TAXATION PROGRAMME EXAMINATIONS

CERTIFICATE LEVEL

C1: BUSINESS MANAGEMENT

FRIDAY 14 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

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2. This question paper consists of FIVE (5) questions of twenty (20) marks each. You MUST attempt all the FIVE (5) questions.

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7. Present legible and tidy work.

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Attempt all five (5) questions.

QUESTION ONE

The modern corporate world today is faced with an acute shortage of leaders in management positions. Many agree that being a manager does not necessarily make one a leader. Effective leadership is crucially needed in emerging markets like Zambia where the business external environment is highly unpredictable.

Required:

(a) Explain five (5) differences between a management and leadership (10 marks)

(b) Explain how a manager working for a small manufacturing firm can analyse the external business environment using the PESTEL model. (10 marks)

[Total: 20 Marks]

QUESTION TWO

(a) Organisations are created for a common purpose. Explain the four (4) common characteristics of an organisation. (8 marks)

(b) A sole trader has complete control over his or her activities, business and finances, though may fail to distinguish between personal and business finances.

Required:

Advise a sole trader on the advantages of the following to their business:

(i) Full control (3 marks)

(ii) Informing ZRA about your business (3 marks)

(iii) Personalized approach (3 marks)

(iv) Quick decision making (3 marks)

[Total: 20 Marks]

QUESTION THREE

(a) Explain the impact of political and legal factors on a business organisation operating in Lusaka. (10 marks)

(b) A central feature of the successful organisation is the diagnosis of its culture and ability of the organisation to adapt to change.

Required:

Explain five (5) factors that influence the development of organisation culture. (10 marks)

[Total: 20 Marks]

QUESTION FOUR

(a) Discuss the motivation theory of Douglas McGregor (8 marks)

(b) Describe the process of effective communication. (6 marks)

(c) State three (3) reasons for the assessment of the business environment by Business organisations. (6 marks)

[Total: 20 Marks]

QUESTION FIVE

(a) Mr. Kafu believes that once the strategy has been formulated, all the members must be responsible about it. Upon being blamed by the Board of Directors for poor organization performance and lack of adherence to the implementation of the strategy, he responded that the board was being unfair and that everyone and not only he were responsible.

Required:

Using a six (6) model of strategic leadership components by the American CEO's, explain to Mr. Kafu about what he has to do as a leader to improve the situation in the company. (12 marks)

(b) Briefly explain the four (4) major categories of grand strategies. (8 marks)

[Total: 20 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

Part (a)

Leadership Vs Management

Leadership	**Management**
- Can only be exercised over people	- Can be exercised over tasks, time, projects, resources
- Is an interpersonal process	- Is an organisational process
- Is based on power/influence	- Is based on authority
- Depends on 'followership': conferred from below	- Depends in legitimacy: delegated from above
- Secures commitment/extra levels of performance	- Secures compliance/standard levels of performance
- Involves influencing, persuading, enthusing, creating/communicating vision for change	- Involves structure, analysis, control activities: planned inputs → predictable outputs

Part (b)

A manager in a small manufacturing firm can use the model PESTEL to analyse the external environment.

Variable	Explanation
Political	Political action can negatively impact manufacturing operations. Government action such as the increase in minimum wage can increase the operating cost of a business. Political instability can also lead to loss of assets through vandalism, terrorism to mention but a few. Apart from lobbying activities, there is little that can be done to protect a business from adverse political action.
Economic	Economic fundamentals such as inflation, exchange rates, the level of trade in the country to mention of few, can have far reaching impact on a manufacturing firm. A weaker local currency means increased input costs for a manufacturing firm which sources supplies from other countries.
Social culture	Social norms and culture can influence consumer tastes and preferences. A manufacturing concern whose products do mirror the social expectations and values of the target market may not enjoy leverage on consumer demand. It is true that the modern consumer sees value in a product which comes with health benefits. In Islamic nations for instance, there is a particular type of dress code which is considered acceptable in society.

Technological	Technology is here to stay and any business including those in manufacturing can drastically minimise operating costs and improve standardisation of output through it. Firms which do not invest in new technology may not compete favourably on the local and international market. This is partly because of failure to minimise costs.
Ecological	Many countries require companies to comply with environmental laws. Non adherence to such laws may lead to penalties. The management team of a manufacturing firm should endeavour to minimise damage to the environment by initiating and implementing environmentally friendly policies.
Legal	The legal framework of a given country must be appreciated in order to minimise compliance risk. All the major laws which affect the manufacturing firm especially those which relate to workers safety must be applied diligently.

SOLUTION TWO

a) The common characteristics of an organisation are:

- Distinct purpose- the expression of the goal or goals that the organisation hopes to accomplish.
- People- it is an organisation because people with different talents need to work together to achieve the organisational goals.
- Deliberate structure- this stipulates and guides members of the organisation on how and where they are to perform their duties. This is determined through job descriptions and the type of structure adopted by each organisation needs.
- Division of labour- coordination which ensures that people work together so that their many efforts contribute to a higher level of accomplishment. (8 Marks)

b) The following are the advantages to a sole trader:

I. Full control- the business growth is subject to the personal efficiency and effectiveness of the owner, his values and aspiration which can add value depending on his or her decisions.

II. Informing ZRA about the business- business registration is a legal requirement in Zambia and compliance to it will offer certain advantages to the sole trader and his business such as protection from forced closures, lawsuits and allow access to financial assistance from individuals and financial institutions.

III. Personalized approach- this is key to the stakeholder relations which are building blocks in business e.g. the nurturing of the customer relations in order to make them stay loyal to the business for its survival.

IV. Quick decision making- there is an advantage because the decisions are made with much flexibility since bureaucracy is not present as may be the case with other forms of business e.g. limited companies since consultations have to be made. (12 Marks)

SOLUTION THREE

(a) Impact of political and legal factors on business organisations

(i) **Political Factors:** The ruling political party have a manifesto the clearly states its social and economic policies. Therefore, the government will formulate policies to suit their social and economic agenda which will directly affect the business organizations. The government will enact laws that affect the operations of business such as minimum wage, price controls, consumer protection laws etc.The stability or instability of the political environment affect the business plans. Consideration of the potential opposition party's economic and social ideologies must be taken into account in case of change of government.

(ii) **Legal Factors:** The Government formulates various laws that regulate business organisation. These laws are enforced by different law enforcement agents such Zambia Revenue Authority, NAPSA, PACRA, ZEMA etc.The laws enacted are labour laws, taxation law, company law, consumer protection laws.

(b) Factors that influence the development of organisation culture

(i) **Nature of Business**: This involves the nature of goods or services provided to the target market. This includes the range and quality of goods and services.

(ii) **Technology**: technological processes and methods employed will influence the culture of the organisation.

(iii) **History**: The philosophical and values of its shareholders and first senior managers will influence its culture.

(iv) **Strategy**: The long term strategic goals will influence the culture the organisation will adopt.

(v) **Size**: The size of the organisation could be in terms of number of employees, departments, branches that will have influence on structure and culture of the organisation.

(vi) **Location**; geographical location and physical features have influence on organizations culture. For example location could be a quiet or busy place.

SOLUTION FOUR

(a) Motivation theory of Douglas McGregor

This is the motivation theory of theory X and theory Y assumption of how managers think about workers developed by Douglas McGregor in the 1960s.

Theory X assumptions

(i) An average worker is lazy and has an inherent dislike of work.

(ii) Most workers must be coerced, controlled and threatened with punishment if objectives need to be achieved .

(iii) An average worker avoids responsibility, prefers to be directed and values security.

(iv) Motivation only occurs at psychological and security levels.

Theory Y assumptions

(i) For most employees work is as natural as rest
(ii) Workers will exercise self-direction and control in the service of objectives to which they are committed.
(iii) Given the right condition, an average worker seeks for responsibility
(iv) Commitment to objectives is a function of rewards associated with achievement.

(b) Process of communication

(i) **Sender:** the originator of the message to be transmitted.

(ii) **Encoding**: translating symbols, words, gestures into meaningful meaning.

(iii) **Channel**: medium of exchange to be used for transmmission

(iv) **Recipient**: Receiver of the message from the sender

(v) **Decoding**: Interpreting the message into meaning information

(vi) **Feedback**: this is the acknowledgement of the message from the sender.

(c) Reasons for assessment of business environment

(i) To ascertain the level of competition in the industry.

(ii) To collect information and use it for strategic decision making

(iii) To collect information to determine how favourable both the economical and political environment is.

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

CERTIFICATE LEVEL

C2: ECONOMICS & FINANCIAL MATHEMATICS

WENESDAY 16 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

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9. Formulae are provided in a separate booklet.

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Attempt all five (5) questions.

QUESTION ONE

(a) Distinguish between each of the following pairs of concepts used in economic theory:

(i) Microeconomics and Macroeconomics (2 marks)

(ii) Revocable and Irrevocable Credit (2 marks)
(iii) Comparative advantage and Absolute advantage (2 marks)

(iv) Direct taxes and Indirect taxes (2 marks)
(v) Treasury Bills and Government Bonds (2 marks)

(b) The demand and supply functions for cases of bathing soap in central province of Zambia is given by:

Demand Function: $P_d = 50 - 2Q_d$

Supply Function: $P_s = 25 + 0.5Q_s$

(i) Determine the equilibrium price and quantity. (5 marks)

(ii) Determine the effect on the market equilibrium if the government decides to impose a fixed tax of K5 on each good. (5marks)

[Total: 20 Marks]

QUESTION TWO

(a) Distinguish between a direct tax and an indirect tax. Give two examples and two advantages of each**.** (8 marks)

(b) Outline any three (3) principles of a 'good' taxation system (the canons of taxation)

(6 marks)

(c) Explain any three (3) functions of taxation in any country/ economy. (6 marks)

[Total: 20 Marks]

QUESTION THREE

(a) In a certain test where scores were approximately normally distributed with a mean of

75 and a standard deviation of 20. What percentage of candidates scored higher than

55? (5marks)

(b) Assembly line produces approximately 3% defective items. In a batch of 150 items, find
the probability of obtaining:

(i) At least one is defective (3 marks)

(ii) None is defective (2 marks)

(iii) Exactly one is defective (3 marks)

(c) A fair coin is tossed 4 times. Find the probability of obtaining:

(i) Exactly two heads (2 marks)

(ii) At least one head (3 marks)

(iii) Three heads and one tail (3 marks)

[Total: 20 Marks]

QUESTION FOUR

(a) A bank manager wishes to investigate the relationship between years of experience (X)
and the number of errors (Y) that bank tellers commit. A survey of eight (8) employees
was conducted and the results are tabulated in the table below:

Employee	A	B	C	D	E	F	G	H
Years of experience	5	6	8	10	11	12	13	15
Number of errors	22	23	16	19	15	15	12	14

Further $\sum x = 80$; $\sum y = 136$; $\sum xy = 1277$; $\sum x^2 = 884$; $\sum y^2 = 2420$

Required:

Using the above data:

(i) Calculate the product-correlation coefficient and interpret it (5 marks)

(ii) Find the coefficient of determination and interpret it (2 marks)

(iii) Find the least squares regression equation of errors on experience (5 marks)

(iv) Predict the number of errors you would expect from an employee with 7 years of experience (2 marks)

(b) Find the Yield to Maturity of a bond with a par value of K1000 and currently trading at

K850 if the coupon rate is 8% and it will mature in 9 years. (6 ma **[Total: 20 Marks]**

QUESTION FIVE

(a) Define the following terms:

(i) Normal yield (2 marks)

(ii) Running yield (2 marks)

(b) What is the difference between yield and return? (3 marks)

(c) Treasury bill (or T-bills) are financial instruments that the Zambian government uses to finance public debt. Suppose you buy a 91- day T-bill with a face value of 20 million kwacha at a discount rate of 2.5% assuming that a year has 360 days, calculate the price of the T-bill. (5 marks)

(d) The Management of Tusha Electronics Company is considering to purchase an equipment to be attached with the main manufacturing machine. The equipment will cost K6,000 and will increase annual cash flow by K2,200. The useful life of the equipment is six (6) years. After six (6) years, it will have no salvage value. The Management wants a 20% return on all investments.

Required:

(i) Compute the net present value (NPV) of this investment project. (6 marks)

(ii) Should the equipment be purchased according to NPV analysis? Explain your answer. (2 marks)

[Total: 20 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a)

(i) Mirco-economics is the branch of economics that studies decision making by a single individual household, firm, industry, or level of government. Macroeconomics, on the other hand, is the branch of economics that studies decision making for the economy as a whole.

(ii) A revocable credit is a documentary credit which gives no guarantee to the exporter that payment will actually be made because it may be cancelled or amended at any time without prior notice to the beneficiary. In contrast, an irrevocable credit is a documentary credit which gives guarantee that, provided the terms and conditions of the credit are complied with, payment will be made. Any cancellation or amendments to this credit can only be made with the consent of all parties.

(iii) Comparative advantage is the ability of a country to produce a good at a lower opportunity cost than its trading partner. Absolute advantage is the ability of a country to produce a good using fewer resources than its trading partner.

(iv) Direct taxes are taxes levied on individuals and corporations such as personal and corporate income taxes, PAYE and Estate and gift tax. In contrast, indirect taxes are taxes levied on goods and services. Examples are customs duties, sales tax, excise taxes and Value-added-tax (VAT).

(v) A treasury bill is a financial instrument used by the government to raise short term funds while a government bond is a financial instrument used by the government to raise long term funds.

(b) (i) Equilibrium occur when $Q_d = Q_s$ and $P_d = P_s$

this implies the functions are written as $P = f(Q)$ taking $P \text{ and } Q$ as only variables on LHS and RHS respectively.

Therefore $50 - 2Q = 25 + 0.5Q$

$0.5Q + 2Q = 50 - 25$

$Q = 10$ the equilibrium quantity

To find the equilibrium price, substitute Q in any of the equations of P

$$P = 50 - 2(10)$$

$$P = 30$$

(ii) If the government imposes a fixed tax of K5 per good then the money that the firm actually receives from the sale of each good is the amount, P, that the consumer pays, less the tax, 5: that is, $P - 5$. Mathematically, this problem can be solved by replacing P by $P - 5$ in the supply equation to get the new supply equation $P - 5 = 0.5Q_S + 25$ that is

$$P = 0.5Q_S + 30$$

The remaining calculations proceed as before. In equilibrium, $Q_d = Q_s$. Again setting this common value to be Q gives

$$P = -2Q + 50$$

$$P = 0.5Q + 30$$

Hence

$$-2Q + 50 = 0.5Q + 30$$

which can be solved as before to give $Q = 8$. Substitution into either of the above equations gives $P = 34$.

SOLUTION TWO

(a) A direct tax is paid directly to the revenue authorities, it is levied on income or profits, examples are income tax, company (corporation) tax, inheritance tax, capital gains tax...

An indirect tax is paid indirectly whenever a purchase is made, collected from an intermediary, eg value added tax, sales tax, import duties....

(b) The Principles of a good tax or Canons of taxation are

- Equity people should pay according to their ability
- Certainty tax to be well defined and easily understood
- Convenience payment to be related to how and when people receive their money
- Economy cost of collection should not be too high to exceed the yield

(c) The functions of taxation

- To raise revenue for the government
- To redistribute income
- To protect infant industries from foreign competition
- To pay social costs for some products e.g. environmental issues
- To provide a stabilising effect on national income, i.e. is expansionary policies to reduce unemployment by lowering taxes or the opposite, to deflate the economy by increases taxes and lower inflation
- To manage aggregate demand, related to the above, boost the economy or reduce...

SOLUTION 3

a) $Z = \frac{x - \mu}{\sigma} = \frac{55 - 75}{20} = {}^{-}1$, which means 1 standard deviation below the mean

$P(z > 55) = \frac{55 - 75}{20} = -1.00$ which give an area of 0.3413 from the normal table

Thus 0.3413 + 0.5 = 0.8413 or 84% scored higher than 55.

b) Poisson distribution because n is very large and P is very small i.e. 0.03

$P(x) = \frac{\lambda^x e^{-}\lambda}{X!}$, $\lambda = np = 150(0.03) = 4.5$

(i) $P(x \geq 1) = 1 - P(x=0) = 1 - \frac{4.5^0 e^{-4.5}}{0!} = 1 - 0.011 =$ **0.9889**

(ii) $P(x=0) = \frac{4.5^0 e^{-4.5}}{0!} =$ **0.0111**

(iii) $P(x=1) = \frac{4.5^1 e^{-4.5}}{1!} = 4.5(0.0111) =$ **0.04999**

c) N = 4, P = ½ or 0.5, q = 1 – 0.5 = 0.5

Using $^nC_r\, p^n q^{n-r}$

(i) $P(r = 2) = {}^4C_2\,(0.5)^4(0.5)^{4-2} = 6 \times 0.25 \times 0.25 =$ **0.375**

(ii) $P(r > 1) = 1 - P(r = 0) = 1 - 0.0625 =$ **0.9375**

Note $P(r = 0) = {}^4C_0(0.5)^4(0.5)^{4-0} = 0.0625$

(iii) $P(r = 3) = {}^4C_3(0.5)^4(0.5)^{4-3} = 0.25$; $P(r = 1) = {}^4C_1(0.5)^4(0.5)^{4-1} = 0.25$

Thus P(3 heads and 1 tail) = P(r = 3) x P(r = 1) = 0.25 x 0.25 = **0.0625**

SOLUTION 4

a) (i) $r = \frac{n\sum xy - \sum x \sum y}{\sqrt{[n\sum x^2 - (\sum x)^2][n\sum y^2 - (\sum y)^2]}}$

$$r = \frac{8(1277) - 80\,(136)}{\sqrt{[8\,(884) - (80)^2][8\,(2420) - (136)^2]}}$$

$$r = \frac{-664}{\sqrt{672 \times 864}}$$

$$r = \frac{-664}{761.976377}$$

$$\underline{\underline{r = -0.87}}$$

There is a high negative correlation between the number of errors and years of experience for bank teller

(ii) $r^2 = (-0.87)^2 \times 100 = 0.7569 \times 100$

$$\underline{\underline{= 75.69\%}}$$

About 76% of the errors are attributed to years of experience while only 24% of them is attributed to other factors

(iii) $b = \frac{n\sum xy - \sum x\sum y}{n\sum x^2 - (\sum x)^2} = \frac{8(1277) - 80(136)}{8(884) - (80)^2} = \frac{-664}{672} = -0.99$

$a = \sum y/n - b\sum x/n = 136/8 - (-0.99)(80/8) = 26.9$

Thus, $Y = 26.9 - 0.99X$ is the prediction equation

(iv) $Y = 26.9 - 0.99(7) = 19.97 = 20$ errors

b) Mkt price = K850, m = K1000 I = 8% of K 100 = K80 n = 9

$\text{YTM} = \text{I} + \frac{(\text{M}-\text{P})}{n} \div \frac{2(\text{P})+\text{M}}{3}$

$\text{YTM} = \frac{80+(1000-850)}{9} \div \frac{2(850)+1000}{3}$

$= \frac{96.66666667}{900}$

$= 0.107407407 * 100$

$= 10.7\%$

Other formula

P = I (PVIFA) + m (PVIF)

AF = 12%, 9 years P = 80 (5.328) + 1000 (0.361) = K787.24

AF 10%, 9 years P = 80 (5.759) + 1000 (0.42474) = K884.72

YTM = A% + ($\frac{\mathrm{H-P}}{H-L}$) (B – A) %)

= 10% + ($\frac{884.72-850}{884.72-787.24}$) (12 – 10%)

= 10% + ($\frac{34.72}{97.48}$) * 2%

= 105 + 0.712351211%

= 10.7%

SOLUTION 5

i) The annual percentage yield is the percentage rate which when compounded annually, would yield the same return as the given interest rate with the given compounding period. Annual percentage yield (APY) is the common basis to compare the investments.

ii) The yield to maturity (YTM) is that discount rate which equates the present value of a bond's cash flow to its price.

b) Money invested by Mrs Sibeso is P_0 = K51200

Interest rate is r = 4.15% = 0.0415

Number of times compounded in a year m = 12

Let S be the equivalent APY.

The value of the investment at the end of one year with this percentage rate is

$$A = 51200\,(1 + S)$$

Amount accumulated after 1 year $= 51200\,\left(1 + \frac{0.0415}{12}\right)^{(12)(1)}$

[As the interest is compounded continuously.]

$$= 51200\,(1.00345)^{12}$$

$51200\,(1 + S) = 51200\,(1.00345)^{12}$

c) [From the definition of APY.]

$$1 + S = (1.00345)^{12}$$

$$1 + S = 1.04219$$

$$S = 0.04219 = 4.21\%$$

c) Note: When future values are brought back to present values at a given rate of interest, the interest rate is referred to as the discount rate.

The present value of the cash outflow is the initial outlay of K400 000. The present value of cash inflows is calculated by summing the present value of each cash inflow as follows:

i) Consider $r = 15\%$

$$NPV_A = 120000(1.15)^{-1} + 130000(1.15)^{-2} + 140000(1.15)^{-3} + 150000(1.15)^{-4}$$
$$= 104348.83 + 98298.68 + 92052.27 + 85762.99 = 380462.77$$

Thus the NPV is

$$380462.77 - 400000 = -19537.23$$

As the NPV is negative, the firm should not invest in this project.

ii) Considering $r = 8\%$

$$NPV_B = 120000(1.08)^{-1} + 130000(1.08)^{-2} + 140000(1.08)^{-3} + 150000(1.08)^{-4}$$
$$= 111111 + 111454 + 111137 + 110254 = 443956$$

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

CERTIFICATE LEVEL

C3: ACCOUNTANCY FOR TAX PRACTITIONERS

MONDAY 14 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

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Attempt all five (5) questions in this paper.

QUESTION ONE

1. The following trial balance was extracted from the books of DMC at the close of business on 28 February 2019

	DR K	CR K
Purchases and sales	974,400.00	1,650,232.50
Cash at bank	43,050.00	
Cash in hand	3,402.00	
Capital Account 1 March 2018		119,700.00
Drawings	179,550.00	
Office furniture	30,450.00	
Rent	35,700.00	
Wages and salaries	329,700.00	
Discounts	8,610.00	1,680.00
Accounts receivables and payables	129,318.00	55,072.50
Inventory 1 March 2018	43,260.00	
Allowance for irrecoverable debts 1 March 2018		4,252.50
Delivery van	39,375.00	
Van running costs	6,457.50	
Bad debts written off	7,665.00	
	1,830,937.50	1,830,937.50

ADDITIONAL INFORMATION

(i) Inventory at 28 February was valued at K25,200.00.
(ii) Wages and salaries accrued at 28 February 2019 were K3,570.00.
(iii) Rent prepaid at 28 February 2019 was K2,415.00.
(iv) Van running costs owing at 28 February 2019 were K756.
(v) Allowance for irrecoverable debts to be increased by K955.50.
(vi) Provide for depreciation as follows: office furniture K3,990.00 delivery Van K13,125.00.

Required:

(a) Prepare the statement of profit or loss account for the year ended 28 February 2019 for DMC (8 marks)

(b) Prepare the statement of financial position as at 28 February 2019 for DMC (9 marks)

(c) Describe the following terms:

(i) Dishonoured cheque (1 mark)

(ii) Cheque Clearing system (2 marks)

[Total: 20 Marks]

QUESTION TWO

The following is a trial balance which has been incorrectly drawn up.

Trial balance at 31 December, 2019

	DR	CR
	K	K
Capital 1 January, 2019	39,225	
Drawings	97,500	
Inventory at 1 January, 2019		42,050
Trade receivables		172,585
Furniture and fittings	12,000	
Cash in hand	4,180	
Trade payables		34,450
Sales		637,550
Returns inwards		12,190
Discount received	7,095	
Business expenses	16,020	
Purchases	360,500	
	536,520	898,825

In additional to the mistakes evident above, the following errors were also discovered:

(1) A payment of K1,575 made to a creditor had not been posted from the cash book into the purchases ledger.
(2) A cheque for K 940 received from a customer had been correctly entered in the cash book but posted to the customer's account as K900.
(3) A purchase of fittings K2,035 had been included in the purchases account.
(4) The total of the discount allowed column in the cash book of K210 had not been posted into the general ledger. (*Note that personal accounts are used as part of the double entry system).*
(5) A page of the sales day book was correctly totalled as K 3,825 but carried forward as K3375. (*Note that personal accounts are used as part of the double entry system).*

Required:

(a) Give the Journal entries, without narratives, necessary to correct the above errors. (5 marks)

(b) Show the suspense account clearly showing the difference in books before the corrections in (a) above. (5 marks)

(c) Show the trial balance as it would appear after all the errors had been corrected. Show all your necessary adjustments. (10 marks)

[**Total: 20 Marks]**

QUESTION THREE

(a) On 31 January, 2019, Chanda's cash book showed that he had an overdraft of K1500 on his current account at the Bank. A bank statement as at end of January 2019 showed that Chanda was in credit with the bank by K325. On checking the cash book with the bank statement, you find the following:

(1) Cheques drawn, amounting to K2,500, had been entered in the cash book but had not been presented.
(2) Cheques received amounting to K2,000, had been entered in the cash book, but had not been credited by the bank.
(3) On instruction from Chanda, the bank had transferred interest from his deposit account amounting to K300 to the business current account, recording the transfer on 5 February, 2019. However, this amount had been credited in the cash book as on 31 January, 2019.
(4) Bank charges of K175 shown in the Bank Statement had not been entered in the cash book.
(5) The payments side of the cash book had been undercast by K50
(6) Dividends received amounting to K1000 had been paid direct to the bank and not entered in the cash book.
(7) A cheque for K250 drawn on deposit account had been shown in the cash book as drawn on the business current account.
(8) A cheque issued to Junza for K125 was replaced when out of date. It was entered again in the cash book, no other entry being made. Both cheques were included in the total of unpresented cheques shown in (1) above.

Required:

(a) Show the following:

(i) Updated cash book to show the current cash book balance (9 marks)

(ii) A statement reconciling the corrected cash book balance with that shown in the bank statement. (6 marks)

(b) Listed below are five (5) errors:

1. A business receives an invoice for K1,250 from a supplier which was omitted from the books entirely.
2. Repairs worth K750 were incorrectly debited to the non-current asset (plant) account instead of the repairs expenses account.
3. The bookkeeper of a business reduces cash sales by K1,400 because they were not sure what K1400 represented. In fact, it was a withdrawal on account of profit
4. Telephone expenses of K2,700 were incorrectly debited to the electricity account.
5. A page in the sales day book has been added up to K142, 125 instead of K144,125

Required:

Write out the journal entries which would correct these errors. Narrations are not required.

(5 marks)

[Total: 20 Marks]

QUESTION FOUR

Tabo Co has the following accounts for the year ended 31 March 2018. The company deals in service support worldwide

	2018	2017
	K	K
Revenue	26,114,400	28,137,600
Cost of sales	19,908,000	20,778,000
Gross profit	6,206,400	7,359,600
Current assets		
Inventories	512,400	936,000
Receivables note 1	4,546,800	5,176,800
Short term deposits and cash	2,462,400	1,740,000
	7,521,600	7,852,800
Current liabilities		
Loans and overdrafts	388,800	973,200
Tax on profits	813,600	920,400
Dividend	140,400	206,400
Payables (note 2)	5,846,400	5,606,400
	7,189,200	7,706,400
Net current assets	332,400	146,400

NOTES

1. Trade receivables	3,542,400	4,026,000
2. Trade payables	2,289,600	2,257,200

Required:

(a) Calculate liquidity and working capital ratios from the accounts of Tabo Company. (10 marks)

(b) Comment on the results of your calculation. (5 marks)

(c) Hector, Ireen and Jack have been in partnership for many years sharing profits and loss equally. No goodwill account has ever existed.
Jack is leaving the partnership. The other two partners are to take over his share of profits equally. Each partners capital before entering good will was K100,000. The goodwill is valued at K450,000.

Required:

Prepare the Goodwill Account for the partnership (5 marks)

[Total: 20 Marks]

QUESTION FIVE

The following relates to the incomplete records of kasumba, a sole trader as at 30 April 2018

	1 May 2017	30 April 2018
	K	K
Inventory	72,000	57,000
Trade payables	63,000	69,000
Insurance prepaid	12,000	-
Insurance owing	-	7,200
Trade receivables	120,000	90,000
Loan (10%)	360,000	360,000
Loan interest owing	-	36,000
Motor vehicle at cost	-	675,000

Other details

Bank summary

RECEIPTS

Balance as 1 May 2017	300,000	
Trade receivables	840,000	
Cash sales banked	246,000	
		1,386,000
PAYMENTS		
Accounts payables	540,000	
Insurance	60,000	
Purchase of motor vehicle	675,000	
Stationery	126,000	
Electricity	60,000	
Dishonored cheque (receivables)	42,000	
	(1,503,000)	(1,503,000)
Balance as at 30 April 2018		(117,000)

Cash account

RECEIPTS

Balance as at 1 May 2017	150,000	
Cash sales	396,000	
Account receivables	13,500	
	559,500	559,500

PAYMENTS

Drawings	120,000	
Rates	15,000	
Water bills	21,000	
Cash banked	246,000	
	402,000	402,000
Balance as at 31 May 2018		157,000

FURTHER INFORMATION

(i) Discount allowed and discount received were K3,600 and K5,100 respectively.

(ii) irrecoverable debts written off amounted to K9,300.

(iii) Sales returns records amounted to K30,000.

(iv) Good taken from the business for private use at cost were K7500. No entry had been made in the books accounts.

(v) Depreciation is charged at 20% on a straight line basis. A full year's depreciation is charged in the year of purchase and non in the year of disposal.

Required:

(a) Calculate the opening capital at 1 May 2017 (3 marks)

(b) Prepare the statement of profit or loss for the year ended 30 April 2018 (11 marks)

(c) Prepare the statement of financial position as at 30 April 2018 (6 marks)

[Total: 20 Marks]

END OF PAPER

SUGGESTED SOLUTION
SOLUTION ONE.
a) DMC statement of profit or loss for thee ended 28 February, 2019

	K	K
Sales		1,650,232.50
Less: cost of gods sold:		
Opening inventory	43,260.00	
Add: purchases	974,400.00	
	1,017,660.00	
Less: Closing inventory	(25,200.00)	
		992,460
Gross Profit		657,772.50
Add: Discount received		1680.00
		6,59,452.50
Less: Expenses:		
Wages and salaries (329,700.00 + 3,570.00)	333,270.00	
Rent (35,700.00 – 2,415.00)	33,285.00	
Discount allowed	8,610.00	
Van running costs (6,457.50 + 756.00)	7,213.50	
Bad debts	7,665.00	
Irrecoverable debts allowance	955.50	
Depreciation:		
Office furniture	3,990.00	
Delivery van	13,125.00	(408,114)
Net profit		251,338.50

(a) Statement of financial position as at 28 February, 2019

	K **Cost**	K **Dep'n**	K **NBV**
Non-current asset:			
Office furniture	30,450.00	3,990.00	26,460.00
Delivery van	39,375.00	13,125.00	26,250.00
			52,710.00
Current assets			
Inventory		25,200.00	
Accounts receivables	129,318.00		
Less: Irrecoverable debs	(5,208.00	124,110.00	
Prepaid expenses		2,415.00	
Cash at bank		43,050.00	
Cash in hand		3,402.00	198,177.00
			250,887.00
Less: Current liabilities			
Accounts payables		55,072.50	
Expenses owing (3,570 + 756)		4,326.00	

			59,398.50
Net assets			191,488.50
Financed by:			
Capital			
Balance at 01.03.2018			119,700.00
Add net profit			251,338.50
			371,038.50
Loss: Drawings			(179,550.00)
			191,488.50

(i) A cheque which the writers bank has refused to make payment upon.
(ii) A book containing forms (cheque) used to pay money out of a current account
(iii) The process by which amounts paid by cheque from an account in one bank are transferred to the account of the payee.

