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CERTIFIED PUBLIC ACCOUNTANT

ADVANCED LEVEL 2 EXAMINATIONS

A2.3 ADVANCED TAXATION

DATE: MONDAY 26, AUGUST 2024

MARKING GUIDES AND MODEL ANSWERS

SECTION A

QUESTION ONE

Marking Guide

Particulars	**Marks**
a)	
Accounting loss	1
Provision for bad and doubtful debts	1
Tax paid	1
Gain on disposal of the asset	2
Withholding tax (WHT)	1
Depreciation	1
Donation	1
Communication	1
Drawings	1
VAT paid	1
Dividends received	1
Interest income	1
Agriculture income	1
Consultancy income	1
Dividends received from Kenya	1
Dividends received from ABC Ltd	1
Interest income	1
Consultancy income	1
Less tax depreciation	3
Adjusted business profit	1
Corresponding tax	1
Foreign tax credit	0.5
WHT on local dividend	0.5
WHT 3%	0.5
WHT on Local interest	0.5
Quarterly prepayment	1
WHT 5%	1
b)	
The meaning of Customs valuation	1
The meaning of identical goods	1
Characteristics of related persons 0.5 marks maximum 2	2
components of the basic value (1 mark maximum 4)	4
c)	
Tax Evasion	2
Tax avoidance	2
Total	**40**

Model Answer

a) Computation of the taxable income, tax liability, and tax payable for the year ended 31/12/2022.

Descriptions	**Amount FRW 000**	**Amount FRW 000**
Accounting Loss		- 700,711
Add non allowable expenses		
Bad debts	Allowed	
WHT	55,000	
VAT	Allowed	
Donation	3,000	
Communication to sister	1,000	
Staff airtime	1,200	
Tax paid	Allowed	
Depreciation	97,500	
Drawings	800,000	
Gain on disposal of asset	3,000	
Total deduction		960,700
Deductions		
Non taxable income		
Agriculture income	- 12,000	
Government treasury Interest	- 2,000	
Add gross Interest	2,105	
Less: 10% Foreign dividend	- 2,000	
Add: Foreign div Grossed	2,500	
Less: 90% Local dividend	- 18,000	
Add: Local div Grossed	21,176	
Less: Consultancy fees	- 4,000	
Add: Consultancy fees grossed	4,124	
Tax depreciation	- 72,500	
Total deductions		- 80,595
Taxable income		179,394
Tax payable		53,626
Less: Advance tax paid		
WHT on interest	105	
WHT on foreign Dividend	500	
WHT on Local Dividend	3,176	
3% WHT on consultancy	124	
WHT on importations	55,000	
IQP	12,000	
Total credit		- 70,905
Net credits		**- 17,279**

Workings:

W1: Capital allowance

Descriptions	Land (FRW "000")	Building	Computers and Accessories (FRW "000")	Motor vehicle(FRW "000")	Furniture (FRW "000")	Capital allowance "000"
Cost / TWDV	85,000	600,000	15,000	125,000	12,000	
Additions				15000	0	
Disposals					15000	
Depreciable Value		600,000	15,000	140,000	-	
W&T rate		5%	50%	25%	25%	
W&T		**30,000**	**7,500**	**35,000**	**-**	**72,500**

W2: PIT computation

From	To	Tax rate	Tax
0	360 000	0%	-
360001	1 200 000	20%	168 000
1200001	179,394,000	30%	53,458,200
Total PIT			**53,626,200**

b) Customs valuation of imported goods" means determining the value of goods for the purposes of levying ad valorem duties of customs on imported goods.

For customs valuation purposes:

Goods are considered as "**identical goods"** or "similar goods" only if they are produced in the same country as the goods being valued. Goods produced by different persons are considered only when identical or similar goods from the same producer are unavailable.

Persons are deemed **related** for customs purposes if:

a) They are officers or directors of each other's businesses;
b) They are legally recognized partners in business;
c) They have an employer-employee relationship;
d) Any person owns, controls, or holds 5% or more of the voting shares of both entities;
e) One person directly or indirectly controls the other;
f) Both are controlled by a third party, or together they control a third person;
g) They are members of the same family.

Additionally, a business association where one is the sole agent, distributor, or concessionaire of the other also qualifies them as related.

