



DEPARTMENT OF TAXATION

The Taxation of Individuals

TXN201-B

Tutorial Letter 201/1/2011

**Solution - Assignment 03 (May 2010 exam paper)
Solution – Integrated Questions, Study Unit 11**

**School of Accounting Sciences
College of Economic and Management Sciences**

Dear Student

Enclosed please find the solutions to Assignment 03/2011 and to the integrated questions in study unit 11 of tutorial letter 103/3/2011. Please work through the solutions in conjunction with the questions and your answers. This is a significant part of the learning process. It is important to understand why marks were allocated to specific parts of your solutions.

You should identify any problem areas early in the semester and make every effort to understand all aspects of the work that you have covered.

We hope that you have found the assignments and questions stimulating.

PLEASE NOTE: The schedules that are contained at the end of the exam paper questions in tutorial letter 101/3/2011 (assignment 3), are the schedules that will also be included in the exam paper that you will be writing during May 2011 and October 2011.

Kind regards

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ANNEXURE A: SOLUTION TO ASSIGNMENT 03/2011

ANNEXURE B: SOLUTIONS TO INTEGRATED QUESTIONS OF STUDY UNIT 11 IN TUTORIAL LETTER 103/3/2011

ANNEXURE A: SOLUTION TO ASSIGNMENT 03**QUESTION 1 (30 marks, 36 minutes)**

Calculation of Vusi's taxable income for the year of assessment ended 28 February 2011

		R	R	
Salary			360 300	
Bonus			40 000	(1)
Travel allowance		60 000		
<u>Less: Travel expenses</u>				
<i>Actual kilometres:</i>				
Total	34 640 km			
Private	<u>(21 040 km)</u>			
Business	13 600 km			(1)
 <i>Deemed cost per kilometre:</i>				
Cost of vehicle	R190 000			
Add: VAT 14%	<u>R 26 600</u>			
Total cost	<u>R216 600</u>			
 Fixed cost R76 041(1)/34 640 km (1) =	2.195			
Fuel	0.815			
Maintenance	<u>0.464</u>			
Total	<u>3.474</u>			
 <i>Actual cost per kilometre:</i>				
Fuel	R20 800			(1)
Finance charges (R121 100/5 years)	R24 220			(1)
Depreciation (R216 600/ 7 years)	<u>R30 943</u>			(1)
Total cost	<u>R75 963</u>			
 <i>Actual cost per kilometre:</i>				
R75 963/34 640km(1) =	<u>R2.193</u>			
Deemed cost p/km is greater than actual cost p/km Therefore deemed cost p/km is used.				
Business expense: 13 600 km x R3.474(1)		<u>(47 246)</u>	12 754	
Use of a company car: R159 600/1.14(1) x 0.85(1) x 4% (1) x 12(1) = R57 120 Gladys travelled less than 10 000km for private purposes: Reduction: 8 400 km /10 000 km (1) x R57 120 =			47 981	
Subsistence allowance		6 320		
<u>Less: deemed expenditure (R276 x 20 nights)</u>		<u>(5 520)</u>	800	(1)
Uniform allowance – exempt from tax			nil	(1)
Medical fringe benefit: Homeshop's contribution			<u>25 200</u>	(1)
			487 035	

QUESTION 1 (continued)

	R	R	
<u>Less:</u> Pension fund contributions [8% x (R360 300 + R40 000) = R32 024]			
Limited to greater of: R1 750 or			
7.5% x (R360 300 (1) + R40 000 (1)) = R30 023		<u>(30 023)</u>	(1)
		457 012	
<u>Less:</u> Donations			
University of Pretshwane (allowed for tax) – R7 000			
Limited to 10% x R457 012 (1) = R45 701 therefore allow in full		<u>(7 000)</u>	(1)
		450 012	
<u>Less:</u> Medical deductions			
Medical aid contribution deduction			
Vusi	25 200		(1)
Fringe benefit	<u>25 200</u>		(1)
	50 400		
Limited to family limit:			
[((R670 x 2) + R410) x 12] = R21 000 (1)	<u>(21 000)</u>	<u>(21 000)</u>	(1)
	29 400	429 012	
Medical expense deduction			
Medical contributions not allowed	29 400		(1)
Qualifying medical expenses not paid	<u>6 800</u>		(1)
	36 200		
In excess of 7.5% x R429 012 (1)	<u>(32 176)</u>	<u>(4 024)</u>	(1)
TAXABLE INCOME		<u>424 988</u>	

