TAX2601 EXAM REVISION PACK

Study Questions and solutions

Written by **Class of 2016**

www.togetherwepass.co.za
info@togetherwepass.co.za
Tel: 021 100 0032

MODULE NOTES

Introduction

As Benjamin Franklin once part it “if you do not want to be taxed, never get born.”

Governments exist to fill the void that would exist if everything was left to private individuals. No one would concerned with other people’s issues so long as it does not affect them. Think of goods like provisions of road and e-toll, if you can pay you will not be able to use the road governments exist so that everyone in society is concerned for. To provide those essential services government need money to do that and governments get their money through taxation, which is part of the laws government use.

To be proficient in taxation are needs to understand the law and how the various governmental agencies apply them and how courts interpret those laws whenever a question of the law arises between a person and the Governmental agencies charged with Enforcing those laws. Tax laws are enforced by SARS through the commissioner.

The Laws of the country are subject to the Constitution of the South Africa and the Bill of Rights of South Africa, that is all Laws and regulations must obey the spirit of the Constitution or they will be void. Law are enacted by parliament after they have been debated as bills, after they have been enacted by parliament they are signed by the President into Law. Parliament enacts Laws by statute.

Application and Interpretation of the Law

- When Laws are being interpreted, they are interpreted literally unless such literal interpretation would lead to an ambiguous result.
- Laws that are clear in legislation that need no courts to interpret them are called statute or statutory law.
- Where a question of the interpretation of the law arises between a personal government agencies that enforces them, where that happens, that would leave the interpretation of that Law to the courts who are the authority on the interpretation of the

Law. Courts in South Africa apply the dovine of stare decisis, which states that are

precedent is established, it should be followed, and if a higher court sets a precedent all lower courts are bound to follow it (previous rulings of higher Courts to be followed by lower courts).

Level of Courts in South Africa

Constitutional Court (deal with Constitutional issues only)

↓

Supreme Court **governed when a case on tax is there).**

(Tax Court – it is a special form only

Therefore it is no court in itself

↓

High Court

↓

Magistrates Courts

Before an aggrieved party can approach the Courts they may try to settle the tax issue using the

Alternative Dispute Resolution Method or the Tan Board.

Alternative dispute Resolution

- Is used to settle any type or level of Tan dispute and for it to be effective and binding on the Parties both must agree to it.
- SARS obliged to keep a register of all disputes settled using this Method.

The Tax Board

- Owing taxpayer who disagrees with any decision of the Commission of SARS may appeal to the tax Board provided that
- The amount in dispute is less than R500 000.00 OR
- The taxpayer and the Commissioner both agree to take the matter to the tax board.
- The team player or the Commissioner does not object to the Board making a ruling on the tax issue.
- The Tax board will be composed of an advocate or attorney who will chair the Board.
- An accountant or representative of the Business / Commercial Community.

The Tax Court

- Is a creation of statute and has no standing in its own right, its decision are only binding on the parties involved. However its rulings or decision have persuasive value on other parties as well.
- The Tax Court will consist of judge of the Supreme Court (who will be Court President), An Accountant 9who has been in practice for 10years) and a representation of the Commercial Community/ Business Community.
- The tax Court will always hear the case between the taxpayer and SAR from the beginning.
- Tax Court rulings do not set precedent hence the tax Court is not bound by its own decisions of the past.
- In any dispute before the Tax Court the burden of proof lies with the tax payer unless an amount is to be determined where the one shifts to the Commissioner.

High Court

- High Courts only adjudicate issue that are on appeal from the high court or tam issues too serious for the Tam Board or Tam Court.

- Decisions of the High Court are binding on all lower courts indulge the Tan Court.

Supreme Court

Hears tax case appeal from the High Court or from the Tan Court with Court President permission.

Decision of the Supreme Court are binding on all Courts.

Constitutional Court

- Deal with only Constitutional issues.
- Taxpayer can only appeal to this court based on Constitutional challenges to the Law.
- One always precedent that has been set by Prior cases brought before the Courts to see how the Courts might decide on a particular issue of the Law or how it is supposed to be applied by the governmental agencies, this is known as case law.
- In Interpretation Case Law one always has to pay particular attention to the Rati decidendi of a case (Reason or ground for decision in that Case) and the Obiter dicta of that case(statement made in passing to support the reason for the decision in the case).
- The level of the Court giving the decision also has to be looked into.
- The Ratio decidendi of a higher court is binding on all lower courts while the Obiter dicta may be used as persusive evidence in the lower courts.
- In administrating the tax system SARS is bound by legislation to keep the affairs of taxpayers secrete and not to disclose them unless they pose a public danger section 4 of the Act.

Taxation and Statute

- Tax is chargeable by virtue of section 5 of the income tax Act 58 of 1962 which states that "there shall be paid annually for the benefit of the national Revenue had an income tax…" sotax is paid on income and on other transaction by virtue of different legislation like VAT, Estate duty etc.

What is Income (Tax formula)

- Income is composed of Gross Income less exempt Income.
- Gross Income is defined by section 1 and has two components, one for residents and other for Non Residents.
- South Africa has a two tier tax system, a residents based for residents and a source based one for non-residents.

Gross Income is the "Total Amount received in cash or otherwise, received by or accrued to or in favour of such resident during any year of assessment excluding receipts of a capital Nature" and for Non-residents from a source within the Republic.

- One applies the literally meaning and also looks at case law to fully understand what gross income is. Case like the lategan case, Butcherbros, Delfos, Lace propriatory Mines.

Gross income as defined by Case Law

- The Delfos Case, Butcher Bros case, Lace propriatory Mines tell us that if anything corporated or incorporeal has a determinable value and is gained or accrues to the taxpayer in any year of assessment it will be taxable in his hands. As long as the Commissioner is able to determine the value of Propely gained by the taxpayer it will be taxable.
- The Delagoa Bay company case, Pyotts case tell us that if a taxpayer receives a property or money or it accrues (meaning that it becomes taxable in his hands on the taxpayer becomes entitled to it) provided it is not Capital in Nature.

Income Vs Capital

- The Visser case
- Separated what is capital and what is income. Capital is not defined in the Act. However no single infallible test to distinguish between capital and income exists and there that as well has been left to the Courts to decide especially where assets are sold
- In the Vesser Case it was held that income is what capital produces, that is Capital is the tree and income is the Fruit of the tree.
- This is especially problematic where taxpayers sale their Income producing Asset or their assets.

Tests used by Courts to distinguish between Capital and Income

- No single test exists, so courts have used various test to determine the nature. However courts have used the intention of the taxpayer to determine whether receipts from selling of Assets is Capital or Income.
- The problem with intention is that it is subjective. However courts have used two types of factors to test or establish the intention of the taxpayer.

Objective Factors

- These are derived from the action of the taxpayer one he has disposed of the Asset. The manner in which the taxpayer deals with the Asset will give evidence of the manner in which the team player has intended to deal with that particular asset.

Subjective Factor

- These are used when a taxpayer had two or more intentions in the acquisition, used and disposal of an Assets.
- These are used to find the Dominent intention of the taxpayer with regards to the Asset.

Juristic person

- Establishing intention for juristic persons is essentially problematic in that juristic persons. However the intentions of companies directors have been in sensibility linked to the intentions of the Company the Courts have said but this are also be a factor in limited circumstances.
- The Memorandum of Incorporation will also be used to deduce the intention of the Company.

Special Inclusions

- These are amounts or accrual that through they are capital in nature, will be included in the Gross Income of a taxpayer by virtue of their being specifically included by a provision of the Income tax Act.
- Some of the specific Inclusions that relate to Business entities are as follows:

a) Lease premiums – payments to lessors in addition to Monthly rentals usually at the beginning of the period.

b) Leasehold improvements

c) Sale of certain Assets that were manufactured by the team payer even through used by taxpayer in his trade.

d) Keyman Insurance policies proceeds

e) Recoupments- recovery of amounts previously granted as capital allowances.

Exempt Income s1o

- These are amount that meet the definition of gross income by is not going to be taxable because of their (a) taxpayer we are dealing with the (e.g.) government and foreign government agencies.
- These are absolute exemptions or full exemptions may also relate to the type of income that they are receiving. For business entitles they are few.

(b) Partial Exemptions-These are exemptions that are not full or absolute part of the income received or accrued will be taxable in the hands of the taxpayer.

- Before an amount should be attempt it is First Gross Income, then if it is exempt, it will be removed from the Gross Income of the Taxpayer to use the Tax formular the following applies.

