THE PAPUA NEW GUINEA UNIVERSITY OF TECHNOLOGY

FIRST SEMESTER EXAMINATION 2022

DEPARTMENT OF BUSINESS STUDIES

AC412 – ADVANCED TAXATION

FRIDAY 8TH JUNE 2022

TIME ALLOWED: 3 HOURS

<u>DIRECTIONS TO STUDENTS</u>

1. **You have 10 minutes to read the examination paper. You must not begin writing during this time.**

2. **PART A: You MUST Answer all Questions. Total Marks 50**
   PART B: You MUST Answer only four (4) Questions. Total Marks 50

   IN TOTAL YOU SHOULD HAVE ANSWERED 5 QUESTIONS.

3. **Make sure that you read each question carefully. The number of marks for each question is given with each question.**

4. **PRINT your name and student number on the answer booklet provided. PLEASE DO IT NOW.**

5. **All answers must be written on the answer booklets provided. No other written material may be accepted. <u>Please hand in every answer booklet provided to you whether used or unused.</u>**

6. **Notes and textbooks are not allowed in the exam hall.**

This Examination is worth 50% of your Final Grade.

PART A – MULTIPLE CHOICE QUESTIONS (COMPULSORY)
(50 Marks)

Question 1

An amount received by a company to compensate for loss of earnings caused by having a project cancelled is

a) a windfall gain because the company was not expecting the payment,
b) a capital gain because the money would be an enduring benefit to the company,
c) an assessable income because it was an amount received to replace loss of earnings, or
d) a capital gain because it was only received in one lump sum by the company

Question 2

Mr A Jordan is a US citizen conducting basketball clinics in Papua New Guinea for three weeks because he needs the money. He is being paid by a US mining company which has not set up business in Papua New Guinea but wants local people to think well of it when they start looking for gold next year. Is the income not assessable because:

a) Mr Jordan is not a Papua New Guinea resident,
b) Mr Jordan receives the money from a US company which is not resident in Papua New Guinea,
c) Mr Jordan learned to coach basketball in the US so the money has a US not Papua New Guinea source, or
d) none of the above because the income is assessable here, having a Papua New Guinea source

Question 3

Papua New Guinea senior public servant, Wari Tumas, has hit the jackpot at the pokies and has been advised by a well meaning friend at the IRC that his winnings are taxable. You tell him that:

a) he won the money during working hours so he is taxable
b) he plays so often that he would be considered a professional gambler so he is taxable
c) he has never claimed any losses so he is not taxable
d) it is a windfall gain or similar so he is not taxable

Question 4
Former Papua New Guinea business identity, Ima Pirot, has made his home in Monaco and moved his family, all his furniture, bank accounts vehicles and other possessions there. He comes back every year to check that his real estate agents, Bone Idle Ltd, are collecting the rent from his office tower and residential complexes. In 2002, he took a few side excursions to the Sepik and stayed over with friends so that he was in Papua New Guinea longer than 6 months. Is he:

a) a tax resident in Papua New Guinea because he was here longer than 6 months
b) a tax non resident because he has a permanent place of abode in Monaco
c) a tax resident because his income comes from Papua New Guinea real estate and he still oversees the business
d) a tax non resident because he is not a Papua New Guinean citizen

Question 5
Harbinger Doom, the company accountant for Icarus Airlines, comes to see you. He had received K100,000 payment in advance in 2006 for airline tickets to be used by various 2007 election candidates. He would prefer the company not to be taxed on this receipt in 2007 because he would like to defer payment of his taxes. You tell him:

a) Icarus is assessable in 2006 because they are a small airline that should operate on a cash basis
b) Icarus is assessable in 2006 because the accruals basis says that is when the sale is made
c) Icarus is assessable in 2007 because the accruals basis says that is when the sale is made
d) Icarus is assessable in 2007 because the Act allows him to defer payment of his taxes

