

EXAMINER'S REPORT

AA3 EXAMINATION - JANUARY 2017

(AA35) CORPORATE AND PERSONAL TAXATION

Question No. 01 (05 marks)

The overall knowledge of the candidates on the terms "Person" and "Year of Assessment" was at a very poor level. Those are the basic concepts of taxation without which thinking about taxation will be an imaginary situation.

Most of the candidates have mixed up the definition of person with the residency of a person, thinking about the "183 Days Rule".

The performance for this question was at an average level.

Question No. 02 (05 marks)

Most of the candidates had no idea about the obligations of employer with regard to the operation of the PAYE system. It was noted from the answers that, most of the candidates were unaware of,

- the date of PAYE payment,
- the date of furnishing annual return,
- the date of furnishing T10 Certificates, etc.

The performance for this question was at a poor level.

Question No. 03 (05 marks)

Generally, the case law knowledge of candidates was very poor in previous examinations.

Most of the candidates did not know the relationship between the definition of "trade" in Section 217 of the Inland Revenue Act and the case of "D. S. Mahavitharana Vs CIR". Some candidates have mixed up the facts of the given case with the case "Ram Iswara Vs CIR".

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

Question No. 04 (05 marks)

Most of the candidates have scored reasonable marks for this question which was to test the knowledge of Value Added Tax (VAT). But marks allocated for the "20th January 2016 payment" was not earned by almost all the candidates.

Majority of the candidates deducted the entire amount for the quarter as tax credit, regardless the payment that is applicable for the previous quarter.

The performance for this question was at a satisfactory level.

Question No. 05 (10 marks)

Part (a) of the question tested the methods available for the Commissioner General of Inland Revenue to recover taxes in default.

For this part, most of the candidates have guessed the answers such as taking legal action against the defaulter, taking the property of defaulter under custody of the Commissioner General. But most of the occasions, no descriptions were provided by candidates about the way in which the Commissioner General of Inland Revenue performs these tasks. This implies that majority of the candidates do not possess a comprehensive knowledge on recovery actions available for the Commissioner General.

The performance for this part of the question was not that satisfactory.

Part (b) of the question tested about the persons who can be an “Authorized Representative” under the Inland Revenue Act.

Following are some of the common wrong answers given by the candidates:

- Commissioner General and other Commissioners of Inland Revenue.
- President of Sri Lanka.
- Chief Justice and Judges in Appeal Court.
- Officer-in-Charge of nearest police station.
- Various names and titles of government servants.

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

Question No. 06 (10 marks)

This question tested the knowledge of Nation Building Tax (NBT). Majority of the candidates has secured at least 7 marks out of 10. The remaining 3 marks lost due to lack of knowledge on occasions where NBT cannot be claimed as an input tax and not knowing the date of furnishing the NBT return.

Most of the candidates have claimed NBT paid on office expenses as an input.

It was noted that nearly half of the candidates did not aware of the date of furnishing the NBT return. This was an unacceptable situation, because calculation of NBT without knowing the date of furnishing the relevant return does not produce a competent prospective employee.

The performance for this question was at an average level.

Question No. 07 (10 marks)

The knowledge on partnership taxation was tested from this question. Considerable number of candidates have secured at least 6 to 8 marks out of 10. The rest of the marks lost due to lack of knowledge in distributing Distributable Profit.

Significant number of candidates have misunderstood the partnership tax rate with individual tax rates accordingly they have applied the individual income tax rate of 4% to 24% to calculate the partnership tax.

In terms of the provisions of Inland Revenue Act No. 10 of 2006, in ascertaining the profit or loss of a partnership, nothing shall be deducted for salaries or other remuneration of partners. However, these candidates who did not aware of this provision, have allowed professional fees paid to partners as allowable deduction in arriving at the partnership profit.

The performance for this question was at a satisfactory level.

Question No. 08 (25 marks)

Computation of corporate income tax according to the Inland Revenue Act No. 10 of 2006 and subsequent amendments up to 31st March 2016 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.

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:

- Legal fees paid to a tax consultant for negotiating with the Inland Revenue Department to reduce the penalty – cannot be considered as incurred in the production of income, hence it should be disallowed. However, majority of the candidates have allowed it.
- Disallowed portion of the rent relating to CEO's rent free residence should be computed as follows:

$$\begin{aligned} 318,000 - 180,000 &= 138,000 \\ 138,000 \times 75\% &= 103,500 \end{aligned}$$

However, this adjustment has not been correctly done by majority of the candidates.

- Lease adjustment should be computed as follows:

$$\begin{aligned} \text{Total lease value} &= 44,000 \times 60 = 2,640,000 \\ \frac{1}{5}^{\text{th}} \text{ of total lease value} &= 2,640,000 \times \frac{1}{5} = 528,000 \\ \text{Lease payment made} &= 440,000 \end{aligned}$$

Whichever is lower is allowed to be deducted.

This adjustment has not been correctly done by majority. There were candidates who have allowed the lease interest paid also.

- Considerable number of candidates have incorrectly computed depreciation allowances. Some have applied incorrect rates to compute depreciation allowances. Some other candidates have computed depreciation allowance for leased assets also.
- Considerable number of candidates have deducted entire donation of Rs.600,000/- as an qualifying payment in arriving at taxable income without concentrating on the limitation of Rs.500,000/- or $\frac{1}{5}^{\text{th}}$ of Assessable Income, whichever is lower.

The performance for this question was at a satisfactory level.

Question No. 09 (05 marks)

Personal income tax computation for the year of assessment 2015/16 was tested. 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 cost of air tickets and accommodation for medical conference. Common mistakes identified are as follows:

- Most of the candidates have not compared the Net rent of the property with the NAV of the same. They have mentioned only the Net rent computed by them as the property income without comparing it with the NAV of that property.
- Sale of Motor car is a capital nature transaction and therefore it is not taxable. However, there were candidates who have considered the gain on sale of Motor car as taxable.
- Some candidates have not deducted the additional allowance on employment income of Rs.250,000/- in arriving at the taxable income.
- There were fewer number of candidates who have applied corporate income tax rate (28%) to compute the tax liability of **Hettige**.
- Some candidates have forgotten to deduct self-assessment tax payments and PAYE in arriving at the balance tax payable.

Overall performance for this question was at a satisfactory level. If the candidates have read the facts given in the question very carefully, they would have earned more marks.

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.

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