

**INSTITUTE OF BANKERS IN MALAWI**

**DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: TAXATION 1 (IOBM – D213)**

**Date: Tuesday, 15th May 2018**

**Time Allocated: 3 hours (08:00 – 11:00 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 numbers 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 Taxation. *(2 marks)*
2. Discuss **four** key canons of Taxation as described by Adam Smith. *(8 marks)*
3. List and explain any **five** reasons why Governments impose taxes on its citizens. *(5 marks)*

**(Total 15 Marks)**

**QUESTION 2**

1. In relation to income from farming, state five expenditures which have to be taken into account when determining taxable income. *(5 marks)*
2. Section 45 and 46 of the Taxation Act provide for inadmissible deductions for purposes of determining taxable income. Discuss any five inadmissible deductions under these two sections. *(5 marks)*
3. What does the statement “Malawi Taxation is based on Source” mean? (*2 marks)*
4. Section 84A of the Taxation Act requires that taxpayers pay Provisional Tax unless certain conditions regarding the amounts or sources of individual taxpayer’s income are expected to apply.

R**equired:**

Under what circumstances is an individual taxpayer not required to pay Provisional Tax? *(3 marks)*

**(Total 15 marks)**

**QUESTION 3**

1. Chayamba General Suppliers is a firm operating in Malawi. In June 2017 the firm became indebted to a supplier based in the United States of America in the sum of $70,000 on account of merchandise supplied. $30,000 was paid in August 2017 and $25,000 was paid in December 2017. The balance of $15,000 was included in the accounts for 31December 2017 at K10,950,000 million using an exchange rate of $1 = K730.

**Required:**

1. Using the formula specified in the Taxation Act, calculate the foreign exchange gains or losses on the transactions given above to be claimed for the year of assessment to 31 December 2016. Assume the following exchange rates were in use:

|  |  |
| --- | --- |
| June 2017: | $1= Malawi Kwacha K700 |
| August 2017: | $1= Malawi Kwacha K715 |
| December 2017: | $1= Malawi Kwacha K730 *(4 marks)* |

ii) State whether the foreign exchange loss on the outstanding $15,000 which has been converted to K10.95 million and included in the accounts to 31 December 2017 is an allowable deduction. Give reasons for your answer.

*(2 marks)*

1. (i) Under Section 45 of the Taxation Act, the deduction of contributions to a fund

providing for sickness, accident, unemployment or other benefits other than

contributions to an approved pension or provident fund is prohibited.

**Required:**

Mention **five** other types of expenditure whose deduction is similarly prohibited. *(5 marks)*

(ii) The first schedule to the Taxation Act contains several types of interest income

which are exempt from taxation.

**Required:**

Mention any **four** types of such exempt interest income. *(4 marks)*

**(Total 15 marks)**

**QUESTION 4**

**Doritosi Iinvestments** has been in business for a long time buying and selling Cooking oil. The following are the transactions for the year ended 30 June, 2017

Comprehensive Income Statement for the Year ended 30 June, 2017.

|  |  |  |
| --- | --- | --- |
| **Item** | **K’000** | **K’000** |
| Sales |  | 45, 600 |
| Cost of sales |  | [34,000] |
| Gross Profit |  | 11, 000 |
| Administration Costs | 7,000 |  |
| Finance costs | 2, 500 |  |
| Other expenses | 2, 100 | [11, 600] |
|  |  | [600] |
| Other Income |  |  |
| Profit on sale of fixed assets | 460 |  |
| Interest from bank deposit account | 345 |  |
| Sundry Income | 200 | 1005 |
| Profit / [loss] before tax |  | 405 |

The following information is available in connection with these results:

1. Included in cost of sales are the following expenses:

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| |  |  | | --- | --- | |  | K'000 | | Depreciation of equipment | 370 | | Wages to staff | 1, 400 | | Fuel and oil for equipment | 800 | | Painting owners house | 1, 250 | | Business electricity and water | 1, 000 | | Packaging materials | 1, 500 | | Salaries and wages | 3, 500 | | Depreciation for van | 500 | | Advertising | 700 | | Customer entertainment | 200 | | Traffic fines | 900 | | Donation to Kamba LEA School | 450 | |  |
|  |  |