Wrong order of deductions: -1

QUESTION 2 (28 marks, 34 minutes)

Accrued leave pay	R 20 000	R	
<u>Less: Exemption s10(1)(x)</u>	<u>(20 000)</u>	-	(1)
Purchased annuity:			
Total returns: $(R1\ 050 \times 12\ \text{months}) \left(\frac{1}{2}\right) \times 25,38\ \text{years} \left(\frac{1}{2}\right) = R319\ 788$			
Y = A/B x C			
A = R110 000 (1)			
B = R319 788			
C = R9 450 (1)			
Y = $R110\ 000 / R319\ 788 \times R9\ 450 = R3\ 251$			
Taxable portion of annuity = $(R9\ 450 - R3\ 251) \mathbf{(1)} = R6\ 199$		6 199	
Unemployment insurance benefits	12 000		
<u>Less: Exemption s10(1)(mB)</u>	<u>(12 000)</u>	-	(1)
Foreign dividends	4 900		
<u>Less: Exemption limited to R3 700</u>	<u>(3 700)</u>	1 200	(1)
Local interest	25 500		
<u>Less: Exemption limited to (R22 300 – R3 700) (1)</u>	<u>(18 600)</u>	6 900	
Rental income	36 000		(1)
<u>Less: Expenses</u>			
Interest on loan	(12 800)		(1)
Replacement of damaged carpets	(4 700)		(1)
Legal fees - deductible	(3 200)		(1)
Capital repayments – not deductible, capital	-		(1)
Net rental income		15 300	
Study fees (not deductible)		-	(1)
Balance c/fwd		<u>29 599</u>	

QUESTION 2 (continued)

	R	R
Capital Gains Tax on disposal of property:		
Valuation date value, greatest of:		
- Market value (not given)		
- TAB = R314 795 (1)		
- 20% x (proceeds less post-1/10/2001 costs)		
- 20% x (R546 000 - R35 000 (1) - R21 000 (1)) = R98 000		
Base cost = R314 795 (1) + R35 000 (1) + R21 000 (1) = R370 795		
Proceeds (R525 000 + R21 000)	546 000	(1)
<u>Less: Base cost</u>	<u>(370 795)</u>	(1)
Capital gain	175 205	
<u>Less: Annual exclusion</u>	<u>(17 500)</u>	(1)
	157 705	
x 25% inclusion rate		<u>39 426</u> (1)
TAXABLE INCOME		<u><u>69 025</u></u>
Taxable amount of lump sum (1) (mark for separate calculation)		
Pension lump sum withdrawal	515 000	
<u>Less: Transfer to preservation fund</u>	<u>(130 000)</u>	(1)
Taxable portion of lump sum	<u><u>385 000</u></u>	
<u>Normal tax on taxable income:</u>		
R69 025 x 18% = R12 425		12 425
<u>Normal tax on taxable amount of lump sum:</u>		
[(R385 000 - R300 000 (1)) x 18%] (1)		15 300
TOTAL NORMAL TAX		<u><u>27 725</u></u>

QUESTION 3 (16 marks, 19 minutes)

	R	Two months R	Monthly R	
Lump sum - taxed separately		-	-	(1)
Pension annuity		56 000	28 000	(1)
Medical contributions - no fringe benefit >65		-	-	(1)
Remuneration from employer (R280 000)		-	-	
Investment income - not remuneration		-	-	(1)
		<hr/>	<hr/>	
		56 000	28 000	
Medical contributions - Savin (R10 080 x 2/12 (1)) allow in full over 65		(1 680)	(840)	(1)
Medical expenses not deductible		-	-	(1)
Balance of net remuneration		<hr/>	<hr/>	
		54 320	27 160	
		<hr/>	<hr/>	
Annual equivalent (x 12/2)		325 920	325 920	(1)
Tax on annual equivalent		77 972		(1)
<u>Less: rebates</u>				
Primary	10 260			
Age	5 675	(15 935)		(1)
Net normal tax		<hr/>		
		62 037		
		<hr/>		
For period x 2/12		10 340		(1)
per directive on lump sum		351 000		(1)
		<hr/>		
		361 340		(12)
		<hr/>		
b) No (1) Savin will not be a provisional taxpayer as his investment income is all exempt and therefore he does not comply with the requirement that the investment income must exceed R20 000 per annum (1) .				
c) 31 August 2010				(1)
28 February 2011				(1)

QUESTION 4 (26 marks)**Part A (10 marks)**

Any **five** of the following tests could be applied to determine whether Fred Fortune's sale proceeds will, on a balance of probabilities, be included or excluded from his gross income.

