

Fundamentals Level – Skills Module

Taxation (Lesotho)

Tuesday 2 December 2014



Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

ALL FIVE questions are compulsory and **MUST** be attempted.
Tax rates and allowances are on pages 2–3.

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

The Lesotho Institute of Accountants

ACCA



Paper F6 (LSO)

SUPPLEMENTARY INSTRUCTIONS

- 1 Calculations and workings need only be made to the nearest M.
- 2 All apportionments should be made to the nearest month.
- 3 All workings should be shown.

TAX RATES AND ALLOWANCES

The following tax rates and tax allowances are to be used in answering the questions:

Second Schedule

(Section 9(1))

Resident individual income tax rates

Chargeable income	Rate of tax
First M51,670	22%
Over M51,670	35%
Personal tax credit	M6,100

Third Schedule

(Section 10)

Resident company income tax rates

Nature of income	Rate of tax
1. Manufacturing income derived from a manufacturing activity of an industrial, scientific or educational nature which promotes industrial, scientific, educational or other development within Lesotho.	10%
2. Other manufacturing income	10%
3. Other income	25%
4. Commercial farming income	10%

Fourth Schedule

(Sections 109 and 116)

Tax rate for trustees, fringe benefits and electing non-residents

The applicable rate is 35%

Fifth Schedule

Minimum chargeable income

The multiplication factors for the purposes of s.16(2) are:

Air travel	100%
Electricity amount	100%
Principal residence amount	5%
Schooling amount	100%
Secondary home amount	5%
Vehicle amount	25%

The amounts specified for the purposes of s.16(6) are:

Air travel amount	M2,500
Electricity amount	M3,000
Principal residence amount	M150,000
Schooling amount, per child	M1,000
Secondary home amount	M20,000
Vehicle amount	M20,000

Sixth Schedule

(Section 41)

Declining balance depreciation rates:

Group	Depreciation rate	Assets included
1	25%	Automobiles, taxis, light general purpose trucks, tractors for use over-the-road, special tools and devices.
2	20%	Office furniture, fixtures and equipment, computers and peripheral equipment and handling equipment, buses, heavy general purpose trucks, trailers and trailer mounted containers, construction equipment.
3	10%	Any depreciable asset not included in another group.
4	5%	Railroad cars and locomotives and railroad equipment, vessels, barges, tugs, and similar water transportation equipment, industrial buildings, engines and turbines, public utility plant.
5	100%	Mining

Value added tax (VAT)

Standard rate	14%
Supplies of electricity and telephone calls	5%
Basic foods and agricultural inputs	0%
Exports	0%

ALL FIVE questions are compulsory and MUST be attempted

- 1 Mr Mokema has worked for five years as a finance manager for Icon Communications, a resident company which provides communication services. In addition to his job with Icon Communications, Mr Mokema also operates his own accountancy business and employs a part-time accountant to assist him with this work.

The details relating to Mr Mokema's different sources of income for the year ended 31 March 2014 are as below:

Employment income	Note	M
Annual salary		540,000
Housing allowance		54,000
Car allowance		36,000
Performance-related bonus		27,000
Education allowance		18,000
Entertainment allowance		20,000
Meals and refreshments	1	6,000
Employer superannuation contributions	2	64,800
Employee superannuation contributions	2	(43,200)
Staff loan	3	30,000
Reimbursements	4	11,500
Membership fee paid	5	(3,500)

The withholding tax (PAYE) remitted to the Lesotho Revenue Authority (LRA) by Icon Communications in respect of Mr Mokema's employment income amounted to M176,183.

