JMC vLearning
"your virtual learning partner"

Income Sources

Chartered Accountancy
Strategic Level
Corporate Taxation (TAX)

Dinusha Rajapaksha
ACA, CTA, Attorney at Law, LL.B Hons.

JMC ජයසේකර කළමනාකරණ මධ්‍යස්ථානය
JAYASEKERA MANAGEMENT CENTRE (PVT) LTD
Estd. 1972

JMC Jayasekera Management Centre (Pvt) Ltd
Pioneers in Professional Education
65/2A, Chittampalam Gardiner Mawatha, Colombo 02 | T: +94 112 430451 | E: info@jmc.lk | F: +94 115 377917

2. INCOME SOURCES

According to section 4 of the IRA, the assessable income of a person for any year of assessment in case of a resident person is such person's income from employment, business, investment or other source for that year, wherever the source arises. Accordingly, the assessable income of a resident company will be the income it earns from business, investment or other source. The taxable income is arrived at after deducting the qualifying payments from the assessable income.

Business Income	xxx
Investment Income	xxx
Other Income	xxx
ASSESSABLE INCOME	**xxx**
Less: Qualifying payments	xxx
TAXABLE INCOME	**xxx**
INCOME TAX LIABILITY	
Taxable income x 14%/24%	xxx
Less : Tax credits	xxx
Balance tax payable/refund claimed	xxx

Concept of Dominancy over the sources of income

The IRA has introduced the concept of dominancy over the sources of income. This means by definition, "employment" is dominant over "business" and "business" is dominant over "investment".

2.1. Business Income or Investment Income

The IRA requires that before determining a taxpayer's taxable income, the type of income earned must be characterized. This involves determining whether a person is engaged in sufficient activity to constitute a "business". Two key distinctions to be made are (1) whether the person is just passively holding assets such that they have an "investment" rather than a "business" or (2) whether the taxpayer is merely engaged in a hobby, which is an activity without a source.

In determining whether an amount is from an investment or business, the connection with each type of activity should be first identified. Therefore, if an amount is derived in the context of a business, it is treated as business income irrespective of whether such returns are specified as "investment income" in section 7. Section 6(2)(g) also emphasize that investment type returns that are "effectively connected" with a business are treated as business income.

Business or Investment

1. Silk Road (Pvt) Ltd a resident company in Sri Lanka is engaged in the business of manufacturing Silk fabric and its office and factory are located in Horana. Silk Road (Pvt) Ltd, acquires an office building and the land for Rs. 50 Mn in Kottawa. The company does not use this building in Kottawa for any of its business activities of manufacturing Silk fabric, but merely rents this building to outsiders. The company has no other rent income from any other buildings.

   Assess whether the Rent income from the Building in Kottawa would constitute "business" or "investment" income for income tax purpose.

2. Toots (Pvt) Ltd is engaged in the business of running a chain of super markets. They identify that their supermarket in Piliyandala is having increased sales. However, there have been several complaints from customers that they do not have sufficient parking. Therefore Toots (Pvt) Ltd has acquired the land and building adjoining the Piliyandala supermarket for Rs. 25 million. The land is now used as a car park for customers coming to the super market. The building was occupied by a Firm of Chartered Accountants which continues to pay rent to Toots (Pvt) Ltd.

   Assess whether the Rent income from the building would constitute "business" or "investment" income for Toots (Pvt) Ltd.

2.2. Computing Business Income

Business has been defined in section 195 as follows;

"business"-

(a) includes-

  (i) a trade, profession, vocation or isolated arrangement with a business character however short the duration of the arrangement; and

  (ii) a past, present or prospective business;

  but

(b) excludes an employment;"

As the "business" definition includes "trade", "profession" and "vocation" we need to clearly understand what these terms constitute.

Trade

No particular factor is determinative in itself as to whether an activity is a business or not. In some circumstances, the existence of one single badge is enough to show trading. In other cases, a combination of the badges of trade need to be looked into. Identifying whether a person is engaged in a trade involves the weighing of the factors that typically indicate such activity to determine whether on a balance the person is conducting a trade:

1. **What is Sold.** If product sold produces no income of itself and cannot be used personally, this points to a trade. So, for example, the purchase of commercial quantities of a product that cannot be used personally would suggest a trade or at least an isolated transaction of a business character.
2. **Length of Ownership.** Trades often make money through buying and selling assets. Investment involves the holding of assets. Therefore, if an asset is held for a short period of time, this suggests a trade rather than an investment.
3. **Repetition.** Repetition of transactions suggests a trade.
4. **Supplementary Work.** Trades often process assets to turn them into saleable products.
5. **Motivation for Activity.** Trades acquire assets or conclude contracts with the intention of making a profit. Trades do not acquire assets or engage in arrangements for personal reasons such as family support, education, housing etc.
6. **Motivation for Sale.** Trades typically sell assets for the same reason they acquire them, in order to make a profit. Other possible reasons for the sale of an asset should be considered such as changes in the market, changes in a work situation, family arrangements etc.

