

Tax Professional

Knowledge Competency Assessment

November 2015

Paper 2

Instructions to Candidates

1. This competency assessment paper consists of four questions.
2. Answer each question in a separate answer book.

Question	Topic	Marks	Answer Book
1	Individual Share Scheme	40	Blue
2	Estate Planning	40	White
3	Taxation of Farmers	40	Pink
4	Other taxes and Tax Administration	40	Green

Total marks: 160 Marks

Time: 4 hours plus ½ hour reading time

The marks specified are an indication of the expected length and detail of your response.

3. Enter your examination number on the cover of each answer book as well as on all answer sheets.
4. Your name must not appear anywhere in the answer books.
5. Answers may not be written in pencil and correction pens (Tipp-ex) may not be used.
6. Answer the questions using effective presentation and pay particular attention to the use of concise language, clarity of explanation and logical argument. Marks will be awarded for these aspects of your response.
7. It is your responsibility to ensure that all answer books are handed in to the invigilator before leaving the examination room, as answer books handed in thereafter will not be marked.

Question 1

40 Marks

Individual Share Scheme

Bruno von Falk works as head of operations at Suite Francaise (Pty) Ltd ('SF'), a South African based company that imports luxury goods from France and is a registered VAT vendor. He is a 66 years old German, who immigrated to South African during 2002. He is married (out of community of property) to Lucille and has two minor children, Celine and Klaus.

In the current tax year, Bruno received a salary of R22 000 per month. He also received a bonus of R25 000 in December 2014. Bruno contributed eight percent of his salary towards the company's pension fund. In addition, Bruno contributes R5 000 a month into a retirement annuity fund (RAF).

Bruno contributed to a medical aid fund. He paid R3 200 per month to cover himself and his three dependants. During the current year Lucille had to have extensive psychological counselling. This cost was not covered by the medical aid and came to an additional R36 000 for the tax year. Klaus also required extensive plastic surgery to clear his nasal passages as he was continually whining. This cost of R18 000 was also paid for by Bruno as it was not covered by his medical aid.

Bruno used his 2012 VW Jetta for private and business use. The car had a cash cost of R168 000 (including VAT) on 1 June 2012. He financed the car over five years and pays finance costs of R1 400 per month (relating to the interest portion only). The company gave Bruno a car allowance of R6 000 per month to compensate him. He travelled 38 000 kilometres in the tax year, 12 000 of which were private. He kept an accurate logbook, and paid for all maintenance on the car. During the year he replaced the tyres, and had two services. The tyres cost R4 560 (including VAT) and the services cost R1 140 in total (including VAT). During the year he also paid R24 000 for all petrol. Bruno maintained proof of all his expenditure.

Bruno was given a cell phone allowance of R400 per month. He had no itemised billing on his cell phone so could not prove any business calls.

The company bought two books in the year which they gave to Bruno. The first was 'Love and War' which cost R228 (including VAT). The other was 'Become a composer'

Bruno had the use of a company unit at the Angellier Villa in Franschhoek for the summer vacation. The unit was donated to the company, and they pay a levy of R2 400 per year. The unit is normally let out to the public for R6 500 per week. Bruno used it for one full week i.e. seven days in the year. He also used the company boat which was anchored at the villa's private lake. The boat had a market value of R340 000 (excluding VAT) when Bruno used the boat for the week he was in Franschhoek. The company had acquired the boat for R350 000 (excluding VAT) on 1 October 2013.

The company also gave Bruno a loan of R200 000 for the period 1 March 2014 to 1 October 2014. The loan was repaid on 1 October 2014. The loan was secured and interest of five percent was charged. You may assume the official rate was ten percent throughout the loan period.

The company expected Bruno to entertain certain guests. He was given an entertainment allowance of R1 200 for the year and was not required to account for this expenditure to SF.

Bruno was given the use of a house by the company from 1 June 2014, as the company required Bruno to be available near the company's main warehouse in Cape Town. Bruno moved into the company house on 1 June 2014. The house had three bedrooms, a lounge, kitchen, dining room and two bathrooms. The company paid all electricity and water bills, and furnished the house. The house was owned by the company. Bruno's remuneration proxy is R337 600.

