

Examiner's report

F6 Taxation (RUS)

December 2014

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General Comments

The examination consisted of five compulsory questions. Question 1 was for 30 marks and question 2 was for 20 marks. There were three further questions of 15 marks each.

The vast majority of candidates attempted all five questions, and there was little evidence of time pressure. Where questions were left unanswered by candidates, this appeared to be due to a lack of technical knowledge or poor exam technique and also due to a failure to read the question requirements carefully as opposed to time pressure.

Both Q1 and Q2 were generally well answered with some credit-worthy answers. Question 3 (especially parts (a) and (c)) appeared to cause the most challenges for candidates, although there were still some satisfactory answers presented by well-prepared candidates who had the requisite technical knowledge on the VAT issues for self-constructed premises.

Part (a) (i) of question 4 was answered well by the majority of candidates. However, part (a) (ii) was not answered as satisfactorily and often the information in the scenario was disregarded.

In part (b) (i) of question 4 candidates performed well when doing the social insurance contributions calculations whereas answers to part (b) (ii) of this question could have been improved if candidates read the question requirements carefully.

Question 5 was answered well by many candidates especially part (a). For part (b), answers could have been improved if more attention had been paid to the scenario given.

In general, candidates performed well on questions 1, 2, 4 (b) (i) and 5 (a). However, it should be noted that some candidates provided highly satisfactory answers to all of the questions presented.

Workings were generally shown although these were sometimes difficult to follow.

Candidates are reminded that each question should be started on a new page with a clear indication of the question number which is being attempted by the candidate. Furthermore, candidates must give more thought to the layout and organisation of their answers. Some candidates tried to show the answers to different parts of a question simultaneously on a page. Such an approach is not recommended.

Overall performance showed that the majority of candidates managed to attempt all questions, and did not have a problem with the time pressure during this exam. In addition, the majority of candidates answered most of the questions using the correct methodological approach which made it easier for them to gain marks.

Overall, the performance of candidates was fairly satisfactory.

Specific Comments

Question One

This 30-mark question tested candidates' ability to cope with the various aspects of core subjects of both profits tax and VAT, taking into account the difference between the direct and indirect expenses for a production company. This included allocation of expenses related to the direct part, such as social insurance contributions, depreciation of production equipment, as well as the correct calculation of indirect expenses such as amortisation

of a trademark, limited voluntary medical insurance, voluntary personal insurance for employees, business entertainment expenses, interest expense, utilization of tax losses, tax losses to be carried forward and the VAT applicable.

Overall, the question was well answered with many strong answers presented. Candidates demonstrated a good appreciation of the practical aspects of the scenario described in the question, especially in the calculation of direct expenses related to raw materials, packaging materials, direct non-linear depreciation of production equipment, as well indirect expenses such as voluntary medical and personal insurance, social insurance contributions, business entertainment expenses and interest expenses.

However, the performance of some candidates could have been improved by more careful attention to the scenario.

Some common errors noted in candidates' scripts included the following:

Part (a)

- Failure to apply the allocation factor to direct expenses
- Application of the incorrect number of months to the formula for non-linear depreciation
- Failure to apply the 30% write-off applicable to the production equipment
- Failure to net off the VAT for the production equipment and coolers
- Allocation of 30% for social insurance contributions to 8 months and 10% to 4 months respectively
- Inclusion of social insurance contributions in the limit to determine the deductible voluntary medical insurance
- Failure to net off the VAT for business entertainment costs
- Incorrect inclusion of the City Guide into deductible business entertainment costs
- Failure to limit the interest expense deduction
- Incorrect utilization of losses or calculation of 20% tax ignoring the utilization of tax losses
- Failure to calculate the tax losses to be carried forward to the future year as required in the question.

Part (b)

- Application of the incorrect VAT rate to raw materials
- Incorrect calculation of VAT on the insurance payments (exempt)
- Failure to apply the reduced VAT rate to prepayments
- Application of VAT to the entire business entertainment expenses rather than just the deductible part

Notwithstanding the above errors, the overall performance in this question was very satisfactory.

Question Two

This 25-mark question covered the topics of taxable and deductible items for personal income tax, including application of different deductions.

