

**INSTITUTE OF BANKERS IN MALAWI**

**DIPLOMA IN BANKING EXAMINATION**

**SUBJECT: TAXATION 1 (IOBM – D213)**

**Date: 5th November 2013**

**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 and not your student number on each answer book used. Answer books without examination number will not be marked.**

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

**SECTION A (60 MARKS)**

Answer **ALL** questions from this section.

**QUESTION 1**

1. Describe the circumstances under which the following items are allowable or deductible for tax purposes according to the Taxation Act.
2. Bad debts
3. Doubtful debts
4. Individual donations. *(6 marks)*

A contract of employment was entered into between an employer and an employee with the following terms of the contract:

* Period of Contract : 30 months
* Gratuity : 25% of basic salary earned over the contract period
* Monthly Salary : MK2, 300, 000 and a housing allowance of 70% of salary

**Required:**

Compute:

1. The amount of gratuity payable upon successful completion of the contract.*(2 marks)*
2. Tax payable on all the earnings by the employee to 30th June 2012 when the Contract came to an end and the Contract gratuity became payable. *(4 marks)*
3. Wife’s earned income under section 73 [4] of the Taxation Act is defined as income derived from any business carried on by the wife in her own right and in which her husband is not employed and is not a partner.

**Required:**

Describe any **four** situations, according to the Act, which can render wife’s earned income to become unearned income. *(3 marks)*  **(15 marks)**

**QUESTION 2**

1. Give **one** reason why initial and investment allowances are also referred to as “first year” allowances. *(1 mark)*
2. Under what circumstances is initial allowance claimed and not claimed by the taxpayer? *(2 marks)*
3. Define the terms Staff housing and Railway lines for purposes of capital allowance claims under the second schedule to the Taxation Act. *(2½ marks)*

1. Petulo, who is a manufacturer, had the following business assets tax written down values, assets disposals and assets additions, for the year ended 30 June, 2012.

|  |  |  |
| --- | --- | --- |
| **Tax written down value for business assets as at 30 June, 2011** | | |
| Item | Tax Written Down Value | Rate of Annual Allowance |
|  | K’ 000 |  |
| Factory Building | 10, 200 | 5% |
| Plant and Machinery | 8, 400 | 10% |
| Motor vehicles | 11, 700 | 20% |
| Furniture and Fittings | 5, 300 | 10% |

During the financial year to 30 June, 2012, the following transactions took place:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Asset Disposals** | | | | | | |
| Description | Plant and Machinery | | Motor Vehicles | | Office Furniture | |
|  | K’ 000 | | K’ 000 | | K’ 000 | |
| Net book value 30/06/11 | 970 | | 0 | | 115 | |
| Tax written down value 30/06/11 | 1, 500 | | 867 | | 450 | |
| Sale proceeds | 1, 800 | | 550 | | 425 | |
| **Asset Additions** | | | | | |
| Date | | Item | | Cost | |
|  | |  | | K’ 000 | |
| 01/07/11 | | New Machinery | | 8, 600 | |
| 03/10/11 | | New Lorry | | 7, 500 | |
| 29/05/12 | | Office Furniture | | 1, 100 | |

**Required**:

1. Calculate the capital allowances, investment or initial as the case may be, and annual allowances on the business assets outlined afore for the financial year ended 30 June, 2012. *(6½ marks)*
2. Calculate the capital gains or capital losses from the asset disposals stated afore. *(3 marks)*

**(Total 15 marks)**

**QUESTION 3**

Zanga Phee Limited is incorporated in Malawi and manufactures sweets and biscuits. The company’s summarized income statement for the year ended 31st December 2011 is as follows:

**Note MK’000 MK’000**

Turnover 150 000

Less cost of sales 1 107 000

Gross profit 43 000

Interest 2 000

**Less operating expenses**

Depreciation 7 200

Audit fees 400

Bad debts 840

Doubtful debts 2 500

Net exchange [gains] 3 [400]

Repairs and maintenance 4 1 300

Pension fund contributions 75

Fringe benefit tax 120

Staff expenses 5 4 500

Director’s fees 1 200

Other allowable expenses 11 300 27 035

**Total profit before tax 17 965**

**Notes:**

1. Included in the cost of sales is MK8,000,000 manufacturing depreciation.
2. Doubtful debts are made up of the following:

**MK’000**

Specific provision 400

General provision 100

**500**

In the previous year specific provision for doubtful debts was K200,000 and general provision was K400,000.

