

Tax Professional EISA Examination

November 2016

Paper 2: Solution

PART A

Aspect of the answer	Details of aspects to be included in answer	Marks	Marks obtained by candidate
Format of letter	RTS address, SARS address, name of SARS official, date, taxpayer name, taxpayer reference number, case number, year of assessment/period.	2	
Layout of letter	Layout of letter is professional. Has an introduction that refers to the SARS audit letter of findings dated xxxx (attached as Annexure A). Uses headings/ or numbering where appropriate.	2	
Language used in letter	Clear and concise language, with the aim of clarifying client's responses to SARS and not to complicate matters further. Response should not be too technical as it is not a tax opinion, yet sufficiently technical to base views on authority and not expose advisor to risk	1	
Views in letter based on authority	No unfounded views or statements, reference to legislation, practice notes and case law where appropriate. However, where refer to authority, this reference is accurate and relevant	1	
Limitation of liability	In the letter (preferably at the end) or in a separate cover letter to the client, the advisor's limitation of liability should be provided. It must be clear that no audit was performed by the tax advisor on the information provided by the client and that management and the public officer takes responsibility for any information provided to SARS.	2	
		Available: 7 Max: 5	

No	Aspect of the answer	Marks	Candidate Mark obtained
1	Demonstration equipment		
	<i>Depreciation claimed on demonstration equipment in the 2014 tax year for which calculations, rulings, records and supporting invoices were requested in compliance with section 11(e) read with Interpretation Note 47 and for which nothing was received, are to be disallowed.</i>		
1.1	SARS audit finding		
	In the SARS letter of audit findings, SARS expresses the view that the company claimed depreciation amounting to R280 500 on the demonstration equipment in the 2014 tax year in terms of Section 11(e) of the Income Tax Act No.58 of 1962 (“the Act”). SARS also expresses the view that stock is usually accounted for in terms of Section 22(1) (a) of the Act at the lower of cost or the market value at year end.	0.5	
	SARS found that part of the stock on which depreciation was claimed, was sold in the 2015 tax year for more than the original cost of the demonstration stock. It appears that SARS is questioning the write off of stock to net realisable value when the item was in fact sold for more than its original cost.	1	
	SARS is proposing an adjustment of R280 500 for the 2014 tax year in respect of depreciation claimed on demonstration equipment that were still on hand at the end of 2014.	0.5	
1.2	Our response		
	We wish to clarify that demonstration equipment is classified as inventory (stock) in terms of IAS 2 for accounting purposes and disclosed accordingly in the annual financial statements of X-Diagnostic. It has always been management’s intention to sell demonstration equipment due the fact that the X-ray analytical equipment is very expensive to manufacture.	1	
	The description in the detailed income statement supporting the 2014 tax return incorrectly referred to “Depreciation on Demo equipment” and should have been more accurately worded as “Write off of demonstration stock”.	1	
	The write down of demonstration stock was correctly disclosed on the ITR14 tax return under the gross profit/loss sub-section of the Income Statement section.	1	
	The demonstration equipment was therefore treated for tax purposes in the 2014 tax return in terms of section 22(1)(a) of the Act at the lower of cost or market value at year end.	1	
	To motivate the tax deductibility of the demonstration equipment write-off, it is firstly important to explain the nature of the demonstration equipment. The demonstration equipment is analytical X-	1	