SOLUTON TWO

JOURNAL ENTRIES	K	K
(1) Trade payable	1,575	
Suspense		1,575
(2) Suspense	40	
Trade receivables		40
(3) Furniture and fittings	2,035	
Purchases		2,035
(4) Discount allowed	210	
Suspense		210
(5) Suspense	450	
Sales		450

(b) **SUSPENSE ACCOUNT**

(2) Trade Receivables	40	(1) Trade Payables	1,575
(3) sales	450	(2) Discount allowed	210
∴Different in books (bal.fig)	1,295		
	1,785		1,785

Q2 CONT'D

TRIAL BALANCE AT 3 DECEMBER, 2019

	K	K
Capital		39,225
Drawings	97,500	
Inventory	42,050	
Trade receivables (172,585 – 40)	172,545	
Furniture and fittings (12,000 + 2,035)	14,035	
Cash in hand	4,180	
Trade payables (34,450 – 1,575)		32,875
Sales (637,550 + 450)		638,000
Returns inward	12190	
Discount received		7,095
Business expenses	16,020	
Purchases (360,500 – 2,035)	358,465	
Discount allowed	210	
	717,195	717,195

SOLUTION THREE

A(1) **REVISED CASH BOOK**

	K		K
(6) Interest (300 x 2)	600	Balance b/f	1500
(7) Dividends	1000	(4) Bank charges	175
(8) Deposit	250	(5) Error of undercast	50
(9) Replaced cheque	125	Adjusted Balance c/d	250
	1975		1975

(ii) BANK RECONCILIATION STATEMENT

Adjusted Cash Book balance (i)		250
Add Back: Unpresented cheques (2,500 – 125)		2,375
		2,625
Less: outstanding lodgments	2,000	
Deposit interest not yet credited	300	(2,300)
Balance as Bank statement		325

(b) **JOURNAL ENTRIES**

(1) Purchase	1,250	
Trade Payables		1,250
(2) Repairs Expenses	750	
Plant (non current Asset		750
(3) Drawings	1,400	
Sales		1,400
(4) Telephone Expenses	2,700	
Electricity Expenses		2,700
(5) Trade receivables (144,125 – 142,125)	2,000	
Sales		2,000

SOLUTION FOUR

a. (i) Current ratio = $\frac{\text{current assets}}{\text{current liabilites}}$

2018 2017

$= \frac{7,521,600.00}{7,189,200.00}$ $= \frac{7,852,800.00}{7,706,400.00}$

= 1.05 = 1.02

(ii) Quick ratio = $\frac{\text{current asset –inventory}}{\text{current liabilities}}$

2018 2017

$= \frac{7,521,600.00 - 512,400.00}{7,189,200.00}$ $= \frac{7,852,800.00 - 936,000.00}{7,706,400.00}$

= 0.97 = 0.90

(iii) Account receivables collection period = $\frac{\text{receivable days}}{\text{sales days}} \text{ x } 365 \text{ days}$

= 2018 2017

$= \frac{3,542,400.00}{26,114,400.00} \text{ x } 365 \text{ days} =$ $\frac{4,026,000.00}{28,137,600.00} \text{ x } 365 \text{ days}$

= 49.5 days = 52.2 days

(iv) Inventory turnover period = $\frac{\text{inventory}}{\text{cost of sales}} \text{ x } 365 \text{ days}$

2018 2017

$= \frac{512,400.00}{19,908,000.00} \text{ x } 365 \text{ days} =$ $\frac{936,000.00}{20,778,000.00} \text{ x } 365 \text{ days}$

= 9.4 days = 16.4 days

(v) Account payables

Payment period = $\frac{\text{Trade payables}}{\text{cost of sales}} \text{ x } 365 \text{ days}$

= 2018 2017

$= \frac{2,289,600.00}{19,908,000.00} \text{ x } 365 \text{ days} =$ $\frac{2,257,200.00}{20,778,000.00} \text{ } 365 \text{ days}$

= 42 days = 40 days

(b)The company’s current ratio is a little lower than average but it’s quick ratio is better than average and very little less than the current ratio. This suggests that inventory levels are strictly controlled, which is reinforced by the low inventory turnover period. It would seem that working capital is tightly managed , to avoid the poor liquidity which could be caused by a long receivables collection and comparatively high payable.

(a) GOODWILL A/C

Goodwill A/c			
	K		K
Hector	150,000	B/f	450,000
Ireen	150,000		
Jack	150,000		
	450,000		**450,000**

SOLUTION FIVE

(a) Kasumba Opening Capital

	K
Bank	300,000.00
Cash	150,000.00
Inventory	72,000.00
Insurance prepaid	12,000.00
Receivables	120,000.00
	654,000.00
Payables	(63,000.00)
Loans	(360,000.00)
Capital at 1 may 2017	231,000.00

(b) Kasumba statement of profit or loss for the year ended 30 April, 2018

	K	K
Sales (w1)		1,220,400.00
Sales returns		(30,000.00)
Net sales		1,190,400.00
Opening inventory	72,000.00	
Add: Purchases (551,100-7,500)	543,600.00	
	615,000.00	
Less: Closing inventory	(57,000.00)	
Cost of sales		(558,000.00)
Gross profit		631,800.00
Add: discount received		5,100.00
		626,700.00
Less: expenses		
Irrecoverable debts	9,300.00	
Discount allowed	3,600.00	
Depreciation of MV (20% X 675,000.00)	135,000.00	
Insurance (w3)	79,200.00	
Rates	15,000.00	
Loan interest (10% x 360,000.00)	36,000.00	
Electricity	60,000.00	
Stationery	126,000.00	
Water bills	21,000.00	

Total expenses
(485,100.00)
Net profit
151,800.00

C. **Kasumba Statement of financial position as at 30 April 2018**

	Cost	Dep	N.B.V
Non-current asset:			
Motor vehicles	675,000.00	135,000.00	540.000.00
Current assets:			
Inventory		57,000.00	
Trade receivables		90,000.00	
Cash		157,500.00	
			304,500.00
Total asset			844,500.00
Equity and liabilities:			231,000.00
Capital			151,800.00
Add: net profit			(127,500.00)
Less: Drawing(120,000 + 7500)			255,300.00
Total equity			
			360,000.00
Non-current liabilities 10% loan			
Current liabilities:			
Trade payable		69,000.00	
Insurance		7,2000.00	
Loan Interest		36,000.00	
Bank overdraft		117,000.00	229,200.00
Total equity and liabilities			844,500.00

Workings:

Trade receivables control A/C

K		K	
Balance b/d	120,000.00	Cash	13,500.00
Dishonoured cheque	42,000.00	Discount allowed	3,600.00
Credit Sales (balance figure)	824,400.00	Bank	840,000.00
		irrecoverable debts	9,300.00
		Sales returns	30,000.00
		Balance c /d	90,000.00
	986,400.00		986,400.00

Total sales:	K
Cash sales	396,000.00
Credit sales	824,400.00
	1,220,400.00

2. Trade payables control A/C

	K		K
Bank	540.000.00	Balance b/d	63,000.00
Discount received	5,100.00	Purchase (bal figure)	551,100.00
Balance c/d	69,000.00		
	614,100.00		614,100.00

3. Insurance A/C

	K		K
Balance b/d	12,000.00	State of profit or loss	79,200.00
Bank	60,000.00		
Balance c/d	7,200.00		79,200.00
	79,200.00		

TAXATION PROGRAMME EXAMINATIONS

CERTIFICATE LEVEL

C4: DIRECT TAXES

TUESDAY 15 DECEMBER 2020

TOTAL MARKS – 100: TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question.

2. This question paper consists of FIVE (5) questions of twenty (20) marks each. You MUST attempt all the FIVE (5) questions.

3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. Cell Phones are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. All workings must be done in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

10. A taxation table is provided on pages 2, 3 and 4 of this paper.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table

Income Tax

Standard personal income tax rates

Income band	Taxable amount	Rate
K1 to K39,600	first K39,600	0%
K39,601 to 49,200	next K9,600	25%
K49,201 to K74,400	next K25,200	30%
Over K74,400		37.5%

Income from farming for individuals

K1 to K39,600	first K39,600	0%
Over K39,600		10%

Company Income Tax rates

On income from manufacturing and other	35%
On income from farming	10%
On income of Banks and other Financial Institutions	35%
On income from mineral processing	30%
On income from mining operations	30%

Mineral Royalty

Mineral Royalty on Copper

Range of Norm Price	Mineral Royalty Rate
Less than US$4,500	5.5% of norm value
From US$4,500 to less than US$6,000	6.5% of norm value
From US$6,000 to less than US$7,500	7.5% of norm value
From US$7,500 to less than US$9,000	8.5% of norm value
From US$9,000 and above	10% of norm value

Mineral Royalty on other minerals

Type of mineral	Mineral Royalty Rate
Base Metals (Other than Copper, Cobalt and Vanadium)	5% on norm value
Cobalt and Vanadium	8% of norm value
Energy and Industrial Minerals	5% on gross value
Gemstones	6% on gross value
Precious Metals	6% on norm value

Capital Allowances

Implements, plant and machinery and commercial vehicles:

Wear and Tear Allowance –	Plant used normally	25%
	Used in Manufacturing and Leasing	50%
	Used in farming and agro-processing	100%

Non- commercial vehicles

Wear and Tear Allowance	20%

Industrial Buildings:

Wear and Tear Allowance	5%
Initial Allowance	10%
Investment Allowance	10%

Low Cost Housing **(Cost up to K20,000)**

Wear and Tear Allowance	10%
Initial Allowance	10%

Commercial Buildings

Wear and Tear Allowance	2%

Farming Allowances

Development Allowance	10%
Farm Works Allowance	100%
Farm Improvement Allowance	100%

Presumptive Taxes

Turnover Tax 4%

Presumptive Tax for Transporters

Seating capacity	**Tax per annum**	**Tax per day**
	K	K
From 64 passengers and over	10,800	29.60
From 50 to 63 passengers	9,000	24.70
From 36 to 49 passengers	7,200	19.70
From 22 to 35 passengers	5,400	14.80
From 18 to 21 passengers	3,600	10
From 12 to 17 passengers	1,800	5.0
Less than 12 passengers and taxis	900	2.50

Property Transfer Tax

Rate of Tax on Realised Value of Land, Land and Buildings and shares	5%
Rate of Tax on Realised Value on a transfer or sale of a mining right	10%
Rate of Tax on Realised Value on a transfer of Intellectual Property	5%

Attempt ALL FIVE (5) questions.

QUESTION ONE

James Pailande was employed by Mapepo Limited on 1 April 2020 as Director Finance. His three (3) year contact provided for a basic salary of K180,000 per annum and a 30% gratuity of his cumulative annual basic salary. He was also entitled to the following allowances:

	K
Housing allowance per month	6,000
Education allowance per child per month	1,500
Electricity allowance per month	1,200
Lunch allowance per day	200

James Pailande has three (3) school going children at a private school in Lusaka. All his children are in their primary education. He works for five (5) days in a week and twenty (20) days in a month for the purposes of computing his lunch allowance.

During the weekends, James Pailande also does some consultancy work and other personal businesses. In the tax year 2020, he received the following investment income:

	K
Management and consultancy fees (net)	15,300
Interest from a Bank deposit Account (net)	24,000
Interest of Government Bonds (gross)	45,000

Deductions from his salary in charge year 2020 included the following:

(1) Pay as You Earn (PAYE) of K8,500.
(2) NAPSA contributions of 5% of his basic salary

Mr James Pailande incurred the following expenditure in the tax year 2020:

(1) As an Associate member of ZICA, he paid subscriptions of K15,000.
(2) Subscriptions to a squash club of K5,500
(3) He paid for medical expenses of K7,000, which the employer later refunded him during the year.

Mr James Pailande visited Cheshire Home on 28 September 2020 and made a donation of 20 blankets worth K10,000 and a cash gift of K3,000 on the same day. He did not receive any consideration for this donation.

Required:

(a) Calculate the income tax payable by James Pailande for the tax year 2020.

(11 marks)

(b) Explain the tax treatment of the following investment income received by an individual:

(i) Rental income (1 mark)

(ii) Dividends (1 mark)

(iii) Royalties (1 mark)

(c) State any six (6) documents required to operate Pay as You Earn (PAYE) system. (3 marks)

(d) Explain the tax implications of not paying PAYE on the due date. (3 marks)

[Total: 20 Marks]

QUESTION TWO

Mary and Monica are in partnership sharing profits and losses in the ratio 2:1. On 31 May 2020, Monica decided to retire from the partnership and on the same date Tumelo was admitted into the partnership. Before Tumelo joined, the partners were entitled to annual salaries of K45,000 each. However, the new partnership agreement provided that Tumelo would be entitled to an annual salary of K30,000, while Mary would continue to earn the same salary as in the previous agreement. The new profit and loss sharing ratio after the admission of Tumelo was 3:2.

The financial statements for the year ended 31 December 2020 showed a net profit of K126,000 after charging the following expenses:

(1) Depreciation at the rate of 25% on cost for each of the two (2) motor cars used by the partners in the partnership was charged during the year. The two (2) motor cars were purchased on 22 March 2019 costing K56,000 each. The motor cars are used for both private and business purposes. The Commissioner General provided a private use adjustment of 20% for each motor car.

(2) The motor car running expenses incurred during the year amounted to K94,000. The partners drove a total of 25,000 kilometres of which 5,000 kilometres related to private use.

(3) The general expenses incurred of K7,000 included K3,000 for telephone bills and K2,400 was donated to a political party, while the remainder of the expenses are all allowable for tax purposes.

(4) The partners took some goods from the business costing K3,400 for their private use without paying for them. The profit mark-up is 20%.

(5) The first born son to Mary works for the partnership on a full time basis. He earns an annual salary of K36,000. However, the other employee doing the same job as Mary's son earns an annual salary of K24,000.

(6) The repairs and renewals incurred during the year amounted to K6,500 of which K1,250 was for re-painting Tumelo's office and all other repairs are allowable for tax purposes.

(7) The charge for electricity is made up of as follows:

	K
Electricity for partners' houses	600
Administrative offices	400
	1,000

(8) All the partners were actively involved in running the partnership and the salaries for Mary and Tumelo of K6, 000 and K4,000 respectively were deducted from the gross profit.

Required:

(a) Calculate the partnership's tax adjusted business profit for the tax year ended 31 December 2020. (9 marks)

(b) Calculate the amount of business profits on which each partner will be assessed for the tax year ended 31 December 2020. (11 marks)

[Total: 20 Marks]

QUESTION THREE

Muntu Wandi recently retired from a Mining Company on the Copperbelt three (3) years ago and immediately set up a stationery business. He has always prepared financial statements to 31 December each year.

For the year ended 31 December 2020, the summarized statement of profit or loss was as follows:

	Notes	K	K
Gross profit			95,600
Less Expenses			
Professional fees	1	9,950	
Repairs and maintenance	2	20,500	
Entertainment expenses	3	5,000	
Motor car running costs	4	12,000	
Other operating expenses	5	3,300	
Depreciation		8,000	
Total expenses			(58,750)
Operating Profit			36,850
Royalties received	6		8,000
Profit on disposal			4,500
Net Profit			49,350

The following additional information has been provided

Note 1: Professional fees	K
Accountancy fees	3,500
Legal fees in connection with issue of share capital	5,500
Legal fees for recovery of bad debts relating to trade debts	200
Legal fees for recovery of loan relating to former employee	350
Legal fees in relation to penalty for non-compliance	400
	9,950

Note 2: **Repairs and maintenance**	
Construction of store room	15,200
Repair and Painting of the Shop	2,900
Other repairs and maintenance	2,400
	20,500

Note 3: Entertainment expenses	
Entertaining customers and suppliers	3,500
Staff Christmas party	1,500
	5,000

Note 4: Motor car running costs

Muntu Wandi uses the car for private purposes and partly for business. It has been agreed with the Commissioner-General that Muntu Wandi has 25% business use.

Note 5: Other Operating Expenses

This includes a donation of K1,000 to a named Political party, trade debts written off amounting to K1,100 and the balance relates to revenue allowable expenses.

Note 6: Royalties

The net amount of royalties received is shown, withholding tax has been deducted at source

Note 7: Profit on disposal

This relates to the profit earned after disposal of old furniture.

Note 8: Capital allowance

On 1 August 2020, Muntu Wandi bought a Canter truck at a cost K80,000 to be assisting with transportation of stationery to major customers. There were no other assets qualifying for capital allowances.

Required:

(a) Explain any five (5); the badges of trade. (10 marks)

(b) Calculate for Muntu Wandi the taxable business profit for the year ended 31 December 2020. (7 ½ marks)

(c) Calculate the income tax payable/refundable for tax year ending 31 December 2020. (2 ½ marks)

[Total: 20 Marks]

QUESTION FOUR

ABC Limited is engaged in manufacturing and construction. Amongst the products it manufactures are plastic bottles. It prepares its financial statements to 31 December each year. For the year ended 31 December, 2020, the company prepared the following statement of profit or loss as below:

		K	K
Gross Profit			1,250,000
Profit on sale of property (note 1)			35,000
Bank interest (note 2)			6,300
			1,291,300
Less Expenses			
Depreciation		95,000	
Donation	(Note 3)	15,200	
Audit fees		55,000	
Licenses, insurance and levies	(Note 4)	14,200	
Legal and professional fees	(Note 5)	6,800	
Rates		5,300	
Salaries and wages		75,050	
Consultation fees		55,000	

Entertainment	(Note 6)	25,100	
Office Expenses		95,000	
Fines and penalties	(Note 7)	9,200	
Loss on sale of motor vehicle		13,000	
Bad debts expenses	(Note 8)	8,200	
			(472,050)
Net profit			819,250

Notes:

Note 1: Profit on sale of property

A piece of land which was acquired five (5) years ago by the company at a cost of K25,000 was sold at an open market of K60,000

Note 2: Bank interest

The amount given is gross.

Note 3: Donations comprised

	K
Donation to an approved public benefit organisation	9,000
Donation to a political party	6,200
	15,200

Note 4: Licenses, insurance and levies

Insurance of company assets	7,800
City Council levies	1,026
Motor vehicle insurance	4,544
Renewal of licenses	830
	14,200

Note 5: Legal and professional fees

Collection of loans from former employees	3,048
Collection of trade debts	3,752
	6,800

Note 6: Entertainment

This relates to entertainment of employees.

Note 7: fines and Penalties

Penalties for late payment of PAYE	7,500
Traffic fines by company drivers	1,700
	9,200

Note 8: Bad debts expenses

Increase in specific provision for bad debts	2,300
Loan to former employees written off	5,500
Increase in general provision for bad debts	400
	8,200

Note 9: Implements, plant and machinery

The company bought the following assets during the year ended 31 December 2020:

Office computers	50,000
Manufacturing equipment	85,000
Toyota light Truck canter	75,000
Toyota Prado Car	105,000

There were no other assets qualifying for capital allowances.

Required:

(a) Calculate the Capital allowances claimable by ABC Limited for the tax year 2020. (5 marks)

(b) Calculate the adjusted business profit for the year ended 31 December 2020. (6 marks)

(c) Calculate the company income tax payable for the tax year 2020. (4 marks)

(d) State any five (5) properties on which property transfer tax (PTT) is charged. (5 marks)

[Total: 20 Marks]

QUESTION FIVE

The Zambia Revenue Authority (ZRA) has a huge responsibility to collect revenue on behalf of the government of the Republic of Zambia. One of the avenues of raising revenues is through levies and taxes.

Required:

(a) Describe the following taxes:

(i) Indirect taxes (2 marks)

(ii) Direct taxes (2 marks)

(iii) Regressive taxes (2 marks)

(iv) Progressive taxes (2 marks)

(v) Capital taxes (2 marks)

(vii) Revenue taxes (2 marks)

(b) One of the objectives of introducing presumptive tax in the transport business is to increase compliance and broaden the tax base by simplifying the tax process.

Required:

Explain any three (3) benefits of presumptive tax for transporters. (3 marks)

(c) Kandola was running a fleet of buses during the year ended 2020

(i) 16 seater bus for 250 days

(ii) 26 seater bus for 230 days

(iii) 50 seater bus for 265 days

(iv) 60 seater bus for 220 days

(v) 80 seater bus for 208 days

Required:

Calculate the presumptive tax payable by Kandola for the tax year 2020. (5 marks)

[Total: 20 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) **JAMES PAILANDE**

PERSONAL INCOME TAX COMPUTATION FOR THE TAX YEAR 2020

	K	K
Earned Income		
Basic salary (180,000 x 9/12)		135,000
Housing allowance (6,000 x 9)		54,000
Education allowance (1,500 x 9 x 3)		40,500
Electricity allowance (1,200 x 9)		10,800
Lunch allowance (200 x 20 x 9)		36,000
		276,300
Investment income		
Management and consultancy fees (15,300 x 100/85)		18,000
		294,300
Less: allowable deductions:		
Subscriptions to ZICA	15,000	
Donations to Cheshire Home (10,000 + 3,000)	13,000	
		(28,000)
		266,300
Less exempt income		(39,600)
Taxable income		226,700
Income tax:		
25% x 9,600		2,400
30% x 25,200		7,560
37.5% x 191,900		71,963
		81,923

Less:

PAYE	8,500	
WHT – M & C fees (18,000 x 15%)	2,700	
		(11,200)
Income tax payable		70,723

(b) (i) The treatment of the following investment income;

Rental income

Rental income received by an individual is taxed at the withholding tax rate of 10% and is a final tax. Therefore rental income is not included in the computation of the final income tax payable by an individual.

(ii) **Dividends**

Dividends receivable from Zambian companies are also subjected to withholding tax at the rate of 15%. The amount of withholding tax deducted at source is the final tax. Dividends are not included in the computation of the final income tax payable by an individual.

(iii) **Royalties**

The rate of withholding tax on royalties is 15%. The individual taxpayer who receives the royalties is still assessed on the gross amount. The amount of withholding tax deducted at source is given as a credit against the income tax charged on the total taxable income.

(c) Documents required to operate the PAYE system

- The employer's guide to PAYE
- Tax tables
- The tax deduction cards known as form ITF/P8
- Employee leaving forms known as form ITF/P13 (part 1)

- Details of old employment known as form ITF /P13 (part 11)
- Particulars of employee commencing employment known as form ITF/P20
- Certificate of pay and tax deducted known as form ITF/P22
- The Pay as you earn monthly returns
- ` Employer's annual declaration and certificate known as form CF/P18

(d) If the tax is not remitted by the due date, then a penalty of 5% per month or part thereof, of the outstanding tax is charged. Interest is also charged from the due date to the date of payment at the Bank of Zambia discount rate plus 2%.

SOLUTION TWO

(a) **COMPUTATION OF TAX ADJUSTED BUSINESS PROFIT FOR THE TAX YEAR 2020**

	K	K
Net profit per accounts		126,000
Add:		
Depreciation (56,000 x 25% x 2)	28,000	
Motor car expenses (5,000/25,000 x 94,000)	18,800	
Donation to political party	2,400	
Drawings (3,400 x 120/100)	4,080	
Salary (36,000 – 24,000)	12,000	
Electricity for partners' houses	600	
Salaries –Mary	6,000	
-Tumelo	4,000	
		75,880
		201,880
Less:		
Capital allowances:		
Motor cars (56,000 x 20% 2 x 80%)		(17,920)
Ta adjusted business profit		183,960

(b) **MARY, MONICA AND TUMELO**

DIVISION OF PARTNERSHIP PROFIT FOR THE TAX YAER 2020

	Total	Mary	Monica	Tumelo
	K	K	K	K
Period: 01.01.2020 – 31 .05. 2020				
Salaries (4,5000 x 5/12)	37,500	18,750	18,750	-
Balance shared (2:1)	39,150	26,100	13,050	-
Total	76,650	44,850	31,800	-

Period: 01.06.2020 – 31.12.2020

Salaries	43,750	26,250	-	17,500
Balance shared (3:2)	63,560	38,136	-	25,424
Total	107,310	64,386	-	42,924
Total profit	183,960	109,236	31,800	42,924

SOLUTION THREE

(a) Badges of trade are as follows:

- Subject matter of the realization

  Some assets are normally held as trading stock, while others are not. If the asset that has been sold is one which is normally held as trading stock, the presumption that a trade is conducted is high.

- Length of the period of ownership

  Trading stock is not normally held for a long period of time as a result, if a person disposes of an asset that he/she held for a long period of time, the presumption that trade is taking place is low.

- Frequency of similar transactions

  If the frequency of similar transactions is high, the chances of classifying a taxpayer as a trader are high.

- Supplementary work and marketing

  If an asset is acquired in a poor state and supplementary work is carried out to improve the asset by making it more marketable, then this asset when sold will give rise to trading profit.

- Circumstances giving rise realization

  A forced sale to raise cash for an emergency indicates that the transaction is not trading in nature as it is a one off transaction aimed at enabling a person to raise money, and not expected to recur.

- Intention

  Intention to trade clearly constitutes trading. However, intention to make a profit may not constitute trading. As such it has to be established as to whether a taxpayer sold an asset with the intention to trade.

(b) Muntu Wandi

Computation of taxable business profit for the year ended 31 December 2020

	K	K
Net profit		49,350

Add:		
Legal fees - share capital	5,500	
Legal fees - loan to former employee	350	
Legal fees - Penalty for non-compliance	400	
Construction of store room	15,200	
Entertaining customers and suppliers	3,500	
Motor car expenses (K12,000 X 75%)	9,000	
Donation to a Political Party	1,000	
Depreciation	8,000	
		42,950
		92,300
Less:		
Royalties	8,000	
Profit on disposal	4,500	
Capital allowance (K80,000 x 25%)	20,000	
(k15,200 x 2%)	304	
		(32,804)
Adjust business profit		59,496
Add Royalties (100/85 x K8,000)		9,412
Assessable income		68,908

(c) **Muntu Wandi income tax computation for the tax year 2020**

First K39,600@0%	0
Next K9,600@25%	2,400
Balance of k19,708 @ 30%	5,912
	8,312
Less WHT on Royalties (15% of K9,412)	(1,412)
Income tax payable	6,900

SOLUTION FOUR

(a) Computation of Capital allowances

Asset type		Capital allowance
		K
Office equipment	50,000 x 25%	12,500
Manufacturing equipment	85,000 x50%	42,500
Toyota light Truck	75,000 x 25%	18,750
Toyota Prado CAR	105,000 x 20%	21,000
Total		94,750

(b) ABC Limited

Adjusted business profit for the year ended 31 December 2020

	K	K
Net Profit		819,250
Add:		
Depreciation	95,000	
Loss on sale of motor vehicle	13,000	
Donation to a Political Party	6,200	
Collection of loans from former employees	3,048	
Penalties for late payment of PAYE	7,500	
Loan to former employees written off	5,500	
Increase in general provision for bad debts	400	
		130,648
		949,898
Less:		
Capital Allowances	94,750	
Profit on sale of property	35,000	
Bank interest	6,300	
		(136,050)

Tax adjusted business profit	<u>813,848 ½</u>

(c) <u>ABC Limited</u>

<u>Income Tax payable for the tax year 2020</u>

	K
Business profit	813,848
Add:	
Bank interest	<u>6,300</u>
Total taxable income	820,148
Income tax (K820,148 x 35%)	287,052
Less WHT on bank interest (K6,300 x 15%	<u>(945)</u>
Income tax payable	<u>286,107</u>

(d) Categories of properties on which PTT is charged

- Any land in Zambia (including any building on the land)
- Any building structure or other improvement thereon
- Any share issued by a company in Zambia that is not listed on the Lusaka Securities Exchange (LuSE)
- Any mining rights or an interest in a mining right
- Any transfer of intellectual property

SOLUTION FIVE

(a)

i. Indirect taxes
This is tax that is levied indirectly. It is imposed on expenditure and borne by the consumers, for example, value added tax and customs and excise duty.

ii. Direct Tax
This is tax levied directly on income and gains.
Normally a percentage of income is paid in the form of tax, for example PAYE, company income tax, and P TT.

iii. Regressive taxes
These are taxes that represent a small proportion of a person's income as the income of that person rises, the average rate of tax falls. VAT is a good of example of regressive because the rate of VAT is the same on the goods whether those goods are bought by a rich or poor person.

iv. Progressive taxes
These are taxes that represent a larger proportion of the person's income. As the person's income rises, the average rate of taxation rises. The rates off tax for lower income levels are less than the tax rates for higher income levels. income tax is a good example of progressive tax.

v. Capital taxes
These are taxes on capital receipts. A capital receipt is an amount of receipt resulting from a disposal of a capital item. An example of capital item is Property Transfer Tax (PTT).

vi. Revenue taxes
These are taxes levied on revenue receipts. A revenue receipt is a receipt arising from a sale of a non -capital item. An example of a revenue receipt is income tax.

(b) Benefits of presumptive taxes

- Simplified process

There is no requirement to file returns nor accounting and business records.

The taxes payable are predictable

- No need for Professional accountancy services
  Very little intellectual or professional effort is required when paying these taxes. Therefore, there is no need to engage an expert to file he returns or pay the tax.
- Cash flow friendly
  The amounts being paid on daily basis look small and do not disrupt the daily cash flow position.
- Equity
  All transporters pay equal amounts according to the sitting capacity of their vehicles.

(c) Presumptive tax paid

		K
i)	16 seaters (250 days x K5)	1,250
ii)	26 seater (230 days x K14.80)	3,404
iii)	50 seater (265 days x K24.70)	6,546
iv)	60 seater (220 days x K24.70)	5,434
v)	80 seater (208 days x 29.60)	6,157

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

CERTIFICATE LEVEL

C5: INDIRECT TAXES

THURSDAY 17 DECEMBER 2020

TOTAL MARKS – 100: TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use this time to carefully study the examination paper so that you understand what to do in each question.
2. This question paper consists of FIVE (5) questions of Twenty (20) marks each. You MUST attempt all the FIVE (5) questions.
3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere in your answer booklet.
4. Do **NOT** write in pencil (except for graphs and diagrams).
5. Cell Phones are **NOT** allowed in the Examination Room.
6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.
7. All workings must be done in the answer booklet.
8. Present legible and tidy work.
9. Graph paper (if required) is provided at the end of the answer booklet.
10. A taxation table is provided on page 2,3 and 4.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table for paper C5- Indirect Taxes (June and December 2020 Examinations)

Value Added Tax

Registration threshold	K800,000
Standard Value Added Tax Rate (on VAT exclusive turnover)	16%

Customs and Excise
Customs and Excise duties on used motor vehicles

	Aged 2 to 5 years		Aged over 5 years	
Motor vehicles for the transport of ten or more persons, including the driver	**Customs duty K**	**Excise duty K**	**Customs duty K**	**Excise duty K**
Sitting capacity of 10 but not exceeding 14 persons including the driver	17,778	22,223	8,889	11,112
Sitting capacity exceeding 14 but not exceeding 32 persons	38,924	0	13,840	0
Sitting capacity of 33 but not exceeding 44 persons	86,497	0	19,462	0
Sitting capacity exceeding 44 persons	108,121	0	43,248	0

	Aged 2 to 5 years		Aged over 5 years	
Motor cars and other motor vehicles principally designed for the transport of persons including station wagons and racing cars	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sedans				
cylinder capacity not exceeding 1000 cc	12,490	10,824	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	16,058	13,917	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	16,545	21,508	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	10,528	13,687
Cylinder capacity exceeding 3000 cc	22,561	29,329	12,032	15,642
Hatchbacks				
cylinder capacity not exceeding 1000 cc	10,705	9,278	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	14,274	12,371	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	15,041	19,553	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	16,545	21,508	10,523	13,687
Cylinder capacity exceeding 3000 cc	19,553	25,419	12,032	15,642
Station wagons				

cylinder capacity not exceeding 2500 cc	16,545	21,508	9,024	11,731
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	13,357	17,598
Cylinder capacity exceeding 3000 cc but not exceeding 2500 cc	22,561	29,329	18,049	23,463
SUVs				
Cylinder capacity not exceeding 2500 cc	21,057	27,374	9,024	11,732
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	24,065	31,284	13,357	17,598
Cylinder capacity exceeding 3000 cc	28,577	37,150	18,049	23,463
	Aged 2 to 5 years		**Aged over 5 years**	
Motor vehicles for the transport of goods –with compression-ignitioninternal combustion piston engine (diesel or semi-diesel):	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Single cab				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	21,926	9,501	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	26,311	11,402	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	30,697	13,302	17,541	7,601
Double cabs GVW exceeding 3 tonnes but not exceeding 5 tonnes	30,274	0	24,119	10,452
Double cabs GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes, **with spark ignition internal combustion piston engine**	30,697	13,302	24,119	10,452
Panel Vans				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	15,348	6,651	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	17,541	7,601	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	21,926	9,501	17,541	7,601
Trucks				
GVW up to 2 tonnes	21,926	9,501	10,963	4,751
GVW exceeding 2.0 tonnes but not exceeding 5.0 tonnes	28,504	12,352	13,156	5,701
GVW exceeding 5.0 tonnesbut not exceeding 10.0 tonnes	24,724	18,955	10,817	8,293
GVW exceeding 10.0 tonnesbut not exceeding 20.0 tonnes	30,905	23,694	11,744	9,004
GVW exceeding 20 tonnes	51,898	0	19,461	0
GVW exceeding 20 tonnes, **with spark ignition internal combustion piston engine**	37,086	28,432	13,907	10,662

Customs and excise duty on new vehicles

1	Motor cars and other motor vehicles (including station wagons) principally designed for the transport of less than ten persons, including the driver:	
	Customs duty:	30%
	Excise duty:	
	Cylinder capacity of 1500 cc and less	20%
	Cylinder capacity of more than 1500 cc	30%
2	Pick-ups and trucks/lorries with gross weight not exceeding 20 tonnes:	
	Customs duty	15%
	Excise duty	10%
3	Buses/coaches for the transport of more than ten persons	
	Customs duty:	15%
	Excise duty:	
	Seating capacity of 16 persons and less	25%
	Seating capacity of 16 persons and more	0%
4	Trucks/lorries with gross weight exceeding 20 tonnes	
	Customs duty:	15%
	Excise duty:	0%

The minimum amount of customs duty on motor vehicles is K6,000.

