Fundamentals Level – Skills Module

Taxation (South Africa)

Tuesday 12 June 2012

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 2–4.

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 29 February 2012/31 March 2012

Rebates	
Primary rebate	R10,755
Secondary rebate (over 65)	R6,012
Tertiary rebate (over 75)	R2,000
Interest exemption	
Under 65	R22,800
Over 65	R33,000
Of which the first R3,700 may be used for foreign dividends or foreign interest	
Medical contribution rates	
Single member	R720
Member plus one dependant	R1,440
Each additional dependant	R440
Companies	
Normal tax rate	28%
STC rate	10%
Official rate of interest (assumed)	8%

Rates of normal tax payable by persons (other than companies)
In respect of the year of assessment ended 29 February 2012

Where the taxable income	
Does not exceed R150,000	18% of each R1 of the taxable income
exceeds R150,000 but does not exceed R235,000	R27,000 plus 25% of the amount over R150,000
exceeds R235,000 but does not exceed R325,000	R48,250 plus 30% of the amount over R235,000
exceeds R325,000 but does not exceed R455,000	R75,250 plus 35% of the amount over R325,000
exceeds R455,000 but does not exceed R580,000	R120,750 plus 38% of the amount over R455,000
exceeds R580,000	R168,250 plus 40% of the amount over R580,000

Tax rates for small business corporations
for the year of assessment ended 31 March 2012

R0 – R59,750	Nil
R59,751 – R300,000	10% of the amount over R59,750
R300,001 and above	R24,025 plus 28% of the amount over R300,000

Car allowance

Maximum vehicle cost for actual expenses	R480,000

Fringe benefit (company car)

Benefit percentage (where no maintenance plan exists)	3·5%
Benefit percentage (where maintenance plan exists)	3·25%

General business reduction: Benefit value x business kms/total kms (as per logbook)
Private fuel reduction: Private fuel (R) x private kms/total kms (as per logbook)
Private maintenance reduction: Private maintenance (R) x private kms/total kms (as per logbook)

Subsistence allowances

Deemed expenditure for meals and incidental costs (per Government regulation) R286 per day (local travel)
Deemed expenditure for incidental costs only (per Government regulation) R88 per day (local travel)
Deemed expenditure for meals and incidental costs (foreign travel) – per published tables therefore supplied in the question where relevant

Common capital allowances

New and unused manufacturing plant and equipment	40%/20%/20%/20%
Used or leased manufacturing plant and equipment	20% each year for 5 tax years
Small business corporation manufacturing plant and equipment	100%
Small business corporation (other assets) – unless wear & tear provides a greater deduction	50%/30%/20%

Wear & tear (based on Interpretation Note 47 and supplied in the question)

Manufacturing building allowance (unless seller's rate supplied)	5%
New or unused commercial building (not manufacturing building)	5%

– No deduction where another section of the Act applies to the building
– Where part of a building is acquired, 55% of the acquisition price is 'cost'
– Where an improvement to the building is acquired, 30% of the acquisition price of the improvement is 'cost'

Research and development 'revenue nature' expenditure	150%
Research and development 'capital nature' expenditure	50%/30%/20%

Capital gains tax

Annual exclusion (while alive)	R20,000
Annual exclusion (in year of death)	R200,000
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 2011

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 – 60,000	19,492	64·6	26·4
60,001 – 120,000	38,726	68·0	29·2
120,001 – 180,000	52,594	71·3	31·9
180,001 – 240,000	66,440	77·7	35·0
240,001 – 300,000	79,185	87·0	44·7
300,001 – 360,000	91,873	93·9	54·2
360,001 – 420,000	105,809	100·9	65·8
420,001 – 480,000	119,683	113·1	67·6
Exceeds 480,000	119,683	113·1	67·6

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 R3·05 per kilometre.

Rating formulae

$$Y = \left[\frac{A}{B + D - C} \right]$$

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Question 1 begins on page 6.

ALL FIVE questions are compulsory and MUST be attempted

1 (a) Ms Farzanah Suliaman (aged 47) was employed as a sales representative for a pharmaceutical company ('the company') on 1 June 2011. Her employment package comprises the following:

(i) A cash salary of R4,000 per month.