No	Aspect of the answer	Marks	Candidate Mark obtained
	ray instruments used mainly for industrial and scientific uses. Generally, the X-ray analytical equipment is ordered specifically for a client based on the client's requirements. Therefore, the X-ray equipment ordered is unique.		
	Due to the fact that clients have different, specific requirements for the X-ray analytical equipment and due to the fact that this type of equipment is large in size, X-Diagnostic does not keep stock on hand of these specialised instruments. The inventory on the balance sheet relates mainly to spare parts for the equipment sold and demonstration equipment.	1	
	The specialised X-ray analytical equipment consists of hardware (including computer hardware such as PC and printer components) and computer software components.	1	
	<p>X-Diagnostic writes off the demonstration stock over 3 years for accounting and tax purposes. This is in accordance with the Group Instruction received. Please refer to the Memo received from Diagnostic Group PLC (attached as Annexure B) which confirms the group policy. The 3-year basis over which X-Diagnostic devalues the demonstration stock is based on the fact that:</p> <ul style="list-style-type: none"> • Technology development and enhancements (especially on the computer software) of the X-ray analytical equipment results in the demonstration equipment being out dated after 3 years; • Demonstration stock is frequently moved between customer sites for demonstration purposes and therefore deteriorates rapidly. 	2	
	Please also refer to Annexure C which provides proof as to how the write down of the demonstration stock for the 2014 tax year was calculated.	1	
	Should SARS wish to refer to Interpretation Note 47 for guidance on write off periods, we wish to again highlight that the X-ray analytical equipment in question is unique and consists of hardware and software components. The write off period of 5 years for X-ray equipment as recommended by Interpretation Note 47 is therefore not suitable for the specialised X-ray analytical equipment that X-Diagnostic sells. A write off period as recommended by the group accounting policy of 3 years is therefore more appropriate for this type of equipment.	3	
	The demonstration stock disposed of in 2015 should be seen in isolation. As mentioned above, X-Diagnostic does not keep stock on hand of the specialised X-ray equipment. This specific item was acquired by X-Diagnostic as demonstration stock in 2014 and was used in a demonstration to SteelCo. Limited. Normally an order would be placed for the X-ray analytical equipment which is then imported from the United Kingdom. This would mean that there is a lead time before delivery		

No	Aspect of the answer	Marks	Candidate Mark obtained
	can take place. The specific demonstration analytical X-ray equipment met the specifications of SteelCo. Limited and to ensure immediate delivery, SteelCo. Limited agreed to acquire the demonstration X-ray analytical equipment. The profit on the sale of the demonstration equipment to SteelCo., including the gain above the original cost, was treated as a revenue gain in the tax calculation and not a capital gain, which also confirms that the demonstration equipment is stock and not a capital asset for tax purposes.	3	
	Based on the above it is respectfully submitted that no adjustment is made for tax purposes in respect of the write down of demonstration stock raised for accounting purposes as we believe there is reasonable justification in terms of section 22 and Practice Note 36 of the Act for X-Diagnostic to write off demonstration equipment over 3 years as supported by the trading history gathered by the Diagnostic Group and the estimation provided.	3	
		<u>Available: 21</u> Max: 15	
2	Penalties claimed as a tax deduction		
	<i>Penalties claimed should be disallowed for Income Tax purposes</i>		
2.1	SARS audit finding		
	SARS is proposing to raise an additional assessment for R1 300 in respect of CIPC penalties.	1	
2.2	Our response		
	Due to the small amount concerned, X-Diagnostic decided to concede to SARS's proposal. Or In terms of section 23(o) of the Act, no deduction will be allowed from taxable income in respect of any expense which constitute a fine or penalty imposed as a result of an unlawful activity in South Africa. A fine was imposed by the CIPC in terms of section 216 of the Companies Act, 2008. Therefore, it is correct to disallow the R1 300 penalty paid by X-Diagnostic to the CIPC.	1	
		<u>Available: 2</u> Max: 2	

No	Aspect of the answer	Marks	Candidate Mark obtained
3	Rotating stock tube provision		
	<i>Rotating stock tube provision claimed in the 2014 tax year for which the sale of the tubes kept on behalf of the customer were not proven to have been included in income of the company in the 2014 and prior tax years</i>		
3.1	SARS audit finding		
	SARS is seeking to disallow the deduction of the rotating stock tube provision of R1 400 513 in the 2014 tax year.	1	
3.2	Our response		
	The rotating stock tube scheme is an <u>agreement</u> where the customer purchases a replacement tube from X-Diagnostic however it is only delivered to the customer when required. It can be several years before it is despatched. Money is therefore <u>received in advance</u> by customers.	2	
	X-Diagnostic only keeps one tube in stock for several rotating stock customers as these tubes have a limited lifespan. When a customer requires a tube, X-Diagnostic releases the tube they have in stock and orders a new tube from the United Kingdom.	1	
	When a customer purchases X-ray equipment, it is not always possible to split the sale price between equipment and replacement tube. The accounting entries are as follow: Dr Bank Cr Sales (for full invoice value including replacement tube) <u>Sale of X-ray equipment and replacement tube</u> Dr Cost of sales Cr X-ray equipment stock Cr Rotating stock tube provision (at cost value) <u>Recording of x-ray equipment sale and providing for future tube expense</u>	1	
	The cash received for the rotating stock tubes was therefore included in income and taxed in full in the year of receipt.	1	
	It may be possible to argue that X-Diagnostic actually incurred the expense for the tube at the time that the agreement was entered and the customer paid on the basis that X-Diagnostic had an unconditional liability to provide the client with a tube (section 11(a)).	1	