Subjective tests: (1)

- Intention at the time of acquisition: (1)
 - The property was purchased as a capital asset which would generate rental returns (1)
 - There is no evidence of a speculative intention. (1)
- Change of intention: (1)
 - Fred had no intention of selling the property prior to receiving the unexpected phone call offer. (1)
 - He did not embark on a profit-making scheme in order to sell the property. (1)
 - A taxpayer who simply sells a capital asset for the best possible price has not necessarily changed his intention and embarked on a profit-making scheme. (1)

Objective tests: (1)

- Activities of the taxpayer: (1)
 - Fred is a retired engineer, and does not appear to be a property speculator. (1)
- Period for which the asset is held: (1)
 - The property was held for a relatively short period, (1)
 - which could indicate that it was purchased for speculative purposes. (1)
- The manner of acquisition: (1)
 - Fred used his own funds to buy the property (1)
 - which would tend to indicate that the property was purchased as a capital investment (1)
- The manner of disposal: (1)
 - The offer to purchase by the Middle Eastern company was fortuitous. (1)
 - That would tend to indicate that it was disposed of as a capital investment. (1)
- Continuity: (1)
 - Fred has not repeatedly bought and sold properties. (1)
 - That would tend to indicate that it was a disposal of a capital investment. (1)

[Maximum 2 marks per 5 tests] – no extra marks for extra tests listed (max 5)

[Maximum 10 marks in total]

QUESTION 4 (continued)**Part B (8 marks)****Calculation of Calvin's taxable income for the year of assessment ended 28 February 2011**

	R	
Prize money – subject to s35 withholding tax, exempt (s10(1)(IA))	-	(1)
Interest – exempt (s10(1)(h))	-	(1)
Royalties – clubs designed in USA sold in SA, exempt (s10(1)(IA))	-	(1)
Net rental income	<u>150 000</u>	(1)
 Taxable income	 <u>150 000</u>	

b) **Calculation of withholding tax**

Withholding tax on prize money - R7 500 000 **(1)** x 15% **(1)** = R1 125 000

Withholding tax on royalties – R500 000 **(1)** x 12% **(1)** = R60 000

Part C (8 marks)

1. Farming income	FI	(1)
2. Other income	OI	(1)
3. Farm development expenditure	CDE	(1)
4. Other income	OI	(1)
5. Farm development expenditure	CDE	(1)
6. Other income	OI	(1)
7. Farm development expenditure	CDE	(1)
8. Farming income	FI	(1)

**ANNEXURE B: SOLUTIONS TO INTEGRATED QUESTIONS OF STUDY UNIT 11 IN
TUTORIAL LETTER 103/3/2011**

SOLUTION 11.1

1. (4) Only interest on loans used for business purposes will be deductible.
2. (2) Of the options only theft by managers or persons responsible for cash in business are not deductible
3. (2)
4. (5) The 45% is calculated as:
 $R500\,000 / (R7\,605 \times 12 \text{ months} \times 10 \text{ years}) = 55\%$
 If 55% is exempt from tax then: $100\% - 55\% = 45\%$ is taxable.
 The calculation is only done for 9 months in the current year of assessment as Carl only started receiving the annuity in June 2010.
5. (1)
6. (5)
7. (3)
8. (1) $R114\,000 \times (4\% - 0.22\%) \times 12 \text{ months}$
9. (3) $(R152\,800 - R57\,000) \times 18/100 \times 7/12$
10. (5) The determined value includes VAT for this purpose.

SOLUTION 11.2

PART A

** Note from the examiner:*

In this question all the information was given per month, it is therefore best to calculate balance of remuneration for a month and then to multiply by 12 only at the end. We have, however, supplied you with two alternative solutions, that you will see, arrive at the same answer.

