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Serial No.....

Institute of Certified Management Accountants of Sri Lanka

Managerial Level

November 2012 Examination

Examination Date : 17th November 2012 **Number of Pages :** 07
Examination Time: 1.00 p:m. – 5.00 p:m. **Number of Questions:** 10

Instructions to Candidates

1. Time allowed is **four (4) hours**.
2. Total: **200 Marks**.
3. Answer **any four (4)** questions in Section A, **all** questions in Part I and any **three (3)** questions from Part II in Section B.
4. **Section A:** Corporate Law and **Section B:** Advanced Taxation
5. **Use 2 Answer Booklets to write 2 sections separately.**
6. The answers should be in **English Language**.

<u>Subject</u>	<u>Subject Code</u>
Corporate Law & Advanced Taxation	(CLT / ML 4 - 304)

SECTION A: Corporate Law

Answer **any four (4)** questions

Question No. 01 (25 Marks)

“A company structure is the most popular business entity because companies provide significant advantages.”

Consider the above statement with reference to the defining characteristics of a company and disadvantages of incorporation, if any.

(Total 25 Marks)

Question No. 02 (25 Marks)

Samson ran a small business engaged in manufacturing sweetmeats. He incorporates the business as Bombay Confectioneries Ltd. and becomes a director. Samson holds 50% of the stated capital and 40% by his son Irosh who is also a director. Rest is held by the other members of the family. Samson continues to run the company as if it was still his own private business and frequently ignores the wishes of Irosh. Samson often uses company money for unexplained purposes.

Now Irosh would like his father Samson who is 72 years old to retire from the management and bring his son, Premil into the management. Premil is a director of a rivalry company of Bombay Confectioneries Ltd.

Advise Irosh, who wish to terminate Samson from the directorship and appoint Premil as a director?

(Total 25 Marks)

Question No. 03 (25 Marks)

Anil, Bandu and Carlo are minority shareholders of ABC Ltd. The directors of ABC Ltd wish to safeguard against the minority shareholders objecting to any of their decisions in the future. To achieve their aim and in order to obtain the voting control of the company they decide to compulsorily acquire Anil, Bandu and Carlo's shares. The directors intend to incorporate a clause in the company's articles of association enabling the directors to acquire shares of existing shareholders at their discretion.

Advise Anil, Bandu and Carlo as to their rights, who wish to object to the inclusion of the clause in the articles.

(Total 25 Marks)

Question No. 04 (25 Marks)

Fresh Ltd. needs to raise finance for the expansion of its fresh food business. The board of directors of Fresh Ltd. is aware that most companies fund their activities through a mixture of equity capital and debt capital. They seek your advice as to the advantages and disadvantages of raising the finance necessary to fund the company's expansion through equity capital and debt capital to the company as well as potential investors.

Advise the board.

(Total 25 Marks)

Question No. 05 (25 Marks)

(a) Explain what is meant by

(i) (1) An Ordinary resolution (2) a Special resolution.

(10 Marks)

(ii) The circumstances in which a company requires a special resolution when exercising its powers.

(07 Marks)

(b) Harry and Marie own a successful soft drink and snack food business which they propose to incorporate as Tasty Ltd. of which they will be the sole shareholders and directors. They know that the company must undergo an audit. They have no idea how to appoint auditors and what qualifications do auditors need.

Advise them.

(08 Marks)

(Total 25 Marks)

SECTION B: Advanced Taxation

Part I

Answer all questions

Question No. 06 (40 Marks)

ABC Bank Ltd. is a resident company of Sri Lanka. It has a branch out side Sri Lanka. Sri Lanka has not entered into a double taxation agreement with that country.

The summarized profit and loss account for the year of 2010 / 2011 and related notes are given below. It includes profit from the branch and income tax paid to that country. No expenditure charged in the profit and loss account of the branch could be disallowed under the domestic law of Sri Lanka and it is assumed that the branch profit has been computed correctly.

	Rs.	Rs.
Interest income	3,455,234,000	
Less: Interest expenditure	<u>2,042,000,000</u>	
	1,413,234,000	
Gross rental income	13,700,000	
Net Dividend received	22,640,000	
Treasury bill interest	41,670,000	
Insurance claim	2,000,000	
Other income	1,900,000	
Profits and income of the foreign branch	<u>20,745,000</u>	
		1,515,889,000
Less: Expenditure		
Salaries	198,320,000	
Director's Remuneration	71,680,000	
Contribution to provident fund	32,400,000	
Contribution to pension fund	27,000,000	
Contribution to gratuity fund	14,062,000	
Contribution to ETF	8,100,000	
Book depreciation	8,750,000	
Foreign travel	3,630,000	
Business entertainment	2,988,000	
Repairs to the building given on rent	4,260,000	
Rent	8,430,000	
Postage and Printing	1,872,000	
Income tax paid to the other country	6,235,000	
Advertising	41,597,000	
Donation made to the government	2,980,000	
Provision for doubtful debt	202,090,000	
VAT on Financial Services paid	148,657,000	
Legal cost – debt recovery case	1,945,000	
Accountancy fees & Auditor's fees	<u>1,670,000</u>	
		<u>786,666,000</u>
Net Profit		<u><u>729,223,000</u></u>