Import VAT is added to the sum of VDP, customs duty and excise duty. It is determined at the standard rate of 16%

Attempt all FIVE (5) Questions.

<u>QUESTION ONE</u>

(a) In relation to goods which are on sale or return agreements:

- (i) Explain the VAT implications of such goods. (3 marks)
- (ii) Explain the tax point of such goods. (3 marks)

(b) Explain the principle of estoppel in VAT cases. (2 marks)

(c) The customs services division of ZRA has a number of functions with regards importation of goods.

Required:

(i) Explain any four (4) functions of the customs division. (4 marks)

(ii) Explain any four (4) methods used to value imported goods. (4 marks)

(d) The Government of the Republic of Zambia is currently promoting the manufacture of goods locally. These goods are subjected to exercise duty.

Required:

Explain any four (4) methods used by the Zambia Revenue Authority (ZRA) to determine the Value for Duty Purpose for excise duty on goods manufactured in Zambia. (4 marks)

[Total: 20 Marks]

QUESTION TWO

(a) ZRA has instituted a Duty Drawback mechanism to make exports competitive on account of duties imposed in order to assist registered exporters in claiming duties paid on imported materials incorporated in goods which are later exported.

Required:

(i) Explain the main purpose of a DDB system. (2 mark)

(ii) State the documents required for exports to be zero rated. (2 marks)

(iii) Explain the challenges of the DDB system from both the exporter's and ZRA's point of view. (3 marks)

(b) The ZRA gives returning residents tax rebates when they come back to take residency in Zambia.

Required:

(i) Explain the conditions necessary for these returning residents to be granted the rebates. (3 marks)

(ii) Explain the types of goods that would apply. (3 marks)

(c) Explain seven (7) Preferential Trade Agreements (PTA) strategy. (7 marks)

[Total: 20 Marks]

QUESTION THREE

(a) Zunda Limited is a partially exempt taxable supplier. In the period ending 30 September 2020, the following details were obtained from its business records:

	K
Input tax on taxable supplies	44,800
Input tax on exempt supplies in the period	22,400
Non-attributable input tax	37,200
Standard rated supplies excluding VAT	400,000
Exempt supplies	60,000
Zero-rated supplies	40,000

Required:

(i) Explain what is meant by partial exempt supplier and how input tax is dealt with for such a supplier.
(3 marks)

(ii) Calculate the recoverable non-attributable input VAT deductible from the output tax for the period ended 30 September 2020. (5 marks)

(iii) Explain any four (4) expenses on which input VAT is not deductible. (4 marks)

(b) Explain any changes in business which may not render the cancellation of VAT registration. (3 marks)

(c) Explain the circumstances under which VAT registration can be cancelled. (5 marks)

[Total: 20 Marks]

QUESTION FOUR

Gabriel Patel is a recent university graduate who has been engaged as a Management Trainee in a commercial bank based in Lusaka. He was granted a loan to import a six (6) years old Sedan saloon car from Japan to ease up his movements to and from work.

The car imported was a Toyota Allion saloon car with a cylinder capacity of 2500cc.

The purchase price of the car was $4,500, freight charges amounted to $405 and insurance costs were $360. Transport charges from Dar-el- salaam to Nakonde were $750, Gabriel incurred incidental costs of $190 up to Nakonde border post and he paid K1,900 to transport the car from Nakonde to Lusaka

The Bank of Zambia Exchange rate was K14.75 per US$1 which the Commissioner General approved. Exchange rate quoted by other financial institutions was K15.05 per US$1.

Required:

(a) Explain the documents Gabriel Patel requires to submit to the customs officers when importing the vehicle. (5 marks)

(b) Calculate the imported taxes paid by Gabriel Patel. (10 marks)

(c) Explain any five (5) powers of ZRA customs officials. (5 marks)

[Total: 20 Marks]

QUESTION FIVE

Limbikani Limited started trading in 2017 and its turnover had consistently fallen below the VAT registration threshold in the first two (2) years. However, in the year 2020, the Company was registered under voluntary registration. The following results were recorded for the month of September 2020:

		K
Sales		69,750
Cost of sales		(30,750)
Gross profit		39,000
Less Expenses:		
Depreciation	2,200	
Bad debts written off	6,500	
Overheads	10,600	
Other expenses	7,400	
		(26,700)
Net profit		12,300

The following additional information is available:

1. Exempt supplies taken as a proportion of total sales amounted to 10% and Zero rated sales were K6,250. The remainder of the sales are all standard rated for VAT.

2. The company also sold goods to customers who were not registered for VAT purposes comprising 20% of total sales.

3. The purchases are 50% of sales. Included in purchases were exempt supplies valued at K7,500. The remainder of the purchases is all standard rated for Value Added Tax purposes.

4. Half of the standard rated purchases were from non-value Added Tax registered suppliers.

5. The bad debts were written off on 30 September 2020. The figure consists of two invoices of K3,250 each in respect of which payment was due on 1 March 2018 and 30 June 2019.

6. The overheads are all standard rated supplies for the purposes of Value Added Tax.

7. The figure for other expenses is inclusive of Value Added Tax and is made up of:

	K
Entertaining suppliers	1,320
Petrol	2,230
Diesel	3,850
	7,400

Unless stated otherwise, all the above figures are VAT exclusive.

Required:

(a) Calculate the amount of VAT payable or repayable for the month of September 2020. (13 marks)

(b) State the due date when the VAT for the month of September 2020 is payable. (2 marks)

(c) Explain any five (5) obligations of a VAT registered trader. (5 marks)

[Total: 20 Marks]

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) Sale or return agreements:

(i) The VAT implications are as follows:

1. Goods are not sold.
2. The seller owns the goods.
3. The customer has unqualified right to return the goods at any time.

(ii) The tax point is the earliest of:

1. The date of adaptation of the goods
2. The date of payment or
3. The date of invoicing

(b) Principle of estoppel

It is an impediment which prevents a party from asserting a fact. For example, a dispute about amount owed or a case where VAT refund claim is being made.

(c) Customs Services Division

(i) Four functions of the customs divisions are:

1. Collection of management of customs duties
2. Regulation and control of imports and exports
3. Facilitation of trade, travel and movement of goods
4. Providing statistical data to the government on imports and exports.

(ii) Methods used to value imported goods are:

1. Transaction value: This is based on the price actually paid or payable including insurance, freight and other incidental costs to the extent that they are paid.
2. Deductive value: This is the price at which identical or similar goods are sold in their quantity in Zambia.
3. Computed value: This is the price based on cost of production, insurance, freight and other costs incurred in the delivery of goods to Zambia.
4. Residual basis of value/fall back method: This is the price arrived at by going through the above methods flexibly.
5. Transaction value of identical goods: This is the price of identical goods imported by another importer into Zambia from the same source, including insurance, freight and other incidental costs.
6. Transaction value of similar goods: This is the price of similar goods imported by another importer into Zambia from the same source, including insurance freight and other incidental costs.

(d) The following are the methods:

1. The price at which a licensed manufacturer of excitable goods offers the goods for sale on the open market
2. The lowest price at which identical goods in the same quantity
3. The lowest price at which identical goods in different quantities are sold within Zambia by another licensed manufacturer in the open market
4. The lowest price at which similar goods in the same quantity or almost the same quantities are sold within Zambia by another licensed manufacturer in the open market
5. The lowest price at which similar goods in different quantities are sold within Zambia by another licensed manufacturer in the open market
6. The price at which the goods would fetch less profit and other costs beyond the manufacturing level

SOLUTION TWO

(a) Duty Draw Back System

(i) DDB system is an export support program introduced by the Government of the Republic of Zambia to enable local manufacturers to claim any taxes incurred either directly or indirectly on any goods produced for export. The main purpose of this system is to avoid double taxation.

(ii) The following are the documents:

1. Commercial invoices
2. Certified copies of the documents presented to Zambian customs at exportation
3. Certified copies of customs import at the country of destination
4. Proof of payment

(iii) The following are the challenges:

1. The drawback system is demanding on the part of the exporter who must keep detailed records to support every claim for drawback from ZRA.
2. The system takes long for the drawback claim to be processed. This means that the system should be reviewed in order to ensure that it can work smoothly and the refunds processed within the reasonable time.
3. The other challenge is integrity and commitment of staff at the ZRA DD unit as well as the integrity of the data used to calculate the duty drawback coefficients.

(b) Tax rebates of returning residents

(i) Conditions to be met:

1 The person claiming the rebate has been resident outside Zambia for a period of not less than two (2) years before the date of arrival in or returns to Zambia.

2 The effects were the property of that person before the date of departure for Zambia from the previous country of residence.

3 The effects must be imported at the time of arrival in Zambia or within six (6) months from the date of arrival of that person.

(1 mark per valid point up to 3 marks)

(ii) the following are goods that are allowed:

1 All personal effects

2 All household effects

3 One motor vehicle per family

(c) The following are the PTA strategies:

1. Reduction and elimination of trade barriers on selected goods traded within the area
2. Cooperation in customs through simplification and hamonisation of customs procedures and regulations

3. Introduction of rules of origin to determine which goods will receive preferential treatment
4. Granting of transit rights to all transporters when coming from or entering other Member States or third parties
5. Clearing and payments arrangements to promote trade in goods and services within the sub region
6. Cooperation to develop coordinated and complementary policies and systems in transport and communications
7. Cooperation in the field of industrial development in order to promote self-sustained industrialization within the PTA to expand trade industrial products and to bring about structural transformation of industry.
8. Cooperation in the area of agricultural development so as to raise production and supply of food to coordinate the export of agricultural commodities to harmonise programmes in agricultural production.
9. Simplification and harmonization of trade documents and procedures in the area.
10. Interventions to assist the least industrialised Member States such as special consideration in allocating multinational industries.

SOLUTION THREE

(a) Partial exemption

(i) A partial exempt supplier is a supplier making both taxable and exempt supplies.

Input tax incurred on purchases and expenses are reclaimable as input tax.

However, input tax on purchases used to make exempt supplies is not. The partially exempt supplier has to arrive at the input tax on the purchases and expenses that correspond to the proportion of their sales that are taxable which he can reclaim.
Therefore, the right to reclaim input tax is restricted to the input tax corresponding to taxable supplies made.

(ii) Recoverable input VAT

Taxable supplies:	K
Standard rated supplies	400,000
Zero rated supplies	40,000
Taxable supplies	440,000
Total supplies (440,000 + 60,000)	500,000

Proportion claimable = $\frac{\text{Taxable supplies}}{\text{Total supplies}} \times 100$

K440,000/K500,000 x 100 = 88%

Amount claimable = K37,200 x 88% = K32,736

(iii) Input tax is not deductible on the following expenses:

1. Input VAT incurred on the purchase of motor cars, unless if the motor cars are bought for resale, or car hire business, or driving school
2. Input VAT incurred on petrol
3. Input VAT incurred on business entertainments
4. Input VAT incurred on expenses incurred for domestic accommodation of directors
5. Input VAT incurred on telephone and internet services
6. Input VAT incurred on diesel is restricted to 90% to be recovered
   (1 mark per valid point up to 4 marks)

(b) Changes not requiring the cancellation of VAT registration

1. A change in the trading name of the business, the name of the business or an address of any partner of the business.
2. A change in the business address of the principal place at which the business is carried on.
3. Transfer of a business as a going concern.

(c) The following are the circumstances:

1. If there is a change in the legal status of an entity, such as where a partnership is dissolved.
2. The business ceases to trade permanently
3. The business is sold
4. The intention to make taxable supplies by an intended trader ceases
5. The value of taxable supplies falls consistently below the VAT registration threshold.
6. The business has been granted registration in anticipation of commencing a business on a certain date, but does not carry out any business on or before the due date.

SOLUTION FOUR

(a) Documents required to be declared when importing the motor vehicle

1. invoice showing the purchase price
2. bill of lading
3. insurance certificate
4. freight statement
5. Contract of sale
6. Manifest or consignment notes

(1 mark per valid point up to 5 marks)

(b) Import taxes

	US$
Purchase price	4,500
Freight charges	405
Insurance costs	360
Transport costs	750
Incidental costs	190
Total	6,205
VDP in K (US$6, 205 X 14.75)	91,524

	Value Of the vehicle K	Taxes Import taxes K
Value for duty purposes	91, 524	
Customs duty	8,423	8,423
	99,947	
Excise duty	10,950	10,950
	110,897	
Import VAT@ 16%	17,744	17, 744
Surtax	2,000	2,000
Total value of the vehicle	130,641	
Total taxes paid		39,117

(c) The powers of the ZRA Customs officials.

1. Powers to stop and search any person, including any person within or upon any ship, aircraft, or vehicle, whom he has good reason to suspect of having secreted about him or in his possession any dutable goods.

2. Powers to enter any shop, office, store, structure or enclosed area for making such examination and enquiry, as he considers necessary.

3. Demand for any book, document or thing which is required under the Act.

4. Examine and make extracts from and copies of such books and documents

5. Take with him onto such premises an Assistant who may be a Police

TAXATION PROGRAMME EXAMINATIONS

CERTIFICATE LEVEL

C6: LAW FOR TAX PRACTITIONERS

FRIDAY 18 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question. You will be told when to start writing.

2. This question paper consists of FIVE (5) questions of twenty (20) marks each. You MUST attempt all the FIVE (5) questions.

3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. **Cell Phones** are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. All workings must be done in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Attempt all FIVE (5) questions.

QUESTION ONE

Mr. Muzo is desirous of acquiring new stock for his new farm in Kapiri. He travelled to the district council where he found goods displayed on various shops for sale. The first shop had a plough he really needed for his farm; it had a tag ***"Special offer, ZMW 3, 400.0 non-negotiable, offer valid till 18:00 hrs".*** He told the shop attendant that he wanted the plough and it must be removed off shelf as he was going to the bank to withdraw money and pay for it. The shop attendant smiled at him and said nothing. Muzo took it that it was done deal and left the shop. In the next shop, Muzo found a multi-purpose harvesting machine with a tag "**ZMW 6, 500.00 cash only"** Muzo quickly signed a cheque as he feared someone could easily purchase it. He left the cheque on the counter in full view of the security guard as the shop owner had stepped out, he notified the guard that the machine was his as he had fully paid for it and the shop owner must be notified as such, and left the shop. Muzo proceeded to the bank to withdraw money and found long queues necessitated by load shedding. He was served last and by this time he found all shops closed. He went back to the shops the following morning and found the plough and the harvester sold. He is agitated by this development as he feels the shop owners are in breach of contract and this will affect his farming season. He hears that you are a good contract lawyer and approaches you.

Required:

(a) With reference to the above scenario, advise Muzo on the legal issues at hand and weigh his chances of success on the two (2) issues at hand. (10 marks)

(b) Distinguish an offer from an invitation to treat (6 marks)

(c) List and briefly explain any four (4) types of torts. (4 marks)

[Total: 20 Marks]

QUESTION TWO

(a) Explain to them the difference between a company and a partnership. (11 marks)

(b) List four (4) implied duties of an employer. (4 marks)

(c) State the five (5) functions of the Pension and Insurance Authority Board. (5 marks)

[Total: 20 Marks]

QUESTION THREE

(a) Write brief notes on:

(i) Hire Purchase (4 marks)

(ii) Annual General Meeting (4 marks)

(iii) Duty of obedience (2 marks)

(b) Outline the priority of preferential payments of *all unsecured debts* of a company under bankruptcy. (5 marks)

(c) State the sources of law in Zambia (5 marks)

[Total: 20 Marks]

QUESTION FOUR

(a) With regard to negotiable instruments, explain the requirements for negotiability. (10 marks)

(b) Explain the main purpose of the objects clause in Company law. (2 marks)

(c) Explain briefly agency by estoppel. (3 marks)

(d) List all the requirements needed for a contract of sale to subsist as provided for under the Sale of Goods Act, 1893. (5 marks)

[Total: 20 Marks]

QUESTION FIVE

Mulenga and Habwangabwanga are very good friends based in Mufulira. They invest almost in the same type of businesses, plan together and simply do everything together. Two years ago they decided to venture in high quality beef animals (cattle) each one buying about 100 animals. The animals graze together and are usually vaccinated at the same time. There has been an outbreak of corridor disease commonly known as '*denkete*' which has led to a number of animals dying. To avoid a total loss, Mulenga decided to insure all his animals including 10 animals for his closest friend Habwangabwanga under livestock insurance with ZSIC Insurance Company. The purpose of the insurance policy was to provide compensation for any animals that died due to corridor disease. A day after insuring his animals, Mulenga sold 4 of them to Mrs. Tailashi who paid immediately, and as soon as Tailashi reached her place, one of the animals died. The same day, 2 animals (bulls) belonging to Habwangabwanga which were among those Mulenga had insured in his name died.

Required:

(a) With reference to the scenario above and giving practical examples, explain who would claim from the insurance company, if any, for the 2 animals (bulls) which died. (6 marks)

(b) Explain if Tailashi would succeed in claiming the compensation from the insurance company for the one (1) animal which died. (5 marks)

(c) Explain the following maxims of equity:

(i) Equity follows the law (3 marks)

(ii) He who comes to equity must come with clean hands (3 marks)

(iii) Equity looks on that as done which ought be done (3 marks)

[**Total: 20 Marks**]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) The main issue to be addressed here is whether a contract was concluded in both instances. In the first instance, the displayed goods amounted to an invitation to treat as discussed in **Fisher v. Bell** and the action taken by Muzo never amounted to an offer and the shop owner was not bound at all. The offer was only valid till 18hrs of the same day and for Muzo to return the following day meant that the offer had lapsed and as such he cannot succeed in this case even if he was to sue. No consideration was paid by Muzo. In the second incident, the tag was clear, consideration was to be by cash only. Muzo signed a cheque and this amounted to counter offer as was seen in the case of **Hyde v Wrench**. For a contract to stand , acceptance must mirror the terms of the contract in totality. In both incidents , there was no contract formed between Muzo and the shop owners and as such Muzo cannot succeed even if he was to sue.

(b)

(c) An offer and invitation to offer are two different terms, which must not be confused with one another. An **offer** is a proposal while an **invitation to offer (treat)** is inviting someone to make a proposal. In an offer, there is an intention to enter into a contract, of the party, making it and thus it is certain. On the other hand, an invitation to offer is an act which leads to the offer, which is made with an aim of inducing or negotiating the terms. So, in an invitation to offer, the offeror, does not make an offer, rather invites other parties to make an offer. Hence, before simply responding to an offer, one must know the difference between offer and invitation to offer, because that makes a difference in the rights of parties.

(d)

- Trespass
- Negligence
- Occupier's liability

- Strict liability
- Defamation
- Nuisance
- Assault
- Battery

Any 4 of the above or correct tort not mentioned above

SOLUTION TWO

a) The following are differences between a Company incorporated and a Partnership;

1. In a company, property belongs to the company whereas in a partnership, it belongs to individuals.
2. Creditors in a company can only levy execution of court order on the company and not on its members. In a partnership, creditors of a firm are also creditors of the partners and can levy execution of a court judgement on the property of each partner.
3. Members of a company cannot dispose of company assets or even incur liabilities on behalf of the company whereas, a partner can dispose of a partnership property and incur liability on behalf of the firm.

4. A member can contract with the company while a partner cannot contract with the firm.

5. Company restrictions on member's authority are effective as against third parties while partnership restrictions on partner's authority contained in the partnership agreement are of no avail to third parties.

b) The following are the employer's implied duties;

1. Duty to provide work
2. Duty to pay wages.
3. A duty to provide a grievance procedure
4. A duty of mutual trust and confidence

c) The following are the duties of pensions and Insurance Authority Board;

1. Administer and manage the fidelity fund.
2. Formulate and enforce standards.
3. Monitor the solvency of insurers.
4. Monitor premium rates.
5. Encourage competition.

SOLUTION THREE

(a) The solution is as follows:

(i) *Hire Purchase:-* This is a form of buying goods on credit whereby the hirer (buyer) obtains immediate use of the goods on hire but does not become the true owner until all instalments are paid in full. if the buyer (hirer) defaults payment, he loses the already paid instalments and the seller repossesses the goods. There is an option of buying the goods at the end of the hire contract. Maintenance of the asset is usually done by the seller (hiree).

(ii) An Annual General Meeting is provided for an incorporated public company which ought to hold it three months after the end of each financial year. It must be noted that failure to hold an annual general meeting by the company would amount to an offence and the company will be fined. This is not the position with private limited companies which can dispense with the holding of the said meeting.

(iii) Duty of obedience

This is the duty of an agent or an employee to carry out the wishes of the principal or the employer as per the agreement. The instructions here must be legal though for this duty to apply.

(b) The preferential payments of all unsecured debts in a bankruptcy is as follows:

1. **First** – Costs and expenses of the winding up including taxes and which shall include the remuneration of the liquidator and costs of any audit carried out.

2. **Secondly** – Preferential debts, that is all amounts due to:

    (i) Wages or salaries earned by way of commission;

    (ii) Accrued leave to employees;

(iii) Accrued paid absence leave;

(iv) Recruitment expenses reimbursable under a contract of employment;

(v) Three months' salary or wages as severance pay to employees.

(vi) Amounts due in respect of workers' compensation and pension contributions.

3. **Thirdly** – Any tax, duty or rates payable in respect of the period prior to the commencement of the winding up but which have become due after that date and all arrears of government rents.

4. **Fourthly** – All rates due to the local authority that are due within the period of three years prior to the start of the winding up.

5. **Fifthly** – Any surplus (if any) would be used for deferred debts, that is, dividends declared but not paid and interest accrued on debts since liquidation.

(C)

1. The Constitution
2. Acts of Parliament
3. Delegated legislation
4. Customary law
5. Law applying to Zambia as prescribed

SOLUTION FOUR

a) The concept of negotiability is one of the most important features of commercial paper, a contract for the payment of money. A negotiable instrument is a written document, signed by the maker or drawer that contains an unconditional promise to pay a certain sum of money on delivery or at a definite time to the bearer. It is essentially a piece of paper that can be transferred multiple times from one person or entity to another without the use of actual cash. A check that can be endorsed multiple times by different parties is an example of a negotiable instrument. Each time the check is endorsed and given to another, it represents payment to that party. Because of this feature, negotiable instruments are highly trusted and are used daily by millions of people.

When dealing with negotiable instruments, below are eight requirements to keep in mind:

- Must be in writing- The writing can be on anything that is readily transferable and that has a degree of permanence.

- Must be signed by the maker or drawer-The signature can be anyplace on the instrument-It can be in any form (such as word, mark or rubber stamp) that purports to be a signature and authenticates the writing. • It can be signed in a representative capacity.

- Must be a definite order or promise to pay- A promise must be more than a mere acknowledgement of a debt. - The words "I/We Promise" or "Pay" meet this criterion.

- Must be unconditional- Payment cannot be expressly conditional upon the occurrence of an event- Payment cannot be made subject to or governed by another agreement. • Payment cannot be paid out of a particular fund (except for a government issued instrument).

- Must be an order or promise to pay a sum certain-An instrument may state a sum certain even if payable in installments, with interest, at a stated discount or at an exchange rate.

- Must be payable in money- Any medium of exchange recognized as the currency of a government is money.

• The maker or drawer cannot retain the option to pay the instrument in money or something else.

- Must be payable on demand or at a definite time-Any instrument payable on sight, presentation or issue is a demand instrument. An instrument is payable at a definite time even though it is payable on a stated date, or within a fixed period after sight, or the drawer or maker has an option to extend time for a definite period. • Acceleration clauses, even if unenforceable, do not affect the negotiability of the instrument.

- Must be payable to order or bearer-An order instrument must name the payee with reasonable certainty. An instrument whose terms intend payment to no particular person is payable to bearer.

b) An objects clause is a provision in a company's constitution stating the purpose and range of activities for which the company is carried on. In Zambian company law, an objects clause circumscribed the capacity, or power, of a company to act.

c) Agency by estoppel means that a defendant will be liable to a plaintiff because the defendant's action caused the plaintiff to reasonably rely on there being an agency relationship between the defendant and someone who purported to act on behalf of the defendant. The defendant will be estopped from denying that that the third party is its agent.

d) Section 2 (1) provides for the requirement as;

- There has to be buyer and seller with full capacity to contract

- There has to be transfer or agreement to transfer property
- Intention to be bound
- There has to be money consideration called price
- There has to be goods.

SOLUTION FIVE

(a) No one would claim because Mulenga never had any insurable interest to insure them in his own name, then Habwangabwanga is not known as the owner of the animals, thus could not claim. The claim would fail as the principle of utmost good faith, ***Banque Financier de la Cite v West Gate Insurance Co. Ltd (1991)*** requiring full disclosure was not done, and secondly Mulenga has no insurable interest ***Macaura v. Northern Assurance Co. Ltd (1925),*** he would not suffer any financial loss personally upon the death of the animals.

(b) Tailashi would not qualify to claim to claim under insurance as he has no insurable interest, the property was sold, payments were done so the property/risk in the sold animals is with the buyer, and cannot claim under insurance. Mulenga's insurable interest ceased upon sale, the buyer must insure the animals he bought in his own name.

(c) The equity maxims (principles) are explained below:

(i) *Equity follows the law* – means that equity will not permit the law a statute to be used as an instrument of fraud. Where the equities are equal, the law prevails, equity will not go against the law in providing its remedies.

(ii) *He who comes to equity must come with clean hands* – means that the past conduct of the party in a dispute must be good for such a one to win a case at equity. He/she must not have been the one in the wrong and then try to seek help from the law.

(iii) *Equity looks on that as done which ought to be done* – means that the court through equity will compel the party to a contract who has not yet done her/his part on a contract to do it as agreed. That is, the court may order specific performance.

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D1: BUSINESS INFORMATION MANAGEMENT

WEDNESDAY 16 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question.

2. This question paper consists of **FOUR (4)** questions of Twenty Five (25) marks each. You must attempt all the **FOUR (4)** questions.

3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. **Cell Phones** are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. All workings must be done in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Answer all FOUR (4) questions.

QUESTION ONE

(a) Zambia Revenue Authority wishes to automate some of their operations to handle domestic taxes by developing an information system called '***electronic tax online***'. This system is expected to be used by the Zambia Revenue Authority employees, organizations and individuals.

Required:

List four any (4) requirements elicitation techniques that can be adopted by Zambia Revenue Authority to investigate requirements for this information system.

(4 marks)

(b) A new Information System can be implemented in an organization using four (4) main conversion strategies namely: the *parallel strategy*, the *direct cutover strategy*, the *pilot study strategy*, and the *phased approach strategy*.

Required:

Explain each of these strategies clearly outlining the impact on the organization's operations and costs. (12 marks)

(c) A computer network is made up of a number of connected computing devices to provide the user to access the different resources.

Required:

Briefly explain the following:

(i) Virtual Private Network (3 marks)

(ii) Internet Service Provider (3 marks)

(iii) Client/Server network (3 marks)

[Total: 25 Marks]

QUESTION TWO

(a) There are different types of Computer Based Information Systems that are used in an organization.

Required:

Briefly explain how each of the following information systems supports knowledge workers in the execution of their duties.

(i) Office automation systems. (2 marks)

(ii) Business intelligence systems (2 marks)

(iii) Expert systems. (2 marks)

(iv) Dashboards. (2 marks)

(b) Online businesses have grown in number. So many different activities bordering on sales of goods and services are happening online. Companies have been using computer networks to exchange information about ordering, invoicing and delivering them to customers.

Required:

Outline any five (5) benefits of using *e-commerce* in business operations. (10 marks)

(c) Knowledge management and collaboration systems are among the fastest growing areas of corporate and government software investment. Therefore, these systems play a key role in an organization.

Required:

State four (4) major steps/activities that make up a knowledge system cycle. (4 marks)

(d) Mention three (3) post implementation activities that follow a successful implementation of an information system in an organization. (3 marks)

[Total: 25 Marks]

QUESTION THREE

(a) Use of ICTs in management of data and channels of communication has made it easy to run business and also helped cut certain costs in businesses. EDI is a form of computer to computer data interchange e.g. sending accounting documents electronically to the customers. This clearly offers substantial saving and benefits to organizations that use it.

Required:

Clearly elaborate the cost reduction effects expected from the implementation of *Electronic Data Interchange* (EDI) in business organisations. (10 marks)

(b) Aligning Business Strategy and Information System strategy is critical to the success of any business organisation in this technology era. The organisation must account for the costs incurred providing and maintaining IS. The IS changing system must encourage the efficient use of IS/IT resources.

Required:

Explain the relationship between Business strategy and IS/IT strategy. (6 marks)

(c) The development of systems was not properly planned in the past. The consequences were often poor designed systems, which costs too much to meet the user's needs.

Required:

Outline in detail any three (3) principles of good software development practice. (9 marks)

[Total: 25 Marks]

<u>QUESTION FOUR</u>

(a) A system must be thoroughly tested before implementation. A system that is not tested may operate with bugs or errors that may cause disruption or disturbance with work and prove to be costly.

Required:

List the types of Information System testing (4 marks)

(b) AIS combine the study and practices of accounting with the design, implementation and monitoring of information systems. Such systems use modern IT resources together with traditional accounting controls and methods to provide users the financial information to be used by accountants in business organizations.

Required:

Briefly describe the five (5) main components of an AIS. (10 marks)

(c) Artificial Intelligence works by creating knowledge base that consists of facts, concepts and the relationship between the computer and the user; using pattern matching techniques to solve problems.

Required:

Mention any five (5) applications of artificial intelligence technology in information systems. (5 marks)

(d) Management Information Systems are computer-based or manual systems that convert data from mainly internal sources into information that can be used to support decision making. This information enables managers to make timely and effective decisions for planning, directing and controlling the activities.

Required:

Describe the use of OAS and KWS in an organisation (6 marks)

[Total: 25 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

QUESTION ONE

a) Answers can be drawn from any of the following; Observation, questionnaires, interviews, joint application development, document analysis

b) In a **parallel strategy**, both the old system and its potential replacement are run together for a time until everyone is assured that the new one functions correctly. This is the safest conversion approach because, in the event of errors or processing disruptions, the old system can still be used as a backup. However, this approach is very expensive, and additional staff or resources may be required to run the extra system.

The ***direct cutover strategy*** replaces the old system entirely with the new system on an appointed day. It is a very risky approach that can potentially be more costly than running two systems in parallel if serious problems with the new system are found. There is no other system to fall back on. Dislocations, disruptions, and the cost of corrections may be enormous.

The ***pilot study strategy*** introduces the new system to only a limited area of the organization, such as a single department or operating unit. When this pilot version is complete and working smoothly, it is installed throughout the rest of the organization, either simultaneously or in stages.
(3 marks)

The ***phased approach strategy*** introduces the new system in stages, either by functions or by organizational units. If, for example, the system is introduced by function, a new payroll system might begin with hourly workers who are paid weekly, followed six months later by adding salaried employees (who are paid monthly) to the system. If the system is introduced by organizational unit, corporate headquarters might be converted first, followed by outlying operating units four months later.

c)

i) **Virtual Private Network** is private tunnel within a public network owned by an organisation used to transmit information. VPN offers security as only the information for that particular organisation is transmitted.
(3 marks)

ii) **Internet Service Provider** is a commercial organisation with a permanent connection to the internet and lease the connections to subscribers for a fee. Internet Service Providers also provide email services and web hosting services.

iii) **Client/server network** is where computers in network play two different role. One computer serves as a server and provides services to other machines called clients. (3 marks)

SOLUTION TWO

a)

i) *Office automation systems*: Supports daily work activities of individuals and groups.

ii) *Business intelligence systems*: Provides computer-based support for complex, non- routine tasks.

iii) *Expert systems*: Mimics human expertise in an area and makes decisions.

iv) *Dashboards*: Provide rapid access to timely information and direct access to structured information in form of reports.

b) Benefits of Electronic Commerce

- The greatest and the most important advantage of e-commerce, is that it enables a business concern or individual to reach the global market.
- It caters to the demands of both the national and the international market, as your business activities are no longer restricted by geographical boundaries. With the help of electronic commerce, even small enterprises can access the global market for selling and purchasing products and services.
- Time restrictions are non-existent while conducting businesses, as e-commerce empowers one to execute business transactions 24 hours a day and even on holidays and weekends. This in turn significantly increases sales and profit.
- Electronic commerce gives the customers the opportunity to look for cheaper and quality products. With the help of e-commerce, consumers can easily research on a specific product and sometimes even find out the original manufacturer to purchase a product at a much cheaper price than that charged by the wholesaler.
- Shopping online is usually more convenient and time saving than conventional shopping. Besides these, people also come across reviews posted by other customers, about the products purchased from a particular e-commerce site, which can help make purchasing decisions.
- It reduces the time period involved with business process re-engineering, customization of products to meet the demand of particular customers, increasing productivity and customer care services.