(ii) Commission earned, being:

R6,000 in June;
R15,000 in July;
R2,000 in August;
R13,000 in September;
R16,000 in October;
R14,000 in November;
R4,000 in December;
R9,000 in January and
R20,000 in February.

(iii) By having the highest sales in February, Ms Suliaman was awarded a holiday trip for two people to Mauritius by the company to be taken in March 2012. The total value of the award is R40,000.

(iv) All sales representatives of the company receive an entertainment allowance of R2,000 per month. The representatives are not required to account to the company for the amounts spent. Ms Suliaman spent R8,000 of the allowance buying rugby season tickets for a large client.

(v) Medical aid contributions are paid half by the company and half by the employee. The total medical contributions to the medical aid for Ms Suliaman (i.e. the company and her own contributions combined) amounted to R3,300 per month. Ms Suliaman's mother is a listed dependant on her medical aid. Prior to her employment, Ms Suliaman had been a member of the same medical aid and funded the entire contribution of R3,300 per month herself.

(vi) Ms Suliaman's mother suffered a stroke during the year. As Ms Suliaman's medical aid did not cover all the costs and Ms Suliaman did not have the necessary cash resources, the company loaned her R100,000 interest free on 1 October 2011 in order to settle all medical costs. The full R100,000 was required to settle the medical costs, none of which was recoverable from the medical aid. No capital repayments have been made by 29 February 2012.

(vii) Ms Suliaman has the use of a new company car. The car was purchased for R199,000 (including value-added taxation (VAT)) in May 2011 and given to Ms Suliaman for her use on 1 June 2011. The new car has a standard maintenance plan. Ms Suliaman maintains a logbook in terms of the use of the car which reflects total kilometres travelled of 30,000 of which 23,000 relate to business travel for the period 1 June 2011 to 29 February 2012. The company pays for all additional maintenance and business fuel. Ms Suliaman has to pay for all private fuel, which amounted to R8,500 for the period 1 June 2011 to 29 February 2012.

(viii) As part of her retirement plan, Ms Suliaman contributes 8% of her cash salary to the company provident fund. In addition, she contributes a further 10% of her cash salary to a retirement annuity fund (which her employer does not take into account for employees tax purposes). She became a member of both funds on 1 June 2011.

(ix) Ms Suliaman had inherited an investment portfolio in 2009 in terms of her father's will. She is a provisional taxpayer and provisional tax of R1,000 had been paid up to 29 February 2012. The investment income earned was:

R25,000 South African interest;
R14,000 foreign interest;
R7,000 foreign dividends and
R9,000 South African dividends.

The investments are in individual companies rather than in collective investment schemes.

(x) Ms Suliaman makes a donation of R2,000 per year to St Luke's Hospice. The Hospice issues the appropriate donation certificate for this donation.

(xi) Employees tax of R28,334 was withheld by the company.

Required:

Calculate the normal tax liability for Ms Suliaman for the year of assessment ended 29 February 2012, indicating clearly any items of income which are exempt or amounts which are not deductible by the use of a zero. (24 marks)

(b) Assume that instead of being awarded the company car in item (vii) in part (a) above, Ms Suliaman had bought the car personally for R199,000 on 1 June 2011 and had received a travel allowance of R3,000 per month. The same logbook information would apply and the same costs would be paid by the company.

Required:

Calculate the taxable inclusion for Ms Suliaman as a result of the receipt of the travel allowance for the year of assessment ended 29 February 2012. You should indicate whether Ms Suliaman should elect to base the calculations on actual or deemed costs. (6 marks)

(30 marks)

2 Ice Cube (Pty) Ltd ('the company') is a closely held company owned by two brothers, Rowan and Harrison Frigid. The company is resident for South African tax purposes, with a financial and tax year end of 31 March 2012.

The company has two operating divisions. Division A produces and sells freshwater pre-packed ice for sale to retail outlets. Division B manufactures ice-making machinery for fishing vessels. The ice-making machinery from Division B produces ice from surrounding seawater resulting in a cost effective solution for smaller fishing operations. Both divisions are considered to run processes of manufacture for tax purposes.

