CERTIFIED PUBLIC ACCOUNTANT

ADVANCED LEVEL 2 EXAMINATIONS

A2.3 ADVANCED TAXATION

DATE: MONDAY, 29 NOVEMBER 2021

MARKING GUIDE AND MODEL ANSWERS

SECTION A

QUESTION ONE

Marking guide

		Marks
a	Profit before tax	1
	0.5 marks for every valid item added back on non-allowable expenses and non-allowable incomes, maximum 7 marks	7
	1 mark for items added back, maximum 2 marks	2
	1 mark for items deducted as allowable expenses, maximum 2 marks	2
	Computation of taxable income, using the correct rate	1
	1 mark for tax paid deducted, maximum 2 marks	2
	Award marks for the following workings as below:	
	W1: Turnover calculation	1
	W2: Professional fees	1
	W3: Donations	1
	W4: Technical services	1
	W5: Royalties	1
	W6: Capital allowances (Format; 01mark, Cost/WDV; 01mark, new assets; 01 mark Accelerated depreciation; 01mark, Tear and wear; 01-mark, depreciation)	5
	Maximum marks for this section	**25**
b	01 mark for each well calculated withholding tax, max. 04	4
c	01 mark for each quarterly prepayment (Q1, Q2 & Q3)	3
	01 mark for student who understands and states that there is no quarterly prepayment in Q4 but final declaration	1
d	02 marks for well-calculated capital gains and 01 mark for well-calculated capital gains tax, max. 03 marks	3
e	01 mark for each valid point, max. 04 marks	4
	Total marks	**40**

Model answers

a.

COMPUTATION OF TAXABLE INCOME AND TAX PAYABLE	
	FRW "000"
Profit before tax	4,078,300
Add back non-allowable expenses	
Thin capitalization is allowed	-
General increase in the provision	673,200
Construction of steel advertising billboards	68,900
Professional fees (W2)	63,900
Donation (W3)	37,300
Technical fees (W4)	184,300
Royalties (W5)	63,600
Fines and penalties	140,500
Depreciation and Amortization	765,900
Cash bonuses	335,800
	6,411,700
Less non-allowable incomes	
Capital gain on shares listed	(20,500)
Dividend from local company (50%*140000)	(70,000)
	6,321,200
Less non-business income	
Dividend from Kenya (50% *140,000)	(70,000)
Interest from Government security	(2,900,000)
	3,351,200
Add back Allowable incomes	
Dividend from Kenya (70,000 x100/80)	87,500
Interest from Government security (2,900,000 x100/95)	3,052,632
Business Income	**6,491,332**
Less Capital Allowances:	
Accelerated Depreciation/Investment allowance (W6)	(667,250)
Depreciation (W6)	(1,006,745)
Taxable Business Income	**4,817,337**
Tax Since it listed 30% shares on RSE the CIT rate 25%	**1,204,334**
Less Tax paid	**-**
WHT on Interest (5% x 3351200)	(167,560)
Foreign tax credit on foreign dividend (15% * 87500)	(13,125)
Tax payable	**1,023,649**

Note: Thin Capitalization: The interest on loan from related party for bank is allowed even if the loan is four times the equity

Workings

W1 Total Turnover calculation	**FRW "000"**
Interest income	18,500,000
Other banking activities (Note 3)	830,000
Total Turnover	**19,330,000**

W2 Professional fees	**FRW "000"**
Amount paid	450,500
Amount Allowed (2%* 19,330,000 as per W1)	386,600
Not allowed (450,500 -386,600)	**63,900**

W3 Donation	**FRW "000"**
Amount donated	230,600
Donation allowed (1% * 19,330,000 as per W1)	193,300
Not allowed (230,600 – 193,300)	**37,300**

W4 Technical fees	FRW "000"
Amount paid	570,900
Amount Allowed (2%* 19,330,000 as per W1)	386,600
Not allowed (570,900 – 386,600)	**184,300**

W5 Royalties	
Amount paid	450,200
Amount Allowed (2%* 19,330,000 as per W1)	386,600
Not allowed (450,200 -386,600)	**63,600**

W6 Capital Allowances

Assets	Buildings FRW "000"	Com and Acc FRW "000"	ICT equip-10yrs FRW "000"	Other assets FRW "000"	Capital Allowance FRW "000"
Cost/WDV	2,000,000	850,000	1,200,000	930,400	
New Assets	500,000	237,200	230,900	366,400	
Accelerated Dep 50%	**250,000**	**118,600**	**115,450**	**183,200**	**667,250**
Depreciable value	**2,250,000**	**968,600**	**1,315,450**	**1,113,600**	
Depreciation rate	5%	50%	10%	25%	
Depreciation	**112,500**	**484,300**	**131,545**	**278,400**	**1,006,745**

Note: Cost of new assets under other assets, includes the cost of billboards of FRW 68,900,000

b. Withholding taxes.