Question 6
Underground Oil Company Ltd, a company incorporated in Papua New Guinea, has moved its administration office to Cairns to save costs. The move has been so successful that all activities take place there, including directors meetings, management meetings and activities and accounting functions. You are specifically asked to give advice on the basis that the Double Tax treaty between the two countries is not effective because there may have been a slip up when it was signed. That being the case you advise that the company will be :

a) considered by Papua New Guinea tax authorities to be a resident of Papua New Guinea because it is incorporated in Papua New Guinea
b) considered by Australian authorities to be a resident of Australia because its central management and control is there
c) both of a) and b)
d) neither of a) nor b) because a company can only be resident in one place

Question 7

You are preparing the tax return for the year ended I December 2005 for a client who is a prosperous citizen and resident in Papua New Guinea. He has several bank accounts with Westpac in Cairns deriving interest income. Your view is that the interest is:

a) assessable to him because it is income derived as a resident of Papua New Guinea and there is no exemption which applies
b) not assessable because it is not Papua New Guinea source income
c) exempt under Section 35 of the Act because the income is derived from a foreign currency deposit
d) none of the above

Question 8

Roger Jolley has done well from his shipping business and has commenced building a block of flats in Port Moresby to make money from the high rents due to the housing shortage there. Before the building is complete he receives an offer that is too good to refuse from Hasta Lavista, an Italian lawyer he knows, and sells at a large profit. You tell him

a) the profit is assessable because he intended to make a profit when he sold it
b) the only reason the profit is not assessable is because he is not normally in the real estate business
c) the profit is not assessable because he was not intending to sell at a profit when he acquired the property
d) None of the above

Question 9

A client comes in and asks you to request the IRC to amend his previous income tax assessments because his employer has been paying his wife alimony direct from his gross wages and he never sees the money. You tell him :

a) he is assessable because he earned the income from which the payment is made
b) the is not assessable because he has never seen the money and never will
c) the is not assessable because, while the income is taxable, he would be allowed a tax deduction for the payment, so it cancels out
d) he is not assessable because it is his wife that will be assessed on it

Question 10
A client comes to you to ask your advice about the sale of his food bar business. The purchaser is prepared to lease the business from him for 2 years at a fixed payment, followed by a large payment to purchase the business at the end. The purchaser is indifferent as to whether the lease is structured as a lease or as an instalment sale provided he only pays what he has offered. You advise your client to:

a) take the deal that is offered because no payment is taxable
b) refuse the deal that is offered because he will pay tax on both the lease and the last payment as he has made a profit on sale of the business
c) refuse the deal because he will pay tax on both the lease and the last payment as there are a stream of payments
d) ask that all the payments be termed capital instalments for the sale of the business so your client won't pay tax on any of the payments

Question 11
Mr C de Mille of Haus Piksa Ltd comes to see you about the tax treatment of the cost of some work he is doing to his movie theatre. He is replacing some tiles in his ceiling with the nearest modem equivalent because he can no longer get the original type. They match in quite nicely with the old ones, are cheaper, offer better insulation and he considers them to be a major improvement over the old ones. He will continually replace tiles as and when he can afford it. Because the tiles are such an improvement he assumes they are not deductible. You tell him:

a) he is right, the tiles are a clear improvement and improvements are a capital expense because they are not incurred in returning the asset to its original condition
b) he is wrong, the cost of the tiles is deductible because he is using the nearest modern equivalent as the old tiles are no longer available.
c) he is right because he is replacing an asset and a replacement is a capital expense
d) he is wrong, the tiles are deductible because he is completing the work as he derives income from the theatre and that means they are incurred in the course of carrying on his business and deductible.

