STRICTLY CONFIDENTIAL

THE PUBLIC ACCOUNTANTS EXAMINATION COUNCIL OF MALAWI

2014 EXAMINATIONS

ACCOUNTING TECHNICIAN PROGRAMME

PAPER TC10(B): TAXATION

TUESDAY 3 JUNE 2014 **TIME ALLOWED: 3 HOURS**
9.00 AM – 12.00 NOON

SUGGESTED SOLUTIONS

SECTION A

ANSWER BOTH QUESTIONS IN THIS SECTION

1. (a) (i) Taxable income for Tonamwana Limited

	K'000	K'000
Profit before taxation		155,400
Add back: Depreciation	11,500	
Depreciation	7,500	
General provisions	300	
Exchange gain realized	2,400	
Repairs and maintenance	380	
Fringe benefits tax	6,200	28,415
		183,815
Less: Capital allowance	15,750	
Exchange gain per A/Cs	1,200	
Exchange loss realized	800	(17,885)
Training allowance	135	
Taxable income		165,795

Tax payable = 165,795,000 x 30% ½ = K49,738,50

(ii) In the 2012/2013 tax year i.e. 1 July 2012 – 30 June 2013.

(iii) 30 June 2013.

(iv) 1. Tax payable = 167,000,000 x 30% = K50,100,000

2. Tax payable = 167,000,000 x 35% = K58,450,000

(b) Where the taxable income for the year of assessment is estimated;

- not to exceed K180,000 or the prevailing tax free limit.
- to exceed K180,000 or the tax free limit but is all from employment or from pension or both employment and pension and in relation to which PAYE tax is being deducted.
- to exceed K180,000 or the tax free limit and to include non-employment or non-pension income of not more than K180,000 or the tax free limit.

(c) Expenditures not allowed under section 45 of the Taxation Act:

(i) The cost incurred by any taxpayer in the maintenance of himself, his family or establishment.

(ii) Domestic or private expenses of the taxpayer including the cost of travel between the taxpayer's residence and place of work.

(iii) Any loss or expense which is recoverable under any insurance contract or indemnity.

(iv) Tax upon the income of the taxpayer or interest payable thereon whether charged in terms of this Act or any other law of any country whatsoever.

(v) Income carried to any reserve fund or capitalized in any way.

(vi) Any expenses incurred in respect of any amounts received or accrued which are not included in the term income as defined in the taxation Act.

(vii) Any expense in respect of which a subsidy has been or will be received.

(viii) Fringe benefit tax and any penalty chargeable thereon.

2. (a) Investment allowance is given to a taxpayer:

- who is also a manufacturer;
- on the cost of industrial buildings and plant and machinery;
- which is brought into use by the taxpayer during the year of assessment;
- is used by the taxpayer in the process of manufacture for the purpose of his business of a manufacturer.

(b) (i) Capital Allowances for year to 31 December 2013

	Factory Buildings	Plant & Machinery	Motor Vehicles	Furniture & Fittings
	K'000	K'000	K'000	K'000
Written Down Value 1/1/2013	18,900	9,500	14,400	7,700
Additions	-	4,200	12,500	2,800
	18,900	13,700	26,900	10,500
Disposals	-	(250)	(620)	(120)
	18,900	13,450	26,280	10,380
Investment allowance	-	(4,200)	-	-
Initial allowance	-	-	-	(560)
Annual allowance	(945)	(925)	(5,256)	(1,038)
Written down value 31/12/13	17,955	8,325	21,024	8,782

(ii) Capital gain or loss

	Plant & Machinery	Motor vehicles	Office furniture
	K'000	K'000	K'000
Proceeds	850	350	695
TWDV	(250)	(620)	(120)
	600 gain	(270) loss	575 gain

(iii)

	K'000
Proceeds	850
Less net book value	860
Accounting loss	(10)

(c) (i) The tax in the four schemes is payable as follows:

(1) PAYE - Within 14 days after the end of the month in which the tax was deducted.

(2) Provisional tax - Within 25 days after the end of each quarter in the year of assessment.

(3) Fringe benefits - Not later than 14 days after the end of each quarter in the year of assessment.

(4) Withholding tax - Within 14 days from the end of the month in which the deduction was made.

(ii) Penalty rates:

PAYE - 20% of the tax payable and a further additional 5% per month or part thereof.

Provisional tax - No penalty where the tax not paid does not exceed10% of the total tax liability.

- 25% of the tax not paid where such unpaid tax exceeds 10% but does not exceed 50%.

- 30% for tax not collected exceeds 50%.

Fringe benefits tax - 20% of unpaid tax.