Some tests adopted by the court of law can be explained through the following cases.

- D. S. Mahawitharana v CIR - CTC – Volume III
- Ram Iswara v CIR - CTC – Volume III
- Commissioner of Income Tax v C. S. De Zoysa - CTC – Volume I
- Rutledge v CIR - 14 TC 490
- CIR v Livingstone and Others - 11 TC 538
- CIR v Fraser - 1942 24 TC 498
- CIR v Reinhold - 34 TC 389
- Martin v Lawry - 11 TC 297

Isolated arrangement with a business character

The definition also includes an "isolated arrangement with a business character however short the duration of the arrangement."

Past business and prospective business

Whether an amount is to be included as a "prospective" business will be a question of fact and degree. The factors considered in determining whether a person conducts a "prospective" business are similar to those considered in determining whether a person conducts a business. A profit motive is also usually a critical element in conducting a business but it is here that there might be a difference between a prospective business and actually conducting a business. With a business the person will have begun the actual activity by which a profit is expected but with a prospective business this will not be the case. A person may have a prospective business even though the actual business is never conducted.

The expenses incurred in the prospective business can be deducted from such business receipt (ex. payment for the future restriction on conducting business) and if there are any losses from the prospective business, such loss can be deducted from the profit, if any.

Prospective business

Meals2Eat (Pvt) Ltd is in currently setting up a restaurant in Matara. Nice2Eat (Pvt) Ltd runs a chain of Chinese restaurants within the southern province and is concerned that Meals2Eat may prove to be a serious threat to their business. Nice2Eat offers to purchase the prospective business - Meals2Eat at a price of Rs. 50 million and under the terms of the arrangement Meals2Eat will agree not to open up a restaurant in Matara for the next 25 years. Meals2Eat accepts the offer before the restaurant is opened.

Determine whether the income of Rs. 50 million received by Meals 2Eat will be considered as its business income.

What is Business income?

A person's income from business for any year of assessment is the gains and profits from conducting the business for that year (section 6(1). The following will be considered to be income from business;

i. Service fees
ii. Sale of trading stock
iii. Gains from realization of capital assets and liabilities of the business
iv. Realisation of depreciable assets of the business

v. Consideration for accepting a restriction on the capacity to conduct business
vi. Gifts
vii. Amounts derived that are effectively connected with the business
viii. Any other amounts required to be included under the Act

What constitutes business income?

ABC Company is engaged in the business of re-modeling motor cycles. They purchase motor cycle tyres from PRQ dealers. PRQ dealers has given a motor lorry worth Rs. 5 million to ABC Company in recognition of its long standing relationship.

Determine whether the amount of Rs. 5 million will be considered as business income for ABC Company.

Service fee

The Act has defined "service fee" to mean "a payment to the extent to which, based on market values, it is reasonably attributable to services rendered by a business of a person, but excludes interest, rent or a royalty". This means that any income earned by providing any services as a business will be considered to be liable for income tax.

Sale of trading stock

Where a person's business is engaged in manufacturing of goods or where the business is engaged in trading of goods, the income from such activities will be considered to be liable for income tax.

Section 195 defines "trading stock" to mean "assets owned by a person that are sold or intended to be sold in the ordinary course of a business of the person, work in progress on such assets, inventories of materials to be incorporated into such assets and consumable stores."

Gains from realization of capital assets and liabilities of the business

This refers to the capital gains arising on sale of capital assets. Section 39 of the IRA provides instances where a realization will arise. This will be discussed in detail under Capital Gains Tax. The sale of a capital asset held for business will be treated as being part of the business income.

