



**CERTIFIED PUBLIC ACCOUNTANT
ADVANCED LEVEL 2 EXAMINATIONS
A2.3: ADVANCED TAXATION
DATE: MONDAY 27, MAY 2024
MARKING GUIDE AND MODEL ANSWERS**

SECTION A

QUESTION ONE

Marking Guide

		Marks
A.	i) 1 mark for any valid point up to a maximum of 5 marks	5
	ii) 1 mark for any valid point up to a maximum of 5 marks	5
	iii) 1 mark for any valid point up to a maximum of 5 marks	5
	iv) 1 mark for any valid point up to a maximum of 5 marks	5
	v) 1 mark for any valid point up to a maximum of 5 marks	5
	<i>Sub-total for this section</i>	25
B		
Kirehe Distillers Limited (Jan - July 2023)		
	Basic Salary	1
	Add Cash benefits;	
	Acting Allowance	1
	Professional allowance	0.5
	Responsibility allowance	0.5
	Relocation allowance	0.5
	House rent	0.5
	Cash gifts	1
	Total Cash emoluments	
	Add: Benefits in Kind & other benefits;	
	Fueled company car	1
	Total Taxable income from Kirehe Distillers	
Cana Limited (Sep - Dec 2023)		
	Basic Salary	1
	Add Cash benefits;	
	Cost of Living allowance	1
	Overtime	1
	Bonus (Once off)	1
	Refund	1
	Private pension	1
	Total Cash emoluments	
	Add house benefit in kind	1
	Add: Income from Livestock	1
	Total Taxable income for Miss Yvette Mbabazi	
	Total Taxable income for Miss Yvette Mbabazi	
	W1: Out of pocket refund	1
	Tax payable computation	1
	<i>Sub-total for this section</i>	15
	Total Marks for Question One	40

Model Answer

A. MEMO:

FROM: Business and tax consultant

TO: Mr. Moise Munyarugendo

TOPIC: Tax Implications of the various Investment options in Rwanda.

Executive Summary:

The Government of Rwanda is intentional on developing key priority sectors in the country, and in addition to putting in place a conducive business environment the Government has put in place very attractive tax incentives for Investors, hence it is important for any Investor to have a good knowledge of these, the next paragraphs I will break down for you the tax implications and considerations for each of the five options you have identified.

INVESTMENT OPTION ONE:

The following are the tax considerations for this investment option.

- a) The Buses with sitting capacity of more than 14 passengers shall be exempted from VAT, this is a great benefit because it allows you to charge a fairly lower price to passengers.
- b) For Electric Buses, The Government has made import of Electric Vehicles and their accessories duty free and zero-rated for VAT. This makes electric buses more competitive than ICEs.
- c) In addition to the above, you can access Government land on a rent-free basis to set up charging stations.
- d) If you get Investment certificate with Rwanda Development Board, with certain conditions to be met it comes with specific benefits like accelerated depreciation, discounted Income tax rates and more industry specific incentives.

INVESTMENT OPTION TWO:

The following are the tax considerations for this investment option.

- a) Rwandan tax law provides Incentives for Property owners who earn rental income, where a flat 50% of Gross rental income is expensed and considered as expense for maintenance and house upkeep costs.
- b) In addition to that, If you have proof of actual interest expense paid within the taxable period, you are allowed to deduct it in arriving at taxable income.
- c) After the above deductions rental income tax is taxed as follows; 0 to 180,000 is taxed at 0%, 180,001 to 1,000,000 is taxed at 20% and over anything over 1,000,000 is taxed at 30%.
- d) In recent tax reforms, the Government has lessened the burden on property owners, with the tax rate on Commercial buildings reduced from 0.5% to 0.3% of its market value on both building and land.
- e) If you get Investment certificate with Rwanda Development Board, with certain conditions to be met it comes with specific benefits like accelerated depreciation, discounted Income tax rates and more industry specific incentives.

INVESTMENT OPTION THREE:

The following are the tax considerations for this investment option.