During the year Bruno saved a farmer, Mr Benoit, from a tractor accident near Stellenbosch. Bruno was hailed as a hero and SF bought Bruno a flat-screen TV as a way of recognising his bravery and the positive press from his actions. The TV cost R11 400 (including VAT).

Bruno had recently invested some money offshore. For the current tax year he received interest R1 000 from the UK, and dividends of R3 000 from investments in Germany. These were listed investments and the dividends received are not exempt under section 10B(2).

Only in respect of part (b) of the Required section.

Lucille is an established painter and sells her paintings at local markets over weekends. On 1 February 2015, her accountant estimated her taxable income at R190 000 in respect of the 2015 year of assessment. She wants to reduce her tax liability, and at the same time, do some good for the community. Consequently, she has decided to make a donation to the Madeleine Foundation, a registered public benefit organisation, on 15 February 2015. The foundation will issue her with a valid section 18A receipt. Lucille must choose between donating cash of R30 000 or some of her paint equipment (e.g. paint brushes, easels and paint), valued at R29 000 on 15 February 2015. The equipment had cost her R34 000 when she purchased them a few months before and they have not yet been used by her.

Note: in terms of Binding General Ruling No 7, passenger cars have a write-off period of five years.

REQUIRED		Marks
Show all your calculations and round off to the nearest Rand. You need not discuss any case law or provide references to the Income Tax Act.		
a)	<p>Calculate Bruno von Falk's normal tax liability in respect of the 2015 year of assessment. Your answer must be in the correct format in which all items are indicated separately in the framework applicable to natural persons.</p> <p>Specifically indicate if an item does not qualify for an exemption or a deduction, as well as if no reduction is allowed against a fringe benefit or an allowance, and provide a brief reason.</p> <p>Effective communication and lay-out.</p>	<p>34</p> <p>1</p>
b)	Briefly advise Lucille as to which option she must choose in respect of the donation to the Madeleine Foundation. You must provide short reasons and calculations in support of your answer. Restrict your answer to a taxation point of view only (i.e. not a cash-flow consideration).	5
TOTAL MARKS		40

Question 2

40 Marks

Estate Planning

You are a registered tax practitioner at a well-established auditing and accounting firm in Pretoria. The firm has offices all over South Africa. As a senior estate specialist you are regularly consulted on administrative as well as tax matters relating to deceased and insolvent estates.

The following is an extract from an e-mail which you have recently received from Anzelle Foreza, a colleague at the firm's Port Elizabeth office.

"I have been appointed as the executor in the deceased estate of one of my late clients, Judy Jackson. Judy was born on 21 January 1940 and has been married to Shane Jackson for the past 35 years. Both Judy and Shane have always been residents of South Africa. Judy has never been a VAT vendor and all the amounts referred to below include VAT where applicable.

I have almost completed all my duties as executor in the estate but still need to address some of the income tax and estate duty aspects of the estate. I have compiled the liquidation section of the executor's account but need to fill in the relevant tax liabilities before I can proceed with the rest of the account.

Attached to this e-mail is **attachment 1**, which is the liquidation account so far.

The following additional information (with reference to the respective voucher numbers reflected on the account) should be relevant to the tax calculations:

IP1: This property was purchased by Judy in 2005 for R3 200 000. It has always been used exclusively as a primary residence by Judy and Shane. Its market value on 30 April 2015 was R6 100 000.

IP2: Judy purchased these residential units in an apartment complex in July 2006 at a total cost of R500 000 each and has leased them out to tenants ever since. Judy's daughter, Annah (a South African resident), inherits these residential units and will continue renting them out to the existing tenants. As Annah was always aware of the fact that she would inherit the apartments from her mother, she built an additional patio onto each of the apartments in 2010 at a total cost of R10 000 for each patio. She made these improvements with Judy's knowledge and approval and the patios are still a part of each apartment at the date of Judy's death. Annah did not pay any donations tax on the improvements made to the apartments. The market value of the apartments amounted to R800 000 each on 30 April 2015, with R20 000 of that value attributable to the patio that has been added.

Judy received rent of R8 000 per month per apartment. The rent has remained unchanged at this amount for the past two years. The only expenses incurred in respect of the apartments are property rates and taxes amounting to R500 per apartment per month. All other costs relating to the apartments are paid by the tenants.

