# Answers

1 Sellena Tourism Limited

**(a)** Capital allowances can be claimed on computers as follows:

Initial allowances are given in the first year in addition to annual allowances, at the standard rate of 20%.

Annual allowances are given based on the cost of the computer in the first year and subsequently based on the tax written down value. The annual allowances are given at the rate of 40%.

**(b)** Sellena Tourism Limited
Capital allowances for the year ended 30 June 2007

| | TWDV 1 July 2006 | Additions | Disposal | Total | Investment | Allowances Initial | Annual | Total | TWDV 30 June 2007 |
|---|---|---|---|---|---|---|---|---|---|
| | K | K | K | K | K | K | K | K | K |
| Industrial buildings | 965,000 | 2,500,000 | – | 3,465,000 | 1,000,000 | – | 173,250 | 1,173,250 | 2,291,750 |
| Plant and machinery | 750,000 | 750,000 | – | 1,500,000 | 150,000 | – | 150,000 | 300,000 | 1,200,000 |
| Motor vehicles | 465,000 | 675,000 | (160,000) | 980,000 | – | – | 196,000 | 196,000 | 784,000 |
| Delivery vehicles | 365,000 | 1,500,000 | – | 1,865,000 | – | 300,000 | 373,000 | 673,000 | 1,192,000 |
| Computers | 450,000 | 275,000 | – | 725,000 | – | 55,000 | 290,000 | 345,000 | 380,000 |
| Furniture and fittings | 135,500 | – | – | 135,500 | – | – | 13,550 | 13,550 | 121,950 |
| | 3,130,500 | 5,700,000 | (160,000) | 8,670,500 | 1,150,000 | 355,000 | 1,195,800 | 2,700,800 | 5,969,700 |

| Summary of allowances | K | Disposal of assets | K |
|---|---|---|---|
| Investment | 1,150,000 | Sale proceeds | 250,000 |
| Initial | 355,000 | Tax written down value | 160,000 |
| Annual | 1,195,800 | | |
| Balancing charge | (90,000) | | |
| | 2,610,800 | Balancing charge | (90,000) |

Notes:
Initial allowances are not available on passenger carrying motor vehicles i.e. saloon cars and double cabs.
No allowances are available on offices as they are not attached to industrial buildings and even though they are less than 20% of total industrial buildings.

**(c)** **Computation of the taxable profits of Sellena Tourism Limited**

| | K | K |
|---|---|---|
| Profit before taxation | | 2,854,108 |
| *Add:* Items not allowed for taxation | | |
| Depreciation | 685,457 | |
| Bad debts provision | 235,000 | |
| Fringe benefits tax | 346,700 | |
| Traffic fines | 35,200 | |
| Donations – political party | 65,000 | |
| Exchange loss – unrealised | 356,000 | |
| Penalties for late payment of PAYE | 89,500 | |
| | | 1,812,857 |
| | | 4,666,965 |
| *Less:* Capital allowances | 2,610,800 | |
| Dividend from PIM | 230,000 | |
| Training allowance (see note) | 382,550 | |
| Profit on sale of fixed assets | 86,500 | |
| | | 3,309,850 |
| Taxable profits | | 1,357,115 |

Note: A training allowance of 50% of the actual amount spent on training for Malawians is deductible, in addition to the actual costs incurred.

**(d)** The tax liability of a company is settled initially through the quarterly payments of provisional tax made during the year. These payments are based on the profit estimate made at the beginning of the year.

The balance of tax payable (if any) is due on submission of the company's income tax return, which must be submitted within 180 days after the end of the financial year.

The balance of income tax to be paid by Sellena Limited for the year ended 30 June 2007 would be calculated as follows:

| | K |
|---|---|
| Taxable profits for the year K1,357,115 | |
| Tax based on the taxable profits at 35% | 474,990 |
| *Less:* | |
| Provisional tax payments | (268,000) |
| Withholding tax on interest at 20% | (29,000) |
| Balance due on submission of the tax return | 177,990 |

## 2 Lapukeni Binali

**(a)** The income of the internet café, since the business is not incorporated, will be assessed on its partners and Lapukeni is one of the partners.