Other sources of income

Business income

Revenue		280,000
Salaries		(95,000)
Sundry expenses	6	(70,000)

Property income

Revenue received	7	36,000
Interest received (gross)	8	6,900

Notes:

- Mr Mokema received free meals and refreshments from Maseru Sun Hotel during the year. It is the policy of Icon Communications to provide free meals to all senior officers such as Mr Mokema on the last Friday of each month at an annual cost of M6,000 per person.
- Icon Communications has established an employer superannuation fund into which it contributes 12% of each employee's basic salary. Mr Mokema also contributes 8% of his basic salary into the fund.
- Mr Mokema was granted a staff loan by Icon Communications on 1 April 2013. The loan is interest-free. The Central Bank of Lesotho's discount rate averaged 18% throughout the year ended 31 March 2014.
- The reimbursements received by Mr Mokema from Icon Communications were as follows:
 - Water and utility payments which are required to be substantiated by supporting documents and are reimbursable up to a maximum amount of M6,500 per annum. Mr Mokema submitted supporting documents evidencing payments amounting to M4,500.
 - Telephone bills which are required to be substantiated by relevant supporting documents and are reimbursable up to a maximum amount of M5,000 per annum. Mr Mokema submitted supporting documents evidencing payments amounting to M6,000.
- Mr Mokema is a member of the Lesotho Institute of Accountants. He paid a membership fee amounting to M3,500 for the year ended 31 March 2014.

6. Sundry expenses of Mr Mokema's accountancy business include a depreciation allowance amounting to M8,500 in respect of a motor van belonging to the business. The motor van is used by the part-time employee for both business and private use. For the year ended 31 March 2014, a log book for the motor van shows that 75% of the total mileage is attributed to business use, while 25% is attributable to private use. The value of the motor van was M110,000 when it was first provided to the part-time employee in February 2013.
7. Revenue received relates to proceeds received from the disposal of 1,200 shares in a resident company. The adjusted cost base (ACB) of the shares at the date of disposal was M30.20 per share.
8. Interest received is from a nominated savings account held with Nedbank Lesotho.

Required:

- (a) **Calculate the income tax payable by Mr Mokema for the year ended 31 March 2014, clearly showing the different sources of income of Mr Mokema, and state the due date by which his tax return should be submitted to the Lesotho Revenue Authority.**

Note: In respect of the employment income, indicate any items which are not chargeable to tax by the use of a zero (0). (14 marks)

- (b) **Calculate the fringe benefits tax (FBT) payable by Icon Communications in respect of fringe benefits provided to Mr Mokema for the year ended 31 March 2014, and state by when employers should file their quarterly fringe benefits returns.** (6 marks)

- (c) **Explain the withholding tax obligations of Nedbank Lesotho in respect of the interest received by Mr Mokema during the year.**

Note: Your answer should include any relevant calculations. (5 marks)

(25 marks)

- 2 Alex Sports Manufacturers is a Lesotho resident company, which has been engaged in the manufacture of a wide range of sportswear for the past 15 years. The company has equity capital of M130,000 and long-term debt of M450,000.

The following information relates to the company's summarised trading results for the year ended 30 September 2014.

The profit after tax for the year is M650,000. This profit is after deduction of the following expenses:

	Notes	M
Staff costs	1	190,000
Motor expenses	2	43,500
Royalties payments	3	4,300
Research and development	4	50,400
Promotion and advertising	5	15,700
Finance charges	6	31,300
Miscellaneous expenses (all tax deductible)		42,700
Corporation tax		110,800

Notes:

1. Staff costs include:
 - (i) Retrenchment payments amounting to M56,900. 45% of this amount is in respect of employees whose terminal benefits were below 25% of their gross salaries during the employment period.
 - (ii) Provision for directors' emoluments amounting to M65,500.
2. Motor expenses include:
 - (i) Traffic fines amounting to M1,200.
 - (ii) Insurance premiums of M5,400 payable to a non-resident insurer.
3. Royalties payments to non-resident companies comprise the following:
 - (i) Acquisition of patent rights to use a specialised technology in the manufacturing process amounting to M2,300.
 - (ii) Right to use a trade-mark in the manufacture of clothing amounting to M2,000.
4. Research and development comprises:
 - (i) Production engineering at a cost of M34,800.
 - (ii) New equipment purchased at a cost of M15,600 on 1 February 2014. No further record in relation to this purchase was made in the books of the company.
5. Promotion and advertising includes winter tracksuits, which cost the company M12,500. They were donated to one of the local football teams. The necessary tax conditions were all met.
6. Finance charges comprise the following:
 - (i) Interest payable on the overdraft amounting to M2,500.
 - (ii) Penalties for late payment of PAYE amounting to M1,800.
 - (iii) Interest on long-term debt amounting to M27,000.