The apartments have qualified for the section 13sex income tax allowance since Judy purchased them in November 2008.

IP3: Judy purchased this property in 2003 for R2 900 000. Judy's daughter, Annah, has been farming with cattle on this property for the past two years and will continue to do so after her mother's death and inheriting the property. Annah has not effected any improvements to this property.

MP1: The total cost of these assets (all purchased during 2004) amounted to R665 000. None of these assets have ever been used for business purposes.

MP2: The motor vehicle was purchased in 2014 for R687 000. Its market value on 30 April 2015 was R600 000 but it could only fetch R590 000 at auction. Judy always used this vehicle for private purposes only.

CF1: Judy owned 50% of the equity shares in Polifin (Pty) Ltd, a company which she started in 2009 with Sue Dos Santos, her friend. The company provides start-up capital to new small businesses. Judy and Sue each contributed share capital of R1 000 to the company in exchange for their shares. In terms of a buy-and-sell agreement Judy's shares were sold to Sue at 20% below market value.

Additional information:

The following information relates to aspects of the estate not reflected in the liquidation account so far:

1. Annah had taken out a life insurance policy with ICU Insurers Ltd on her mother's life in 2004. The policy paid out R3 500 000 to Annah on 12 May 2015. Annah had an agreement with Judy in terms of which Judy paid 60% of the premiums on the policy and Annah the other 40%. The total premiums (including interest at 6%) on the policy since inception amounted to R120 000.
2. Judy and Shane have a son, Timothy, who immigrated to Spain in 2008 and who has been a resident of Spain ever since. Timothy stays in a villa in Spain which belonged to Judy and which she purchased in 2006 for R1 200 000. The villa is bequeathed to Timothy and had a market value of R2 200 000 on 30 April 2015. No death taxes were paid in Spain in respect of the villa. Judy owed R50 000 to a bank in Spain in respect of a loan that she took out to provide financial assistance to Timothy in 2013.
3. During 2013 Judy created the Jackson Family Trust, a South African trust, to which she donated cash of R2 000 000. The trust used the cash to purchase a commercial property which produces net rental of R20 000 per month. The trustees of the trust are Judy, Shane and Annah with Judy, Shane, Annah and Timothy as beneficiaries of the trust. The trustees can distribute income or capital of the trust in their discretion, but such a distribution has to be approved

by at least two trustees. The trustees distributed the R20 000 rent received during March 2015 in equal portions to the beneficiaries on 10 April 2015.

4. Judy had no assessed loss or assessed capital loss from 2014 and has sold no capital assets during 2015. She had no income other than that which is evident from the abovementioned information.
5. Three years ago Judy promised Sue that she (Sue) could have Judy's beautiful diamond necklace the day that Judy died. At the date of Judy's death the necklace was worth R110 000 and Judy's family made sure that the necklace was given to Sue.
6. All the cash left in the estate is bequeathed to Judy's local church (not a registered PBO) in terms of her valid will.

I need some assistance with completing the missing amounts and sections of the executor's accounts in this estate. Could you please help me with the following:

1. Calculation of the outstanding income tax liabilities in the estate.
2. Is there any donations tax or estate duty payable on the diamond necklace which Sue received/took?
3. Compiling of the estate duty addendum of the accounts.
4. Should the trust property of the Jackson Family Trust be included in the liquidation account? I wasn't sure therefore I left it out of the provisional account as reflected in the attachment. I am also not sure if this trust property would have any estate duty consequences for Judy's estate.

Thanking you in advance for your help.

Anzelle Foreza"

YOU ARE REQUIRED TO:

Write an e-mail to Anzelle in which you show the following:

1. Calculation of the income tax liability in respect of Judy Jackson for her final period of assessment. Show all your calculations. Refer to Annexure 1 for the tax table and rebates for 2016. Except for the tax table and rebates you may assume that income tax legislation, as it applies to the 2015 year of assessment, is unchanged for the 2016 year of assessment. (19)

2. Advise Anzelle on whether there is any donations tax or estate duty payable by Judy or Sue in respect of the diamond necklace. Refer to the relevant legislation. (4)
3. The Estate Duty Addendum which has to be submitted as part of the executor's account in terms of the requirements of the Administration of Estates Act 66 of 1965. Show all your calculations. You may assume that the estate of the late Judy Jackson has no income tax liability. (13)
4. Advise Anzelle on whether the trust property should be included in the liquidation account. Furthermore, advise Anzelle on whether the trust property would be subject to estate duty in Judy's estate. Provide reference to legislation to support your views on both matters.