- Electronic commerce reduces the burden of infrastructure to conduct businesses and thereby raises the amount of funds available for profitable investment. It also enables efficient customer care services.

c) Creation, acquiring, storage, disseminating, management, Refinement

d)

- Support (helping in the use of the system)
- maintenance (continuing to refine and improve the system)
- project assessment (analysing the project to understand what activities were done well—and should be repeated—and what activities need improvement in future projects). (3 marks)

SOLUTION THREE

a) Electronic Data Interchange is the electronic exchange of business documents, such as orders, bills, confirmations either through a third party or directly with a business partner. Businesses constantly order supplies from various suppliers, each order having a unit cost. EDI ordering can cut that cost by a factor of 10 percent per order, faster transmission of order, faster replenishment of supplies from time of order, strategic alliances with EDI suppliers and possible cost benefits, reduction in use of paper, reduction in errors and loss of documents

b) A **business strategy** is the combination of all the decisions taken and actions performed by the **business** to accomplish the **business** goals and to secure a competitive position in the market. It is the backbone of the **business** as it is the roadmap which leads to the desired goals.
IT strategy (information technology strategy) is a comprehensive plan that outlines how technology should be used to meet business goals.

Most business a now being driven using technology and therefore the need to match the IT strategy to business strategy.

The IT strategy should be used to achieve the business goals and objectives

c) Principles of good software development practice which should ensure efficient maintenance.

1 Any change must be properly authorised by a manager in the user department

2 The new program requirements must be specified in full and in writing. These specifications will be prepared by a systems analyst. A programmer should use these specifications to produce an amended version of the program.

3 In developing a program version, a programmer should keep working papers. He or she can refer back to these later to check in the event that there is an error in the new program or the user of the program asks for a further change in the program.

4 The new version program should be tested when it has been written. A programmer should prepare test data.

5 Provisions should be made for further program amendments in the future. One way to do this is to leave space in the program instruction numbering sequence for new instructions to be inserted later.

6 A record should be kept for all program errors that are found during 'live' processing and of the corrections that are made to the program.
7 Each version of the program should be separately identified, to avoid a mix-up about what version of a program should be used for 'live' operating. (9 marks)

SOLUTION FOUR

a) Types of IS testing:
   - Unit testing
   - Integration testing
   - System testing
   - User acceptance testing

b) Components of an Accounting Information System include
- Hardware
- Software
- Procedures/controls
- People
- Data/information

c) Artificial intelligence (AI) technology, which consists of computer-based systems (both hardware and software) that attempt to emulate human behaviour. Such systems would be able to ***learn*** *languages*, ***accomplish physical tasks***, ***use a perceptual apparatus***, and ***emulate human expertise*** and ***decision making***. Although AI applications do not exhibit the breadth, complexity, originality, and generality of human intelligence, they play an important role in modern knowledge management.

   Expert systems are an intelligent technique for capturing tacit knowledge in a very specific and limited domain of human expertise.

   Artificial is being used a number of areas such as
   - Robotics
   - Autonomous vehicles (self-driving cars)
   - In education – automated grading systems
   - Health care for diagnostic purposes
   - In business – robotic process automation in doing jobs done by humans
   - In gaming

     etc

d) **Office Automation Systems** are used by data workers to improve the efficient operations of the office. They increase the productivity of data workers in the office by supporting the coordination and communication activities of the typical office. They include thing like word processing, electronic mail, voice messaging systems etc.

Knowledge Work Systems support the information and knowledge workers in the organization, ensuring that new knowledge and technical expertise are properly integrated into the business and performance the coordinating activities of the typical office. Knowledge workers are people who hold formal university degrees and often are members of a recognized profession, like engineers, doctors, layers, and scientists, whose job consists primarily of creating new information and knowledge.

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D2: FINANCIAL MANAGEMENT

FRIDAY 18 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question. You will be told when to start writing.
2. This question paper consists of **FOUR (4)** questions of Twenty Five (25) marks each. You must attempt all the **FOUR (4)** questions.
3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.
4. Do **NOT** write in pencil (except for graphs and diagrams).
5. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.
6. All workings must be done in the answer booklet.
7. Present legible and tidy work.
8. Graph paper (if required) is provided at the end of the answer booklet.
9. Formulae, Present Value, and Annuity tables are provided at the end of this question paper.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Attempt all FOUR (4) Questions.

<u>QUESTION ONE</u>

The following forecasted cash flow data relates to KG Inc. for the period from November 2019 to June 2020.

Month	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun
	K'000	K'000	K'000	K'000	K'000	K'000	K'000	K'000
Sales	80	100	110	130	140	150	160	180
Purchases	40	60	80	90	110	130	140	150
Wages	10	12	16	20	24	28	32	36
Overheads	10	10	15	15	15	20	20	20
Dividend declared	Nil	20	Nil	Nil	Nil	40	Nil	Nil
Capital Expenditure	Ni	Nil	30	Nil	Nil	40	Nil	Nil

It is expected that 45% of the sales will be on cash basis and the reminder on credit. Credit sales are paid two months after the month of sale. KG Inc. pays for purchases a month following the purchase. It is expected that 65% of wages will be paid in the current month and the reminder in the following month. Overheads are paid the month after they are incurred and dividends are paid three months after they are declared. In October 2019, KG Inc. had declared dividends of K10,000. It is expected that capital expenditure will be paid for, two months after it is incurred. The expenditure for October, 2019 was K11,000. The opening cash balance is K20,000.

Management of KG Inc. commented that it is pleased with the above figures as they show that sales will have increased by more than 100% in the period under review. The company has in place an overdraft facility with its bank of about K50,000.

Required:

(a) Prepare a cash flow forecast for the six-month period January to June, 2020. (14 marks)

(b) Comment on your results in the light of the Management's comments and offer advice. (6 marks)

(c) Discuss the advantages and disadvantages to KG Inc. of using overdraft finance to fund any cash shortages forecast by its cash flow forecasts. (5 marks)

[Total: 25 Marks]

QUESTION TWO

Supastore Ltd expects demand for a 10kg bag of mealie meal to be 255,380 units. The company manufactures 10kg bags in batch sizes of 50,000 units at regular intervals throughout the year. The company maintains a buffer inventory of the 10kg bags, which is sufficient to meet demand for 30 working days.

The company normally pays trade suppliers after 60 days, but it's supplier of grain has offered a discount of 1% for a cash settlement within 20 days. Supastore Ltd has a short – term cost of debt of 8% and uses a working year of 365 days.

Details of the current inventory management system are detailed below:

Item	Amount
S = Selling Price per unit	K19
Co =Ordering cost per order	K25
P = Purchase cost per unit	K11
I = Inventory holding cost per unit per year	K0.10

Required:

(a) Identify any five (5) stakeholder groups related to Supastore Ltd, and discuss their financial objectives and any conflicts of interests that may arise. (10 marks)

(b) Calculate the annual cost of the current ordering policy. Ignore financing costs. (4 marks)

(c) Compute the annual saving if the economic order quantity model is used to determine an optimal ordering policy. Ignore financing costs. (4 marks)

(d) Discuss the benefits and limitations of using a just-in-time inventory management system. (7 marks)

[Total: 25 Marks]

QUESTION THREE

Kiliag Plc, is a company that produces fruit juices for the local and international markets and is based in Western Province of Zambia. Kiliag Plc has done a feasibility study on a new line of product. This product is in form of a new line of fruit juice to be produced from the Masuku fruit, a wild fruit. The feasibility study involved the production and commercialization of this drink. A sample of the drink produced after undergoing quality tests proved very popular and international orders were received from neighboring countries. However, for mass production to take place there was need to order a new type of machine from Torino-Italy.

The machine is expected to cost K3,400,000 with an estimated scrap value of K250,000. This machine is to be depreciated on a straight line basis in line with Kiliag plc policy on depreciation of fixed assets.

You, as Finance Director, working with a financial consultant, Mr. Leon, were engaged to estimate annual production and sales volume of the Masuku Juice over a four year life.

The information produced and submitted was as follows:

	Year 1	Year 2	Year 3	Year 4

Volume in Units	19,000	16,500	14,500	14,500

The unit contribution in current price terms is as follows:

	K
Selling Price per unit	100
Less variable costs	50
Contribution per unit	50

Selling price inflation is estimated at 10% per annum while variable cost inflation is estimated at 8% per annum.

The introduction of this new production line of Masuku juice will not result in any increase in physical capacity in terms of production space. Therefore, no renovations to the existing factory building structure will be required as enough capacity is available. However, there will be need to make an additional investment in terms of working capital. This will be 5% of the sales revenue at the beginning of each year.

Kiliag Plc pays tax on profits at the rate of 35%, one (1) year in arrears; however, the tax liability is reduced by capital allowances which are claimed at the rate of 25% on cost per annum.

Kiliag Plc's pre-tax nominal cost of capital is at 10.77%.

Required:

(a) Evaluate the proposed investment in the Masuku Juice Product using the Net Present Value (NPV) and the Internal Rate of Return (IRR). (15 marks)

(b) Advise on the acceptability of the proposed investment in the product and discuss two limitations of the evaluations you have carried out. (3 marks)

(c) Explain the term "market efficiency" in the context of stock markets, describing the forms of efficiency a stock market may exhibit. (7 marks)

[Total: 25 Marks]

QUESTION FOUR

NAT Inc. has fully paid K110 million ordinary share capital of K1 each. The current market price of each share is K2.50. NAT Inc. also has 9% loan stock issued at a par value of K100 with six years to maturity. It's redeemable at a 5% premium. The pre-tax cost of debt is 15.7% per year. NAT Inc. has just paid a total dividend of K120 million to its shareholders which translates to an annual growth of 5%, which is expected to continue in the near future. The equity beta for NAT Inc. is 1.21. The risk free rate is 7% per year and the expected market return is 16%. The annual corporate tax is payable at 30%.

Required:

(a) Calculate the market value of the loan stock for NAT Inc. (6 marks)

(b) Estimate the market value per share of NAT Inc. using the dividend valuation method.

(6 marks
)

(c) Calculate the current weighted average cost of capital for NAT Inc. (5 marks)

(d) Discuss whether changing the capital structure of a company can lead to a reduction in its cost of capital and hence to an increase in the value of the company.

(8 marks)

[Total: 25 Marks]

END OF PAPER

Formula Sheet

Economic order quantity

$$= \sqrt{\frac{2C_oD}{C_H}}$$

Miller – Orr Model

$$\text{Return point} = \text{Lower limit} + (\frac{1}{3} \times \text{spread})$$

$$\text{Spread} = 3\left[\frac{\frac{3}{4} \times \text{transaction cost} \times \text{variance of cash flows}}{\text{interest rate}}\right]^{\frac{1}{3}}$$

The Capital Asset Pricing Model

$$E(r_i) = R_f + \beta_i(E(r_m) - R_f)$$

The asset beta formula

$$\beta_a = \left[\frac{V_e}{(V_e + V_d(1 - T))}\beta_e\right] + \left[\frac{V_d(1 - T)}{(V_e + V_d(1 - T))}\beta_d\right]$$

The Growth Model

$$P_o = \frac{D_o(1+g)}{(r_e - g)}$$

Gordon's growth approximation

$$g = br_e$$

The weighted average cost of capital

$$WACC = \left[\frac{V_e}{V_e + V_d}\right]k_e + \left[\frac{V_d}{V_e + V_d}\right]k_d(1-T)$$

The Fisher formula

$$(1+i) = (1+r)(1+h)$$

Purchasing power parity and interest rate parity

$$s_1 = S_0 \times \frac{(1+h_c)}{(1+h_b)} \qquad f_0 = s_0 \times \frac{(1+i_c)}{(1+i_b)}$$

Present Value Table

Present value of 1 i.e. $(1 + r)^{-n}$

Where r = discount rate
n = number of periods until payment

Discount rate (r)

Periods (n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0·990	0·980	0·971	0·962	0·952	0·943	0·935	0·926	0·917	0·909	1
2	0·980	0·961	0·943	0·925	0·907	0·890	0·873	0·857	0·842	0·826	2
3	0·971	0·942	0·915	0·889	0·864	0·840	0·816	0·794	0·772	0·751	3
4	0·961	0·924	0·888	0·855	0·823	0·792	0·763	0·735	0·708	0·683	4
5	0·951	0·906	0·863	0·822	0·784	0·747	0·713	0·681	0·650	0·621	5
6	0·942	0·888	0·837	0·790	0·746	0·705	0·666	0·630	0·596	0·564	6
7	0·933	0·871	0·813	0·760	0·711	0·665	0·623	0·583	0·547	0·513	7
8	0·923	0·853	0·789	0·731	0·677	0·627	0·582	0·540	0·502	0·467	8
9	0·914	0·837	0·766	0·703	0·645	0·592	0·544	0·500	0·460	0·424	9
10	0·905	0·820	0·744	0·676	0·614	0·558	0·508	0·463	0·422	0·386	10
11	0·896	0·804	0·722	0·650	0·585	0·527	0·475	0·429	0·388	0·350	11
12	0·887	0·788	0·701	0·625	0·557	0·497	0·444	0·397	0·356	0·319	12
13	0·879	0·773	0·681	0·601	0·530	0·469	0·415	0·368	0·326	0·290	13
14	0·870	0·758	0·661	0·577	0·505	0·442	0·388	0·340	0·299	0·263	14
15	0·861	0·743	0·642	0·555	0·481	0·417	0·362	0·315	0·275	0·239	15

(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0·901	0·893	0·885	0·877	0·870	0·862	0·855	0·847	0·840	0·833	1
2	0·812	0·797	0·783	0·769	0·756	0·743	0·731	0·718	0·706	0·694	2
3	0·731	0·712	0·693	0·675	0·658	0·641	0·624	0·609	0·593	0·579	3
4	0·659	0·636	0·613	0·592	0·572	0·552	0·534	0·516	0·499	0·482	4
5	0·593	0·567	0·543	0·519	0·497	0·476	0·456	0·437	0·419	0·402	5
6	0·535	0·507	0·480	0·456	0·432	0·410	0·390	0·370	0·352	0·335	6
7	0·482	0·452	0·425	0·400	0·376	0·354	0·333	0·314	0·296	0·279	7
8	0·434	0·404	0·376	0·351	0·327	0·305	0·285	0·266	0·249	0·233	8
9	0·391	0·361	0·333	0·308	0·284	0·263	0·243	0·225	0·209	0·194	9
10	0·352	0·322	0·295	0·270	0·247	0·227	0·208	0·191	0·176	0·162	10
11	0·317	0·287	0·261	0·237	0·215	0·195	0·178	0·162	0·148	0·135	11
12	0·286	0·257	0·231	0·208	0·187	0·168	0·152	0·137	0·124	0·112	12
13	0·258	0·229	0·204	0·182	0·163	0·145	0·130	0·116	0·104	0·093	13
14	0·232	0·205	0·181	0·160	0·141	0·125	0·111	0·099	0·088	0·078	14
15	0·209	0·183	0·160	0·140	0·123	0·108	0·095	0·084	0·074	0·065	15

Annuity Table

Present value of an annuity of 1 i.e. $\frac{1 - (1 + r)^{-n}}{r}$

Where r = discount rate
n = number of periods

Discount rate (r)

Periods (n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0·990	0·980	0·971	0·962	0·952	0·943	0·935	0·926	0·917	0·909	1
2	1·970	1·942	1·913	1·886	1·859	1·833	1·808	1·783	1·759	1·736	2
3	2·941	2·884	2·829	2·775	2·723	2·673	2·624	2·577	2·531	2·487	3
4	3·902	3·808	3·717	3·630	3·546	3·465	3·387	3·312	3·240	3·170	4
5	4·853	4·713	4·580	4·452	4·329	4·212	4·100	3·993	3·890	3·791	5
6	5·795	5·601	5·417	5·242	5·076	4·917	4·767	4·623	4·486	4·355	6
7	6·728	6·472	6·230	6·002	5·786	5·582	5·389	5·206	5·033	4·868	7
8	7·652	7·325	7·020	6·733	6·463	6·210	5·971	5·747	5·535	5·335	8
9	8·566	8·162	7·786	7·435	7·108	6·802	6·515	6·247	5·995	5·759	9
10	9·471	8·983	8·530	8·111	7·722	7·360	7·024	6·710	6·418	6·145	10
11	10·37	9·787	9·253	8·760	8·306	7·887	7·499	7·139	6·805	6·495	11
12	11·26	10·58	9·954	9·385	8·863	8·384	7·943	7·536	7·161	6·814	12
13	12·13	11·35	10·63	9·986	9·394	8·853	8·358	7·904	7·487	7·103	13
14	13·00	12·11	11·30	10·56	9·899	9·295	8·745	8·244	7·786	7·367	14
15	13·87	12·85	11·94	11·12	10·38	9·712	9·108	8·559	8·061	7·606	15

(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0·901	0·893	0·885	0·877	0·870	0·862	0·855	0·847	0·840	0·833	1
2	1·713	1·690	1·668	1·647	1·626	1·605	1·585	1·566	1·547	1·528	2
3	2·444	2·402	2·361	2·322	2·283	2·246	2·210	2·174	2·140	2·106	3
4	3·102	3·037	2·974	2·914	2·855	2·798	2·743	2·690	2·639	2·589	4
5	3·696	3·605	3·517	3·433	3·352	3·274	3·199	3·127	3·058	2·991	5
6	4·231	4·111	3·998	3·889	3·784	3·685	3·589	3·498	3·410	3·326	6
7	4·712	4·564	4·423	4·288	4·160	4·039	3·922	3·812	3·706	3·605	7
8	5·146	4·968	4·799	4·639	4·487	4·344	4·207	4·078	3·954	3·837	8
9	5·537	5·328	5·132	4·946	4·772	4·607	4·451	4·303	4·163	4·031	9
10	5·889	5·650	5·426	5·216	5·019	4·833	4·659	4·494	4·339	4·192	10
11	6·207	5·938	5·687	5·453	5·234	5·029	4·836	4·656	4·486	4·327	11
12	6·492	6·194	5·918	5·660	5·421	5·197	4·988	4·793	4·611	4·439	12
13	6·750	6·424	6·122	5·842	5·583	5·342	5·118	4·910	4·715	4·533	13
14	6·982	6·628	6·302	6·002	5·724	5·468	5·229	5·008	4·802	4·611	14
15	7·191	6·811	6·462	6·142	5·847	5·575	5·324	5·092	4·876	4·675	15

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) CASH FLOW FORECAST FOR THE SIX MONTHS ENDED JUNE 2020

Period	Jan	Feb	Mar	Apr	May	Jun
	K'000	K'000	K'000	K'000	K'000	K'000
Receipts:						
Sales- Cash Receipts (45%)	49.50	58.50	63.00	67.50	72.00	81.00
Sales- Credit sales (55%)*	44.00	55.00	60.50	71.50	77.00	82.50
Total Receipts	**93.50**	**113.50**	**123.50**	**139.00**	**149.00**	**163.50**
Payments:						
Purchases	60.00	80.00	90.00	110.00	130.00	140.00
Wages (W1)	14.60	18.60	22.60	26.60	30.60	34.60
Overheads	10.00	15.00	15.00	15.00	20.00	20.00
Dividends	10.00	-	20.00	-	-	-
Capital expenditure	-	-	30.00	-	-	40.00
Total expenditure	**94.60**	**113.60**	**177.60**	**151.60**	**180.60**	**234.60**
Surplus	(1.10)	(0.10)	(54.10)	(12.60)	(31.60)	(71.10)
Balance b/f	20.00	18.90	18.80	(35.30)	(47.90)	(79.50)
Balance b/d	**18.90**	**18.80**	**(35.30)**	**(47.90)**	**(79.50)**	**(150.60)**

WORKINGS

	Notes						

	* Two months after month of sale e.g. November credit sales are paid in January.						
W1		Jan	Feb	Mar	Apr	May	Jun
	Wages-65%	10.4	13	15.6	18.2	20.8	23.4
	Wages balance-35%	4.2	5.6	7	8.4	9.8	11.2
	Total	14.6	18.6	22.6	26.6	30.6	34.6

(b) Comments And Advice

The overdraft arrangements are quite inadequate to service the cash needs of the business over the six-month period given that the business will have a forecasted cash deficit of K35.3 million in March which is projected to increase to K150.6 million by the end of June 2020. If the figures are realistic then action should be taken now to avoid difficulties the near future.

The following are possible courses of action:

(1) Some activities could be such as the forecasted capital expenditure can curtailed or postponed.
(2) Other sources of cash could be explored, for example a long-term loan to finance the capital expenditure and a factoring arrangement to provide cash due from accounts receivable more quickly.
(3) Efforts to increase the speed of debt collection could be made.
(4) Payments to accounts payable could be delayed.
(5) The dividend payments could be postponed (the figures indicate that this is a small company, possibly owner-managed).
(6) Staff might be persuaded to work at a lower rate in return for, say, an annual bonus or a profit sharing agreement.
(7) Extra staff might be taken on to reduce the amount of overtime paid.
(8) The stock holding policy should be reviewed; it may be possible to meet demand from current production and minimise cash tied up in inventories.

(1 mark for each valid point up to a maximum of 6 marks)

(c) Advantages and disadvantages of using overdraft finance to fund cash shortages

Advantages

(1) Cash flow forecast shortages are short term in nature so it is unlikely that a long-term loan will be appropriate to fund these. Typically, temporary deficits are funded by an overdraft granted by the company's bank where interest is charged on the overdrawn amount at a rate over base.

(2) Overdraft finance has the advantage of being flexible and that interest is only due on the actual overdrawn amount.
(3) The rate of interest is flexible as it is variable and linked to a base rate and so can go down as well as up.

Disadvantages

(1) The risk of an interest rate increase as the rate is not fixed.

(2) Also, the overdraft is repayable on demand. Banks usually ask for some collateral when lending such as a fixed or floating charge on the company's assets.

(1 mark for each valid point up to a maximum of 5 marks)

SOLUTION TWO

(a) Key stakeholders in Supastore

Stakeholders in Supastore will include shareholders, creditors, employees, customers, directors and managers. The stakeholders share in the returns and risks generated by the company in different ways - because of differences in risk appetite and investment horizons, and thus conflicts of interest are likely to arise within and among stakeholder groups for instance equity and preference shareholders might prefer different dividend policies. Good corporate governance practices are meant to resolve different stakeholder conflicts.
Objectives of stakeholder groups are as follows:

Shareholders

Their primary interest is wealth maximization. For listed companies, the objective can be set in terms of total shareholder return, whose achievement is measured by metrics such as dividend yield and price/earnings ratio.

For companies that are not listed, the overall objective might be profit maximization with performance indicators such as return on capital employed, gearing, earnings per share etc.

Directors and managers

Conflict relating to this stakeholder group arise from the separation that exists between ownership of an entity and daily control. Non – financial objectives of managers can be inconsistent with those of the company. Since shareholders are not involved in decision making on a daily basis, managers can make decisions that reward themselves at the expense of shareholders and other stakeholders. Share ownership schemes are one way of aligning these conflicting interests.

Lenders/Suppliers

Lenders are primarily concerned with receiving payment of interest and the principal on their loans at maturity, and therefore monitor performance indicators that measure liquidity and solvency. Profitability of the entity is therefore their overriding objective for both lenders and suplliers.

Employees

Their primary interest lies in receiving a living wage and security of employment. Wages are a cost and can therefore conflict with the profit motive of shareholders. Performance bonuses related to company profitability are a way of managing this conflict.

Suppliers and customers

Customers are primarily interested in customer satisfaction, that is the quality of goods and services they receive. To archive customer satisfaction, the company can set objectives in terms of quality, lead times and price.

(b) Supastore Ltd has a current order size of 50,000 units:

Item	Computation
Average number of orders per year = demand/order size =	255, 380/50, 000 = 5.11 orders.
Annual ordering cost =	5.11 x 25 = K127.75
Buffer inventory held =	255, 380 x 30/365 = 20,990 units.
Average inventory held =	20,990 + (50, 000/2) = 45, 990 units
Annual holding cost =	45, 990 x 0.10 = <u>K4, 599</u>

(c) Economic Order Quantity:

Item	Computation
EOQ	= $((2 \text{ X } 255,380 \text{ X } 25)/0.10)^{0.5}$ = 11,300 units
Average number of orders per year	= 255, 380/11,300 = 22.6 orders
Annual ordering cost	= 22.6 x 25 = K565.00
Average inventory held	= 20,990 + (11,300/2) = 26, 640 units
Annual holding cost	= 26, 640 x 0.1 = <u>K2, 664</u>
Annual holding with EOQ ordering policy	= 2,664 + 565 = <u>K3, 229</u>
Saving compared to current policy	= 4, 599 – 3, 229 = <u>K1,370</u>

(d) Just In Time

<u>Benefits</u>

(1) Eliminates waste by minimizing or eliminating stock defects, breakdowns and production delays, using workflow planning and a focus on quality control.

(2) Stronger relationship between a buyer and its suppliers, through firm contracts , which offers security to the supplier, and benefits from regular orders, continuity in business and certainty in production planning.

(3) The buyer benefits from lower holding and purchase costs through bulk purchase discounts, investment in inventory, and transfer of supply chain bottlenecks to the supplier.

(4) Emphasis on quality control reduces scrap, reworking and setup costs. Improved production design can eliminate unnecessary material movements, which results in smooth flow of material and work through the production system, resulting in no queues or idle time.

<u>Drawbacks</u>

(1) Contrary to theory, benefits may not be realized due to unforeseen delays, and errors in delivery times.
(2) The buyer is dependent on the supplier for the quality of delivered materials and components. Poor quality in materials can lead to production downtimes.

(3) The buyer might not be able to find alternative buyers in the event of increases in material prices.

SOLUTION THREE

(a) Calculations of Net Present Value (NPV) and Internal Rate of Return.

Note: all of the cash flows are in K' millions

	Yr 1	Yr 2	Yr 3	Yr 4	Yr 5
Sales(W1 x Units)	2,090	1,997	1,930	2,123	
Variable Costs(W2xUnits)	(1,026)	(963)	(913)	(989)	
Pre-tax cashflow	1,064	1,034	1,017	1,134	
Tax (35%)		(372)	(362)	(356)	(397)
Tax saved(W3)		306	306	306	219
Working Capital	5	3.3	(9.7)	106.5	
Scrap Value				250	
Net Cashflow	1,069	971.3	951.4	1,440.5	(178)
DCF at 7%	0.935	0.873	0.816	0.763	0.713
Present Value	1,000	848	776	1,099	(127)

Sum of Present Values		K3,596
Initial Outlay:	K3,400	
Working Capital(W4)	104	(K3,505)
Net Present Value		K91

	Year 1	Year 2	Year 3	Year 4	Year 5
Net Cashflow	1,069	971.3	951.4	1,440.5	(178)
DCF at 10%	0.909	0.826	0.751	0.683	0.621
Present Values	972	705	715	984	(111)

Sum of Present Values	K3,265
Less initial outlay	(3,505)
Net Present Value	(240)

Internal Rate of Return:

= 7+[91/(91+240)x(10-7)]

= 7.82%

The net present value is positive and the internal rate of return is less than the cost of capital.

Workings

(1) Forecast selling prices per unit

Year 1=K100x1.10=K110.00

Year 2=K110x1.10=K121.00

Year 3=K121x1.10=K133.10

Year 4=K133.10x1.10=K146.41

(2) Forecast Variable costs per unit

Year 1=K50x1.08=K54.00

Year 2=K54x1.08=K58.32

Year 3=K58.32x1.08=K62.98

Year 4=K62.98x1.08=K68.02

(3) Capital Allowances and tax saved

Year 1-Year 3 = 25%XK3, 500,000

=K 875,000

Tax saved per year=35%x K875,000

=K306,250

Year 4

Income Tax Value=K3,500,000-(K875,000X3)

=K3,500,000-K2,625,000

=K875,000

Tax saved on balancing allowance on disposal of the machine:

Tax saved = 35%x(K875,000-K250,000)

= 35%xK625,000

= K218,750

(4) Movements in working capital Investment

	Opening Balance	Closing Balance	Change
	K'000	K'000	K'000
1	104.5	99.8	5
2	99.8	96.5	3.3
3	96.5	106.15	(9.65)
4	106.15	0	106.15

(5) Post tax nominal cost of capital=10.77%x(1-0.35)

= 7%

(b) The project using the net present value calculation shows that the project is financially viable but the internal rate of return is less than the cost of capital.

The cash-flows relating to the project are conventional and this results in only one IRR arising.

Also since there is only one project under consideration, there is no conflict between the decision based on the NPV rule and that based on the IRR rule.
The limitations of the evaluation used indicate the fact that both the NPV and the IRR heavily depend upon the forecast sales volumes.

The reliability of the forecast sales volumes needs to be investigated. Also it has been assumed that inflation for both sales price and variable costs will remain constant year after year. In reality, inflation varies year after year.

(c) "Efficient" in the context of stock markets relates to the ways in which information about shares and the underlying company are processed by investors in the market. Efficiency in a stock market means that relevant information is absorbed quickly and accurately by investors leading to shares being priced at a value that reflects their true worth. This should mean that shares are always valued at their true worth. This should mean that shares are always valued at their true value and therefore it is not possible for investors to make abnormal gains over the long-term.

There are generally thought to be three levels of stock market efficiency that exist with their own characteristics.

(1) Weak Form

In a weak form efficient market share prices reflect all relevant published information relating to the past share price and trading performance. However, any new information relating to the share or company is not anticipated by the market. The effect of this is that as information about company becomes more available to the market on random basis changes in the share prices will be equally random. Therefore investors should not be able to make abnormal gains over the long term by analyzing trends in share performance or share prices.

(2) Semi-strong form

The semi-strong form of efficiency is one step on from the weak form and is where share prices quickly and accurately reflect all publicly available information. Such publicly available information relates to the future prospects of the company, information relating to the industry in which the company operates and information in general about the state of the economy. The effect of this form of efficiency is that the share price already reflects all information that has been published about the company, both historical and future prospects, therefore there is no chance of an investor making abnormal gains by studying this information.

(3) Strong form

In a strong form, efficient market the share price will already reflect all information about the company whether or not this is publicly available. Therefore as the share price already reflects all information there is no chance of investors making abnormal gains even if they do have inside information.

SOLUTION FOUR

(a) Cost of debt = 15.7%x (1- 0.3) = 11%

Year		Cash flow	Discount@11%	PV
1-6	Interest (9x0.7)	6.3	4.231	26.66
6	Redeem	105	0.535	56.18
Market value per nominal of loan stock				82.84

Total market value of loan stock:

82.84/100 x K55m = **K45.56million**

(b) Market value per ordinary share

$$Po = \frac{K1.1\ (W1) \times 1.05}{0.1789\ (W2) - 0.05}$$

= K8.96 per share

Workings:

(1) Number of shares = K110m/K1 = 110m

Dividend per share = K120m/110m = K1.1 per share

(2) Cost of equity = 7% + 1.21 (16%-7%) = 17.89%

(c) COMPUTATION OF WACC

Weighting:	K'm	%
Equity: (110m x K2.5)	275.00	86

Debt =	$\frac{45.56}{320.56}$	$\frac{14}{100}$

WACC = 17.9% x 0.86 + 11% x 0.14 = 16.93%

(d) Discussion of capital structure

The value of a company can be expressed as the present value of its future cash flows, discounted at its weighted average cost of capital (WACC). The value of a company can therefore theoretically be maximized by minimising its cost of capital.

The capital structure comprises of equity and debt and therefore if the WACC depends on the capital structure of a company, then the minimum WACC will arise when the capital structure is optimal.

Theories have been developed regarding the idea of an optimal capital structure. The traditional theory of capital structure suggests that the WACC decreases as debt is introduced at low levels of gearing, before reaching a minimum and then increasing as the cost of equity responds to increasing financial risk.

Miller and Modigliani originally argued that the in a perfect market without tax, WACC is independent of a company's capital structure, depending only on its business risk rather than on its financial risk.

However, real world capital markets are not perfect and companies pay taxes on profit. Since interest is a tax-allowable deduction in calculating taxable profit, debt is a tax efficient source of finance and replacing equity with debt will decrease the WACC of a company.

Increasing gearing will lead to a decrease in the WACC of a company and hence increase its value. But at high levels of gearing, the WACC of a company will increase due to increasing bankruptcy risk. Consequently, it can be argued that use of debt in a company's capital structure can reduce its Weighted average cost of capital and increase its value, provided that gearing is kept to an acceptable level.

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D3: BUSINESS TAXATION

WEDNESDAY 16 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question.

2. This paper consists of **FOUR (4)** questions of twenty five (25) marks each. You MUST attempt all the **FOUR (4)** questions.

