
Answers

Marks

1 Deluxe Engineering Limited

(a) Withholding tax for the year ended 31 December 2013

	K	
Rental paid for general manager's house K2,100,000 at 15%	315,000	½
Management fees K25,000,000 at 10%	2,500,000	1
Purchase of fixed assets:		
Motor vehicle – K8,500,000 at 3%	255,000	½
Desk tops – K825,000 at 3%	24,750	½
Laptop – K325,000 at 3%	9,750	½
	<u>3,104,500</u>	
		<u>3</u>

Marking note: Withholding tax would not be deducted in the case of the purchase of assets if the supplier(s) had a withholding tax exemption certificate. Candidates who clearly stated this as the reason for not calculating tax at 3% were given equal marks.

Marks

(c) Taxable income for the year ended 31 December 2013

	K	K	
Profit before taxation		11,407,450	½
Add items not allowed for taxation			
Manufacturing costs:			
Depreciation of plant and factory	7,500,000		½
Provision for material losses	155,000		½
Pension contributions above 15%	1,650,000		1
Administrative expenses:			
Depreciation	10,589,000		½
Pension contributions above 15%	1,022,640		1
Fringe benefits tax	919,500		½
Donations to a local church	35,000		½
Finance costs:			
Provision for doubtful debts	712,950		½
Impairment of goodwill	237,500		½
Penalty for late payment of taxes	315,200		½
		23,136,790	
		<u>34,544,240</u>	
Less items allowed for taxation			
Profit on the sale of fixed asset	32,500		½
Dividend received	62,500		½
Capital allowances (from part (b))	25,982,700	(26,077,700)	½
Adjusted profits for taxation		<u>8,466,540</u>	
			<u>8</u>

(d) Tax payable for the year ended 31 December 2013

	K	
Tax based on adjusted profits for the year K8,466,540 at 30%	2,539,962	½
Less: Provisional tax	(3,000,000)	½
Withholding tax on interest K175,000*20%	(35,000)	1
Withholding tax on rent K600,000*15%	(90,000)	1
Tax refundable	<u>(585,038)</u>	
		<u>3</u>

(e) If Deluxe Engineering Limited's holding company is a foreign company, then it would pay:

Value added tax (VAT) on the management fees payable, since this is a taxable supply and the holding company would not be registered for VAT in Malawi.		1
		1
Deluxe Engineering Limited would have to self declare the VAT payable.		½
Withholding tax on the remitted management fees would be payable at the non-resident tax rate of 15% (rather than at 10%).		1
	K	
VAT on management fee	4,125,000	½
Non-resident withholding (border) tax	3,750,000	½
	<u>7,875,000</u>	

Also, should the company declare a dividend, then border tax would be payable at the rate of 10% on the amount paid to its foreign holding company.

½

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2 Mabvuto Soka

(a) The benefits provided to Mabvuto will be taxed as follows:

Benefits provided to him in cash form will be added to his salary and subject to PAYE.	1
In this case, the benefits paid in cash are: the housing allowance, telephone allowance and water allowance.	$\frac{1}{2}$
Benefits which do not involve a cash payment to Mabvuto will be subject to fringe benefits tax (FBT) at 30% of their taxable value.	1
FBT is payable by the employer.	$\frac{1}{2}$
The benefits not paid in cash are:	
– the free use of the car, the annual value of which is 15% of the cost of the car; and	$\frac{1}{2}$
– the free electricity, the value of which is the electricity consumed.	$\frac{1}{2}$
	<u>4</u>

(b) Taxable income of the wholesale business for the year ended 30 June 2013

	K	K	
Profit before taxation		2,093,110	$\frac{1}{2}$
Add items not allowed for taxation			
Depreciation	455,000		$\frac{1}{2}$
Drawings	575,500		$\frac{1}{2}$
Esmie's salary	0		1
School fees	445,000		$\frac{1}{2}$
Traffic fines	65,000	1,540,500	$\frac{1}{2}$
		<u>3,633,610</u>	
Less allowable items			
Capital allowances		(460,000)	$\frac{1}{2}$
Taxable income		<u>3,173,610</u>	<u>4</u>

(c) Tax payable on the employment earnings of Mabvuto for the year ended 30 June 2013