- a) By law all fresh agricultural products are exempt from VAT, hence the local sales to Inyange Industries shall not attract VAT.
- b) Specific to Milk though, locally processed Milk is exempt from VAT, so even processed milk for export shall enjoy zero VAT, which the corresponding input VAT can be claimed.
- c) *Income tax:* Income earned by an agriculturalist or a pastoralist on agricultural or livestock activities is exempt if the turnover from agricultural or livestock activities do not exceed twelve million Rwanda francs (FRW 12,000,000) in a tax period.
- d) land used for agricultural, livestock or forestry activities whose area is equal to or less than two hectares is exempted from the property tax.
- e) If you get Investment certificate with Rwanda Development Board, with certain conditions to be met it comes with specific benefits like accelerated depreciation, discounted Income tax rates and more industry specific incentives.

INVESTMENT OPTION FOUR:

The following are the tax considerations for this investment option;

- a) Medical sector is one of the highly incentivized sectors in the Country with almost everything exempted or zero-rated.
- b) To begin with, all medical services including equipment intended for persons with disabilities are exempted from VAT. There is a comprehensive list provided regularly via a Ministerial order that can be used as reference. This would include all medical consultations, surgeries and all other related services.
- c) Drugs to be sold at the pharmacy shall be VAT exempt as well, not on only in the pharmacy but also on importation.
- d) Selling shares: Selling shares to the public via Rwanda Stock exchange comes with enormous income tax advantages Mr. Munyarugendo. As an example, in the recent Government amendment of different taxes, if you sell at least 30% of shares to the public you get a discounted income tax rate from 28% to 25% of taxable profit. This income tax rate becomes 20% if you sell at least 40% of shares to the public.
- e) A registered investor, investing an equivalent of at least fifty million United States Dollars (USD 50,000,000) and contributing at least thirty per cent (30%) of this investment amount in form of equity in the health sector is granted to a maximum of seven (7) year corporate income tax holiday, he is also entitled to the accelerated depreciation at 50% on the new assets invested worth 50,000 USD each.

INVESTMENT OPTION FIVE:

The following are the tax considerations for this investment option.

- a) Generally, Dividend income is taxed at a flat 15% withholding tax, but it is wise to but shared listed on Rwanda Stock exchange as the withholding tax is 5% instead.
- b) It is even more favored when selling shares held with a company listed with Rwanda Stock exchange, the capital gains thereof are exempted from capital gains tax, which is normally 5%.
- c) Investment in Government bonds: Interest Income from Government bond is by default taxed at 15% like any other investment income. However, the interest income derived from

the Treasury bond with a maturity period of three years and above, the withholding tax is 5%.

- d) Income from your investment in Kenya and Ghana shall be the same, I expect the income to come when it is already net of withholding tax from the respective countries. The tax authority shall require you to gross it up with the withholding tax charged prior to receipt and include it in taxable income.
- e) Overall, dividends paid between resident companies and unrealized foreign exchange gains on outstanding loan are excluded from corporate taxable income but foreign income is not, hence you should make careful consideration and of this difference.
- f) Also, If during a tax period, a resident in Rwanda generates income derived from taxable activities performed abroad, the income tax payable by that resident in respect of that income is reduced by the amount of foreign tax payable on such income. The amount of foreign tax payable shall be substantiated by appropriate evidence such as tax declaration, a withholding tax certificate or other similar acceptable document and shall not exceed the tax payable in Rwanda on income from abroad.

