation to government as a qualifying payment when calculating Taxable Income.
- (5) Certain candidates deducted Rs.1,000,000/- that was required to tax at 0% when arriving at the business profit of the partnership.
- (6) The most of candidates applied the correct partnership tax rate at 6% to tax the profit of the partnership.

**Performance: Overall performance for this question is at satisfactory level.**

## **Question No. 07**

### **What was tested?**

This question was required to calculate the balance Value Added Tax (VAT) payable/(over paid) for the quarter ended 31<sup>st</sup> March 2021 by a company, which was engaged in manufacturing of plastic items for the both foreign and domestic customers.

### **Observations:**

- (1) The most candidates have secured a reasonable marks allocated for the question.
- (2) The majority has applied correct VAT rate 0% for export sales and 8% for local sales to other persons.
- (3) Some candidates were unable to recognize the difference between exempt supplies and SVAT supplies, and stated that sales made to SVAT registered persons are exempted from tax.

- (4) Input tax on imported and locally purchased raw material was properly claimed by the majority of candidates while repair charges on motor vehicle used by a director were disallowed by the majority.
- (5) Considerable number of candidates has proportionately disallowed input tax while some candidates have recalculated VAT at 8% for input tax as well.
- (6) Claiming brought forward excess input tax and installment payments were properly done by the majority when reaching the balance tax payable.
- (7) Some candidates have applied different VAT rates instead of 8% given by the question itself.
- (8) The overall knowledge on input-output mechanism in relation to VAT was understood by the majority.

**Performance: Overall performance for this question was at satisfactory level.**

### **Question No. 08**

#### **What was tested?**

The basic theoretical knowledge on corporate taxation for the year of assessment 2020/2021 was tested by this question. Accordingly, the question was required:

- (1) To assess the Assessable Income, Taxable Income, gross Income Tax payable, and balance tax payable of a resident company when there were sources of income from business and investment.
- (2) To decide the Income Tax rate when the company is engaged in manufacturing business with annual turnover over 500 million.
- (3) To evaluate the practical aspect of applying general deductions (Section 10), main deductions (Section 11), and specific deductions Section 12 - 19) of the act in ascertaining the business profit.

#### **Observations:**

(1) **Presentation format:**

The majority has shown good performance by understanding the presentation and identification of statutory contents of the corporate Income Tax computation.

(2) **Asset disposal and capital allowances:**

The majority has correctly applied the rates for capital allowances as stipulated by the act. However, some candidates were experiencing difficulties in calculating balancing allowance for assets disposal. Some candidates have not stated anything about the land. The rate of capital allowances for building and computer software were unknown by considerable number of candidates. Some candidates have added the profit from disposal of lorry as an investment income instead of treating as a profit from business.

(3) **Disallowable expenses:**

Gratuity provision and general provision for debtors have been added back to the accounting profit by the most of candidates. But, Economic Service Charges written off has not been added back to accounting profit by many candidates. Instead of that they claimed it as a qualifying payment or tax credit. The most of candidates did not know that research and development expenses can claim up to 200%. Some candidates have claimed research and development expenses as a tax credit. Also, actual payment of gratuity has forgotten by many candidates.

(4) **Donation:**

Both donation made to the government (Ministry of Disaster Management and National Kidney Fund) were added back to the accounting profit by majority of candidates. However, some have did not know about how to claiming donation.

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

The company was engaged in the business of manufacturing and selling consumer goods in the local market for which 18% Income Tax rate is applicable. On the other hand, it has a dividend income and interest income for which 14% and 24% is applicable respectively. Only a very few candidates has applied all three respective tax rates to estimated tax liability of the company. However, most of candidates have applied the standard rate 24% for the whole profit by not understanding business of manufacturing of the company. Unfortunately, some candidates have applied the individual slab rate for corporate taxation as well.

(6) **Identification of tax credit**

Quarterly installment payment was the only tax credit available for the company, which was claimed by the majority. However, some candidates have claimed Economic Service Charges and research and development expenses as tax credits.