Basic Value for Taxation of Imported Goods:

The basic value includes:

- The value of the goods for customs duty purposes, whether duty is payable or not.
- Additional costs such as insurance and freight incurred in bringing the goods to Rwanda.
- Charges for services facilitating importation.
- Any applicable customs duty, excise, port charges, or other fiscal charges, excluding value-added tax.

If goods are re-imported after export for repair, renovation, or improvement without changing their nature, the import value is adjusted by the increase in the goods' value due to these processes."

b) Tax avoidance and tax evasion

Tax avoidance is the legal practice of exploiting the tax system to reduce tax liability. This can be done by taking advantage of deductions, exemptions and loopholes in the law. It's important to note that while tax avoidance is legal, it must be done within the bounds of the law and ethical standards.

Tax evasion is the illegal act of deliberately misrepresenting or concealing information in order to reduce tax liability. This may involve under-reporting income, inflating deductions or hiding money in undeclared accounts. Tax evasion is a criminal offence which can result in significant penalties, including fines and imprisonment. Article 87 of the N° 026/2019 of 18/09/2019 on tax procedures stipulates that upon conviction, he or she is liable to imprisonment for a term of not less than two (2) years and not more than five (5) years.

SECTION B

QUESTION TWO

Marking Guide

Particulars	**Marks**
a)	
Basic salary	1
House benefit	1
Taxable employment income	1
Consultancy fee	1
Rwandan income	1
Foreign income (income from the UK)	1
Total taxable income	1
Gross Tax:	DNA
First	0.5
Excess	0.5
Total Gross Tax	0.5
Tax Liability on Rwandan Income:	DNA
First	0.5
Excess	0.5
Total Tax Liability on Rwandan Income	0.5
Tax Liability on Foreign Income:	DNA
Gross Tax	1
Less: Tax Liability on Rwandan Income	1
DTR	2
b)	
For a clear explanation on how WHT is being applied	2
For a clear reference to the law on PE	2
For recommendation	2
Total	**20**

Model answer

a)

Description	**Amount (FRW)**
Gross salary	1,500,000
Add housing benefit:	
80,000 × 12	960,000
Taxable employment income	2,460,000
Consultancy fee	2,500,000
Rwandan income	4,960,000
Foreign income (income from the UK)	5,000,000
Total taxable income	**9,960,000**

Gross Tax:

Calculation	**Amount (FRW)**
First	168,000
Excess [9,960,000 - 1,200,000] × 30%	2,628,000

Total Gross Tax	**2,796,000**

Tax Liability on Rwandan Income:

Calculation	**Amount (FRW)**
First	168,000
Excess [4,960,000 - 1,200,000] × 30%	1,128,200
Total Tax Liability on Rwandan Income	**1,296,200**

Tax Liability on Foreign Income:

Calculation	**Amount (FRW)**
Gross Tax	2,796,000
Less: Tax Liability on Rwandan Income	1,296,200
Tax Liability on Foreign Income	**1,499,800**

Double Taxation Relief (DTR):

Calculation	**Amount (FRW)**
Lower of:	
Tax for Foreign Income	1,499,800
Actual Tax Paid	650,000
Thus, DTR	**650,000**

b) As Mr. Owen has not registered a business in Rwanda, the local bank applies withholding tax (WHT) and reverse charge VAT before paying him. However, according to Article 6 (Permanent Establishment) of the Rwandan Tax Law, if services, including consulting services, are provided by a person with the support of employees or other personnel for more than ninety (90) days in any twelve (12) month period, whether continuously or intermittently, the person is considered to have a permanent establishment (PE) in Rwanda.

Even if VAT and income tax (in the form of WHT) are paid, Mr. Owen must register his business in Rwanda and comply with all relevant tax requirements. These include:

Income tax: Ensure the correct declaration and payment of corporate income tax.

VAT: Comply with VAT regulations if all conditions are met.

PAYE: If Mr. Muhire Christian is engaged on the basis of an employment contract, Mr. Owen must comply with PAYE regulations.

WHT: If Mr. Muhire is considered a consultant, WHT must be applied appropriately.

In addition, Mr. Owen should be aware of decentralized taxes, such as Trading licenses and other fees, which will be applicable once he registers his business.