B. Yvette Mbabazi's Taxable income calculation for the tax period 2023

Description	Workings	RWF '000	RWF '000
Kirehe Distillers Limited (Jan - July 2023)			
Basic Salary	(42000/12x7)	24,500	
Add Cash benefits;			
Acting Allowance	(10%x42m/12x5)	1,750	
Professional allowance	(150,000x5)	750	
Responsibility allowance	(185,000x5)	925	
Relocation allowance		540	
Cash gifts		950	
House rent (850,000-400,000)	(450,000x7)	3,150	
Total Cash emoluments			32,565
Add: Benefits in Kind			
Fueled company car	(10%x32565)	3,257	
Total Taxable income from Kirehe Distillers			35,822
Cana Limited (Sep - Dec 2023)			
Basic Salary	(48m/12x4)	16,000	
Add Cash benefits;			
Cost of Living allowance	(120,000x4)	480	
Overtime	(90,000x4)	360	
Bonus (Once off)		3,500	
Refund	(W1)	150	
Private Pension contribution	(60,000x4)	240	
Total Cash emoluments			20,730
Add house benefit in kind	(20%x 20730)	4,146	
Add: Income from Livestock	(18m-12m)	6,000	10,146
Total Taxable income for Miss Yvette Mbabazi			66,698

Computation of personal income tax payable

From	To	Tax rate	Tax payable (Frw 000)
0	360,000	0%	-
360,001	1,200,000	20%	168
1,200,000	Above	30%	19,649.4
			19,817.4

W1: Out of pocket refund	RWF '000
Total refund	300
Less: Personal expenses (50%)	(150)
Eligible amount	150
Taxable amount	150

SECTION B

QUESTION TWO

Marking Guide

	Marks
a. 02 Marks for valid definition of tax evasion	2.0
02 Marks for valid definition of tax avoidance	2.0
02 Marks for explanation of link with Integrity and tax evasion	2.0
<i>Sub-total for this section</i>	<i>6.0</i>
b. 03 Marks for each valid point in scenarios 1 to 3, maximum 03 marks for each	9.0
Scenario 4:	
01 mark for showing knowledge of thin capitalization	1.0
02 Marks for proper calculation of disallowable interest	2.0
02 Marks for proper calculation of allowable Interest	2.0
<i>Sub-total for this section</i>	<i>14.0</i>
<i>Total Marks for Question Four</i>	<i>20.0</i>

Model Answer

- a. **Tax Avoidance** is about a taxpayer taking advantage of loopholes in the tax system to minimize their tax liability but legitimately. This practice is not illegal, however most Revenue Authorities put in place anti-avoidance legislations to discourage it. There is a thin line between tax avoidance and tax evasion.

Tax evasion on the other hand is about a taxpayer deliberately and unlawfully breaching the tax system and regulations in place to reduce their tax liability. Tax evasion is illegal and punishable by law.

A professional accountant is expected to demonstrate highest level of integrity, by being objective and honest in all their work. As a professional accountant, I have the obligation to ensure that I do maintain honesty in my relationships and any work-related matters at any time.

For Imali's Managing director, undervaluing import cost is fraud and is an obvious form of tax evasion. Upon knowing this I would escalate it to my superior with all relevant evidence. I must consider very carefully the approach of escalation, including seeking legal opinion. Eventually such fraud has to be reported to relevant authorities, which brings in another issue of confidentiality breach for my job but for such things as fraud I have to make a judgement, confidentiality by concealing fraud does not make me a good accountant.

b.

1) Imported Service:

- Reverse charge VAT of 18% shall have to be applied on this transaction as it is an imported service.
- The fact that Imali has not shown the proof that the service is not available in Rwanda, the company is liable for Reverse charge VAT on the Invoice.
- In addition to Reverse charge VAT the company should withhold 15% and pay to Rwanda Revenue Authority, this is because it is paying to a non-resident supplier.
- The Company shall pay $18\% \times (\text{USD } 7,000 \times 1,100 \times 100/85) = \text{Frw } 1,630,588$
- The company shall gross up the USD 7,000 for withholding tax base and compute the payable amount in the following way; $\text{USD } 7,000 \times 1,100 \times 100/85 = \text{Base amount}$. The base amount $\times 15\% = \text{Withholding tax payable}$. $(7000 \times 1100 \times 100/85 \times 15\%) = \text{Frw } 1,358,823.5$

2) Rent of Vehicle for Production Manager:

- Imali Limited should add the RWF 950,000 to the production manager's salary for November, this shall effectively increase the tax base for PAYE.
- The understanding from tax law is that the rent of vehicle is a benefit for the production manager and should be taxed same way as the other allowances are taxed. It is different if it was a company fueled car, that one is capped at 10% of total emoluments.
- However, it should be noted that the RWF 950,000 is just for tax purposes and does not filter down to the net salary. It is adjusted after calculation of tax.

