Fundamentals Level – Skills Module

Taxation (South Africa)

Monday 6 June 2011

Time allowed
Reading and planning: 15 minutes
Writing: 3 hours

ALL FIVE questions are compulsory and MUST be attempted.
Tax rates and allowances are on pages 2–3.

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

Paper F6 (ZAF)

ACCA

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest R.
2. All apportionments should be made to the nearest month.
3. All workings should be shown.

TAX RATES AND ALLOWANCES

The following tax rates and allowances are to be used in answering the questions.

Year ending 28 February 2011/31 March 2011

Rebates	
Primary rebate	R10,260
Secondary rebate (over 65)	R5,675
Interest exemption	
Under 65	R22,300
Over 65	R32,000
Medical contribution rates	
Single member	R670
Member plus one dependant	R1,340
Each additional dependant	R410
Companies	
Normal tax rate	28%
STC rate	10%
Official rate of interest (assumed)	12%

Rates of normal tax payable by persons (other than companies)
in respect of the year of assessment ended 28 February 2011

Where the taxable income	
Does not exceed R140,000	18% of each R1 of the taxable income
exceeds R140,000 but does not exceed R221,000	R25,200 plus 25% of the amount over R140,000
exceeds R221,000 but does not exceed R305,000	R45,450 plus 30% of the amount over R221,000
exceeds R305,000 but does not exceed R431,000	R70,650 plus 35% of the amount over R305,000
exceeds R431,000 but does not exceed R552,000	R114,750 plus 38% of the amount over R431,000
exceeds R552,000	R160,730 plus 40% of the amount over R552,000

Tax rates for small business corporations
for the year of assessment ended 31 March 2011

R0 – R57,000	Nil
R57,001 – R300,000	10% of the amount over R57,000
R300,001 and above	R24,300 plus 28% of the amount over R300,000

Car allowance

Maximum vehicle cost for actual expenses	R400,000

Fringe benefit (company car)

Benefit percentage	2·5%
Reduction for all private fuel paid	0·22%
Reduction for all maintenance paid	0·18%

Subsistence allowances

Deemed expenditure for meals and incidental costs (per Government regulation) R276 per day
Deemed expenditure for incidental costs only (per Government regultion) R85 per day

Capital gains tax

Annual exclusion	R17,500
Primary residence exclusion	R1,500,000

(where proceeds are R2 million or less, the full gain is excluded for the portion of the property used for domestic purposes as a primary residence)

Inclusion rate (natural persons)	25%
Inclusion rate (non-natural persons)	50%

Time apportioned base cost formula: $Y = B + \left[\frac{(P - B) \times N}{(T + N)}\right]$

Travel allowance table

for years of assessment commencing on or after 1 March 2008

Value of the vehicle (including VAT but excluding finance charges or interest)	Fixed cost	Fuel cost	Maintenance cost
R	R p.a.	c/km	c/km
0 – 40,000	14,672	58·6	21·7
40,001 – 80,000	29,106	58·6	21·7
80,001 – 120,000	39,928	62·5	24·2
120,001 – 160,000	50,749	68·6	28·0
160,001 – 200,000	63,424	68·8	41·1
200,001 – 240,000	76,041	81·5	46·4
240,001 – 280,000	86,211	81·5	46·4
280,001 – 320,000	96,260	85·7	49·4
320,001 – 360,000	106,367	94·6	56·2
360,001 – 400,000	116,012	110·3	75·2
Exceeds 400,000	116,012	110·3	75·2

Notes:
Where reimbursement is based on actual business kilometres travelled and no other compensation is paid to such employees and the kilometres travelled for business does not exceed 8,000, the prescribed rate is R2·92 per kilometre.

Rating formulae

$$R = \left[\frac{F}{B + D - (C + L + G)}\right]$$

$$Y = \left[\frac{A}{B + D - (C + L)}\right] \times (B - L) + (L \times R)$$

ALL FIVE questions are compulsory and MUST be attempted

1 Mrs Mokomele, aged 45, works as a salaried manager at a packing company (We-Pack Ltd). In addition to her employment at the packing plant, Mrs Mokomele also earns income from various investments and rents various properties. The details of her employment package, rental trade and investment income for the year of assessment ended 28 February 2011 are supplied below.