Withholding tax - 20% of the tax not paid on time

SECTION B

ANSWER THREE QUESTIONS ONLY FROM THIS SECTION

3. (a) Wholly, exclusively and necessarily means that an expenditure:

- must be specific for the business.
- expenditure that would be necessary to produce income or for the trade.
- dual purpose expenditure would be disallowed.
- private purpose expenditure is not allowed.

(b) (i) Bad debts are those that:

- They must be proved to be bad to the satisfaction of the Commissioner.
- They must have become bad during the year of assessment.

Doubtful debts are those that:

- They must be specific and not general.
- The amount to be considered for an allowance must be only that part of the debt considered doubtful and not necessarily the whole debt.

(ii) The income of the taxpayer must include the amount of the provision allowed as a deduction in the previous year of assessment. This adjustment is not affected by whatever happens to the debt itself.

<u>If debt remains unpaid</u>

A new provision is claimed that is if the debt continues to be considered doubtful.

<u>If debt recovered</u>

There will be no need to make a new provision since the debt is recovered.

<u>If the debt has become bad</u>

The debt will now be written off and the write off will be allowed as a deduction if conditions are satisfied.

(c) (i) The capital loss of K320,000 would not be deductible from assessable income.

(ii) <u>Only K270,000</u> would be allowed as a deduction as there will be a restriction on the amount deductible to <u>the lesser of the realized capital loss or any capital gain realized by the taxpayer</u>.

(d) The answers <u>would differ if the</u> assets attracted capital allowances. <u>There is no restriction</u> on assets which attract capital allowances. Therefore in both (c)(i) and (c)(ii) the full amounts of K320,000 and K420,000 would be allowed as a deduction from assessable income.

(e) The Commissioner may estimate the taxpayers' income where:

(1) a taxpayer makes default in furnishing any return or information; or

(2) the Commissioner is not satisfied with the return or information furnished by the taxpayer.

(3) the commissioner has reason to believe that a taxpayer is about to leave Malawi without furnishing a return or a satisfactory return.

(f) (i)
- Monetary
- Imprisonment.

(ii) Any three of the following:

- making a false statement or giving false information
- keeping false books of account or other records
- making a false claim for repayment of any tax
- omission of income from a return
- claiming any deduction of allowance to which one is not entitled or allowed.

4. (a) (i) For a club to be exempt it needs:

– to be formed and operated solely or principally
– for – social welfare
  – civic improvement or
  – other similar purposes and

– If its receipts or accruals are not shared among the members.

(ii) The taxable income is 6.25% of its gross receipts and accruals from:

– sales of goods
– cinematograph performances
– stage plays
– gambling machines
– rate applicable to companies

(b) Kabuli Sports club taxable income computation

	K
Bar receipts	375,000
Gambling machines	322,000
Stage plays	319,000
Cinematograph performances	291,000
	1,307,000

Taxable income = 6.25% x 1,307,000	=	K816,875
Tax payable = 816,875 x 30%	=	K245,062.50

(i) Fringe benefit is any asset service or other benefit in kind provided by or on behalf of an employer to an employee if such benefit includes an element of personal benefit to the employee.

(ii) If an employee contributes towards a fringe benefit provided to him.

- the taxable value of the benefit will be reduced by the amount of the contribution.
- the employer will pay less tax on the benefit as a result.
- the employee's tax status is unchanged as it is not affected by the contribution.

(iii) Where the property is owned by the employer:

- the cost of a gardener shall not constitute a taxable fringe benefit.
- the cost of security guard and watchman shall not constitute a fringe benefit.
- the taxable value will be reduced by 50%.

5. (a) (i) One common feature between exempt and zero rated supplies is that VAT is not payable in respect of both supplies.

(ii) Main differences are:

- Exempt supplies are not subject to VAT; while
- Zero rated supplies are subject to VAT;
- Input tax is not claimable in respect of exempt supplies; while
- Input tax is claimable in respect of zero rated supplies.

(b) A taxable supply becomes a relief supply if the supply is made to:

- individuals;
- organizations; and
- businesses.

Specified in the Third Schedule to the VAT Act.

The user of the goods and services that qualify as relief supplies enjoys an advantage in that no VAT is payable because of the relief that is given.

(c) A taxable person qualifies for input tax deduction in respect of taxable supply of motor vehicles or motor vehicle spare parts if the taxable person is in the business of:

- dealing in motor vehicles; or
- hiring of motor vehicles; or
- selling of motor vehicle spare parts.