Notes

- (1) Bank has let its buildings in Colombo and suburbs for commercial purposes.
- (2) Bank has received an insurance claim in respect of a motor van used for the transport of cash. The Van was fully damaged due to a technical fault. This van was purchased during the year of assessment 2005 / 2006 for Rs.2,000,000/-.
- (3) Other income is from the profit from disposal of a motor car used for travelling.
- (4) All the funds to which the contributions have been made on behalf of employees have been approved by the Commissioner General, subject to the limits imposed by them.
- (5) Allowance for depreciation had already been granted on all the assets other than;
 - (i) Building constructed in the year of assessment 2006 / 2007. The cost of construction was Rs.60,000,000/-.
 - (ii) Computer hardware purchased in the year of assessment 2008 / 2009 for Rs.8,000,000/-.
 - (iii) Furniture purchased in the year of assessment 2008 / 2009 for Rs.8,000,000/-.

A motor car has been purchased during the year from the sale proceeds of the sold car. The cost of new motor car is Rs.3,000,000/-.
- (6) Foreign travel expenditure is in relation to visits made to the foreign branch.
- (7) Rent paid is for branch offices in remote areas.
- (8) Donation made to the government includes the cost of dry rations given to flood affected people in Ratnapura, amounting to Rs.243,000/-. No receipt has been received in respect of the donations of the dry rations.
- (9) Bad debt provision is only for specific provisions and it amounts to 4% of the loan and advance account as at balance sheet date. All the previous years, bad debt provision was less than 1% of the total advances and loans.
- (10) Company has distributed dividends amounting to Rs.16,000,000/- during the above year of assessment (Please disregard the calculation of deemed dividend tax).
- (11) Economic Service Charge (ESC) has been paid on the liable turnover.
- (12) Self assessment payments made during the year amounts to Rs.200,000,000/-.

You are required to compute the income tax liability of the company, any tax credits available and the balance tax payable for the year of assessment 2010/2011. (Total 40 Marks)

End of Part I

Part II

Answer **any three (3)** questions

Question No. 07 (20 Marks)

(a) Identify the sources of income liable to income tax and compute such liable income for the purposes of tax in year of assessment 2010 / 2011 in each of the following cases.

(i) Mrs. Thilini Perera is attached to a manufacturing company and she has been provided with a residence rent free. This was taken on rent by the company and rent paid by the company for a month was Rs.12,000/-. Rating assessment of the residence is Rs.80,000/- and rates payable is 20% of the rating assessment. The gross salary she received was Rs.1,250,000/- during the above year of assessment. Further, she has been provided a vehicle in which the engine capacity is less than 1500 cc.. **(04 Marks)**

(ii) Mr. Raja Samaranayake has given his house on rent to a doctor. He uses this house for a medical laboratory. Monthly rent was Rs.30,000/- . This house has a floor area of 1100 sq.ft. and it was constructed during the year of assessment 2005 / 2006. Rating assessment of this house is Rs.100,000/- and rates payable is 20%. **(04 Marks)**

(iii) Mr. Lalith Kannangara has a fixed deposit in a commercial bank. During the year of assessment 2010 / 2011, the bank has paid an interest of Rs.180,000/- after deducting withholding tax. Further he received Rs.64,000/- semi-annual coupon interests from a treasury bond. **(02 Marks)**

(b) Sri Lanka Green Products Corporation is a public corporation which has 100% of its capital provided by the Government of Sri Lanka other than by way of a loan. Its adjusted profit for the year of assessment 2010/2011 is Rs.76,450,000/-.

After considering other incomes, deductions allowable under Sections 32 and allowances for qualifying payments, it had to pay Rs.20,750,000/- as income tax under section 61(1)(a) of the Inland Revenue Act No. 10 of 2006 for the above year of assessment.

The aggregate amount of dividends distributed during that year of assessment is Rs.9,500,000/-.