Question 12

You work doing the accounting and tax work for a restaurant that has become the flavour of the month in Port Moresby and is enjoying tremendous success. Times were not always so good and the company running the restaurant did make losses in the past and is hopeful of recovering those losses. The current owners purchased the company when the old owners become alarmed at the size of the losses they were incurring and the prospects for the business and sold out. The boss now comes to you and says he is sick of the hours involved in running a restaurant and wants to change the business into an industrial catering business which will give him much better hours. You tell him:

a) this is a fine idea and the company will still be able to claim its losses because they have been incurred less than 20 years ago

b) this is a fine idea but the company will not be able to claim its losses because it needs to pass either a continuity of ownership or continuity of business test and it hasn't done that.

c) this is a fine idea and the company will still be able to claim its losses because the company first passed the continuity of business test (when he bought the restaurant company) and then the continuity of ownership test (after he changes the business). Since he has at all times passed one of the two tests he will be able to claim his losses.

d) this is a fine idea but the company will not be able to claim its losses because they need to have been incurred by a primary production company and selling food is not primary production

Question 13

A company incurs legal expenses during the year for advice concerning all of the following:

1. purchasing a new warehouse
2. trying to prevent a foreign competitor setting up in Papua New Guinea
3. chasing debts owed to it by its customers
4. borrowing money for income producing purposes

A tax deduction is available (even if not in the current year but at some time in the future) for:

a) 1. and 4.
b) 2. and 4.
c) 3. and 4.
d) 1. and 3.

Question 14

A tax deduction is available to a company in the year of income for the following

a) repairs, unrealised exchange losses and entertainment expenses
b) security expenses of staff, provision of long service leave for staff and bad debts written off during the audit of the previous years accounts
c) loss on sale of property bought for investment purposes, electricity expenses incurred in respect of staff accommodation and provision of leisure facilities
d) none of the above

Question 15

A deduction is available to a company for expenditure incurred on repairs if

a) it was apparent the item being repaired required those repairs at time of purchase
b) the repairs constituted an improvement or addition
c) the repairs restored the asset to its original condition
d) none of the above

Question 16

A company is entitled to a double tax deduction for:

a) salaries paid to staff while they are attending a full time professional training course
b) wages paid to registered apprentices
c) salaries of full time trainers not engaged in the income earning activities of the company
d) all of the above

Question 17

Under Section 101 losses of previous years may be carried forward

a) if incurred in the last 20 years
b) indefinitely
c) if deductions exceed assessable income
d) if deductions exceed assessable income and exempt income

Question 18
A resident company in January 1996 borrowed Aus $3 million to be repaid at the end of six years. The rate of exchange throughout 1996 was 1 kina = 1 Aus $. Interest was fixed at 10% during the duration of the loan. Establishment and other costs associated with raising the loan amounted to K80,000. At the end of the year of income 2002, when this loan was repaid, the rate of exchange was 1 Kina = Aus .4 8.

Allowable deductions for 1996 would be:

a) K316,000
b) K380,000
c) K3,316,000
d) K3,380,000

Question 19
Refer to question 18. Assessable income/ allowable deduction in respect of the foreign exchange gain/loss when the loan was repaid in 2002 would be

a) assessable income of K3,250,000 (forex gain)
b) allowable deduction of K3,250,000 (forex loss)
c) assessable income of K6,250,000 (forex gain)
d) allowable deduction of K6,250,000 (forex loss)

Question 20
Personal income tax is

a) applied at a flat rate
b) proportional
c) progressive
d) regressive

Question 21
Salary and wage income is assessed to tax each:
a) year
b) month
c) fortnight
d) week

Question 22
A rebate of tax of 25% is allowed for expenses incurred in earning salary and wages income to the extent of:

a) the first K200 of the expenses
b) all but the first K200 of the expenses
c) all the expenses incurred
d) none of the expenses incurred

Question 23
Lump sum superannuation payments are taxable at the marginal rate of 2% if:

a) accrued before 1 January 1993
b) contributions were made on behalf of the employee for greater than the 15 years
c) contributions were made on behalf of the employee for greater than the 7 years and they are aged over 50 years at time of payment
d) all of the above

Question 24
Payments of salary and wages tax made in arrears, that is for work done in previous periods, are taxable;

a) over the previous 26 fortnights
b) in the fortnight they are received
c) over the period that the work they refer to was done
d) none of the above

Question 25
The first K5, 000 of non-salary and wages income earned by an individual is taxable:

a) at a rate of nil b6cause of the K6,600 tax free ttreshold
b) at the top marginal rate of 47%
c) at the difference between the tax on salary income plus non salary income less tax deducted from the employees salary and wages
d) at the difference between the tax on salary income plus non salary income less the tax on his or her salary and wages tax income