No	Aspect of the answer	Marks	Candidate Mark obtained
	(Also refer to the <i>Ackermans</i> case that explains actually incurred includes the ‘undertaking of an obligation to pay’)		
	<p>Even if SARS seeks to add back the Rotating stock tube provision as non-deductible, X-Diagnostic would have been entitled to claim a section 24C allowance (read with SARS Interpretation Note 78) equal to the Rotating stock tube provision as the income was received in advance in terms of a contract with the client whereby X-Diagnostic will have to incur future expenditure to provide the client with a replacement tube. X-Diagnostic is able to link a replacement tube acquired to a specific client agreement.</p> <p>[The stock tube on hand cannot be linked to a specific contract. If it could be linked, then section 24 C would not have been available as no further expenditure will be incurred.]</p>	3	
	Based on the above it is respectfully submitted that no adjustment is made for tax purposes in respect of the rotating stock tube provision raised for accounting purposes as we believe there is reasonable justification in terms of section 11(a) or section 24C of the Act for X-Diagnostic to claim a deduction/allowance equal to the rotating stock tube provision.	2	
		Available: 12 Max: 12	
4.	Burden of proof		
	<p>In terms of section 102 of the TAA, the burden of proof that an amount, transaction, event or items is exempt, taxable, deductible or correctly valued, lies with the taxpayer.</p> <p>Based on our responses above, we believe that we have provided sufficient proof to SARS that:</p> <ul style="list-style-type: none"> • The write down of demonstration equipment should be allowed as a tax deduction in terms of section 22(1)(a) of the Act • The penalty should be disallowed as a tax deduction in terms of section 23(o) of the Act • The provision for rotating stock tube provision should be allowed as a deduction in terms of section 11(a) or alternatively section 24C of the Act <p>Should SARS require additional information, please do not hesitate to contact us on e.g. taxmanager@rts.co.za</p>	2	

No	Aspect of the answer	Marks	Candidate Mark obtained
5.	Understatement penalty		
	<p>Section 222 of the TAA states that in event of an ‘understatement’ a taxpayer must pay, in addition to the tax payable for the relevant tax period, the understatement penalty as determined per the table in section 223, unless the ‘understatement’ results from a bona fide inadvertent error. ‘Understatement’ per section 221 of the TAA means any prejudice to SARS or the fiscus as a result of</p> <ul style="list-style-type: none"> • A default in rendering a return • An omission from a return • An incorrect statement in a return or • If no return is required, the failure to pay the correct amount of tax <p>Based on the responses provided above, no default exists in our opinion in respect of the write-off of demonstration equipment and the claiming of the rotating stock tube provision as we are of the view that the statements provided in the 2014 tax return were correct and no omissions were made. The non-add back of the penalties was a bona fide inadvertent error made by X-Diagnostic. We therefore respectfully request that SARS do not levy the understatement penalty</p>	3	
		<u>Available: 5</u> Max: 3	
	AVAILABLE	47	
	MAX	40	

No	Aspect of the answer	Marks	Candidate Mark obtained
ELO	Competency Evaluation		
<i>ELO 3</i> <i>ELO 4</i>	<i>Mediate tax disputes related to income tax, payroll taxes and VAT</i> <i>Write tax opinions</i>		
	<p>A score of 50% indicates that the candidate is able to: Review the SARS audit letter of findings; Review the information provided by the client; Identify whether the SARS audit findings are correct or not; Respond to the SARS audit letter of findings in accordance with the Tax Administration Act; Provide responses that clearly set out the SARS audit finding and the correct tax treatment based on the application of the correct legislative reference and/or supporting documents provided by the client</p>		