(1) Employment package

Mrs Mokomele has an employment package, comprising the following for the year ended 28 February 2011:

- Annual cash salary of R400,000
- Monthly travel allowance of R5,000 (Note i)
- Employer paid medical contributions of R2,500 per month (Note ii)
- Clothing allowance for business suits of R500 per month (Note iii)
- Bursary for Mrs Mokomele's son of R9,000 per year (Note iv)
- Subsistence amounts (Note v)
- Contribution to pension fund by Mrs Mokomele – 10% of cash salary

Mrs Mokomele also contributes R4,000 per month to a Retirement Annuity Fund (RAF), which her employer (We-Pack Ltd) takes into account in determining her employees tax.

Notes:

(i) Mrs Mokomele kept a travel logbook. She travelled a total of 26,000 kilometres for the year, of which only 5,000 related to business travel. Mrs Mokomele did not record any of her expenses. Her motor car cost R384,000 (including VAT) in June 2007.

(ii) We-Pack Ltd pays all of the medical contributions of its employees in full.

(iii) We-Pack Ltd requires all managers to dress smartly in business suits. Mrs Mokomele asked for a monthly clothing allowance to purchase her business suits. She buys all her business suits from retail clothing stores.

(iv) When Mrs Mokomele's son began studying at university, she asked We-Pack Ltd to give her son a bursary to cover some of the tuition fees. The bursary was granted in terms of a bursary scheme available to all children of managers at We-Pack Ltd.

(v) Mrs Mokomele has to occasionally visit other packing plants in South Africa. For the days that she is away, she is paid a subsistence allowance of R300 per day for meals and incidental costs. The accommodation is charged directly to We-Pack Ltd. She does not need to account to her employer as to how she spent the allowance and does not keep any records of the amounts spent. In May 2010, Mrs Mokomele received an advance subsistence payment of R1,800 for an eight-day business trip in June 2010. The trip was ultimately cancelled, but We-Pack Ltd did not require Mrs Mokomele to repay the amount. All her other trips took place and (apart from the amount in May 2010) she received a further R7,500 (being for 25 days) in subsistence allowances.

(2) Investment income

Mrs Mokomele had received a large inheritance from her late uncle in 2000. She invested most of the money into shares, interest-bearing investments and collective investment schemes.

Income from the investments for the year ended 28 February 2011 comprises the following:

Income type	Amount
South African dividends	R35,000
South African interest	R80,000
Distribution from a collective investment scheme (CIS) – within 12 months of receipt by the CIS	
South African dividends	R10,000
South African interest	R40,000
Distribution from a collective investment scheme (CIS) – 15 months after receipt by the CIS (all South African interest)	R30,000

Mrs Mokomele also sold some of her shares for R550,000. The base cost amounted to R165,000.

(3) Rental trade

Some of the inheritance Mrs Mokomele received was used to purchase a property (Property A) on 1 October 2001 for rental purposes. Mrs Mokomele rents this property out as holiday accommodation. Some years generate profits and other years losses depending on the demand for holiday accommodation.

Mrs Mokomele also purchased a flat (Property B) on 1 March 2004 near the university her son, Bongi, attends. Bongi and two of his friends live in the flat. They each pay a nominal rental (currently R500 per month) to Mrs Mokomele. This rental does not cover the expenses related to this flat.

Mrs Mokomele achieved a trading profit of R5,000 for Property A and a trading loss of R8,000 for Property B for the year ended 28 February 2011.

The Commissioner ring-fenced the losses on Property B since the year ended 28 February 2005. For each of the preceding years of assessment (i.e. before 1 March 2010), Mrs Mokomele was taxed at the maximum marginal rate. There is an assessed loss brought forward for Property B of R13,000.

NOTE: Mrs Mokomele made no provisional tax payments during the year.