5. Attachment1:

FIRST AND FINAL LIQUIDATION AND DISTRIBUTION ACCOUNT IN THE ESTATE OF THE LATE JUDY JACKSON IDENTITY NUMBER 2101400214089, MARRIED OUT OF COMMUNITY OF PROPERTY WITHOUT THE ACCRUAL SYSTEM, RESIDENT AT 1118 ENDURANCE STREET, SOUTHSIDE, PORT ELIZABETH, AND WHO DIED THERE ON 30 APRIL 2015				
Master's Reference Number: 4454GR12X99				
LIQUIDATION ACCOUNT				
	Voucher	Rand	Rand	
ASSETS				20,712,000
IMMOVABLE PROPERTY		18,833,000		
Reduced to cash:				
Primary residence: 1118 Endurance Street, Southside, Port Elizabeth, registration division TR, Eastern Cape province, 1998 sq. metres in extent. Held under deed of transfer J999 dated 2005. <i>Sold at auction</i>	IP1	6,333,000		
Not reduced to cash:				
Six residential apartments: 19 Circle Crescent, Dawn Beach, Kwa-Zulu Natal, registration division KJ, 770 sq. metres in extent. Held under deed of transfer 0025 dated 2008. <i>At valuation</i>	IP2	4,800,000		
Farm Strangeland: 882 Agrivine Road, Polokwane, registration division NK 67, 3.4 Ha in extent. Held under deed of transfer 0101 dated 2003. <i>At valuation</i>	IP3	7,700,000		
<i>The abovementioned two properties (IP 2 and IP 3) are bequeathed to the deceased's major daughter in terms of clause A of the deceased's valid will.</i>				
MOVABLE PROPERTY		1,079,000		
Furniture and personal effects, as more fully detailed in the attached schedule. <i>At valuation</i>	MP1	489,000		
<i>Awarded to the deceased's surviving spouse, Shane, in terms of clause B of the will</i>				
Motor vehicle: 2014 Mercedes E-Class, registration no. FG 58 BJ GP <i>Sold at auction</i>	MP2	590,000		
CLAIMS IN FAVOUR OF THE ESTATE		800,000		
50% interest in Polifin (Pty) Ltd: sold in terms of a buy and sell agreement, proceeds	CF1	800,000		
LIABILITIES				???
ADMINISTRATION COSTS:		1,173,624		
Transfer costs	L1	77,700		
Valuation charges	L2	34,000		
Advertisements	L3	499		
Auctioneer's commission	L4	333,000		
Bank charges	L5	2,905		
Master's fees	L6	600		
Executor's fees at statutory tariff (Assets x 3.5%)	L7	724,920		
CLAIMS AGAINST THE ESTATE:				???
Funeral expenses:				
Ill Funerals	L8	30,000		
SoSo Bank: overdraft no. 2111555	L9	189,432		
SARS:				
- Income tax: Judy Jackson final assessment	L10	???		
- Income tax: Deceased estate late Judy Jackson	L11	???		
ESTATE DUTY:				???
Balance for Distribution				???

ANNEXURE 1

Tax Table: Natural persons 2016

Taxable income	Tax rate
R0 – R181 900	18% of each R1
R181 901 – R284 100	R32 742+ 26% of amount above.....R181 900
R284 101 – R393 200	R59 314 + 31% of amount above.....R284 100
R393 201 – R550 100	R93 135 + 36 % of amount above.....R393 200
R550 101 – R701 300	R149 619 + 39% of amount above.....R550 100
R701 301 +	R208 587 + 41% of amount above.....R701 300

TAX REBATES 2016:

Persons under 65:	R13 257
Persons 65 years or older:	R7 407
Persons 75 years or older:	R2 466

Question 3

40 Marks

Taxation of Farmers

Mr Kettle Farmer (58 years old) has a farm in the Vredefort koepel near Parys, Free State. He farms with cattle and also has a number of other farms on which he plants mealies every year. He asks you to do his tax calculation for him for the year of assessment ending 28 February 2015.

