

Strategic Level Exam -June 2024

Corporate Taxation – Target Paper 02

Prepared by:- Prabath Weerasinghe BB Mgt (HRM) SP, ACA, MAAT, ACMA, ATII, MBA Taxation
– PIM USJP

SECTION 1

Question 01

(a) Maxima Co.,Ltd (MaCo) incorporated and a resident company in Vietnam. Company engaged in the business of manufacturing, installation, and service of aluminum structures. Company has been offered a contract to install aluminum structures at a Housing scheme constructed by Sky Residence Jawaththa (Pvt) Ltd (SRJ) a company incorporated in Sri Lanka. Total cost estimated by MaCo is for the service of the installation was Rs. 250,000,000/- (USD equivalent LKR value) and this includes total installation cost. Estimated cost of the building project was Rs. 800,000,000/-. MaCo has manufactured aluminum building (Prefabricated building structure) at their plant in Vietnam and imported to (prefabricated building structures) Sri Lanka. Separate agreement was entered by SRJ with MaCo for the purchases of prefabricated aluminum structures and total price quoted for the aluminum structures was Rs. 350,000,000/- (USD equivalent LKR value).

MaCo has entered into an agreement with Tong Fu (Pvt) Ltd (Ton Fu), a resident company incorporated in Vietnam and engaged in the business of supply of installation services. Tong Fu provided Three (3) machines which are specially use in the building installation projects. Cost of the machines were Rs. 100,000,000/-. Tonh Fu Company purchased the machineries for this project. As per the terms and conditions, a fee for machines is to be paid based on the number of hours used. Therefore, MaCo has entered into an agreement with Tong Fu for the use of machineries. Those are machinery specially used for this type of project and total service fee agreed was Rs. 175,000,000/- (USD equivalent LKR value). Tong Fu has sent their expert employees who can operate those machineries. Salaries for the employees are paid by the Tong Fu. Total salary and other cost incurred by Tong Fu

for the project was Rs. 60,000,000/- and Rs. 45,000,000/- respectively (USD equivalent LKR value). The employees stayed at the building site and their activities were completed within a period of 45 days.

MaCo has started the project on 01st July 2023 and completed the project within a period of 182 days. After the completion of the project, the building was duly handed over to SRJ.

Required:

- i. Discuss whether MaCo is required to pay income tax in Sri Lanka for Y/A 2023/24 and if required compute the income tax liability of MaCo in Sri Lanka for Y/A 2023/24.

Support your answer citing statutory provisions of the Inland Revenue Act No. 24 of 2017, as amended (IRA) and the double tax agreement between Sri Lanka and Vietnam.

Your answer should include an analysis of the following.

- Permanent establishment exposure of MaCo in Sri Lanka
- Whether the full contract value that includes income from the following is liable to tax in Sri Lanka
 1. Supply of prefabricated building
 2. Rendering installation services

(10 marks)

- ii. Assess the requirement for the deduction of withhold tax when remitting the payment in relation to installation services to Tong Fu in Vietnam.

Support your answer citing statutory provisions of the IRA and any relief that may be invoked pursuant to the DTA with Sri Lanka and Vietnam.

(5 marks)

(b) Mr. Saigon, employee to Tong Fu received a salary of Rs. 30,000,000/- (USD equivalent LKR value) during the employment period in Sri Lanka and has made an investment of Rs. 10,000,000/- in the Commercial Bank (Ceylon) PLC a listed company in the Colombo stock exchange. In the month of December 2023, Commercial Bank (Ceylon) PLC has distributed a dividend (Gross) of Rs. 5,000,000/- for this investment. He has sold all shares for Rs. 15,000,000/-.

(c) Further SRJ has obtained a software for the control of electricity used by the housing scheme form Elector Vietnam Ltd (EV) a company incorporated in Vietnam. This is a fully owned subsidiary company of Ireland company.. As per the contract, annual license fee of Rs. 25,000,000/- to be paid for the software.

Mr. Saigon and Mr. Diagon, the managing director to EV approach you for tax consultation. They are seeking your advice on the Income tax and other tax liability in Sri Lanka on the transaction entered by them, during the year 2023/24.

Required:

- i. Advise whether Mr. Saigon is required to pay income tax in Sri Lanka for Y/A 2023/24 and if required compute the income tax liability of Mr. Saigon in Sri Lanka for Y/A 2023/24.

(5 marks)

- ii. Advise Mr. Diagon the requirement for the payment of income tax in Sri Lanka including the requirement of deduction of withhold tax when remitting the payment in relation to installation services to Elector Vietnam Ltd (EV).

Support your answer citing statutory provisions of the IRA and any relief that may be invoked pursuant to the DTA.

(5 marks)

Question 02

(a) Bio Tech Laboratory (Pvt) Ltd (BTL) is engaged in the business of providing laboratory services for fabric and garment testing services to local clients. Income received from laboratory service represents more than 70% of the total turnover of the company. BTL is registered as a Registered Identified Purchaser (RIP) as well as a Registered Identified Supplier (RIS) under the Simplified value-added tax (SVAT) scheme.