Tax Formula

- Gross Income (Incomes that meet definition).
- Exempt Income (Absolute or Partial)

Income

- Always First Include an amount into Gross Income then deduct it from Income if it is exempt.
- Residency

- Residence of a person is where that person normal stays literally. However for taxpurpose Residency has a specific.
  - Ordinarily resident is not defined and has no special meaning nor technical meaning. Therefore it has been left to the Courts to decide what that mean.
  - There is also a physical presence test attached to the working of resident, applicable only if a person does not meet the ordinarily resident definition.
  - In Cohen vs CIR it was decided by the courts that a person’s ordinarily resident in the Country to which he would naturally and as a matter of course return from his wanderings.
  - For juristic persons (companies, trusts etc.) the place where they are formed or effectively managed determine their residency.
  - Another Case to note on residence is CIR vs Kuttel as it reinforced the tension in Cohen vs CIR.

General deduction Formula

- Taxpayers can deduct certain amount from their income to arrive at their taxable income, provided it meets certain conditions. In order to deduct a certain amount from income, the onus/burden of proof is always with the tax payer to prove that the amount is deductible.
- The general deductions Fomular is found in section 11a of the Income tax Act as read in conjuction with 323g of the same Act.
- See 11(a)- (2)states that “The shall be allowed to be deducted from the Income of a taxpayer expenses and losses actually incurred in the Production of income provided that such expenditure / losses are not of a capital nature.

- For the deductions to be available the taxpayer must be carrying on a trade or in the production of income (trade)

- So from this it follows that any expense incurred by any taxpayer are deductible in that particular year of Assessment they are incurred.

- Expenses are voluntary incurrences that are boune by the Taxpayer.
- Losses are involuntary incurrence that occur to the taxpayer.

Segments of the General deduction fomular

Trade

- Trade is any activity that is undertaken by a taxpayer and is widely defined. Usually trade is carried on with a profit motive, therefore a trade is continuous in nature.

- However the absence of a profit does not preclude an activity from being a trade (Burgess vs CIR)

Actually lectured (Edgars stores vs CIR)

- All before an expense is deductible, it should have become due and payable, that is it should have been incurred.

- If a condition attaches to any expense for it to become due and payable, before that condition happens the taxpayer is not liable to expend any monies, therefore no expenditure would have occurred.

During the year of Assessment

For any expense to be deductible, it should have been incurred by the taxpayer in the year of Assessments if a taxpayer does not claim an item of expenditure in the year of Assessment. They can never claim that item of expenditure in another year of assessment unless some e.g. specific rules apply.

In The Production of Income

For an expense to be deductible, it's should have been incurred in the production of income,

Here they are two important Landmark case that one has to become familiar with, the "Port Elizabeth electric tramway company Ltd vs CIR.

Port Elizabeth Electric Tramway vs CIR

The taxpayer was an operator of tax pays. A driver of the Tram and accident and died. The family sued the company and was awarded damages, the issue before the court was, were the damages deductible for tax purposes.

Held: It is inseparable that a driver of tram would be involved in an accident at one time or another would be involved in an accident as accidents are part and parked of being on the road. Therefore the damages could be deducted as accidents could not be removed from the income producing activities of the tax payer.

Joffe and Co. (Pty) Ltd vs CIR

- In this case, the taxpayers where engineers of reinforced concrete. On one of their jobs.

The concrete structure as it was not properly done they were working on collapsed killing one of the workmen working on it. The family of the workmen sued the company for damaged and was awarded damages. The Question before the court was where the damages deductible for tax purposes.

Held: As the concrete was not properly done by the engineers, this was negligence. It is not expected of taxpayer to be negligent in carrying out their activities. As a result the damages where not deductible for tax purposes. Negligence is not a natural con commitant of under taking of activities.

From the above presented two cases it is important to recognise that expenses incurred in the production of income in a trade are deductible, if the originating cause of the expense cannot be separated from the income earning activities as long as Negligence is not involved.

Also the amounts of the expenditures and need not to be of a capital nature for it to be deductible. Establishing whether expenditure is of a capital nature or not has been a fertile ground for disagreement and continues to be so.

The courts have also applied different tasks to establish whether an amount of expenditure is capital in nature or not, none of the test are conclusive in all by themselves, they are always applied in conduction with other tests. The tests are as follows:

a) True Nature of Transactions
b) Closeness to income operating activities or income earning structure
c) Creating an asset or advantage that provides on enduring benefit
d) Once and for all expenditure

One important case in this regard is the new state areas case. In this case the taxpayer was a gold miner. The taxpayer was required to install a sewage system and link it to the local authority system. The system was installed and the cost borne by the local authority, to be repaid to the local authority over 60 months for the portion on its property. The issue before the courts was were either of the instalments payable in respect of the sewage system capital in nature or not.

> **Held**: For the portion that was on the property of the tax payer where ownership
>
> was going to pass to the owner, it was Capital (Acquisition of an Asset) and for the portion that was not on the property of the taxpayer and where ownership was never going to pass to the taxpayer it was a revenue expense as it was recurrent in nature and did not lose it nature by mere fact that it had been discharged by instalments over a number of years.

Specific deduction

- If expenses do not meet the general deductions formula to be deducted does not mean it might not be deductible, e.g. because it is of a capital nature.
- There may be a specific provision in the Income tax Act that makes it deductible.
- If an expense is deductible under both the general deductions formula or a specific provision, it can only be claimed once not on both and under the specific provision . (Double deductions not allowed).

Legal Expenses

- Legal Expenses of any action at Law are deductible under 5110 provided that they do not pertain to expense of a capital nature.

Restraint of Trade

- Any restraint of Trade payment is deductible on the longer 3 years or the number of

  years specified in the Contract; for example if the contract says the restraint of trade is in effect for two years then it will be written off over 3 years, but if the contract says the restraint of trade is in effect for 5 years it will be written off 5 years for tax purposes.

Registration of Patents, Acquisitions of patents, copyrights and trademarks

- Expense relating to registration of patents or trademarks/copyrights or design may be deducted under section 11 (QB).

- In the year that the Taxpayer first brings the patent or copyright into use 10% of the expenditure incurred in procuring it or developing it is deductible provided the lost exceed R5000.
- However the acquisition of a trademark will not qualify for a deduction

Research and Development Expenditure

Where a taxpayer has incurred research and expenditure that relates to the creation of intellectual property, they can deduct under section 11D of the Act.

If the expenditure is carried on after approval is obtained from the department of science and technology then the taxpayer may deduct 150% of the expenditure.

If no approval is obtained from the department only 100% will be deductible.

Research and development only constitute technical research to develop intellectual properly or scientific knowledge and does not include market research.

Bad debt and Doubtful debts

- Debts that are in coverable are allowed as a deduction provided they were incurred in the income of the taxpayer before (Bad debts).
- To claim a provision of doubtful debts a list of those doubtful debts must be provided to the commissioner and he will allow 25% of that list as provided by taxpayer as or use a formula as provided for in legislation.
- If a provision as granted to a taxpayer as a deduction, it should be included in his income in the following year.

Pension fund and Benefit fund Contributions by the employer

- Contribution to pension funds and benefit funds will be allowed as deductions in the funds of the employer as long as they are deemed not to be excessive.

- For the expenditure not to be limited by the commissioner it should not exceed 10 % of the approved remuneration payable to employees.

Enmities to force employees and their dependents

- If the employee resigned due to old age or ill health then any payment made to them or their dependants will deductible as when it is incurred by the former employer.

Trading Stock

- Special rules pertain to trading stock and are contained in section 22 of the income tax Act.
- Opening stock and purchases are deducted from income of a tax payer in any year of assessment.
- Closing stock is added to income of the taxpayer in any year of Assessment.

Donations to Public Benefit Organisation

-

- Any donation to a public benefit organisation (e.g. S.P.C.A.) that are accompanied by a section 1A receipt are deductible from the income of the taxpayer, provided the donation does not exceed 10% of the taxable Income of the tax payer before the deduction.

Prohibited Deduction

Certain expenses may not be deducted even if the meet the requirement of s11 (a) and include the following

(a) Issued losses – losses that will be reimbursed will not be allowed as a deduction.
(b) Taxes , penalties or interest on taxes will not be allowed as a deduction
(c) Expenses incurred to produce exempt income.
(d) Non trade expenditure
(e) Restraint of trade payments (to be earlier deducted as provided for
(f) Fines and corrupt activities

Prepaid **Expenses**

- Prepaid expenses are limited to R100 000 if the prepayment is for a period longer than 6 months into the next coming year of assessment and the expenditure exceed R100 000.
- If the expenditure in excess of 6 months exceed R100 000 in aggregate, no deductions will be available to the taxpayer and those deductions will only be claimed in the year of assessment to which they relate to.

Capital Allowance

- A taxpayer will be allowed to deduct part of expenditure that was incurred in buying Capital assets or on assets used in the production of Income for the taxpayer.
-

- The capital allowances that can be claimed by a taxpayer will be claimed under specific rules in the Income tax Act.

