

**INSTITUTE OF BANKERS IN MALAWI**

**DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: TAXATION 1 (IOBM – D213)**

**Date: Tuesday, 10th November, 2015**

**Time Allocated: 3 hours (13:30 – 16:30 hours)**

**INSTRUCTIONS TO CANDIDATES**

1 This paper consists of **TWO** Sections, A and B.

2 Section A consists of 4 questions, each question carries 15 marks.

Answer **ALL** questions.

3 Section B consists of 4 questions, each question carries 20 marks. Answer **ANY TWO** questions.

4 You will be allowed **10 minutes** to go through the paper before the start of the examination, you may write on this paper but not in the answer book.

5 Begin each answer on a new page.

6 **Please write your examination number on each answer book used. Answer books without examination number will not be marked.**

7 All persons writing examinations without payment will risk expulsion from the Institute.

8 If you are caught cheating, you will be automatically disqualified in all subjects seated this semester.

9 DO NOT open this question paper until instructed to do so.

**SECTION A (60 MARKS)**

Answer **ALL** questions from this section.

**QUESTION 1**

1. Define Assessable Income in line with Section 11 of the Taxation Act. *(3 marks)*
2. Mrs Mbewe who had worked in Holland for ten years as an ambassador came back to Malawi in 2014. He immediately set up a Coffee shop in the city of Zomba. The following figures are contained in his records for the tax year ending 30 June 2015;

MWK

**Income**

Profit from the coffee shop 5,455, 000

Salary (Gross) 1,000,000

Bank Interest

* Standard Bank in Malawi (Gross) 80,000
* Bank in Holland (Gross) 455,000

Capital Gain 765,500

Rent (Gross) 540,000

Dividends from a Malawian Company net of tax 136,000

**Expenditure**

Donations

* MAP 2,000
* Malawi Red Cross 54,000
* Black man’s Church 5,000

Repairs 155,400

Insurance 25,540

Mortgage repayment 678,000

**Notes**

1. The Coffee shops’ profit is for the period of 15 months, from 1 April, 2014 to 30 June 2015; all other transactions related to the tax year ending 30 June, 2015. Assume that the coffee evenly throughout the period.
2. In arriving at the coffee shop profit, Mrs Mbewe’s cash drawings of K450,000 were deducted. She drew the cash in January, 2015.
3. The salary shown above was in respect of a part time assignment which Mrs Mbewe accomplished between January 2015 and May 2015.
4. The capital gain was realized from the sale of one of Mrs Mbewe’s personal car.
5. Repairs, insurance and mortgage relate to the house which Mrs Mbewe received rent. The mortgage repayment is made of K478, 000 interest and the balance loan repayments.

**Required:**

1. Compute taxable income for Mrs Mbewe’s for the tax year ended 30 June, 2015. *(7 marks)*
2. Give reasons why you have excluded any income or expenditure from the computation of taxable income for Mrs Mbewe in (i) above.

*(2.5 marks)*

1. What are tax credits? *(1 mark)*
2. Calculate tax credits on the following transactions; K1, 000, 000 salary earned evenly over a period of five months; K80, 000 interest earned from Standard Bank in Malawi and K540, 000 rental earned for rent out a house. *(4.5 marks)*

**(Total 15 marks)**

**QUESTION 2**

1. Chikondi is running a manufacturing business. The capital allowances Schedule as at 1 July, 2014 contained the following information:

|  |  |  |
| --- | --- | --- |
| **Asset Type** | **Tax Written Down Value in MK’000** | **Annual Allowance Rate** |
| Fa Factory Building | 58, 800 | 5% |
| Plant and Machinery | 20, 400 | 10% |
| Motor vehicles | 45, 200 | 20% |
| Furniture and Fittings | 12, 600 | 20% |

During the year to 30 June 2015, the following transactions were recorded:

**Fencing**

Fencing of the factory which started in 2013 was completed and brought into use during the year under review and an amount of K1,475, 000.00 was spent in this final phase.

**Plant and Machinery**

Some aging machinery was sold for K1, 225, 000. This sale resulted in a capital loss of K500, 000. New replacement machinery was acquired at a cost of K6, 900,000.

**Motor Vehicle**

One motor vehicle with a tax written down value of K2, 380,000 was sold for K3, 450, 000. A replacement vehicle, saloon type was acquired at a cost of K15, 200, 000.

**Furniture and Fittings**

Additional furniture and fittings were acquired at a cost of K1,250, 000.

**Staff Housing**

One staff house was constructed at a cost of K11, 700, 000. It is the taxpayer’s programme to construct at least one staff house every year until pressure on staff housing is reduced.

