

Fundamentals Level – Skills Module

Taxation (Malawi)

Monday 2 June 2008

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 page 2.

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 – 84,000		0
84,001 – 120,000	15%	5,400
120,000+	30%	–

Company rates

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 equipment
	– Trailers
	– Farm fencing
15%	– Mobile cranes
17.5%	– General plant and equipment on double shift
20%	– Motor cycles
	– Motor vehicles
	– Pick-ups
	– Light lorries (for light work)
	– Cement mixers
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

ALL FIVE questions are compulsory and MUST be attempted

- 1 (a) Milambe Insurance Company Limited was incorporated in Malawi in 1986. The company is involved in general insurance business.

The company makes up its financial statements to 31 December, each year.

The following are the results of the company for the year ended 31 December 2007.

Income	Note	K
Gross earned premiums		6,250,600
Reinsurance premiums		(2,650,100)
		<u>3,600,500</u>
Fees and commissions		348,300
Investment income	1	1,265,460
Other income	2	68,900
		<u>5,283,160</u>
Expenses		
Policy holders' claims and benefits	3	(1,685,400)
Bank interest		(325,750)
Management expenses	4	(930,465)
Finance costs	5	(735,482)
		<u>(3,677,097)</u>
Total expenses		<u>(3,677,097)</u>
Profit before income tax		<u><u>1,606,063</u></u>

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

1. Investment income

	K
Interest from bank deposits	179,960
Investment income from	
– Treasury bills	300,000
– Dividends	325,000
Rental income	460,500
	<u>1,265,460</u>

2. Other income

	K
Profit on the sale of plant and equipment	865,400
Exchange loss	(796,500)
	<u>68,900</u>

The profit on the sale of the plant and equipment is in respect of a flat owned by the company that was sold during the year. The capital gain taking into account indexation was calculated as K486,500.

3. Policy holders' claims and benefits

	K
Insurance claims	1,385,521
Provision for premium income (2% of premium debtors)	625,725
Recoveries from re-insurers	(325,846)
	<u>1,685,400</u>

Only 1% of the premium debtors relates to the proportion of the risks taken by Milambe Insurance Company Limited.

4. Management expenses

	K
Depreciation	365,100
Subscriptions – African Institute of Insurers	65,000
Donations – Macoha	22,500
– Masinkha Church	10,000
Fringe benefits tax	125,000
Communication and accommodation	165,600
Repairs and maintenance – vehicles	177,265
	<u>930,465</u>

5. Finance costs

	K
Interest on loans	335,850
Finance lease charges	165,175
Other finance costs	234,457
	<u>735,482</u>

The loan was obtained to finance the acquisition of shares in the National Investment Trust. The dividend received from the Trust is included in dividend income in the financial statements.

Included in other finance costs is K85,000, being the write off of a loan given to the managing director and duly approved by the Board.

6. The capital allowances claimable by the company for the year have been agreed at K385,450

Required:

- (i) **State the provisions with regard to the determination to taxation of income from insurance business, other than taxable income from life insurance.** (7 marks)
- (ii) **Compute the taxable income of Milambe Insurance Company Limited for the year ended 31 December 2007.** (9 marks)

- (b) Maliba Limited is a company involved in the manufacturing of shoes. The company is located in the Chirimba Industrial Area.

The following information is available in connection with the property and equipment used in Maliba Limited's business for the year ended 31 December 2007.

Tax written down values (TWDV) as at 1 January 2007:

	K
Factory building	8,500,600
Motor vehicles (saloon)	2,800,800
Plant and equipment	6,750,250
Computers	2,500,000
Motor lorries (for light work)	3,681,465

The following transactions took place during the year ended 31 December 2007:

Additions to property and equipment at cost:

		K
April	Machine (new)	865,500
July	Lorry (for light work)	1,265,000
August	Factory extension	2,465,000
September	Computers (two desktops)	465,000

Included in the cost of the factory extension is the cost of an office amounting to K620,500.

Disposals

April – Motor vehicle (sale proceeds) K350,000

The vehicle had been purchased in January 2006 for K791,666.

Required:

Prepare the capital allowances schedule for Maliba Limited for the year ended 31 December 2007, and compute the total allowances available to the company for that year.

Note: you should pay particular attention to the presentation of the schedule. (14 marks)

(30 marks)

2 Maziko Tebulo is employed as a program manager by Pensioners Foundation, a charitable organisation operating in Malawi. The foundation headquarters are based in the United Kingdom.

Maziko's salary, which is paid in US dollars, is transferred directly into his bank account. His annual salary is US\$48,000. The arrangement is that Maziko will pay the respective PAYE directly to the Malawi Revenue Authority.

The following additional information is available in connection with the affairs of Maziko:

1. He runs three minibuses which operate between Lilongwe, Dwangwa and Mzuzu. The summarised profit and loss statement for this business for the year ended 30 June 2008 is as follows:

	K	K
Minibus fares		3,825,600
Less Expenditure		
Depreciation	390,000	
Tyres and tubes	365,100	
Fuel and oils	1,651,500	
Salaries	365,000	
Road permits	24,000	
Licences	86,500	
Minibus tax	90,000	
Minibus Operators Association fee	45,000	
Maintenance costs	465,000	
	<u>4,650,600</u>	
Net profit for the year		<u>343,500</u>

The minibus tax is the tax payable by minibus operators. This tax is payable quarterly as provisional tax.