Repairs and improvement section 11 (d)

- Repairs are costs that are incurred to keep an asset in the same working order it was before. (CIR vs African products manufacturing co. Ltd).

- It does not matter if the materials used, as long as the productive capacity of the asset is not matter of the materials used, as long as the productive capacity of the asset is not enhanced it will be regarded as a repair and be deductible under section 11 (d).

- An improvement is an expenditure that improves the productive capacity of an asset either by changing the units it produces or extent its useful life.
- Improvements are not deductible at once as a deduction but will be allowed over the write off period of the asset as provided for by legislation or General Binding Ruling.

Capital Allowances Section 12C

- For assets used in the process of manufacturer various deductions are available depending on the nature of the taxpayer when they first used the asset.

- For taxpayer (Normal) who use assets in a process similar to manufacture two types of deductions are available.
- For new and unused assets the will be written off as follow
- 40% in the first year
- 20% in the following 3 years

Used Assets

For used assets that are used for the first year by the taxpayer deductions will be available at 20% per year over 5 years.

- Deductions under section 12 C are not prorated for time. Is assets actually bought by a taxpayer for asset inherited or trading.
- There will be section 11(e) available.

Small business corporations (section 12E)

- Small business corporations that uses assets in a process similar to manufacture the manufacturing assets are written off in full in the year the taxpayer first brings them into use.
- For Non manufacturing Assets used by small business corporation they are allowed as follows –

  50% in the First year

  30% in the second year

  20% in the third year

- General wear and tear allowances (section 11 (e))
- Section 11(e) allowances is available for any asset that has a value, that is it can be used on inherited assets, trade inns etc.
- Section 11 € is used in connection with general binding ruling 7 which gives the number of years over which the asset may be written - off.
- Section 11 (e) alliances are prorated for the number of months they have been used in the current year of assessment. That is the deductions is multiplied by the number of months the asset has been used in the business.

Buildings used in a process of manufacture section 13 (1)

- Building costs excluding land are allowable under section 13 9(c) of the Income tax at 5% provided that the build are used majorly (above 50%) to produce taxable income.

- This allowance is available for buildings erected after 1 October 1999. This allowance is not apportioned for part of the year.

Commercial Building s13 (quoin)

- Applies only to new and unused building or improvements erected after 01 April 2007.
- The allowance granted will be at 5% for each year of assessment not apportioned for part of the year.
- Where a tax payer buys also bought part of the building after 21 October 200 without constructing it the cost must be adjusted to 55 % of the cost of acquisition if the part is acquired or 30% if it is an improvement to the building that is acquired.

Residential units and sale of low cost units on loan account

- A residential unit is a building or a self-contained unit used for residential accommodation excluding building used hotels.
- An allowance of 5% per annum to taxpayers who own such units will be available if the following conditions are met.
- A tax payer owns reward unused residential units
- The units are used by the taxpayer for purposes of trade
- The Units are in the republic and the taxpayer owns at least 5 of the residential units.
- If the residential units are low cost residential units n additional 5 % allowance maybe claimed.
- A low cost residential unit is either

  A standalone unit costing less than R200 000 and the monthly rental charged does not exceed 1% of cost (2000) or

  An apartment whose cost does not exceed R250 000 and the monthly rental does not exceed 1% of the cost (R2500).

If the employer sell a low cost residential unit to any of his employed through an interest free loan an additional 10% allowance may be claimed as a deduction in any year of assessment.

An amount paid back by the employee to the employer will deemed to be recoupment and be included in the taxpayer income.

Disposal of Assets on which allowance have been claimed

Where a taxpayer disposes of assets where allowances have been claimed previously, Grunted allowances that are recovered by the taxpayer will be treated as recoupment.

If the assets on which allowances where being claimed is sold at below its Income tax value a scrapping allowance will arise and be granted as a deduction (s116)).

Recoupment or scrapping allowance is calculated follows	**R**
Proceeds / cost (whichever is lower)	xxxx
Less income tax value	(xxx)
Recoupment / (scrapping allowance if negative)	**xxxx**

Income tax values calculated as follows	**R**
Cost	xxxx
Less Accumulated wear and tear / allowances claimed	(xxxx)
Income tax value	**xxxx**

This calculation and adjustment is to be done every time a temperature disposes of an allowance asset (Depreciable assets for temperatures)

No scrapping allowances are available for buildings though.

Types of Tax payers

Tax payer will be treated differently for purposes, depending on their nature.

Sole traders

Sole traders are not tax payers as defined, so the individuals running the sole proprietorship will be in their individual person.

The tax will be calculated as per the tax tables that apply individuals and tax will be applied on a sliding scale.

Partnership

As w ell as sole traders, partnerships are also not a legal concept and not tax entity as well. Partners will be the one's taxed on their individual persons on the tax tables on their profit sharing ratios. Deductions to partners will also be available to the partners on their profit sharing ratios.

Companies

Are separate legal entity and taxpayer in its own right, companies are owned by shareholders but are taxed separately.

Tax on companies is calculated on their taxable income as calculated from the tax framework. There are different types of companies which have different tax rates applicable to its table income.

Normal companies are taxed a t 2% of their taxable income.

Small business corporations.

- This is a special type of company for tax purposes. To be regarded as a small business corporation, companies have to meet the following criteria.
  Section [12(E (4))].
  - Gross income in any year of assessment does not exceed R20 Million
  - None of the shareholders/members has any interest in any other company 5% interest in listed companies, cooperatives.

Not more than 20% of all the total receipts and accruals other than capital receipts consist of investment income and income from rendering of services.

- Small business corporations are taxed on a sliding scale as follows on taxable income not exceeding R63556 @ 0% taxable income exceeding R63556 – R350 000 @ 7% Taxable exceeding R350 000

Close Corporations

Are regarded the same as companies for tax purposes

Micro businesses

- Are a special type of easily for tax purposes and can be either companies or individuals.
- Micro business are taxed on a simplified tax system called turnover tax.
- Trusts may never be regarded as micro businesses and the following may never qualify as micro businesses
  - Persons with interest is in other companies
  - Personal services providers and labour brokers
  - Investment income and professional service providers if more than 20% comes from investment income or rendering professional services.

Taxable Turnover

Qualifying turnover means total receipts from the carrying on of business activities and does not exceed R1 million.

50% of all capital receipts will be included in taxable income.

Levying of turnover tax	
R0 - R50000	0%
R150 000-R300 000	1%

R300 000 – R500 000	R1500 + 2% of amount above R300 000
R500 000 – R750 000	R5500+4% f amount above R500 000
R750 000 and above	R15500+0% of amount above R750 000

Trusts

- Trusts are a tax vehicle and estate planning vehicle to form a trust deed is required that specifies the beneficiaries of their trust specifies their rights and obligations of the parties involved in the trust.
- A trust is a separate entity for tax purposes and will be taxed in its own right.
- There are various types of trusts, normal trusts are taxed at 40% on their taxable income and special trusts are taxed on the same basis as individuals.

Collection of taxes from taxpayers

- Salaried employees make provision for their annual tax liability by paying employees tax (P.A.Y.E) on a monthly basis.
- Employers are responsible for collecting P.A.Y.E and paying it over to SARS.
- Other business entities or taxpayers who obtained other income other than from employment will pay their tax liability through Provisional tax.

Provisional tax Payment

- It is not another tax but a way of collecting tax for SARS.
- Provisional tax payments are made twice per year with an optional third payment of provisional tax payment available.
- To provide for provisional tax, a tax payer estimates his/her taxable income and pays half of the tax due in the first payment and the second provisional tax is calculated on the revised taxable income of the taxpayer.
- There are special rules that apply to the calculation of provisional tax payments and in summary are as follows.

- For taxpayers whose taxable income does exceed R1000 000, the Provisional tax is calculated as follows:

i. Estimate the taxable income

ii. Calculate tax payable and divide by 2 and that will be the 1st provisional tax payable.

iii. For the second payment a revised estimate is used, as long as the taxable income no penalties will be payable.

- If the estimate that the taxpayer makes is less than 90% of his actual taxable income penalties might be levied by the commissioner.

- If the taxable income of the taxpayer is done R100 000 the estimate should be 80% of the taxable income, otherwise penalties will be imposed by the commissioner.

- If the taxpayer cannot estimate his/her taxable income the commissioner may use his previous taxable income to levy the provisional tax.
- If the last assessed taxable income is greater than the taxpayer estimated taxable income the commissioner may use that to levy the taxpayers provisional tax if the last assessment is older than 1 months it should be adjusted and it will be adjusted upwards by % to arrive at the commissioners estimates taxable income from which to levy provisional tax.

Capital Gains tax

- Capital Gains tax is a tax that is payable as disposal of assets. For Capital gains to be chargeable there should have been a disposal or lancination of property or assets.

