STRICTLY CONFIDENTIAL

THE PUBLIC ACCOUNTANTS EXAMINATION COUNCIL OF MALAWI

2011 EXAMINATIONS

ACCOUNTING TECHNICIAN PROGRAMME

PAPER TC 10(B): TAXATION

MONDAY 5 DECEMBER 2011 **TIME ALLOWED: 3 HOURS**
9.00 AM - 12.00 NOON

SUGGESTED SOLUTIONS

SECTION A

BOTH QUESTIONS TO BE ANSWERED IN THIS SECTION

1. (a) (i) Capital allowances

	Buildings	Plant & Machinery	Motor vehicles	Furniture & Fittings	Computers
	K'000	K'000	K'000	K'000	K'000
B/fwd 1/10/09	14,500	7,500	6,200	2,600	1,500
Additions	2,500	3,750	8,400	-	840
Disposals		(500)	(120)	-	
	17,000	10,750	14,480	2,600	2,340
Investment	(2,500)	(3,000)	-		
Initial			(1,000)		(168)
Annual	(725)	(775)	(2,896)	(260)	(926)
	13,775	6,975	10,504	2,340	1,246

(ii) Capital gain or loss

	Proceeds	TWDV	Gain/(loss)
Saloon	250,000	120,000	130,000
Production machine	-	500,000	(500,000)
Net loss			370,000

(b)

		K'000	K'000
Profit before tax			8,860
Add back:	Depreciation	4,200	
	Pension costs	2,350	
	Property revaluation	140	
	Penalty for PAYE late payment	260	
	Interest on Directors loans	52	
	Donation Malawi Christian Church	25	
	Fringe benefits tax	600	7,627
			16,487
Less:	Tax free interest	10	
	Dividends from	1,450	
	Capital allowances	3,500	4,960
	Taxable income		11,527
	Tax at 30% x 11537		3,458.10

(c) Additional investment allowance, according to paragraph 4(2) of the Second Schedule is an allowance that is given to a taxpayer who is eligible for the investment allowance and who invests in an area designated for such additional allowance by the minister by order published in the gazette.

(d) A manufacturer shall include the owner of a business carried on in buildings with the definition of industrial building contained in paragraph 8 of Second Schedule of the Taxation Act and the owner of a plantation producing tea, coffee, tobacco, sugar, cocoa or such other crop as the Minister may approve.

(Paragraph 10(3) of Second Schedule to the Taxation Act)

2. (a) (i) There are two types of clubs and these are as follows:

(1) Clubs which are formed or operated solely or principally for
- social welfare
- civic improvement
- other similar purposes

and which do not distribute any of their income to the members

(2) Those which are formed or operated solely or principally for
- pleasure
- recreation

(ii) Income tax treatment
The income of clubs, societies and associations which are formed or operated solely or principally for social welfare or civic improvement are exempt from Taxation.

(Paragraph (iv) First Schedule of the Taxation Act)

Taxable income of clubs formed or operated solely or principally for pleasure or recreation is subject to tax.

(Section 61(1) of the Taxation Act)

(b) The taxable income of a club or association which is subjected to taxation is deemed to be an amount equivalent to 6¼% of all receipts of the club or association from:

- sales of goods
- cinematograph performances
- stage plays and
- gambling machines

(c) (i) Computation of taxable income of Katuka club for the financial year ended 31 December 2010.

	K'000
Sale of food	600
Sale of drinks	600
Video shows	460
Live band performances	560
Gambling machines	60
	2,280
Taxable income 6¼% thereon	142.50

(ii) Tax on K55,600
Tax rate 30%
Tax payable 55,600 x 30% = 16,680

(iii) It will be assessed in 2010/2011 tax year.

(d) For purposes of the Taxation Act a qualified reorganization means:

- re-organisation pursuant to a written plan
- undertaken for valid business purposes
- does not have its purpose tax avoidance by any person who is party to the reorganization

(e) A public officer is an employee who the company appoints to be responsible for ensuring that all taxation matters are properly dealt with.

SECTION B

ANSWER THREE QUESTIONS ONLY FROM THIS SECTION

3. (a) The term 'foreign currency liability' means a liability which is denominated in foreign currency.

or

the amount of which is determined by reference to a foreign currency and include notes and coins of such foreign currency.

(b) (i) Total value of goods at time of establishing the transaction.

