

Fundamentals Level – Skills Module

Taxation (Malawi)

Tuesday 4 June 2013



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 Public Accountants Examination Council of Malawi

ACCA



Paper F6 (MWI)

SUPPLEMENTARY INSTRUCTIONS

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

TAX RATES AND ALLOWANCES

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

Income tax rates: Individuals

K		Cumulative K
0 – 180,000	0%	0
180,001 – 240,000	15%	9,000
240,001 +	30%	–

Company rate

Locally incorporated	30%
Externally incorporated	35%

Annual Allowance – rates

(Guidelines laid down by the Commissioner of Taxes)

5%	– Industrial buildings
	– Railway lines
	– Farm improvements
10%	– General plant and machinery
	– 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

Value Added Tax

– Standard rate	16·5%
– Zero rate	0%

Capital gain indices

Year	CPI	2013 conversion factor
2003	154·20	2·6042
2004	172·00	2·3346
2005	198·50	2·023
2006	226·10	1·776
2007	244·10	1·6450
2008	265·40	1·5130
2009	287·70	1·3957
2010	309·05	1·2993
2011	333·77	1·2031
2012	358·54	1·1200

ALL FIVE questions are compulsory and MUST be attempted

- 1 Madimba Engineering Limited is a company incorporated in Malawi. The company makes up its financial statements to 31 December annually.

The following are the summarised results for the year ended 31 December 2012:

Statement of profit or loss

	K	K
Gross profit from trading activities		5,560,500
Dividends received from Malawi companies	125,600	
Interest received	89,500	
Fair value adjustment	235,800	
Profit on sale of property and equipment	336,600	787,500
		<u>6,348,000</u>
Less: Expenditure		
Administration costs	3,456,000	
Finance costs	752,800	
Loss on sale of shares	78,100	
Impairment of investments	175,580	
Loss on sale of equipment	85,400	
Depreciation	675,100	
Tax penalties	44,500	(5,267,480)
Net profit		<u>1,080,520</u>

The following additional information is available in connection with this financial statement:

1. The profit on sale of property and equipment relates to profit on sale of an office building. The building was bought in October 2003 for K875,000. It was sold in February 2012 for K1,321,000. The fair value adjustment added to the asset at the date of sale was K425,000 and accumulated depreciation was K315,500.

The proceeds were invested in another office building on 15 July 2012. The cost of the new office was K4,500,000. The old and new offices are located some distance away from the factory premises.

2. Administration costs are made up of:

	K
Salaries and wages	2,559,750
Fringe benefits tax	361,250
Donations to local school	175,000
Donations to Save the Children Fund	185,000
Subscription to Chamber of Commerce	175,000
	<u>3,456,000</u>

3. Finance costs are made up of:

	K
Legal costs for debt collection	199,800
Interest on bank overdraft	124,350
Interest on loan to finance office building	135,800
Stamp duty for share capital increase	292,850
	<u>752,800</u>

4. The loss on sale of shares refers to shares in an unlisted company which were bought in 2004.

	K
Cost of shares	125,200
Fair value adjustment	(35,000)
	<hr/>
	90,200
Sale proceeds	12,100
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Loss on sale of shares	78,100
	<hr/>

5. The loss on sale of office equipment was made up as follows:

	K
Cost in January 2005	657,000
Depreciation	(459,900)
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	197,100
Sale proceeds June 2012	111,700
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Loss on disposal	(85,400)
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The total capital allowances claimed on this asset at the end of the year were K525,600.

6. The company has capital losses brought forward of K15,800 and trading losses of K485,100.
 7. Capital allowances including balancing charges/allowances for the year have been agreed at K695,250.

Required:

- (a) Calculate any capital gains or losses based on the sale of the assets, giving appropriate reliefs, for Madimba Engineering Limited for the year ended 31 December 2012. (9 marks)
- (b) Calculate the balancing charge or allowances for Madimba Engineering Limited for the year ended 31 December 2012. (1 mark)
- (c) Compute the profits or losses which would be chargeable to tax for Madimba Engineering Limited for the year ended 31 December 2012. (12 marks)
- (d) Companies are required to pay provisional tax. On the basis that Madimba Engineering Limited did not pay any provisional tax for the year, explain the basis upon which provisional tax ought to have been paid and calculate any penalties which would be imposed on Madimba Engineering Limited for the year ended 31 December 2012. (5 marks)
- (e) State the requirements for offsetting trading losses. (3 marks)

(30 marks)

- 2 Mwai is in partnership with Dengu and they trade as fishmongers in Mangochi. They started the business on 1 July 2011. They will share profits in the ratio of 3:7, since Mwai is not involved full time in the business as he has paid employment as an agricultural scientist for one of the farms in the area.

The partnership essentially buys and sells fish. However, to supplement this they also do some fishing. They bought a second-hand boat for K325,000. In addition, they bought fishing nets for K125,000 and a second-hand pick up vehicle for K675,000.