- Capital gains is not separate term as it is pulled into the taxable income of a taxpayer by section 26A of the Income tax act.
- Capital gains became liveable in South Africa from 1 October 2001.
- To calculate capital gains one has to look at the eight schedule of the income tax act.

Assets acquired after 1 October

- To calculate Capital gains for assets that are disposed of that where acquired after 1 October 2001 will be calculated as follow

	R
Proceeds (Amount obtained on s ale of Asset)	xxxx
Less : recoupment (wear and tear allowances previously claimed)	(xxxx)
Adjusted proceeds recovered)	Xxxx
	(xxxx)
Less : Base costs	(xxxx)
Cost of acquisition	Xxxx
Less wear and tear allowances claimed	(xxxx)
Costs to sell asset(the capital asset)	xxxx
Capital gain	Xxxx
Inclusion rate for companies at 66.6%	xxxx

Capital gains will be included in the taxable income of a taxpayer at 66.6% of the capital gain.

Assets acquired before 1 October 2001

For assets that were acquired before 1 October 2001 a value for calculating capital gains for tax purposes will have to be established. And there were specific rules that have been laid out by legislation (Time apportioned base cost).

The Law laid out the following options for the taxpayer

The 20% here the taxpayer has the option to deduct 20% of the proceeds obtained from the disposal of the asset as the base cost.

The Law also makes provision for the taxpayer to have obtained the value of the asset on 1 October 2001.

The cost involved in obtaining that value will be included in the base cost of the asset.

Also included in this will be expenditure to improve the asset after 1 October 2001.

Time apportioned Base cost – this is a formula provided for by legislation to calculate the base cost of an asset, being disposed that was acquired before 1 October 2001.
The way to calculate Capital Gains in this case will be as follows:

	R	R
Proceeds (Amounts from selling assets or Deemed Amount)		xxxx
Less Amounts included in taxable income (Recoupment)		xxxx
Adjusted proceeds		xxxx
Less Base Cost (higher of)		
20% Rate	xxxx	
20% of proceeds		
Or		
VDV and expenditure after		
Valuation value 91 October 2001 value)	xxxx	
Costs after (1 October 2001)	xxxx	
Base cost	xxxx	
Or		
Time apportioned Base Cost		
Will be given always	xxxx	

Higher of the Three (after claimed deducting wear and tear allowances	(xxxx)
Capital gain	**xxxx**

Inclusion at 66.6%

The Tax formula	R	R
Gross Income – general Inclusions (s1)		xxxx
Specific Inclusions(s1)		
Total Gross Income		xxxx
		xxxx
Less Exemptions (s10): General and specific		(xxxx)
Income		xxxx
Add Other inclusions in income		xxxx
Less Deductions available to the taxpayer		
		Capital allowances
General deductions		

Subtotal		
Add Taxable capital gain at inclusion rate (66.6%)	xxxx	
Subtotal	xxxx	(xxxx)
Less Donations allowable (section 1:limited to 10% of taxable)		xxxx
		xxxx
		xxxx
Income before donations		
Taxable income		(Xxxx)
		xxxx

QUESTIONS AND SUGGESTED SOLUTIONS

<u>IMPORTANT INSTRUCTIONS</u>:

e) All amounts exclude VAT unless stated otherwise.
f) All persons mentioned are residents of the Republic of South Africa unless stated otherwise.
g) SARS = South African Revenue Service

<u>The answering of this paper</u>:

(c) This paper consists of four (4) questions.
(d) Answer all the questions.
(e) Start each question on a new (separate) page.
(f) **Show all workings, where applicable. Where an amount is subject to a limitation, clearly indicate the application of the limitation. Where any item is exempt from tax or not allowable as a deduction, this must be indicated. All amounts must be rounded to the nearest rand.**
(g) Please complete the cover page of the answer book in full.
(h) You are reminded that answers may **NOT** be written in pencil.
(i) Principle errors will be marked negatively.

(j) Proposed timetable **(try as far as possible not to deviate from this timetable):**

Question	Topic	Marks	Minutes
1	Tax liability of a company	23	28
2	Capital allowances	26	31
3	Capital gains tax	25	30
4	Gross income and general deduction	26	31
	TOTAL	**100**	**120**

QUESTION 1 (23 marks, 28 minutes)

Rashupi Trailers (Pty) Ltd (Rashupi) is a company that manufactures and sells trailers. The company is **not** a small business corporation as defined in the Income Tax Act and its financial year ends on 31 March.

The company's accountant calculated the taxable income of R4 781 142 **without** taking into account the transactions that took place in February and March 2015. The following is a summary of the transactions that took place in the last two months of the year of assessment ended on 31 March 2015:

Income	**Notes**	**R**	**R**
Sales			800 000
Local dividends			150 000
Interest			355 000
Expenditure			
Trading stock	1		
- opening stock		244 000	
- purchases		486 000	
- closing stock		(457 000)	
- cost of sales			(273 000)
Dividends paid	2		(250 000)
Salaries			(455 000)
Doubtful debts - 2015	3		(54 000)
Restraint of trade	4		(450 000)
Depreciation	5		(36 111)
Contribution by employer	6		(57 630)
Leave pay provision			(45 247)

Notes:

1. The accountant had not taken trading stock into account in calculating the taxable income of R4 781 142. The information in the table below relates to the trading stock.

	01/04/2014		**31/03/2015**	
	Cost Price	**Market Value**	**Cost Price**	**Market Value**
Trailers	R244 000	R350 000	R457 000	R420 000

2. Rashupi paid a dividend of R250 000 to its shareholders.

3. The following table relates to the doubtful debts:

	01/04/2013 – 31/03/2014	**01/04/2014 – 31/03/2015**
List of doubtful debts	R78 000	R54 000

Dieketseng Moloi, the former Chief Executive Officer of Rashupi, was paid R450 000 on 15 January 2015 to restrain her from working for the competition for a period of 24 months.

iv. Depreciation was calculated as follows:

Description	Date of purchase	Date brought into use	Cost R	Depreciation R
Manufacturing machines - new and unused	05/02/2015	01/03/2015	350 000	11 667
Trucks - new and unused	01/05/2010	01/06/2010	440 000	24 444
				36 111

The accountant was not sure how to account for the transaction for taxation purposes and did not take the capital allowances into consideration when calculating the taxable income of R4 781 142.

Binding general ruling No 7 makes provision for the following write-off period:

- Trucks – 4 years

a) Rashupi made contributions of R57 630 to a medical aid scheme for the benefit of its employees. The remuneration approved by the Commissioner in this regard was R480 000.

b) Rashupi had an assessed loss of R274 145 in the previous year of assessment. The company also made a provisional tax payment of R976 214 for the current year of assessment.

REQUIRED:	MARKS
Calculate Rashupi Trailers (Pty) Ltd's normal tax liability for the year of assessment ended 31 March 2015 by starting with the taxable income of **R4 781 142**.	**23**

QUESTION 2 (26 marks, 31 minutes)

Bear Cut & Drill (Pty) Ltd is a South African company that manufactures a wide range of steel products for the building industry. The company is **not** a small business corporation as defined in the Income Tax Act and its tax year ends on 31 March 2015.

The accountant has approached you to assist with the income tax calculation for Bear Cut & Drill (Pty) Ltd for the 2015 year of assessment. The company has an accounting profit of **R2 676 387** for the 2015 year of assessment **before** the following has been taken into account:

1. Repairs and maintenance

On 31 October 2014, a severe hailstorm caused damage to the factory roof. Bear Cut & Drill (Pty) Ltd repaired the damaged roof on 30 November 2014 at a total cost of R72 000 of which R65 000 was covered by an insurance policy.

During the period the factory roof was repaired, Bear Cut & Drill (Pty) Ltd also enlarged the factory floor space to increase its production capacity. The total cost of the additions to the factory building was R250 000 and was completed on 30 November 2014 and brought into use on 2 December 2014.

2. Factory machinery

On 15 August 2014 Bear Cut & Drill (Pty) Ltd purchased a new steel bending machine at a total cost of R450 000 to be used directly in its process of manufacturing steel products. Installations costs of R20 000 were incurred and the machine was brought into use on 5 September 2014.

Bear Cut & Drill (Pty) Ltd decided to sell a steel drill machine, which it originally purchased second hand on 30 June 2012 for R120 000 and brought into use on the same date. The steel drill machine was sold for R80 000 on 28 February 2015.

3. Other assets purchased and sold

Bear Cut & Drill (Pty) Ltd had the following non-manufacturing assets on hand at 31 March 2015:

α A delivery truck that was purchased new on 30 June 2014 at a total cost of R185 000 and brought into use on 1 August 2014.
β Two laptop computers that were purchased on 31 May 2013 at a total cost of R15 000 and brought into use on the same date.