Division B runs its operations in Durban whereas Division A is housed in Cape Town. As a result, the divisions run separate accounting systems, which are consolidated at year end to produce the annual financial statements of the company.

The following selected transactions took place between 1 April 2011 and 31 March 2012. All amounts are stated exclusive of VAT where appropriate:

(i) A new administration building was acquired on 15 June 2009 for R13 million. As part of the original acquisition plan, 20% of the building space is used to house the on-going research and development (R&D) activities.

(ii) The freshwater ice manufacturing building for Division A had become too small for the expanding operations and was sold for R10 million. The building had originally cost R6 million on 30 April 2002. A replacement building had been purchased for R20 million. The company elects any provision to minimise immediate tax effects.

(iii) One of the machines used for the R&D activities had to be replaced. Machine T had originally cost R450,000 on 20 February 2011 and was sold for R495,000 on 1 November 2011. The replacement machine (Machine Z) was acquired for R500,000 on 15 December 2011 and brought into use in the R&D activities on 1 February 2012.

(iv) The pipeline (considered part of the machinery for tax purposes) for pumping river water into the ice-making machines of Division A was ripped out by a flood on 24 June 2011. The machines and pipeline had been fully written off for tax purposes. No capital gain or capital loss arose from this pipeline being destroyed.

A replacement pipeline was ordered and installed by 25 July 2011 at a cost of R200,000. Cosmetic repairs had to be made to the machines to facilitate the attachment of the new pipeline, which cost R40,000. It was found, during the installation of the new pipeline that the previous pipeline had not been properly secured. New securing pins were acquired and installed at an additional cost of R50,000. The new securing pins are of a better design than the old ones. The company's insurance policy paid out R150,000 for the pipeline, but did not pay out anything for the cosmetic repairs or the new securing pins.

(v) The company pays a royalty for the patent pertaining to the production of the saltwater ice-making machinery for fishing vessels. The patent is owned by an unconnected non-resident company. The annual royalty fee paid on 1 March 2011 was R4 million. On 1 March 2012, the next annual royalty payment was made and amounted to R4,250,000.

(vi) The salaries and wages expensed to the income statement amounted to R30 million. SARS considers the 'approved remuneration' to amount to R25 million. Of the R30 million expensed, R6 million relates to contributions made by the company to employee's pension and medical funds.

Required:

(a) Discuss whether or not Division A and Division B may be separately registered for value-added taxation (VAT) purposes and what requirements, if any, must be met for any such registration. (5 mark)

(b) Assuming that Division A and Division B have NOT been separately registered for VAT, calculate the income tax effects for Ice Cube (Pty) Ltd for each of the transactions (i) to (vi) above for its year of assessment ended 31 March 2012. You should provide brief explanations to support each of your calculations. (20 marks)

(25 marks)

3 Big Entertainment Ltd is a company providing entertainment services. It is in financial distress and the directors have decided to dispose of some of the company assets to improve the cash flow. Despite the financial distress, the company does not have an assessed loss, but does have an assessed capital loss of R400,000. The company is a value-added tax (VAT) vendor and has a February year end. All values below include VAT, where appropriate.

The company wishes to dispose of the following assets:

1. A yacht, used for entertaining important clients. The yacht did not qualify for any capital allowances and originally cost R12,000,000 (considered an arm's length price) when acquired second hand from a non-vendor on 1 October 2000. The yacht is 24 metres long. The market value of the yacht on 1 October 2001 was R11,500,000. The company would sell the yacht for its current market value of R7,000,000. (8 marks)
2. A plot of vacant land which had been purchased on 1 April 2009 for R3 million from a non-vendor. The transfer duty of R240,000 had been paid from cash resources at the time. The company had planned to build a large night club on the land but could not get the zoning permission. The market value of the land is currently R2,800,000 and, being zoned for residential use only, would be purchased by a non-vendor. The selling costs will amount to R160,000 for commission and legal fees paid to VAT vendors. (4 marks)
3. The company also operated a partnership with The Party Company (Pty) Ltd. The partnership owned music equipment for use at live functions. Big Entertainment Ltd can apply its 60% voting rights in the partnership (which matches the profit & loss sharing percentage) to force the sale of the music equipment. The equipment was originally acquired at a cost of R570,000 on 1 October 1999. Its market value on 1 October 2001 was R870,000 and the current market value is R960,000. This equipment has been fully written off for tax purposes. (8 marks)