Other relevant information

The company's revenue includes the following:

- (i) Gross dividends received amounting to M52,000. 15% of this amount relates to dividends received from local companies. The remaining 85% was received from non-resident companies. The amount includes foreign tax suffered on the dividends totalling M12,500.
- (ii) Interest received amounted to M25,700. 30% of the interest was received net of tax from local financial institutions. The remaining 70% was received from foreign financial institutions and was received net of foreign tax of M1,500. Only the net interest has been recorded in the accounts so far.

Required:

- (a) Explain the limitation imposed on the deductibility of interest payable, and calculate the interest deduction which should be allowed in arriving at Alex Sports Manufacturers chargeable income for the year ended 30 September 2014. (4 marks)
- (b) Calculate the chargeable income of Alex Sports Manufacturers for the year ended 30 September 2014.
Note: Your answer should start with the profit after tax for the year as given in the question. Indicate by the use of a zero ('0') any items of expenditure which do not require adjustment. (11 marks)
- (c) Calculate the tax payable by Alex Sports Manufacturers for the year ended 30 September 2014, and state the due date for payment.
Note: Your answer should start with the chargeable income calculated in (b) above. (6 marks)
- (d) Calculate the tax instalments payable by Alex Sports Manufacturers for the year ending 30 September 2015, and state the due date for each instalment. (3 marks)
- (e) Calculate the withholding tax payable by Alex Sports Manufacturers in respect of the royalty payments. (2 marks)
- (f) Explain the conditions which must be met in order for a donation (as in note 5) to be treated as an allowable deduction. (3 marks)
- (g) Explain the income tax treatment in the hands of the recipient individual of terminal benefits which are below 25% of the basic salary earned during the employment period (as in note 1). (1 mark)

(30 marks)

- 3 Khabo Hypermarket (Pty) commenced its operations in December 2012. The company registered for value added tax (VAT) on 1 February 2014.

The following monthly information was extracted from the company's general ledger:

	Sales M	Purchases M	Operating expenses M
December 2012	72,000	22,000	22,020
January 2013	54,000	27,800	11,050
February 2013	60,000	36,000	11,400
March 2013	71,000	44,000	10,800
April 2013	72,500	45,700	11,060
May 2013	66,900	39,500	10,950
June 2013	59,800	39,500	10,950
July 2013	67,300	41,800	11,110
August 2013	66,600	41,230	10,700
September 2013	70,200	44,000	10,920
October 2013	71,900	55,300	11,150
November 2013	69,700	43,600	11,020
December 2013	74,300	47,200	10,950
January 2014	58,300	34,900	11,030
February 2014	65,200	40,150	11,800

Additional information:

1. All the sales, purchases and operating expenses are taxable at the standard rate of VAT.
2. Sales are stated inclusive of VAT.
3. Purchases and operating expenses are stated inclusive of VAT, where appropriate.
4. Purchases for the last three months from November 2013 to January 2014 include the following amounts for purchases still held in opening stock at February 2014:

	M
November 2013	17,400
December 2013	15,200
January 2014	16,900

5. The operating expenses include:
 - (i) A monthly insurance premium of M4,500.
 - (ii) A finance lease instalment of M750 payable at the beginning of February 2014 for 48 months. This is in relation to the acquisition of a delivery truck. The truck would have cost M26,220 if purchased for cash.

Required:

- (a) **State, giving reasons, whether Khabo Hypermarket (Pty) should have compulsorily registered for VAT, and if so on which date.** (3 marks)
- (b) **Explain how any additional VAT payable as a result of failure to register for VAT is calculated, and state whether any additional VAT is payable by Khabo Hypermarket (Pty).** (4 marks)
- (c) **Calculate the VAT payable by/refundable to Khabo Hypermarket (Pty) for the month of February 2014, assuming that all conditions necessary to recover any allowable pre-registration input VAT are met.**
Note: Your answer should clearly include any exemption, where appropriate. (5 marks)
- (d) **State any THREE VAT obligations of Khabo Hypermarket (Pty) as a vendor.** (3 marks)

(15 marks)

- 4 Mr Nkamo, a resident individual, has been engaged in a wide range of investment ventures in Lesotho and South Africa. As one of these investment ventures, Mr Nkamo owned a motel located in the outskirts of Maseru city, Lesotho, which he rented out. In October 2012, Mr Nkamo decided to emigrate to South Africa. Due to unfavourable business prospects in Lesotho, Mr Nkamo also decided to sell his motel. The transaction was executed by his lawyers. All of Mr Nkamo's business and private assets were professionally revalued and disposed of for their market values in June 2013.