Bear Cut & Drill (Pty) Ltd sold one of its passenger vehicles that was damaged during the hail storm on 31 October 2014 for R59 500. This vehicle was originally purchased for R90 000 on 1 April 2014 and brought into use on the same date.

Binding general ruling No. 7 allows for the following write-off periods where applicable:

ι Delivery trucks – 4 years
ιι Laptop computers – 3 years
ιιι Passenger vehicles – 5 years

QUESTION 2 (continued)

4. Factory building

The factory building that houses the whole manufacturing process of Bear Cut & Drill (Pty) Ltd was originally erected on 31 July 2011 at a total cost of R3 600 000 and brought into use on 1 August 2011. Several windows of the factory building were damaged by a hailstorm on 31 October 2014 and had to be replaced at a cost of R61 000 on 2 November 2014, of which no amount was covered by the company's insurance policy.

5. Commercial building

Bear Cut & Drill (Pty) Ltd purchased a used commercial building at a total cost of R350 000 on 31 August 2014 and brought it into use on 15 September 2014. The building was used mainly to house the debtors and creditors administration of Bear Cut & Drill (Pty) Ltd from the date the building was brought into use.

6. Other information

Loose CC, one of Bear Cut & Drill (Pty) Ltd's debtors, was liquidated on 15 November 2014 and owed Bear Cut & Drill (Pty) Ltd R18 000 (excluding any finance charges). The liquidators managed to recover R2 000 of the outstanding balance of R18 000 on 17 February 2015 and remitted that amount to Bear Cut & Drill (Pty) Ltd on 19 February 2015.

Bear Cut & Drill (Pty) Ltd claimed a doubtful debt allowance of R42 500 for the 2014 year of assessment. The list of doubtful debtors on 31 March 2015 amounts to R212 000.

The monthly rental for the telephone and security system of R4 000 for March 2015 was not accounted for in the accounting records. The rental invoice dated 1 March 2015 was only received via e-mail on 15 April 2015.

Bear Cut & Drill (Pty) Ltd has incurred an assessed tax loss of R181 697 during the 2014 year of assessment.

REQUIRED:	**MARKS**
Calculate the income tax liability of Bear Cut & Drill (Pty) Ltd for the year of assessment ended 31 March 2015. Start your calculation with the accounting profit of **R2 676 387** as provided.	**26**

QUESTION 3 (25 marks, 30 minutes)

PART A (17 marks, 20 minutes)

Aerostar (Pty) Ltd manufactures and sells sports cars. Aerostar (Pty) Ltd has a February year-end and an assessed capital loss brought forward from the previous year of assessment of R64 500.

The following capital transactions took place during the 2015 year of assessment:

Transaction one

Factory A was sold on 12 January 2015 to an unconnected person for R780 000. Factory A was purchased on 15 July 1999 for R250 000 and was brought into use on the same date directly in the process of manufacturing the sports cars. Transfer costs of R25 000 were incur-red on the purchase price of Factory A. The total capital allowances claimed on Factory A was R220 000 up to the date of disposal.

Other information applicable to Factory A:

Market value on 1 October 2001	R350 000
Time-apportionment base cost (TAB)	R 98 125

Transaction two

Aerostar (Pty) Ltd sold manufacturing machine C on 18 May 2014. The capital gain on this machine was R50 000.

REQUIRED:	MARKS
Calculate the taxable capital gain/capital loss of Aerostar (Pty) Ltd for the year of assessment ended on 28 February 2015.	17

PART B (8 marks, 10 minutes)

Aerostar (Pty) Ltd had a taxable income of R1 150 622 for the 2013 year of assessment and the date of the assessment was 30 July 2013. The company's 2014 tax assessment was issued on 15 June 2014 and reflected a taxable income of R1 320 564. The actual calculated taxable income for the 2015 year of assessment was R1 055 877. Aerostar (Pty) Ltd **is a small busi-ness corporation** as defined and the company has a February year-end.

REQUIRED:	MARKS
i Calculate the first provisional tax payment for the 2015 year of assessment and clearly state on which date the payment must be made to SARS. b) Calculate the second provisional tax payment for the 2015 year of assess-ment and clearly state on which date the payment must be made to SARS. **Note: All amounts must be rounded to the nearest Rand.**	8

QUESTION 4 (26 marks, 31 minutes)

XYZ Trust is a resident of the Republic for tax purposes and its year of assessment ends on 28 February 2015. The trust has several investments (that produce interest and dividends), as well as a business that sells electric chainsaws.

Seven electric chainsaws were sold to a timber company (the customer) for R14 000 in total on 2 December 2014. XYZ Trust supplied the customer with a warranty against any mechanical failure of these seven chainsaws. This means that XYZ Trust will replace any faulty chainsaw without charging any costs to the customer. The warranty is applicable for a period of six months from the date of sale.

XYZ Trust originally purchased the chainsaws for R1 500 each from their supplier. The auditors made a warranty provision of R10 500 at year-end (debit: warranty expense, credit: provision).

The accountant calculated the following amounts for the 2015 year of assessment for the trust (you can assume that the calculations are correct):

Taxable income	=	R1 253 000
Qualifying turnover	=	R1 798 000
Taxable turnover	=	R1 120 000

REQUIRED:		**MARKS**
(a)	Explain the difference between direct and indirect taxes. Give an example of a tax that will classify as a direct tax and an indirect tax.	**4**
(b)	Provide two reasons why XYZ Trust will not qualify as a micro business.	**2**
(c)	State when a legal entity will be classified as a resident of the Republic for tax purposes.	**3**
(d)	Shortly discuss what the implication for tax purposes is if a legal entity is a resident of the Republic.	**1**
(e)	State the two types of tests that the courts have established to assist in deciding whether income is of a capital nature or not.	**2**
(f)	Name one of the court cases that are applicable to the “received by, accrued to, or in favour of” requirement of the gross income definition.	**1**
(g)	Discuss whether the warranty expense would be deductible or not by XYZ Trust for the 2015 year of assessment in terms of the general deduction formula section 11(*a*) and section 23 (prohibited deductions) of the Income Tax Act: List the requirements of the general deduction formula and briefly discuss each element at the hand of the given information. Make a brief reference to the relevant case law to strengthen your argument.	**13**

SUGGESTED SOLUTION

QUESTION 1

		R	R	
Taxable income (given)			4 781 142	
Sales			800 000	(1)
Local dividends			150 000	(1)
Dividend exemption			(150 000)	(1)
Interest			355 000	(1)
			5 936 142	
Expenditure				
Trading stock (sec 22)				
- opening stock at cost (lower of cost/MV)			(244 000)	(1)
- closing stock at market value (lower of cost/MV)			420 000	(1)
- purchases			(486 000)	(1)
Dividends paid - no deduction			Nil	(1)
Salaries			(455 000)	(1)
Doubtful debts (sec 11(*j*)) - 2014	78 000 x 25%		19 500	(1)
- 2015	54 000 x 25%		(13 500)	(1)
Restraint of trade (sec 11(*cA*)):				
The **lesser** of:				(1)
R450 000/2 = R225 000				
R450 000/3 = R150 000			(150 000)	(1)
Depreciation - no deduction can be claimed			Nil	
Manufacturing machine (sec 12C) - R350 000 x 40%			(140 000)	(1)
Trucks (sec 11(*e*)) - (R440 000/4) x (2/12)			(18 333)	(3)
Contribution to medical aid scheme (sec 11(*l*))		57 630		
Limited to 10% of approved remuneration		48 000	(48 000)	(2)
Leave pay provision - not actually incurred and prohibited deduction			Nil	(1)
			4 820 809	
Assessed loss brought forward			(274 145)	(1)
Taxable Income			**4 546 664**	
Normal tax liability at 28%			1 273 066	(1)
Provisional tax paid			(976 214)	(1)
Normal tax payable to SARS			**296 852**	
			Marks	**[23]**

