ACCA

Examiner's report

F6 Taxation (BWA)

June 2015

General Comments

There were two sections to the examination paper and all of the questions were compulsory. Section A consisted of 15 multiple choice questions (two marks each) which covered a broad range of syllabus topics. Section B had four questions worth 10 marks each and two longer questions worth 15 marks, each testing the candidates' understanding and application of the Botswana tax system in more depth. This is the first examiner's report since the introduction of the new exam format and question types. The following paragraphs report on each section and focus on some of the key learning points.

The majority of candidates demonstrated a reasonable understanding of the principles of the various types of taxes and their application in different situations,

The vast majority of candidates answered all questions and there did not appear of any time pressures. A few parts of questions were not attempted but this appeared to be more due to a lack of knowledge rather than a shortage of time. Candidates are urged to always attempt a question however difficult it may be since there is always the possibility of scoring some marks whereas not attempting an answer will always result in zero marks.

The questions where candidates performed less strongly were questions 1(b), 3(c), 5(c) and 6 which totalled 23 marks.

Specific Comments

Section A

Multi Choice Questions

This is the first time that multi choice questions were included in the F6 (BWA) exam and, in general, candidates dealt with these well. There were 15 questions each worth 2 marks and they provided a broad coverage of the syllabus. Candidates had to select will one correct answer from four possible answers – the remaining three answers being "distractor" answers i.e. answers that are plausible but incorrect. Candidates are not required to show workings but must just select one option. The following question is reviewed with the aim of giving future candidates an indication of the types of questions asked, guidance on dealing with exam questions and to provide a technical debrief on the topics covered by the specific question selected.

Example 1

Which of the following are the necessary conditions for a company to be allowed to claim a deduction for tax purposes in respect of a bad debt?

(1) The debt must have been included in income either in the current year or a prior year
(2) The debt must be more than one year old
(3) The debt must be irrecoverable
(4) The debt must be due to the taxpayer

A 1, 2 and 4
B 1, 2 and 3
C 1, 3 and 4
D 2, 3 and 4

This question tested candidates' knowledge on the requirements for claiming a bad debt deduction for income tax purposes and this is an example of a question where there is more than one correct statement (although only one correct answer). There are three requirements which must all be present before a bad debt can be deducted and they are (i) that the debt is due to the taxpayer, (ii) the debt is bad (i.e. irrecoverable) and (iii) the debt must have been included in the taxable income of the taxpayer. Thus a debt that has been purchased cannot be deducted because it is not due to the taxpayer nor has it ever been included in the taxable income of the taxpayer and a staff loan cannot be deducted because it has never been included in income. The distracter statement was the condition that the debt must be one year old before a deduction can be claimed; this is not a requirement for an income tax deduction but is instead a requirement for recovery of VAT paid. The correct answer was, therefore, C.

Section B

Question One

This 10 mark question dealt with capital gains of both immoveable property and shares. A factory building had been purchased and then extended twice before its sale. In the case of a sale of immoveable property, the original cost must be increased by applying the cost of living index which then gives the tax cost. The majority of candidates performed this satisfactorily and then deducted the loss made on the sale of shares. Note that whilst immoveable property is subject to indexation, shares are not and instead there is a flat 25% allowance. However, in this case, there was a loss on the shares and so the moveable property allowance was not claimed. Remember that a capital loss can only be deducted against a capital gain and the loss can only be carried forward for one year.

Part (b) required an explanation of holdover relief. However, many candidates instead gave an explanation for rollover relief. There is a difference between the two with rollover relief being when a capital gain arising on the sale of an immoveable property is deducted from the cost of a new replacement property so that the capital gain is effectively deferred until the second property is sold. Holdover relief, on the other hand, is applied in the event of a group reorganisation between two or more resident companies where there is no change in beneficial ownership or when the merger is due to companies listing on the Botswana Stock Exchange.

Part (c) asked for an explanation of a balancing charge in the case of a disposal of immoveable property. The majority of candidates gave adequate explanations but very few were able to state that the balancing charge on immoveable property is limited to the capital allowances that have been claimed. Where the selling price exceeds the original cost of the property then the excess is subject to capital gains tax.

Question Two

This was a 10 mark VAT question and the majority of candidates tackled it well. Various transactions were listed and candidates had to calculate the tax payable or refundable by considering whether the transactions were standard rated, zero rated or exempt. The question included transactions that had no VAT effect such as interest, medical aid contributions and the purchase of shares and candidates were told to indicate, by the use of zero (0) these items with no VAT impact. The majority of candidates were aware of these.

Residential rent is an exempt supply but so is any expenditure in connection with that residence including repairs and utilities. On the other hand, commercial rent is a standard rated supply and all costs associated with that property can be claimed as input tax credits. Credit notes must mirror the original tax invoice; so if the original invoice is in respect of zero-rated supplies then the credit note must also be zero-rated.

Some candidates got their outputs and inputs mixed up and a few simply listed the transactions without indicating whether the resulted in output VAT payable and input tax recoverable.