PART B.1

X-Diagnostic (Pty) Ltd

Income tax reference

number:6419/923/49/6

Year of assessment ended

31 December 2015

Tax reasonability test

Tax Adjustment Description	Sch	Tax Reasonability Calculation	Client's tax calculation	Difference	Comments	Marks	Mark obtained
Net profit per financial statements		7 441 067	7 441 067	-	Agreed to AFS	1	
Add:							
Depreciation		151 626	151 626	-	Agreed to AFS	1	
Repairs and maintenance			-	-	Detail required of repairs and maintenance to identify any capital items (s11(a))	1	
Recoupment on Sale of Asset			-	-	Error in AFS Note 1: plant and equipment. It appears that assets were disposed with a cost and accumulated depreciation of R377 585. Require detail of assets disposed and proceeds to determine any recoupment/scraping allowance	1	
Income in advance - Prepayments received		13 899 040	15 938 115	(2 039 075)	A detail breakdown is required for the deferred income (R1 391 740) and debtors with credit balances (R12 507 300). Adjustment = R1 391 740 + R12 507 300. Amounts received in advance should be added in the tax computation into gross income definition.	2	

Unrealised foreign exchange difference -related parties	P/Y	-	11 570	(11 570)	Require 2014 tax return calculation to confirm amount. Section 24I(10) was deleted and replaced by section 24I(10A) effective from 1 Jan 2014. Deferral of exchange difference now only applicable to non-current assets/liabilities. It appears that all exchange items will realise within 12 months, therefore no deferral of exchange items. [Consider requesting a correction of 2014 tax return and/or VDP]	2
Doubtful debts allowance - 2014	P/Y	137 761	137 761	-	Require 2014 tax return to confirm amount. [See comment below in respect of section 11(j) doubtful debt allowance]	1
Section 24C allowance - 2014	P/Y	4 825 679	4 825 679	-	Require 2014 tax return to confirm amount. Net of income received in advance and sec24C allowance do not agree to 2014 deferred tax asset for income received in advance	2
Prepayment - 2014	P/Y	62 736	62 732	4	Agreed to 2014 deferred tax asset for prepayments. Difference not material	1
Deduct:			-	-		
Profit on Sale of Asset		-	-	-	Assets with a carrying value of Rnil (cost and acc depreciation of R377 585) were disposed. Require detail on assets disposed and proceeds	1
Unrealised foreign exchange difference - related parties		-	(212 924)	212 924	Foreign exchange differences relate to current assets/liabilities, therefore no deferral ito section 24I(10A) effective from 1 Jan 2014	1
Wear and tear on fixed assets	1	(400 221)	(400 221)	-	Require detail tax asset register. It appears that no apportionment is done. Furniture and fittings are written off over 5 years instead of 6 years per IN47	2

				Tax adjustment for the different provisions are shown separately below. The provision on which the deferred tax asset (current and prior year) was created differ from the tax return sch2. Also provisions (excluding provision for bad debt) per schedule 2 do not agree with the provisions per note 5 of the AFS. Detail of provisions per the AFS should be obtained. [The client's adjustment for provision in the tax calculation currently do not include provision for bad debt]		
Decrease in provisions	2	-	(691 080)	691 080		2
Prior year provisions		(5 224 808)		(5 224 808)	If 2014 tax return is re-opened, reconsider whether sundry accruals and stock write off provision may qualify for a deduction	1
Bad debt provision - current year		451 691		451 691	Agreed to Note 3 of AFS. Correct to add back provision ito section 11(a) and 23(g). Effectively movement in provision is claimed in terms of section 11(i)	1
Bonus provision - current year		550 000		550 000	Agreed to Schedule 2 Provisions. Correct to add back in terms of section 7B variable remuneration	1
Leave pay provision - current year		234 001		234 001	Agreed to Schedule 2 Provisions. Correct to add back in terms of section 7B variable remuneration	1
Warranty provision - current year		575 119		575 119	Agreed to Schedule 2 Provisions. Correct to add back as X-Diagnostic does not have an unconditional liability to pay yet (no accrual in terms of section 11(a)).	1
Stock write off provision - current year		2 425 718		2 425 718	Require more information on calculation of estimate. If comply with section 22 (1) & Practise note 36, then no adjustment is required for provision	1
Sundry accruals		-		-	Obtain detail list of accruals. If X-Diagnostic had an unconditional liability at year end to pay the accrual, then it can be argued that it is deductible ito 11(a)	1