**Required:**

1. Calculate the tax written down value of the machinery that was sold. *(2 marks)*
2. Calculate the capital gain or capital loss on the motor vehicle that was sold. *(2 marks)*
3. Calculate capital allowances due for the year to 30 June 2015.

(Assume initial allowance has been claimed where appropriate.) *(11 Marks)*

**(Total 15 Marks)**

**QUESTION 3**

Malola Limited is incorporated in Malawi and manufactures Potato Crisps. The company’s summarized Profit and Loss Account for the year ended 31 December, 2014 is as follows:

|  |  |  |  |
| --- | --- | --- | --- |
| **Details** | **Notes** | **MK’ 000** | **MK’ 000** |
| **Sales** |  |  | **256, 000** |
| Cost of sales |  |  | 170, 400 |
| **Gross Profit** |  |  | **85, 600** |
| Interest |  |  | 3, 000 |
| **Overheads** |  |  |  |
| Depreciation | 1 | 17, 600 |  |
| Audit fees |  | 1,400 |  |
| Bad debts |  | 2,840 |  |
| Doubtful debts | 2 | 800 |  |
| Net exchange [gains] | 3 | [400] |  |
| Repairs and maintenance | 4 | 8, 300 |  |
| Fringe benefit tax |  | 650 |  |
| Staff expenses |  | 11, 400 |  |
| Directors fees |  | 320 |  |
| Other allowable expenses |  | 14, 400 |  |
| **Total Overheads** |  |  | **57, 310** |
| **Total Profit before Tax** |  |  | **31,290** |

Notes

1. Included in the cost of sales is K12,000,000 in respect of plant and equipment depreciation.
2. Doubtful debts are made up of the following:

**K’000**

Specific provision 500

General provision 300

800

3. Net exchange gains are in respect of imported machinery and are made up of the following:

**K’000**

Exchange gains - realized (2,200)

Exchange losses - realized 1 500

Exchange losses - unrealized 300

**Total Net Exchange Gains** **(400)**

In the previous years all exchange gains and losses were realized.

1. Repairs and maintenance includes an amount of K2, 300,000 for repairs for the Managing Directors personal car.

5 Capital allowances are agreed at an amount of K14, 500,000.

**Required:**

1. Compute the taxable payable for the accounting year ended 31 December, 2014. Briefly explain your reasons for each adjustment to the accounting profit before tax. *(7 marks)*
2. In which tax year is this tax going to be assessed? *(1 mark)*
3. By when is Malola Limited expected to have submitted the income tax return? *(1 mark)*
4. How much tax would Malola Limited pay if it was a foreign company?

*(1 marks)*

1. Define the term “mining expenditure” as provided in part II of the second schedule to the Taxation Act. *(5 marks)*

**(Total 15 Marks)**

**QUESTION 4**

(a) (i) Describe the **two** types of clubs or associations which are recognized under the Taxation Act. *(3 marks)*

(ii) How is income of such clubs, societies or associations treated for tax purposes?  *(2 marks)*

(b) (i) Where a club or association is subject to tax, state how the taxable

income is computed. *(3 marks)*

(ii) Mandevu Sports Club, which is a taxable club, carried out the following transactions in the year ended 31 December 2014:

Income : K5,670,000

This was made up as follows:

|  |  |
| --- | --- |
| Ground entrance fees  Rentals from accommodation  Sale of food  Sale of drinks  Club membership fees  TV shows – live football  Live band performances  Gambling machine | K’000  1,220  1250  5 90  1650  380  1 70  120  290  5,670,000 |

**Expenses : K2, 875,000**

The breakdown was as follows:

|  |  |
| --- | --- |
| Trading licence  Food licence  Salaries and wages  Cost of goods sold  Repairs and maintenance | K’000  1 40  150  1,480  685  420  **2,875,000** |

**Required**

# (i) Compute the taxable income of Mandevu Sports Club for the financial year to 31 December 2014. *(3 marks)*

(ii) Calculate the amount of tax payable on the taxable income computed in (i) above. *(3 marks)*

(iii) State the tax year in which the taxable income computed in (i) above will be assessed. *(1 mark)*

**(TOTAL 15 marks)**

**SECTION B (60 MARKS)**

Answer **ANY TWO** questions from this section

**QUESTION 5**

(a) Mr. Kadango is a registered taxpayer and operates the following tax schemes:

(1) PAYE (Pay As You Earn)

1. Provisional tax

(3) Fringe Benefits Tax

(4) Withholding tax

**Required:**

1. State when the tax in each of the four schemes is payable.

*(4 marks)*

(ii) State the rate at which a penalty for late payment is charged

in respect of each of the above tax schemes. (*6 marks)*

# (b) Non-resident tax is not payable on certain types of income.

**Required:**

(i) State those types of income. *(2 marks)*

(ii) Why is taxation an important instrument to governments? *(4 marks)*

(c) An individual taxpayer had a taxable income amounting to K9, 475,000 arising from employment, rents and interests as at 30 June 2014. The amount was agreed to by the Commissioner.