	Amount FRW "000"	Country	DTA in Place?	Applicable WHT rate	WHT amount FRW "000"
Technical fees	570,900	Turkey	Yes	10%	57,090
Royalty fees	450,200	Kenya	No	15%	67,530
Professional fees	450,500	United Arab Emirates	Yes	10%	45,050
Interest	4,000,000	Turkey	Yes	10%	400,000

c. Quarterly prepayments

Quarterly Prepayments	**FRW "000"**	**FRW "000"**
Tax liability	**1,023,649**	
Quarter one 1/1/2021 - 30/6/2021 (25%*1,023,649)		255,912
Second Quarter 1/7/2021 - 30/9/2021(25%*1,023,649)		255,912
Third quarter 1/10/2021 - 31/12/2021(25%*1,023,649)		255,912
Fourth quarter (Final Declaration) 1/1/22 -31/3/2022		Final declaration

d. Capital gains

Capital Gain	FRW
Market value of shares (250,000*350)	87,500,000
Less cost of shares (250,000*200)	50,000,000
Capital Gain	37,500,000
Capital gain tax at 5%	1,875,000

e. Conditions to carry forward a loss for more than five years

i. Submit a written application to the Commissioner General of Rwanda Revenue Authority for carrying forward the loss for more than five (5) tax periods

ii. Submit his or her application with the declaration of tax for the fifth tax period.

iii. Present sound reasons that caused the loss for which he or she is requesting to carry forward and reliable strategies to overcome such a loss.

iv. Prove that the loss was derived from the investments carried out.

v. Submit the certified financial statements of the tax period corresponding to the loss.

vi. Be a credible taxpayer who declares and promptly pays tax and not guilty of tax evasion in the previous five (5) years.

vii. Not to have distributed any profits in the previous five (5) years

SECTION B

QUESTION TWO

Marking guide

		Marks
a	Award maximum 03 marks for well calculated customs value	3
	Award 01 mark for Import VAT calculation	1
	Award 01 mark for correct computation of Reverse charge VAT on imported services	1
	Output VAT: 02 marks for right calculation (01 mark for each valid point in calculation, max. 02 marks)	2
	Input VAT: 02 marks for right calculation (Including apportionment)	2
	01 mark for the right calculation of net VAT claimable	1
	Maximum marks for this section	10
b	01 mark for a good Memo format and introductory statement (s)	1
	01 mark for each valid tax incentive, max. 05 marks	5
c	0.5 marks for each valid point max. 04 marks	4
	Maximum marks for this section	10
	Total marks	**20**

Model answers

a. COMPUTATION OF THE VAT PAYABLE OR CLAIMABLE

INPUT VAT	**FRW**
CIF	431,800,000
Import duty 25%	107,950,000
	539,750,000
Excise tax 10%	53,975,000
Custom Value	**593,725,000**
VAT on Imports @ 18%	106,870,500
Reverse charge VAT on foreign service (18%)	1,440,000
Output VAT	
sale of zero-rated goods	-
Sale of standard goods	39,600,000
Debit Note (10,000,000 x18%)	(1,800,000)
Output VAT	**37,800,000**
Calculation of allowed Input VAT	
Taxable sales (250M +220M)	470,000,000
Total sales (250M+220M+187.4006M)	657,400,600
Proportionate of taxable sales to total sales	71%
Allowed input VAT (71% x 106,870,500) +1,440,000	**77,318,055**
VAT Claimable (Output -Input VAT)	**(39,518,055)**

b. Investment incentives available in Rwanda

MEMO TO MAGNET INTERNATIONAL LIMITED:

FROM: RWANDA DEVELOPMENT BOARD

TOPIC: TAX RELATED BENEFITS OF INVESTING IN RWANDA

Dear Investors,

This Memo is brief summary of tax incentives available for Investors who choose to invest in Rwanda