Value in foreign currency = $200,000
Rate $1 = 152
Therefore value $200,000 x 152
= K30,400,000

(ii) April 2010 payment

ar1 –ar2

Amount of 1st repayment $40,000
∴ (40,000 x 152) – (40,000 x 154)
6,080,000 – 6,160,000
Loss (K80,000)

October 2010 payment
Amount of payment $85,000
∴ ($85,000 x 152) – ($85,000 x 150)
12,920,000 - 12,750,000

Gain K170,000
Dec 2010 payment = $75,000
∴ ($75,000 x 152) – ($75,000 x 159)
= 11,400,000 – 11,925,000
Loss K525,000

(iii) Net gain loss from transactions above
= (K80,000) + 170,000 – (525,000)
= Net loss = K435,000
Gain or loss if paid in April
(200,000 x 152) – (200,000 x 154)
= 30,400,000 – 30,800,000
Loss = K400,000
∴ K435,000 – K400,000
= K35,000 savings

(iv) Realised foreign exchange losses are deductible in full except where the taxpayer has unrealized foreign exchange gains.
Where there are unrealized foreign exchange gains, the realized foreign exchange losses to be allowed as a deduction will only be excess of the realized foreign exchange losses over the unrealized foreign exchange gains.

(Section 28(5) of the Taxation Act)

(v) The amount of realized foreign exchange losses not allowed as a deduction is carried forward to future tax years under similar restriction provisions.

(Section 28(5) of the Taxation Act)

(c) Cost of goods as calculated in b(i)
= K30,400,000
Add duty at 25% = 30,400,000 x 25%
= 7,600,000
38,000,000

Add VAT @ 16.5% = 38,000,000 x 16.5%
= 6,270,000
Total cost ∴ = K44,270,000

4. (a) (i) Direct taxes are assessed on income or property with the expectation that the persons from whom the tax is collected lose purchasing power.

Indirect taxes or collected from producers or sellers in the expectation that they will pass it on to consumers.

(Refer to MCA Taxation Manual)

(ii) Examples of direct taxes are:

- Income tax and
- property tax (city rates)

Examples of indirect taxes are:

- Value added tax
- Customs duty
- Excise duty

(b) (i) Income for an individual

Basic salary (220,000 x 3) + (250,000 x 6)

660,000 + 1,500,000

= K2,160,000

Housing allowance (25% x 220,000 x 3) + (25% x 250,000 x 6)

165,000 + 375,000

K540,000

⇒ Christmas bonus	110,000	
⇒ Clothing allowance	75,000 x 3	= K225,000
⇒ Motor vehicle allowance	62,500 x 9	= K562,500
Total		= K3,597,500

(ii) Tax payable: on K3,597,500

1st 120,000	@ 0% =	0
Next 36,000	@ 15% =	5,400
Balance 3,441,500	@ 30% =	1,032,450
		1,037,850

(iii) Total tax payable K1,037,850 ½

Less tax paid under PAYE K

(45,000 x 3) + (55,000 x 6)

135,000 + 330,000 = 465,000

Balance 572,850

5. (a) (i) The imposition of penalties under the Taxation Act is meant to achieve:

- compliance by the taxpayers
- collection of revenue by the government
- enforcement of rules and regulations contained in the taxation Act.

(ii) In certain circumstances:

- the taxpayers will not pay the penalties as they will appeal against such penalties and therefore money will not be realized
- some penalties are not adequate to motivate taxpayers to pay as some taxpayers would appear to benefit more from the non-compliance.

(b) (i) If it appears to the commissioner that any taxpayer is unable for any cause to furnish an accurate return of income, the commissioner may accept the taxpayers estimate of the amount of his taxable income.

(Section 89(2) of the Taxation Act)

(ii) The commissioner may estimate the taxpayers income in the following cases.

1. where a taxpayer makes default in furnishing any return or information; or
2. where the commissioner is not satisfied with the return or information furnished by the taxpayer
3. where the commissioner has reason to believe that a taxpayer is about to leave Malawi without furnishing a return or a satisfactory return.

(Section 89(1) of the Taxation Act)

(c) (i) An entity is registable as taxable for purposes of the Value Added Tax (VAT) Act where:

(i) the entity makes taxable supplies of goods or services

(ii) the business turnover is K6,000,000 or more.

Any entity which satisfies criterion (i) above and whose business turnover is below the K6,000,000 mark stipulated in (ii) above may apply for voluntary registration.

(ii) The VAT Act does allow group registration provided

- one company must control the other (as is the case here)

- the commissioner general approves registration

- both companies remain jointly and severally liable for VAT payable by the group.

However Income Tax Act does not allow group registration of a company and its subsidiary.

(d) (i) Conditions to be fulfilled
The taxable person must:

- be in business of hiring motor vehicles
- be in the business of selling of motor vehicle spare parts, or

- use motor vehicle or motor vehicle spare parts
- wholly
- exclusively and necessarily in his or her business

(ii) According to Section 14 (i)

- Income of a taxpayer shall include any amount of annuity received.
- Excluded will be the amount representing undeducted purchase price in case of an annuity which has been purchased.