**Required:**

Calculate the tax payable by the taxpayer. *(4 marks)*

**(TOTAL: 20 marks)**

**QUESTION 6**

1. List any **five** general conditions that all traders dealing with goods and services that attract Excise Tax must comply with according to the customs and Excise Tax Law. *(2½ marks)*
2. For purposes of Customs duty, the law demands that all goods must be cleared at the border port except in some circumstances where the importer is allowed to clear at an inland port.

**Required:**

Name any four reasons/circumstances that may necessitate the Commissioner General of the Malawi Revenue Authority to allow an importer to clear their goods at the inland port. *(2½ marks)*

1. State the circumstances under which each of the following may be allowed as a deduction from taxpayers assessable income:
2. Bad debts *(3 marks)*
3. Doubtful debts *(3 marks)*
4. Research and experiments *(3 marks)*
5. Individual donations *(3 marks)*
6. Repairs *(3 marks)*

**(Total 20marks)**

**QUESTION 7**

(a) (i) In accordance with the Taxation Act, under what circumstances may a taxpayer appeal to the Commissioner,? *(3 marks)*

(ii) What are the actions available to the Commissioner in a case where an appeal is made to him by the taxpayer?  *(3 marks)*

(b) The Taxation Act provides for a penalty of up to twice the difference between the tax which should have been charged and the tax that was charged if there was any intent to defraud.

**Required:**

(i) What is the penalty reduced to if the offence was done without any intent to defraud? *(1 mark)*

(ii) Why might the higher rate of penalty be so rarely charged?  *(1 mark)*

(iii) State **three** specific offences that the Taxation Act in Section 112 would consider to be evidence of intent to defraud.  *(3 marks)*

(c) Paragraph 9 of the second schedule to the Taxation Act, defines farm improvements. This definition excludes three types of buildings.

**Required:**

Mention the **three** types of buildings.  *(3 marks)*

(d) How is the taxable income of a person carrying a short term insurance business determined? *(5 marks)*

**(Total: 20 marks)**

**QUESTION 8**

1. For purposes of the Taxation Act, define the term ‘amount realized’ in relation to

an asset:

1. that has been sold for cash  *(1 mark)*
2. that has been exchanged for another. *(1 mark)*
3. Calculate the amount of realized capital loss which is deductible from assessable

income in the following circumstances, assuming that the capital loss arises from

the disposal of assets on which no capital allowances were given:

1. a taxpayer has a realized capital loss of K805,000 and there is no realized capital gain.  *(2 marks)*
2. a taxpayer has a realized capital loss of K450,000 and there is a realized capital gain of K280,000. *(2 marks)*

1. How would your answers in (b) above, differ if the capital losses and gains related

wholly to the disposal of assets on which capital allowances had been given?

*(2½ marks)*

(d) How does a foreign exchange loss or gain arise? *(3 marks)*

(e) Ben Chiwala a Malawian business man imported trade goods whose value was

$140,000 in February 2014. On the day of the initial transaction, the rate of

exchange was $1 to K440. Payment for the goods was made in June 2014 and on the

day of settlement; the rate of exchange was $1 to K515.

**Required**

Using the formula provided for in the Taxation Act calculate the foreign exchange gain or loss on the day the payment for the goods was made. *(4 marks)*

(f) A taxpayer’s records for the year of assessment to 30 June 2014 had the following information on foreign exchange transactions:

Realized foreign exchange losses amounted to K756, 000.

Realized foreign exchange gains amounted to K430, 000; and unrealized foreign exchange gains amounted to K330, 000.

**Required:**

How much will be allowed as a deduction and how much will be taxable? Give reasons for your position. *(4½ marks)*

**(TOTAL: 20 marks)**

**END OF EXAMINATION PAPER**

**APPENDIX I**

**TAX RATES AND ALLOWANCES**

**Income Tax Rates: Individuals**

Cumulative Tax Rate MK

0 – 144, 000 0% 0

144, 001 – 180, 000 15% 5,400

180, 001+ 30% –

**Investment Allowances**

New 100%

Second hand 40%

**Provisional Tax Penalty Rates**

If the amount of Provisional Tax unpaid as a percentage of total tax liability

**Penalty**

Does not exceed 10%. Nil.

Exceeds 10% but does not exceed 50%. 25% of the unpaid amount of provisional tax.

Exceeds 50%. 30% of the unpaid amount of provisional tax.