Through the Investment Promotion and Facilitation Law N° 06/2015, which was effectively repealed by Law N° 006/2021. In a bid to improve Rwanda's competitiveness as an investment destination, The investment code provides the following fiscal incentives to a registered and qualifying investor

- Zero corporate income tax for companies planning to relocate headquarters to Rwanda and that fulfil certain requirements, as well as entities registered by philanthropic investors.
- 15% preferential corporate income tax for strategic sectors i.e. energy, transport, affordable housing, ICT and financial services.
- Accelerated depreciation of 50%for key priority sectors i.e. tourism, construction, manufacturing and agro-processing
- Exemption of capital gains tax
- Seven-Year corporate income tax Holiday for large projects in strategic sectors i.e energy, exports, tourism, health, manufacturing, and ICT
- Repatriation of capital and assets
- Customs exemption on products used in Export Processing Zones (EPZs).
- Prompt settlement of VAT refunds.
- Additional key incentives for priority sectors such as incentives for: the construction and development of the Kigali Innovation City; the creation and growth of the Kigali Financial Centre; for film production and post-production; mining exploration; and start-ups.
- There are other specific tax incentives in form of lower Corporate Income Tax rates with certain conditions like exporting, being listed in Rwanda Stock Exchange.

There are other non-fiscal incentives that accompany the fiscal incentives, ie; Quick business and investment online registration, Assistance with tax-related services and exemptions, Assistance to access utilities (water & electricity), Assistance with obtaining visas and work permits, One stop centre that provides notary services, Provision of Aftercare services to fast track project implementation.

c. Obligation of the EBM Users

- To purchase certified set of electronic billing machines from a licensed supplier.
- To install certified electronic billing machines at the sales location.
- To issue receipt generated by certified electronic billing machines to every customer purchasing items or service.
- To ensure that certified electronic billing machines is placed at a place which is accessible and easily seen by customers.
- To ensure that all items or services sold through certified electronic billing machine have clearly defined name and appropriate tax rate.
- To include client 's TIN on the receipt upon request from the client who performs the payment prior to start issuing a receipt.
- To put a conspicuous notice containing the following information at a place where the certified electronic billing machine is installed:
- To make certified electronic billing machine available for control with respect to its being intact and the correctness of its operations.
- To perform compulsory technical inspection of certified electronic billing machine with appropriate service point once such obligation is requested by the Commissioner General.
- To store the copies of certified electronic billing machines journal records within ten (10) years.
- To ensure that the user manual is received at the time of supply by the dealer.
- To ensure that the supplier has registered certified electronic billing machine at the time of supply with the Authority.
- To report change of sales location to the Authority through procedure prescribed by the Commissioner General.
- Not to stop using certified electronic billing machine for more than twelve (12) hours without prior notification to the Authority; 15) To report malfunctions of certified electronic billing machine to the Authority within six (6) hours.

QUESTION THREE

Marking guide

		Marks
a	**Rental income tax;**	
	Award maximum marks as below for each well calculated amount;	
	Option 1: Allowable expenses	1
	Interest	1
	Right calculation of Rental Income Tax	2
	Option 2: Allowable expenses	1
	Depreciation	1
	Interest	1
	Right calculation of Rental Income Tax	2
	01 mark for right opinion to the investor with regard to best investment option	1
	Maximum marks for this section	***10***
b	**Taxable income of MRU Associates**	
	0.5 marks for each valid non-allowable expense added back, max. 03 marks	3
	0.5 marks for each sub-total rightly computed max. 02 marks	2
	0.5 marks for each disallowable investment (other) income max. 01 mark	1
	01 mark for allowable interest income	1
	01 mark for correct calculation of tax liability	1
	01 mark for adjustment of Withholding tax paid on interest, adjustable from tax liability	1
	01 mark for final tax liability payable	1
	Maximum marks for this section	***10***
	Total marks	**20**

Model answers

a. **Tax planning**

The investor has two options to invest in and each option has different tax treatment with regard to income generated.