**Performance: Overall performance for this question was at satisfactory level.**

## Question No. 09

### What was tested?

Computation of personal Income Tax for the year of assessment 2020/2021 of a resident individual who is a Chartered Accountant by profession was expected. The source of income included income from employment and investment.

### Observations:

The question was attempted by almost all candidates, and the overall approach in answering the question was in a satisfactory level. The common omission and mistake observed during the process of evaluation are summarized as follows:

#### (1) Employment Income:

- (i) Some candidates have taken into account per month salary as gross salary for the year without multiplying by 12 months to get the total salary.
- (ii) Reimbursement of medical expenses under common scheme provided by the company and conference expenses incurred to travel to India were considered as employee income of the taxpayer incorrectly by some candidates.
- (iii) The entire amount of reimbursement of telephone bill was taken as an income without taking into consideration 50% while some have exempted from tax.

#### (2) Income from investment:

- (i) Rent income was calculated correctly for the tax purpose, however, 25% repair allowance was not claimed under qualifying payment. Also, some candidates have treated rent income as a business income of the taxpayer.
- (ii) Considerable number of candidates have considered dividend income, which was paid out of dividend received from another company as an income of the taxpayer.

#### (3) Other common mistakes:

- (i) Some candidates were not able to apply the correct individual Income Tax rates in their tax computation while certain candidates have applied individual income tax rates prescribed in the old act.
- (ii) Some candidates had identified self-assessment payment and APIT as tax credits but it deducted from Taxable Income without deducting from gross tax liability.
- (iii) The Majority of candidates have not claimed the cost of listed company shares Rs.900,000/- and educational expenses Rs.250,000/- under qualifying payments and reliefs. Further, the most of candidates did not aware about these expenses are limited to Rs.1,200,000/-. Hence, many candidates did not have an adequate knowledge on the claimable qualifying payments and reliefs, which are entitled for an individual taxpayer.



- (iv) Some candidates have not applied the correct flow when calculating the 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.
- (v) Some candidates have stopped tax computation at Taxable Income without completing the answer.

**Performance: Overall performance for this question was at satisfactory level.**

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**As a whole, common reasons for Poor Performances of question paper by some Students:**

- (1) Ignoring fundamental principles in taxation.
- (2) Lack of awareness on relevant taxing laws such as Stamp Duty and subsequent amendments to the Inland Revenue Act.
- (3) Less attention to read the question paper properly before starting to answer the questions. In such a scenario, candidates have misunderstood the questions that resulted in missing certain important requirements of the questions.
- (4) Attention was not given to refer past question papers and model answers to improve the knowledge.
- (5) Less attention was given to refer Corporate and Personal Taxation Study Text in which the most of fundamental principles and rules are properly explained.
- (6) Poor time management by providing lengthy answers for small marks. For example, answer for the residency rule, case law, statutory requirements to fulfill a valid appeal, etc.
- (7) Some candidates have applied the provisions of old Inland Revenue Act No. 10 of 2006 instead of provisions of new Inland Revenue Act No. 24 of 2017.
- (8) Inability to analyze the questions properly to know the requirement of questions, which permits candidate to organize the answer including the format and presentation.
- (9) Some candidates did not show the proper workings to support their figures, which they have arrived in the process of calculation.

**Suggestions to improve the performance at future examinations:**

- (1) Candidates must concentrate on time management before answering to the question paper. Students should answer on the requirement of the questions and marks allocated.
- (2) Answering the past question papers and check with model answers to improve the examination skills.
- (3) Devoting full attention to refer the Study Text.
- (4) Referring subsequent amendments to the Inland Revenue Act No. 24 of 2017 published by the Department of Inland Revenue by way of gazette notifications and paper notices.
- (5) Focusing on basic fundamental principles of taxation.
- (6) Providing appropriate workings for each and every calculations.
- (7) Answering the question paper with legible handwriting that allows the Examiner to understand the facts clearly.
- (8) Answering a new question on a new page of the answer booklet.
- (9) Students are advised to read the question paper properly in order to provide correct answers and secure full marks allocated for respective questions.
- (10) Always use the reading time 15 minutes to read the question paper to understand the question first.

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