3. Enter your student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. **Cell Phones** are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. You must write ALL your answers in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

10. A taxation table is provided on pages 2,3, 4,5 and 6 of this paper.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table

Income Tax

Standard personal income tax rates

Income band	Taxable amount	Rate
K1 to K39,600	first K39,600	0%
K39,601 to 49,200	next K9,600	25%
K49,201 to K74,400	next K25,200	30%
Over K74,400		37.5%

Income from farming for individuals

K1 to K39,600	first K39,600	0%
Over K39,600		10%

Company Income Tax rates

On income from manufacturing and other	35%
On income from farming	10%
On income of Banks and other Financial Institutions	35%
On income from mineral processing	30%
On income from mining operations	30%
On income from manufacture of products made out of copper cathodes	15%

Mineral Royalty

Mineral Royalty on Copper

Range of Norm Price	Mineral Royalty Rate
Less than US$4,500	5.5% of norm value
From US$4,500 to less than US$6,000	6.5% of norm value
From US$6,000 to less than US$7,500	7.5% of norm value
From US$7,500 to less than US$9,000	8.5% of norm value
From US$9,000 and above	10% of norm value

Mineral Royalty on other minerals

Type of mineral	Mineral Royalty Rate

Base Metals (Other than Copper, Cobalt and Vanadium)	5% of norm value
Cobalt and Vanadium	8% of norm value
Energy and Industrial Minerals	5% of gross value
Gemstones	6% of gross value
Precious Metals	6% of norm value

Capital Allowances

Implements, plant and machinery and commercial vehicles:

Wear and Tear Allowance –	Plant used normally	25%
	Used in Manufacturing and Leasing	50%
	Used in farming and agro-processing	100%
	Used in mining operations	20%

Non- commercial vehicles

Wear and Tear Allowance	20%

Industrial Buildings:

Wear and Tear Allowance	5%
Initial Allowance	10%
Investment Allowance	10%

Low Cost Housing **(Cost up to K20,000)**

Wear and Tear Allowance	10%
Initial Allowance	10%

Commercial Buildings

Wear and Tear Allowance	2%

Farming Allowances

Development Allowance	10%
Farm Works Allowance	100%
Farm Improvement Allowance	100%

Presumptive Taxes

Turnover Tax 4%

Presumptive Tax for Transporters

Seating capacity	**Tax per annum**	**Tax per day**
	K	K
From 64 passengers and over	10,800	29.60
From 50 to 63 passengers	9,000	24.70
From 36 to 49 passengers	7,200	19.70
From 22 to 35 passengers	5,400	14.80
From 18 to 21 passengers	3,600	9.90
From 12 to 17 passengers	1,800	4.90
Less than 12 passengers and taxis	900	2.40

Property Transfer Tax

Rate of Tax on Realised Value of Land, Land and Buildings and shares	5%
Rate of Tax on Realised Value on a transfer or sale of a mining right	10%
Rate of Tax on Realised Value on a transfer of Intellectual Property	5%

Value Added Tax

Registration threshold	K800,000
Standard Value Added Tax Rate (on VAT exclusive turnover)	16%

Customs and Excise duties on used motor vehicles

	Aged below 5 years		Aged 5 years and over	
Motor vehicles for the transport of ten or more persons, including the driver	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sitting capacity of 10 but not exceeding 14 persons including the driver	17,778	22,223	8,889	11,112
Sitting capacity exceeding 14 but not exceeding 32 persons	38,924	0	13,840	0
Sitting capacity of 33 but not exceeding 44 persons	86,497	0	19,462	0
Sitting capacity exceeding 44 persons	108,121	0	43,248	0

	Aged below 5 years		Aged 5 years and over	
Motor cars and other motor vehicles principally designed for the transport of persons including station wagons and racing cars	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sedans				
cylinder capacity not exceeding 1000 cc	12,490	10,824	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	16,058	13,917	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	16,545	21,508	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	10,528	13,687
Cylinder capacity exceeding 3000 cc	22,561	29,329	12,032	15,642
Hatchbacks				
cylinder capacity not exceeding 1000 cc	10,705	9,278	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	14,274	12,371	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	15,041	19,553	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	16,545	21,508	10,523	13,687
Cylinder capacity exceeding 3000 cc	19,553	25,419	12,032	15,642
Station wagons				
cylinder capacity not exceeding 2500 cc	16,545	21,508	9,024	11,731
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	13,357	17,598
Cylinder capacity exceeding 3000 cc but not exceeding 2500 cc	22,561	29,329	18,049	23,463

SUVs				
Cylinder capacity not exceeding 2500 cc	21,057	27,374	9,024	11,732
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	24,065	31,284	13,357	17,598
Cylinder capacity exceeding 3000 cc	28,577	37,150	18,049	23,463
	Aged below 5 years		**Aged 5 years and over**	
Motor vehicles for the transport of goods -with compression-ignition internal combustion piston engine (diesel or semi-diesel):	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Single cab				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	21,926	9,501	8,770	3,801
GVW exceeding 1.5 tonnes but not exceeding 3.0 tonnes	26,311	11,402	15,348	6,651
GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes	30,697	13,302	17,541	7,601
Double cabs GVW exceeding 3 tonnes but not exceeding 5 tonnes	30,274	0	24,119	10,452
Double cabs GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes, **with spark ignition internal combustion piston engine**	30,697	13,302	24,119	10,452
Panel Vans				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	15,348	6,651	8,770	3,801
GVW exceeding 1.5 tonnes but not exceeding 3.0 tonnes	17,541	7,601	15,348	6,651
GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes	21,926	9,501	17,541	7,601
Trucks				
GVW up to 2 tonnes	21,926	9,501	10,963	4,751
GVW exceeding 2.0 tonnes but not exceeding 5.0 tonnes	28,504	12,352	13,156	5,701
GVW exceeding 5.0 tonnes but not exceeding 10.0 tonnes	24,724	18,955	10,817	8,293
GVW exceeding 10.0 tonnes but not exceeding 20.0 tonnes	30,905	23,694	11,744	9,004
GVW exceeding 20 tonnes	51,898	0	19,461	0
GVW exceeding 20 tonnes, **with spark ignition internal combustion piston engine**	37,086	28,432	13,907	10,662

Surtax

On all motor vehicles aged more than five (5) years from year of manufacture	K2,000

Customs and Excise on New Motor vehicles

Duty rates on:

1.	**Motor cars and other motor vehicles (including station wagons) principally designed for the transport of less than ten persons, including the driver:**	
	Customs Duty:	
	Percentage of Value for Duty Purposes	30%
	Minimum Specific Customs Duty	K6,000
	Excise Duty:	
	Percentage of Value for Duty Purposes for Excise Duty Purposes	
	Cylinder capacity of 1500 cc and less	20%
	Cylinder Capacity of more than 1500 cc	30%
2.	**Pick-ups and trucks/lorries with gross weight not exceeding 20 tones:**	
	Customs Duty	
	Percentage of Value for Duty Purposes	15%
	Minimum specific Customs Duty	K6,000
	Excise Duty:	
	Percentage of Value for Duty Purposes for Excise Duty Purposes	10%
3.	**Buses/coaches for the transport of more than ten persons**	
	Customs Duty:	
	Percentage of Value for Duty Purposes	15%
	Minimum Specific Customs Duty	K6,000
	Excise Duty:	
	Percentage of Value for Duty Purposes for Excise Duty Purposes	
	Seating Capacity of 16 persons and less	25%
	Seating Capacity of 16 persons and more	0%
4.	**Trucks/lorries with gross weight exceeding 20 tonnes**	
	Customs Duty:	
	Percentage of Value for Duty Purposes	15%
	Excise Duty:	
	Percentage of Value for Duty Purposes for Excise Duty Purposes	0%

Attempt all FOUR (4) questions.

QUESTION ONE

The following summarised statement of profit or loss for the year ended 31 December 2020, has been extracted from the financial statements of BMC Mining Corporation, a Zambian resident subsidiary of a foreign based Multinational Mining company. BMC is engaged in mining operations of base metals. The group maintains its accounts in US dollars.

BMC MINING CORPORATION
STATEMENT OF PROFIT OR LOSS FOR THE YEAR ENDED 30 DECEMBER 2020

	Note	K
Revenue	(1)	978,000,000
Cost of sales		(450,240,000)
Gross profit		527,760,000
Operating expenses	(2)	(224,445,000)
Investment income	(3)	1,785,000
Profit for the year		305,100,000

The following additional information is available:

(1) This comprises sales of cobalt for the year amounting to K378,000,000 being the norm value of the mineral, with the remaining balance of the sales representing the norm value of copper sold during the year based on London Metal Exchange cash price which ranged between $6,100 and $6,900 per metric tonne throughout tax year 2020.

(2) Included in operating expenses, is mineral royalty tax paid by the company during the year which was computed correctly and paid on the relevant due dates. Also included in operating expenses are depreciation charges of K336,000, amortisation of intangible assets of K144,000, mineral transportation costs of K6,600,000, expenditure on drilling boreholes for the local mining community of K1,600,000, expenditure on construction of a police post in the local mining township of K600,000, donations to political parties of K60,000, donations to approved public benefit organisations of K350,000 and staff salaries of K160,080,000. The balance represents miscellaneous allowable operating expenses.

(3) Investment income includes treasury bill interest of K595,000 (net) rental income of K720,000 (net) and unrealised foreign exchange gains of a capital nature of K470,000.

(4) There were no implements plant and machinery qualifying for capital allowances at 1 January 2020, however, the company incurred the following expenditure and acquired the following assets locally from Zambian resident suppliers:

Expenditure	*Cost*
	K

Construction of new central administration offices	14,600,000
Purchase of mining equipment	2,400,000
Construction of new smelting plant	1,600,000
Purchase of four (4) Pool cars at a cost of (K450,000 each)	1,800,000
Purchase of a 4,700cc Toyota Land Cruiser (GXL)	1,500,000
Purchase of a 2,700cc Land Rover Discovery	1,200,000

The Toyota Land cruiser (GXL) is provided to the Chief Executive Officer on a personal to holder basis, while the Land Rover Discovery is provided to the Chief Finance Officer on a personal to holder basis. The private use by each executive of each vehicle is 40%.

(5) The company incurred a tax adjusted mining loss of US$60 million in the year ended 31 December 2019.

(6) Mining losses can be indexed using the following formula:

$$1+\frac{(R_2-R_1)}{R_1} \text{ x Tax loss brought forward}$$

(7) The following Zambian Kwacha per US Dollar (K/US$) average mid exchange rates have been provided and approved by the Commissioner General:

Accounting Period	*Average BOZ Mid Exchange rate*
	K/US$
Y/e 31 December 2019	13.50
Y/e 31 December 2020	14.50

Required:

(a) Compute the taxable mining profits for the tax year 2020, and show the amount of the tax loss remaining unrelieved at 31 December 2020. (20 marks)

(b) Calculate the total income tax payable by the company for the tax year 2020. (5 marks)

[Total: 25 Marks]

<u>QUESTION TWO</u>

Yako Farms Limited (YFL) is a Zambian resident company engaged in farming operations. The company currently sells all of its farm produce domestically but is considering exporting some of its produce to neighbouring countries. To do this, it needs to acquire more non-current assets either by hire purchase, loan finance, finance lease or operating lease. The company is registered for Value Added Tax.

The summarised statement of profit or loss for the year ended 31 December 2020 is shown below:

		K
Turnover		12,650,000
Cost of sales		(6,150,000)
Gross profit		6,500,000
Operating expenses	(Note 1)	(1,950,000)
Finance cost		(450,000)
Investment income	(Note 2)	525,000
Profit before tax		4,625,000

The following information is relevant:

(1) Operating expenses include depreciation charges of K137,000, pasture maintenance costs of K165,000, expenditure on destruction of weeds, plants and animal pests detrimental to the land of K230,000, costs associated with the acquisition of new farm land of K47,000, staff salaries of K960,000 and fines for breach of labour regulations of K87,000. The balance represents general business expenses which are all allowable for tax purposes.

(2) The company earned the following gross investment income in the tax year 2020, which has been included under investment income in the statement of profit or loss shown above, withholding tax has already been paid:

		K
Dividends from non-listed Zambian company		270,000
Dividends from Zambian mining companies	75,000	
Bank deposit interest	45,000	
Interest on Government bonds		135,000

(3) The following capital expenditure incurred by the company in the tax year 2020, was not recorded in the financial statements:

		K
Construction of Storage Facilities		475,000
Purchase of farm implements and machinery		145,000
Rose flower plantation development costs	520,000	

(4) Capital allowances on other qualifying assets have been agreed at K350,000.

(5) Provisional income tax of K335,000 was paid during the tax year 2020.

Required:

(a) Explain the Income Tax and Value Added Tax implications of financing the purchase of non-current assets using the following options:

(i) Hire purchase (3 marks)
(ii) Loan finance (3 marks)
(iii) Finance lease (3 marks)
(iv) Operating lease (3 marks)

(b) Calculate the adjusted taxable profit for Yako Farms Limited for the tax year 2020. (8 marks)

(c) Calculate the company income tax payable by Yako Farms Limited for the tax year 2020. (5 marks)

[Total: 25 Marks]

QUESTION THREE

(a) Tata Ziba, a sole trader, imported a second hand, 1900 cc Toyota Corolla (Sedan) car on 21 January 2020. The car was manufactured in Japan in January 2018. The cost of the car was $3,360. Tata Ziba incurred insurance costs of $610, transportation costs of $920 and other incidental costs of $320 up to the Nakonde border post. Other incidental costs incurred in transporting the car from Nakonde to Lusaka amounted to $1,850.

At the date of entry into Zambia, the exchange rate provided by the Bank of Zambia and approved by the Commissioner General was K14.50 per US$1 while that approved by the Bureau de Change was K14.60 per US$1.

Required:

(i) Calculate the total import taxes paid by Tata Ziba on the importation of the car. (6 marks)

(ii) Explain any four (4) conditions that must be met for customs officers to use the transaction value method in valuing imported goods. (4 marks)

(iii) Explain the procedure to complete the customs clearance of a motor vehicle. (4 marks)

(b) Mazala Ltd is a Zambian resident company registered for VAT. It trades in stationery which is standard-rated for VAT purposes. During the month of June 2020, the company had a turnover of K4,520,000 (VAT exclusive). Purchases and other expenses amounted to K1,650,000 (VAT exclusive) and K725,800 (VAT inclusive) respectively.

On 2 June 2020, the company bought a Mitsubishi Pajero car and a Toyota Hilux van at a cost of K175,600 (VAT inclusive) and K285,700 (VAT inclusive) respectively. Petrol and diesel expenses amounted to K48,320 (VAT inclusive) and K71,500 (VAT inclusive) respectively.

Required:

(i) Calculate the amount of VAT payable for the month of June 2020, clearly showing whether input VAT will be recoverable or not on each of the above items. (7 marks)

(ii) State the date when the VAT you have calculated above, should have been paid, explaining the consequences of paying the VAT late. (2 marks)

(iii) Calculate the amount of any penalties payable on late payment of the VAT assuming Mazala Ltd paid the VAT for the month of June 2020, on 10 August 2020. (2 marks)

[Total: 25 Marks]

QUESTION FOUR

(a) Mata, Tata and Fata have been partners suppling timber and preparing accounts to 31 December annually. They share the profits in the ratio 5:3:2 respectively. On 31 December 2020, they ceased trading and sold all the business assets.

As at 1 January 2020 the partnership had the following assets:

	Cost	Income tax value
	K	K
Office equipment	100,000	50,000
Toyota Camry motor car	85,000	68,000
Toyota Hilux motor van	90,000	22,500
Nissan Hard Body motor van	80,000	20,000

Other information

(1) The Toyota Camry motor car was sold for K75,000, the Toyota Hilux Van was sold for K49,500, the Nissan Hard Body motor van was sold for K40,000 and the office equipment was sold for K120,000.

(2) The partnership's tax adjusted profit before capital allowances for the year ended 31 December 2020 is K750,200.

Required:

Calculate the amount of profits on which each partner will be assed for the tax year 2020. (7 marks)

(b) Zama Chartered Bank Plc is a national bank which is resident in the Republic of Zambia and is a subsidiary of ASSA Group Bank Plc, a multinational bank.

The statement of profit or loss of Zama Chartered Bank Plc for the year ended 31 December 2020 shows a net profit of K5,675,600 which was arrived at after accounting for the following:

1. General allowable administration expenses amounting to K825,000.
2. Staff canteen costs amounting to K62,400.
3. Loan losses previously written off recovered during the period of K242,900.
4. Depreciation of assets of K186,600.
5. Increase in specific provision of loan losses of K95,600.
6. Increase in general provision of loan losses of K679,000.
7. Fines for breach of banking laws amounting to K57,400.
8. Other income which included dividends from Zambian companies of K153,700 (gross), realised trading gains of K131,000, unrealised trading gains of K56,900 and royalties of K280,600 (gross).
9. Irrecoverable loans losses written off amounting to K867,000.
10. Costs in connection with acquisition of land of K74,300.
11. Donations to an approved public benefit organisation amounting to K34,700.
12. Donations to political parties amounting to K345,300.
13. Utilities and electricity expenses amounting to 78,500.
14. Purchase of office equipment at a cost of K395,600.

Transactions in capital assets

Zama Chartered Bank plc had the following transactions in capital assets during the period:

(1) On 1 April 2020, the company acquired and installed an ATM at a cost of K155,172 to be used wholly and exclusively for business purposes.
(2) The company purchased, on 24 May 2020, a motor car to be used as a pool car, with a cylinder capacity of 2,000cc at a cost of K232,000.
(3) On 22 May 2020, the company acquired a motor van with a cylinder capacity of 3,000cc, at a cost of K150,000 to be used wholly and exclusively for business purposes.
(4) On 1 October 2020, the company acquired a coin counting machine at a cost of K158,621 to be used for business purposes.

Other information

(1) There were five (5) differently abled persons employed by the company on a full time basis who are registered with Zambia Centre for Persons Living with Disabilities (ZCPLD). The company has accommodated them in company owned houses for which they pay no rent. The annual gross emoluments of each of the persons in the year ended 31 December 2020 was K91,520. The total salaries paid have been included in the general administration expenses.

(2) Provisional income tax paid by the company during the tax year 2020 amounted to K1,673,200.

Required:

Calculate the final amount of company income tax payable by Zama Chartered Bank Plc for the tax year 2020. (18 marks)

[Total: 25 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) COMPUTATION OF TAXABLE MINING PROFITS

	K'000	K'000	
Net profit as per accounts		305,100	
Less expenses			
Mineral royalty tax(W1)	75,240		
Depreciation	336		
Amortisation	144		
Drilling boreholes	1,600		
Construction of police post	600		
Donations to political party	60		
Personal to holder motor car benefit			
- Toyota land cruiser	40		
- Land Rover Discovery	30		
		78,050	
		383,150	
Less:			
Treasury bill interest	595		
Rental income	720		
Unrealised foreign exchange gains	470		
Capital allowances (W2)	2,432		
		(4,217)	
Taxable mining profits before loss relief		378,933	
Less Tax loss (W3)		(189,467)	(W)
Final taxable mining profit		189,466	

WORKING

(1) MINERAL ROYALTY

	K'000
Cobalt (K378 m x 8%)	30,240
Copper (K600 m x 7.5%)	45,000
	75,240

(2) BMC

COMPUTATION OF OTHER CAPITAL ALLOWANCES ON QUALIFYING EXPENDITURE

	K
Central Administration Offices	
Wear & tear allowance	
(K14,600,000 x 2%)	292,000
Mining equipment	
Wear & tear allowance	

(K2,400,000 x 20%)	480,000
Smelting plant	
Wear and tear allowance	320,000
(K1,600,000 x 20%)	
Pool cars	
Wear and tear allowance	
(K450,000 x 20%) x 4	360,000
Toyota land cruiser	
Wear & tear allowance	
K1,500,000 x 20%	300,000
Land Rover Discovery	
Wear & tear allowance	
(K1,200,000 x 20%)	240,000
Boreholes	
Wear & tear allowance	
(K1,600,000 x 20%)	320,000
Construction of police post	
Wear & tear allowance	
(K600,000 x20%)	120,000
	2,432,000

(3) Loss Relief

	K'000
Translated Loss b/f (US$60m x K13.50)	K810,000
Loss b/f Indexed	
[(1 + (14.50 – 13.50/13.50)] x K810m	870,000
Less loss relief	
(K378,933,000 x 50%)	(189,467)
Unrelieved tax loss at 31 Dec 2020	680,533

The profits are enough to offset the whole loss and the whole amount of the loss will be relieved. Therefore, the amount of loss to be relieved will be restricted to 50% of the taxable profits.

(b) BMC MINING

COMPANY INCOME TAX COMPUTATION FOR THE TAX YEAR 2020

	K'000
Taxable Mining profit	189,466
Treasury bill interest	
(K595,000 x100/85)	700
Total taxable business profit	190,166
Company income tax on mining profits	
(K189,466,000 x 30%)	56,840
Company income tax on treasury bill interest	
(K700,000 x 35%)	245
	57,085
Less Tax already paid	
WHT on Treasury Bill interest	
(K700,000 x 15%)	(105)
Company Income Tax payable	56,980

SOLUTION TWO

(a) The following are the taxation implications:

(i) Hire purchase

1. Hire purchase interest (difference between the cash price of the asset and total plan any deposit repayments) is an allowable deduction when computing the taxable business profits.
2. Capital allowances are claimable on the cash price of the qualifying asset.
3. Value added tax on the cash price of the asset is claimable provided the VAT is one which is recoverable.

(ii) Loan Finance

(1) Interest cost will not be an allowable expense when computing the taxable business profit of the company because the loan was used to finance the purchase of a non-current asset.
(2) Capital allowances will be claimable on the VAT exclusive cost of the non-current asset.
(3) The input VAT incurred on the purchase of the non-current asset will be claimable provided the VAT is one that is recoverable.

(iii) Finance lease

(1) Finance lease interest will be an allowable expense when computing the taxable business profits of the company.
(2) Capital allowances on the VAT exclusive cost of the asset will be claimable.
(3) The input VAT incurred on the purchase of the non-current asset will be claimable provided VAT is one that is recoverable.

(iv) Operating lease

(1) The operating lease rentals exclusive of VAT will be allowed when computing the taxable business profits of the company.
(2) No capital allowances will be claimable by the company on the leased non-current asset.
(3) The input VAT on operating lease rentals will be claimed by the company provided VAT is one which is recoverable.

(b) (i) YAKO FARMS LIMITED

COMPUTATION OF TAXABLE PROFITS FOR THE TAX YEAR 2020

	K	K
Profit before tax		4,625,000
Add:		
Depreciation	137,000	
Land acquisition costs	47,000	
Fines	87,000	
		271,000
		4,896,000
Less:		
Capital allowances	1,022,000	
Dividends from mining companies	75,000	
Dividends from non-listed companies	270,000	
Bank interest	45,000	
Interest on Government bonds	135,000	
		(1,547,000)
Tax adjusted profit		3,349,000

Workings

Capital allowances	K	
Capital allowances on farm implements and machinery (K145,000 x 100%)	145,000	
Storage facilities	475,000	
Development allowance: (K520,000 x 10%)	52,000	
Other capital allowances	350,000	
		1,022,000

(c) YAKO FARMS LIMITED

COMPANY INCOME TAX COMPUTATION FOR THE TAX YEAR 2020

	K
Tax on investment income (K45,000 +135,000) x 35%	63,000
Tax on farming profits (K3,349,000 x 10%)	334,900
	397,900
Less	
WHT on bank interest (K45,000 x 15%)	(6,750)
WHT on Interest on Government bonds (K135,000 x 15%)	(20,250)
Provisional income tax	(335,000)
Tax payable	35,900

SOLUTION THREE

(a) Tata Ziba

(i) Importation of the Vehicle

Value for duty purposes $

Cost 3,360 ½ Insurance

610

Freight charges 920

Other incidental costs 320

5,210

Exchange rate K14.50

VDP in Zambian kwacha 75,545

Value of the vehicle Import taxes

K K

Value for customs duty 75,545

Customs duty 16,545 16,545

92,090

Excise duty 21,508 21,508

113,598

Import VAT (16% x K113,598) 18,176 18,176

131,774

Total import taxes 56,229

(ii) The conditions are:

1. There should be no restriction to the use of goods.
2. There should be no condition to deter the determination of value for duty purpose (VDP).
3. No part of the proceed on resale would accrue to the seller, unless included in the value.
4. No relationship exists to influence the value.

(iii) The clearance procedure of the motor vehicle is:

1. Presentation of genuine import documents
2. Revaluation by customs if necessary
3. Payment of customs duty, excise duty, import VAT and processing fee
4. Processing of the declaration form CE20 by customs

(b) Value Added Tax

(i) Mazala Ltd

VAT payable for the quarter ended 30 June 2020

	K	K
Output Value Added Tax		
Sales (K4,520,000 X 16%)		723,200
Input Value Added Tax		
Purchases (K1,650,000 x 16%)	264,000	
Other expenses (K725,800 x 4/29)	100,110	
Motor car (irrecoverable)	0	
Motor van (K285,700 x 4/29)	39,407	
Petrol (irrecoverable)	0	
Diesel (K71,500 x 4/29) x 90%)	8,876	(412,393)
VAT payable		310,807

(ii) The VAT of K310,807 should have been paid not later than 18 July 2020. If the VAT is paid late penalties are charged at a rate of 0.5% of the VAT payable per day, plus interest on overdue tax at a rate of 2% above the Bank of Zambia discount rate. (2 mark)

(iii) Since the VAT should have been paid on 18 June 2020 but it was actually paid on 10 August 2020. This means that the VAT was paid late by 23 days. (1 mark)

Therefore, the penalty on late payment of VAT is K35,743 (K310,807 x 0.5% x 23 days).

SOLUTION FOUR

(a) MATA, TATA AND FATA
PARTNERSHIP'S CAPITAL ALLOWANCES COMPUTATION FOR THE TAX YEAR 2020

Cost/ITV	Capital allowances	
Equipment	K	K
Income Tax Value b/f	50,000	
Disposal (limited to original cost)	(100,000)	
Balancing charge		(50,000)
Toyota Camry Motor car		
Income Tax Value b/f	68,000	
Disposal	(75,000)	
Balancing charge		(7,000)
Toyota Hilux Van		
Income Tax Value b/f	22,500	
Disposal	(49,500)	
Balancing charge		(27,000)
Nissan Hard Body motor van		
Income Tax Value b/f	20,000	
Disposal	(40,000)	
Balancing charge		(20,000)
Total Balancing charge on plant and machinery		(104,000)

	Total	Mata	Tata	Fata
	K	K	K	K
Tax adjusted profits	750,200			
Add				
balancing charge	104,000			
Final taxable profits	854,200			
Share of profits (5:3:2)	854,200	427,100	256,260	170,840

(b) ZAMA CHARTERED BANK PLC COMPUTATION OF INCOME TAX PAYABLE FOR THE TAX YEAR 2020

	K	K
Profit for the period		5,675,600
Add:		
Canteen expenses	62,400	
General provision for loan losses	679,000	
Acquisition of land	74,300	
Donations to political parties	345,300	
Purchase of office equipment	395,600	
Free accommodation		
(30% x K91,520) x 5	137,280	
Fines for breach of banking laws	57,400	
Depreciation	186,600	
		1,937,880
		7,613480
Less:		
Disabled people (K1,000 X 5)	5,000	
Unrealised trading gains	56,900	
Capital allowances (workings)	262,348	
Dividends	153,700	
Royalties	280,600	
		(758,548)
Taxable profit		6,854,932

Income tax computation	K
Taxable profits	6,854,932
Add royalties	280,600
Total taxable income	7,135,532
Income tax K7,135,532 x 35%	2,497,436
Less:	
Provisional tax	(1,673,200)
WHT-Royalties K280,000 x 15%	(42,090)
Income tax payable	782,146

Workings

Computation of capital allowances	K
Pool Car	
Wear and tear allowance	
(K232,000 x 20%)	46,400
Motor Van	
Wear and tear allowance	
K150,000 x 25%	37,500
Office equipment	
Wear and tear allowance	
(K400,000 X 25%)	100,000
Coin counting machine	
Wear and tear allowance	
(K155,172 x 25%	39,655
ATM	
Wear and tear allowance	

K155,172 x 25%	38,793
Total capital allowances	262,348

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D3: BUSINESS TAXATION

WEDNESDAY 16 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question.

2. This paper consists of **FOUR (4)** questions of twenty five (25) marks each. You MUST attempt all the **FOUR (4)** questions.

3. Enter your student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. **Cell Phones** are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. You must write ALL your answers in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

10. A taxation table is provided on pages 2,3, 4,5 and 6 of this paper.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table

Income Tax

Standard personal income tax rates

Income band	Taxable amount	Rate
K1 to K39,600	first K39,600	0%
K39,601 to 49,200	next K9,600	25%
K49,201 to K74,400	next K25,200	30%
Over K74,400		37.5%

Income from farming for individuals

K1 to K39,600	first K39,600	0%
Over K39,600		10%

Company Income Tax rates

On income from manufacturing and other	35%
On income from farming	10%
On income of Banks and other Financial Institutions	35%
On income from mineral processing	30%
On income from mining operations	30%
On income from manufacture of products made out of copper cathodes	15%

Mineral Royalty

Mineral Royalty on Copper

Range of Norm Price	Mineral Royalty Rate
Less than US$4,500	5.5% of norm value
From US$4,500 to less than US$6,000	6.5% of norm value
From US$6,000 to less than US$7,500	7.5% of norm value
From US$7,500 to less than US$9,000	8.5% of norm value
From US$9,000 and above	10% of norm value

Mineral Royalty on other minerals

Type of mineral	Mineral Royalty Rate
Base Metals (Other than Copper, Cobalt and Vanadium)	5% of norm value
Cobalt and Vanadium	8% of norm value
Energy and Industrial Minerals	5% of gross value
Gemstones	6% of gross value
Precious Metals	6% of norm value

Capital Allowances

Implements, plant and machinery and commercial vehicles:

Wear and Tear Allowance –	Plant used normally	25%
	Used in Manufacturing and Leasing	50%
	Used in farming and agro-processing	100%
	Used in mining operations	20%

Non- commercial vehicles

Wear and Tear Allowance	20%

Industrial Buildings:

Wear and Tear Allowance	5%
Initial Allowance	10%
Investment Allowance	10%

Low Cost Housing **(Cost up to K20,000)**

Wear and Tear Allowance	10%
Initial Allowance	10%

Commercial Buildings

Wear and Tear Allowance	2%

Farming Allowances

Development Allowance	10%
Farm Works Allowance	100%
Farm Improvement Allowance	100%

Presumptive Taxes

Turnover Tax 4%

Presumptive Tax for Transporters

Seating capacity	**Tax per annum**	**Tax per day**
	K	K
From 64 passengers and over	10,800	29.60
From 50 to 63 passengers	9,000	24.70
From 36 to 49 passengers	7,200	19.70
From 22 to 35 passengers	5,400	14.80
From 18 to 21 passengers	3,600	9.90
From 12 to 17 passengers	1,800	4.90
Less than 12 passengers and taxis	900	2.40

Property Transfer Tax

Rate of Tax on Realised Value of Land, Land and Buildings and shares	5%
Rate of Tax on Realised Value on a transfer or sale of a mining right	10%
Rate of Tax on Realised Value on a transfer of Intellectual Property	5%

Value Added Tax

Registration threshold	K800,000
Standard Value Added Tax Rate (on VAT exclusive turnover)	16%

Customs and Excise duties on used motor vehicles

	Aged below 5 years		Aged 5 years and over	
Motor vehicles for the transport of ten or more persons, including the driver	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sitting capacity of 10 but not exceeding 14 persons including the driver	17,778	22,223	8,889	11,112
Sitting capacity exceeding 14 but not exceeding 32 persons	38,924	0	13,840	0
Sitting capacity of 33 but not exceeding 44 persons	86,497	0	19,462	0
Sitting capacity exceeding 44 persons	108,121	0	43,248	0

	Aged below 5 years		Aged 5 years and over	
Motor cars and other motor vehicles principally designed for the transport of persons including station wagons and racing cars	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sedans				
cylinder capacity not exceeding 1000 cc	12,490	10,824	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	16,058	13,917	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	16,545	21,508	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	10,528	13,687
Cylinder capacity exceeding 3000 cc	22,561	29,329	12,032	15,642
Hatchbacks				
cylinder capacity not exceeding 1000 cc	10,705	9,278	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	14,274	12,371	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	15,041	19,553	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	16,545	21,508	10,523	13,687
Cylinder capacity exceeding 3000 cc	19,553	25,419	12,032	15,642
Station wagons				
cylinder capacity not exceeding 2500 cc	16,545	21,508	9,024	11,731
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	13,357	17,598
Cylinder capacity exceeding 3000 cc but not exceeding 2500 cc	22,561	29,329	18,049	23,463

SUVs				
Cylinder capacity not exceeding 2500 cc	21,057	27,374	9,024	11,732
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	24,065	31,284	13,357	17,598
Cylinder capacity exceeding 3000 cc	28,577	37,150	18,049	23,463
	Aged below 5 years		**Aged 5 years and over**	
Motor vehicles for the transport of goods -with compression-ignition internal combustion piston engine (diesel or semi-diesel):	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Single cab				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	21,926	9,501	8,770	3,801
GVW exceeding 1.5 tonnes but not exceeding 3.0 tonnes	26,311	11,402	15,348	6,651
GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes	30,697	13,302	17,541	7,601
Double cabs GVW exceeding 3 tonnes but not exceeding 5 tonnes	30,274	0	24,119	10,452
Double cabs GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes, **with spark ignition internal combustion piston engine**	30,697	13,302	24,119	10,452
Panel Vans				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	15,348	6,651	8,770	3,801
GVW exceeding 1.5 tonnes but not exceeding 3.0 tonnes	17,541	7,601	15,348	6,651
GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes	21,926	9,501	17,541	7,601
Trucks				
GVW up to 2 tonnes	21,926	9,501	10,963	4,751
GVW exceeding 2.0 tonnes but not exceeding 5.0 tonnes	28,504	12,352	13,156	5,701
GVW exceeding 5.0 tonnes but not exceeding 10.0 tonnes	24,724	18,955	10,817	8,293
GVW exceeding 10.0 tonnes but not exceeding 20.0 tonnes	30,905	23,694	11,744	9,004
GVW exceeding 20 tonnes	51,898	0	19,461	0
GVW exceeding 20 tonnes, **with spark ignition internal combustion piston engine**	37,086	28,432	13,907	10,662

Surtax

On all motor vehicles aged more than five (5) years from year of manufacture K2,000

Customs and Excise on New Motor vehicles

Duty rates on:

1. Motor cars and other motor vehicles (including station wagons) principally designed for the transport of less than ten persons, including the driver:

Customs Duty:	
Percentage of Value for Duty Purposes	30%
Minimum Specific Customs Duty	K6,000
Excise Duty:	
Percentage of Value for Duty Purposes for Excise Duty Purposes	
Cylinder capacity of 1500 cc and less	20%
Cylinder Capacity of more than 1500 cc	30%

2. Pick-ups and trucks/lorries with gross weight not exceeding 20 tones:

Customs Duty	
Percentage of Value for Duty Purposes	15%
Minimum specific Customs Duty	K6,000
Excise Duty:	
Percentage of Value for Duty Purposes for Excise Duty Purposes	10%

3. Buses/coaches for the transport of more than ten persons

Customs Duty:	
Percentage of Value for Duty Purposes	15%
Minimum Specific Customs Duty	K6,000
Excise Duty:	
Percentage of Value for Duty Purposes for Excise Duty Purposes	
Seating Capacity of 16 persons and less	25%
Seating Capacity of 16 persons and more	0%

4. **Trucks/lorries with gross weight exceeding 20 tonnes**

Customs Duty:	
Percentage of Value for Duty Purposes	15%
Excise Duty:	
Percentage of Value for Duty Purposes for Excise Duty Purposes	0%

Attempt all FOUR (4) questions.