Option one: Investment in commercial building		
Gross rent		187,400,500
Less allowable expenses (50%)		(93,700,250)
Less interest (30%x500M) *12%		(18,000,000)
Taxable income		75,700,250
Tax liability		
(0 - 180,000)	0%	-
(180,001-1,000,000)	20%	168,000
(1,000,001 -75,700,250) *30%	30%	22,410,075
Tax payable		**22,578,075**

Option two: Investment in machines for rent		
Gross rent		187,400,500
Less allowable expenses (10%)		(18,740,050)
Less interest (30%x500m) *12%		(18,000,000)
less depreciation (25% *500m)		(125,000,000)
Taxable rental income		**25,660,450**
Tax liability		
(0 - 360,000)	0%	-
(360,001 - 1,200,000)	20%	168,000
(1,200,001 - 25,660,450)	30%	7,338,135
Tax payable		**7,506,135**

If the investor wants to minimize the tax liability, he should invest in machines for rent

b. Computation of taxable income of MRU associates

	FRW "000"
Profit before tax	96,800
Add back non allowable expenses	
Donation	10,700
Bad debt	24,500
Communication (20%*10500)	2,100
Other expenses	5,700
Finance cost	110,500
	250,300
Less non allowable incomes	
Dividend from local company	(48,900)
	201,400
Less interest on government security	(31,300)
	170,100
Add allowable interest (31,300*100/85)	36,824
Taxable income	**206,924**
Tax liability (30%)	***62,077***
Less WHT on interest (15% *36,824)	(5,524)
Tax payable	***56,553***

QUESTION FOUR

Marking guide

		Marks
a	01 mark for right format and line items of Balance sheet, the main work starts from net assets	1
	0.5 marks for each valid point used in adjusting Net assets to arrive at taxable income	3
	02 marks for correct calculation of 2019 tax liability	2
	02 marks for correct calculation fines and penalties on 2019 tax liability	2
	02 marks for correct calculation of 2020 tax liability	2
	02 marks for correct calculation fines and penalties on 2020 tax liability	2
	03 marks for detailed working of depreciation (0.5 marks for each year depreciation and other major line items in calculation, max. 03 marks)	4
	01 mark for right conclusion and advise in line with total tax including fines and penalties	1
	Maximum marks for this section	**17**
b	1 mark for correct calculation of percentage of completion	1
	01 mark for correct calculation of contract Revenue for the year	1
	01 mark for the right advise on tax treatment	1
	Maximum marks for this section	**3**
	Total marks	**20**

Model answers

(a)

	2018 Amount FRW "000"	**2019 Amount** FRW "000"	**2020 Amount** FRW "000"
Non-current assets			
Motor vehicle	25,000	25,000	60,000
Furniture and fittings	10,000	12,000	25,000
Computer and accessories	4,200	4,800	5,500
Investment in government bond	40,000	69,600	70,000
TOTAL NON-CURRENT ASSETS	**79,200**	**111,400**	**160,500**
Current assets			
Inventory	15,400	30,800	30,500
Receivables	2,100	11,800	30,000
Cash and cash equivalents	10,900	8,700	12,600
TOTAL CURRENT ASSETS	**28,400**	**51,300**	**73,100**
TOTAL ASSETS	**107,600**	**162,700**	**233,600**
Bank loan	30,000	25,800	15,000
Account payable	19,500	10,600	16,000
TOTAL LIABILITIES	**49,500**	**36,400**	**31,000**
NET ASSETS	**58,100**	**126,300**	**202,600**
Increase in the net asset value		68,200	76,300
Add interest on the government bond		8,352	8,400
Add: private expenses (health insurance of her family; FRW 200,000*12)		2,400	2,400
less Interest on loan		(3,870)	2,250
Less Depreciation of assets W1		(8,413)	(18,322)
Taxable incomes	**-**	**66,670**	**71,028**

Tax liability 2019		**FRW**
0 - 360,000	0%	-
360,001 - 1,200,000	20%	168,000
1,200,001 - 66,470,000	30%	19,641,000
		19,809,000

Fines and penalties:	
Fixed administrative fine (Turnover >20m)	300,000
Late declaration and payment 60% (Late by >60 days)	11,885,400
Interest late payment (1.5% non-discounted for 12 months; April 2020 to March 2021)	3,565,620
Total taxes and penalties 2019	**35,560,020**