Question 26
Benefits that may be provided to an employee exempt from income tax include:

a) provision of vehicles, accommodation under an approved low cost housing scheme and leave fares
b) provision of private telephone , leave fares and payment of school fees
c) provision of leave fares, entertainment allowance and payment of school fees
d) provision of accommodation under an approved low cost housing scheme, leave fares and payment of school fees

Question 27
Lump sum superannuation payouts are

a) not taxable
b) taxed at 2%
c) taxable as normal salary or wage income
d) taxable in respect of employer contribution and interest earned.

Question 28
Provisional tax is:

a) payable in respect of salary and non salary income
b) payable in the same year as the income in question is earned
c) paid in three instalments during the year
d) is a first and final tax

Question 29
A man with taxable income has three dependants.

a) He is entitled to an allowable deduction for these dependants
b) He will automatically receive an allowance for these dependants
c) He is entitled to a tax refund for these dependants
d) He will normally be entitled to a rebate for these dependants.

Question 30
Beneficiaries of a trust in PNG are:

a) taxable on any distributions
b) exempt on any distributions
c) may be either taxable or exempt depending on the status of the trust from which they derive income
d) none of the above

Question 31
A resident individual receives dividend income of K74,700 on 1 February 2007 (net of DWT)

a) gross dividend is K87, 399
b) tax payable is K12, 699
c) tax payable is KI 5,300
d) the DWT applicable to the dividend is K 15,3 00 and the dividend income is exempt from further tax.

Question 32
A senior manager and sole shareholder of a company received an interest free loan of K2 million from the company with no set repayment conditions. The IRC deemed the payment to be a dividend payment from the company.

The senior manager would be

a) taxed on the payment at normal personal income tax rates
b) taxed on the payment at 17% since it is deemed to be a dividend
c) entitled to a credit for DWT withheld
d) be taxed on the payment at 30%

Question 33
The purpose of a unit trust is to

a) allow distributions to non residents
b) allow landowners to take an interest in resource projects
c) ensure that beneficiaries are not taxable on their distributions
d) provide an opportunity for investors to participate in different investments

Question 34
A company, which has never paid or received a dividend before, receives a cash dividend of K83, 000 from a subsidiary. It now declares a dividend to its shareholders of the same amount as was declared in its favour and it will pay dividend withholding tax to the IRC of

a) nil
b) K17, 000
c) K83, 000 x 17%
d) K17, 000 x 17%

Question 35
A company with a credit available of K 13, 000 in its refundable dividend withholding tax account intends to declare a dividend of K 100, 000 to its shareholders. The dividend withholding tax it actually has to pay to the IRC in due course is:

a) K4, 000
b) K13, 000
c) K17, 000
d) none

Question 36
Included in a company's income was K19, 090 dividend income (net of DWT). The company would normally be entitled to receive

a) credit of K3, 245 for DWT paid
b) rebate of K5, 727 for tax payable on dividend income
c) rebate of K3, 910 for tax payable on dividend income
d) credit of K3, 910 for DWT

Question 37
Income earned by a Papua New Guinea non-resident is

a) not taxable if that income is derived in Papua New Guinea
b) not taxable if that income is derived overseas
c) fully taxable regardless of the source of income
d) taxable if the income was derived overseas

Question 38
Income derived from an overseas source by a Papua New Guinea resident is

a) tax free
b) taxed at the top marginal rate
c) taxed only in the country where the income is derived
d) taxed at normal `Personal income tax rates

Question 39
A company deriving overseas income

a) is entitled to a rebate equal to the tax payable if the income is dividends
b) is entitled to a credit equal to overseas tax paid
c) will be subject to the terms of a double tax agreement
d) is entitled to a credit equal to the amount of Papua New Guinea tax payable

Question 40
Losses incurred in deriving overseas income

a) may be carried forward indefinitely and offset against taxable income
b) are an allowable deduction against a taxpayer's income
c) are an allowable deduction against a taxpayer's overseas income
d) are not deductible against income