Section 195 defines a "capital asset"-

"(a) means each of the following assets:-
  - (i) land or buildings;
  - (ii) a membership interest in a company, partnership or trust;
  - (iii) a security or other financial asset;
  - (iv) an option, right or other interest in an asset referred to in the foregoing paragraphs; but

(b) excludes trading stock or a depreciable asset;"

Section 195 further defines the following terms;

land or buildings" includes a structural improvement to land or buildings, an interest in land or buildings or an interest in a structural improvement to land or buildings, and includes the following:—

(a) a lease of land or buildings;
(b) a lease of a structural improvement to land or buildings; or
(c) an exploration, prospecting, development, or similar right relating to land or buildings; and
(d) information relating to a right referred to in paragraph (c);

"membership interest" in an entity means a right, whether of a legal or equitable nature, including a contingent right, to participate in income or capital of the entity and includes the interest of a partner in a partnership, the interest of a beneficiary in a trust and shares in a company;

The gain from the realization of a capital asset used in the business will be considered as a business income.

Realisation of depreciable assets of the business

The profit or loss on the sale of assets that are being used in the business will be considered as income from business.

Section 195 defines "depreciable asset" –

(a) means an asset to the extent to which it is employed in the production of income from a business and which is likely to lose value because of wear and tear, obsolescence or the passing of time; but
(b) excludes goodwill, an interest in land, a membership interest in an entity and trading stock;

The calculation of the tax profit or loss has been specified in the Act. Please refer section on Capital Allowances.

Amounts derived that are effectively connected with the business

The Act requires that amounts derived that are "effectively connected" with the business and that would otherwise be included in calculating the person's income from an investment. The Act does not define the meaning of "effectively connected" and as such we will have to interpret these words in light of the antecedent facts.

The "effectively connected" test is a question of nexus or association. There are varying degrees of connection and so it is not possible to state concrete rules in this area. Nevertheless, all that is required is an "effective" connection with a business and so a broad approach should be adopted.

For example, a person who owns a commercial property with three floors, uses the first two floors of the building in conducting his business. The remaining floor of the building has been rented out to another company. Will the rent income from this be considered as his business income or his investment income? The determining criteria will be if the rent income is "effectively connected" with his business.

Another example would be, where a person conducting his business, generates cash flows in excess of what is required for the day to day operations of the business. Therefore, the excess funds are placed in Fixed deposits and the person earns interest income on same. Will the interest income be considered to be "effectively connected" with the business? In this case, as the person is given the option of either using the excess funds in the business or investing it in fixed deposits, it will be considered that the person has made a decision to "invest". As such it is not effectively connected in carrying out the business, but rather an option has been made to invest such money. As such the interest income will be considered as "investment income". It is however, still open to the taxpayer to show that there is an effective connection between the business and the interest derived. (*Ceylon Steel Corporation Limited v Commissioner General of Inland Revenue.*)

Alternatively, where a person decides to sell his obsolete raw materials (scrap sales), this transaction will be considered to be "effectively connected" with the business. As such it will be considered as part of the business income of the person.

Exclusions from business income

Section 6(3) specifically excludes the following in computing the business income;

1. exempt amounts
2. Final withholding payments
3. Amounts that are included in calculating a person's income from an employment

Exempt amounts

The Third schedule to the IRA provides a list of items which are considered to be exempt from Income Tax. A few examples are given below;

- gain made on realisation of an asset consisting of shares quoted in any official list published by any stock exchange licensed by the Securities and Exchange Commission of Sri Lanka;
- A dividend paid by a resident company to a member to the extent that dividend payment is attributable to, or derived from, another dividend received by that resident company or another resident company;
- dividends from and gains on the realisation of shares in a non-resident company where derived by a resident company with respect to a substantial participation in the non-resident company. In this paragraph, "substantial participation" means—
  - (i) holding 10 percent or more of the value of shares in the company, excluding redeemable shares; together with
  - (ii) control, either directly or indirectly, of 10 percent or more of the voting power in the company;

What constitutes Business Income

Assess whether the following will be included in Business Income

1. Sale of manufactured toys
2. Income received by providing transport and logistics services
3. Disposal of a machine for which capital allowances have been claimed and the tax written down value is lesser than the Sale price
4. Dividend paid out of dividend received
5. Insurance claim received for damaged stocks
6. Sale of shares in a private limited company in an investment company
7. Sale of shares in a listed company

2.3. Computing Investment Income

Investment has been defined in section 195 as follows;
"investment" means –

(a) the owning of one or more assets, including one or more assets of a similar nature or that are used in an integrated fashion, and
(i) includes a past, present or prospective investment; but
(ii) excludes a business or employment; or

(b) a game of chance, including lotteries, betting or gambling;"

Accordingly, Investment involves holding assets passively for gain. As per the concept of dominancy over the sources of income, it excludes business or employment.