	R	
Salary received	30 000	(1)
Travel allowance (R10 000 x 80% (1))	<u>8 000</u>	
Net remuneration	38 000	
<u>Less:</u> Pension fund contribution – R2 500		
Limited to the greater of		
7.5% x R30 000 (1) = R2 250; or		
R1 750/12 mnths = R146 (1) , therefore limit	<u>(2 250)</u>	(1)
Balance of remuneration	<u><u>35 750</u></u>	
Annual equivalent of balance of remuneration (R35 750 x 12 mnths (1))	<u><u>429 000</u></u>	

OR ALTERNATIVELY		
Salary received (R30 000 x 12 mnths (1))	360 000	(1)
Travel allowance (R10 000 x 12 mnths x 80%) (1)	<u>96 000</u>	
Net remuneration	456 000	
<u>Less:</u> Pension fund contribution – R2 500 x 12 mnths = R30 000		
Limited to the greater of		
7.5% x R360 000 (1) = R27 000; or		
R1 750 (1) , therefore limit	<u>(27 000)</u>	(1)
Balance of remuneration	<u><u>429 000</u></u>	

Tax on annual remuneration	114 050	(1)
<u>Less:</u> Primary rebate	<u>(10 260)</u>	(1)
T ₂	<u><u>103 790</u></u>	

SOLUTION 11.2 (continued)

	R	
Employees tax on net remuneration for the period (R103 790/12 mnths) (1)	<u>8 649</u>	
Net remuneration annual equivalent	429 000	
<u>Add: Annual payment (received in December)</u>	<u>20 000</u>	(1)
Total net remuneration annual equivalent	<u>449 000</u>	
Tax thereon	121 590	
<u>Less: Primary rebate</u>	<u>(10 260)</u>	
T ₁	<u>111 330</u>	
Tax on bonus (T ₁ -T ₂) (R111 330 – R103 790)	7 540	(1)
Tax on net remuneration	<u>8 649</u>	(1)
Total employees tax for December	<u>16 189</u>	

PART B

	R	R
Travel allowance - received		120 000
<u>Less: Business portion:</u>		
Cost per kilometre		
<u>Deemed cost</u>		
Value of car R450 000		
Fixed cost per kilometre <u>R116 012</u> * ¹ (1)		
35 000 km (1)	3,315	
Fuel cost	1,103 * ²	
Maintenance cost	<u>0,752</u>	
Cost per kilometer	<u>5,170</u>	
<u>Actual cost</u>		
Depreciation (Limited to R400 000 (1) over 7 years (1))	57 143	
Finance charges* ³	42 100	(1)
Fuel	28 000	(1)
Insurance premiums and license fees	9 600	(1)
Maintenance (all covered under a maintenance plan)	-	(1)
Total vehicle expenses	<u>136 843</u>	
Cost per kilometre	<u>R136 843</u>	
35 000km	R3,910	(1)
∴ Deemed cost per kilometre will be selected as this is the highest.		
∴ Business travelling expenses (20 000 km x R5,170)		<u>(103 400)</u> (1)
Amount to be included in income		<u>16 600</u>

SOLUTION 11.2 (continued)**Notes from the examiner:**

- *1 *When marking a travel allowance question we can see if the VAT has been included or excluded depending on the Fixed cost used.*
- *2 *By taking the amounts for fuel and maintenance from the tables and converting them straight away to Rands it means that all your figures are in Rands and can be easily added together – this is a personal choice, you can work in cents and convert the cost per tables to Rands after you have added the three costs together – your answer might differ by a couple of cents due to rounding BUT remember that we mark principles and not figures!!*
- *3 *The finance charges in this question are based on a loan of R350 000 (R450 000 – R100 000 deposit), therefore they do not need to be limited.*

SOLUTION 11.3

	R	R	
Salary		202 800	
Bonus		17 518	
Taxable foreign dividend	1 230		
<u>Less: exemption – limited to R3 700</u>	<u>(1 230)</u>	-	(1)
Taxable foreign interest	4 730		
<u>Less: exemption – limited to balance of (R3 700 – R1 230(1))</u>	<u>(2 470)</u>	2 260	
Taxable local interest	29 160		
<u>Less: exemption – limited (R22 300 – R3 700) (1)</u>	<u>(18 600)</u>	10 560	
Local dividends (exempt s 10(1)(k))		-	(1)
Travel allowance	42 750		
<u>Less: Travel deduction claimed against allowance</u>			
Value of vehicle (R275 000 + R38 500)	R313 500		
<u>Cost per kilometre:</u>			
Fixed cost per kilometre (R96 260(1)/24 365km (1) x 9/12(1))	R2,963		
Fuel cost per kilometre (from table)	R0,857		
Maintenance cost per kilometre (from table)	<u>R0,494</u>		
Total cost per kilometre	<u>R4,314</u>		
Business travel (10 500 km's x R4,314) (1) ltd to allowance received	<u>(42 750)</u>	-	(1)
Subsistence allowance received	2 248		
<u>Less: Deemed portion of the allowance (R276 x 8 days)</u>	<u>(2 208)</u>	40	(1)
Medical aid fringe benefit		12 000	(1)
Holiday accommodation – fringe benefit (R350 x 2 x 7 days) (1) + R200(1) + 0(1)		5 100	
Interest on bond (private)		-	(1)
Subtotal		<u>250 278</u>	