From his bank statements and the monthly summaries of payments prepared by his wife (to whom he is married out of community of property) you establish the following information relating to his taxes:

	Income	Note	R
1	Sale of cattle	1	1 500 000
2	Dividends received from local companies		20 000
3	Interest received on fixed deposit at bank		30 000
4	Sale of milk to a local dairy		250 000
5	Sale of maize		500 000
6	Rental received for grazing let to a neighbour		120 000
7	Rental received from two holiday cottages on the farm		12 000
	Payments		
8	Repairs to shed on the farm		17 500
9	Labour costs for the year		760 000
10	Veterinary fees for attending calving sessions		74 500
11	New milking machines bought	5	425 000
12	Seed and fertilizer for the maize		240 000
13	He built a dam next to the river – total costs		812 000
14	New tractor bought 1 January 2015 and brought into use immediately		460 000
15	Money spent to prevent soil erosion		140 000
16	Office furniture bought for farm office	5	6 000
17	Computer bought for farm office		12 000

6	You also establish that he received a subsidy from the Government amounting to R150 000 to build his dam.										
	Required										
(a)	Calculate the taxable income of Kettle Farmer for the year of assessment ending 28 February 2015 with reference to the First Schedule and other sections of the Income Tax Act. (25)										
(b)	Also explain to Kettle the tax consequences of the inheritance of the Ayrshire stud from his father. He wants to know what the implications would be if he sold the stud immediately on inheritance. (4)										
(c)	<p>If the taxable farming income of Kettle were previously as follows, explain to him the working of par 19:</p> <table data-bbox="293 936 715 1205"> <tr> <td>2014</td> <td>no income</td> </tr> <tr> <td>2013</td> <td>R25 000</td> </tr> <tr> <td>2012</td> <td>R23 000</td> </tr> <tr> <td>2011</td> <td>R20 000</td> </tr> <tr> <td>2010</td> <td>R15 000</td> </tr> </table> <p>You can assume that he did not make any contributions to annuities or that he had any other non-farming income for the purpose of answering (c) (3)</p>	2014	no income	2013	R25 000	2012	R23 000	2011	R20 000	2010	R15 000
2014	no income										
2013	R25 000										
2012	R23 000										
2011	R20 000										
2010	R15 000										
(d)	<p>Discuss the tax consequences should Kettle give his eldest son the right to farm on one of his farms valued at R2 million. (2)</p> <p>Also discuss the valuation of a farm used for <i>bona fide</i> farming when the farmer dies and the farm is valued for estate duty purposes. (1)</p>										
(e)	<p>When Kettle brought you his bank statements and other tax information he also left you 5 kg of biltong and a hind quarter of one of his cattle (cow). If you bought this at a butchery it would have cost you R4 000 – approximately what you would have charged him for the tax calculation.</p> <p>Discuss your actions if any re the above receipt of biltong and meat from Kettle:</p> <ul style="list-style-type: none"> - Firstly on your own tax calculation - Secondly, in the tax calculation of Kettle. (5) 										

Question 4

40 Marks

Other Taxes and Tax Administration

Part A

On 1 March 2014, Mr Haneef (aged 68) formed a discretionary *inter vivos* trust called the Haneef Family Trust ('the Trust'). The beneficiaries of the Trust are his two children, Imraan (aged 20) and Trusha (aged 16).

On the same date, 1 March 2014, Mr Haneef donated R650,000 in cash as well as his 5% interest in the ordinary shares of an unlisted company, Investall (Pty) Ltd ('Investall'), to the Trust. This was the only donation Mr Haneef made in his 2015 year of assessment. The fair market value of Mr Haneef's interest in Investall was valued at R250,000 on 1 March 2014 and at R300,000 on 28 February 2015.

On 15 December 2014, Investall declared a cash dividend in the amount of R600,000. No STC credits were available and no election to reduce contributed tax capital was made. The trustees decided, on the same date, to distribute the Trust's portion of the dividend income to Imraan in order for him to furnish the flat he had recently moved into.