QUESTION 2

	R	R	
Accounting profit – (given)		2 676 387	
Repairs to factory building (sec 11(*d*))	(72 000)		(1)
Less: Recovered from insurance (sec 23)	65 000	(7 000)	(1)
Addition to factory building (sec 13) (R250 000 x 5%)		(12 500)	(1)
New steel bending machine (sec 12C) ((R450 000 + R20 000) x 40%)		(188 000)	(2)
Drill machine sold			
Cost	120 000		
Section 12C allowance: 2013 (R120 000 x 20%)	(24 000)		(1)
2014 (R120 000 x 20%)	(24 000)		(1)
2015 (R120 000 x 20%)	(24 000)	(24 000)	(1)
Tax value	48 000		(1)
Proceeds	80 000		
Recoupment (sec 8(4)(*a*))	32 000	32 000	(1)
Delivery truck (sec 11(*e*)) (R185 000/4 x 8/12)		(30 833)	(2)
Laptop computers (sec 11(*e*)) (R15 000/3)		(5 000)	(1)
Damaged vehicle sold			
Cost	90 000		
Wear & tear (sec 11(*e*)): 2015 (R90 000/5 x 7/12)	(10 500)	(10 500)	(1)
Tax value	79 500		
Proceeds	59 500		(1)
Section 11(*o*) scrapping allowance	20 000	(20 000)	(1)
Building allowance (sec 13) (R3 600 000 x 5%)		(180 000)	(1)
Repair of damaged windows (sec 11(*d*))		(61 000)	(1)
Commercial building (sec 13*quin*) (Not new, no allowance)		Nil	(1)
Bad debts (sec 11(*i*))	(18 000)		(1)
Less: Amount recovered	2 000	(16 000)	(1)
Doubtful debt allowance (sec 11(*j*)) – 2014		42 500	(1)
Doubtful debt allowance – 2015 (R212 000 x 25%)		(53 000)	(1)
Telephone and security system rental (sec 11(*a*)) - March 2015		(4 000)	(1)
Sub-total		2 139 054	
Less: Assessed loss from 2014		(181 697)	(1)
Taxable income for 2015		1 957 357	
Income tax (R1 957 357 x 28%)		548 060	(1)

MARKS [26]

QUESTION 3

PART A

Transaction one - Factory A	**R**	**R**	
Tax value			
Cost price		250 000	
Add: Transfer costs		25 000	(1)
		275 000	
Less: Capital allowances (given)		(220 000)	(1)
Tax value on date of sale		55 000	(1)
Recoupment			
Selling price		780 000	(1)
Less: Tax value		(55 000)	(1)
Recoupment		725 000	
Limited to previous allowances		220 000	(1)
Adjusted proceeds			
Proceeds		780 000	
Less: Recoupment		(220 000)	
Adjusted proceeds		560 000	(1)

Calculate valuation date value (VDV)

Total expenditure = R55 000 (tax value)

Adjusted proceeds = R560 000

Paragraph 26 is applicable because proceeds > expenditure			(1)
VDV is the greater of:			(1)
1. Market value as at 1 October 2001		350 000	(1)
2. Time Apportionment base cost (TAB)		98 125	(1)
3. 20% - rule: Adjusted proceeds	560 000		(1)
Less: Expenditure incurred after 1 October 2001	Nil		
	560 000		
R560 000 x 20%		112 000	(1)

Market value is the highest, VDV is therefore R350 000

Base cost = VDV + Cost after 1 Oct 2001 = R350 000 + Rnil = R350 000

Capital gain		
Proceeds (adjusted)	560 000	
Less: Base cost	(350 000)	
	210 000	(1)

QUESTION 3 (continued)

Calculation of taxable capital gain

	R	
Factory A	210 000	
Manufacturing Machine C	50 000	
Aggregate capital gain	260 000	(1)
Less: Assessed capital loss	(64 500)	(1)
Net capital gain	195 500	
Taxable capital gain at an inclusion rate of 66.6%	130 203	(1)

Marks [17]

PART B

		R	
a	1st provisional tax payment (payable on 31 August 2014)		(1)
	Taxable income assessed in 2014 (Basic amount)	1 320 564	(1)
	(2014 assessment is more than 14 days old)		
	Tax on R1 320 564 =		
	(R1 320 564 – R550 000 = R770 564 x 28% = R215 758) + R59 451 *	275 209	(2)
	x 50% for the first payment	137 605	(1)
b	2nd provisional tax payment (payable on 28 February 2015)		
	Lower of: Basic amount (2014 assessment) 1 320 564		
	Actual estimated taxable income 1 055 877		(1)
	Actual estimated taxable income for 2015	1 055 877	(1)
	Tax on R1 055 877 =		
	(R1 055 877 – R550 000 = R505 877 x 28% = R141 646) + R59 451 *	201 097	
	Less: 1st provisional tax payment	(137 605)	(1)
	Amount payable to SARS	63 492	

Marks [8]

* The amount used in the DVD (R59 702) is based on the old 2014 tax table. The amounts used in this tutorial letter are the correct ones. The method and principles remain unchanged.

QUESTION 4

PART A

Difference between direct and indirect tax:

Direct tax: **The same person who earns the income pays the tax** e.g. **income tax, dividends tax and capital gains tax.**	(2)
Indirect tax: The seller bears the impact of the tax while the **consumer pays the tax / This is tax imposed upon a taxable sales transaction** e.g. **VAT**	(2)

PART B

XYZ Trust will not qualify as a micro business:

The **qualifying turnover** for the 2015 year of assessment **exceeds R1 million.**	(1)
A **trust** cannot qualify as a micro business.	(1)

PART C

Legal entity classified as a resident for tax purposes:

A person other than a natural person (in other words a business entity such as a company or a close corporation) is a resident of the Republic if it is: **incorporated, established or formed** in the Republic, **or**	(2)
has its **place of effective management** in the Republic	(1)

PART D

Implication for an entity of being a resident:

Residents are taxed on **worldwide (all)** income.	(1)

PART E

Two types of tests - income is of a capital nature or not:

Subjective tests.	(1)
Objective tests	(1)

QUESTION 4 (continued)

PART F

Court case that is applicable to the “received by, accrued to, or in favour of” requirement:

Geldenhuys v CIR	(1)
CIR v **People's Stores** (Walvis Bay) (Pty) Ltd	(1)
Lategan v CIR	(1)
Name any one	Max (1)

PART G

The requirements of the general deduction formula are:

- **Trade (1)** – **XYZ carries on a trade of selling electric chain saws (1)**
- **Expenditure or loss (1)** – in this case **there could be expenditure of R1 500 (1)** per chain saw that is returned, although **there was no expense at year-end (1)**.
- **Actually incurred (1)** – an expense is only incurred **if a chain saw is returned (1)** and needs to be replaced. The expense is therefore **conditional (1)** and is **not actually incurred (1)**. (***Edgars Stores*** **(1)**)
- **In the year of assessment (1)** – no chain saws were returned on 28 February 2015, therefore **no expense was incurred in the 2015 year of assessment (1)**.
- **In the production of income (1)** – the chain saws are XYZ Trust’s trading stock and the replacement of a stock item relates to earning income from selling chain saws, as it forms part of the sale agreement. It is **closely connected** to (or **is an inevitable concomitant)** **(1)** of the **income producing operations (1)** (***Port Elizabeth Electric Tramway Com-pany Ltd*** **(1)**) and the replacement of a chain saw is thus in the production of income.
- **Not of a capital nature (1)** – The expenditure relates to the Trust’s **trading stock and is not of a capital nature (1)**.

Section 23 prohibits this deduction **(1)**.

Conclusion (1): The expense does not meet all the requirements of the general deduction formula, on the basis that there is no amount actually incurred at year-end, and will not be deducted for income tax purposes.

(**Total 19; Max 13**)

OCTOBER/ NOVEMBER 2014

Question 1

Sfix (pty) Limited	R
Taxable income before the expenses	5 989 747

1) Water tank

Repairs	(20 000)
Wear and tear: New tank (36 000/6)	(6 000)

2) New machine AA

Cost (1/07/13) 600 000

Money costs 15 000

615 000

Sec (12c) 61 500 ×40 %	(240 000)

3) Machine BB (Second hand)

Cost (1/08/12)	250 000		
Wear and tear	(250 000 × 20 %)	(50 000)	
Recoupment			
Proceeds			180 000
Income tax value		(150 000)	
Cost		250 000	
Accumulated W&T		(100 000)	30 000

4) Manufacturing building cc

Cost (1/09/10) 2 500 000

Wear and tear (513) [5% ×2 500 000] (125 000)

5) Building DD

Cost 25 000 5 000 000 × 0.2 = 1 000 000

6) Building EE

Commercial building R1 700 (340 000) 000×0.2

7) Building LL

Cost R130 000×5%	(6 500)
Additional 5%	(6 500)

Sale of low cost

Residential unit 130 000× 10% (3 000)

8) Building XX

Cost 12 000 000× 5% Recoupment (800 000 × 5%)

9) Generator (sec 11c) (600 000)

R30 000~~×5×~~12 (40 000)

(1 500)

9.2) Office furniture

Cost R66 000 1×6	(11 000)
	(11 000)

Scrupling allowance

9.3) Heavy duty truck

Cost 225 000 1×3	=	(75 000)

Toolbox	(2 000)
9.4) Rental of photocopy machine	(42 000)
Tenable income	(3 499 247)
tax there on @ 28%	R 979 789