3) Forklift acquisition on hire purchase.

- First of all, the Input VAT on the cost can be claimed by Imali Limited by netting it off the output VAT on sales. It would be calculated as follows; $(75,000,000 / 1.18) \times 18\% = 11,440,677.9$
- The company shall utilize wear and tear tax allowable expense on the asset. Heavy machinery is depreciated at 5%, hence Imali shall enjoy $\text{Frw } (75,000,000 \times 100/118) \times 5/100 = 3,177,966$ depreciation.
- However, if the company has a valid investment certificate, and given the asset value is over \$50,000 the company can enjoy a 50% depreciation in the year of purchase 2023. There are other considerations like keeping the asset for a minimum of three years.
- The interest on the purchase $(20\text{m} + 10\text{m} \times 8) - 75\text{m} = 25\text{m}$. This RWF 25 million shall be allowable interest for income tax purposes.
- Finally, the monthly repayment of the principal amount of the cost shall not be considered as expense for tax purposes.

4) Loan from Related party:

- Interest on Loan from related party has to meet thin capitalization rules for threshold to be allowed for Income tax purposes.
- In Rwanda, the interest paid on loans and advances from related entities is not tax deductible to the extent that the total amount of loans/advances exceeds four times the amount of paid-up equity.
- For the above scenario, the interest and foreign exchange loss shall be subjected to thin capitalization calculation, with a maximum Debt: Equity ratio of 4:1
- Below calculation shall support the above argument in more detail.

Particulars	RWF '000
Allowable debt (Four times Equity)	80,000
Total Debt acquired	100,000

Disallowable Debt	20,000
Total Interest	1,000
Interest allowable (80m/100mx1m) on thin capitalization	800
<i>Disallowable Interest (Total Interest - Allowable Interest)</i>	200

QUESTION THREE

Marking Guide

Description	Marks
Award 1 marks for a well explained method (up to 6 marks)	6
Scenario 1: using CUP method	3
Scenario 2: using the resale price method	3
Scenario 3: using the cost plus method	4
Award 1 mark for a well feature of a customs union (up to 4 marks)	4
Total	20

Model Answers

a) The available methods for determining arm's length prices in Rwanda include:

Comparable Uncontrolled Price (CUP) Method: This method involves comparing the price charged in a controlled transaction with the price in a comparable uncontrolled transaction. It's especially useful when a similar uncontrolled transaction is readily available for reference.

Cost Plus Method: The cost-plus method focuses on the costs incurred in producing goods or services, and adds an arm's length profit margin to arrive at a fair price. It's often used in scenarios where the producer provides unique inputs or performs unique functions.

Resale Price Method: This approach examines the resale price of goods to unrelated parties, deducts a suitable gross profit margin, and arrives at an arm's length price. It's applicable when the distributor or reseller adds substantial value.

Transactional Net Margin Method (TNMM): TNMM involves comparing the net profit margin from a controlled transaction with the net profit margins of similar uncontrolled transactions. It's particularly valuable when profit margins are considered the most reliable indicator.

Profit Split Method: The profit split method is employed when it's challenging to apply other methods. It divides the combined profits of the related entities in a manner consistent with what unrelated parties would have done in a similar situation.

Any Other Method that Yields an Arm's Length Result: Rwanda's regulations allow the use of any other method that can demonstrate an arm's length result, provided it complies with the arm's length principle.

b) Scenario 1:

The CUP price for microprocessors sold to TechLink Nyamabuye. can be calculated as follows:

Price of microprocessors sold to ubumwe Ltd (per unit) RWF 25,000

Adjustment for transport cost Frw 300

Transfer price (per unit) based on CUP method RWF 25,300

Scenario 2:

The arm's length price for the related party transaction is calculated as follows:

- Sales of tablets by TechCo to unrelated parties RWF 2,800
- Less: Arm's length resale price margin based on Company D's transactions (15% x RWF 2,800) RWF 420
- Less: arm's length price for the promotion and sale of tablets : Arm's length price for promotion and marketing functions performed by TechCo for TabletTech based on transfer pricing analysis RWF 200
- Transfer price (based on resale price method) $2800 - (420 + 200) = 2,180$ RWF

Scenario 3:

The transfer price for the related party transaction can be calculated as follows:

- Direct and indirect costs incurred by Autotech to manufacture one unit of automotive components RWF 75.00
- Arm's length margin (18% x RWF 75.00) RWF 13.50
- Transfer price (based on cost-plus method) RWF 88.50

c) The main features of a Customs Union include the following:

- i. A common set of import duty rates applied on goods from third countries (Common External Tariff, CET);
- ii. Duty-free and quota-free movement of tradable goods among its constituent customs territories;
- iii. Common safety measures for regulating the importation of goods from third parties such as phyto-sanitary requirements and food standards.
- iv. A common set of customs rules and procedures including documentation;
- v. A common coding and description of tradable goods (common tariff nomenclature, CTN);
- vi. A common valuation method for tradable goods for tax (duty) purposes (common valuation system);
- vii. A structure for collective administration of the Customs Union.

QUESTION FOUR

Marking guide

Requirement (a)

0.5 mark for every valid point

4

Requirement (b)

Taxable income declared		0.5
Add Back		
Sales not declared		1
Overstatement of Non-EBM invoices		1
Overstatement of depreciation		1
Total add backs		
Taxable income rectified		0.5
Taxable income rounded off		1
Corresponding tax (30%)		1
Tax paid on declaration		1
Tax not paid		1
Understatement fine (20%)		1
Fixed fine for non-cooperation with the audit team		1
Late payment interests until 15th November 2022		1.5
Total tax due		0.5
<u>Total marks for this section</u>		<u>12</u>

Requirement (c)

Corresponding VAT	1
Administrative fine of ten (10) times	1
Clear comment on penalties	2
Total marks for this section	4

Total Marks for the question

20

Model Answer

- a) A person who, while intending tax evasion, commits one of the following acts:
- Use of forged documents in his or her accounts
 - Counterfeit and use of documents or materials of the tax administration used for taxation
 - Hiding taxable goods or assets related to business
 - Making a declaration indicating that the taxpayer has not made sales
 - Changing the trade name by a person prosecuted in relation to tax
 - Fraudulent registration of trade under the name of another person
 - Hiding accounting documents from the tax administration or damaging them

- Use of forged accounting records; commits an offence of tax evasion.

b) Computation of evaded tax and corresponding penalties:

Taxable income declared		6,761,846
Add Back		
Sales not declared	15,350,000	
Overstatement of non-EBM invoices	1,500,000	
Overstatement of depreciation	12,120,000	
Total add backs	28,970,000	28,970,000
Taxable income rectified		35,731,846
Taxable income rounded off		35,732,000
Corresponding tax (@30%)		10,719,600
Tax paid on declaration		2,028,600
Tax not paid		8,691,000
Understatement fine (20%)		1,738,200
Fixed fine for non-cooperation with the audit team		500,000
Late payment interests until 15th November 2022	working	4,171,680
Total tax due		15,100,880

Working: Late payment interests

$$w=8,691,000*1.5/100*32$$

c) Umurishyo Ltd failed to issue an EBM invoice; it is stipulated by the law that a person registered for the Value Added Tax who sells goods or services without issuing an electronic invoice is liable to an administrative fine of ten (10) times the value of the evaded Value Added Tax.

The corresponding penalty to pay is computed as follows:

Sales to Mr Kanyemera	15,350,000
Corresponding VAT	2,763,000
Fixed fines for not using EBM correctly	200,000
Administrative fine of ten (10) times	27,630,000
Total	27,830,000

In case of the fault will be repeated, the company will be liable to an administrative fine of twenty (20) times the value of the evaded Value Added Tax.