<u>QUESTION ONE</u>

The following summarised statement of profit or loss for the year ended 31 December 2020, has been extracted from the financial statements of BMC Mining Corporation, a Zambian resident subsidiary of a foreign based Multinational Mining company. BMC is engaged in mining operations of base metals. The group maintains its accounts in US dollars.

BMC MINING CORPORATION
STATEMENT OF PROFIT OR LOSS FOR THE YEAR ENDED 30 DECEMBER 2020

	Note	K
Revenue	(1)	978,000,000
Cost of sales		(450,240,000)
Gross profit		527,760,000
Operating expenses	(2)	(224,445,000)
Investment income	(3)	1,785,000
Profit for the year		305,100,000

The following additional information is available:

(8) This comprises sales of cobalt for the year amounting to K378,000,000 being the norm value of the mineral, with the remaining balance of the sales representing the norm value of copper sold during the year based on London Metal Exchange cash price which ranged between $6,100 and $6,900 per metric tonne throughout tax year 2020.

(9) Included in operating expenses, is mineral royalty tax paid by the company during the year which was computed correctly and paid on the relevant due dates. Also included in operating expenses are depreciation charges of K336,000, amortisation of intangible assets of K144,000, mineral transportation costs of K6,600,000, expenditure on drilling boreholes for the local mining community of K1,600,000, expenditure on construction of a police post in the local mining township of K600,000, donations to political parties of K60,000, donations to approved public benefit organisations of K350,000 and staff salaries of K160,080,000. The balance represents miscellaneous allowable operating expenses.

(10) Investment income includes treasury bill interest of K595,000 (net) rental income of K720,000 (net) and unrealised foreign exchange gains of a capital nature of K470,000.

(11) There were no implements plant and machinery qualifying for capital allowances at 1 January 2020, however, the company incurred the following expenditure and acquired the following assets locally from Zambian resident suppliers:

Expenditure	*Cost*
	K
Construction of new central administration offices	14,600,000
Purchase of mining equipment	2,400,000
Construction of new smelting plant	1,600,000
Purchase of four (4) Pool cars at a cost of (K450,000 each)	1,800,000
Purchase of a 4,700cc Toyota Land Cruiser (GXL)	1,500,000
Purchase of a 2,700cc Land Rover Discovery	1,200,000

The Toyota Land cruiser (GXL) is provided to the Chief Executive Officer on a personal to holder basis, while the Land Rover Discovery is provided to the Chief Finance Officer on a personal to holder basis. The private use by each executive of each vehicle is 40%.

(12) The company incurred a tax adjusted mining loss of US$60 million in the year ended 31 December 2019.

(13) Mining losses can be indexed using the following formula:

$$1+\frac{(R_2-R_1)}{R_1} \text{ x Tax loss brought forward}$$

(14) The following Zambian Kwacha per US Dollar (K/US$) average mid exchange rates have been provided and approved by the Commissioner General:

Accounting Period	*Average BOZ Mid Exchange rate*
	K/US$
Y/e 31 December 2019	13.50
Y/e 31 December 2020	14.50

Required:

(c) Compute the taxable mining profits for the tax year 2020, and show the amount of the tax loss remaining unrelieved at 31 December 2020. (20 marks)

(d) Calculate the total income tax payable by the company for the tax year 2020. (5 marks)

[Total: 25 Marks]

QUESTION TWO

Yako Farms Limited (YFL) is a Zambian resident company engaged in farming operations. The company currently sells all of its farm produce domestically but is considering exporting some of its produce to neighbouring countries. To do this, it needs to acquire more non-current assets either by hire purchase, loan finance, finance lease or operating lease. The company is registered for Value Added Tax.

The summarised statement of profit or loss for the year ended 31 December 2020 is shown below:

		K
Turnover		12,650,000
Cost of sales		(6,150,000)
Gross profit		6,500,000
Operating expenses	(Note 1)	(1,950,000)
Finance cost		(450,000)
Investment income	(Note 2)	525,000
Profit before tax		4,625,000

The following information is relevant:

(6) Operating expenses include depreciation charges of K137,000, pasture maintenance costs of K165,000, expenditure on destruction of weeds, plants and animal pests detrimental to the land of K230,000, costs associated with the acquisition of new farm land of K47,000, staff salaries of K960,000 and fines for breach of labour regulations of K87,000. The balance represents general business expenses which are all allowable for tax purposes.

(7) The company earned the following gross investment income in the tax year 2020, which has been included under investment income in the statement of profit or loss shown above, withholding tax has already been paid:

		K
Dividends from non-listed Zambian company		270,000
Dividends from Zambian mining companies	75,000	
Bank deposit interest	45,000	
Interest on Government bonds		135,000

(8) The following capital expenditure incurred by the company in the tax year 2020, was not recorded in the financial statements:

	K
Construction of Storage Facilities	475,000
Purchase of farm implements and machinery	145,000
Rose flower plantation development costs	520,000

(9) Capital allowances on other qualifying assets have been agreed at K350,000.

(10) Provisional income tax of K335,000 was paid during the tax year 2020.

Required:

(d) Explain the Income Tax and Value Added Tax implications of financing the purchase of non-current assets using the following options:

(v) Hire purchase (3 marks)
(vi) Loan finance (3 marks)
(vii) Finance lease (3 marks)
(viii) Operating lease (3 marks)

(e) Calculate the adjusted taxable profit for Yako Farms Limited for the tax year 2020. (8 marks)

(f) Calculate the company income tax payable by Yako Farms Limited for the tax year 2020. (5 marks)

[Total: 25 Marks]

QUESTION THREE

(c) Tata Ziba, a sole trader, imported a second hand, 1900 cc Toyota Corolla (Sedan) car on 21 January 2020. The car was manufactured in Japan in January 2018. The cost of the car was $3,360. Tata Ziba incurred insurance costs of $610, transportation costs of $920 and other incidental costs of $320 up to the Nakonde border post. Other incidental costs incurred in transporting the car from Nakonde to Lusaka amounted to $1,850.

At the date of entry into Zambia, the exchange rate provided by the Bank of Zambia and approved by the Commissioner General was K14.50 per US$1 while that approved by the Bureau de Change was K14.60 per US$1.

Required:

(iv) Calculate the total import taxes paid by Tata Ziba on the importation of the car. (6 marks)

(v) Explain any four (4) conditions that must be met for customs officers to use the transaction value method in valuing imported goods. (4 marks)

(vi) Explain the procedure to complete the customs clearance of a motor vehicle. (4 marks)

(d) Mazala Ltd is a Zambian resident company registered for VAT. It trades in stationery which is standard-rated for VAT purposes. During the month of June 2020, the company had a turnover of K4,520,000 (VAT exclusive). Purchases and other expenses amounted to K1,650,000 (VAT exclusive) and K725,800 (VAT inclusive) respectively.

On 2 June 2020, the company bought a Mitsubishi Pajero car and a Toyota Hilux van at a cost of K175,600 (VAT inclusive) and K285,700 (VAT inclusive) respectively. Petrol and diesel expenses amounted to K48,320 (VAT inclusive) and K71,500 (VAT inclusive) respectively.

Required:

(iv) Calculate the amount of VAT payable for the month of June 2020, clearly showing whether input VAT will be recoverable or not on each of the above items. (7 marks)

(v) State the date when the VAT you have calculated above, should have been paid, explaining the consequences of paying the VAT late. (2 marks)

(vi) Calculate the amount of any penalties payable on late payment of the VAT assuming Mazala Ltd paid the VAT for the month of June 2020, on 10 August 2020. (2 marks)

[Total: 25 Marks]

QUESTION FOUR

(c) Mata, Tata and Fata have been partners suppling timber and preparing accounts to 31 December annually. They share the profits in the ratio 5:3:2 respectively. On 31 December 2020, they ceased trading and sold all the business assets.

As at 1 January 2020 the partnership had the following assets:

	Cost	Income tax value
	K	K
Office equipment	100,000	50,000

Toyota Camry motor car	85,000	68,000
Toyota Hilux motor van	90,000	22,500
Nissan Hard Body motor van	80,000	20,000

Other information

(3) The Toyota Camry motor car was sold for K75,000, the Toyota Hilux Van was sold for K49,500, the Nissan Hard Body motor van was sold for K40,000 and the office equipment was sold for K120,000.

(4) The partnership's tax adjusted profit before capital allowances for the year ended 31 December 2020 is K750,200.

Required:

Calculate the amount of profits on which each partner will be assed for the tax year 2020.
(7 marks)

(d) Zama Chartered Bank Plc is a national bank which is resident in the Republic of Zambia and is a subsidiary of ASSA Group Bank Plc, a multinational bank.

The statement of profit or loss of Zama Chartered Bank Plc for the year ended 31 December 2020 shows a net profit of K5,675,600 which was arrived at after accounting for the following:

15. General allowable administration expenses amounting to K825,000.
16. Staff canteen costs amounting to K62,400.
17. Loan losses previously written off recovered during the period of K242,900.
18. Depreciation of assets of K186,600.
19. Increase in specific provision of loan losses of K95,600.
20. Increase in general provision of loan losses of K679,000.
21. Fines for breach of banking laws amounting to K57,400.
22. Other income which included dividends from Zambian companies of K153,700 (gross), realised trading gains of K131,000, unrealised trading gains of K56,900 and royalties of K280,600 (gross).
23. Irrecoverable loans losses written off amounting to K867,000.
24. Costs in connection with acquisition of land of K74,300.
25. Donations to an approved public benefit organisation amounting to K34,700.
26. Donations to political parties amounting to K345,300.
27. Utilities and electricity expenses amounting to 78,500.

28. Purchase of office equipment at a cost of K395,600.

Transactions in capital assets

Zama Chartered Bank plc had the following transactions in capital assets during the period:

(5) On 1 April 2020, the company acquired and installed an ATM at a cost of K155,172 to be used wholly and exclusively for business purposes.
(6) The company purchased, on 24 May 2020, a motor car to be used as a pool car, with a cylinder capacity of 2,000cc at a cost of K232,000.
(7) On 22 May 2020, the company acquired a motor van with a cylinder capacity of 3,000cc, at a cost of K150,000 to be used wholly and exclusively for business purposes.
(8) On 1 October 2020, the company acquired a coin counting machine at a cost of K158,621 to be used for business purposes.

Other information

(3) There were five (5) differently abled persons employed by the company on a full time basis who are registered with Zambia Centre for Persons Living with Disabilities (ZCPLD). The company has accommodated them in company owned houses for which they pay no rent. The annual gross emoluments of each of the persons in the year ended 31 December 2020 was K91,520. The total salaries paid have been included in the general administration expenses.
(4) Provisional income tax paid by the company during the tax year 2020 amounted to K1,673,200.

Required:

Calculate the final amount of company income tax payable by Zama Chartered Bank Plc for the tax year 2020. (18 marks)

[Total: 25 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(c) COMPUTATION OF TAXABLE MINING PROFITS

	K'000	K'000	
Net profit as per accounts		305,100	
Less expenses			
Mineral royalty tax(W1)	75,240		
Depreciation	336		
Amortisation	144		
Drilling boreholes	1,600		
Construction of police post	600		
Donations to political party	60		
Personal to holder motor car benefit			
- Toyota land cruiser	40		
- Land Rover Discovery	30		
		78,050	
		383,150	
Less:			
Treasury bill interest	595		
Rental income	720		
Unrealised foreign exchange gains	470		
Capital allowances (W2)	2,432		
		(4,217)	
Taxable mining profits before loss relief		378,933	
Less Tax loss (W3)		(189,467)	(W)
Final taxable mining profit		189,466	

WORKING

(4) MINERAL ROYALTY

	K'000
Cobalt (K378 m x 8%)	30,240
Copper (K600 m x 7.5%)	45,000
	75,240

(5) BMC

COMPUTATION OF OTHER CAPITAL ALLOWANCES ON QUALIFYING EXPENDITURE

K

Central Administration Offices

Wear & tear allowance

(K14,600,000 x 2%)	292,000
Mining equipment	
Wear & tear allowance	
(K2,400,000 x 20%)	480,000
Smelting plant	
Wear and tear allowance	320,000
(K1,600,000 x 20%)	
Pool cars	
Wear and tear allowance	
(K450,000 x 20%) x 4	360,000
Toyota land cruiser	
Wear & tear allowance	
K1,500,000 x 20%	300,000
Land Rover Discovery	
Wear & tear allowance	
(K1,200,000 x 20%)	240,000
Boreholes	
Wear & tear allowance	
(K1,600,000 x 20%)	320,000
Construction of police post	
Wear & tear allowance	
(K600,000 x20%)	120,000
	2,432,000

(6) Loss Relief

	K'000
Translated Loss b/f (US$60m x K13.50)	K810,000
Loss b/f Indexed	
[(1 + (14.50 – 13.50/13.50)] x K810m	870,000
Less loss relief	
(K378,933,000 x 50%)	(189,467)
Unrelieved tax loss at 31 Dec 2020	680,533

The profits are enough to offset the whole loss and the whole amount of the loss will be relieved. Therefore, the amount of loss to be relieved will be restricted to 50% of the taxable profits.

(d) BMC MINING

COMPANY INCOME TAX COMPUTATION FOR THE TAX YEAR 2020

	K'000
Taxable Mining profit	189,466
Treasury bill interest	
(K595,000 x100/85)	700
Total taxable business profit	190,166
Company income tax on mining profits	
(K189,466,000 x 30%)	56,840
Company income tax on treasury bill interest	
(K700,000 x 35%)	245
	57,085
Less Tax already paid	
WHT on Treasury Bill interest	
(K700,000 x 15%)	(105)
Company Income Tax payable	56,980

SOLUTION TWO

(d) The following are the taxation implications:

(v) Hire purchase

4. Hire purchase interest (difference between the cash price of the asset and total plan any deposit repayments) is an allowable deduction when computing the taxable business profits.
5. Capital allowances are claimable on the cash price of the qualifying asset.
6. Value added tax on the cash price of the asset is claimable provided the VAT is one which is recoverable.

(vi) Loan Finance

(4) Interest cost will not be an allowable expense when computing the taxable business profit of the company because the loan was used to finance the purchase of a non-current asset.
(5) Capital allowances will be claimable on the VAT exclusive cost of the non-current asset.
(6) The input VAT incurred on the purchase of the non-current asset will be claimable provided the VAT is one that is recoverable.

(vii) Finance lease

(4) Finance lease interest will be an allowable expense when computing the taxable business profits of the company.
(5) Capital allowances on the VAT exclusive cost of the asset will be claimable.
(6) The input VAT incurred on the purchase of the non-current asset will be claimable provided VAT is one that is recoverable.

(viii) Operating lease

(4) The operating lease rentals exclusive of VAT will be allowed when computing the taxable business profits of the company.
(5) No capital allowances will be claimable by the company on the leased non-current asset.
(6) The input VAT on operating lease rentals will be claimed by the company provided VAT is one which is recoverable.

(e) (i) YAKO FARMS LIMITED

COMPUTATION OF TAXABLE PROFITS FOR THE TAX YEAR 2020

	K	K
Profit before tax		4,625,000
Add:		
Depreciation	137,000	
Land acquisition costs	47,000	
Fines	87,000	271,000
		4,896,000
Less:		
Capital allowances	1,022,000	
Dividends from mining companies	75,000	
Dividends from non-listed companies	270,000	
Bank interest	45,000	
Interest on Government bonds	135,000	(1,547,000)
Tax adjusted profit		3,349,000

Workings

Capital allowances	K	
Capital allowances on farm implements and machinery (K145,000 x 100%)	145,000	
Storage facilities	475,000	
Development allowance: (K520,000 x 10%)	52,000	
Other capital allowances	350,000	
		1,022,000

(f) YAKO FARMS LIMITED

COMPANY INCOME TAX COMPUTATION FOR THE TAX YEAR 2020

	K	K
Tax on investment income (K45,000 +135,000) x 35%	63,000	
Tax on farming profits (K3,349,000 x 10%)	334,900	
		397,900
Less		
WHT on bank interest (K45,000 x 15%)	(6,750)	
WHT on Interest on Government bonds (K135,000 x 15%)	(20,250)	
Provisional income tax	(335,000)	
Tax payable		35,900

SOLUTION THREE

(c) Tata Ziba

(iv) Importation of the Vehicle

Value for duty purposes $
Cost 3,360 ½ Insurance
610
Freight charges 920
Other incidental costs 320
5,210
Exchange rate K14.50
VDP in Zambian kwacha 75,545

	Value of the vehicle K	Import taxes K
Value for customs duty	75,545	
Customs duty	16,545	16,545
	92,090	
Excise duty	21,508	21,508
	113,598	
Import VAT (16% x K113,598)	18,176	18,176
	131,774	
Total import taxes		56,229

(v) The conditions are:

5. There should be no restriction to the use of goods.
6. There should be no condition to deter the determination of value for duty purpose (VDP).
7. No part of the proceed on resale would accrue to the seller, unless included in the value.
8. No relationship exists to influence the value.

(vi) The clearance procedure of the motor vehicle is:

5. Presentation of genuine import documents
6. Revaluation by customs if necessary
7. Payment of customs duty, excise duty, import VAT and processing fee
8. Processing of the declaration form CE20 by customs

(d) Value Added Tax

(iv) Mazala Ltd

VAT payable for the quarter ended 30 June 2020

	K	K
Output Value Added Tax		
Sales (K4,520,000 X 16%)		723,200
Input Value Added Tax		
Purchases (K1,650,000 x 16%)	264,000	
Other expenses (K725,800 x 4/29)	100,110	
Motor car (irrecoverable)	0	
Motor van (K285,700 x 4/29)	39,407	
Petrol (irrecoverable)	0	
Diesel (K71,500 x 4/29) x 90%)	8,876	
		(412,393)
VAT payable		310,807

(v) The VAT of K310,807 should have been paid not later than 18 July 2020. If the VAT is paid late penalties are charged at a rate of 0.5% of the VAT payable per day, plus interest on overdue tax at a rate of 2% above the Bank of Zambia discount rate. (2 mark)

(vi) Since the VAT should have been paid on 18 June 2020 but it was actually paid on 10 August 2020. This means that the VAT was paid late by 23 days. (1 mark)

Therefore, the penalty on late payment of VAT is K35,743 (K310,807 x 0.5% x 23 days).

SOLUTION FOUR

(c) MATA, TATA AND FATA

PARTNERSHIP'S CAPITAL ALLOWANCES COMPUTATION FOR THE TAX YEAR 2020

Cost/ITV	Capital allowances	
Equipment	K	K
Income Tax Value b/f	50,000	
Disposal (limited to original cost)	(100,000)	
Balancing charge		(50,000)
Toyota Camry Motor car		
Income Tax Value b/f	68,000	
Disposal	(75,000)	
Balancing charge		(7,000)
Toyota Hilux Van		
Income Tax Value b/f	22,500	
Disposal	(49,500)	
Balancing charge		(27,000)
Nissan Hard Body motor van		
Income Tax Value b/f	20,000	
Disposal	(40,000)	
Balancing charge		(20,000)
Total Balancing charge on plant and machinery		(104,000)

	Total	Mata	Tata	Fata
	K	K	K	K
Tax adjusted profits	750,200			
Add balancing charge	104,000			
Final taxable profits	854,200			
Share of profits (5:3:2)	854,200	427,100	256,260	170,840

(d) ZAMA CHARTERED BANK PLC COMPUTATION OF INCOME TAX PAYABLE FOR THE TAX YEAR 2020

	K	K
Profit for the period		5,675,600
Add:		
Canteen expenses	62,400	
General provision for loan losses	679,000	
Acquisition of land	74,300	
Donations to political parties	345,300	
Purchase of office equipment	395,600	
Free accommodation		
(30% x K91,520) x 5	137,280	
Fines for breach of banking laws	57,400	
Depreciation	186,600	
		1,937,880
		7,613480
Less:		
Disabled people (K1,000 X 5)	5,000	
Unrealised trading gains	56,900	
Capital allowances (workings)	262,348	
Dividends	153,700	
Royalties	280,600	
		(758,548)
Taxable profit		6,854,932

Income tax computation	K
Taxable profits	6,854,932
Add royalties	280,600
Total taxable income	7,135,532
Income tax K7,135,532 x 35%	2,497,436
Less:	
Provisional tax	(1,673,200)
WHT-Royalties K280,000 x 15%	(42,090)
Income tax payable	782,146

Workings

Computation of capital allowances	K
Pool Car	
Wear and tear allowance	
(K232,000 x 20%)	46,400
Motor Van	
Wear and tear allowance	
K150,000 x 25%	37,500
Office equipment	

Wear and tear allowance	
(K400,000 X 25%)	100,000
Coin counting machine	
Wear and tear allowance	
(K155,172 x 25%	39,655
ATM	
Wear and tear allowance	
K155,172 x 25%	38,793
Total capital allowances	262,348

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D4: PERSONAL TAXATION

TUESDAY 15 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading. Use it to study the examination paper carefully so that you understand what to do in each question. You will be told when to start writing.
2. This question paper consists of **FOUR (4)** questions of twenty Five (25) marks each. You MUST attempt all the **FOUR (4)** questions.
3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must NOT appear anywhere on your answer booklet.
4. Do **NOT** write in pencil (except for graphs and diagrams).
5. **Cell phones** are **NOT** allowed in the Examination Room.
6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.
7. All workings must be done in the answer booklet.
8. Present legible and tidy work.
9. Graph paper (if required) is provided at the end of the answer booklet.
10. A Taxation table is provided on pages 2 and 3

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table for paper D4– Personal Taxation (June and December 2020 Examinations)

Income Tax

Standard personal income tax rates

Income band	Taxable amount	Rate
K1 to K39,600	first K39,600	0%
K39,601 to 49,200	next K9,600	25%
K49,201 to K74,400	next K25,200	30%
Over K74,400		37.5%

Income from farming for individuals

K1 to K39,600	first K39,600	0%
Over K39,600		10%

Company Income Tax rates

On income from manufacturing and other	35%
On income from farming	10%
On income of Banks and other Financial Institutions	35%
On income from mineral processing	30%
On income from mining operations	30%

Mineral Royalty

Mineral Royalty on Copper

Range of Norm Price	Mineral Royalty Rate
Less than US$4,500	5.5% of norm value
From US$4,500 to less than US$6,000	6.5% of norm value
From US$6,000 to less than US$7,500	7.5% of norm value
From US$7,500 to less than US$9,000	8.5% of norm value
From US$9,000 and above	10% of norm value

Mineral Royalty on other minerals

Type of mineral	Mineral Royalty Rate
Base Metals (Other than Copper, Cobalt and Vanadium)	5% on norm value
Cobalt and Vanadium	8% of norm value
Energy and Industrial Minerals	5% on gross value
Gemstones	6% on gross value
Precious Metals	6% on norm value

Capital Allowances

Implements, plant and machinery and commercial vehicles:

Wear and Tear Allowance –	Plant used normally	25%
	Used in Manufacturing and Leasing	50%
	Used in farming and agro-processing	100%

Non- commercial vehicles

Wear and Tear Allowance	20%

Industrial Buildings:

Wear and Tear Allowance	5%
Initial Allowance	10%
Investment Allowance	10%

Low Cost Housing **(Cost up to K20,000)**

Wear and Tear Allowance	10%
Initial Allowance	10%

Commercial Buildings

Wear and Tear Allowance	2%

Farming Allowances

Development Allowance	10%
Farm Works Allowance	100%
Farm Improvement Allowance	100%

Presumptive Taxes

Turnover Tax 4%

Presumptive Tax for Transporters

Seating capacity	**Tax per annum**	**Tax per day**
	K	K
From 64 passengers and over	10,800	29.60
From 50 to 63 passengers	9,000	24.70
From 36 to 49 passengers	7,200	19.70
From 22 to 35 passengers	5,400	14.80
From 18 to 21 passengers	3,600	9.90
From 12 to 17 passengers	1,800	4.90
Less than 12 passengers and taxis	900	2.50

Property Transfer Tax

Rate of Tax on Realised Value of Land, Land and Buildings and shares	5%
Rate of Tax on Realised Value on a transfer or sale of a mining right	10%
Rate of Tax on Realised Value on a transfer of Intellectual Property	5%

Value Added Tax

Registration threshold	K800,000
Standard Value Added Tax Rate (on VAT exclusive turnover)	16%

Customs and Excise
Customs and Excise duties on used motor vehicles

Motor vehicles for the transport of ten or more persons, including the driver	**Aged 2 to 5 years Customs duty K**	**Excise duty K**	**Aged over 5 years Customs duty K**	**Excise duty K**
Sitting capacity of 10 but not exceeding 14 persons including the driver	17,778	22,223	8,889	11,112
Sitting capacity exceeding 14 but not exceeding 32 persons	38,924	0	13,840	0
Sitting capacity of 33 but not exceeding 44 persons	86,497	0	19,462	0
Sitting capacity exceeding 44 persons	108,121	0	43,248	0

Motor cars and other motor vehicles principally designed for the transport of persons including station wagons and racing cars	**Aged 2 to 5 years Customs duty K**	**Excise duty K**	**Aged over 5 years Customs duty K**	**Excise duty K**
Sedans				
cylinder capacity not exceeding 1000 cc	12,490	10,824	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	16,058	13,917	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	16,545	21,508	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	10,528	13,687
Cylinder capacity exceeding 3000 cc	22,561	29,329	12,032	15,642
Hatchbacks				
cylinder capacity not exceeding 1000 cc	10,705	9,278	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	14,274	12,371	8,564	7,422

Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	15,041	19,553	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	16,545	21,508	10,523	13,687
Cylinder capacity exceeding 3000 cc	19,553	25,419	12,032	15,642
Station wagons				
cylinder capacity not exceeding 2500 cc	16,545	21,508	9,024	11,731
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	13,357	17,598
Cylinder capacity exceeding 3000 cc but not exceeding 2500 cc	22,561	29,329	18,049	23,463
SUVs				
Cylinder capacity not exceeding 2500 cc	21,057	27,374	9,024	11,732
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	24,065	31,284	13,357	17,598
Cylinder capacity exceeding 3000 cc	28,577	37,150	18,049	23,463

	Aged 2 to 5 years		**Aged over 5 years**	
Motor vehicles for the transport of goods – with compression-ignitioninternal combustion piston engine (diesel or semi-diesel):	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Single cab				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	21,926	9,501	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	26,311	11,402	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	30,697	13,302	17,541	7,601
Double cabs GVW exceeding 3 tonnes but not exceeding 5 tonnes	30,274	0	24,119	10,452
Double cabs GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes, **with spark ignition internal combustion piston engine**	30,697	13,302	24,119	10,452
Panel Vans				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	15,348	6,651	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	17,541	7,601	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	21,926	9,501	17,541	7,601
Trucks				
GVW up to 2 tonnes	21,926	9,501	10,963	4,751
GVW exceeding 2.0 tonnes but not exceeding 5.0 tonnes	28,504	12,352	13,156	5,701

GVW exceeding 5.0 tonnesbut not exceeding 10.0 tonnes	24,724	18,955	10,817	8,293
GVW exceeding 10.0 tonnesbut not exceeding 20.0 tonnes	30,905	23,694	11,744	9,004
GVW exceeding 20 tonnes	51,898	0	19,461	0
GVW exceeding 20 tonnes, **with spark ignition internal combustion piston engine**	37,086	28,432	13,907	10,662

Customs and excise duty on new vehicles

1 Motor cars and other motor vehicles (including station wagons) principally designed for the transport of less than ten persons, including the driver:

Customs duty:	30%
Excise duty:	
Cylinder capacity of 1500 cc and less	20%
Cylinder capacity of more than 1500 cc	30%

2 Pick-ups and trucks/lorries with gross weight not exceeding 20 tonnes:

Customs duty	15%
Excise duty	10%

3 Buses/coaches for the transport of more than ten persons

Customs duty:	15%
Excise duty:	
Seating capacity of 16 persons and less	25%
Seating capacity of 16 persons and more	0%

4 Trucks/lorries with gross weight exceeding 20 tonnes

Customs duty:	15%
Excise duty:	0%

The minimum amount of customs duty on motor vehicles is K6,000.

Import VAT is added to the sum of VDP, customs duty and excise duty. It is determined at the standard rate of 16%

ATTEMPT ALL THE FOUR (4) QUESTIONS

QUESTION ONE

(a) Explain why it is important to distinguish between employed and self-employed for income tax and NAPSA contributions purposes. (5 marks)

(b) **For the purposes of this question assume that today's date is 31 December 2020**

Ahmed was born in an Asian country in 1980. He has always lived in that Asian country, where he is also domiciled and has been employed by Exen International. On 1 October 2020, Exen International acquired 100% of the ordinary share capital of Exotic Zambia Ltd, a company incorporated and resident in Zambia. Ahmed was immediately appointed the Chief Executive Officer for Exen Zambia Limited, on a three-year contract commencing on that date, to oversee the smooth transition and integration of the company into the group, after which he will relocate back to his home country in Asia permanently.

Ahmed arrived in Zambia to take the position on 1 October 2020. His annual salary was K720,000. He was accommodated in a company owned house with a market value of K1,800,000, which can be let out for commercial rentals of K6,000 per month. The company paid for the expenses in relation to the house which included electricity bills amounting to K1,200 per month, house keeper's wages of K3,000 per month, and security services for the house which amounted to K5,000 per month.

He was provided with a personal to holder motor car with a cylinder capacity of 3000cc, which the company acquired at a cost of K650,000 in October 2020. The company also paid for all the motor car running expenses which amounted to K4,500 per month.

Ahmed is further entitled to a monthly entertainment allowance of K2,000 and the company paid his golf club subscriptions of K2,500 and his membership fee to a local fitness gym of K1,000 per month.

On arrival in Zambia, Ahmed immediately made some investments in Government of Zambia Bonds and in fixed deposit accounts with Zambian banks, from which he generated Government bond interest of K17,000 and fixed deposit interest of K5,000 by 31 December 2020. These were the actual amounts received by Ahmed in each case.

Ahmed holds various investments in his home country in Asia. These include properties that are let out on a commercial basis in the Asian country, shares in the companies that are resident in the Asian country and debentures of companies' resident in the Asian country. On 31 December 2020, the following investment income was credited to his Zambian bank account in respect of these investments:

Dividends	K27,900
Rental income from property let out in the Asian country	K74,400
Debenture interest	K48,000

The amount of the dividends and rental income were net of withholding tax at the rate of 38% deducted in the foreign country and the amount of the debenture interest was net of withholding tax at the rate of 20% deducted in the foreign country.

Required:

(i) Explain giving reasons, why Ahmed will be regarded as being resident and ordinarily resident in Zambia in the tax year 2020. (3 marks)

(ii) Compute the amount of income tax payable, payable by Almed for the tax year 2020. (17 marks)

[Total: 25 Marks]

QUESTION TWO

A share option scheme is a scheme under which the employer grants options to employees to buy shares in that employer's company in future. Employees can either exercise the options or allow them to lapse once the options vest. There are tax benefits for both the employer and the employee where such a scheme is approved for tax purposes. However, such benefits do not normally apply where the share option scheme being operated by the employer is not approved for tax purposes.