QUESTION THREE

Marking Guide

Particulars	**Marks**
a)	
Standard rated sales	0.5
Credit note	1
Standard credit sales	1
VAT reverse charge	0.5
Bad debt	1
Export	1
Standard rated purchase	1
Credit note	1
Consulting fee for July 2023	1
Purchase of office supplies	1
Electricity bill	1
Communication expense	1
Standard credit purchases	1
Debit note	1
Purchased office furniture	1
Rent for July 2023	1
b) 1ne mark for clearly stating the following:	
Registration	1
Rates	1
exemptions	1
Input tax credits	1
Filing and payment	1
Total	**20 Marks**

Model answer

a) VAT computation

Output VAT:

Date	**Description**	**Working**	**Amount FRW "000"**
06 July 2023	Standard rated sales	500,000 * 18/118	76,271
07 July 2023	Credit note	120,000 * 18/118	(18,305)
09 July 2023	Standard credit sales	150,000 * 18/118	22,881
02 July 2023	VAT reverse charge	10,000 * 18/100	1,800
27 July 2023	Bad debt		-
31 July 2023	Export	Zero rated	-
	Total Output VAT		**82,647**

Input VAT

Date	Description	Working	Amount FRW "000"
02 July 2023	Standard rated purchase	300,000 * 18/118	45,763
07 July 2023	Credit note	110,000 * 18/118	(16,780)
24 July 2023	Consulting fee for July 2023	30,000 * 18/118	4,576
15 July 2023	Purchase of office supplies	8,000 * 18/118	1,220
18 July 2023	Electricity bill	4,500 * 18/118	686
21 July 2023	Communication expense	(2,500 * 18/118) * 60/100	229
12 July 2023	Standard credit purchases	250,000 * 18/118	38,136
25 July 2023	Debit note	Given	700
29 July 2023	Purchased office furniture	45,000 *18/118	6,864
04 July 2023	Rent for July 2023	6,000 * 18/118	915
	Total Input VAT		**82,310**

VAT payable = 82,647,000 – 82,310,000 = 337,000

b. The main aspects of the Rwandan VAT system are as follows:

- **Registration obligation**: Taxpayers must register for if their annual sales exceed FRW 20,000,000 per year or FRW 5,000,000 per quarter.
- **Input tax credits**: Registered taxpayers can claim input tax credits on VAT paid on locally purchased and imported products, thus reducing the amount of VAT payable to the RRA.
- **Standard rate:** The standard VAT rate in Rwanda is 18%, applicable to most goods and services, unless exempted or zero-rated.
- **Exemptions and zero-rating**: Certain goods and services, such as basic foodstuffs and healthcare, are exempt from VAT. Exports and certain international services are zero-rated.
- **Filing and payment:** VAT returns must be filed periodically - monthly or quarterly - depending on the company's turnover. Payments must be made shortly after the end of each reporting period.

QUESTION FOUR

Marking Guide

Descriptions	Marks
a)	
salary	1
communication allowance	1
Overtime allowance	1
Rent	1
Benefit in Kind (car)	1
Domestic staff	1
Medical insurance	1
Medical expenses for spouse	1
Reimbursement	1
Total employment income	1
Consultancy income	1
Total Income	1
Total PIT	1
Less tax paid at Source (PAYE)	1
TAX PAYABLE	1
b)	
1 mark for a well stated method (maximum 5)	5
Total	**20 Marks**

Model Answer

a) Computation of Nkundimana Emanuel's taxable employment income for the year, and tax payable:

Description	Working	**Amount (FRW)**
salary	900,000 x 12	10,800,000
communication allowance	120,000 x 12	1,440,000
Overtime allowance	60,000 x 12	720 000
Domestic staff	70,000 x 2 x 12	1,680,000
Medical insurance	(100,000 - 60,000) x 12	480,000
Medical expenses for spouse		3,000,000
Reimbursement		Exempted
Rent	150,000 x 12	1,800,000
Total Cash Emolument		19,200,000
Benefit in Kind (car)	10% of 12,960,000	1,920,000
Total taxable income		21,120,000
Other income:		
Consultancy income		15,000,000
Total Income		36,120,000

Tax payable

From	To	Tax rate	Tax payable
0	360,000	0%	0
360,000	1,200,000	20%	168,000
1,200,001	Above	30%	10,476,000

b) The Rwanda Revenue Authority (RRA) has several methods and procedures for verifying income that has been omitted or understated. These methods are designed to ensure that taxpayers comply with tax legislation, and to uncover any discrepancies or omissions in declared income. Here are some of the common methods used by the RRA to identify such problems:

- **Audits:** Random and targeted audits to verify the accuracy of tax returns and financial statements.
- **Data matching:** Comparing taxpayer information with third-party data from banks, employers and other institutions.
- **Automated systems and analysis:** Use of Electronic billing machines reports, electronic filing, and data mining systems to detect inconsistencies and anomalies in reported income.
- **Inter-agency cooperation:** Collaboration with other government agencies and international bodies to collect and share financial information.
- **Field investigations**: Field visits and lifestyle verification to ensure that declared income corresponds to visible wealth and expenses.

