QUESTION 1

55 marks

After qualifying as a CA you started your own business as a practising accountant. In an attempt to increase your tax-related work you wrote a short article on taxation that was published in a local newspaper. You concluded the article by inviting taxpayers to e-mail their tax queries to you and undertook to answer each query by means of a brief reply e-mail.

You received e-mails from Mr Indigo, Mr Turbot and Mr Coquilles, extracts of which are represented below.

E-mail 1: Mr Indigo

11 marks

From: Pete Indigo [mailto:pindigo@lantic.co.za]
Sent: 1 March 2009 12:44 PM
To: C Accountant
Subject: Tax query

I own a 'corner cafe'. I trade in my own name and am a vendor for VAT purposes. My trading hours are from seven in the morning to seven in the evening, seven days a week. The cafe makes taxable supplies only. Each night I take a loaf of sliced white bread, a litre of fresh milk and an evening newspaper home with me. Net of VAT, these items cost me R21.00. I would have sold them to a customer for R25.39 (R23.10 plus VAT of R2.29). I make no entries in my books (or financial records) regarding these items, apart from debiting 'purchases' when I buy them.

REQUIRED

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<th>In your reply to Mr Indigo, explain, with reasons, the normal tax and VAT consequences of his actions.</th>
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**Presentation marks:** Arrangement and layout, clarity of explanation, logical argument and language usage.

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E-mail 2: Mr Turbot

From: Barry Turbot [mailto:barryt@ecu.ac.za]
Sent: 6 March 2009 16:32 PM
To: C Accountant
Subject: Tax query

The East Coast University (‘ECU’) retrenched some workers as part of its rationalisation process. I am its former handyman and one of the workers who was retrenched.

I then formed Turbot CC of which I am the sole member. In addition to myself, my CC has two full-time employees. My employees and I work from 07h00 to 16h30 each day, five days per week, and we occasionally also work overtime.

My biggest client is the ECU which uses my services as a handyman on an ongoing and regular basis. In fact, almost all Turbot CC’s work is for the ECU. While we do on the odd occasion work for private clients (i.e. other than the ECU), these clients are mostly employees of the ECU. The ECU does not use the services of another handyman. At the end of each month my CC invoices the ECU with the amount due from it for handyman services required by and provided to it.

Turbot CC rents trading premises, consisting of a workshop, storeroom and office, from the ECU at a market-related monthly rental. Although we do some work on these leased premises, most of the work is performed in the various buildings owned and used by the ECU.

Turbot CC’s gross income for its 2009 year of assessment (ended on 28 February 2009) was R850 000. Approximately R750 000 of this income was derived from the ECU.

Apart from my membership of Turbot CC, I am not a member of another close corporation, nor do I hold shares in a company.

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<td>(a)</td>
<td>Discuss, with reasons, whether Turbot CC is a ‘personal service company’.</td>
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<td>(b)</td>
<td>Discuss, with reasons, whether Turbot CC is a ‘small business corporation’.</td>
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<td>(c)</td>
<td>Discuss, with reasons, what tax consequences would arise for the East Coast University if it should have deducted employees’ tax from its payment to Turbot CC but failed to do so.</td>
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Presentation marks: Arrangement and layout, clarity of explanation, logical argument and language usage. 1
E-mail 3: Mr Coquilles

From: Jacques Coquilles [mailto:jcoquilles@telkomza.net]
Sent: 8 March 2009 09:02 AM
To: C Accountant
Subject: Tax query

I am a 77 year-old retired judge. My taxable income consists of my pension and the returns from various investments (net rentals, taxable dividends and interest). According to my calculations, my total amount of taxable income for the 2009 year of assessment was R700 000.

I relinquished my driver’s licence two years ago. Because my wife, who is 75 years old, has never driven a car and because I am unable to use public transport, I employ Izaak Walten-Pike on a full-time basis as my driver. Izaak is 31 years old.

In terms of Izaak Walten-Pike’s employment contract with me he is entitled to the following benefits:

- A cash salary of R4 800 per month (for the 2009 year of assessment).
- Free accommodation in a furnished three-roomed granny flat situated on the residential property where I live and that I own. I could earn a rental of R1 500 per month if I let the flat on an arm’s length basis. Izaak does not have to pay for electricity or water and these services cost me R300 per month.
- Free meals. They are prepared by my housekeeper and are served to Izaak in the flat. My wife has estimated that the meals that we provide to Izaak cost R2 700 per month.
- The free use of a cellular telephone. Although it is used mainly for business purposes (I telephone Izaak when I need to be driven somewhere or fetched), Izaak does have the incidental use of it. This cell phone costs me R250 per month.
- The infrequent or incidental use of my motor car. The car cost R340 860 (R299 000 plus VAT of R41 860) on 1 March 2008. Izaak’s use of my motor car costs me R150 per month.

Izaak Walten-Pike’s ‘remuneration factor’ (as defined in paragraph 9(1) of the Seventh Schedule) is R51 000. His earnings and benefits from me are his sole receipts and accruals and he is not entitled to any tax deductions or allowances.

I have not claimed any portion of the cost of employing Izaak Walten-Pike as a deduction in the determination of my R700 000 taxable income.

I paid my first provisional tax payment for the 2009 year of assessment timeously (before 31 August 2008) and estimated my taxable income at an amount equal to my basic amount.

I paid my second provisional tax payment for the 2009 year of assessment timeously (before 28 February 2009). I estimated my taxable income at R600 000, although my basic amount was R625 000. (I thought my net rental income was going to be less than it had been in the previous two years.) The additional tax in terms of paragraph 20 of the Fourth Schedule resulting from this underestimate amounted to R2 000.

Employees’ tax of R85 930 was deducted from my pension for the 2009 year of assessment and my first provisional tax payment amounted to R47 760.
REQUIRED

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<td>(a) Calculate, with reasons, the employees’ tax that Mr Coquilles should deduct from the remuneration of Mr Walten-Pike each month. Provide reasons for including in remuneration or excluding from remuneration each of the benefits to Mr Walten-Pike.</td>
<td>10</td>
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<td>(b) Discuss, supported with reference to legislation, whether the expenses that Mr Coquilles incurred regarding the employment of Mr Walten-Pike, or a portion thereof, would be deductible in determining Mr Coquilles’ taxable income.</td>
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<td>(c) Assuming that Mr Coquilles has not yet been assessed and his taxable income is correctly calculated as R700 000, calculate the third provisional tax payment that Mr Coquilles has to make on 30 September 2009 that would be sufficient to cover his normal tax liability for the 2009 year of assessment.</td>
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**Presentation marks:** Arrangement and layout, clarity of explanation, logical argument and language usage. 2