Required:

(a) Calculate the employees tax withheld by Mrs Mokomele's employer (We-Pack Ltd) for the year of assessment ended 28 February 2011. (10 marks)

(b) List the dates by which the provisional tax returns for Mrs Mokomele's year ended 28 February 2011 were due. (2 marks)

(c) Calculate Mrs Mokomele's final income tax liability for the year of assessment ended 28 February 2011, and state any amounts carried forward. (18 marks)

(30 marks)

2 Tea Co Holdings Ltd is the JSE listed holding company of Test Co (Pty) Ltd ('Test') and Blend Co (Pty) Ltd ('Blend'). Both Test and Blend are involved in processes of manufacture. Test Co tests, clears and packs tea whereas Blend mixes and blends tea. Test and Blend are both value added tax (VAT) vendors whereas Tea Co Ltd is not. All the companies have financial years ending in March each year.

The following transactions took place in Blend Co (Pty) Ltd for the year of assessment ended 31 March 2011:

(i) One of Blend's tea leaf drying machines (Machine A) broke down on 5 April 2010. As Machine A was beyond repair, it was withdrawn from use and sold for R40,000 to a scrap metal merchant on 10 April 2010. The machine had originally been acquired (new) on 1 June 2007 for R500,000.

(ii) Blend purchased a tea leaf drying machine (Machine B) from Test for R250,000 on 15 October 2010. The machine had a market value of R175,000 on 15 October 2010. Test had originally purchased this machine for R400,000 (second-hand) from an unconnected person on 17 May 2008.

(iii) Blend needed to expand its operations and needed to move its tea bag stitching machine to new premises. To this end, Blend entered into a ten-year lease with Test for a plot of vacant land. In terms of the lease, a building to house machinery had to be built to a cost of at least R1,500,000. The lease rental payments are R50,000 per month. The lease commenced on 1 April 2010 and the building was completed and brought into use at a total cost of R2,000,000 on 2 August 2010. The lease terms are all arm's length.

The stitching machine (Machine D), which had been built and brought into use on 10 November 2009 at a total cost of R630,000, was moved at a cost of R37,500 to the new building on 2 August 2010.

(iv) The stitching machine is a patented design. The patent was renewed at a cost of R3,000.

(v) On 10 September 2010, the employee operating the stitching machine lost a finger when it was caught by the needles sewing the tea bags. The company paid a lump sum compensation amount of R80,000.

(vi) Blend had a warehouse for the tea stocks that it had purchased on 24 January 2003 for R800,000. As the business was expanding and the stock volumes on hand increasing, the warehouse was sold on 20 July 2010 for R1,200,000. A new warehouse was acquired from a property developer for R2,300,000 and brought into use on 20 July 2010.

Tea Co Holding Ltd essentially holds shares in its operating companies and acts as financier for the group. As a result, its only income streams are dividends from the shareholdings and interest from loans made.

For its year of assessment ended 31 March 2011, Tea Co Holdings Ltd earned R100,000 from dividends and R540,000 from interest. Audit fees incurred have amounted to R40,000. The audit involves not only the work for Tea Co Holdings Ltd but also for the consolidated financial statements.

Required:

(a) Based on the information above, provide ONE reason why Blend Co (Pty) Ltd cannot be a small business corporation. (1 mark)

(b) Calculate the income tax effects for Blend Co (Pty) Ltd for each of the transactions (i) to (vi) above for its year of assessment ended 31 March 2011. You should provide brief reasons to support each of your calculations. (17 marks)

(c) Discuss the deductibility of the audit fees for Tea Co Holdings Ltd for the year ended 31 March 2011. (7 marks)

(25 marks)

3 Mrs Mpotulo (aged 65) emigrated to Australia on 30 June 2010 for her retirement. Each of Mrs Mpotulo's children previously emigrated to Australia after graduating from university (the last leaving on 1 February 2001).

Mrs Mpotulo was aware that capital gains tax arose on emigration. She is seeking quantification of her capital gains tax inclusion for the year ending 28 February 2011. She has an assessed capital loss brought forward from the year ended 28 February 2010 of R100,000.