Question 41
Foreign contractors tax is

a) levied at 48% of (a notionally calculated) taxable income
b) a withholding tax that is a first and final tax
c) levied at 12% of gross income
d) all of the above

Question 42
Management fees

a) paid to related companies are not deductible
b) are subject to 17% with-holding tax
c) are an allowable deduction
d) paid to related companies may not be fully deductible

Question 43
The main purpose of double tax agreements is to

a) minimise tax evasion
b)" avoid taxpayers being taxed twice on the same income
c) promote trade and investment between countries
d) all of the above

Question 44
Interest paid by a Papua New Guinea company to an Australian resident will be subject to

a) tax at normal personal income tax rates
b) withholding tax of 10%
c) withholding tax of 15%
d) withholding tax of 17%

Question 45
In the double tax agreement between Papua New Guinea and Australia, if a clause in the agreement conflicts with the tax law of either country

a) the provisions of Papua New Guinea income tax legislation will prevail
b) the provisions of Australian income tax legislation will prevail
c) the provisions of the double tax agreement will prevail
d) each country will apply its own domestic tax legislation

Question 46
An overseas company which incorporates a local subsidiary
a) will be subject to corporate company tax at normal Papua New Guinea rates
b) will pay a higher tax rate of 48%
c) will pay a higher tax rate, but will not be subject to dividend withholding tax
d) may claim a full deduction for management fees paid to the parent company

Question 47
The tax regime for resource projects is, for the most part, ringfenced. This means

a) a company must declare all its income in its tax return.
b) only income and expenditure in relation to a particular project are included in a tax return
c) no exploration or other expenditure outside of a project may be claimed as a deduction
d) with few exceptions, only project related income and expenditure maybe included in the calculation of taxable income in respect of the project.

Question 48
Allowable exploration expenditure

a) may be amortized by a divisor of four each year or by the number of years remaining for the project
b) consists of a pool of exploration expenditure incurred in an exploration or development licence
c) should be reduced by amounts claimed as an outright deduction under S.155N
d) may be claimed as a deduction regardless of when the exploration expenditure was incurred

Question 49

Which of the following statements relating to allowable capital expenditure (ACE) is correct

a) ACE and AEE expenditure is amortized in the same way
b) Expenditure on short life assets may normally be amortized at a. faster rate than expenditure on long life assets
c) ACE includes capital expenditure and excludes exploration expenditure
d) Capital expenditure in a resource project may only be amortized in accordance with the ACE provisions

Question 50
Additional profits tax

a) is a tax based on the overall profitability of a resource company
b) may apply when the rate of return of a project exceeds a certain level
c) only applies to gas projects
d) will normally be triggered at the start of very successful projects

PART B – (i) QUESTION ONE IS COMPULSORY (12.5 Marks)

(ii)ANSWER ANY THREE QUESTIONS FROM QUESTION TWO - EIGHT(All questions carry equal marks) (37.5 Marks)

Question One (12.5 Marks)

A business had the following trading results for July.

	K
Sales	570,000
Receipts received from July sales:	350,000
Taxable supplies	264,000
Payments made for taxable supplies	150,000.

Required

Calculate net GST to Internal Revenue Commission in August. The business has annual sales of over K500,000.

Question Two (12.5 Marks)

The owner of a dance hall, on ascertaining that a portion of the ceiling of the hall was in need of repairs, decided to replace the whole of the ceiling with a different but better material. The new ceiling, in addition to enhancing the appearance of the hall, improved the acoustics. The total cost of the material and of erecting the new ceiling was K240,000, it was estimated that the cost of repairing the ceiling would have been K150,000.

Required

With reference to S.72, discuss the amount, if any, allowable as a deduction for income tax purposes.