Section 7(2) specifies what is to be included when computing "investment income".

(a) dividends, interest, discounts, charges, annuities, natural resource payments, rents, premiums and royalties;
(b) gains from the realisation of investment assets as calculated under Chapter IV;
(c) amounts derived as consideration for accepting a restriction on the capacity to conduct the investment;
(d) gifts received by the person in respect of the investment;
(e) winnings from lotteries, betting or gambling; and
(f) other amounts required to be included under this Act.

It is noted that many of the types of income mentioned above as investment income may also be derived in the context of business. The effective connection with the type of activity determines whether an amount is from business or investment. The "effectively connected" test is a question of nexus or association. So, if an amount is derived in the context of business, it is treated as business income irrespective of whether it is mentioned in section 7.

In this regard, the approach of the court of Appeal in *Ceylon Steel Corporation Limited v Commissioner General of Inland Revenue* will apply. Further the classification of items under generally acceptable accounting principals will be a guide.

Dividend

The Act has defined "dividend" in section 195 as

(a) means a payment derived by a member from a company, whether received as a division of profits, in the course of a liquidation or reconstruction, in a reduction of capital or share buy-back or otherwise;
(b) includes a capitalisation of profits –
  (i) whether by way of a bonus share issue, increase in the amount paid-up on shares or otherwise; and
  (ii) whether an amount is distributed or not; and
(c) excludes a payment to the extent to which it is –
  (i) matched by a payment made by the member to the company;
  (ii) debited to a capital, share premium or similar account; or
  (iii) otherwise constitutes a final withholding payment or is included in calculating the income of the member;

Dividend

Assess whether the following transaction will be considered as "dividend" under the IRA;

1. A company has capitalized its retained earnings of Rs. 200Mn to its capital account by increasing the paid up value of the shares
2. A company has decided to buy-back the shares of one of its shareholder at a value of Rs. 100Mn. The amount recognized in the books as Stated capital in respect of his shares was Rs. 65Mn
3. A company issues bonus shares to existing shareholders in the company amounting to Rs. 35Mn by transferring this amount from the company's retained profits to the company's share capital.

Interest

The Act has defined "interest" in section 195 as

"interest" includes –
(a) a payment, including a discount or premium, made under a debt obligation that is not a repayment of capital; and
(b) a swap or other payment functionally equivalent to interest;
(c) a commitment, guarantee or service fee paid in respect of a debt obligation or swap agreement; and
(d) a distribution by a building society;

Natural Resource Payment

The Act has defined "natural resource payment" in section 195 as

"natural resource payment" means a payment, including a premium or like amount, for the right to take natural resources from land or the sea or calculated in whole or part by reference to the quantity or value of natural resources taken from land or the sea;

Natural resource payments

Mr. Perera owns an agricultural land which it is believed that there are certain minerals. ABC Company is a mining company. In the year of assessment 2020/21 ABC Company pays Mr. Perera Rs. 1 Mn for the right to enter his property and test for the existence of the minerals. In the year of assessment 2021/22 ABC Company discovers substantial quantities of various minerals and signs a 5 year contract which allows them to extract minerals and has agreed to pay Mr. Perera a "royalty" of 5% of the value of minerals extracted. Extraction begins in the year of assessment 2021/22 and in that year ABC Company pays Mr. Kasun "royalties" of Rs. 2 Mn.

Determine if the following payments are "natural resource payments";

1. Payment of Rs. 1 Mn received in Y/A 2020/21
2. Payment of Rs. 2 Mn received in Y/A 2021/22

Rent

The Act has defined "Rent" in section 195 as
"rent" –

(a) means a payment, including a payment of a premium or like amount, for the use of or right to use property of any kind;

(b) includes a payment for the rendering of, or the undertaking to render, assistance ancillary to a use or a right referred to in paragraph (a); but

(c) excludes a natural resource payment or a royalty;

A person may lease a tangible asset in return for rent. The activity of the person in leasing the asset may or may not amount to a business. Where it does not amount to business, the rent must be included in calculating the person's income from investment.