The management of BTL has started diploma course for merchandisers and quality assurance for personnel in garment industries during the Y/A 2023/24. The following information was identified with respect to value-added tax (VAT) for the taxable period ended, December 2023.

Description	Rs.
Turnover	
• Laboratory testing services to exporters – Registered for SVAT as RIP	50,000,000/-
• Laboratory testing services to local manufacture of Garments – registered for VAT.	10,000,000/-
• Quality assurance diploma course fee to local candidates	3,000,000/-
• Quality assurance diploma course fee to foreign candidates	7,000,000/-
VAT paid on importation and local purchases.	1,000,000/-
• Imports of testing materials – VAT deferment scheme	800,000/-
• Imports of machinery used for testing service – VAT deferment scheme.	500,000/-
• Imports of equipment and accessories used for quality assurance diploma courses.	200,000/-
• Purchases of other materials for diploma courses – SVAT suppliers	150,000/-
• Building rent – Lab	100,000/-
• Building rent – Diploma course	
• Expenditure incurred by administration office	700,000/-

Following additional information provided by the company for the above taxable period.

- The diploma course is recognized by the ministry of education and the university grant commission as high national diploma.
- Foreign candidates joined for the course virtually and examination or evaluation process also made vis internet.
- Course fees to be paid at the beginning of the course.
- Company has collected all the SVAT credit vouchers.
- Company has sold scrap packing material to a local party and collected Rs. 345,000/- during the above period.

Required:

- i. Assess the VAT liability/overpayment for the taxable period ended 31.12.2023.

(15 marks)

- (b) As per the company policy Bio Tech Laboratory (Pvt) Ltd (BTL) is providing company vehicles for its employees at top management. Depreciation policy of the company is five years for these vehicles. After the expiration of a five (5) year period employee is entitled to get the ownership of the motor vehicle used by them at the net book value. Tax authority has requested information from the company and their argument is profit earned by the company shall be treated for capital gain tax. Management seeks your advice on the possible tax exposure on the above scheme.

Required:

- i. Advise the management on the applicable taxes for the company on the above scheme.

(10 marks)

SECTION 2

Question 03 (based on the common pre-seen)

Question 03

In addition to the information provided in the common pre-seen in relation to Quick Eats IT (Pvt) Ltd, the following additional information in relation to the company for the year ended 31 March 2024 is made available.

(i) The detailed for unaudited income statement of Quick Eats IT for the year ended 31 March 2024 is as follows.

Description	Note	Amount (LKR) 'Mn
Revenue	01	3,000
Cost of sales	02	(1,800)
Gross profit		1,200
Other Income	03	50
Administration, Distribution, and other expenses	04	(304)
Profit from operating activities		946
Finance Income	05	100
Finance cost	06	(918)
Profit before tax		128
Income Tax expenses		60
Profit for the year		188

Note: - 01 - Revenue

During the year company has recorded Rs. 1,000,000,000/- from the Software development services made to foreign clients. They are using this software for delivery services. This sale was done on 05th May 2023. During the year Rs. 250,000,000/- was remitted to Company's Bank account in USD and Rs. 250,000,000/- was received is Euro. Balance amount as at 31.03.2024 was Rs. 500,000,000/- and it was received in GBP in the month of April 2024.

Note: - 02 - Cost of sales

Payments to development team and related direct cost are included.

Note: 03: - Other Income

a) Renting and hiring computer equipment Rs. 50,000,000/-.

Note 04: - Extract of some of the expenses recorded under administrative, distribution and other expenses.

Description	Note	(Rs.) 'Mn
Salaries and wages		35.0
EPF & ETF	(i)	5.25
Provision for retirement benefits	(ii)	27.5
Provision for Bad and doubtful debts	(iii)	30.0
Other expenses	(iv)	20.0
Staff welfare and uniforms	(v)	10.0
Machine Repair expenses	(vi)	30.0
Advertising and promotion	(vii)	2.5
Marketing expenses	(viii)	6.2
Donation	(ix)	5.0
Depreciation and impairment		48.8
Fines and penalties	(x)	4.0
Legal and professional fees	(xi)	1.5
Training cost	(xii)	7.3
Amortization	(xiii)	70

i.

- i. EPF 12% and ETF 3% has been made for all staff these funds are approved funds for tax purposes.
- ii. Gratuity provision represent the provision for retirement benefit. During the year Gratuity payment of Rs. 20,000,000/- was made for staff members who got terminated their employment during the year.
- iii. Amount represents the bad debt provision made for trade debtors.
- iv. This represented related expenses made for Software development to foreign clients
- v. Staff welfare expenditure shows uniforms, tea and water provided to office staff.
- vi. Computer and peripherals charges was Rs. 15,000,000/- and which is included in the repair cost. Balance amount is for improvement cost made to power supply system for computers, and this system was purchased in the year 2017.
- vii. Advertising and promotion expenses are related to payment of Rs. 2,500,000/- made to local advertising firm
- viii. Marketing expenses is for the promotion campaign made at foreign market.
- ix. Donation represented the cash donated to government school. This is an approved donation.
- x. Tax authority has issued an assessment for the year 2019/20. Company lodged an administrative review. Tax authority and the company came for an agreement. Fine and penalties are related to the Income tax and penalties paid at the settlement.
- xi. Legal fee of Rs. 500,000/- was made to tax consultant for the settlement of above tax matter. The Lawyer has accepted cash payment only. Rs. 700,000/- has been made in

the month of January for consultation obtained from a lawyer for the preparation of agreement entered with foreign clients. As this payment to foreign consultants, Company has not deducted WHT from this payment. Balance amount represented fee payment to freelance software development services made by a consultant in Sri Lanka. No WHT has been deducted.