Prepayment - 2015	(114 243)	(114 242)	(1)	Agree to prepayments as per deferred tax asset in AFS. Require a detail breakdown of prepayments to verify if it meets the requirements of section 23H (will be incurred within 6 months after year end and balance of total prepayments less than R100 000)	1	
Doubtful debts allowance - 2015	-	(99 055)	99 055	A list of doubtful debtors need to be provided with reasons why debtor is doubtful and steps taken to try and recover outstanding monies. Doubtful debt allowance may only be claimed on specific doubtful debtors.	2	
Section 24C allowance - 2015	(8 339 424)	(9 562 869)	1 223 445	Require detail of contracts, income received in advance per contract, estimated gross profit margin/expected future expenditure per contract in order to calculate s24C allowance. For reasonability test accepted 60% cost percentage as used by client in tax calculation: R13 899 040 * 60% = R8 339 424	2	
Income in advance - Prepayments received - 2014	P/Y (8 949 098)	(8 949 098)	-	Require 2014 tax return to confirm amount. Net of income received in advance and sec24C allowance do not agree to 2014 deferred tax asset for income received in advance	1	
Other						
Goodwill	-	-	-	No movement in balance, therefore no adjustment required. Normally will reverse any movement on goodwill as it is capital in nature	1	
Loans to/from group companies	-	-	-	Transfer pricing needs to be considered. More information is required on transactions with foreign connected parties	1	

Taxable income/(loss) [including capital gains]		7 726 644	8 539 061	(812 417)	1
Tax @ 28% of	=	2 163 460	2 390 937	(227 477)	1
					35
					30

AVAILABLE
MAXIMUM

ELO	COMPETENCY EVALUATION
ELO 1 & 2	Calculate a tax liability Review tax balances
	<p>A score of 50% indicates that the candidate is able to:</p> <ul style="list-style-type: none"> Prepare an income tax calculation from information provided by the client; Review a client's calculation and identify incorrect or missing tax adjustments; Identify where additional information is required to determine a tax adjustment accurately; Analyse information from financial statements and identify tax risks and potential errors;

PART B.2

RTS Incorporated

Client: X-Diagnostic (Pty) Ltd ("X-Diagnostic")

To: Hillary Millar+B3

From: RTS Tax Manager

Date: 25 November 2016

Memorandum in respect of high level tax review

Scope of assistance

We have performed a high-level review of X-Diagnostic's tax calculation for purposes of the ITR14 tax return for the 2015 tax year of assessment

Limitation of liability

Review is based on information provided

No audit was performed on the information provided

Management, and in particular the Public Officer, is responsible for the completeness and accuracy of the information

Language and layout

Clear language, not too technical as the memo is addressed to the financial manager

Layout needs to be professional and uncomplicated

Available
Maximum

Marks	Marks obtained
1	
1	
1	
1	
1	
1	
7	
5	

Number	Tax Issue Identified	Recommendation		
1	<p>Disposal of assets: The cost of the plant and equipment as per note 1 to the AFS from 2014 to 2015 does not reconcile. It appears that PPE with a cost of R377 585 and accumulated depreciation of R377 585 has been disposed of.</p>	<p>Detail of assets disposed are required as well as the amount of proceeds in order to calculate the accounting profit/loss, recoupment/scraping and/or capital gain/loss.</p>	2	
2	<p>Fixed Asset allowances: For accounting purposes, furniture and fittings are written off over 5 years whereas Interpretation Note 47 require a 6 year write off period. It is therefore expected that a deferred tax asset should be recognised, however in note 2 of the AFS no deferred tax asset was raised in respect of plant and equipment. A detail fixed asset register was not provided. There is a risk that the wear and tear allowances on fixed assets were not calculated correctly in terms of the Act and Interpretation Not 47.</p>	<p>The accounting and tax fixed asset register should be reviewed to ensure that the correct write off period is used per asset and that wear and tear allowance is calculated correctly. The wear and tear allowance should be apportioned if the asset is not used for the full year. The deferred tax calculation should be reviewed and updated.</p>	2	
3	<p>Unrealised foreign exchange differences: Based on the tax calculation provided, it appears that an adjustment for unrealised foreign exchange differences were made in the 2014 tax return. Section 24I(10) was deleted and replaced by section 24I(10A) effective from 1 Jan 2014. Deferral of exchange difference now only applicable to non-current assets/liabilities. It appears that all exchange items will realise within 12 months, therefore no deferral of exchange items required in the 2014 and 2015 tax returns.</p>	<p>Consider requesting a correction of 2014 tax return and/or Voluntary Disclosure in respect of the 2014 tax year (however the amount concerned may not be material and it appears that understatement is more a bona fide inadvertent error). In respect of the 2015 tax year, foreign exchange differences do not need to be deferred if it relates to current assets or current liabilities.</p>	2	