The income will be arrived at by disallowing items of expenditure which are not allowed for taxation. Allowable expenses including capital allowances will be deducted to arrive at the taxable profit.

The taxable profits of the business will be shared amongst the partners in accordance with their profit sharing agreement to form the basis of their respective taxable incomes.

**(b) Computation of taxable income of Lapukeni from the business for the year ended 30 June 2007.**

| | K |
|---|---|
| Profit before taxation | 425,500 |
| *Add:* Joseph's salary | 250,000 |
| Depreciation | 200,000 |
| | 875,500 |
| *Less:* Capital allowances | |
| Computers K465,500 at 40% | 186,200 |
| Taxable profits | 689,300 |

Share of profits

| | Lapukeni K | Joseph K | Total K |
|---|---|---|---|
| Salary | – | 250,000 | 250,000 |
| Share of profits | 244,055 | 195,245 | 439,300 |
| Total profits | 244,055 | 445,245 | 689,300 |

**(c) Computation of the income tax payable by Lapukeni and Jane for the year ended 30 June 2007.**

| | Lapukeni K | Jane K |
|---|---|---|
| Salary | 1,200,000 | 60,000 |
| Housing allowance | 480,000 | 24,000 |
| Partnership profits | 244,055 | |
| Directors fees | 120,000 | |
| Net rents | 84,000 | |
| Interest | 31,800 | |
| | 2,159,855 | 84,000 |
| Tax | | |
| First K72,000 | Nil | Nil |
| Next K36,000 | 5,400 | 1,800 |
| Balance at 30% | 615,556 | – |
| Total tax | 620,956 | 1,800 |

Workings

(1) Rent

| | K | K |
|---|---|---|
| Rental income | | 720,000 |
| *Less:* Mortgage interest | 504,000 | |
| Property management fee | 72,000 | |
| Repairs to roof | 60,000 | |
| | | 636,000 |
| Net rent | | 84,000 |

(2) Interest

| | K |
|---|---|
| Gross amount | 41,800 |
| *Less* exempt | 10,000 |
| | 31,800 |

**(d) Additional tax payable by or refundable to Lupukeni**

| | K | K |
|---|---|---|
| Total tax as calculated above | | 620,956 |
| *Less:* | | |
| PAYE (Working 1) | 477,000 | |
| Withholding tax | | |
| Rent at 10% | 72,000 | |
| Interest (Working 2) | 1,200 | |
| Directors fees at 10% | 12,000 | |
| Provisional tax (5/9 × 160,000) | 88,889 | |
| | | (651,089) |
| Refundable to Lapukeni: | | (30,133) |

Workings

(1) Calculation of PAYE

| | |
|---|---|
| Salary | 1,200,000 |
| Housing allowance | 480,000 |
| | 1,680,000 |
| First K72,000 | 0 |
| Next K36,000 | 5,400 |
| Balance at 30% | 471,600 |
| | 477,000 |

(2) Withholding tax on interest

Withholding tax will have been deducted on payments over K10,000 as follows:

| | |
|---|---|
| December (12,000 – 10,000) | 2,000 |
| June (14,000 – 10,000) | 4,000 |
| | 6,000 |
| Withholding tax deducted at 20% | 1,200 |

**3 Presco Limited**

**(a)** VAT is charged according to the Act on:

(1) every supply of goods and services made in Malawi;

(2) every importation of goods; and

(3) the supply of any imported service, other than exempt goods and services.

The person(s) responsible for paying the tax are:

(1) In the case of a taxable supply, the taxable person making the supply.

(2) In the case of imported goods, the importer.

(3) In the case of imported services, the person importing the service.

