



Examiner's report

F6 Taxation (LSO)
June 2009

General Comments

The examination consisted of five compulsory questions. The first two questions carried 25 and 30 marks respectively. The last three each question carried 15 marks. Some of the questions were fully computational while others were a combination of computations and narrative aspects.

The overall performance was not satisfactory. The main contributing factor for most candidates was failure to carefully read and understand the contents of questions. In some cases there was some evidence of poor time management. The candidates who attempted the first two questions first performed better than those who attempted these questions last. On the other hand those who started with the last three questions first provided excellent answers than those who did these questions last. Where not all the questions were answered, question four was frequently omitted.

Presentation of answers for some candidates was very disappointing. Workings were not clear and at times not shown. Many candidates seemed to confuse allowable deductions and tax credits.

Candidates should note that answers should be clearly labelled and each question should always start on a new page.

Specific Comments

Question One

This 25 mark question was divided into four parts. The question basically tested candidates' ability to calculate the tax liability of the taxpayer who is employed and at the same time operates a business. The overall performance was disappointing in this question.

In part (a) candidates were to calculate the income tax payable for the year. This means that candidates were to consider all the sources of income of the taxpayer, which are employment income and business income in this case. To arrive at correct chargeable income, any expenses incurred should be deducted against relevant source of income. This is the correct presentation and it enables candidates to easily realise if there is a loss in any of the sources of income. This is with the exception of employment income.

The business expenses were wrongly mixed up with employment expenses in most of the answers. However, most candidates correctly calculated the allowable superannuation fund contributions. The treatment of the wedding present expense was also correct. Some candidates considered the expense as an allowable deduction while others disallowed it. Since the question was not clear as to what kind of wedding present was, either treatment was considered correct.

The tricky part for most candidates was the treatment of withholding tax related to employment income (PAYE). Some candidates added it back to employment income, others ignored it. Candidates failed to recognise that this is withholding tax already paid and the taxpayer is entitled to a tax credit for any withholding tax paid when calculating the tax liability.

Part (b) of the question was not well done by most candidates. Candidates were expected to calculate the total PAYE for Dr. Moremi's employees. The first step was to ascertain the tax residence for each employee in order to provide deductions accordingly. That is, the tax liability for each employee ought to be calculated individually. There was too much confusion demonstrated in most of the answers. This included repetition of the answers provided in part (a). In some cases the value of a gift and superannuation fund contributions were not included in the calculations of the tax liability of a resident employee.

Part (c) of the question was a narrative question and was also not well answered. The main focus was on the expenses incurred in producing employment income as prescribed by Income Tax Regulations. While most

candidates described the general deduction formula, while others provided a list of allowable deductions as per section 33 of the Income Tax which was certainly irrelevant. Few candidates were able to answer this question.

The last part was also a narrative question. There were some candidates who did well in this question which was about the tax treatment of the gift received. However, there were still some who provided irrelevant thresholds.

Question Two

The 30 mark question focused on corporation tax. The question was divided into three parts. The performance in general was very good. Most candidates demonstrated a general understanding of basic aspects involved in the calculation of corporation tax.

Part (a) of the question focused on the calculation of advance corporation tax (ACT). Most candidates seemed to be very conversant with this question. However, few of them appeared to have a problem with the treatment of deemed dividends, while others ignored them, others deducted them from the dividends paid. Again some failed to state the due date of the ACT. There is always a mark for stating a due date.

Part (b) of the question was about calculation of the corporation tax liability. Many candidates were able to pick up more marks in this part as well. The most common error was the calculation of local sales. Most candidates failed to exclude the value added tax (VAT) when calculating the chargeable income.

In addition, the deductions appeared to pose a major problem to a number of candidates. There were some candidates who demonstrated lack of understanding of the pooling method of depreciation. For those who got this method right most of them failed to recognise that group four depreciable assets (which was the factory building in this case) are not eligible for this method, and hence, single asset method should be used. Apportionment of operating costs was also a problem for most candidates. This was basically due to failure to carefully read and understand the question.

Part (c) of the question focused on the calculation of withholding tax. This basically tested candidates' ability to apply correct withholding tax rates. Different rates were applied without any thought of the correct tax treatment. The correct tax rate was 25% which is a standard rate because the expense was payable to a non-resident. The reduced rate of 10% was not applicable as there is no tax treaty between the two member states, that is, Lesotho and China.

Question Three

This 15 mark question focused on the (value added tax) VAT. The question tested candidates' ability to calculate VAT based on the given scenario. Most candidates did not gain as many marks as expected.

In part (a) the question clearly stated that the transactions are inclusive of VAT where appropriate. This statement was very crucial but it was often ignored by some candidates thereby resulting in wrong calculations. This is also another evidence of failure to carefully read the question.

Most candidates failed to score higher marks on the calculation of input VAT due to a number of reasons. Some candidates displayed lack of knowledge regarding the treatment of pre-registration opening stock. While most answers indicated that the vendor can only claim input VAT paid on purchases, some frequently omitted the input VAT paid on the purchase of the car and rent. The majority of candidates seemed not to be aware that a vendor may claim input VAT paid not only on the goods bought for resale but also capital goods, utilities and certain services used for taxable supplies.

The output VAT was also wrong for most answers because they included the 14% charged on the exports. The exports are zero rated not exempt as others indicated.

Part (b) and (c) involved narrative aspects and the main focus were on the treatment of bad debts. The question was rather general not specifically confined to the given scenario as most of the answers indicated. However, most candidates seemed to have a general understanding on part. Though the majority of candidates provided incomplete and sometimes unclear answers, there were still some candidates who managed to obtain higher marks.

Question Four

This 15 mark question dealt with calculation of chargeable gains. The performance was fair for most candidates. Most of them seemed to be prepared for this part. The question required candidates to explain and at the same time calculate chargeable gains or losses for the year for each scenario given. The explanation part was frequently omitted by most candidates.

In the first scenario, most candidates were able to differentiate between a gain which is taxable and one which is not. However, hardly anyone mentioned that the latter will be deferred until disposal of the replacement premises.

In the second scenario the gain was correctly calculated by most candidates. The indexation was well done. However, the explanation part was often ignored.

The last scenario appeared to have some complications for some of the candidates. The explanation part was frequently omitted in most answers and the calculation of the correct cost of the extension seemed to be a major problem. Most candidates indexed the cost for inflation which was wrong, as the extended portion was held by the taxpayer for less than 12 month period. Again, no one recognised that the extended portion ought to be depreciated for a period of two months. The cost base of an asset should include the cost of acquiring producing or improving the asset together with indirect expenses such as depreciation.

Question Five

This 15 mark question focused mainly on the tax residence of an individual taxpayer. The question was divided into three parts and the performance was generally very good for most candidates. Those who failed to score higher marks, was mainly due to poor time management.

However, most answers to part (b) demonstrated confusion as regards the residence rules for the first and last years of an individual's residence in Lesotho. Part (a) of the question was often repeated to answer this part. In some cases incomplete and unclear answers were provided.

Part (c) of the question was to be answered based on the given scenario. Candidates were expected to mention two bases of collection of taxes, namely, residence and source of income. Again, the treatment of superannuation fund contributions was also relevant. Rather, most answers included some irrelevant information.

The calculation of the tax payable was correctly dealt with by most candidates. However, some candidates who provided the correct explanation regarding the treatment of superannuation fund contributions did the opposite when calculating the tax payable, that is, they wrongly allowed the contributions.