4	<p>Advertising, promotions and marketing expenses: There is a risk that the amount of R291 011 include expenses that may create an enduring benefit and that are therefore of a capital nature and not deductible in terms of section 11(a) of the Act.</p>	<p>Detail required to assess if any items of a capital nature are included relating to advertising expenses. If the advertising expense will create an enduring benefit, the amounts should be capitalised. A section 11(e) allowance may potentially be available.</p>	1	
5	<p>Discounts allowed: Possible input tax not claimed on discounts allowed</p>	<p>Enquire as to the VAT treatment of discounts allowed and ensure that input tax is claimed where output tax was previously paid on a sales invoice but a discount has now been provided</p>	2	
6	<p>Debt collection cost: Debt collection cost of R190 163 may potentially include cost incurred to recover staff loans.</p>	<p>A detail breakdown of debt collection cost should be provided to assess if there are any legal fees of a capital nature included in this total, or legal fees relating to the debt collection of staff loans which is not in the production of income</p>	1	
7	<p>Entertainment expenses: There is a risk that input tax has been claimed on entertainment expenses</p>	<p>Review entertainment expenses and ensure that no input tax has been claimed on these expenses</p>	1	
8	<p>Legal fees: Legal fees of R25 130 may include expenses of a capital nature which are not deductible in terms of section 11(a) of the Act.</p>	<p>A detail breakdown of debt collection cost should be provided to assess if there are any legal fees of a capital nature included in this total</p>	1	
9	<p>Motor vehicle expenses: Motor vehicle expenses of R275 326 may include expenses of a capital nature which are not deductible in terms of section 11(a) of the Act. Motor vehicle expenses could also include reimbursive travel which should be reported on the employees' IRP5 certificates under the correct IRP5 code.</p>	<p>The detail of motor vehicle expenses should be reviewed to assess if there any expenses of a capital nature. A possible section 11(e) allowance may be available. Furthermore, if this expense includes reimbursive travel expenses, the correct treatment for PAYE and IRP5 certificate purposes should be considered.</p>	2	

10	ITC Infrastructure: The amount of R264 685 may include expenses of a capital nature which are not deductible in terms of section 11(a) of the Act.	The detail of ITC infrastructure expenses should be reviewed to determine if there are any expenses of a capital nature that should be capitalised for tax purposes. A section 11(e) allowance may be available for certain non-permanent assets	1	
11	Repairs and maintenance: Could potentially include amounts of a capital nature.	A detail breakdown of repairs and maintenance to the amount of R44 049 should be provided to assess if there are any expenses of a capital nature that should be capitalised for tax purposes. A section 11(e) allowance may be available for non-permanent assets	1	
12	Small Assets: Small assets with a value of above R7 000 should be capitalised.	A detail breakdown of small assets expensed should be reviewed to ensure that no small assets with a value above R7000 were expensed. Small assets with a value more than R7000 should be capitalised for tax purposes and a possible s11(e) allowance may be available	1	
13	Overseas Travel: The overseas travel of R573 563 may include amounts of a capital nature or costs relating to spouses that accompanied staff on travel which costs are not in the production of income of the company and not deductible in terms of section 11(a) of the Act.	A detail breakdown of overseas travel should be prepared that set out who travelled, when, where, and the reason for travel. Any travel of a capital nature (e.g. to purchase capital assets) or that relates to spouses of staff members, should be disallowed for tax purposes. Consider any fringe benefit tax on travel expenses incurred in relation to spouses of staff members.	1	