Royalty

The Act has defined "Royalty" in section 195 as "royalty" means a payment, including a payment of a premium or like amount, derived as consideration for –

(a) the use of or right to use a copyright of literary, artistic or scientific work, including cinematograph films, software or video or audio recordings, whether the work is in electronic format or otherwise;

(b) the use of or right to use a patent, trade mark, design or model, plan, or secret formula or process;

(c) the use of or right to use any industrial, commercial, or scientific equipment;

(d) the use of or right to use information concerning industrial, commercial or scientific experience;

(e) the rendering of or the undertaking to render assistance ancillary to a matter referred to in paragraph (a), (b), (c) or (d); or

(f) a total or partial forbearance with respect to a matter referred to in paragraph (a), (b), (c), (d) or (e);

Rent and Royalty

Determine whether the following payments will be considered as "Rent" or "Royalty";

1. Payment made for the use of land and building
2. Amount received due to right to use of an industrial equipment
3. Amount received due to right to use any information in relation to a scientific experience
4. Amount received for the right to use of copyright
5. Amount received to use a motor vehicle

Annuities

The Act has not defined "annuity". Therefore, since this is connected with investment income, the annuity has to stem from an investment made by the person. The following case law illustrates what constitutes an "annuity".

- *The Commissioner of Inland Revenue v J. M. Rajarathnam CTC* – Volume III

Section 31(2) of the IRA states that payments made to a person under an annuity shall be treated as interest and a repayment of capital under a loan made by the person to the payer of the annuity.

Gains from the realization of Investment assets

Section 39 of the IRA provides instances where a realization will arise. This will be discussed in detail under Capital Gains Tax. Section 195 defines as "investment asset".

"investment asset" –

(a) means a capital asset held as part of an investment, but-

(b) excludes the principal place of residence of an individual, provided it has been owned by the individual continuously for the three years before disposal and lived in for at least two of those three years (calculated on a daily basis);

Investment Asset

Assess whether the following can be treated as "investment assets".

1. An individual who own a land and house in which he has been living for the past 6 years
2. A place of residence owned by an individual who has rented it out to a family
3. A property which consists of land and building which was rented out to a company to be used for storage
4. A holding company which owns shares in several hotel companies within the group
5. A company engaged in the business of manufacturing that has an investment in shares in a subsidiary company

Exclusions from investment income

Section 7(3) specifically excludes the following in computing the investment income;

1. exempt amounts
2. Final withholding payments
3. Amounts that are included in calculating a person's income from an employment or business

What constitutes Investment Income

Assess whether the following will be included in Investment Income

1. A company is engaged in the business of manufacture of articles for export and domestic market. It has earned dividend income of Rs. 1.2 Mn which has been distributed by a resident company from dividends received.
2. A company is engaged in the real estate and property management business. It has received rent income of Rs. 3Mn.
3. A company is engaged in producing and exporting cinnamon. It owned a land in Kottawa which was not used in any business activities. This was disposed for a price of Rs. 250 Mn.

2.4. Computing Other Income

A person's income from other sources shall be the person's gains and profits from any source whatsoever for the year, not including profits of a casual and non-recurring nature.

Section 8(2) specifically excludes the following in computing Other income;
1. exempt amounts
2. Final withholding payments
3. Amounts that are included in calculating a person's income from an employment, business or investment

The following case law provides an illustration on identifying other income;
- *Wickramasinghe v Commissioner of Income Tax* - CTC – Volume 1

2.5. Method of Accounting for Income sources (Section 21)

2.5.1. Timing of inclusions and deductions in calculating income

Section 21(1) provides that the timing of inclusions and deductions in calculating a person's income shall be made according to generally accepted accounting principles. The definition provided in section 195 is;
"generally accepted accounting principles" means—
(i) those adopted, from time to time, by the Institute of Charted Accountants (Sri Lanka); and
(ii) the International Financial Reporting Standards;

2.5.2. Business Income

When a person is conducting a business, it must account for income tax purposes on an accrual basis.

2.5.3. Individual person

An individual shall account for income tax purposes on cash basis in calculating the individual's income from an employment or investment.

2.5.4. Other instances

A person shall account for income tax purposes, from any other sources on either cash basis or accrual basis, whichever properly computes the person's income.

Method of accounting Assess the method of accounting for the following income sources; A company engaged in manufacturing business 1. On the turnover from sale of products 2. On interest income earned

2.5.5. Change in Method of Accounting (Section 21(5)

The CGIR may by written notice require a person to use a particular method of accounting or may approve an application of a person to change the person's method of accounting. The CGIR shall be satisfied that the new method is necessary to properly compute the person's income.

In terms of section 21(6) of the IRA, where a person's method of accounting changes, adjustments shall be made in the year of assessment following the change, so that no item is omitted or taken into account more than once.