QUESTION 2

Nick my chick (NmC)	
Sales (2 000 000-25 000)	1 975 000
Local dividend	50 000
Exemption	(50 000)
Lease agreement income	
Leases rental (5 000×12)	60 000
Premium	300 000
Income	2 335 000
Expenses	
Water and electricity	(45 000)
Salaries	(280 000)
Opening inventory	(200 000)
Closing inventory	350 000
Purchases of raw materials	(600 000)
Pimp my chicken pakals	
Purchased	-
Renewal cost	(16 000)
Restraint of trade payment	
330 000÷3 or 330 000÷5	
Whichever is lesser	(66 000)
Bad debts: Trade debtors	(30 000)
: Loan to employee	-
Doubtful debts allowance: Previous year	(28 125)
Provision (126 000× 25%)	(31 500)
Chicken coops destroyed by fire (400 000)	
Insurance payment: Recopment	(380 000)
Donation 28 000	(28 000)

Limited to 10 % of 1 424 625

Tenable income	1 396 625

Tan these as per tan table

-67 111 @ 0%	
67 111- @ 7%	(20 852)
365 001-550 000 @ 21 %	(38 850)
1 396 625-550 000 @ 28%	237 055
Total tan liability	**26 757**

QUESTION 3

Sparkle Unicorns (Pty) Ltd
Capital gain: Factory building –land

Proceeds on disposal	1 500 000
Base cost	(250 000)
Capital gain on land	1 250 000

Building:

Proceeds on disposal	3 500 000
Less amount included in income	(450 000)
	3 050 000
Base cost	(300 000)
Cost	750 000
	(450 000)
Accumulated wear and tear	2 750 000
Capital gain	

Aggregate capital gain on factory

Building: Land	1 250 000
:Building	2 750 000
Capital gain on factory buildin	400 000
Selling costs	(40 000)

Capital gain			3 960 000
Machinery			
Proceeds		480 000	
Less amounts included in income		(380 000)	
Adjusted proceeds		100 000	

Base cost

Higher of		
TAB	398 750	
Wear and tear claimed	(380 000)	
	18 750	
Market value @ 1/10/01	400 000	
Wear and tear claimed	(380 000)	
	20 000	(20 000)
Capital gain		80 000

Aggregate capital gain

Factory building	3 960 000
Machinery	80 000
Total capital gain	4 040 000
Inclusion rate @ 66.6 %	2 690 640

Question 4

Part A

An amount is only deductible for tax purposes if it meets requirements of section 11(a) as read with section 23 (a). The onus is on the tax payer to prove that an amount is deductible.

Eagle owner paid for his visit while the visit was not wholly for business. As was decided in the case of IE Training care, an amount is only deductible if it is a natural commitment of the business. Attending workshops to see the latest designs to map out future designs is part of Mr. Tech's job; so the amount is deductible to the extent that it is incurred for tax purposes. Therefore to the extent that it is not incurred in the production of income, it will not be deductible.

Therefore, cost of R148 625 (185 000-36 375) would not be deductible for tax purposes as it will not laid out for the tax purposes as per sec 23 (a)

Part B a)

- The tax practitioner should file a notice to appeal with the commissioner
- The notice should be filed within 30 business days
- The tax practitioner should file an address that the commissioner can use to file.

b)

- The tax payer can take the matter to the tax board if tax is less R500 000 but as the amount is above the specified amount.
- The tax payer can take the matter to the tax court by filling with the tax court.

Part C)

a) First provisional tax payments

Basic amount as last assessment last done more than 18

months ago 901 389 ×1.08 = 1 051 380

First provisional tax payment R1 051 380 × 28% = 294 386 /2 =147 193

b) Second provisional tax

payment Estimated 1 025	
414× 28 =	287 116
Less profit provisional tax	(147
payment Second provisional tax	193) 139
payment	923

OCT/NOV 2013

QUESTION 1

c) Administrative steps to lodge an appeal to
SARS - To lodge an objection,

i) It must be lodged on the prescribed forms

ii) It must be submitted within the prescribed period of 30 days

iii) It must specify the grounds on which it is being made

iv) It must specify an address on which the tax payer will receive notice on from the commissioner.

v) The appeal must signed by the tax payer.

d) When an objection has been settled SARS has to keep the following in its records

i)Details that should be made known to the tax payer

ii)The settlement agreement in writing

iii)The explanation of how the issue was settled and how it is to be treated in future.

iv)The secrecy provisions that pertain to SARS work

v)The altered assessment that is final unless fraud is involved on the part of the tax payer.

e) Income tax

i) Income tax

ii) Vat

iii) Provisional tax and P.A.Y.E

iv) Estate duty

v) Transfer duty

vi) Exercise duty

Question 2

a) i) Its income should be R20 million or less in any year of assessment ended 31 March 2013

ii) It should not own any shares in other companies that are more than 5% of those companies, whether operating or not.

iii) Its investment income should be 20% or less of its total income

iv) The company may not be a personal service provider

v) The shareholders must be natural persons in any year of assessment under review

b) Tax liability for Fratela Ltd for the year of assessment ended 28 February 2013 (SBC)

	R
Taxable income before latest and capital	385 000
gains Interest received	17 500
Capital gain @ 0.666 × 55 000	36 630
	419 130
Tax there on as per tax tables	
=R21 051 + (419 130 – 350 000)×	40 407
28% Less provisional tax payment	(30250)
made Find tax liability/ tax done	10 157

c) Tax liability for fratulaLtd for the year of assessment ended 28 February 2013 (Micro business company)

		R
Taxable turnover		610000
		27 500
Capital gain 50 % ×55		637500
000 Quality turnover		
Tax there on @ rate		
applicable (0-150 000) @	-	
0%		
(150 000- 300 000) @	1500	
1% (500 000-300 000)	4000	
@ 2 % (637 500 500	5 500	11 000
000) @ 4%		(30250)
Provisional tax payments		(19 250)
made		
Tax refund due		

d) Final tax liability of Fratula Limited for the year of assessment ended 28 February

Question 3

Part A

Brand guru (Pty) Ltd Gross income for the year of assessment ended 31 March 2013

	R
Consultation fees (Included in gross income as it is recurrent and earned In the tax payers income earning activities)	285 000
Company logo (included in gross income as it is recurrent in nature and Earned in the tax payers normal operations	165 000
Business cards (included as it forms tax payers normal operations and income already earned as tax payers entitled	10 000
Lease premium of (450 000) included as specifically included under Special inclusions part of gross income definition	400 000
Lease rent (included as specifically included under specification on the Definition of gross income)	405 000
Sale of building B (Not included as it is capital in nature. Building is a long lived asset and forms part of the income earning structures of the company)	-

Part B

Heavy James Grey Gross income for the rear of Assessment ended 28 February 2013

Divided received from Brand guru (from revenue within the republic)	12 000
Consultation work realized for brand guru (from a source within the republic)	55 000
Interest received from an investment in the republic (from a source within the republic)	36 000
Rent received from apartment in the republic (from a source within the republic)	60 000

Part C

Ziyawa More (Pty) Ltd

Normal tax liability for the year of assessment eneded 31 March 2013

1) Tanzanite tour concert (5 000 000 × 20 %)	1 000 000
Dividends earned	90 000
Interest earned	75 000

Part B

<u>Heavy James Grey Gross income for the rear of Assessment ended 28 February 2013</u>

Divided received from Brand guru (from revenue within the republic) 12 000

Consultation work realized for brand guru (from a source within the republic) 55 000

Interest received from an investment in the republic (from a source within the republic) 36 000

Rent received from apartment in the republic (from a source within the republic) 60 000

Part C

Ziyawa More (Pty) Ltd

Normal tax liability for the year of assessment eneded 31 March 2013

1) Tanzanite tour concert (5 000 000 ×	1 000000
20 %) Dividends earned	90 000
Interest earned	75 000

2)	Riyania concert expenses	(186 000)
	Restraint of trade (100 000/3 0r 100 00 /5)	(20 000)
	Low lost residential unit (does not qualify as cost exceed R30 000)	-
	Loan to employee written off	-
3)	Insurance premium actual incurred for assessment year (165 000 – 120 000)	45 000
	Prepaid (165 000 $\times\frac{8}{11}$) R120 000	
4)	Delivery vehicles $\frac{120\ 000 - 20\ 000}{4}$: Wear and tear	(25 000)
	Accident damaged vehicle $\frac{20\ 000}{4} \times \frac{8}{12}$	(3 334)
	Write off of vehicle (20 000 -5 000-3 334)	(11 666)
	Indemnity insurance receipt	10 000
	Administrative building (Denied)	-
	Painting costs	-
	Music equipment for concerts rented	(28 000)
	Riyania accommodation	(30 000)
	Scented candles	(850)
	Taxable income before section 18 A deductions	825 150
	Donations to public benefit organization (c18 A) limited to 10 % of R82 515 =R82 515 Actual Actual R50 680	(50 680)
	Assessed losses brought forward	774 470
	Assessed taxable income for the year	(386 470)
	Tax there on @ 28%	R108 772