**(b) Calculation of the additional value added tax and penalties due:**

| Month | Re-assessed amount K | Amount paid K | Amount underpaid K | Due date | Number of days to 31 January 2007 K | Interest K | Total due K |
|---|---|---|---|---|---|---|---|
| January | 36,800 | 36,800 | 0 | – | – | – | – |
| February | 42,600 | 38,500 | 4,100 | 25 March | 312 | 1,095 | 5,195 |
| March | 47,800 | 42,100 | 5,700 | 25 April | 281 | 1,371 | 7,071 |
| April | 86,000 | – | 86,000 | 25 May | 251 | 18,481 | 104,481 |
| May | 77,500 | 66,100 | 11,400 | 25 June | 220 | 2,147 | 13,547 |
| June | 44,500 | 44,500 | – | – | – | – | – |
| July | 32,500 | 50,100 | (17,600) | – | – | – | – |
| August | 96,000 | 75,000 | 21,000 | 25 September | 128 | 373 | 3,773 |

The interest rate is the bank rate plus one-quarter of the rate i.e. 31·25%. Interest is payable from the due date of payment i.e. the 25th of the month following the end of the VAT period to which the return relates. The value to be used to calculate the interest for August will be offset by the overpayment in the month of July.

**(c)** A taxable person who fails to submit a return on the due date is liable to a penalty of K20,000 and a further penalty of K1,000 for each day the return is not submitted.

**4 (a)** The special allowances given to tax payers who are engaged in pastoral, agricultural or other farming operations are that the expenditure on the following will be fully (100%) allowable as a deduction from the taxable income of such farmers when incurred:

- the stumping, levelling and clearing of lands;
- works for the prevention of soil erosion;
- boreholes;
- wells;
- aerial and geographical surveys; and
- any water control works connected with the cultivation and growing of rice, sugar or such other crop that the Minister may approve.

**(b)** Farmers who derive taxable income from the growing of timber may elect that their taxable income be determined as follows:

- The cost of planting the timber to be carried forward until the timber has reached maturity.
- To the cost above until the timber reaches maturity a fixed percentage of 5% will be added annually.
- When such timber is sold, the proportionate part of the cost and the total of the fixed percentage added annually will be deducted from the proceeds and the balance included in taxable income or assessed loss.
- Each year the annual fixed percentage will be added to the taxable income or deducted from the assessed loss.
- All expenditure incurred by the farmer including deductions under ss.33 and 34 and the second schedule on the maintenance and upkeep of such timber will be deducted from the taxable income or added to the assessed loss.

**(c)** The taxable income of any club, society or association formed, organised or operated principally for pleasure or recreation shall be liable to taxation notwithstanding that it arises from transactions with its members. The taxable income is equivalent to six and one-quarter per cent of all receipts by or accruals to, or in favour of it from the sale of goods, cinematograph performances, stage plays and gambling machines. Tax will be charged at the rate applicable to companies, currently 30%.

## 5 Limbani Limited

**(a) (i)** (1) to (3) Withholding tax must be paid over on the 14th of the month following the month it was deducted.

(4) Fringe benefits tax must be paid on the 14th of the month following the end of the quarter to which it relates.

(5) Provisional tax is paid quarterly, and must be paid within 30 days from the end of the quarter.

**(ii)**

| | K | K |
|---|---|---|
| Taxable profits | | 2,205,000 |
| Tax at 30% | | 661,500 |
| *Less:* Provisional tax | 465,425 | |
| Withholding tax on interest received | 29,000 | |
| | | 494,425 |
| Balance of tax payable | | 167,075 |

The payment of withholding tax on payments to suppliers has no effect on the tax payable. Such withholding tax is claimable against the income tax payable by the recipient.

Fringe benefits tax is not allowable as a deduction, and is added back to arrive at the taxable profits. Nor is it deductible from income tax payable.

Value added tax is an indirect tax which is ultimately paid by the consumer. VAT is not an expense to the business and is accounted for under a separate system using monthly returns.

**(b) (i)** Capital gains and losses are dealt with according to whether capital allowances were claimed on the asset or not.

Where capital allowances have been claimed on the asset the resulting capital gain will be included in the income in full. Similarly any resulting capital loss (balancing charge) will be deducted from the income in full. There are no restrictions with regard to claiming such losses.

Where capital allowances have not been claimed any capital gain is treated as the taxable income of the year in which the gain was realised.

However, a capital loss can only be offset against capital gains. Any excess loss is not available for offset against other income and must be carried forward to be offset against future gains.