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

**MK’000**

Realized exchange gains [1 200]

Realized exchange loses 500

Unrealized exchange losses 300

**400**

1. Repairs and maintenance includes an amount of K170,000 for work completed but not paid for by 31st December 2011.
2. Staff expenses include K80,000 being the cost of tuition and related expenses incurred by Zanga Phee Limited in respect of a Malawian employee who obtained a diploma in food processing.
3. Capital allowances are agreed at an amount of MK12, 000, 000.

**Required:**

1. Compute the taxable income for Zanga Phee for the accounting year ended 31st December 2011 briefly. *(9 marks)*
2. Compute Corporation tax payable by Zanga Phee Limited. *(2 marks)*
3. Compute Corporation tax payable by Zanga Phee Limited assuming that it was a cell phone operator. *(2 marks)*
4. Compute Corporation tax payable by Zanga Phee Limited assuming that it was a foreign Company [incorporated outside Malawi] *(2 marks)*  **(Total 15 marks)**

**QUESTION 4**

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. In readiness for Christmas, a church in Blantyre had obtained a quotation to imported 150 Christmas decorations candles from South Africa. The prospective supplier has just emailed a quotation which indicates that the cost of each candle is 10 South African Rand C.I.F Blantyre.

An enquiry from Malawi Revenue Authority reveal that, upon arrival at the border port of the imported candles, the church will be required to pay 25% customs duty, 20% excise tax and 16.5% Value added Tax.

**Required:**

1. Explain the term C.I.F normally used in international trade. (*1½ marks)*
2. Advice how much the church will pay to Malawi Revenue Authority, should they go ahead to import the candles as Christmas is fast approaching. [Assume the exchange rate at the time of the arrival of the candles will be MK50 to 1 South African rand]. *(8½ marks)*

**(Total 15 marks)**

**SECTION B (40 MARKS)**

Answer **ANY TWO** questions from this Section

**QUESTION 5**

**Zaithwa Nsipe** is a senior manager employed by Masenjere Industries Plc. She earns a basic salary of K48,000,000 per annum. During the tax year 2011/2012 she was provided with the following benefits:

A loan of K20,000,000 on 1st October, 2011 at an interest rate of 4% per annum. This money was used to procure a house. The official rate of interest during the 2011/2012 tax year was 31.25% per annum. [For the purpose of this question, assume that simple interest is calculated on the loan which will be repaid in 10 years].

A Toyota Prado vehicle with a cost price of K68,000,000, first registered in 2011, but given to Zaithwa on the 1st August 2011. Total mileage in 2011/2012 amounted to 20,000 kilometres of which only 80% was business. During the tax year Zaithwa paid K5, 000 per month [with effect from August 2011] towards the use of the car, which entitled her to use it privately.

The use of a Hi-Fi system; worth K100,000 – this has to be returned to the company if Zaithwa leaves their employment.

A medical policy; This had cost the company K140,000 but would have cost Zaithwa K255,000 if she had arranged the same policy herself.

In addition to the above, Zaithwa also received a bonus of K8, 000, 000 on 31st January 2012 in respect of Masenjere Industries Plc superb financial performance.

Other income for the tax year comprised of K180,000 interests from the local building society and K40,500 from an NBS Bank Investment Account. Both amounts were received on the 31st December 2011 and were the actual amounts credited to her accounts.

