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Serial No.....

Society of Certified Management Accountants of Sri Lanka

Intermediate Stage Pilot paper

Instructions to candidates:

1. Time allowed is **three (3) hours**.
2. Answer **all** questions.
3. Answers should be entirely in the **English** language.

<u>Subject</u>	<u>Subject Code</u>
Taxation	(TAX)

Question No. 01 (35 Marks)

Master Engineers (Pvt) Ltd. is a resident company manufacturing electrical items. The draft balance sheet and other relevant information for the year ending 31/3/2006 are given below. Compute the income tax liability of the company for the year of assessment 2005/2006.

Draft Balance Sheet as on 31/3/2006.

Fixed assets

Land, buildings, equipment, vehicles etc 411,835,000
Investment in shares 75,000,000

Current assets

Inventories 30,000,000
Trade and other receivables 201,000,000
Deposits 1,300,000
Cash & Bank 140,100,000
859,235,000

Share capital & liabilities

Share capital 360,000,000
Profit & Loss account balance 311,835,000

Liabilities

Provision for gratuity (Balance 31/3/2005 Rs 8,900,000) 9,000,000
Trade & other payables 160,000,000
Accrued expenses 10,000,000
Loan from Bank 8,400,000
859,235,000

1.

(c) A land for the construction of the building to be used for business purpose was

	<u>1/4/2005</u>	<u>Additions</u>	<u>Disposals</u>	<u>31/3/2006</u>
	Rs.	Rs.	Rs.	Rs.
(a) Assets				
Land & Buildings	100,000,000	250,000,000	-	350,000,000
Plant & Machinery	70,000,000	28,000,000	16,000,000	82,000,000
Furniture	800,000	200,000	-	1,000,000
Office equipment/ Computers	1,000,000	210,000	-	1,210,000
Motor Vehicles	20,000,000	1,800,000	1,000,000	<u>20,800,000</u>
				<u>455,010,000</u>
(b) Depreciation				
Land & Buildings	0	4,000,000	-	4,000,000
Plant & Machinery	20,000,000	9,900,000	9,000,000	20,900,000
Furniture	410,000	90,000	-	500,000
Office equipment/ Computers	800,000	100,000	-	900,000
Motor Vehicle	14,600,000	<u>2,900,000</u>	625,000	<u>16,875,000</u>
		<u>16,990,000</u>		<u>43,175,000</u>

purchased in 2002. During the year the building was constructed expending Rs.2,220,000,000/-. The building was completed in August 2005. Further during the year a house was purchased for the occupation of the Managing Director.

(d) Two machines purchased in 2001/2002 were sold during the year and replaced with two new machines.

(e) Furniture for the office was purchased as follow: -

	Rs.
2000/01	450000
2002/03	150000
2005/06	200000

Furniture purchased during the year was placed in the Managing Director's house.

(f) A computer was purchased during the year.

(g) A motor van used for transport purchased in 2002/03 was sold during the year and a new lorry was purchased.

(h) All assets other than those referred to above have been purchased in 2000/2001.

2.	Other incomes of the company were as follows: -	Rs.	Rs.
	Income from interest in Fixed Deposits (net)		16,000,000
	Dividends (net)		750,000
	<u>Profit/Loss on disposal of assets</u>		
	Profit on sale of machinery	500,000	
	Loss on sale of van	<u>(160,000)</u>	340,000
	Profit on the sale of shares in companies not quoted		<u>140,000</u>
			<u>17,230,000</u>

3. The net profit was arrived at after changing all expenses including;- Rs.

Directors Emoluments	1,800,000
Depreciation	16,990,000
Rent	15,000,000
Foreign Traveling (see note 5)	330,000
Advertisement & Entertainment expenses (see note 6)	620,000
Professional fees (see note 7)	790,000
Commission to broker on sale of shares	10,000
Gratuity Provision	1,500,000
Charity & Donations (see note 8)	1,720,000
4. The Net Profit before tax as per draft accounts was Rs 48,000,000. A dividend of Rs. 3,000,000 proposed last year was paid during the year. Out of this dividend amounting to Rs 500,000 was from dividends received.	
5. Foreign Traveling consists of the following:-	Rs.
Cost of air ticket to Managing Director to go on a holiday	200,000
Cost of air ticket to employee sent on training	130,000
6. Advertisement & Entertainment expenses	Rs.
Printing of diaries & calendars	170,000
Entertainment expenditure	400,000
Advertising of Vacancies in the Company	40,000
7. Professional fees incurred were	Rs.
In the collection of trade debts	190,000
Accountancy fees	500,000
Payment to a lawyer for pursuing an income tax appeal	100,000
8. Charity & Donations	Rs.
Payment to a village temple for development of the temple	106,000
Government Tsunami Fund	1,500,000
Provision of milk powder to an orphanage which is an approved charity	14,000
Cash donation to YMBA, an approved charity	100,000
(Total 35 Marks)	

Question No. 2 (30 Marks)

Mr.Lal Fernando is an executive in AB Ltd since 1995, for the year of assessment 2005/2006.He received the following income from the company.