Currently only 50% of gains on assets on which capital allowances have not been claimed are taxable and a similar provision applies to such losses.

**(ii) Treatment of Madimba Limited's capital gains/losses for the year ended 30 June 2007**

Madimba Limited will have no capital losses on non-capital allowance assets to carry forward as at 1 July 2006, therefore only the current year's gains and losses need to be considered.

| **Capital allowances claimed** | **K** |
|---|---|
| Capital gain | – |
| Capital loss | 18,000 |
| Loss to be claimed against income of the year | (18,000) |
| **Where allowances not claimed** | |
| Capital gain | 15,000 |
| Capital loss | (22,000) |
| Net capital loss | (7,000) |

The K7,000 loss cannot be offset against other income but must be carried forward to be offset against future gains, thus 60% of the loss or K4,200 will be carried forward.

| | | | Marks |
|---|---|---|---|
| 1 | (a) | Allowances available on computers | |
| | | Initial allowance | $^1/_2$ |
| | | Annual allowance: first year | $^1/_2$ |
| | | subsequent years | $^1/_2$ |
| | | rate | $^1/_2$ |
| | | | 2 |
| | (b) | Calculation of capital allowances | |
| | | Additions: industrial building | 1 |
| | | other ($^1/_2$ mark each) | 2 |
| | | Disposal | $^1/_2$ |
| | | Investment allowance (1 mark each) | 2 |
| | | Initial allowances (1 mark each) | 2 |
| | | Annual allowances ($^1/_2$ mark each) | 3 |
| | | Tax written down values at the end of the year ($^1/_2$ mark each) | 3 |
| | | Balancing charge | 1 |
| | | Summary of allowances | $^1/_2$ |
| | | No initial allowance on passenger vehicle | $^1/_2$ |
| | | No allowance on offices | $^1/_2$ |
| | | | 16 |
| | (c) | Computation of taxable profits | |
| | | Profit before taxation | $^1/_2$ |
| | | Items not allowed for taxation ($^1/_2$ mark each) | $3^1/_2$ |
| | | Items deductible other than the training allowance ($^1/_2$ mark each) | $1^1/_2$ |
| | | Training allowance | 1 |
| | | No adjustment for: cutlery losses | $^1/_2$ |
| | | overdraft arrangement fee | $^1/_2$ |
| | | lease charge interest | $^1/_2$ |
| | | | 8 |
| | (d) | Tax payable | |
| | | Provisional tax: based on profit estimate | $^1/_2$ |
| | | quarterly during the year | $^1/_2$ |
| | | Balance within 180 days | $^1/_2$ |
| | | Tax at external companies' rate | 1 |
| | | Deduction of provisional tax | $^1/_2$ |
| | | Deduction of withholding tax on interest | 1 |
| | | | 4 |
| | | | **30** |

| | | | Marks |
|---|---|---|---|
| 2 | (a) | Income from a partnership business | |
| | | Assessed on partners | 1 |
| | | Normal principles of computation apply | 1 |
| | | Shared on agreed basis amongst partners | 1 |
| | | | 3 |
| | (b) | Computation of taxable income from the business | |
| | | Depreciation | $^1/_2$ |
| | | Joseph's salary | $^1/_2$ |
| | | Capital allowances | 1 |
| | | Share of profits: Joseph's salary | 1 |
| | | Allocation of remainder ($^1/_2$ mark each) | 1 |
| | | | 4 |
| | (c) | Computation of income tax payable by Lapukeni and Jane | |
| | | Salary ($^1/_2$ mark each) | 1 |
| | | Housing allowance ($^1/_2$ mark each) | 1 |
| | | Partnership profit | $^1/_2$ |
| | | Director's fees | $^1/_2$ |
| | | Net rents | $^1/_2$ |
| | | Taxable interest | $^1/_2$ |
| | | Calculation of tax payable (1 mark each) | 2 |
| | | Workings for net rent: | |
| | | Rental income | $^1/_2$ |
| | | Mortgage interest | $^1/_2$ |
| | | Property management fee | $^1/_2$ |
| | | Repairs to roof | $^1/_2$ |
| | | No adjustment for new driveway | $^1/_2$ |
| | | Working for taxable interest: | |
| | | Gross amount | $^1/_2$ |
| | | Application of K10,000 exemption | 1 |
| | | | 10 |
| | (d) | Additional tax payable by or refundable to Lapukeni | |
| | | Calculated tax (from (c)) | $^1/_2$ |
| | | PAYE and withholding tax on interest ($^1/_2$ mark each) | 1 |
| | | Withholding tax on rent and director's fees (1 mark each) | 2 |
| | | Provisional tax (apportioned) | 1 |
| | | Tax refundable | $^1/_2$ |
| | | Working for PAYE: | |
| | | Housing allowance included in calculation | $^1/_2$ |
| | | Calculation of PAYE | 1 |
| | | Working for withholding tax on interest: | |
| | | Application of K10,000 exemption | 1 |
| | | Withholding tax at correct rate | $^1/_2$ |
| | | | 8 |
| | | | **25** |