QUESTION FIVE

Marking Guide

Description	Marks
Output VAT	
Exports to DRC	1
standard rated sales	0.5
credit note	1
Standard credit sales	0.5
VAT reverse charge	1
Input VAT	
standard rated purchase	0.5
credit note	1
accounting fee for March 2022	0.5
Purchase of fuel	0.5
VAT reverse charge (unavailable service)	1
Electricity bill	0.5
Telephone expense	1
standard credit purchases	0.5
debit note	0.5
Purchased computers	0.5
rent for March 2022	0.5
legal fees	0.5
VAT payable	0.5
Award 0.5 Mark for each valid point	2
Award 1 mark for explanation and 1 for each condition	4
Explanation on SEZs	2
Total	20

Model Answers

a) Computation of the VAT payable

Output VAT

Date	Description	working	Amount FRW "000"
03/04/2022	Exports to DRC	zero rated	-
03/06/2022	Standard rated sales	405,700 *18/118	61 886
07/03/2022	Credit note	100,000*18/118	- 15 254
03/09/2022	Standard credit sales	128,500 * 18/118	19 602
03/15/2022	VAT reverse charge	30,000 *18/100	5 400
	Total output VAT		71,634

**Input
VAT**

Date	Description	working	Amount FRW "000"
03/02/2022	Standard rated purchase	265,000 * 18/118	40 424
03/07/2022	Credit note	95,000*18/118	-14 492
03/12/2022	Accounting fee for March 2022	26 500 * 18/118	4 042
03/15/2022	Purchase of fuel	Exempt	0
03/15/2022	VAT reverse charge	30,000 * 18/100	5 400
03/18/2022	Electricity bill	3,900 * 18/118	595
03/21/2022	Telephone expense	(1,950 * 18/118) * 60/100	178
03/24/2022	Standard credit purchases	205,000*18/118	31 271
03/25/2022	Debit note	Given	0,55
03/29/2022	Purchased computers	Exempt	0
03/31/2022	Rent for March 2022	5,000*18/118	763
03/31/2022	Legal fees	2,000*18/118	305
	Total inputs VAT		68 487

VAT payable (71634,000 - 68,487,000)=

3,147,000

ii. VAT TAX POINT

The article 10 of the law no 37/2012 of 09/11/2012 establishing VAT states that the taxation period for the supply of the goods and services shall be the one that is the earliest among the following:

1. The date of issuance of the invoice
2. The date of payment for goods and services whether in whole or partial except the advance payment made to the constructors who reimburse it from invoices presented to the client.
3. The date on which goods are removed from the premises of the supplier or when they are given to the recipient
4. The date of the service delivery.

iii. Post sale adjustment for unrecoverable debts.

The article 10 of the law no 37/2012 of 09/11/2012 establishing VAT states that if a taxpayer has supplied goods or services for consideration and has paid all the tax on these goods and services to the Commissioner general but has not within 24 months after delivery of such goods and services received payment in whole or in part from the recipient, the taxpayer is allowed a refund of the tax paid for which he/she did not receive.

The following are conditions to be fulfilled

1. An amount equivalent to the debt was previously included in the value of the taxable goods or services.
2. The debt is written off from the books of accounts of the supplier of goods or services

3. The supplier of goods or services has taken all possible steps in pursuing payment but has shown convincing evidence that the debtor is insolvent.

b) Here's a general overview of how VAT typically worked in SEZs in Rwanda:

Exemptions

Depending on the specific SEZ and the type of business activity, certain exemptions or incentives related to VAT are available. These include reduced VAT rates or exemptions on specific goods or services.

Investors in SEZs can be eligible for VAT refunds or credits on eligible inputs used for their business operations, as long as they comply with the SEZ regulations.

Registration and Compliance:

Businesses operating within SEZs are typically required to register for VAT with the Rwanda Revenue Authority. They are also required to maintain proper VAT records and submit periodic VAT returns.

Customs Procedures:

SEZs often have specific customs procedures to facilitate the importation of goods into the zones. Customs clearance procedures within SEZs are generally streamlined to encourage trade and investment.

END OF MARKING GUIDE AND MODEL ANSWERS