SOLUTION 11.3 (continued)

<u>Less:</u> Pension fund contributions	R	R	
Actual R16 224, limited to the greater of 7,5% x R202 800 (1) = R15 210; or R1 750, therefore limited to		(15 210)	(1)
<u>Less:</u> Arrears pension contribution, R2 000 limited to R1 800		<u>(1 800)</u>	(1)
		233 268	
<u>Less:</u> Donation – R15 000 limited to (R233 268 (1) x 10% = R23 327) therefore, allow in full.		<u>(15 000)</u>	(1)
		218 268	
<u>Less:</u> Medical contributions deduction			
Employee's medical contributions (R28 800 – R12 000)	16 800		(1)
Fringe benefit	<u>12 000</u>		(1)
	28 800		
limited to (R670 + R670 + R410) = R1 750 (1) x 12 mnths	<u>(21 000)</u>	<u>(21 000)</u>	(1)
	7 800	197 268	
Medical expenses			
Contributions not deducted above	7 800		(1)
Medical expenses not re-imbursed	<u>21 300</u>		(1)
	29 100		
As exceeds (7.5% x R197 268) (1)	<u>(14 795)</u>	<u>(14 305)</u>	(1)
TAXABLE INCOME		<u><u>182 963</u></u>	

SOLUTION 11.4**Calculation of taxable income**

	R	R
Salary		580 000
Travel allowance		
Deemed cost per km		
Fixed cost: (R76 041 (1) /29 200km (1) x 365/365 x 100c)	260.4c	
Fuel	81.5c	
Maintenance	<u>46.4c</u>	
Total cost per km	<u>388.3c</u>	
Actual cost per km	R	
Depreciation (R234 500/7 yrs x 12/12)	33 500	(1)
Fuel	30 700	(1)
Capital repayments	-	(1)
Insurance	16 900	(1)
Finance charges (R116 100/5 yrs)	<u>23 220</u>	(1)
Total vehicle expenses for the year	<u>104 320</u>	
Actual cost per km (R104 320/29 200km (1) x 100c)	<u>357.3c</u>	
The deemed cost per km will be selected as it is the highest (1)		
Allowance received	75 000	
Cost of business travel (388.3c/100c x 11 200km)	<u>(43 490)</u> (1)	31 510
Use of company car:		
R214 400 x 100/114 (1) x 4% (1) x 7 mnths (1)		52 660
Low interest loan: [R98 000 x (9.5% - 3.5%) (1) x 6/12] (1)	2 940	
[R98 000 x (8.5% - 3.5%) (1) x 6/12]	<u>2 450</u>	5 390
Foreign dividends	1 204	
<u>Less:</u> Exemption limited to maximum of R3 700	<u>(1 204)</u> (1)	-
Local interest	25 414	
<u>Less:</u> Exemption limited to (R22 300 – R1 204) (1)	<u>(21 096)</u>	4 318
Right of use of computer (R14 700 (1) x 15% (1) x 8/12) (1)		1 470
Receipt of complementary air tickets: no taxable benefit (destination in SA & employer in business of transporting passengers for reward)		- (1)
		<u>675 348</u>
<u>Less:</u> Income protection premiums (payout non-taxable)		<u>-</u> (1)
		675 348

SOLUTION 11.4 (continued)

Amount carried over	R 675 348	
<u>Less:</u> Retirement annuity contributions: R37 800 + R3 200 (1) = R41 000, limited to the greater of R1 750 ($\frac{1}{2}$) or R3 500 – 0 = R3 500 ($\frac{1}{2}$), or 15% x R675 348 (1) = R101 302 Therefore allow actual	(41 000)	(1)
	<u>634 348</u>	
<u>Less:</u> Medical expenses (handicapped family member – deduct in full)	(21 360)	(1)
	<u>612 988</u>	
<u>Taxable income</u>	<u>612 988</u>	