| | | | Marks |
|---|---|---|---|
| 3 | (a) | Application of VAT | |
| | | Items subject to a VAT charge ($^1/_2$ mark each) | $1^1/_2$ |
| | | Persons responsible ($^1/_2$ mark each) | $1^1/_2$ |
| | | | 3 |
| | (b) | Calculation of additional VAT | |
| | | Calculation of over or underpayments ($^1/_2$ mark each) | 3 |
| | | Correct due dates | 1 |
| | | Correct number of days ($^1/_2$ mark each) | $2^1/_2$ |
| | | Correct rate of interest | 1 |
| | | Interest calculations ($^1/_2$ mark each) | $2^1/_2$ |
| | | Offsetting of overpayment in July against underpayment in August | 1 |
| | | | 11 |
| | (c) | Penalties | |
| | | Fixed K20,000 penalty | $^1/_2$ |
| | | K1,000 per day | $^1/_2$ |
| | | | 1 |
| | | | **15** |
| 4 | (a) | Pastoral, agricultural and farming operations ($^1/_2$ mark each per item deductible) | 3 |
| | (b) | Timber growing | |
| | | By election | 1 |
| | | Cost carried forward | 1 |
| | | Annual fixed percentage added | 1 |
| | | Apportion on sale | 1 |
| | | Effect of annual percentage on taxable income | 1 |
| | | Effect of other expenditure | 1 |
| | | | 6 |
| | (c) | Clubs and societies | |
| | | Taxable not withstanding from members | 1 |
| | | Proportion of income | $^1/_2$ |
| | | Types of income | 1 |
| | | Applicable tax rate | $^1/_2$ |
| | | | 3 |
| | | | **12** |

| | | | | Marks |
|---|---|---|---|---|
| **5** | **(a)** | **(i)** | Withholding tax | 1 |
| | | | Fringe benefits tax | 1 |
| | | | Provisional tax | 1 |
| | | | | 3 |
| | | **(ii)** | Calculation of tax payable | |
| | | | Tax payable | 1 |
| | | | Provisional tax deducted | $^1/_2$ |
| | | | Withholding tax on interest deducted | $^1/_2$ |
| | | | Explanations: | |
| | | | re withholding tax on supplier payments | 1 |
| | | | re fringe benefits tax | 1 |
| | | | re value added tax | 1 |
| | | | | 5 |
| | **(b)** | **(i)** | Capital gains | |
| | | | Capital allowances claimed: | |
| | | | Treatment of gains | 1 |
| | | | Treatment of losses | 1 |
| | | | Capital allowances not claimed: | |
| | | | Treatment of gains | 1 |
| | | | Treatment of losses | 2 |
| | | | 60% factor | 1 |
| | | | | 6 |
| | | **(ii)** | Calculation of gain | |
| | | | No losses carried forward at 1 July 2006 | 1 |
| | | | Capital allowances claimed: | |
| | | | Loss to be claimed in year | 1 |
| | | | Capitals allowances not claimed: | |
| | | | Offset of loss against gain in year | 1 |
| | | | Restricted carry forward of loss | 1 |
| | | | | 4 |
| | | | | **18** |