The following are the summarised results of their first year of trading to 30 June 2012:

	K	K
Fish sales		8,500,000
Less:		
Purchase of fish	3,500,000	
Partners' salaries	720,000	
Wages	475,000	
Depreciation	135,000	
Fuel	445,800	
Insurance	125,800	
Rent for market office	36,000	
House rent for Dengu	360,000	
School fees for Dengu's children	400,000	
Donation to local chief	15,000	(6,212,600)
Net profit		<u>2,287,400</u>

The following additional information is available:

1. Partners' salaries are made up as follows:

	K
Mwai	120,000
Dengu	600,000
	<u>720,000</u>

2. Mwai's remuneration package for his employment for the year ended 30 June 2012 was:

	K
Salary	800,000
Bonus	225,000
Car – cost when new two years ago	3,000,000
Rental for house – unfurnished	480,000
Fuel for car	200,000
Electricity and water paid cash to Mwai	70,000

3. The following other income was earned by Mwai during the year:

	K
Interest on savings account (gross)	25,000
Dividend	25,000
Director's fees – Malengo Limited	27,000
(the director's fee has been accounted for net after deducting withholding tax)	

4. PAYE was duly deducted from the salary earned from employment but not from that earned from the partnership.
5. The partnership paid a total amount of withholding tax of K600,000 on the amounts paid to the partners during the year.

Required:

- (a) **Compute the taxable income of the partnership for the year ended 30 June 2012. Give a brief explanation of your treatment of the fishing nets.** (9 marks)
- (b) **Allocate the taxable profits for the year ended 30 June 2012 between the partners.** (3 marks)
- (c) **Calculate the actual tax payable by both Mwai and his employer for the year ended 30 June 2012.** (5 marks)
- (d) **Calculate the total tax payable by/or refundable to Mwai for the year ended 30 June 2012.**

Note: You should indicate any income not taxable by the use of a zero (0).

(8 marks)

(25 marks)

- 3 (a) Input Value Added Tax (VAT) is claimable from output VAT.

Required:

State FIVE circumstances when input VAT is not claimable.

(5 marks)

- (b) The following transactions were entered into by Primrose Supermarkets Limited in the month of February 2013.

	Note	K	K
Sales	1		2,556,250
Interest received			45,000
Purchases	2	850,500	
Rent	3	225,000	
Salaries		80,000	
Electricity	4	45,000	
Water charges		65,000	
Consultancy charges	5	450,000	
Packaging materials		65,000	
Furniture and fittings	6	88,000	
Staff welfare	7	35,000	

The following additional information is available:

1. Included in sales figure is the sale of fresh fish totalling K300,000.
Items were sold to the general manager at a reduced total price of K25,000. The normal sales value of these items was K35,000.
2. Purchases include the cost of buying fish from fish vendors amounting to K165,000.
3. Rent is for the supermarket and also for the general manager's house. The rental for the manager's house is K60,000, the balance being for the supermarket.
4. Electricity costs include K15,000 paid to the general manager.
5. Consultancy charges were paid to a foreign consultant who is not registered for VAT in Malawi.
6. The cost of furniture and fittings includes cost of labour of K2,500 paid to a carpenter who is not registered for VAT.
7. Staff welfare is the cost of a coffin for a member of staff.

All amounts are stated exclusive of any applicable VAT.

Required:

Calculate the value added tax (VAT) payable to the Malawi Revenue Authority or the excess available for carry forward for the month of February 2013, showing the VAT treatment of all of the items listed.

Note: Where an item does not result in any VAT payable or reclaimable, indicate this with a zero (0) against the item, giving a brief explanation. (10 marks)

(15 marks)

- 4 James Phiri is involved in farming activities and has a farm in Mchinji. He grows tobacco and timber on his farm.

For the past six years he has grown timber on 50 hectares of land and this timber is expected to mature in the year to 31 December 2012.

The costs incurred on the growing of the timber has been as follows:

	K
Year 1	850,000
Year 2	200,000
Year 3	150,000
Year 4	75,000
Year 5	65,000
Year 6 (year to 31 December 2012)	15,000

The yield is expected to be 50 cubic metres per hectare. During the year to December 2012, 500 cubic metres was harvested and sold at K2,125 per cubic metre.

James has also cleared another 30 hectares of virgin land at a cost of K400,000 for which he received a subsidy of K225,000.

He also has spent K225,000 on the growing of a tobacco crop, which will be harvested and sold after 31 December 2012.

Required:

- (a) In accordance with the provisions of special trades, state how the taxable income derived from timber will be determined. (4 marks)
- (b) On the basis of (a), calculate the taxable income for James Phiri in respect of the timber for the year ended 31 December 2012. (7 marks)
- (c) Explain how subsidies for and expenditure on future crops are dealt with for tax purposes. (4 marks)

(15 marks)

- 5 Zakeyu is contemplating starting a business which will be engaged in the selling and repairing of computers and related equipment. He will work full time in this business.

He will be preparing his financial statements to 31 December each year.

The following are his expected results for his first year of trading to 31 December 2012:

	K	K
Turnover		10,500,000
Cost of sales		(4,500,500)
		<hr/>
		5,999,500
Bank interest (gross)		55,000
Less: Other expenditure		
Salaries	2,565,500	
Motor vehicle expenses	175,000	
School fees for child	235,000	
Depreciation	355,000	
Rent and rates	650,000	
Utilities	36,500	(4,017,000)
	<hr/>	<hr/>
Profit		2,037,500

Included in salaries is a salary of K1,800,000 payable to Zakeyu.

He will have use of the motor vehicle, which will be used 50% for private purposes. The vehicle, which is second-hand, will cost K1,500,000.

School fees are payable for his son at Bwaila Private School.

The projected rent and rates include the cost of renting a house for himself at K360,000 per annum. The balance of the rent is for business premises.

Zakeyu has not decided whether he should operate as a sole trader or incorporate a limited company. He has approached you for advice.

Zakeyu has no other sources of income.

Required:

Advise Zakeyu whether to operate as a sole trader or to incorporate a limited company. Your advice should take into account both the taxes payable and the earnings available to Zakeyu. Support your answer with detailed calculations.

(15 marks)

End of Question Paper