6. (a) (i) The provision of cash allowances does not constitute a fringe benefit as is defined in the Taxation Act.
The allowance if paid in cash is taxable in the hands of the employee.

(ii) The employer can be allowed to shoulder the tax burden relating to cash allowances.
In these circumstances then the employer will be required to pay extra tax on the arrangement to have tax paid by the employer.

(iii) The house to be made available to the employee must belong to the employer.

When this is so, the taxable value of the housing benefit is reduced by 50%.

Following this reduction, the fringe benefits tax payable by the employer is similarly reduced.

(iv) In addition to the reduction in the taxable value of the housing fringe benefit and fringe benefits tax payable the provision of gardener, security guard and watchman does not constitute a taxable fringe benefit.

(v) The tax liability arising from cash allowance paid to the employee for school fees may be reduced if, instead of paying the allowance, in cash direct to the employee, the money is paid direct to the institution.

The tax burden thus shifts from the employee to the employer.

The employer becomes liable to fringe benefits tax as he has provided a taxable fringe benefit.

Additionally there is a 50% reduction in taxable value where the fees is paid to the institution, resulting in reduced tax liability of the employer.

(b) Fringe benefits tax computation

Housing accommodation

Taxable value calculation

Rental value = 120,000

10% of salary x 45,000 = 45,000 since unfurnished

Therefore taxable value = K120,000

3 months benefit = 120,000 x 3 = K360,000

Motor vehicle

15% of 7,500,000 = 1,125,000 p.a.

3 months = $\frac{1,125,000}{12}$ x 3 = 281,250

School fees

K250,000 per quarter, taxable value = K250,000

Taxable value = 50% x 250,000 = K125,000

Summary of taxable values for quarter ended 30 September

		K
Housing Accommodation	=	360,000
Motor vehicle	=	281,250
School fees	=	125,000
		766,250
Tax at 30%	=	K229,875

7. (a) Five offences committed by (any person) listed under Section 112 of the taxation Act.

(i) failure to comply with any notice served as the taxpayer by the Commissioner under the taxation Act.

(ii) the taxpayer gives any incorrect information or omits any relevant information from any statement required to be made to the commissioner under Section 20.

(iii) failure to keep records, books or accounts as required to be kept under Section 54.

(iv) being a public officer of a company, fails to furnish to the commissioner documents and particulars relating to the notification of dividends declared as required under Section 69.

(v) failure to furnish the commissioner returns or particulars relating to persons employed by him as required under Section 85.

(vi) the taxpayer or his agent fails to furnish any other persons with a certificate as required under Section 87(3).

(vii) fails to deduct the tax due, or to remit to the commissioner tax deducted, under Section 76.

(b) Where a taxpayer makes up his accounts for a period of 12 months ending on some day other than 30 June, the Commissioner may in his discretion accept such accounts for assessment in respect of the assessment year ending on 30 June prior or subsequent to the closing date of such accounts and no part of such assessment shall be charged to tax in any other year of assessment.

All subsequent accounts of the taxpayer shall unless the commissioner otherwise agrees, be made up for each succeeding period of 12 months ending on such other date.

(c) (i) Mining expenditure is capital expenditure incurred in Malawi by a person carrying out or about to carry out mining operations in Malawi. The capital expenditure herein includes:

- Searching for or in discovery and testing or winning access to deposits or minerals.

- In the acquisition of or of rights in or over such deposits, other than the acquisition from a person who has carried on many operations in relation to such deposits.

- In the provision of plant and machinery and industrial buildings which would have little or no value to such person if the mine ceased to be worked.

- On the construction of any buildings or works which would have little or no value if the mine ceased to be worked.

- On development, general administration and management prior to the commencement of mining operations.

(ii) Mining expenditure to 30 June 2010

	K
Construction of site buildings	52,000
Acquisition of machinery	122,000
Testing of samples	17,000
General administration	45,000
	236,000

The whole K236,000,000 would be deductible in the first year of assessment.

(iii) Mining expenditure for the period to 30 June 2011

	K
Acquisition of mining rights	5,000
Additional site building	22,000
Motor vehicles and trucks	116,000
General administration	54,000
	197,000

The allowance in this year shall be apportioned normally based on time of use by each of the mining companies Nobia and Kayera as follows:

	K
Nobia July to Dec = 6 months = 50% x 197,000	98,500
Kayera Jan to June = 6 months = 50% x 197,000	98,500

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