- xii. Training cost of Rs. 7,300,000/- has been paid for training program conducted for staff during the month of January 2024. This was paid to training institute which is a company established in Sri Lanka. No withholding tax has been deducted from the fee payment.
- xiii. Total cost represented amortization of software .

Note 5:- Finance income

- b) Interest Income – RFC Rs. 70,000,000/- (USD equivalent value)
 c) Exchange gain – Transaction Gain Rs. 15,000,000/-. Translation gain Rs. 15,00,000/-

Note 6:- Finance costs

Interest on loan obtained and used for the business is Rs. 908,000,000/- (Loan obtained and balance as of 31.03.2024 is Rs. 3000Mn)

Overdraft interest Rs. 10,000,000/-

Note 7:- Property, plant and equipment acquired during the year is as follows:

Description	Cost Rs. '000
Land	75,000
Building	150,000
Computer	30,000
Motor vehicles – Cars – executive	20,000
Computer equipment	5,000
Computer software – ERP with 5-year warranty period	40,000

Capital allowance have been fully claimed for all other assets remaining as at 01.04.2023

Note 8:- Bank overdraft was Rs. 100,000,000/-, has been used for the business.

Note 9:- Tax loss brought forwarded from the year 2022/23 is Rs. 25,000,000/-

Unless otherwise stated all the expenses are incurred to produce income. You may assume that expenses are incurred propionate to generate the respective business income.

Required:

Assess the balance income tax payable, by Quick Etas IT (Pvt) Ltd (Quick Eats IT) in respect of the Y/A 2023/24.

(30 marks)

- b) Board of directors of in in the evaluation process of a proposal made by a foreign client. Accordingly, development of software services can be done for few clients at their country and expertise knowledge shall be shared by the Quick Etas IT (Pvt) Ltd All the accommodation and logistic arrangement is made by the client including supply of required equipment. Profit will be shared between the two party equally.

Required:

Advice the possible tax implication to the Quick Etas IT (Pvt) Ltd (Quick Etas IT) in respect of the above business arrangement.

(05 marks)

- c) Rs.20 million worth of Computer equipment was damaged due to a bad weather during the year of assessments 2024/25 and Rs. 8 million were recovered through the insurance claim. Balance amount of Rs. 12 million will be charged as an expense by the company for income tax purposes.

Required:

Advice the possible tax implication to the Quick Eats IT (Pvt) Ltd (Quick Etas IT) by explaining the stock loss which was not recovered through the insurance You may refers to the provision of tax law and legal precedents.

(05 marks)

- d) As per the provision of Colombo Port City Act, company can enjoy a tax exemption. Board member has informed the opportunities available for the company to the audit committee. Company is evaluating the setting up a business at the Colombo Port City. Audit Committee chairman seeks your advice on the possible tax benefits and risk exposure on the proposal.

Required:

Advice the possible tax implication to the Quick Etas IT (Pvt) Ltd (Quick Eats IT) in respect of the said Law.

(05 marks)

Strategic Level Exam -June 2024

Corporate Taxation – Question Bank VAT

Prepared by:- Prabath Weerasinghe BB Mgt (HRM) SP, ACA, MAAT, ACMA, ATII, MBA Taxation
– PIM USJP

Sudu Araliya Finance Ltd (SAF) is providing financial facility for ventures represented Small and Medium Sector in Sri Lanka. In addition to this company is providing business consultation services. Company stated the business in the month of January 2023.

Following information is extracted from the monthly financials statements provided for the month of December 2023.

Turnover – Interest Rs. 500,000,000/-

Business consultation service Rs. 50,000,000/-

Profit before tax Rs. 250,000,000/-

This has been worked out after deducting all the information including the following.

Depreciation Rs. 10,000,000/-. Staff salary Cost Rs. 5,000,000/- . EPF and ETF expenses Rs. Rs.750,000/-. Gratuity payment Rs. 1,250,000/-. VATFS and SSCL FS of Rs. 15,000,000/- and 2,500,000/-.

Following assets have been purchased in the month of January 2023.

Building Rs. 50Mn, Motor Cars for executive staff Rs. 15Mn. Computer and equipment Rs. 8Mn.

Required:

Assess the VAT and SSCL liability for the taxable period ended 31.12.2023.

(You may assume that no input VAT credit available for the month)

(15 marks)