	K	
Salary	6,000,000	$\frac{1}{2}$
Bonus	450,000	$\frac{1}{2}$
Housing allowance	600,000	$\frac{1}{2}$
Telephone allowance	65,000	$\frac{1}{2}$
Water allowance	75,000	$\frac{1}{2}$
Total earnings from employment	<u>7,190,000</u>	
Tax payable:		
First 240,000	0	
Next K60,000 at 15%	9,000	
Remainder (K7,190,000 – 300,000) at 30%	2,067,000	
Total tax payable	<u>2,076,000</u>	$\frac{1}{2}$
		<u>3</u>

(d) Tax payable by Mabvuto and Esmie for the year ended 30 June 2013

	K	Mabvuto K	Esmie K	
Employment earnings:				
Mabvuto (from (c))		7,190,000		1/2
Esmie			1,560,000	1/2
Business income (from (b))		3,173,610		1/2
Dividend received		0		1/2
Director's fees		125,000		1/2
Interest received	110,000			1/2
Interest received (wife)	22,000			1
	132,000			
Less exempt	(10,000)	122,000		1
Rental income (wife)	345,000			1
Less:				
City rates	(32,000)			1/2
Plumbing maintenance	(22,000)			1/2
Driveway (capital)	0	291,000		1
Taxable income		10,901,610	1,560,000	
Tax payable:				
First K240,000		0	0	
Next K60,000 at 15%		9,000	9,000	
Excess over K300,000				
K10,601,610 at 30%		3,180,483		
K1,260,000 at 30%			378,000	
		3,189,483	387,000	1
Less tax credits				
PAYE:				
Mabvuto (from (c))		(2,076,000)		1/2
Esmie			(387,000)	1
Director's fees (K125,000*10%)		(12,500)		1
Interest received:				
Mabvuto (K100,000*20%)		(20,000)		1
Esmie (K12,000*20%)		(2,400)		1
Rental income (none – as per question)		0		1/2
Tax payable		1,078,583	–	
				14
				25

3 Bwanoni Limited**(a) Explanations of the value added tax (VAT) treatment of items**

- As the company is registered for VAT, it should charge VAT on all of its supplies except for exempt supplies. The sale of the motor vehicle is a taxable supply on which VAT should have been charged. 1
- VAT is chargeable on a deposit made by a customer. The time of supply and point at which VAT is chargeable is the date of receipt of the payment or part payment, i.e. in this case in March 2014. 1
- Where a discount is granted to a customer, the relevant VAT is a credit and should reduce the VAT payable. 1/2
The debit note issued for the undercharge increases the sales value and as such should be included as a part of sales. 1/2
- VAT on hotel expenses is not allowed unless the company is in the business of entertaining. 1/2
VAT on spare parts is not claimable unless either the company is involved in the business of selling spare parts; or once they are used on vehicles which are used wholly and exclusively and necessarily for the purpose of the business. 1/2
VAT is not chargeable on the rental of residential property (exempt supply). 1/2

	Repairing a warehouse is a business expense and the related VAT is claimable.	Marks ½
	Supplies bought from a supplier who is not registered for VAT will not include VAT, so no input VAT can be claimed.	½
5.	VAT charged on a saloon car is not claimable but should be taken as part of the cost of the car for capital allowance purposes.	½
	VAT charged on furniture will be claimable provided it is used wholly and exclusively for the purpose of the business (i.e. it is not household furniture).	½
6.	VAT on bad debts is allowable as a reduction in input VAT if it can be proven that efforts were made to collect the debts, but have not succeeded.	1
		<u>8</u>

(b) Adjusted VAT return for the period ended 31 March 2014

	Value K	Rate	VAT K	
Sales and other outputs (working 1)	27,020,000	16.5%	4,458,300	W
Underpayment from previous period	100,000	16.5%	16,500	½
Value of zero rated supplies	825,000	0%	0	½
Total value and VAT due on outputs	<u>27,945,000</u>		<u>4,474,800</u>	
Value of exempt supplies	345,200		—	½
Purchases and other expenses (working 2)	16,178,600	16.5%	2,669,469	W
Capital goods	2,500,000	16.5%	412,500	½
Other adjustments (working 3)	746,970	16.5%	123,250	W
Excess VAT brought forward from the previous period				
less application for refund	0		0	
Zero rated purchases and other expenses	650,000	0%	0	½
Total value and VAT on inputs	<u>20,420,770</u>		<u>3,205,219</u>	
VAT payable			1,269,581	½

Workings:

	K	
1. Sales		
Per original return	26,550,000	
Motor vehicle	350,000	½
Deposit	120,000	½
	<u>27,020,000</u>	
2. Purchases		
Per original return	22,500,000	
Less:		
Hotel expenses	(145,900)	½
Spare parts	(75,500)	½
Rental of residential property	(600,000)	½
Purchases from unregistered suppliers	(5,500,000)	½
	<u>16,178,600</u>	
3. Other adjustments		
Discounts to a customer	96,970	½
Bad debts	650,000	½
	<u>746,970</u>	

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			Marks
4 (a)	The following expenditure incurred by persons involved in mining operations is specifically deductible:		
(i)	in searching for or in discovering and testing or winning access to deposits of minerals;		1
(ii)	in the acquisition of rights over the deposits, other than from a person who has carried out mining operations in relation to such deposits;		1
(iii)	in the provision of plant and machinery and industrial buildings which would have no value if the mine ceased to be worked;		1
(iv)	on the construction of any buildings or works which would have little or no value if the mine ceased to be worked;		1
(v)	on development, general administration and management prior to the commencement of mining operations.		1
	Such mining expenditure is claimable in full (100%) in the year it is incurred.		1
			<u>6</u>
(b)	JNJ Mining Limited		
	Income tax payable for the year ended 31 December 2013		
	K	K	
Profit before taxation		8,929,000	½
<i>Add:</i>			
Depreciation	2,961,000		½
Premium (19/20*3,600,000)	3,420,000		1
Clinic (50%*1,200,000)	<u>600,000</u>	6,981,000	1
		<u>15,910,000</u>	
<i>Less:</i>			
Mining expenditure (specialised equipment)		<u>(6,000,000)</u>	1
Taxable income		<u>9,910,000</u>	
Less tax losses brought forward		<u>(5,000,000)</u>	1
Taxable income		<u>4,910,000</u>	
Tax payable at 30%		1,473,000	1
			<u>6</u>
(c)	A company must submit its self-assessment return within 180 days from the end of the year of assessment.		
	The balance of tax payable should be remitted at the same time that the return is submitted.		
	The penalty for the late submission of a company return is a fine of K200,000.		
			1
			<u>3</u>
			<u>15</u>

5 Millenium Limited

(a) (i) Lower expenditure option for the company

	Option 1 K	Option 2 K	
Salary	3,511,600	2,450,000	½
Bonus	600,000	–	½
Pension contributions (10% of salary)	351,160	245,000	1
Housing allowance	–	800,000	½
Commission on sales	–	1,400,000	½
School fees	<u>750,000</u>	<u>–</u>	1
Total payments	<u>5,212,760</u>	<u>4,895,000</u>	
Fringe benefits tax			
School fees: 50% of K750,000 at 30%	112,500	–	1
Car: 15% of K6,500,000 at 30%	<u>–</u>	<u>292,500</u>	1
	<u>5,325,260</u>	<u>5,187,500</u>	
			<u>6</u>

(ii) Higher take home pay for the sales manager

	Option 1 K	Option 2 K	
Salary	3,511,600	2,450,000	1/2
Bonus	600,000	–	1/2
Housing allowance	–	800,000	1/2
Commission on sales	–	1,400,000	1/2
School fees/use of car	–	–	1/2
Total income	4,111,600	4,650,000	
Less tax	(1,152,480)	(1,314,000)	1/2
Income after tax	2,959,120	3,336,000	
Less pension (5% of salary)	(175,580)	(122,500)	1
Take home pay	2,783,540	3,213,500	
Add school fees paid by employer	750,000	–	1
	3,533,540	3,213,500	

Working: Income tax payable

	Option 1 K	Option 2 K	
First K240,000 at 0%	0	0	
Next K60,000 at 15%	9,000	9,000	
Excess over K300,000:			
K3,811,600 at 30%	1,143,480		
K4,350,000 at 30%		1,305,000	
	1,152,480	1,314,000	1
			6

(b) Based on the calculations in (a)(i), Option 2 would appear the cheaper option for the company by K137,760 per annum. However, this does not take into account the following:

- the need for the company to fund the capital cost of purchasing the company car and its annual running costs;
- the possibility that sales (and thus the 2% commission payable to the sales manager) may be higher or increase at a faster rate than expected;
- the fact that a higher proportion of the costs of Option 2, i.e. the fringe benefit tax, is not tax deductible.

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Tutorial note: Given that Millenium Limited is stated as being a highly profitable company, all of the expenditure, other than the fringe benefits tax, will be tax deductible, so their effective 'after tax' cost to the company will only be 70% of their absolute cost.