Tutorial letter 202/2/2014

Taxation of Individuals

TAX3702

Semester 2

Taxation Department

Solution: Compulsory Assignment 1

Bar code

Dear Student

Enclosed are the solutions to Assignment 1/2/2014. Please work through the solutions alongside the assignment and your answers. This is a significant part of the learning process. Note that it is very important to understand why a specific answer is correct while other options are not.

You should identify any problem areas early in the semester and make every effort to understand all aspects of the work that you have studied.

We hope that you have found the assignments stimulating.

Kind regards

LECTURERS: TAX3702

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ASSIGNMENT 1 – SECOND SEMESTER

SUGGESTED SOLUTIONS

<u>ASSIGNMENT 1</u> (70 marks, 84 minutes)

1. 1 - Normal tax is calculated per the tax tables, without deducting rebates.

2. 4 - Net normal tax is calculated as follows: normal tax is calculated per the tax tables and then reduced by rebates and tax credits to equal net normal tax. Prepaid taxes are not taken into account when determining net normal tax.

3. 1 - Net normal tax is calculated as follows: normal tax is calculated per the tax tables and then reduced by rebates and tax credits to equal net normal tax. The taxpayer had no dependants, therefore his medical scheme fees tax credit amounted to R2 904 (R242 x 12).

4. 4 - Normal tax is calculated per the tax tables and it must only be reduced by rebates and tax credits to equal net normal tax, it is not reduced by prepaid taxes. Where a person dies during the year of assessment, the primary, secondary and tertiary rebates are apportioned from the beginning of the year of assessment up to the date of death.

5. 4 - Gifts and fixed property are capital in nature and are not included in gross income. (33,3% of the capital gain will be included in taxable income – refer to the income tax framework.) Exempt income is not excluded from gross income.

6. 2 - Gross income less exempt income = income. Local interest is partially exempt and alimony receipts are fully exempt. They were therefore deducted in order to determine 'income'.

7. 1 - Gross income less exempt income = income. Income less allowable deductions (plus any taxable capital gain) = taxable income. There were no allowable deductions in this question but there was a 'taxable capital gain' that had to be included in the determination of 'taxable income'.

8. 2 - The person was in SA more than 91 days during the 2014 year of assessment, <u>and</u> more than 91 days in SA during each of the preceding 5 years of assessment (2009 to 2013) <u>and</u> more than 915 days in SA in total during the preceding 5 years of assessment (2009 to 2013).

9. 2 - A: capital receipts excluded; B: receipts other than cash are included in gross income; C: amounts received in the form of annuities are specially included in gross income; D: amount 'accrued', therefore included.

10. 3

11. 4 Inheritances are capital receipts and are excluded from gross income. The other amounts are either revenue in nature or are capital receipts that are specially included in gross income.

12. 2 - The deemed fixed cost is based on the VAT inclusive cost of the vehicle. It must also be apportioned for the period that the travel allowance was received.

13. 3 - The finance charge amount was for the full year of assessment. It therefore had to be apportioned for the period that the travel allowance was received. Capital repayments cannot be included in the determination of actual cost p/km. Wear and tear, calculated over a 7-year period, is included in the determination of actual cost p/km but must be apportioned for the period that the travel allowance was received.

14. 5 The determined value includes VAT. Two completed periods of 12 months lapsed from the date of purchase to the date Albert received the use of the vehicle.

15. 2 - As the vehicle is subject to a maintenance plan, 3.25% **per month** is used. Albert had the use from 1 April 2013 to 28 February 2014, which is 11 months.

16. 3 - The cash equivalent may be reduced by the private kilometres travelled multiplied by the fuel rate per km, as read from the deemed travel expense table, in relation to the vehicle's determined value.

17. 4 - The accommodation is furnished and the employer pays electricity costs, therefore C = 19%. The formula is also apportioned for the 3-month period that the employee received the benefit.

18. 5 - Right of use of an asset: private use is negligible therefore there is no taxable benefit.

19. 3 - The employee received a <u>subsidy</u> in respect of the loan from the financial institution. Therefore, the benefit is based on the difference between the interest rate paid by the employee and the interest charged by the financial institution.

20. 1 - The employee received a <u>low interest</u> loan from his employer. Therefore the benefit is based on the difference between the interest rate paid by the employee and the official rate of interest.

21. 3 - Foreign interest received by South African residents is fully taxable. All the other options are fully exempt.

22. 2 - Foreign interest is fully taxable and local dividends are fully exempt. The foreign dividends have a ratio exemption of 25/40 of the gross foreign dividend. Local interest is exempt up to the amount of R23 800 (for taxpayers < 65 years).

23. 3 - Investment income is split equally between spouses married in community of property. A salary does not constitute investment income.

24. 4 - General deduction formula: there must be an unconditional obligation to pay the expense in order to meet the "actually incurred" requirement. A payment subject to a resolutive condition does not meet that requirement. See *Edgars Stores Ltd v CIR*. All the other statements are correct.

25. 2 - General deduction formula: an expense does not have to be "necessarily incurred" in order to be deductible. All the other statements are correct.

26. 3 - The pension fund contribution deduction is limited to 7.5% of the retirement funding income. The limit for past period pension fund contributions is a separate calculation.

27. 1 - A maximum of R1 800 per year is allowed as a deduction in respect of past period pension fund contributions. Past period pension fund contributions that were disallowed in previous years, may be carried forward to the current year of assessment and taken into account.

28. 5 - The RAF deduction is limited to 15% of non-retirement funding income. The salary of R200 000 constitutes retirement funding income. In order to determine non-retirement funding income, the current pension fund and past period deductions need to be added back.

29. 3 - The donation deduction is limited to 10% of taxable income (the subtotal before the deduction).

30. 1 - The amount paid by the employer for the year of assessment constitutes the fringe benefit.

31. 4 - The first two dependants qualify for a R242 medical scheme fees tax credit each and thereafter each dependant qualifies for a R162 medical scheme fees tax credit.

32. 3 - The amount paid by the employer and employee for the year of assessment, must be reduced by 4 x the medical scheme fees tax credit. This amount, if positive, is added to the other qualifying medical expenses. If this total exceeds 7.5% of the taxable income before the medical deduction, the excess is deductible.

33. 1 - Family member with a disability: the amount paid by the employer and employee for the year of assessment, must be reduced by 4 x the medical scheme fees tax credit. This amount, if positive, is added to the other qualifying medical expenses. That amount constitutes the medical expense deduction for a taxpayer (<65) with a disability, or with a disabled family member.

34. 4 - Where RAF contributions or donations or medical expenses have been deducted from income in order to determine taxable income, these deductions must be apportioned between SA-sourced income and foreign income.

The proportion of the deduction that relates to foreign income is deducted from foreign income. That total will constitute the amount of foreign taxable income that can be taken into account for purposes of calculating the section 6*quat* rebate. Refer to question 5.3 on pages 191 to 194 in the textbook.

35. 2 - The formula is:

$$\frac{\text{Taxable income from all foreign sources}}{\text{Taxable income from all sources}} \times \text{Normal tax payable on taxable income from all sources}$$