The minibuses were all bought at the beginning of the year and cost K650,000 each.

2. Other income:	K
Director's fees – Mpico (gross)	125,000
Dividend from NITL (net)	65,000
Interest received (net)	45,000

The interest received was from a fixed deposit account maintained during the year with the National Bank of Malawi.

The interest received was as follows:	K
May 2008	35,000
June 2008	10,000
	<u>45,000</u>

3. The exchange rates applicable during the year on receipt of the salary transferred were:

July 2007 to December 2007 1US\$ – K139.40

January 2008 to June 2008 1US\$ – K138.25

4. Maziko owns a house in Mpingwe, which he lets out to Pharmacy Limited at a monthly rental of K35,000.

The outgoings on this property during the year were:

	K
City rates	65,000
Repairs and maintenance	45,000
Paving the driveway	125,000
Mortgage payments (of which K13,000 per month is interest)	360,000

5. Withholding tax on the rentals and director's fees was duly deducted and remitted to the Malawi Revenue Authority on payment.

6. Maziko is married to Judith whose only source of income is a salary of K360,000 per year. She works as a secretary at a local hospital.

Required:

- (a) Calculate the income tax payable by or refundable to Maziko Tebulo on the assumption that all taxes payable by him for the year ended 30 June 2008 were paid on the due dates. (19 marks)
- (b) State when PAYE is due and the penalties that would be payable if PAYE had not been paid on Maziko's salary during the year. (2 marks)
- (c) State the responsibilities of an employer with regard to the payment of PAYE. (4 marks)

(25 marks)

- 3 (a) (i) **List the requirements for and the circumstances that must exist for a company to register for value added tax (VAT).** (3 marks)
- (ii) **State the effect that failure to register will have on a company required so to do.** (2 marks)
- (b) **VAT is applied when there is a taxable supply; state when a taxable supply is deemed to have occurred.** (7 marks)
- (c) **Explain the provisions introduced in the 2007 Tax Amendment Act in respect of duties and VAT on expenditure on tourism related items.** (3 marks)
- (15 marks)**

- 4 Titanic Limited (Titanic) is a locally incorporated company in the tourism industry. The company currently employs a manager and six tour guides. The company makes up its accounts to 31 March each year.
- The following are the salaries and benefits paid by the company to its employees for the financial year ended 31 March 2008.

Manager

- (1) Monthly salary of K65,000.
- (2) A fully furnished house. The house is rented by Titanic at K35,000 per month. The manager contributes 10% of his salary towards the rental.
- (3) School fees paid for his two children at St Augustine Secondary School. The total fees paid during the financial year were K465,000.
- (4) Telephone costs of K35,000 were paid to Malawi Telecommunications Limited during the year. The telephone is installed in the manager's house.
- (5) An allowance of K5,000 per month is paid to the manager for water and electricity.
- (6) A motor vehicle with unlimited usage was provided during the year. The vehicle cost K4,500,000 when bought by Titanic in 2005.

Tour guides

- (1) Monthly salary of K45,000, paid to each guide.
- (2) A housing allowance is paid at 40% of basic salary, to each guide.
- (3) Mileage claims are paid to the guides for the use of their own vehicles while on company business. The average claim per guide is K8,750 per month.
- (4) Motor vehicle loans were provided to the tour guides by Titanic. The total amount of these loans was K5,600,000. Interest at 10% was charged to the employees on these loans. The bank base lending rate during the year was 22.5%.

Required:

- (a) **Explain the administrative provisions with regard to the taxation of fringe benefits provided by an employer to its employees.** (3 marks)
- (b) **Calculate the fringe benefits tax that would be payable on the benefits provided by Titanic Limited to its employees for the year ended 31 March 2008, giving reasons for any items you exclude from your computation.** (9 marks)

(12 marks)

5 Dulani and Phiso intend to commence a business venture selling spare parts for cars.

They are not certain how they should operate the business venture. The options they are considering are a partnership or an incorporated company.

If they use a partnership they will share profits as follows:

Dulani	60%
Phiso	40%

If they form an incorporated company they will hold shares in the same proportion (60:40), and distribute 50% of the profits after tax as dividends.

The following are expected to be the results of their first twelve (12) months of trading.

	Note	K	K
Sales			12,860,790
Cost of sales			5,401,160
Gross profit			7,459,630
Less: Expenditure			
Salaries and wages	1	4,250,600	
Rent and rates		860,750	
Travelling and entertainment		335,860	
Depreciation	2	975,000	6,422,210
Profit before taxation			1,037,420

Notes:

1. Included in salaries and wages are the salaries to be paid to Dulani and Phiso as follows:

	K
Dulani	1,368,000
Phiso	1,260,000

2. Depreciation relates to a delivery vehicle on which capital allowances will be claimed. The capital allowances are expected to be K1,370,000 in the first year.

Required:

- (a) Advise Dulani and Phiso on which of the two structures – partnership or incorporated company – is the better option in terms of the amount of tax payable, assuming that Dulani and Phiso have no other sources of income.

Note: for the purposes of your calculations, you should use the tax rates given at the front of this question paper. (16 marks)

- (b) State what other factors they should take into account in arriving at their decision. (2 marks)

(18 marks)

End of Question Paper