You are required to compute the income tax liability of the corporation for the year of assessment 2010/2011. **(10 Marks)**

(Total 20 Marks)

Question No. 08 (20 Marks)

(a) What are a supply of goods and a supply of service? **(04 Marks)**

(b) What is the time of supply when it comes to hire purchase agreement? **(04 Marks)**

(c) Rich Colour Garments Ltd. is a garment manufacturing company and its total supply consists of standard rated supplies, suspended supplies and zero rated supplies. However, zero rated supply and suspended supply do not exceed 50% of its total taxable supplies. The fabric required for manufacturing of garments was mainly imported and VAT is paid up front. The company was not entitled to clear cargo under deferred facility. The company furnishes its VAT return on a quarterly basis.

The following transactions took place during the quarter ending March 2011.

Supplies:	Standard supply	Rs.34,325,250
	Suspended supply	Rs. 6,830,000
	Zero rated supply	Rs. 6,270,000

Imports:	Raw materials	Rs. 17,232,350
	Machine	Rs. 8,550,000
	Motor car	Rs. 3,000,000

Local Purchase:

Other materials and accessories: From registered persons	Rs.7,420,300
: From non-registered persons	Rs.2,475,000

All purchases are shown excluding VAT.

Other expenses

Telephone bill	Rs. 684,000
Water bill	Rs. 340,000
Electricity bills	Rs. 6,300,000
Salaries and wages	Rs. 10,600,000

No brought forward input tax is available for this taxable period.

You are required to compute the following relating to the quarter ending on 31/03/2011.

- (i) Output tax
- (ii) Input tax
- (iii) Disallowable input tax
- (iv) VAT payable
- (v) Carry forward input (if any) to the quarter ending with 30/06/2011.

(12 Marks)

(Total 20 Marks)

Question No. 09 (20 Marks)

- (a) “Unabsorbed input VAT claimable as at 31/12/2010 was frozen by the budget for the year 2011.” Explain how it was claimable after 01/01/2011 but prior to 31/12/2011 including treatment in situations where there are no taxable supplies in a particular period. **(10 Marks)**
- (b) China Road Network Corporation is a construction company incorporates and managed in China. It has a permanent establishment in Sri Lanka and it has constructed a toll road from Jaffna to Hambantota on build, operate and transfer (BOT) basis.

During the year of assessment 2010 / 2011, US dollars 106,000 has been remitted to its head office out of the profits for the year of assessment 2009 / 2010. Further, it has remitted US dollars 6,000 out of the dividends received from Sri Lankan resident companies. It has been confirmed that one US dollar is equal to Rs.115/- for relevant period.

Considering the fact that the employees of the company (of Chinese origin) are responsible for maintenance activities of the road and that for this purpose they use imported raw materials and capital goods, the Commissioner General was satisfied that the company is unable to ascertain the profits and income to be payable to the Sri Lankan government. Therefore, the company has been granted an approval by the Commissioner General of Inland Revenue under section 83 of the Inland Revenue Act to ascertain the profits and income by considering 9% of the total sum receivable. The turnover for the year of assessment 2010 / 2011 is Rs.138,250,000/-.

You are required to compute the income tax liability of the company for the year of assessment 2010 / 2011.

(10 Marks)

(Total 20 Marks)

Question No. 10 (20 Marks)

- (a) Mr. Pandula Dias has received an assessment rejecting the return furnished by him. This was the second such assessment received by him. He has no idea as to why such an assessment was issued since no communication was sent to him by the department. He is not satisfied with the assessment and therefore he wants to make an appeal. When drafting the grounds of appeal, what sort of advice would you give to Mr. Dias? **(05 Marks)**

- (b) XYZ is a non-resident company which has been incorporated in the United Kingdom. The company provides professional services to Sri Lankan companies as well as to companies outside Sri Lanka. Foreign currency receivable from countries outside Sri Lanka has been remitted to Sri Lanka through a bank. The company has claimed an exemption on these remittances. The Department of Inland Revenue has issued an assessment on the total profits and income of the company disregarding the request for exemption.

You are requested to comment on the validity of this assessment. (05 Marks)

- (c) Mr. Suranjith Kothalawela had paid Rs.98,000/- as income tax for the year of assessment 2009 / 2010. Taxable income for the year of assessment 2010 / 2011 is Rs.1,435,000/-. In order to eliminate paying penalty, he has made quarterly payments on the due dates, correctly.

You are requested to compute the final payment which had to be made on or before 30th September 2011. (05 Marks)

- (d) A notice in writing has been sent by the Department of Inland Revenue for the recovery of taxes in default. Assessee has made an objection within the stipulated time period. He was called for an interview by the Assessor. Since the Assessee has not responded, the Assessor has decided to settle the objection by confirming the assessment. Discuss whether such decision is within the law or not. **(05 Marks)**

(Total 20 Marks)

End of Part II

End of Section B

End of Question paper