1. Administration costs include:

|  |  |
| --- | --- |
| Salaries and wages | 1, 600 |
| Depreciation furniture | 500 |
| Medical costs – staff | 800 |
| Rent and rates | 2, 400 |
| Professional fees |  |
| Debt collection | 70 |
| Audit fees | 500 |
| Property valuation | 800 |
| Subscription and donations |  |
| Trade magazine | 150 |
| Save the children fund | 650 |
| Fringe benefits tax | 400 |

1. Finance costs include:

|  |  |
| --- | --- |
| Bad debts written off | 750 |
| Provision for doubtful debts – 2% of debtors | 450 |
| Interest for late payment of taxes | 200 |
| Interest on bank overdraft | 700 |

1. Other expenses include:

|  |  |
| --- | --- |
| Staff welfare | 250 |
| Depreciation | 500 |
| Directors fees | 2,000 |

1. The company capital allowances were calculated and agreed at K3, 200,000

**Required:**

Compute the taxable profits for Doritosi Iinvestments for the year ended 30 June, 2016. **(Total 15 Marks)**

**SECTION B (40 MARKS)**

Answer ANY **TWO** questions from this section

**QUESTION 5**

1. Value Added Tax [VAT] works on the credit system.

**Required**:

state any **two** advantages to the Government of using the credit system. *(2 marks)*

1. State any **four** obligations of a VAT registered taxpayer. *(4 marks)*
2. The following transactions were recorded in the books of a VAT registered taxpayer for the month of March, 2017.

Business related expenditure, inclusive of VAT at 16.5%

|  |  |
| --- | --- |
| **Expenditure** | **MK** |
| Security | 349,500 |
| Legal | 233,000 |
| Stationery | 104,850 |
| Office furniture | 815500 |
| Office rental | 582,500 |
| Water | 151,450 |
| Electricity | 174,750 |

Business related expenditure, exclusive of VAT

|  |  |
| --- | --- |
| **Expenditure** | **MK** |
| Salaries | 8,000, 000 |
| Postal services | 300, 000 |

In addition to the above transactions, the value of sales net of VAT were K12, 000, 000 and K5, 000, 000 in respect of local sales and exports respectively.

**Required**:

1. State and describe **three** types of supplies in terms of VAT. *(3 marks)*
2. Calculate the amount of VAT paid or payable on each of the expenditures appearing in the books of the Taxpayer, show all your workings clearly. *(9 marks)*
3. Calculate the amount of VAT chargeable on total sales i.e. local and exports, indicating gross sales values thereafter. *(2 marks)*

**(Total 20 marks)**

**QUESTION 6**

1. (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) **Neno Sports Club**, which is a taxable club, carried out the following

transactions in the year ended 31 December 2017:

|  |  |
| --- | --- |
| Income | :K7,060,000 |

This was made up as follows:

|  |  |  |  |
| --- | --- | --- | --- |
|  | | K'000 | |
| Ground entrance fees | | 1,220 | |
| Rentals from accommodation | | 1250 | |
| Sale of food | | 790 | |
| Sale of drinks | | 1650 | |
| Club membership fees | | 980 | |
| TV shows – live football | | 710 | |
| Live band performances | | 460 | |
| Gambling machine | | 190 | |
|  | | 7,250 | |

|  |  |
| --- | --- |
| Expenses | :K2,962,000 |

The breakdown was as follows:

|  |  |
| --- | --- |
|  | K’000 |
| Trading licence | 140 |
| Food licence | 115 |
| Salaries and wages | 1, 480 |
| Cost of goods sold | 685 |
| Repairs and maintenance | 542 |
|  | 2,962 |

**Required:**

1. Compute the taxable income of Neno Sports Club for the financial year to 31 December 2017. *(4½ marks)*
2. Calculate the amount of tax payable on the taxable income computed in (1) above. *(1½ marks)*
3. State the tax year in which the taxable income computed in (1) above will be assessed. *(1 mark)*

(c) (i) When may the Commissioner accept the taxpayer’s estimate of amount taxable income? *(2 marks)*  (ii) When may the Commissioner estimate the taxpayer table income or assessed loss? *(2 marks)*

**(Total 20 Marks)**

**QUESTION 7**

1. i) Define a fringe benefit in terms of the Taxation Act *(2 marks)*

(ii) State the records that must be kept by an operator of fringe benefits tax system. *(1½ marks)*

(iii) State any **two** offences that can lead into a fringe benefits tax operator to be penalized. *(2 marks)*

1. Assume that your friend got employed on 1 October, 2017 by one of the reputable banks downtown Blantyre as a Relationship Manager. This position went away with the following benefits:
2. A salary of K900, 000 per month;
3. A motor vehicle without restriction to business use only which was bought in 2016 at K20, 000, 000.
4. A company house which is fully furnished. The house is being rented for him at K450, 000 per month.
5. The bank pays for DSTV subscription, Water and electricity charges for your friend at K60, 000, K50, 000 and K40, 000 per month directly to service providers.