QUESTION FIVE

Marking Guide

Description	**Marks**
a)	
Capital Gain	1
Interest Income	2
Interest Income	1
Dividend Income	2
Interest Income	1
Royalty Income	1
Interest Income	2
Capital Gain	1
Dividend Income	2
b)	
Clear explanation (most-favored-nation)	3
c)	
Clear Discuss the income reconstruction	4
Total marks	**20**

Model Answer

a) computation of the WHT

Income Type	Workings	Withholding Taxes
1. Capital Gain	Proceeds from the sale of shares (8,000 x 400)	
	Cost of the shares (300 x 8,000)	
	Capital Gain: 800,000	
	Capital Gain Tax (800,000 x 5%)	40,000
2. Interest Income	(25,000,000 x 8% x 10/12)	
	Interest Income: 1,666,667 FRW	
	Withholding Tax (1,666,667 x 15%)	250,000
3. Interest Income	(10,000,000 / 85) x 100	
	Interest Income: 11,764,706	
	Withholding Tax (11,764,706 x 15%)	1,764,706
4. Dividend Income	(250 x 100,000)	
	Dividend Income: 25,000,000	
	Withholding Tax (25,000,000 x 5%)	1,250,000
5. Interest Income	Exempted since maturity of deposit > 1 year	Exempted
6. Royalty Income	15% of 20,000,000 FRW	3,000,000
7. Interest Income	(7,000,000 / 95) x 100	
	Interest Income: 7,368,421	
	Withholding Tax (7,368,421 x 5%)	368,421
8. Capital Gain	Exempted since capital gain on listed shares is exempt	Exempted
9. Dividend Income	(3,000,000 / 95) x 100	
	Dividend Income: 3,157,895	
	Withholding Tax (3,157,895 x 5%)	157,895

b) The "most-favored-nation principle in international trade guarantees that any favorable trade treatment granted to one nation must be extended to all other nations under similar conditions. This principle promotes fairness by preventing discriminatory practices between trading partners. For example, if country A grants lower tariffs to country B on a certain product, it must offer the same lower tariffs to all other WTO member countries on that product. This rule helps to maintain equitable trade relations worldwide, and encourages countries to negotiate fair trade agreements that benefit all parties concerned.

c) Income reconstruction plays a pivotal role in tax enforcement by enabling revenue authorities to ascertain and verify taxable income when there are suspicions of underreporting or fraud. This process is crucial when taxpayers lack adequate records or when existing records do not accurately reflect income. According to tax regulations, taxpayers are obligated to maintain accounting records that account for inventory, classify expenses correctly, and record improvements to depreciable assets. Failure to maintain these records can lead to the use of income reconstruction by tax authorities to determine taxable income.

The authority to reconstruct income allows revenue authorities to use direct and indirect methods. Direct methods focus on specific transactions, such as analyzing bank deposits without reported sources or scrutinizing invoices for unreported sales. These methods aim to pinpoint specific omissions or errors in reported income. In contrast, indirect methods provide circumstantial evidence of income, such as the net worth method, which compares assets and liabilities over time to detect unreported income.

Taxpayers have the right to challenge reconstructed income assessments. They can rebut the authority's position by demonstrating that the method used was arbitrary, capricious, or erroneous. This can be achieved by providing evidence of non-taxable sources for the reconstructed income, such as gifts, inheritances, or loans. Moreover, taxpayers must show that their records, if maintained properly, accurately reflect income, thus contesting the need for income reconstruction.

Overall, income reconstruction serves as both a verification tool for unconventional accounting methods and a means to calculate income quickly when records are lost or inadequate. It underscores the importance of maintaining accurate financial records and highlights the regulatory framework that governs tax compliance and enforcement.

End Of Marking Guides and Model Answers