Required:

(a) Explain the meaning of the following terms in the context of employee share option schemes:

(i) Exercise or strike price (2 marks)
(ii) Exercising the options (2 marks)
(iii) Lapse of options (2 marks)

(b) Explain the tax consequences to an employee arising on the grant of share options, exercising the option and subsequent sale of any shares in a share option scheme established by an employer which is not approved for tax purposes. (6 marks)

(c) Describe the procedure a company must follow to have a share option scheme approved for tax purposes. (3 marks)

(d) Explain any **six (6)** conditions that must be met for a share option scheme to be approved for tax purposes. (6 marks)

(e) Explain any four (4) benefits for both the employee and employer of an approved share option scheme. (4 marks)

[Total: 25 Marks]

QUESTION THREE

Assume that today's date is 31 December 2019 for the purpose of this question:

(a) Kunda is contemplating starting a public passenger transportation business on 1 January 2020. He intends to buy six (6) buses, each with a sitting capacity of seventy-eight (78) passengers, at a cost of K450,000 each. He estimates that the daily takings will be K800 per day, for six (6) working days per week, for four weeks per month, throughout the tax year 2020.
He will employ six (6) employees that will be paid a monthly salary of K3,000 each. Each driver will pay NAPSA contribution of 5% of the monthly salary and Kunda will also contribute 5% of each driver's salary as NAPSA contribution.
The bus running expenses will average K2,500 for each bus per month.

Required:

(i) Explain the types of persons that are required to pay presumptive taxes and the types of persons who are exempt from presumptive taxes for transporters. (2 marks)

(ii) Explain any five (5) merits of presumptive taxes compared with regular income tax system. (5 marks)

(iii) Explain any three (3) weaknesses of presumptive taxation. (3 marks)

(iv) Advise Kunda of his tax assessment in the tax year 2020 in respect of his transport business. Your answer should include appropriate calculations of the total amount of tax payable by Kunda in the tax year 2020. You should also explain the taxation implications arising from the acquisition of buses and tax treatment of the expenses to be incurred in running the business. (5 marks)

(b) On 1 April 2020, Kabwe started working as a self-employed contractor. On 1 May 2020 he purchased a motor van at a cost of K166,000 with an expected business use of 60%. Motor van running expenses are expected to average K4,500 per month. He will hire three employees to assist him run the business and they will be paid a monthly salary of K16,000 each. He will pay monthly employer's NAPSA contributions of K800 for each employee. And he will pay K6,000 per month for his personal insurance.

With effect from 1 August 2020, Chakudwa Ltd employed Kabwe as a self-employed contractor for a period of five months to December 2020, at an agreed contract price of K225,000 which will be paid to him monthly in arrears, in five equal instalments. He is expected to work on this project at the premise of the company and spend at least six (6) hours per day during his week days. He will be assisted by employees of Chakudwa Ltd when executing his duties and rectify any faulty work done by his assistants outside the contract time and he will not be paid for that extra work.

The company will purchase equipment at cost of K68,000 which Kabwe will use exclusively on the project and will pay for all expenses to be incurred on the project.
Kabwe's income from his other clients is estimated to be K85,000 per month.

Required:

In respect of the contract signed by Kabwe with Chakudwa Ltd. On 1 August 2020:

(i) Provide expalnations that the Zambia Revenue Authority may query Kabwe's self-employed status. (6 marks)

(ii) Provide explanations that Chakudwa Ltd can advance to justify Kabwe's self-employed status. (4 marks)

[Total: 25 Marks]

QUESTION FOUR

For the purposes of this question, you should assume that today's date is 31 December 2019

Simwinga and Namwinga have been in business for some years now running their business as a partnership. They have always prepared their financial statements to 31 December each year.

These two persons are considering incorporating their business on 1 January 2020 and run it as a limited company but they are not sure whether this will be beneficial to them. The only assets owned by the partnership business are a Delivery van and a Motor car which were acquired on 1 January 2019 at a cost of K180,000 and K124,000 respectively. The market value of the Delivery van and the Motor car are expected to be K140,000 and K90,000 respectively on 1 January 2020. All the assets are used wholly and exclusively for business purposes.

If Simwinga and Namwinga continue to run their business as a partnership, they will continue to draw their annual salaries of K280,000 and K220,000 respectively. Any balance of profit or loss will be shared between them in the ratio of 2:3 respectively. The tax adjusted profit before capital allowance and any expenses relating to them is expected to be K630,000 for the tax year 2020.

If Simwinga and Namwinga incorporate their business, they will run their business as a limited company in the name of SN Limited, and all the partnership assets will be taken over by the new company at their market values. Simwinga and Namwinga will be employed by the company as directors at an annual salary of K280,000 and K220,000 respectively. Any balance of profits will be distributed as dividends to Simwinga and Namwinga in the ratio 2:3 respectively. The tax adjusted business profit is expected to be K630,000 for the tax year 2020. This profit figure is after all tax adjustments have been made but before capital allowances and any expenses relating to Simwinga and Namwinga.

There will be no NAPSA contributions made by Simwinga, Namwinga nor SL Limited because the two individuals are both above the retirement age.

Required:

(a) Calculate the amount of income tax payable by Simwinga and Namwinga for the tax year 2020 if they continue to run their business as a partnership. (9 marks)

(b) Calculate the amount of income tax payable by Simwinga, Namwinga and SL Limited for the tax year 2020 if they incorporate their business and the withholding tax payable on dividends. (12 marks)

(c) Advise Simwinga and Namwinga whether they should incorporate their business and run it as a Limited company. Your answer should be supported by a computation of income after tax. (4 marks)

[Total: 25 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) **Chikwanda**

Chikwanda will be required to pay turnover tax. This is because he is carrying on a business whose annual turnover is less than K800,000.

Turnover tax applies to any person carrying on a business with an annual turnover of K800,000 or less and any person whose income consists of amounts, which are subjected to withholding tax, where withholding tax is not the final tax.

Chikwanda was therefore required to pay turnover tax at the rate of 4% of its monthly turnover within 14 days after the end of each month throughout the tax year 2020.

James

James will be required pay tax under the provisional income tax system and not turnover tax. This is because even though the annual turnover from the business does not exceed K800,000, the business is voluntarily registered for VAT. Furthermore, this income for the income is not in the form of emoluments from employment that are taxable under the Pay As You Earn system.

Person carrying on a business where the annual turnover is K800,000 or below which have voluntarily registered for VAT are exempt from paying turnover tax and are assessed under normal income tax through the self-assessment under provisional income tax.

Brian

Brian is an individual carrying on businesses for the transportation of public passengers for reward and therefore will be required to pay presumptive taxes for transporters and will not be required pay income tax on the profits he will generate in the tax year 2020.

The amount of presumptive taxes payable will be fixed estimated amounts based on the seating capacity of the motor vehicles he will use in the transportation business.

(b) (i) **Chikwanda**

- Chikwanda will pay turnover tax at the rate of 4% of its gross monthly turnover without deducting any business expenses.
- Since the turnover was earned evenly throughout the year, the amount of monthly turnover is: 1/12 × K600,000 = K50,000.
- The monthly turnover tax will be computed as follows:

  K50,000 × 4% = K2,000
- The total amount of turnover tax that will be paid in the tax year 2020 is:

  K2,000 x 12 = K24,000

(ii) James

Computation of income tax payable

	K	K
Profit as per accounts		320,000
Add		
Staff loans written off	15,200	
Entertaining customers	19,200	
Donation to an unapproved charity	13,000	
		47400
Taxable profit		367,400
Income Tax		
On first K39,600 x 0%		0
On next K9,600 x 25%		2,400
On next K25,200 x 30%		7,560
Balance K293,000 x 37.5%		109,875
K367,400		119,835

(iii) **Brian**

The amount of presumptive taxes paid by Brian will be computed as follows:

PRESUMPTIVE TAXES PAID

	K
Toyota Noah: (W)	736.80
Hiace bus: (W)	901.60
Rosa bus: (W)	1,198.80
	2,837.20

WORKINGS:

Vehicle	Possible Operational Days	Non operational days	Operational days	tax rate per day	Presumptive Tax

Toyota	325	18	307	2.40	736.80
Hiace bus	194	10	184	4.90	901.60
Rosa bus	87	6	81	14.80	1198.80
					2837.20

(d) Advance income Tax (AIT) is chargeable and withheld when goods are imported for commercial purposes.

This tax is targeted at unregistered business importers who make commercial imports to broaden the tax base and to enhance tax compliance for registered taxpayers.

(2 marks)

(a) A refund may be due to the importer who has paid Advance Income Tax and fulfils the following conditions are fulfilled:

(1) The importer is registered for Income Tax or Turnover Tax;
(2) The importer submits an Income Tax Return or a Turnover Tax Remittance Card at the end of the respective charge year;
(3) The importer provides proof of payment such as receipts and any other relevant documents;
(4) The importer makes a claim that will be subjected to the refund processes as outlined in the Income Tax Act.

SOLUTION TWO

(a) The following are the reasons why ZRA may not consider Mundia to be self-employed:

1. Healthwise Hospital has not employed another Medical Practitioner to replace Mundia. This can be assumed that Mundia and Healthwise Hospital have agreed to let Mundia work for the hospital whilst doing her own business.
2. Mundia is paid on a monthly basis just like employees are remunerated.
3. There are specific times when Mundia is required to report at the premises of Healthwise Hospital every day. This means that Mundia is controlled by Healthwise Hospital.
4. Mundia is assisted by other Healthwise Hospital's medical staff when necessary.

(b) The following are the reasons why Healthwise Hospital may consider Mundia to be self employed:

1. Mundia and Healthwise Hospital signed a contract that specified the beginning and end. This means that she signed a contract for service.
2. Mundia and Healthwise Hospital agreed on a fixed contract price, except that the work done is measured with reference to period.
3. Mundia uses her own tools and equipments in the performance of the duties at Healthwise hospital.
4. Mundia does not exclusively work for Healthwise Hospital because she has a wide range of clients.

(c) Mundia

Income tax payable for the tax year 2020

	K	K
Business profits		190,840
Income from Healthwise: K301,500 x 3/12		75,375
Salary: K570,000 x 2/12		95,000
Housing allowance: K95,000 x 25%		23,750
School fees allowance: K4,000 x 2		8,000
Accrued leave pay		49,940
Taxable income		442,905

Computation

First K39,600 @0%	0
Next K9,600 @25%	2,400
Next K25,200 @30%	7,560
Balance K368,505 @37.5%	138,189
Income tax liability	148,149

Income tax on foreign income	
Dividends: M$4,200 x K14.40 x 6.5%	3,931
Bank interest: M$2,184 x K14.40 x 6.5%	2,044
Income tax payable	154,124

Workings

Taxable business profits for the tax year 2020

	K	K
Revenue: K216,800 x 4 months		867,200
Less:		
Salaries: K10,780 x 10 x 4	431,200	
Employer's NAPSA: K431,200 x 5%	21,560	
Other operating expenses: K31,690 x 4	126,760	
Capital allowances:		
Toyota Prado: K168,000 x 20% x 65%	21,840	
Medical Equipments: K300,000 x 25%	75,000	
		(676,360)
Taxable business profit		190,840

SOLUTION THREE

(a) Joseph and Henry

(i) Tax implications of investment options:

1. Shares in a Zambian listed company
   - No tax is charged on dividends paid by Zambian resident companies listed on the Lusaka Securities Exchange (LuSE).
   - Therefore, no withholding tax will be deducted from the dividends Joseph will be receiving if he buys shares in a company that is listed on LuSE.

2. Shares in a foreign company
   - Dividends received from foreign sources are chargeable to Zambian income tax. The chargeable amount is the gross amount.
   - Therefore, if Joseph buys shares in a Democratic Republic of Congo (DRC), any dividend income he will receive from those shares will be liable to Zambian income tax, subject to any double taxation relief which may be available.

3. Government of Zambia bonds
   - Interest income earned from Government bonds in Zambia is subjected to withholding tax at the rate of 15% for an individual which is a final tax. Therefore, if Joseph invests in Government bonds, the income he will earn will be subjected to withholding tax at the rate of 15% which is final and he will therefore, not be subjected to further income tax on that income.

4. Interest on debentures in Inter-Trade, a company resident in Botswana will - - be taxed in Zambia subject to any double taxation relief available. Therefore, the interest receivable will be included in the Zambian income tax - computation at gross

(ii) Henry

Personal income Tax computation for the tax year 2020

	K
Gross Royalties received (K127,024 X 100/85)	149,440

Income Tax Computation:

Tax band	Taxable amount	Tax rate	Tax
First	39,600	0%	
Next	9,600	25%	2,400
Next	25,200	30%	7,560
Balance	75,040	37.5%	28,140
			38,100
Less:			
WHT (15% x K149,440)			(22,416)
Final income tax payable			15,684

(b) Persons who are not liable to turnover tax are:

1. Any person carrying on business where the annual turnover is over K800,000.
2. Any individual or partnership carrying on the business of public service vehicle for the carriage of persons.
3. Any partnership carrying on business irrespective of whether the annual turnover is over K800,000 or not.
4. Income of partners arising from the partnership since the partnership producing that profit is excluded from turnover tax.
5. Any person whose business earnings are subjected to withholding tax were the withholding tax is the final tax.
6. Any business registered for voluntarily registered for value added tax.
7. Any person who is involved in mining operations as provided under the mines and minerals Development Act.

(c) The property transfer tax implications arising on the transactions listed are as follows:

1. Properly transfer tax will arise on the market value of the property when sold as follows:

   PTT is not chargeable on transfer to the immediate family and immediate family include only spouse, blood children, step children or adopted children. The nephew is not part of the immediate family. However, where the immediate family member pays a consideration to the transferor, PTT arising will be based on the consideration paid.

   The PTT arising will therefore be as follows: Disposal to son – K12,000 X 5% = K600:

   The nephew is not an immediate family member. Therefore, the normal rules will apply. I.e. PTT will be charged on the realised value of K30,000 (K60,000 X ½).

   PTT = K30,000 x 5% = K1,500.

2. The transfer of the motor vehicles is outside the scope of property transfer tax as motor vehicles are not chargeable property.
3. Transfer of shares listed on the Lusaka Securities Exchange is exempt from property transfer tax, therefore, no PTT arises on disposal of shares of a public limited company (Plc).
4. No properly transfer tax arising on the purchase of property.

5. The sale of the residential property in Lusaka Chalala residential area will result in property transfer tax based on the market value as follows: Property transfer tax: K670,000 X 5% = K33,500.

SOLUTION FOUR

(a) Double taxation

(i) Double taxation relief is the relief that is given to a person in order to eliminate the effects of double taxation in cases where income that was subjected to tax in one country is also subjected to tax in the country where it is being received.

(ii) The three (3) methods of giving Double taxation relief are as follows:

Treaty relief

This applies when there is a treaty agreement between Zambia and the foreign country. A double taxation agreement may provide for full recovery of any foreign tax covered by the agreement, by means of a tax credit to a Zambian resident individual, against the Zambian income tax, as long as the relief does not exceed the equivalent Zambian tax charge. In some cases, the treaty may provide that income is only charged to income tax in one of the two countries, or income is charged to tax in one country, with the tax being apportioned between the two countries.

Unilateral relief (unilateral credit relief)

This applies when there is no treaty between Zambia and the foreign country. Relief is given for foreign tax unilaterally in Zambia. Under this relief, the amount of foreign tax suffered is credited against the Zambian income tax on the foreign income, provided that the amount of foreign tax being credited against Zambian tax does exceed the Zambian tax on that foreign income. As a result, the amount of foreign tax available for credit is the lower of:

1. The actual amount of foreign tax paid to foreign tax authorities, and
2. The Zambian tax chargeable on the foreign income.

Unilateral expense relief

This relief applies when neither treaty relief nor unilateral credit relief is available. Relief is given by deducting the foreign tax from the foreign income before including it in the Zambian tax computation.

(b) Tax planning

(i) Manzi and Kanzi

Income tax payable for the tax year 2020

	Manzi	Kanzi
	K	K
Salary	180,000	180,000
Income Tax		
First K39,600 @0%	0	0
Next K9,600 @25%	2,400	2,400
Next K25,200 @30%	7,560	7,560
Balance K105,600 @37.5%	39,600	39,600
	49,560	49,560

(ii) Income tax and NAPSA implications for the Company

Cash bonus payment

1. A cash bonus payment will be an allowable deduction when computing taxable business profits. The company will therefore have tax savings.
2. The amount of income tax savings will amount to: K100,000 x 2 x 35% = K70,000.
3. The company will be required to pay NAPSA contributions on behalf of Manzi and Kanzi as employer's NAPSA contributions subject to the NAPSA limit.

Cash dividend payment

1. The dividend payment will not be an allowable deduction when computing the taxable business profits for the company.
2. Dividends will be paid out of profits already subjected to income tax.
3. NAPSA contributions will not be payable by the company as dividends do not attract NAPSA contributions because they do not qualify as earnings.

(1 mark per valid point up to 5 marks)

(iii) Income tax and NAPSA implications for Manzi and Kanzi

The income tax and NAPSA implications of the additional K100,000 will be as follows:

Cash bonus payment

1. The bonus will be an additional taxable emolument for both Manzi and Kanzi. It will therefore be assessed as taxable emoluments at a rate of 37.5%.
2. The additional income tax payable on the bonus by Manzi and Kanzi will be: K100,000 x 37.5% = K37,500 each.
3. The NAPSA contributions will not be an allowable deduction for tax purposes.

Cash dividend payment

1. The dividends will be subjected to withholding tax at the rate of 15%.
2. The withholding tax deducted at source is the final tax and, therefore, no further tax will be assessed on dividends.
3. The amount of withholding tax payable by each individual will amount to: K100,000 x 15% = K15,000.
4. NAPSA contributions will not be deductible by both Manzi and Kanzi as dividends do not qualify for allowable deductions.

(1 mark per valid point up to 6 marks)

(c) An individual is regarded as resident in Zambia if:

1. An individual is physically present in Zambia for a period of at least 183 days during the tax year.
2. An individual comes to Zambia with the intention of remaining here for more than twelve months or with the intentions of establishing permanent residence is deemed to be resident and ordinarily resident in Zambia from the date of arrival.

END OF SOLUTIONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D5: INTERNATIONAL TAXATION

THURSDAY 17 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question.

2. This question paper consists of **FOUR (4)** questions of Twenty Five (25) marks each. You must attempt all the **FOUR (4)** questions.

3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. **Cell Phones** are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. All workings must be done in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

10. A Taxation table is provided on pages 2, 3 and 4.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table for paper D5– International Taxation 2020 Examinations

Income Tax

Standard personal income tax rates

Income band	Taxable amount	Rate
K1 to K39,600	first K39,600	0%
K39,601 to 49,200	next K9,600	25%
K49,201 to K74,400	next K25,200	30%
Over K74,400		37.5%

Income from farming for individuals

K1 to K39,600	first K39,600	0%
Over K39,600		10%

Company Income Tax rates

On income from manufacturing and other	35%
On income from farming	10%
On income of Banks and other Financial Institutions	35%
On income from mineral processing	30%
On income from mining operations	30%

Mineral Royalty

Mineral Royalty on Copper

Range of Norm Price	Mineral Royalty Rate
Less than US$4,500	5.5% of norm value
From US$4,500 to less than US$6,000	6.5% of norm value
From US$6,000 to less than US$7,500	7.5% of norm value
From US$7,500 to less than US$9,000	8.5% of norm value
From US$9,000 and above	10% of norm value

Mineral Royalty on other minerals

Type of mineral	Mineral Royalty Rate

Base Metals (Other than Copper, Cobalt and Vanadium)	5% on norm value
Cobalt and Vanadium	8% of norm value
Energy and Industrial Minerals	5% on gross value
Gemstones	6% on gross value
Precious Metals	6% on norm value

Capital Allowances

Implements, plant and machinery and commercial vehicles:

Wear and Tear Allowance –	Plant used normally	25%
	Used in Manufacturing and Leasing	50%
	Used in farming and agro-processing	100%

Non- commercial vehicles

Wear and Tear Allowance	20%

Industrial Buildings:

Wear and Tear Allowance	5%
Initial Allowance	10%
Investment Allowance	10%

Low Cost Housing **(Cost up to K20,000)**

Wear and Tear Allowance	10%
Initial Allowance	10%

Commercial Buildings

Wear and Tear Allowance	2%

Farming Allowances

Development Allowance	10%
Farm Works Allowance	100%
Farm Improvement Allowance	100%

Presumptive Taxes

Turnover Tax 4%

Presumptive Tax for Transporters

Seating capacity	Tax per annum	Tax per day
	K	K
From 64 passengers and over	10,800	29.60
From 50 to 63 passengers	9,000	24.70
From 36 to 49 passengers	7,200	19.70

From 22 to 35 passengers	5,400	14.80
From 18 to 21 passengers	3,600	9.90
From 12 to 17 passengers	1,800	4.90
Less than 12 passengers and taxis	900	2.50

Property Transfer Tax

Rate of Tax on Realised Value of Land, Land and Buildings and shares	5%
Rate of Tax on Realised Value on a transfer or sale of a mining right	10%
Rate of Tax on Realised Value on a transfer of Intellectual Property	5%

Value Added Tax

Registration threshold	K800,000
Standard Value Added Tax Rate (on VAT exclusive turnover)	16%

Customs and Excise
Customs and Excise duties on used motor vehicles

	Aged 2 to 5 years		Aged over 5 years	
Motor vehicles for the transport of ten or more persons, including the driver	**Customs duty K**	**Excise duty K**	**Customs duty K**	**Excise duty K**
Sitting capacity of 10 but not exceeding 14 persons including the driver	17,778	22,223	8,889	11,112
Sitting capacity exceeding 14 but not exceeding 32 persons	38,924	0	13,840	0
Sitting capacity of 33 but not exceeding 44 persons	86,497	0	19,462	0
Sitting capacity exceeding 44 persons	108,121	0	43,248	0

	Aged 2 to 5 years		Aged over 5 years	
Motor cars and other motor vehicles principally designed for the transport of persons including station wagons and racing cars	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sedans				
cylinder capacity not exceeding 1000 cc	12,490	10,824	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	16,058	13,917	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	16,545	21,508	8,423	10,950
Cylinder capacity exceeding 2500 cc but not	18,049	23,463	10,528	13,687

exceeding 3000 cc				
Cylinder capacity exceeding 3000 cc	22,561	29,329	12,032	15,642
Hatchbacks				
cylinder capacity not exceeding 1000 cc	10,705	9,278	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	14,274	12,371	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	15,041	19,553	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	16,545	21,508	10,523	13,687
Cylinder capacity exceeding 3000 cc	19,553	25,419	12,032	15,642
Station wagons				
cylinder capacity not exceeding 2500 cc	16,545	21,508	9,024	11,731
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	13,357	17,598
Cylinder capacity exceeding 3000 cc but not exceeding 2500 cc	22,561	29,329	18,049	23,463
SUVs				
Cylinder capacity not exceeding 2500 cc	21,057	27,374	9,024	11,732
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	24,065	31,284	13,357	17,598
Cylinder capacity exceeding 3000 cc	28,577	37,150	18,049	23,463

	Aged 2 to 5 years		**Aged over 5 years**	
Motor vehicles for the transport of goods –with compression-ignitioninternal combustion piston engine (diesel or semi-diesel):	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Single cab				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	21,926	9,501	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	26,311	11,402	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	30,697	13,302	17,541	7,601
Double cabs GVW exceeding 3 tonnes but not exceeding 5 tonnes	30,274	0	24,119	10,452
Double cabs GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes, **with spark ignition internal combustion piston engine**	30,697	13,302	24,119	10,452
Panel Vans				
GVW exceeding 1.0 tonne but not exceeding	15,348	6,651	8,770	3,801

1.5 tonnes				
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	17,541	7,601	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	21,926	9,501	17,541	7,601
Trucks				
GVW up to 2 tonnes	21,926	9,501	10,963	4,751
GVW exceeding 2.0 tonnes but not exceeding 5.0 tonnes	28,504	12,352	13,156	5,701
GVW exceeding 5.0 tonnesbut not exceeding 10.0 tonnes	24,724	18,955	10,817	8,293
GVW exceeding 10.0 tonnesbut not exceeding 20.0 tonnes	30,905	23,694	11,744	9,004
GVW exceeding 20 tonnes	51,898	0	19,461	0
GVW exceeding 20 tonnes, **with spark ignition internal combustion piston engine**	37,086	28,432	13,907	10,662

Customs and excise duty on new vehicles

1 Motor cars and other motor vehicles (including station wagons) principally designed for the transport of less than ten persons, including the driver:

Customs duty:	30%
Excise duty:	
Cylinder capacity of 1500 cc and less	20%
Cylinder capacity of more than 1500 cc	30%

2 Pick-ups and trucks/lorries with gross weight not exceeding 20 tonnes:

Customs duty	15%
Excise duty	10%

3 Buses/coaches for the transport of more than ten persons

Customs duty:	15%
Excise duty:	
Seating capacity of 16 persons and less	25%
Seating capacity of 16 persons and more	0%

4 Trucks/lorries with gross weight exceeding 20 tonnes

Customs duty:	15%
Excise duty:	0%

The minimum amount of customs duty on motor vehicles is K6,000.

Import VAT is added to the sum of VDP, customs duty and excise duty. It is determined at the standard rate of 16%

All FOUR (4) questions are Compulsory and MUST be attended.

QUESTION ONE

Mundia was born in Western Province of the Republic of Zambia on 1 April 1978. He lived in the Republic of Zambia until 31 December 2018 when he left Zambia for the United Kingdom of Zomba where he took up employment with one the multinational corporations that also has a permanent establishment in Zambia. The contract of employment was for a period of eighteen months ending 30 June 2020 and was agreed and signed in Zambia.

Mundia worked in the United Kingdom of Zomba at an annual salary of K260,000 payable to him in Zomban pounds through a Zomban bank. The average annual amounts of Zomban income tax on the annual salary amounted to K58,500. None of the salaries were paid to a Zambian Bank.

Upon the expiry of his contract on 30 June 2020, he received his gratuity of K450,000. Zomban income tax of K169,500 was paid out of this amount of gratuity. The gratuity was credited to his Zambian bank on 31 July 2020, net of Zomban income tax.

On 1 August 2020, Mundia took up employment with Lintox Ltd, a Zambian company at an annual salary of K360,000 as well as the following annual allowances:

	K
Housing allowance	36,000
Education allowance	45,000

PAYE paid on emoluments from employment with Lintox Limited for 2020 was K35,000.

Required:

(a) Explain whether Mundia would be regarded as being resident and ordinarily resident in Zambia for each of the tax years 2018, 2019 and 2020. (6 marks)

(b) Assuming that under the double taxation treaty between Zambia and the United Kingdom of Zomba, Zomban emoluments and gratuities received in Zambia, before deduction of Zomban income tax is chargeable to Zambian income tax at the rate of 10%, calculate the final amount of income tax payable by Mundia for the tax year 2020. (8 marks)

(c) Advise Mundia as to how his tax position would have been for the tax year 2020 if he had received his foreign salary through his Zambian Bank. (3 marks)

(d) Explain the tax treatment of the following types of income:

(i) Domestic investment income of non-residents (4 marks

(ii) Domestic employment income of non-residents (4 marks)

[Total: 25 Marks]

QUESTION TWO

(a) International trade is the purchase, sale or exchange of goods and services across national borders which opens up doors for countries to have production capabilities they wouldn't have a chance to take advantage of. Trade transactions to other countries increases the demand of the product from other countries and the overall productivity increases.

Required:

(i) Explain four (4) benefits of international trade. (4 marks)

(ii) Explain the Mercantilism, Absolute advantage and Comparative advantage as theories of international trade. (6 marks)

(b) Global trade has expanded much faster than global output which is mainly attributed to a fundamental shift from national economies which were isolated from each other by barriers to cross-border trade, distance zones, language and national differences in government regulation, culture and business systems and towards a world in which national economies are merged into an interdependent global economic system. All this has led to countries in many regions forming Regional Economic Groupings in order to achieve greater economic integration.

Required:

(i) Explain the benefits of globalization on the Zambian economy (3 marks)

(ii) Explain the problems of over reliance on global trade. (4 marks)

(iii) Explain the four (4) advantages and four (4) disadvantages of Regional Economic Groupings. (8 marks)

[Total:25 Marks]

QUESTION THREE

Loshida Plc is a multinational company resident in a country known as Blueland. The company is engaged in the manufacture of computers and phones and Zambia has been the major importer of Loshida Plc's products. On 31 March 2020 the board of directors of Loshida Plc decided to open an operation in Zambia by establishing a production plant believing that this would enable customers from Zambia and neighboring countries to access computers and phones at affordable prices. Loshida Plc completed the construction of a production plant in Zambia on 1 May 2020 at a total cost of K2,900,000. Loshida Plc did not incorporate a new company in Zambia and the head office remained in Blueland. Loshida Plc appointed five (5) directors in Zambia of which one was sent from Blueland to come and spearhead the Zambian operations while the other four (4) directors are Zambians who were appointed on commencement of the company's operations in Zambia. The directors of the Zambian operations will be travelling to Blueland at the end of every quarter to attend the meetings regarding key decisions of the company's operations.

Andrew Philips who was the Operations Manager of Loshida Plc in Blueland was sent to Zambia as the Managing Director of the Zambian operations at an annual salary of K600,000 and arrived in Zambia on 1 May 2020 when the operations of the company commenced. According to a signed contract of service with Loshida Plc, Andrew was expected to be in Zambia for the next five (5) years.

On 31 December 2020, Andrew Philips received bank interest from his savings with a bank resident in Blueland amounting to K140,000, which was net of withholding tax deducted in Blueland at the rate of 30%. This interest was credited to Andrew Philips's newly opened bank account with a Zambian bank.

There is no double taxation agreement between Zambia and Blueland. When computing Zambian income tax, credit is available against any foreign tax paid.

Required:

(a) Advise the directors of Loshida Plc, with reasons, whether the company will be regarded as a Zambian resident company for taxation purposes. (4 marks)

(b) Describe what constitutes a Permanent Establishment in accordance with the OECD guidelines and advise the directors of Loshida Plc whether the Zambian operations will be regarded as a Permanent Establishment. (7 marks)

(c) Explain, with reasons, whether Andrew Philips will be regarded as a Zambian resident in the 2020 tax year. (4 marks)

(d) Explain how the foreign income received by non-residents is treated for income tax purposes. (3 marks)

(e) Calculate the income tax payable by Andrew for the tax year 2020. (7 marks)

[Total: 25 Marks]

QUESTION FOUR

Hantobolo, a Zambian resident, and Donny, a US resident, are in partnership sharing profits and losses in the ratio 2:3. Hantobolo runs a Zambian branch selling agricultural equipment to farmers in Central Province and other parts of Zambia and sought a foreign direct investment and as such partnered with Donny, a long-time colleague he met at the University in the US when he was pursuing his first degree in Agricultural Science. Donny Miles is running the branch of the same business in the US.

The partnership profits for the year ended 31 December 2020 were as follows:

Zambian branch	K1,400,000
US branch (before US tax)	$250,000

The above figures are tax adjusted business profits . The Commissioner General has advised that the exchange rate to be used for the purposes of translating the foreign income is K14.50 per Us Dollar. Business profits are taxed at a rate of 30% in the US. Hantobolo received his share of the US profits on 30 December 2020 net of US tax.

During the year, Hantobolo received royalty income of K42,500 (net) from a Zambian resident company and foreign dividends amounting to $10,000 net of withholding tax of 20%. The provisional income tax paid for the tax year 2020 was K123,500.

Required:

(a) Calculate the income tax payable by Hantobolo for the tax year 2020 assuming a unilateral credit relief is available against Zambian income tax on foreign income earned by Zambian residents. (12 marks)

(b) Explain how a unilateral credit relief method of double taxation applies between Zambia and the foreign country. (4 marks)

(c) Explain what is meant by Foreign Direct Investment (FDI) and explain five (5) reasons for engaging in FDI. (6 marks)

(d) State two (2) types of Foreign Direct Investment (3 marks)

[Total: 25 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) An individual is resident in Zambia in any tax year when he or she is physically present in Zambia for a period of at least 183 days. An individual who normally lives in Zambia in the normal course of life is ordinarily resident in Zambia for tax purposes.

For the tax year 2018, Mundia will be regarded as having been resident in Zambia since he was physically present in Zambia for at least 183 days in the tax year.

Mundia will not be treated as having been resident in Zambia for the tax year 2019 as he will not have been physically present in Zambia for at least 183 days in the tax year. His period of absence from Zambia covers the entire tax year 2019.

For the tax year 2020, Mundia will be regarded as being resident as his period of physically staying in Zambia would be of at least 183 days.