2.5.6. Cash basis accounting (Section 22)

Section 22 provides;

(1) Under the cash basis of accounting, a person –
- (a) derives an amount when payment is received by or made available to the person; and
- (b) incurs an expense or other amount when it is paid by the person.

(2) For the purpose of this section, payment received in relation to an amount shall include –
- (a) used on behalf of the person either at the instruction of the person or under any law;
- (b) reinvested, accumulated or capitalised for the benefit of the person;
- (c) credited to an account, or carried to any reserve, or a sinking or insurance fund for the benefit of the person; or
- (d) constructive receipt.

Section 195, defines
"received", in relation to a person, includes –
- (a) applied on behalf of the person either at the instruction of the person or under any law;
- (b) reinvested, accumulated or capitalised for the benefit of the person;
- (c) credited to an account, or carried to any reserve, or a sinking or insurance fund for the benefit of the person; or
- (d) made available to the person;

"payment" means the conferring of value or a benefit in any form by one person on another person and includes –

(a) the transfer by one person of an asset or money to another person or the transfer by another person of a liability to the one person;
(b) the creation by one person of an asset that on creation is owned by another person or the decrease by one person of a liability owed by another person;
(c) the provision by one person of services to another person; and
(d) the making available of an asset or money owned by one person for use by another person or the granting of use of such an asset or money to another person;

Cash basis accounting

Assess the method of accounting in the following situation;

1. At the request of an individual, a bank credits interest income of his fixed deposit applicable for the year of assessment 2021/22 to his current account maintained by him in the same bank. He has not withdrawn such interest income from his current account during the year of assessment.
2. A holding company provides advisory services to its subsidiary company for a value of Rs. 2 Mn per month. The subsidiary company, instead of payment of the fees, agrees to provide its office space at a concessionary rate to compensate the fee.

2.5.7. Accrual basis accounting (Section 23)

Section 23 provides;

(1) Under the accrual basis of accounting, a person –
(a) derives an amount when it is receivable by the person; and
(b) incurs an expense or other amount when it is payable by the person.

Section 23(2) explains;
An amount shall be receivable by a person when the person becomes entitled to receive it, even if the time for discharge of the entitlement is postponed or the entitlement is payable by instalments.

Section 23(3) explains;
(3) An amount shall be treated as payable by the person when all the events that determine liability have occurred and the amount of the liability can be determined with reasonable accuracy, but not before economic performance with respect to the amount occurs.

Economic performance occurs –

(a) with respect to the acquisition of services or assets, at the time the services or assets are provided;

(b) with respect to the use of an asset, at the time the asset is used; and

(c) in any other case, at the time the person makes payment in full satisfaction of the liability.

Accrual basis accounting

A company has disposed of its factory building on 20.12.2020 for a sum of Rs. 300Mn. The buyer has agreed to settle the total consideration in ten equal monthly installments of Rs. 30Mn each starting from 01.01.2021. The company is of the view that the total tax liability arising from the disposal could be declared for the year of assessment 2020/21 as seven instalments together with the final installment will be received in the year of assessment 2020/21.

Advise the company on the method of accounting.

Occurrence of inaccuracy in accrual basis accounting

Section 23(6) and (7) provides;
An inaccuracy occurs –

(a) when a person is calculating for a payment of a particular quantity to which the person is entitled or that the person is obliged to make; and

(b) subsequently that entitlement or obligation being satisfied by a payment received or made by the person, as the case requires, of a different amount, including by reason of a change in currency valuations.

An inaccuracy is deemed to occur when –

(a) a person is calculating for a payment of a particular quantity that the person is obliged to make; and

(b) subsequently that obligation is not satisfied by a payment being made by the person within three years of the obligation arising.

The IRA in section 26(5) specifies how such inaccuracy is to be addressed;

(a) appropriate adjustments shall be made at the time the payment is received or made to remedy the inaccuracy, or at the time of the deemed inaccuracy; and

(b) the Commissioner-General may require the person to include the appropriate adjustment in the year of assessment in which the inaccuracy originally occurred notwithstanding the time limits specified in Part II of this Act for the amendment of assessments.

CHAPTER REVIEW EXERCISES

1. Calculate income tax payable by ABC (Pvt) Ltd for the year of assessment 2021/2022 based on the following information.

   i. Assessable income from the business of Rs. 35,400,000.
   ii. Interest income of Rs. 1,725,000.
   iii. Dividend income of Rs. 630,000 (out of profits).
   iv. Company has made donation to the Government of Rs. 1,200,000 during the year of assessment.