During the year ended 28 February 2015, the Trust earned interest income of R33,250 from SA Bank in respect of the R650,000 cash deposit. The trustees, in terms of their discretionary powers, decided, on 28 February 2015, to distribute the interest income to Trusha's school in order for Trusha to take part in an overseas school choir tour.

You may assume that all persons (juristic or natural) mentioned in this scenario, meet the definition of 'resident' in section 1(1) of the Income Tax Act.

Part B

Dee Gumede (aged 23) obtained a qualification in professional child care and on 1 March 2014 she started her own business as a sole trader, running a daycare facility for babies and toddlers. An excerpt from her financial statements for the year ended 28 February 2015 appears below. Dee has also provided additional information in Notes 1 to 4. The daycare business was Dee's only source of income in her 2015 year of assessment.

Dee's Daycare

Detailed income statement for year ended 28 February 2015

	Note	Rands
Services Rendered		
Daycare services		1,011,300
Other income		
Interest income	1	1,800
Expenses		
Bank charges		(400)
Children's meals		(27,600)
Cleaning materials		(6,900)
Depreciation on educational toys	2	(2,900)
Rental of daycare premises	3	(96,000)
Salaries and wages	4	(220,000)
Telephone Expenses		(8,600)
Net profit before tax		650,700

Note 1

- Interest income earned was earned on Dee's positive current account balance with SA Bank.

Note 2

- Dee spent R29,000 in total on educational toy sets.
- Each toy set cost between R160 and R4,500.

Note 3

- The balance sheet includes a prepayment of R8,000 for the March 2015 rental payment.

Note 4

- Dee has employed Abigail Able to assist in the daycare on a full-time basis.
- Of the R220,000 relating to Abigail's employment, R20,000 is in respect of leave pay that has accrued to Abigail, but has not been paid to her as at year end.

Required		Marks
Part A		
a	<p>Draft an email to Mr Haneef, advising him of the donations tax consequences of his donation of cash and unlisted shares to the Trust. Your answer should include an explanation of why donations tax is applicable in this scenario, how it should be calculated, the amount of the liability, the date by which it is payable and who is liable to pay the donations tax.</p> <p><i>Presentation mark</i></p>	<p>8</p> <p>1</p>
b	<p>With regard to Mr Haneef’s transfer of the unlisted shares to the Trust:</p> <ol style="list-style-type: none"> i. Calculate the Securities Transfer Tax (STT) liability (if any). ii. Indicate which person (juristic or natural) is liable for the STT, and the date by which the STT must be paid to SARS. 	<p>1</p> <p>2</p>
c	<p>With regard to the dividend in respect of the 5% interest in Investall:</p> <ol style="list-style-type: none"> i. Calculate the Dividends Tax liability (if any). ii. Discuss which person (juristic or natural) bears the liability for the Dividends Tax. Consider the Trust, Imraan and Investall in your discussion. iii. Indicate which person (juristic or natural) is required to withhold the Dividends Tax and pay it over to SARS, and the date by which it must be paid to SARS. 	<p>2</p> <p>6</p> <p>2</p>
d	<p>Briefly explain, with short reasons, the income tax treatment of the interest income distributed to Trusha’s school?</p> <p><i>Do not address the tax consequences for the school.</i></p>	<p>3</p>
Total		25

Required		Marks
Part B		
a	Dee uses eFiling for all her tax submissions as she finds it much easier than manually submitting returns. Based on the financial information provided, list all the tax types Dee would have registered for on eFiling and provide a brief explanation as to why she would have been required to register for these tax types.	4
b	What is the timeframe in which Dee would have been required to register for the taxes identified above?	1
c	<p>Dee needs assistance in determining her taxable income for the 2015 year of assessment. Based on the financial information provided, you are required to prepare a computation starting with net profit before tax of R650,700 that contains the relevant income tax adjustments required to arrive at the correct amount of taxable income. Please provide a full explanation for each adjustment.</p> <p><i>You may assume that:</i></p> <ul style="list-style-type: none"> • <i>The financial information provided is reliable; and</i> • <i>Dee has thus far complied with the tax legislation in respect of all taxes for which she was required to register.</i> 	10
Total		15