Tax liabilities and penalties 2020		**FRW**
(0 - 360,000)	0%	-
(360,001 - 120,000)	20%	168,000
(1,200,001 – 71,028,000)	30%	20,948,400
Tax liability		**21,116,400**
Fines and Penalties:		
Fixed administrative fine (Turnover > 20m)		300,000
Late declaration and payment 20% (Late by <30 days)		4,223,280
Interest on late payment (1.5% for one month)		316,746
Total taxes and penalties 2020		**25,956,426**

Total taxes Including fines and penalties for 2019 and 2020 **61,516,446**

Since the assessment indicated on the notes of assessment is overstated, Ms Igabe Grace should lodge in appeal to the commissioner general for over assessment of tax**.**

<u>Workings</u>

W1 Depreciation	**Motor Vehicles**	**Computers**	**Furniture**	**Depreciation**
2018 cost	25,000	4,200	10,000	
Depreciation	**6,250**	**2,100**	**2,500**	***10,850***
WDV 31/12/2018	**18,750**	**2,100**	**7,500**	
1/1/2019 WDV	18,750	2,100	7,500	
New assets	-	600	2,000	
	18,750	**2,700**	**9,500**	
Depreciation	***4,688***	***1,350***	***2,375***	***8,413***
WDV 31/12/2019	**14,063**	**1,350**	**7,125**	
1/1/2020 WDV	14,063	1,350	7,125	
New assets	35,000	700	13,000	
	49,063	2,050	20,125	
Depreciation	***12,266***	***1,025***	***5,031***	***18,322***

(b)

	FRW
Contract price	800,000,000
Estimated cost	750,000,000
Cost of work certified	213,864,000

Percentage of completion Cost of work certified/estimated cost (213.864M/750M) = **29%**
29%

Contract revenue for the year ended 31/12/2020 800,000,000 x 29%=232,000,000

Treatment of the loss at the end of the contract

The loss at the end of the contract can be carried backwards to offset
the previously reported profits.

The loss at the end of the contract can be carried backwards or forward to offset the previously reported profits.

QUESTION FIVE

Marking guide

		Marks
a	01 mark for each valid point in definition of related person, max. 03 marks	3
b	01 mark for each valid point, max. 08 marks	8
c	01 mark for each well explained point, max 05 marks	5
d	01 mark for each relevant point listed max. 04 marks	4
	Total marks	**20**

Model answers

a. Related party

- An individual and his or her spouse and their direct lineal ascendants or direct lineal descendants and their relatives in collateral lineage to at least third degree.

-A person who participates directly or indirectly in the management, control or capital of another.

- A third person who participates directly or indirectly in the management, control or capital or both control and capital of another person.

- Persons referred to under sub items a), b) and c) who participate directly or indirectly in the management, control or capital of an enterprise.

b. Computation of the Arm's length price

	FRW
Price to the external customer	200,000
Less gross margin (20%)	(40,000)
less assembling cost	(10,000)
less administration and selling costs	(8,000)
Arm's length price	**142,000**
Adjustment of profits	
Reported profits	128,400,000
Add under stated profit (148450 -142000) *850	5,482,500
Adjusted profits	133,882,500
Tax payable 30%	***40,164,750***

c. Schemes available to promote exports under EAC

- **Duty and Value Added Tax Remission Schemes**

The Partner States agree to support export promotion by facilitating duty and value added tax remission schemes. For purposes of this Article the Partner States may establish duty and value added tax remission schemes. The implementation of this Article shall be in accordance with the duty and value added tax remission schemes specified in the customs law of the Community

- **Manufacturing under Bond Schemes**

The Partner States agree to support export promotion by facilitating manufacturing under bond schemes within their respective territories. The procedure for manufacturing under bond allows imported goods to be used in a customs territory for processing or manufacture. Duty and taxes are payable on compensating products at the rate of import duty appropriate to them.

- **Export Processing Zones**

The Partner States agree to support the establishment of export processing zones. Entry into an export processing zone allow total relief from payment of duty on imported goods used directly in the production of goods for export by a person authorized to carry out that activity in the zone.

- **Special economic zones**

The Partner States may provide for the establishment of free ports for the purpose of facilitating and promoting international trade and accelerating development within the Customs Union

d. Challenges of implementing the trade liberalization policy

i. Protection of local producers
ii. Political factors
iii. Definition of the rule of origin
iv. Capturing the subsidies given

END OF MARKING GUIDE AND MODEL ANSWERS