Examiner's report

F6 Taxation (BWA)
June 2013

General Comments

The paper consisted of 5 compulsory questions. One question was for 25 marks, another for 30 marks and the remaining three for 15 marks each. Questions 1 and 2 count for 55 marks and so therefore should be given priority by candidates since it is performance in these two questions which will ultimately determine the difference between passing and failing.

The overall standard of the answers was reasonable with many candidates scoring high marks. Most candidates appeared to be well prepared and exhibited good exam technique. A noticeable difference in the answers to this paper was that the majority of candidates appeared to have come to grips with, and mastered, the mechanics of a tax computation. This is so important and central to this exam since in any tax paper there will be 3 or 4 sections where the candidate is called upon to perform a tax computation.

The paper was considered reasonable and should not have presented too much trouble to well prepared candidates. The paper gave plenty of opportunities to score marks and in general candidates took advantage of this. All questions were answered and there was no sign of time pressures.

Specific Comments

Question One
The first question is always for 25 marks and relates to an individual (or partnership) who carries on business for her own account as well as having income from a number of different sources such as interest, rent etc. Very often with individuals their personal tax affairs get mixed up with their business tax affairs and so it is necessary to identify such transactions and then adjust for them in the tax computation.

Parts 1(a) and 1(b) calculating the chargeable income from the guest house and rents were well answered by most. The mother's salary is a bona fide expense and so is deductible and what must be added back are the personal expenses of Thapelo. This part of the question was answered well.

However most candidates answered 1(c) incorrectly. Most answered that the capital gain on the sale of shares listed on the Botswana Stock Exchange was exempt from capital gains tax but with effect from 1 July 2011. This is only true if the shares have been held for more than one year which, in the question, they had not.

Parts 1(d) and 1(e), the calculation of taxable income from all sources and tax payable, were also well answered by the majority. Some candidates still have trouble with dividend income, which is exempt, and credit cannot be claimed for tax withheld at source the argument being that dividends are paid out of taxed profits and therefore to tax a dividend is effectively double taxation.

Question Two
The second question is always for 30 marks and relates to a corporate tax situation. Only average marks were achieved in this question largely because of the final part which candidates found difficult.

Part 2(a) related to a claim for rollover relief on the replacement of plant and most were alive to this option and claimed the relief. In practice it is very important that all possible relief that is granted by the tax legislation is claimed.

Before Part 2(b) could be calculated it was first necessary to calculate the capital allowances amount. Some candidates try to short-cut this part but it is strongly recommended that the full calculation, i.e. the make up of cost and accumulated allowances, is shown as it usually carries generous marks for what is essentially an arithmetical exercise. The calculation of taxable income was generally handled well with the majority of candidates showing a sound understanding of the mechanics of a tax computation. The starting point of a tax computation is the accounting profit or loss which is then adjusted for items that are not taxable or deductible and for tax allowances to arrive at taxable income. Items that are commonly added back are amounts that do not represent actual expenditure incurred – i.e. depreciation and amortisation, write off or impairment of assets, provisions and IFRS adjustments. In addition certain amounts such as interest, royalties and management and consultancy payable to non-residents can only be claimed as a deduction in the year in which the withholding tax is paid and not the year in which the expenditure is incurred. Part 2(c) was straightforward.

Part 2(d) candidates found difficult but it is a common exam question mainly because it is encountered often in practice and accordingly candidates should prepare for such a question. When persons sell their businesses they often have the option of either selling the shares of the company that houses the business or just selling the assets of the business and the question is which is the most tax efficient option. The sale of the shares should have been quite straightforward although many seemed to struggle with it. The sale of assets comprised two parts – the tax on the balancing charge arising on the sale of assets and the capital gains tax arising on the sale of goodwill. In each case the tax must be deducted from the P5 million sale price and the net compared with each other. However, when selling assets out of a company the sale proceeds are paid into the company and the only legitimate manner of exiting these proceeds is by means of a dividend and this was given in the question. A dividend attracts a 7.5% withholding tax and so adds to the tax cost of selling assets and invariably selling the shares is the cheaper option. Very few candidates understood the dividend aspect and generally unsatisfactory marks were obtained for this part.

Question Three

This was a VAT question and should have been answered better than it generally was. VAT is a transactional tax and each transaction can be categorised.

Part 3(a) required candidates to categorise the various transactions into either standard rated, zero rated and exempt supplies. However, certain types of payments – such as salaries and wages – are not categorised at all and the question required a fourth category of "those to which VAT does not apply". Many candidates missed this requirement and categorised dividends and fair value adjustments into exempt supplies, which is not correct. Although the VAT is nil, whether the supply is exempt or VAT does not apply, getting the correct exempt supplies is important from an apportionment and de minimus perspective.

Part 3(b) was not answered well because many candidates missed the fact the figures were stated inclusive of VAT. Therefore to calculate the net VAT payable required the calculation to be 12/112.

Part 3 (c) required candidates to define the scope of VAT in Botswana and the majority answered this satisfactorily.

Question Four

The first part of this question was answered well. Masego already is in receipt of a salary but he wants to see if he can structure this in a way that will lessen his tax. Most candidates scored reasonable marks on part 4(a) of the question, which required a comparison of the total tax payable under both scenarios. Some candidates attempted to calculate a cash flow but this was not in the question. Note that if an airfare back to your home town is a contractual condition then it is exempt from tax.

Part 4(b) required a description of the PAYE system and whilst most knew that it existed they were not able to explain very well how the system works. Many candidates stated that PAYE is a tax – it is not a tax but instead is a method of collection. PAYE is a withholding tax on employment income and is a very effective means of making large numbers of individuals pay the correct amount of tax.

Part 4(c) follows on from 4(b) in that only employees are subjected to PAYE. Accordingly it is necessary to distinguish between those people that are employed and those that are self-employed. Again candidates had difficulty in explaining the differences.

Question Five

The question looked at various sources of revenue and tested candidates' knowledge on the taxation of such revenue streams.

The sale of unlisted shares is always liable to capital gains tax. The sale of listed shares is also liable to capital gains tax if they have not been held for more than one year. The sale of a loan account is normally done at par and accordingly there is no tax impact. For assets to fall within the CGT net they must be part of a business; if they are personal assets then there is no capital gain.

Any income derived from a business is liable to income tax including farming. However, in the case of dryland farming there is an exemption if the total extent of land involved in such farming operations did not exceed 100 hectares but this information was not supplied in the question.

Most candidates correctly stated the filing date for income tax returns of individuals to be 30 September.

Part 5(c) required a definition of the residence of an individual, which is important because it determines in which country a person is taxed.