The analysis of the assets disposed of by Mr Nkamo is detailed below:

Assets	Note	Date acquired/ Constructed	Original cost M	Market value M
Investment assets				
Land	1	August 1995	–	120,000
Building premises (motel)	2	June 1997	600,000	1,300,000
Swimming pool		December 2002	55,000	170,000
Boundary wall		May 2013	140,000	210,000
Business assets				
Furniture and fittings	3	September 1999	260,000	500,000
Equipment	3	February 2000	210,000	1,500,000
Private assets				
Residential premises		May 1996	560,000	1,100,000

Notes:

1. The land was inherited from Mr Nkamo's late father. It was intended to be used for the construction of another business building. The market value of the land at the date of Mr Nkamo's inheritance was M45,000.
2. The cost of building premises includes the cost of works which were carried out in October 2000. This work related to an extension which was erected at a cost of M80,000, and repairs to a leaking roof costing M12,000.
3. There were additions to the furniture and fittings and equipment following the acquisitions referred to above. The adjusted cost base (ACB) for furniture and fittings and equipment on 1 April 2013 amounted to M550,000 and M950,000, respectively.

Other relevant information

Legal fees and stamp duties totalling M5,500 were incurred in respect of the disposals.

The relevant indexation numbers are given as follows:

August 1995	160
May 1996	180
June 1997	190
September 1999	200
February 2000	220
October 2000	230
December 2002	260
April 2013	310
May 2013	313
June 2013	315

Required:

- (a) Calculate the chargeable income for Mr Nkamo for the year ended 31 March 2014, and provide explanation(s) for any items excluded from your calculations. (13 marks)
- (b) Explain the circumstances in which neither a gain nor a loss is recognised as a result of the application of the indexation rule. (2 marks)

(15 marks)

5 You are given the following two independent scenarios:

(a) Mr Khaka, a Lesotho resident, established a trust fund in 2005. He died in February 2013 at the age of 65. The terms of Mr Khaka's will provide the following information:

- Mr Khaka's wife, Ntebo, should be a trustee of a trust established in 2005. Ntebo will be entitled to 60% of the trust income.
- Mr Khaka's only child, Palesa, should be a beneficiary of the trust. Palesa will be entitled to the remaining 40% of the trust income.

The total trust income for the year ended 31 March 2014 amounts to M1,500,000. The income does not take account of a trading loss of M70,000 incurred by the trust in the year ended 31 March 2013.

Required:

(i) Calculate the tax payable by Ntebo and Palesa for the year ended 31 March 2014, in their capacity as trustee and beneficiary, respectively. (5 marks)

(ii) Explain how your answer to (i) would differ if the income received by Ntebo and Palesa was not trust income but rather the income of a partnership, in which they were both partners.

Note: Calculations are not required. (2 marks)

(iii) Explain whether Ntebo would be liable to tax if the trust were to receive foreign source income in the future, giving reasons for your answer. (4 marks)

(b) Mafa, aged 25, acquired the following assets under the terms of his late father's will. Mafa's father died in December 2013.

	Valuation – December 2013 M
100 acres of unimproved land	150,000
Building premises rented out to business merchants (the rental income for the year ended 31 March 2014 was M200,000)	1,600,000
Annuity payment from the trust estates	60,000
Ordinary shares in Alex Holdings (Pty) – an unquoted non-resident company (Mafa received dividends of M30,000 in respect of this shareholding in January 2014)	600,000

Required:

Calculate the chargeable income of Mafa for the year ended 31 March 2014. Your answer should clearly indicate by the use of a zero (0) any items which are exempt from tax. (4 marks)

(15 marks)

End of Question Paper