However, where the taxable person uses the motor vehicles or motor vehicle spare parts:

- wholly
- exclusively; and
- necessarily

for the business, such taxable person shall qualify for input tax deduction in respect of such motor vehicles and motor vehicle spare parts

(d) (i)

	VAT
VAT on services	
Telephone	74,250
Electricity	28,875
Security	56,925
Stationery	37,290
Rent	86,130
	283,470
Add: VAT on raw materials	
$\frac{1,689,250}{116.5} \times 16.5$ =	239,250
Total	522,720

(ii)

Value of exports	K4,200,000
VAT thereon at 0%	-
Total value of export sales	K4,200,000
Value of local sales	6,300,000
VAT on sales at 16.5%	1,039,500
	7,339,500

Total value of VAT on sales therefore 0+1039500 = K1039500

(iii)

	K
Total value of VAT on sales	1.039,500
Total VAT on purchases	522,720
VAT payable	516,780

6. (a) Section 58 allows taxpayers who are engaged in pastoral, agricultural or other farming operations:

(i) Stumping, clearing and leveling of lands;

(ii) Works for the prevention of soil erosion;

(iii) Boreholes;

(iv) Wells;

(v) Aerial and geographical surveys;

(vi) Any water control work connected with the cultivation and growing of rice, sugar or such other crop as the minister may approve.

(b) Farmers who derive their taxable income from growing timber may elect that their taxable income be determined as follows:

(i) The cost of planting the timber to be carried forward until the timber has reached maturity.

(ii) To the cost above, until the timber has reached maturity a fixed percentage of 5% will be added annually.

(iii) When such timber is sold, the proportionate part of the cost and the total of the fixed percentage added annually will be deducted from the proceeds and the balance included in taxable income or assessed loss.

(iv) Each year the annual fixed percentage will be added to the taxable income or deducted from the assessed loss.

(v) All expenditure incurred by the farmer including deductions under Section 33 and Section 34 and the Second schedule on maintenance and upkeep of such timber will be deducted from the taxable income or added to the assessed loss.

(c) Formula for exchange gains/losses

$ar_1 - ar_2$
where a = amount of foreign currency
r_1 = official rate of exchange at the time of establishing the transaction
r_2 = official rate of exchange at the time of the transaction settling.

1st payment September 2012

(3000 x 560) – (3,000 x 525)
1,680,000 – 1,575,000
= 105,000 gain

2nd payment November 2012

(2000 x 560) – (2,000 x 570)
1,120,000 – 1,140,000
= (20,000) loss

3rd payment January 2012

(1500 x 560) – (1,500 x 545)
840,000 – 817,500
= 22,500 gain

(d) Chawaka Limited

Penalty for provisional tax liability for year 2012/2013

Taxable income given	= 72,300,700
Actual tax at 30%	= 30% x 72,300,700
	= 21,690,210
Total tax liability	
% of tax not paid	= 100%
Penalty for amount not paid exceeding 50% is 30%	
Penalty therefore	= 30% x 21,690,210
	= K6,507,063

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

- Searching for or discovery and testing or winning access to deposits of minerals.
- The acquisition of rights over such deposits other than from a person who has carried on mining operations in relation to such deposits.
- The provision of plant and machinery and industrial buildings which would have little or no value if the mine ceased to be worked.
- The construction of buildings or works which would have little or no value if the mine ceased to be worked.

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

(ii) Mining expenditure for the period to June 2012

	K'000
Construction of site buildings	165,000
Acquisition of machinery	425,000
Testing of samples	44,000
General administration & management	126,000
	760,000

The whole expenditure will be claimed as a deduction from assessable income.

(iii) Mining expenditure for year to 30 June 2014

Total expenditure 477,000

The allowance will be apportioned in such a manner as the Commissioner General may determine to be just and reasonable between K & M and Glo Metals i.e. based on time.

K & M Limited = $5/_{12}$ x 477,000 = 198,750
Glo Metals Limited = $7/_{12}$ x 477,000 = 278,250

(b) (i) A taxpayer may appeal to the Commissioner when he/she is aggrieved by:

(1) Any assessment made upon him by the Commissioner
(2) The determination by the Commissioner of a reduction in tax under the double tax relief arrangements **(Sections 123 or 124 of the Taxation Act)**.
(3) Any decision of the Commissioner in relation to an assessment.

(ii) The Commissioner:

(1) may amend the assessment, decision or determination or disallow the appeal;
(2) shall send to the applicant written notice of his decision on the appeal;
(3) shall record any amendment of the assessment in the assessment register.

(iii) Direct taxes are assessed on income or property with the expectations that the persons from whom the tax is collected losses purchasing power. Examples are income tax and property tax.

Indirect taxes are collected from products or sellers in the expectation that they will pass it on to consumers. Examples are value added tax, customs duty.

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