Question 4

Capital gains

Tambotie Limited

Building	R	R
Proceeds	3 500 000	
Base cost	(3 340 000)	
Cost 11/03/05	3 250 000	
Transfer cost incurred	90 000	
Capital gains on building	160 000	

Manufacturing Machine		
Proceeds from insurance	680 00	
Less Amount included in income	(372 000)	
Adjusted proceeds	308 000	
Base cost	(248 000)	
Costs	620 000	
Wear and tear claimed	(372 000	
Capital gains	60 000	

Aggregate capital Gains		
Building	160 000	
Manufacturing machine	60 000	
Aggregate capital gain	220 000	
Assessed loss brought forward	(12 000)	
Capital gains	(20 800)	
Inclusion rate @ 66.6%		138 528

Part B

Grey (Pty) Ltd

Base cost of building

20 % rule = 8 250 000 × 20 % =	1 650 000	
Valuation date value	907 000	
Value	900 000	
Valuation costs	7 000	
Time apportioned base cost	85 600	
Therefore base cost		121 650 000

An amount should be included in gross income if it meets the definition of gross income. The campaign receipt originates from the company's normal income generating activities. The R10 000 exchange of artwork for advertising is from selling artwork which are the operation of dinner fela Pty ltd and are therefore revenue in nature and the amount is clearly identified. The amount has accrued to dineper fela(Pty)on 28 March 2013 as the contract amount is theirs to do as and whatever they desire to do therefore the amount has been accrued on the tax payer on the Golden days case. The amount is clearly identified as was decided in the Butcher brothers case therefore it can be included in gross income as it was received in the current year of assessment as 28 March it falls within the current year of assessment.

1b) An amount will be deductible from the income of the tax payer if it meets the definition of the general deductions formulas 511(a) was read in conjuction with 523. The onus or better off to prove that an amount is deductible falls on the tax payer.

- The cost of the town houses were incurred in the production of income as Dikolodo fela built the house with a view to sell them in the generation of income, therefore the amount will be deductible.
- The loss that Dikolodo fela (pty) Ltd suffered did not arise from its income generating activities as hurricanes are not a natural concomitant of undertaking building operations as was decided in the case of the Port Elizabeth Tramway case on in the Joffe case, therefore the amount of the loss would not be deductible as hurricanes do not satisfy the natural concomitant criteria.
- The loss was suffered in the current year of assessment and therefore meets the year of assessment criteria.
- From the above that the loss was not incurred in the production of income for the originating cause of the loss does not have any relation with the income generating activities of Dikolodo limited the amount will not be deductible for tax purposes as the loss will not be deductible from the evidence on case law. The company may use provisions from trading stock to get the loss deductible.
- Therefore the loss on trading stock might not be deductible using the general formula but deductible under trading stock rules.

Question 2

a) Sunshine private limited
As sunshine limited has a 31March year end the first provisional tax payment will be due in September at the end of the month. 15 September 2012 can be used and R120 000 can be used as the estimate of income
<u>First provisional tax payment</u>
R120 000 ×28% = 336 00/2 = <u>R168 000</u>
Therefore the tax payer, Sunshine Limited should pay as the first provisional tax payment.

<u>Second Provisional tax payment</u>

Estimate of income	R1 784 432 ×28% =	R499 641
Less first provisional tax payment		(R168 000)
Second provisional tax payment		R331 641

b) If the assessment was issued on 15 June 2012 the amount of R1 354 980 could have been used as the provisional taxable amount for the estimate for provisional tax payer.

Question 2b

Mafuba (Pty)Ltd : Procedures to follow when rectifying incorrect 2012 tax assessment.

- To appeal an assessment that does not exceed R500 000 the company may do so using the alternative dispute resolution or the tax board if the Mafuba chooses this.
- To appeal, Mafuba should file a notice to appeal within 30days of receipt of the assessment from SARS.
- The appeal should be signed by representatives of Mafuba (Pty)Ltd.
- The appeal should be delivered to the commissioner at the address specified: the assessment for the purpose of tax.
- The appeal should specify an address which the commissioner can deliver his decision to the tax payer.

Question 3

Lazy age CC (small business corporation)

Taxable income for the year of assessment ended 28 February 2013

Sales (450 000 +5 025 000)	5 475 000
Closing inventory	<u>330 000</u>
	5 802 000
Opening inventory	(290 000)
Purchases	(3 587 150)
Doubtful debts: Previous year	12 500
: Current year (93 000× 25%)	23 450
Bad debts written off	(119 000)
Personnel costs: Salaries and wages	(650 000)
: Contributions to pension fund (limited to 10%of approved)	
Remuneration = 0.1×650 000= R65 000 Actual R125 850	(65 000)
Loss of income lawsuit settlement (in the production of income)	(1 000 000)
Legal cost: Any Khumalo case (sec 11 (c)	(6 000)
: Jenny Levin (not in the production of income)	-
Advertising costs : vacant posts	(3 750)
: erecting a bill board (capital 50% W&tT allowable)	(12 925)
Cosmetic manufacturing machine	(300 000)
Delivery vehicles (85 000 ×20%)	(17 000)
Manufacturing building (section 13(1) R 1 250 000) × 0.05)	(62 500)
Recoupment: old manufacturing machine	20 000
Trademarks: renewal	(8 500)
New trademark purchased	-
New trademark purchased	-
Restraint of trade payment (312 000/3 or 312 000/4) the lesser	<u>(78 000)</u>
Assessed loss	(385 775)
Section 18A deduction	-
Assessed loss	<u>388 775</u>

Question 4

Notes cc

Income tax liability for the year of assessment ended 31March 2013

Taxable income before adjustment	5 800 000
1) Vehicles : Wear & tear (completely written off)	
2) Building cc R 1 200 000 × 20 %	(240 000)
3) Small item assets (R4 500 ×2)	(9 000)
4) Manufacturing machine ATM : R300 000 ×20% (sec 12c)	(6 000)
5) Manufacturing machine LL R450 000×40%	(180 000)
6) Manufacturing building: wear and tear (900 000× 5%)	(450 000)
Recoupment (800 000 × 5%)	(40 000)
7) Repair costs	(220 000)
Extension cost (30 000×$\frac{1}{5}$)	(60 000)
8) Furniture sold: wear and tear (30 000 ×$\frac{1}{6}$)	(5 000)
: scapping allowance (10 000-(30 000-5 000×1.5)	(12 500)
9) Manufacturing machine PP: recoupment (290 000 – 290 000×$\frac{5}{5}$	(290 000)

Capital gains proceeds	310 000	
Base cost		
Cost	290 000	
Accumulated w&t	(290 000)	
Capital gain	310 000	
0.666×310 000		206 460
Taxable income		5 099 960
Tax expense @ 28%		R1 427 989

Question 5
Frozen lemons CC

Proceeds		390 000
Less amount taken into account in determination of income		(480 000)
Adjusted proceeds		842 000
Base cost: higher of		
20% rule	130 000	
Base cost rule 890 000×20%	178 000	
Less wear and tear accumulated	(48 000)	
Valuation date value	44 500	
Valuation	88 000	
Valuation costs	4 500	
Less accumulated wear and tear	(48 000)	
Or time apportioned base cost	42 000	
Time apportioned base cost	90 000	
Less accumulated wear and tear claimed	(48 000)	130 000
Capital gain		712 000
Assessed loss brought forward		30 000
Taxable capital gain		682 000
Inclusion rate at 66.6%		454 212

MAY/JUNE 2014

Question 1

Rashupi Trailers (Pty)Ltd

Normal tax liability for the year of assessment ended 31March 2014

	R
Taxable income before adjustments	4 781 142
Sales	800 000
Closing inventory	420 000
	1 220 000
Opening inventory	(244 000)
Purchases	(486 000)
Dividend paid to share holders	-
Learnership agreement: yearly allowance	(50 000)
:Completion allowance	(50 000)
Salaries	(455 000)
Doubtful debts(54 000× 25%): current year	(13 500)
:previous year (78 000×25%)	19 500
Restraint of trade (450 000/2 or 450 000/3) whichever is lower	(150 000)
Wear and tear: new and unused machines (R350 000 ×40%)=	(140 000)
:Trucks 440 000 already written off	-

:Trucks 440 000 already written off	-
Medical aid contribution R57 630 limited to 10% of approved Remuneration = R 48 000 (480 000 ×10%) Actual	(48 000)
Assessed loss brought forward	(274 145)
Taxable income	4 157 997
Tax expense @ 28%	1 164 239
Less first provisional tax payment	(976 214)
Normal tax liability	188 025