Her assets include the following:

1. A holiday home in Hermanus (Western Cape). This home had been purchased by her late husband on 23 August 1998 at a cost of R320,000 (including transfer duty and legal fees). The holiday house was not valued on 1 October 2001. In 2002, he had paid for an extension to be built at a cost of R250,000. He died on 29 December 2007 and left the house to Mrs Mpotulo when its value was R2,700,000.

   This holiday house had a value of R3,400,000 on 30 June 2010.

   Mrs Mpotulo decided to sell the house on 1 November 2010, achieving a sales price of R3,750,000. Selling costs of R187,500 were incurred.

2. Her furniture and fittings were to be shipped to Australia. The total market value on 30 June 2010 was R1,600,000 and the purchase prices totalled R1,500,000 (all acquired after 1 October 2001). She sold some furniture for the equivalent of R300,000 (with an original base cost of R250,000) on 1 August 2010.

3. Mrs Mpotulo owns a motor car with a value of R400,000, which had originally cost R750,000.

4. Kruger rands (coins made mainly from gold) were sold on 1 May 2010 for R57,000, which had originally cost R23,000. These were sold to pay for her airline ticket to Australia.

Required:

(a) Identify, giving brief reasons, the date of disposal for each asset in (1) to (4) above for the purposes of determining the taxable capital gain of Mrs Mpotulo for the year ended 28 February 2011. (4 marks)

(b) Compute the taxable capital gain for Mrs Mpotulo for the year ended 28 February 2011. For each asset, calculate the capital gain or capital loss before applying any exclusions. (16 marks)

(20 marks)

4 Dr Daniels runs a medical practice from a house in a residential suburb. His patient billings are approaching R1 million. He has not yet registered for value added tax (VAT) and has a number of questions for you to answer.

Questions regarding VAT:

(1) If Dr Daniels' billings (turnover) exceeds R1 million for a 12-month period, by when must he apply to register for VAT?

(2) If his patient billings are around R900,000 but he sells the furniture in his office for R150,000 in order to buy new furniture for R200,000, must he register for VAT?

(3) If he registers for VAT, what must appear on the patient invoice (billing)? Note: Consider only full VAT invoices.

(4) If he registers for VAT, what is the effect for VAT purposes if a patient does not pay the invoice?

In addition to the above, Dr Daniels downloaded a number of electronic books onto his iPad device (an electronic device for reading electronic books) on 15 May 2011. On the same day, he paid a total of United States $300 for these electronic books. For all tax purposes, this foreign currency transaction is translated to R2,310. The website company does not issue any invoices for the purchases. Dr Daniels purchased these books for recreational use only and not for use in his medical practice.

Required:

(a) Answer the questions (1) to (4) above raised by Dr Daniels, providing reasons with your answers. (9 marks)

(b) Explain the correct value added tax (VAT) treatment of purchase of the electronic books, including reference to time of supply. Support your answer with calculations. (6 marks)

(15 marks)

5 Max Green (aged 34) works as a draftsman for a firm of architects. His monthly salary, before taxes, from the firm of architects is R12,000. He receives no additional benefits from his employer. The employer has withheld employees tax of R15,940.

In addition to his employment (above), Max started his own home business (a sole proprietorship) on 1 October 2009. The business involves the collecting and sorting of recycling for residential homes. The new business began trading on 15 April 2010, earning income from that date. Before the commencement of trading, Max incurred pre-trade expenditure of R20,000. The turnover for the new business is expected to be R450,000 for the year ending 28 February 2011. Max also expects to incur revenue expenditure (all qualifying for deduction) of R200,000.

Max inherited some money in 2002 and earned interest of R30,000 for the year ended 28 February 2011 on the deposit balance.

Max made provisional tax payments amounting to R25,000 for the year ended 28 February 2011.

Required:

(a) Provide TWO reasons why Max should not register as a value-added tax (VAT) vendor. (2 marks)

(b) Explain when in the year ended 28 February 2011 Max Green became a provisional taxpayer and within what timeframe he needs to apply for registration. (2 marks)

(c) Calculate Max's total income tax liability and amount payable for the year ended 28 February 2011. (6 marks)

(10 marks)

End of Question Paper