The majority of candidates were aware of the date of filing of the VAT return for part (b).

Question Three

This 10 mark question concerned withholding tax and was dealt with reasonably well by the majority of candidates Withholding tax is an important aspect of Botswana tax and will affect most businesses at some stage or another. Part (a) required candidates to state whether certain transactions are liable to withholding tax or not. Tax must be withheld from payments to non-residents of interest, royalties and management and consultancy fees. The definition of management and consulting fees is very wide including fees for administrative and technical services so that virtually all service-type payments are caught.

There is no withholding tax in respect of the purchase and transport of goods since these do not fall within the definition of management or consultancy fees. Management fees, interest and technical fees paid to non-residents are all liable to withholding tax. Insurance premiums are not liable to withholding tax and nor are advertisements. The rate of withholding tax, if applicable, is 15% unless reduced under a double tax treaty.

Part (b) required a restatement of taxable income after it was shown that certain of the expenses listed in (a) had not been paid as at the year end and neither had the relevant withholding tax. Accordingly the accrued expenses that are liable to withholding tax – i.e. management fees and technical fees – had to be added back whereas the transport costs, which were not liable to withholding tax did not have to be added back.

Most candidates missed the gist of part (c) which asked the question of when is withholding tax payable – and specifically whether it is payable on an accruals basis or on a payments basis. Whilst the vast majority of candidates knew that the tax is payable by the 15th of the month following deduction very few stated whether the deduction of tax was at the time of accrual or payment. The answer is that tax must be withheld from the payment of the expense and the date of accrual is irrelevant to the triggering of the withholding tax liability.

Question Four

The third 10 mark question dealt with the liability of certain transactions to income tax and candidates were required to give reasons why a transaction was or was not liable to tax.

Interest paid by banks or building societies does not have to be declared by individual taxpayers (this is a different rule than applies to companies or trusts) provided that the interest paid has been subject to withholding tax.

To score well, candidates should have recognised that, as David was a citizen of Botswana, he was liable to tax on his worldwide income. The receipt of a cash prize is of a fortuitous nature and, therefore, was not taxable. Although gains on the sale of shares are generally taxable as capital gains, gains arising on the sale of shares listed on the BSE are specifically exempt. The restraint of trade receipt was of a capital nature and therefore not liable to income tax. Candidates generally performed well here but were not always able to give coherent reasons for their answer.

Part (b) was not answered as well. This question involved the calculation of post-tax income. David had been made an offer of employment from a company and he wanted to know how much additional cash he would have in his pocket if he accepted the offer. It was necessary to calculate the tax cost of the package which included the taxable benefit of a company car. Then in order to arrive at the post-tax income David would be left with, his pension contributions and the tax payable had to be deducted from the salary.

This was arguably a more challenging requirement. However, future candidates are advised that they should be prepared for this type of question which involves basic planning.

Question Five

Under the new exam format, there will always be a 15 mark question on company tax.

Candidates appeared well prepared in this area and performed well on part (a) which involved a calculation of taxable income.

It was necessary to first calculate the balancing allowance on the sale of the non-current assets as this was included in the tax computation. The majority of candidates made the correct adjustments in respect of deductible and non-tax deductible items such as impairments, provisions and fair value adjustments which are required in terms of IFRS accounting rules but have no place in calculating a company's income tax liability. Also most candidates were aware of the necessity of limiting the deduction of interest paid to a non-resident by reference to the amount of withholding tax paid.

However, many candidates also adjusted for interest receive – this was not correct as interest received is taxable in full and, therefore, no adjustment was required.

Part (b) was generally well answered.

Part (c) was not well answered by the majority of candidates. Self-assessment tax (SAT) is payable every quarter in advance and very often companies have to estimate what their ultimate tax liability will be and accordingly make round figure payments especially at the beginning of the cycle. In this example, a round figure amount of P100, 000 had been paid for the first SAT payment and the question was what was the minimum amount that needed to be paid for the second SAT payment. Candidates should have been able to calculate that, because the first payment had been overpaid, the second payment could be reduced.

Question Six

This was another 15 mark question and this time focussed on the tax affairs of an individual, Naledi. Many candidates appeared to find this question somewhat challenging. The individual in question had business income as well as various items of investment income. Certain payments were stated net of withholding tax and certain income items were received net of withholding tax so it was necessary to ascertain the gross amount of the payment or receipt for the purposes of the tax computation.

Another required calculation was the capital allowances claim. A point that many candidates failed to spot was that the remaining allowances on the plant were less than the annual allowance and so the claim was limited to the balance of allowances remaining.

Candidates should have started with the net accounting profits and then added -back any expenses which was not tax deductible and deducted any income which was not taxable or any special allowances. Additionally, in the case of individuals, any expenses which constitute private expenditure should be disallowed. Many candidates appeared to struggle with the tax computation and were uncertain which items and which amounts required adjustment.

Candidates were required to quantify Naledi’s taxable income from all sources and this included from business, rents and interest. However, many ignored this part of the question.