Required:

For each of the above assets, assuming the disposals take place at market value on 29 February 2012:

Calculate the capital gain or capital loss arising on the disposal, providing explanations in support of your answer and indicate whether or not any provision will prevent the aggregation of the capital gain or capital loss.

Note: The mark allocation is provided against the assets above for guidance.

(20 marks)

4 Rowan Evans and Harrison Charles are two recently graduated engineering students. They would like to start their own engineering consulting business and are considering registering a closely-held company (in terms of the Companies Act of 2008).

They have supplied the following information:

– The company will have a February year end.
– The company will initially have only one major client. However, this client's business will lead to further clients in about three years' time.
– Rowan and Harrison will hold the equity shares in the company equally.
– The company will employ an additional two staff members and a receptionist. The receptionist will initially work part-time.
– The company will make an annual donation to a charity of the employees' choice of R20,000.
– Rowan and Harrison will each draw a salary, but also receive dividends from the company (declared annually).
– All the consulting work will be performed at the company's own premises.

Required:

(a) (i) In respect of each type of tax for which the company will be liable to account, state the dates by which returns or declarations must be made and the dates on which payments should be made. (10 marks)

(ii) State the penalties if the returns in part (i) are submitted late, and/or payments are made late. (3 marks)

(b) State when the company must register for value-added tax (VAT). (2 marks)

(15 marks)

5 Baby Group Ltd, a JSE listed company, has two operating subsidiaries, namely: Teddy (Pty) Ltd and Tot Furn (Pty) Ltd. Teddy (Pty) Ltd manufactures teddy bears for sale in retail stores and Tot Furn (Pty) Ltd manufactures high-end baby nursery furniture. Tot Furn (Pty) Ltd also operates a crèche for babies and toddlers. This is an exempt supply and represents 15% of turnover, which the Commissioner has accepted as the correct apportionment between the making of exempt and taxable supplies. All the companies in the group have a March year end. Baby Group Ltd is the only company of the group that is not a value-added tax (VAT) vendor.

As the manufacture of teddy bears is a niche market, Baby Group Ltd would like to sell the business of Teddy (Pty) Ltd to Tot Furn (Pty) Ltd. However, the directors are concerned about the VAT consequences of such a sale.

The balance sheet of Teddy (Pty) Ltd shows the following assets:

	Original cost (including VAT)	**Sales Price (including VAT)**	**Market value**
Land and buildings	4,000,000	3,500,000	4,500,000
Furniture and equipment	570,000	450,000	700,000
Computer equipment	120,000	100,000	90,000
Motor vehicles	300,000	300,000	220,000
Trading stock	1,140,000	1,140,000	2,000,000

(i) The land and buildings, motor vehicles and trading stock would be sold to Tot Furn (Pty) Ltd for taxable supply use only.

(ii) The computer equipment would be sold to Tot Furn (Pty) Ltd. The computer equipment would host the invoicing software for invoicing the crèche services and sale of baby furniture.

(iii) The furniture and equipment would be sold to Baby Group Ltd for use in the Head Office.

Required:

(a) Explain whether or not the disposal of the business is a taxable supply for value-added tax (VAT) purposes and whether or not Teddy (Pty) Ltd must issue a tax invoice. (3 marks)

(b) List the requirements for the disposal of the business to be the disposal of a going concern at the zero rate. (3 marks)

(c) Calculate, for Teddy (Pty) Ltd, the output VAT for the disposal of each asset in notes (i) to (iii), assuming the business is not sold as a going concern. Support your calculations with explanations. (4 marks)

(10 marks)

End of Question Paper