**Required:**

Compute the fringe benefits tax payable for the quarter ending 31 December, 2017 on provision of a motor vehicle,furnished rented house, payment of DSTV subscription, water and electricity charges.  *(9½ marks)*

1. The Commissioner General is given discretionary powers under the Taxation Act because administration of the Taxation Act demands constant use of “common sense”.

**Required**:

State any **five** examples of expressly stated discretionary powers of the Commissioner General under the Taxation Act. *(5 marks)* **(Total 20 marks)**

**Question 8**

1. State when the following allowances are claimed in line with the second schedule of the Taxation Act
2. Investment allowances. *(2½ marks)*
3. Initial allowances. *(2 marks)*
4. Annual allowances. *(1 mark)*
5. **Makanami Investments** capital allowances tax schedules as at 31 December, 2017 were as listed:

|  |  |  |
| --- | --- | --- |
| **Asset** | **Tax written Down Value**  **MK 000** | **Rate of Annual Allowance** |
| Factory Building | 45,000 | 5% |
| Plant and Machinery | 17,000 | 10% |
| Motor vehicles | 22,000 | 20% |
| Furniture & Fittings | 9,000 | 10% |
| Computer Equipment | 4,000 | 40% |

During the year to 31 December, 2017, the following transactions took place:

*Plant and Machinery:*

Some plant and machinery was sold for K3, 200,000. This transaction resulted into a gain of K900, 000. New replacement machinery was acquired at a cost of K8, 000,000.

*Furniture and Fittings:*

New furniture and fittings were purchased at a cost of K700, 000. Additional fittings were bought second hand at K300, 000.

*Motor Vehicles:*

One saloon motor vehicle acquired in October 2016 for K7,000,000 was sold during the year for K4,000,000. Another vehicle, a pick up, with a tax written down value of K1,200,000 was involved in an accident and was written off. The insurance paid k5, 000,000 as compensation, and the whole amount was used to purchase another single cabin pick up as a replacement.

*Office Equipment:*

The new computers worth K2,500, 000 were acquired during the year.

*Factory Building:*

A total of K5, 500,000 was spent on the extension of the factory building. The extension was only used for business from January, 2018.

**Required:**

1. Compute the tax written down value for the machine that was sold. *(1 mark)*

ii) Calculate the capital allowances due for the year ended 31 December, 2017. (*8½ marks)*

According to the Customs and Excise Act, goods may be imported for a number of reasons.

**Required:**

1. State any **three** reasons that the Act allows that goods should be imported for. *(3 marks)*
2. State any **four** documents that are commonly used in customs clearance which must be submitted to Customs. *(2 marks)*

**(Total 20 marks)**

**END OF EXAMINATION PAPER**

Appendix

**TAX RATES AND ALLOWANCES**

**The following rates of tax and allowances are to be used when answering the questions:**

**TAX RATES AND ALLOWANCES**

**Income Tax Rates: Individuals**

Cumulative Tax Rate MK

0 – 360, 000 0% 0

360, 001 – 420, 000 15% 9,000

420, 001-36, 00,000 30% –

36,000,001+ 35%

**Company rates**

Locally incorporated 30%

Externally incorporated 35%

**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.

**Annual allowance – rates**

(Guidelines laid down by the Commissioner of Taxes)

5% – Industrial buildings

– Railway lines

– Farm improvements

10% – General plant and equipment

– Trailers

– Farm fencing

15% – Mobile cranes

17·5% – General plant and equipment on double shift

20% – Motor cycles

– Cars

– Pick-ups

– Light lorries (for light work)

– Cement mixers

– Tractors

25% – Light lorries (for heavy work)

– Tippers

– Tracked tractors

– Tree-dozers

– Scrapers

– Graders

– Bulldozers

– General plant and equipment working 24 hours a day

– Tractors (for heavy work)

– Transport services

40% – Computers