Salary	Rs 200,000/ per month
Entertainment allowance	Rs 25,000/ per month
Bonus	Rs 600,000/ per month

- He contributes 8% of his salary to the Employee's Provident Fund and the company contributes 12%. In addition the company contributes 3% to the Trust Fund.
- The company has given him a house to stay free of rent. The rating assessment of the house is Rs 120,000/ and rates are paid at 30%. The company pays a rent of Rs. 20,000/-per month for this house.
- In 2004 the company has helped him to take a car on lease. On this car the company pays a lease rent of Rs 30,000/ per month on his behalf and he pays Rs 20,000/ per month. In addition the company pays a traveling allowance of Rs 15,000/ per month for traveling between his home and office.

- During the year he commenced construction of a house in Kandy to be used as his family's residence as his children were schooling in Kandy. During the year he incurred an expenditure of Rs 1400,000/- on the construction. He has not constructed a house before this.
- From May 2005, he received an income from rent amounting to Rs 30,000/ per month from a house which he inherited from his father in 1996. He paid rates of Rs. 20,000/- for the year and incurred Rs 60,000/ for repairs. The house was vacant in April 2005 as he could not find a tenant. He paid Rs 15,000/ to a newspaper to place an advertisement.
- During the year he sold a coconut estate, which he had inherited from his father. The value at the time of inheritance was Rs.2,000,000. The estate fetched a price of Rs 3,000,000/-. He paid Rs 30,000/ to the broker who found the buyer. The income from the estate from April to date of sale was as follows.

	Rs.	Rs.
Sale of coconuts	300,000	
Replanting subsidy	50,000	350,000
Less: paid to plucker	(25,000)	
Paid to watcher	(48,000)	
Other expenses		
Including replanting	<u>(20,000)</u>	<u>93,000</u>
		<u>257,000</u>

- He deposited Rs 2,000,000/ in the NSB and received a net interest income of Rs .210,000/. He deposited Rs 500,000/ in a private bank at 11% monthly interest on October 2005. Withholding tax was not deducted on this amount as the amount of interest was less than Rs 108,000/
- During the year he took 2 weeks leave and was allowed by the company to take up a consultancy service in the Maldives. He received an income of US \$ 200,000 (US \$ 1 = Rs 102/-).
- He brought back his savings amounting to US \$ 180,000 and deposited in an NRFC account and received an interest income of US \$ 2,000.
- He pays a life insurance premium of Rs 30,000 per annum. He donated Rs. 18,000/- to an approved charity. His PAYE deduction amounted to Rs 750,000 for the year.

You are required to compute his Statutory Income, Assessable Income, Taxable Income and the Tax Payable for the year of assessment 2005/06.

Any income exempt from tax, excluded from tax should be clearly worked out and stated.

(Total 30 marks)

Question No. 3 (15 Marks)

Mr. Silva & Mr. Perera are partners of a legal consultancy firm, sharing profit in the ratio of 3:2 respectively.

- (1) Their net income for the year ending 31/3/2006 was Rs 1200,000 in arriving at this net income the following expenses were also charged.

Rs.

Partner's salaries	Silva	600,000
	Perera	500,000
Interest on partner's capital	Silva	75,000
	Perera	60,000

(2) In arriving at the net income, dividends on an investment by the partnership amounting to Rs 90,000/ net has been included.

You are required to compute

- (i) The divisible profit of the partnership and divide the divisible profit and other income of the partnership between the two partners.
(ii) The income tax payable by the partnership. **(15 marks)**

Question No. 4 (10 Marks)

According to the particulars given below, compute the Value Added Tax liability of Sivarex for the quarter ended 31/3/2006. He has paid VAT amounting to Rs.200,000 for the months of January & February.

The figures given are exclusive of VAT. The VAT rate where VAT is payable can be assumed to be 15%. Also what is the last date before which the liability should be paid?

	Rs.
Sale of manufactured items	3,000,000
Sale of exempt items	500,000
Imported raw materials	1,000,000
Purchase of material from a person not registered for VAT	200,000
Purchase of diesel from a petrol shed	600,000
Payment for electricity	60,000
Payment to Accountant registered for VAT	40,000
	(Total 10 marks)

Question No. 5 (10Marks)

(a) Mr. Bastians received an additional income tax assessment, rejecting his return for the year of assessment 2005/06, dated 6th May 2006, from the Deputy Commissioner of the Colombo East branch of the Inland Revenue Department.

The tax payable on return amounted to Rs. 85,000/-. Out of this amount he has paid only Rs. 45,000/. In the notice of assessment an additional tax of Rs. 125,000/ was claimed.

- (i) Since he is aggrieved by this assessment, to whom should he address the appeal against this assessment?
(ii) What are the conditions that he should adhere to do ensure that it is a valid appeal? **(5 marks)**

(b)

- (i) On what is the Economic Service Charge payable for the period 1/4/2005 to 31/3/2006? Is it on the profit or on the turnover?
(ii) Under what circumstances does the liability to the Economic Service Charge arises for the same period?
(iii) What is the maximum amount a person is liable to pay as Economic Service Charge for the same period?
(iv) On what dates are the Economic Service Charge payables for the same period?
(v) Is the Economic Service Charge an additional tax or levy? Or can the payment be set off against any other tax? Explain. **(5 marks)**

(Total 10 Marks)
End of question paper