Question Three (12.5 Marks)

An employee with three dependants who lives and works in Goroka receives K1,740 per fortnight. In addition he receives the following employment related benefits: Accommodation which is rented by the employer for K450 per week Entertainment allowance of K100 per fortnight A company vehicle (without petrol). Education fees of one child to private school. The annual fees amount to K6,000 per year and are paid directly to the school by the employer. Employer contribution of K20 per fortnight to an authorised superannuation fund.

Required

Calculate A. Taxable income for the year ended 31 December 2010.
B. Salary or wage tax payable
C. Tax rebate at end of year

Question Four

XYZ Company Ltd issued the following income statement in 2010.

Sales	150,000	
Cost of goods sold	65,000	
Gross profit		85,000
Other Income		
Rental income	12,000	
Bank interest	5,000	
Profit from sale of vehicle	8,000	25,000
		110,000
Less: Costs		
Wages	25,000	
Advertising	4,500	
Vehicle running expenses	7,000	
Net discounts	700	
Depreciation	7,200	
Debts written off	500	
Doubtful debts	400	
Insurance	800	46,100
Net profit (before tax)		63,900

Other information:

1. Profit from sale of vehicle: Sale price 20,000; cost price 18,000; written down value 12,000.
2. Wages include K7, 500 paid to a full time training officer.
3. Depreciation relates to equipment purchased at the end of June 2001. Cost price K120, 000.Depreciation is calculated at 12% straight line. The prescribed rate for tax purposes is 7.5% straightline. The business is also

allowed to claim accelerated depreciation of 20 % of the cost of the equipment.

4. Losses carried forward K12, 700.

Required:

Calculate Taxable Income

Question Five

A taxpayer's total taxable income for the year ended 31 December 2010 was as follows:

Salary	67,500
Rental income from Fiji	140,000
Interest income from New Zealand	20,500
Dividend income from UK	10,400

Foreign tax paid in respect of the taxpayer's overseas income was:

Rental income	45%
Interest income	15%
Dividend income	25%

Required

Calculate net tax payable by the taxpayer on non-salary income.

Question Six

A Papua New Guinea subsidiary of a New Zealand company pays royalty fees of 1.75 million to its New Zealand parent for architectural designs developed in the company's head office.

A. What taxes would normally be withheld from this payment?

B. If the foreign company was a non-associated company, what taxes would be normally withheld by the Papua New Guinea company?

C. If the New Zealand company, being a non associated company, incurred the following expenses in relation to the design work:
payment to agency in New Zealand for hire of architects
for additional design work 725,000
travel and accommodation expenses in Papua New Guinea
in connection with this work 122,500

Required

Calculate taxable income and tax payable.

Question Seven

The following resource company operating in a petroleum project provided the following figures in its tax return. Figures are in US dollars. Tax Rate is 30% (for incentive rate petroleum operations).

- Sales income 107.5m
- Interest income 2m
- Share of project operating costs 15m
- Sole costs (overheads) 4m
- Petroleum development levy (to be calculated)?
- Interest expense 1.5m
- Section 219C prescribed infrastructure development expenditure 1.5m. Assume there are no carry forward entitlements from the prior year in respect of Section 219C prescribed infrastructure development expenditure.

- Exploration expenditure: AEE written down balance: 80m
- (S. 155N) Exploration pool: written down balance (Start of year) 60m. Addition during year: 8m
- Allowable capital expenditure:
  Long life asset pool (start of year): 60m (historical cost); 42m (undeducted balance)
  Additions during the year: 8m

Royalties and development levies are based on sales less 7% (for transport and processing costs); Estimated remaining life of production: 8 years.

Required:

Calculate taxable income and net tax payable

Question Eight

A firm employs a workforce which has an annual salary or wages bill of K2.4 million. During a year of income, the firm employs a staff training officer whose annual salary is K59,500. Four employees whose annual wages total K80,000 are sent to Lae Technical College for a six months course. The fees payable and other expenses total KI 7,000. Other training expenses, including training consumables and depreciation of in-house training facilities amount to K8,000.

Required
Calculate allowable deductions in respect of salary and wages and training expenditure, and net training levy payable, if any.

TOTAL MARKS [50 + 50 = 100 MARKS]

END OF EXAM