The most common mistakes encountered in candidates' scripts were:

In part (a)

- The social deduction at source in relation to the pension contributions was often ignored in the calculation of Vladimir's taxable base
- Material aid in kind of reimbursement of medicines was often either ignored or shown as fully exempt for Vladimir
- Emotional intelligence training was often incorrectly shown as taxable (with no explanation)
- Housing allowance was often not attributed based on the relevant proportion mentioned in the scenario
- Corporate loan interest related to the housing allowance was often calculated with the incorrect number of days, incorrect rate and wrong allocation
- The imputed interest income on the corporate loan was frequently calculated ignoring the data in scenario in respect of the housing allowance

In part (b)

- Income from insurance agreement was often not recognized correctly
- The educational deduction for Vladimir's sister was often ignored or the full 52,000 RR was wrongly deducted
- Some candidates showed both the housing allowance and corporate loan interest in the final settlement of PIT liability for Vladimir

In part (c)

- The children allowance calculation was often based on the incorrect number of months
- Some candidates deducted both Olga's actual expenses **and** a professional deduction
- Some candidates calculated Olga's tax at 13% rather than utilising the housing allowance for Olga
- Many candidates forgot to show the amount of Olga's housing allowance to be carried forward to future years
- Some candidates did not include the prize deduction for income subject to 35% tax

Notwithstanding the above common errors, overall performance on this question was satisfactory.

Question Three

Question 3 examined VAT issues in respect to VAT tax base for construction works conducted by a company's own workforce and the impact on VAT in the case that the constructed premises were used in the future for either (i) VAT non-taxable transactions only or (ii) both taxable and non-taxable transactions

Part (a) was arguably the most straightforward part of the question. Nevertheless many candidates were unable to state the recognition date to define the VAT taxable base in the circumstances.

Part (b) required a calculation of the VAT liability for constructed premises for both Quarter 1 and Quarter 2 based on the scenario given. The typical mistakes encountered were as follows:

- Forgetting to net off the VAT for materials when calculating the output VAT on the premises
- Forgetting the claw-back in Quarter 2 of the input VAT on the prepayments made in Quarter 1
- Failing to calculate the input VAT on investment in non-current assets in the relevant quarter



Part (c) consisted of two subparts, which required candidates to explain the VAT impact if the constructed premises were either used (i) for VAT non-taxable transactions only or (ii) for both taxable and non-taxable transactions.

Generally, answers to part (c) were unsatisfactory due to a lack of technical knowledge on this area.

Question Four

Part (a) of this question focused on the different security insurance contributions (SIC) payable depending on the type of agreement concluded with an individual.

In subpart (i) well prepared candidates clearly identified the different approaches and gave their opinion in terms of the most beneficial option, as required by the question.

The most commonly made error here was applying an incorrect rate of SIC.

In subpart (ii), candidates' performance was less satisfactory.

One of the most common mistakes made here was applying an incorrect rate of SIC or decreasing/increasing remuneration by the actual expenses reimbursed.

Answers to part (b) (i) were more satisfactory and many candidates presented comprehensive answers.

The typical mistakes made are listed below:

- Failing to gross up the bonus for the year
- Including the reimbursement of business trip expenses into the taxable base
- Reducing the taxable base by reimbursement of the interest paid
- Excluding the canteen tickets from the taxable base
- Excluding the voluntary medical insurance for Anastacia's husband from the taxable base
- Treating material aid as exempt or, alternatively, forgetting the material aid deduction

Subpart (ii) of this question reviewed the criteria for reimbursement of mortgage interest by an employer to be exempt for personal income tax (PIT). Answers here tended to be slightly too vague.

Nevertheless the overall performance on this question was satisfactory.

Question Five

Question 5 consisted of 2 parts and reviewed the application of the thin capitalization rules.

Part (a) of the question focused on the thin capitalization rules and the deductible interest, deemed dividend and relevant withholding tax in respect of a loan.

The majority of candidates managed to correctly calculate the company's net assets position and revalue the loan in order to calculate the capitalisation ratio and deductible interest and thus performed well in this part of the question.

However, it is worth noting the following common mistakes:

- Some candidates calculated the deductible interest using the actual interest rate



- Some candidates calculated the deemed dividend without taking into account the total interest and limitation on the deductible interest for corporate profits tax.

Part (b) of the question reviewed candidates' understanding of how the capitalisation ratio, deductible interest and deemed dividend would change if the loan was provided by a Russian company owned by a foreign company. The only common mistake was use of the incorrect rate for withholding tax on dividends.

It should be noted here that some candidates omitted to answer this part of the question entirely. Where candidates attempted this part, answers were generally satisfactory.