14	<p>Income received in advance: The amount of income received in advance added to taxable income could not be agreed to the deferred income and debtors with credit balances per the AFS or the deferred tax balance raised on income received in advance. There is a risk that not all income received or accrued per the gross income definition is included in taxable income.</p>	<p>A detail breakdown is required for the deferred income (R1 391 740) and debtors with credit balances (R12 507 300). Amounts received in advance should be added in the tax computation. A section 24C allowance may be available for income received in advance in terms of a contract for which future expenditure will be incurred. To calculate the section 24C allowance, the future expected expense must be estimate or the expected gross profit margin for the contract needs to be supported. Furthermore, we require an understanding of the accounting basis on which the deferred income was raised. If it relates to invoices raised in advance and X-Diagnostic is not unconditionally entitled to the money, the deferred income need not be included in gross income. A tax opinion might be necessary to assess the tax treatment of the deferred income.</p>	5	
15	<p>Doubtful debt allowance: A doubtful debt allowance of 25% on the provision for doubtful debt (excluding VAT) was claimed in the tax calculation. However, no detail breakdown of the specific doubtful debtors was provided. Doubtful debt allowance may only be claimed on specific doubtful debtors. There is a risk that SARS may disallow the doubtful debt allowance.</p>	<p>A list of doubtful debtors need to be provided with reasons why doubtful and steps taken to try and recover outstanding monies</p>	2	
16	<p>Prepayments: Prepayments were agreed to the balance on which a deferred tax asset was raised in AFS. There is a risk that no tax deduction may be claimed for prepayments in terms of section 23H of the Act.</p>	<p>Require a detail breakdown of prepayments to verify if it meets the requirements of section 23H (will be incurred within 6 months after year end or total prepayments less than R100 000)</p>	2	

17	<p>Provisions: The total provisions (excluding provision for bad debt and warranty provision) per tax schedule 2, do not agree to the provisions total as per note 5 of the AFS. Furthermore, the balance on which the deferred tax asset was raised in respect of provisions, also does not agree to the provision total per tax schedule 2.</p>	<p>A detail breakdown of provisions as per the AFS should be obtained. Tax schedule 2 and potentially the tax calculation, will have to be updated before submission of the tax return to ensure that the correct provision balances are adjusted for.</p>	3	
18	<p>Stock write-off provision: Stock write-off provision is added back in client's calculation. If the stock write-off provision complies with section 22(1) and Practise note 36, then no adjustment is required for the provision</p>	<p>Require more information on calculation of estimate as well as breakdown. If this provision includes the "depreciation of demo equipment" as explained to SARS in the response letter, then no adjustment in respect of the write off of demo equipment is needed.</p>	2	
19	<p>Sundry accruals are added back in client's tax calculation. There may be an opportunity to allow a tax deduction of the sundry accruals.</p>	<p>A detail list of accruals is required. If X-Diagnostic had an unconditional liability at year end to pay the accruals, then it can be argued that it is deductible in terms of 11(a) of the Act.</p>	2	
20	<p>Loans to and from group companies: Transactions with connected parties may require tax adjustments to be made.</p>	<p>Transfer pricing needs to be considered in respect of transaction with foreign connected parties. We recommend a transfer pricing review.</p>	2	

AVAILABLE

36

MAXIMUM

25

ELO	COMPETENCY EVALUATION
<i>ELO 2 & 4</i>	<i>Review tax balances Write tax opinions</i>
	<p>A score of 50% indicates that the candidate is able to: Review information provided by a client on a multi-disciplinary basis (e.g. accounting treatment, income tax, VAT and employees' tax); Identify tax risks or potential tax risks and provide recommendations or procedures to address tax risks/potential tax risks; Identify where additional information is required to assess whether a tax issue exist; Identify tax opportunities; Draft a memorandum to a client that sets out the tax issues identified and the recommendations or procedures to address tax issues; Support the tax issue identified with the correct tax legislative reference;</p>