**Required:**

1. Why should providers of benefits to employees have to pay Fringe Benefits Tax?

1. Calculate the value of benefits provided by Masenjere Industries Plc to Zaithwa Nsipe for the 2011/2012 tax year.
2. How is Fringe benefit tax payable?
3. What is the due date for fringe benefit tax?
4. What is the penalty for not paying fringe benefits tax?
5. Calculate the amount of Income Tax payable by Zaithwa for the 2011/2012 tax year.  **(Total 20 marks)**

**QUESTION 6**

1. Describe the **two** types of clubs, societies or associations which are recognised under the Taxation Act.
2. How is the income of such clubs, societies or associations treated by the Malawi Revenue Authority?
3. Where a club or association is subject to tax, state how the taxable income is computed.
4. The transactions of Tikumbe Club, which is a taxable club and registered in Malawi, for the financial year ended 31 December, 2012 were as listed below:

|  |  |
| --- | --- |
| Income | K’000 |
| Rental from excess accommodation | 320 |
| Gambling machine | 510 |
| Ground entrance fees | 405 |
| Live band performances | 201 |
| Sale of food | 300 |
| Video shows | 90 |
| Sale of drinks | 225 |
| Club membership fees | 190 |
| Expenses | K’000 |
| Repairs and maintenance | 415 |
| Trading licence | 125 |
| Cost of goods sold | 450 |
| Food licence | 130 |
| Salaries and wages | 500 |

**Required:**

1. Compute the taxable income of Tikumbe club for the financial year ended 31 December 2012.
2. Calculate the amount of tax payable on the taxable income computed in [i]
3. State the tax year in which the taxable income computed in [i] above will be assessed.
4. Explain how Turnover Tax works. **(Total 20 marks)**

**QUESTION 7**

1. A Malawian trader obtained a foreign currency loan facility whose proceeds were used to import machinery from China. The loan amount was $155, 000 and was obtained in September 2012. The repayment of the loan was made as listed:

February 2013 $105, 000

April 2013 $ 50, 000

Exchange rates for the relevant periods were as listed:

September 2012 $1 = K320

February 2013 $1 = K350

April 2013 $1 = K362

**Required:**

1. Define the term ‘foreign currency liability” in terms of the Taxation Act.
2. Calculate the value of the foreign currency in Malawi Kwacha, at the time of establishing the foreign currency liability, in September 2012.
3. Calculate the total amount of foreign exchange gain, or foreign exchange loss, as the case may be, realised on the loan transaction upon being paid in full.
4. Calculate how much would have been saved in realised foreign exchange losses or how much would have been realised as additional foreign exchange gains if the whole of this foreign exchange liability was settled in February 2013.
5. What restrictions if any, is imposed on the deductibility of realised foreign exchange loss?
6. The Taxation Act exempts certain capital gains and losses realised on transfer or disposal of any capital asset from being assessable for tax.

**Required:**

State any **four** situations which those exempt capital gains or losses could arise. **(Total 20 marks)**

**QUESTION 8**

1. Under what circumstances will a taxpayer make an appeal to the Commissioner General under the Taxation Act?
2. Describe any **five** offences in relation to taxation as provided for in section 112 of the Taxation Act.
3. Define “Residence” as provided for in the taxation Act.
4. Thabwa Limited, a company incorporated in Malawi, whose taxable profits for 2011/2012 tax year amounted to K13, 900, 000 had never paid provisional tax during this period.

**Required:**

Calculate the penalty that the company is liable to.

1. Name any **three** circumstances where the Commissioner General may estimate the taxpayer’s income according to section 89[1].
2. List any **one** situation where the Commissioner General may send an additional assessment to the taxpayer or their tax representative. **(Total 20 marks)**

**END OF EXAMINATION PAPER**

**TAX RATES AND ALLOWANCES**

**Income Tax Rates: Individuals**

Cumulative Tax Rate MK

0 – 180, 000 0% 0

180, 001 – 240, 000 15% 9,000

240, 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.