As Mundia will have gone to the United Kingdom of Zomba with an intention of coming back to Zambia upon expiry of his contract, he will remain ordinarily resident in Zambia for all the three tax years in question.

(b) MUNDIA
PERSONAL INCOME TAX COPUTATION FOR THE TAX YEAR 2020

		K
Zambian emoluments:		
Salary (360,000 x 5/12)		150,000
Housing allowance (36,000 x 5/12)	15,000	
Education allowance (45,000 x 5/12)	18,750	
		183,750
Less exempt income	(39,600)	
Taxable income		144,150
Computation		
25% x K9,600	2,400	
30% x K25,200		7,560
37.5% x K109,350	41,006	
		50,966
Tax on Zomban emoluments:		
Gratuity: K450,000 x 10%	45,000	
		95,966
Less PAYE		(35,000)
Income tax payable	60,966	

(c) Mundia still remains ordinarily resident in Zambia. As he is domiciled in Zambia, income arising from sources from all over the world is chargeable on him where applicable, subject to double taxation relief.

This would be all his foreign income that would be deemed to be taxable income of Zambian residents, provided such income is not exempt from Zambian income tax.
As such, the position would be that the salary would be included in the computation of Zambian income tax.

(d) Income of non-residents

(i) Domestic Investment Income of non-residents

In the case of investment income (e.g. dividends, interest and royalties) paid to non-residents, domestic law usually provides for flat-rate final withholding tax on the gross amount if they are sourced in the country and not attributable to a permanent establishment.
The tax rate is typically set at 20 -30 percent in developing and transition countries and then is often reduced to 10- 20 percent in tax treaties.

The rates are set at this level in domestic law to leave room for negotiating in the tax treaty process but usually to be below normal company tax rate in recognition of the fact that the tax is gross and does not take into account of expenses.

In tax treaty negotiations, developing and transition countries will come under considerable pressure from industrial countries to reduce withholding tax rates on interest and royalties to zero.
The argument used by industrial countries is that the gross tax often wipes out the entire profit with the result that the price charged to the resident or permanent establishment in the country is increased.

(ii) Domestic Employment Income of non-residents

Employment income of non-residents is usually subject to the normal wage withholding tax and not to any special final withholding tax, despite the policy arguments that flat-rate withholding tax is the appropriate method for non-residents.

There are special collection problems where the employer is a non-resident, but tax treaties usually will protect the employee from taxation by the country where the work is performed in this event through the 183-day rule unless a permanent establishment bears the wages.
If the employee is present for 183 days or more, residence will usually arise and the more permanent connection with the country will facilitate withholding tax, although it is easy for

temporarily present employees to slip through the net unless attention is given this issue by the tax administration.
Powers in the domestic law for the tax administration to prevent a person from leaving a country unless taxes are paid can provide some assistance to tax collection depending on how easy o difficulty it is to exit the country

SOLUTION TWO

(a) International trade

(i) The following are the benefits of international trade:

1. Countries that have a surplus of resources to their needs can take advantage to export them while countries with a deficit of raw material must either import or accept restrictions on its economic prosperity and standard of living.
2. International trade increases competition amongst suppliers in the world's markets.
3. International trade creates larger markets for a firm's output, and so some firms can benefit from economies of scale by engaging in export activities.
4. There may be political advantages to international trade because the development of trading links provides a foundation for closer political links.

(ii) Mercantilism

This theory states that nations should accumulate financial wealth through exports and discouraging imports. This would be achieved through trade surpluses, government intervention and colonization.

Absolute Advantage

A country has an absolute advantage in the production of a good if it is more efficient than another country in producing that good. This means that a country can produce more of a particular good with a given amount of resource than another country.
The theory states that trade should not be restricted by tariffs or banned but allowed to flow freely according to the demand of the market.

Comparative Advantage

This theory states that a country may not be able to produce the good more efficiently than any other country but can produce the good more efficiently than any other good within its own country.
This is accomplished if one country has the absolute advantage in two different types of exports but it costs more monetarily or in labour than another country.

(b) Globalisation

(i) The following are the benefits of globalisation

1. Foreign Direct Investment tends to increase at a much greater rate than the growth in world trade, helping boost technology transfer, industrial restructuring, and growth of global companies.

2. Increased competition from globalisation helps stimulate new technological development, particularly with the growth in FDI, which helps improve economic output by making processes more efficient.

3. Globalisation has enabled large companies to realise economies of scale that reduce costs and prices, which in turn support further economic growth, although this can hurt many small businesses attempting to compete domestically.

(ii) The following are the problems of over reliance on global trade:
1. Globalisation leads to interdependence between nations, which could cause regional or global instabilities, if local economic fluctuations end up impacting a large number of countries relying on them.
2. Some see the rise of nation states, multinational or global firms and other international organisations as a threat to sovereignty. Ultimately this could lead to some leaders become nationalistic or xenophobic.
3. The benefits of globalisation can be unfairly skewed towards rich nations or individuals, creating greater inequalities and leading to potential conflicts both nationally and internationally as a result.
4. Some countries may implement tariffs and other form of protectionism designed to contain the risks in the financials systems in order to make any crisis less damaging. This puts the benefits of globalisation to question.

(iii) Advantages of Regional Economic Groupings
1. The larger markets created through trading groups permit economies of scale which reduces the average cost of production due to mass production.
2. Trade groupings bring manufacturers in numerous countries closer together, resulting in greater competition which promotes greater efficiency within firms.
3. Trade groupings eliminate tariffs, thus driving the cost of imports down. This results in changes in demand and consumers make purchases based on the lowest prices, allowing firms with a competitive advantage in production to thrive.
4. The increased consumption experienced with changes in combines with greater amount of products being manufactured to result in an efficient market.

Disadvantages
1. Economic groupings bear an inherent bias in favour of their participating countries.
2. An economic grouping is likely to lead to at least partial loss of sovereignty for its participants particularly if it is coupled by a political union.
3. No country wants to let foreign firms gain domestic market share at the expense of local companies without getting something in return. This means countries wanting to joining economic groupings must be prepared to make concessions.
4. Economic groupings increase trade among participating countries which may result in countries become increasingly dependent on each other.

SOLUTION THREE

(a) A company is regarded as a resident in Zambia if:
1. It is incorporated or formed in Zambia and;
2. Its effective management and control is exercised in Zambia. A company is effectively managed in Zambia if its board of directors or other central management boards meet in Zambia

Loshidal Plc will not be regarded as a Zambian resident company because the company was incorporated in Blueland and its effective management is exercised in Blueland.

(b) A Permanent Establishment is a fixed place of the business through which the operations of an enterprise are partially or wholly carried on.
Permanent Establishment includes a place of management, branch, an office, a factory, a workshop, a mine, oil or gas well, a quarry or any other place of extraction of natural resources.

A building site or construction or installation project may constitute a Permanent Establishment if it lasts more than twelve (12) months.

Loshida Plc operates in Zambia through a factory which is a fixed place through which the business of the company is carried on. Therefore, the Zambian operation will be regarded as a Permanent Establishment.

(c) An individual is regarded as a resident in Zambia if:
1. He or she is physically present in Zambia for a period of at least 183 days excluding the date of arrival and departure
2. He or she comes to Zambia for the purpose that will take more than twelve (12) months or who comes to take up permanent residence in Zambia is regarded as a resident on the day of arrival.

Andrew Philips will be regarded as a resident in Zambia for the tax year 2020 because he was present in Zambia for at least 183 days during the tax year 2020 and he is expected to be in Zambia for five years which is more than twelve months.

(2 marks)

(d) In Zambia only persons resident in Zambia are liable to income tax on their worldwide income or income from Zambian sources is liable to tax. Therefore, when a non-resident receives income from foreign sources, that income is not taxable in Zambia. This is because there is neither relationship between the state and the tax payer nor the relationship between the state and the income.

(e) Andrew Philips
Income tax payable for the tax year 2020

		K
Salary: K600,000 x 8/12		400,000
Foreign income		
Bank interest: K140,000 x 100/70	200,000	
Taxable income		600,000

Computation	
First K39,600 @0%	0
Next K9,600 @25%	2,400
Next K25,200 @30%	7,560
Balance K525,600 @37.5%	197,100
Income tax liability	207,060
Less:	
Double taxation relief (w)	(60,000)
Income tax payable	147,060

Workings

Double taxation relief

- Foreign tax paid: K200,000 x 30% = **K60,000**

- Zambian tax:

$$\frac{\text{Gross foreign income}}{\text{Total assessable income}} \times \text{Zambian tax}$$

$$\frac{K200{,}000}{K600{,}000} \times K207{,}060 = \mathbf{K69{,}020}$$

- The double taxation relief is **K60,000**

SOLUTION FOUR

(a) HANTOBOLO

PERSONAL INCOME TAX COMPUTATION FOR THE TAX YEAR 2020

		K
Share of partnership profits:		
Zambian branch (1,400,000 x 2/5)	560,000	
US branch (250,000 x 14.50 x 2/5)	1,450,000	
Royalties (42,500 x 100/85)		50,000
Foreign dividends (10,000 x 14.50 x 100/80)		181,250
		2,241,250
Less: Exempt income		(39,600)
Taxable income		2,201,650
Income tax:		
25% x K9,600		2,400
30% x K25,200		7,560
37.5% x K2,166,850		812,569
		822,529
Less tax already paid:		
Provisional income tax		(123,500)
Double taxation relief (DTR):		
Foreign profits (W1)		(435,000)
Foreign dividends (W2)		(36,250)
WHT on royalties (50,000 x 15%)		(7,500)
Income tax payable		220,279

Workings:

Double Taxation relief:

1. Foreign profits
   - Foreign tax paid on foreign income = K1,450,000 x 30% = **K435,000**
   - Zambian tax charge on foreign income

$\frac{\text{Gross foreign income}}{\text{Total assessable income}}$ x Zambian tax charge

$\frac{1,450,000}{2,241,250}$ x 822,529 **= K532,144**

2. Foreign dividend:

Foreign tax paid on dividends = K181,250 X 20% **= K36,250**

Zambian tax charge on foreign income

181,250 x 822,529 **= K66,518**

2,241,250

(b) The Unilateral credit relief applies where there is no treaty relief. Relief is given for foreign tax unilaterally in the republic of Zambia.

Under this relief, the amount of foreign tax suffered is credited against Zambian income tax on the foreign income, provided that amount of foreign tax being credited against Zambian tax cannot exceed the Zambian tax on that foreign income. As a result, the amount of foreign tax available for credit is the lower of:

1. The actual amount of foreign tax paid to foreign tax authorities; and
2. The Zambian tax chargeable on the foreign income.

(c) FDI is defined as an investment in a business by an investor from another country in which the foreign investor has control over the company purchased.

The following are the reasons of engaging in FDI:

1. Market seeking**:** - to meet local demand or as a way of exporting to markets other than the home market.
2. Raw material seeking: - to extract raw materials in places where they can be found, whether for export or for further processing and sale in the host country.
3. Production efficiency seeking: - to locate production where one or more factors of production are cheap relative to their productivity.
4. Knowledge seeking: - to set up operations in countries in which they can gain access to technology or management expertise.
5. Political safety seeking: - to seek political safety by setting up new operations in those countries which are thought be unlikely to expropriate or interfere with private enterprises.

(d) Types of Foreign Direct Investment

1. Horizontal FDI

This arises when a firm duplicates its home based activities at the same value stage in a host country through FDI.

2. Platform FDI

This is FDI from the source country into a destination country for the purpose of exporting to the third country.

3. Vertical FDI

This takes place when a firm through FDI moves upstream or downstream in different value chains. i.e when firms perform value adding activities stage by stage in a vertical fashion in a host country.

END OF SOLUTONS

TAXATION PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

D6: TAX AUDIT AND INVESTIGATIONS

MONDAY 14 DECEMBER 2020

TOTAL MARKS – 100; TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading time. Use it to study the examination paper carefully so that you understand what to do in each question.

2. This question paper consists of **FOUR (4)** questions of Twenty Five (25) marks each. You must attempt all the **FOUR (4)** questions.

3. Enter your Student number and your National Registration Card number on the front of the answer booklet. Your name must **NOT** appear anywhere on your answer booklet.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. **Cell Phones** are **NOT** allowed in the Examination Room.

6. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

7. All workings must be done in the answer booklet.

8. Present legible and tidy work.

9. Graph paper (if required) is provided at the end of the answer booklet.

10. A Taxation table is provided on pages 2, 3 and 4.

DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.

Taxation table for paper D6– Tax Audit and Investigations (June and December 2020 Examinations)

Income Tax

Standard personal income tax rates

Income band	Taxable amount	Rate
K1 to K39,600	first K39,600	0%
K39,601 to 49,200	next K9,600	25%
K49,201 to K74,400	next K25,200	30%
Over K74,400		37.5%

Income from farming for individuals

K1 to K39,600	first K39,600	0%
Over K39,600		10%

Company Income Tax rates

On income from manufacturing and other	35%
On income from farming	10%
On income of Banks and other Financial Institutions	35%
On income from mineral processing	30%
On income from mining operations	30%

Mineral Royalty

Mineral Royalty on Copper

Range of Norm Price	Mineral Royalty Rate
Less than US$4,500	5.5% of norm value
From US$4,500 to less than US$6,000	6.5% of norm value
From US$6,000 to less than US$7,500	7.5% of norm value
From US$7,500 to less than US$9,000	8.5% of norm value
From US$9,000 and above	10% of norm value

Mineral Royalty on other minerals

Type of mineral	Mineral Royalty Rate
Base Metals (Other than Copper, Cobalt and Vanadium)	5% on norm value
Cobalt and Vanadium	8% of norm value
Energy and Industrial Minerals	5% on gross value
Gemstones	6% on gross value
Precious Metals	6% on norm value

Capital Allowances

Implements, plant and machinery and commercial vehicles:

Wear and Tear Allowance –	Plant used normally	25%
	Used in Manufacturing and Leasing	50%
	Used in farming and agro-processing	100%

Non- commercial vehicles

Wear and Tear Allowance	20%

Industrial Buildings:

Wear and Tear Allowance	5%
Initial Allowance	10%
Investment Allowance	10%

Low Cost Housing **(Cost up to K20,000)**

Wear and Tear Allowance	10%
Initial Allowance	10%

Commercial Buildings

Wear and Tear Allowance	2%

Farming Allowances

Development Allowance	10%
Farm Works Allowance	100%
Farm Improvement Allowance	100%

Presumptive Taxes

Turnover Tax 4%

Presumptive Tax for Transporters

Seating capacity	Tax per annum K	Tax per day K
From 64 passengers and over	10,800	29.60
From 50 to 63 passengers	9,000	24.70
From 36 to 49 passengers	7,200	19.70
From 22 to 35 passengers	5,400	14.80
From 18 to 21 passengers	3,600	10
From 12 to 17 passengers	1,800	5.0
Less than 12 passengers and taxis	900	2.50

Property Transfer Tax

Rate of Tax on Realised Value of Land, Land and Buildings and shares	5%
Rate of Tax on Realised Value on a transfer or sale of a mining right	10%
Rate of Tax on Realised Value on a transfer of Intellectual Property	5%

Value Added Tax

Registration threshold	K800,000
Standard Value Added Tax Rate (on VAT exclusive turnover)	16%

Customs and Excise
Customs and Excise duties on used motor vehicles

	Aged 2 to 5 years		Aged over 5 years	
Motor vehicles for the transport of ten or more persons, including the driver	**Customs duty K**	**Excise duty K**	**Customs duty K**	**Excise duty K**
Sitting capacity of 10 but not exceeding 14 persons including the driver	17,778	22,223	8,889	11,112
Sitting capacity exceeding 14 but not exceeding 32 persons	38,924	0	13,840	0
Sitting capacity of 33 but not exceeding 44 persons	86,497	0	19,462	0
Sitting capacity exceeding 44 persons	108,121	0	43,248	0

	Aged 2 to 5 years		Aged over 5 years	
Motor cars and other motor vehicles principally designed for the transport of persons including station wagons and racing cars	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Sedans				
cylinder capacity not exceeding 1000 cc	12,490	10,824	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	16,058	13,917	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	16,545	21,508	8,423	10,950
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	10,528	13,687
Cylinder capacity exceeding 3000 cc	22,561	29,329	12,032	15,642
Hatchbacks				
cylinder capacity not exceeding 1000 cc	10,705	9,278	7,136	6,185
Cylinder capacity exceeding 1000 cc but not exceeding 1500 cc	14,274	12,371	8,564	7,422
Cylinder capacity exceeding 1500 cc but not exceeding 2500 cc	15,041	19,553	8,423	10,950

Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	16,545	21,508	10,523	13,687
Cylinder capacity exceeding 3000 cc	19,553	25,419	12,032	15,642
Station wagons				
cylinder capacity not exceeding 2500 cc	16,545	21,508	9,024	11,731
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	18,049	23,463	13,357	17,598
Cylinder capacity exceeding 3000 cc but not exceeding 2500 cc	22,561	29,329	18,049	23,463
SUVs				
Cylinder capacity not exceeding 2500 cc	21,057	27,374	9,024	11,732
Cylinder capacity exceeding 2500 cc but not exceeding 3000 cc	24,065	31,284	13,357	17,598
Cylinder capacity exceeding 3000 cc	28,577	37,150	18,049	23,463

	Aged 2 to 5 years		**Aged over 5 years**	
Motor vehicles for the transport of goods –with compression-ignitioninternal combustion piston engine (diesel or semi-diesel):	**Customs duty**	**Excise duty**	**Customs duty**	**Excise duty**
	K	**K**	**K**	**K**
Single cab				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	21,926	9,501	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	26,311	11,402	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	30,697	13,302	17,541	7,601
Double cabs GVW exceeding 3 tonnes but not exceeding 5 tonnes	30,274	0	24,119	10,452
Double cabs GVW exceeding 3.0 tonnes but not exceeding 5.0 tonnes, **with spark ignition internal combustion piston engine**	30,697	13,302	24,119	10,452
Panel Vans				
GVW exceeding 1.0 tonne but not exceeding 1.5 tonnes	15,348	6,651	8,770	3,801
GVW exceeding 1.5 tonnesbut not exceeding 3.0 tonnes	17,541	7,601	15,348	6,651
GVW exceeding 3.0 tonnesbut not exceeding 5.0 tonnes	21,926	9,501	17,541	7,601
Trucks				
GVW up to 2 tonnes	21,926	9,501	10,963	4,751
GVW exceeding 2.0 tonnes but not exceeding	28,504	12,352	13,156	5,701

5.0 tonnes				
GVW exceeding 5.0 tonnesbut not exceeding 10.0 tonnes	24,724	18,955	10,817	8,293
GVW exceeding 10.0 tonnesbut not exceeding 20.0 tonnes	30,905	23,694	11,744	9,004
GVW exceeding 20 tonnes	51,898	0	19,461	0
GVW exceeding 20 tonnes, **with spark ignition internal combustion piston engine**	37,086	28,432	13,907	10,662

Customs and excise duty on new vehicles

1 Motor cars and other motor vehicles (including station wagons) principally designed for the transport of less than ten persons, including the driver:

Customs duty:	30%
Excise duty:	
Cylinder capacity of 1500 cc and less	20%
Cylinder capacity of more than 1500 cc	30%

2 Pick-ups and trucks/lorries with gross weight not exceeding 20 tonnes:

Customs duty	15%
Excise duty	10%

3 Buses/coaches for the transport of more than ten persons

Customs duty:	15%
Excise duty:	
Seating capacity of 16 persons and less	25%
Seating capacity of 16 persons and more	0%

4 Trucks/lorries with gross weight exceeding 20 tonnes

Customs duty:	15%
Excise duty:	0%

The minimum amount of customs duty on motor vehicles is K6,000.

Import VAT is added to the sum of VDP, customs duty and excise duty. It is determined at the standard rate of 16%

All FOUR (4) questions are compulsory and MUST be attempted.

QUESTION ONE

Bresmar Investment Ltd is a transportation company. The company has over the years been contracted by Kalomo Mining Plc to provide transportation within and outside the mines. During the year ended 31 December 2020, the company made a loss as per accounts of K170,000. The annual turnover of the company has always exceeded K800,000. The profit figure was arrived at after charging the following expenses:

1. General expenses of K100,000 which includes K40,000 for a fine in respect of breach of health and safety regulations, K20,000 for a donation to a political party and advertising expenses amounting to K15,000. The balance consists of revenue expenses which are allowable for tax purposes.
2. Leasing charges amounting to K150,000 of which K50,000 relates to operating lease and the balance consist of finance costs incurred on finance leases.
3. During the year ended 31 December 2020 the company held a party where all the suppliers and Directors of Kalomo Mining Plc at a cost of K55,000.
4. Professional fees amounting to K90,000 of which K40,000 relates to accountancy services and K50,000 for fees in connection with a late submission of a tax return.
5. Fines amounting to K5,000 relates to the traffic speeding offences committed by two (2) Directors during the year.
6. Depreciation for all the assets owned by the company amounted to K350,000.
7. Penalties for late payment of employer's NAPSA contribution K35,000.

Other information

Due to lack of capital, Bresmar Investment Ltd entered into the following lease agreements:

Operating lease

	Date leased	Original cost (VAT exclusive)
		K
Tata Truck	6 January 2020	100,000
Fuso Truck	2 January 2020	80,000

Finance lease

	Date leased	Original cost (VAT exclusive)
		K
Tipper Truck	1 January 2020	250,000
Nissan Truck	12 January 2020	280,000
Mitsubishi Truck	31 December 2019	300,000

The Directors of Bresmar Investment Limited received notification from the Zambia Revenue Authority (ZRA) that the tax inspectors will be coming to visit the premises of the business. The Directors are not sure whether the purpose of the visit is to conduct a tax audit or a tax investigation.

Required:

(a) Explain the difference between tax audit and tax investigation. (4 marks)

(b) Explain four (4) factors that can trigger a tax investigation. (4 marks)

(c) Explain the income tax and VAT implications of acquiring assets under each of the following:

(i) Operating lease. (3 marks)

(ii) Finance lease. (3 marks)

(d) In relation to Bresmar Investment Limited;

(i) Explain the capital allowances implications on the leased assets. Your answer should include a computation of total amount of capital allowances claimable by the company for the tax year 2020. (5 marks)

(ii) Compute the amount of company income tax payable by Bresmar Investment Limited for the tax year 2020. (6 marks)

[Total: 25 Marks]

QUESTION TWO

(a) Technology has influenced almost every industry across the globe in both product and service provision. The Telecommunication sector is one of the sectors that has embraced the use of technology in their service provision. In the quest to ensure quality service provision, the Telecommunication industry has Roaming Facilities to ensure communication beyond borders.

Required:

(i) Explain the tax treatment of roaming charges and income. (3 marks)

(ii) Explain the tax treatment of discounts given to airtime dealers. (3 marks)

(b) The authority of a tax auditor to conduct an audit or investigation is spelled out under Section 57 and 58 of the Income Tax Act of the laws of Zambia. Auditors must be firm in the assertion of their authority to carry out all aspects of an examination of a taxpayer. This becomes very important in dealing with individuals who may not cooperate and attempt to create obstacles to prevent an auditor from making a complete and thorough investigation. The tax auditor has also the powers to make an estimated assessment on the taxpayer.

Required:

(i) Explain the circumstances under which an estimated assessment can be made on the tax payer by the tax auditor. (3 marks)

(ii) Explain the basis which can be used by the tax auditor to determine an estimated assessment. (4 marks)

(c) Tax payers are required by law to keep appropriate accounting records and books for the purpose of verifying the amount of tax liability declared. Small and Medium Enterprises (SMEs) usually provide inadequate records which increases the risk that the tax auditor will see no clear audit trail or adequate records to support a proper calculation of the tax liability of the tax payer.

Required:

Explain how the tax auditor may use each of the following indirect methods to verify income:

(i) Source and application of funds method. (3 marks)

(ii) Mark-up method. (3 marks)

(iii) The Net Worth method. (4 marks)

(iv) Unit and Volume method. (2 marks)

[Total: 25 Marks]

QUESTION THREE

You have been recently employed by the Zambia Revenue Authority as an assistant tax auditor upon completion of a Diploma in Taxation Programme. Your team is visiting PC Bank Limited to conduct a tax audit. Your team leader has asked you to maintain working papers as you carry out a tax audit at PC Bank Limited's premises and document any audit findings.
PC Bank Limited, is a Zambian resident company. The bank is an 80% owned subsidiary of GTT Bank Corporation, a multinational company resident in a foreign country.

PC Bank Limited prepares its financial statements annually to 31 December. The Statement of profit or loss for the year ended 31 December 2020 is as follows:

	Notes	K'000
Interest income		65,750
Interest expense		(13,000)
Net interest income		52,750
Provision for loan losses	1	(8,330)
Net interest income after provision for loan losses		44,420
Non-interest income	2	6,000
Net interest and other income		50,420
Non-interest expenses	3	(15,750)
Income before taxes		34,670
Income tax expense	4	(6,000)

Income after tax	28,670

The following additional information is relevant:	K'000
Note 1: Provision loan losses	
This comprises the following	
Irrecoverable loans written off	3,790
Increase in specific provision for loan losses	7,000
Decrease in general provision for loan losses	(2,460)
	8,330
Note 2: non – interest income	
This includes the following	
Dividends from an unlisted Zambian company (net)	95
Unrealized trading gain	1,640
Royalties (gross)	2,500
Rental income (net)	1,765
	6,000
Note 3: non- interest expenses	
This includes	
Loss on disposal of Office Equipments	6,200
Depreciation	2,500
Employer NAPSA contributions	85
Entertaining employees	3,412
Other allowable business expenses	3,553
	15,750

Note 4:
The income tax expense represents the provisional income tax paid for the tax year 2020

Note 6: Implements, Plant and Machinery
The only assets qualifying for capital allowances were as follows:

	Original cost	Income tax value 1 January 2020
	K'000	K'000
ATM machines	17,150	8,520
Finance Director Personal to holder car (3000cc)	700	420
Built in Cash in transit Van	500	400
Office Equipment	10,000	2,500

The Office Equipment were sold during the year for K2,500.

Required:

(a) Explain the importance of audit Working Papers (3 marks)

(b) Explain the meaning of each of the following terms in the context of tax audits:

(i) Relevant evidence

(ii) Reliable evidence

(iii) Sufficient evidence

(6 marks)

(c) Calculate the income tax payable by PC Bank Limited for the tax year 2020. (16 marks)

[Total: 25 Marks]

QUESTION FOUR

Many businesses are currently facing reduced production and profitability. One of the reasons which have led to low productivity and profitability is increased operational and production costs and tax is one of the liabilities which every business has to pay. However, some businesses have not been submitting their TAX returns and remitting correct taxes to ZRA. Non-compliance in terms of submitting tax returns and non-payment of taxes has led to increased tax audits by ZRA.

Required:

(a) Explain the main reasons of carrying out a tax audit. (3 marks)

(b) Discuss four (4) main theories that have contributed to the evolution of audit theory (8 marks)

(c) Outline the objectives of Compliance Risk Management and the process a tax auditor has to undertake to accomplish it. (4 marks)

(d) An important requirement needed before an auditor meets a client is to write a formal introductory meeting letter to the client.

Required:

State any Six (6) matters which should be included in the letter of introductory meeting and its importance. (6 marks)

(e) Explain the assurances provided by a qualitative tax audit. (4 marks)

[Total: 25 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

SOLUTION ONE

(a) A tax audit is an examination of a tax return and its supporting books of accounts and any other related information. It can also be conducted to examine whether the tax payer has correctly assessed and reported the tax liability, and to check tax payers' compliance with tax legislation.

On the other hand, tax investigation is an in-depth examination process by a tax authority in order to recover tax undercharged in previous years of assessment. It is usually carried out when a taxpayer is suspected of tax evasion.

(b) The following are the factors which could trigger a tax investigation:

1. Mathematical errors: constant calculation errors are in a return which are submitted may prompt the tax audit.
2. Omission of income: Deliberate failure to report some income generated in the business would prompt a tax audit.
3. Reported many losses: Losses in the business are normal and no tax is paid in an event where a company makes losses. However, constant reporting of losses may call up tax audit.
4. Too many deductions: Each taxpayer aims at reducing the tax liability and as such claiming too many deductions may imply intentional plans to reduce the tax liability and may prompt tax audit.

(c) Operating and Finance leases

(i) Operating Lease

The following are the tax implications:

1. The lessee will not be able to claim capital allowances on the leased assets because the legal owner (Lessor) claims the capital allowances.
2. Lease rentals payable on the lease are tax allowable when computing the tax adjusted business profits for the lessee.
3. Value Added Tax paid on lease rentals is recoverable as input VAT if the lessee is registered for VAT and for as long as the input VAT is one which is recoverable.

(ii) Finance Lease:

The following are the tax implications:

1. The lessee will be able to claim capital allowances on the leased assets and any expenses incurred on those assets is an allowable deduction when computing the taxable business profits.
2. The finance cost incurred on the finance lease is an allowable deduction when computing the taxable business profits

3. Value Added Tax on the cost of the leased the assets is claimable as input VAT if the lessee is registered for VAT and for as long as the input VAT is one which is recoverable.

(d) Bresmar Investment Limited

(i) The company will not be able to claim any capital allowances on the Tata Truck and the Fuso Truck because these assets are leased under an operating lease in which case the legal owner claims capital allowances.

However, the company will be able to claim capital allowances on the assets leased under finance lease.

Computation of Capital allowances for the tax year 2020.

	Cost/ITV	Capital allowance
	K	K
Tipper Truck		
Cost	250,000	
Wear & tear @25%	(62,500)	62,500
ITV c/f	187,500	
Nissan Truck		
Cost	280,000	
Wear & tear @25%	(70,000)	70,000
ITV c/f	210,000	
Mitsubishi Truck		
Cost	300,000	
Wear & tear @25%	(75,000)	75,000
ITV c/f	225,000	
Total capital allowance		207,500

(ii) Computation income tax payable for the tax year 2020.

	K	K
Loss as per accounts		(170,000)
Add:		
Fine- breach of safety regulations	40,000	
Donation to political party	20,000	
Entertaining suppliers and customers	55,000	
Penalty- late submission of tax return	50,000	
Fees for over speeding	5,000	
Depreciation	350,000	
NAPSA penalty	35,000	

555,000	
385,000	
Less:	
Capital allowances (a)	(207,500)
Taxable profit	177,500
Company income tax payable: 177,500 X 35%)	62,125

SOLUTION TWO

(a) Telecommunications

(i) Tax treatment of roaming charges

Making a call to someone on roaming me facility entails charging both the person making the call as well as the one receiving the call.

The tax treatment of these charges will be determined by establishing where the income arising from this service facility is recorded or accrued.

When the roaming charges are receivable by a company resident here in Zambia, then that income will be subjected to the Zambian laws regarding VAT and Income tax.

(ii) Tax treatment of discounts given to airtime dealers

A discount is an allowance given for either prompt payment or buying in bulk or in fulfilling any terms of an agreement between trading parties.

A discount does not form part of the gross sales revenue that the airtime manufacturer gives to airtime dealers.

This means that a discount will be a reduction in the amount of taxable income that an air time manufacturer would record for a given tax year.

(b) Estimated Assessment

(i) An estimated assessment is determined by the tax auditor where the taxpayer fails to provide records of accounts for instance in a situation where the taxpayer claims that the records have been stolen or destroyed.

In such cases there may appear to be no basis for making an assessment therefore, an estimated assessment would be used.

(1½ marks per valid point up to 3 marks)

(ii) Basis of an estimated assessment

1. The life style of the taxpayer may act as the basis. Only persons with income of a certain level may be able to afford certain types of life style and not everybody.
2. The net worth of the taxpayer is deduced from statement of financial position in the form of Non-current assets and investments and trade payables. The net worth of the tax payer can be used to determine the taxable income by adjusting it for allowable and disallowable expenses.

(2 marks per valid point up to 4 marks)

(c) Indirect methods of verifying income

(i) Source and application of funds method

This method analyses taxpayers cash flows and comparisons of all known expenses with receipts for the period in order to determine the actual tax liability.

Net increases and decreases in assets and liabilities are taken into account along with non-deductible expenses and non-taxable receipts.

The excess of expenses over the sum of reported and non-taxable income is the amount of unreported taxable income.
This method is based on the theory that any excess expense items over income items represent an understatement of taxable income.

(ii) Mark-up method

This method produces a reconstruction of income based on the use of percentages or ratios considered typical for the business under examination in order to determine the actual tax liability.
The method consists of an analysis of sales and/or cost of sales and an application of an appropriate percentage of mark-up to arrive at the tax payer's gross receipts.
The mark-up method is the formal indirect method which overcomes the weaknesses of other indirect methods which do not effectively reconstruct income.

(iii) The net worth method

This method is based on the theory that increases in a taxpayer's net worth during a taxable year, adjusted for non-deductible expenditure and non-taxable income, must result from taxable income.

The method requires a complete reconstruction of the tax payer's financial history, all assets, liabilities, non-deductible expenses, and non-taxable income must be accounted for during the relevant period.

The tax payer's net worth is determined at the beginning and at the end of the tax year. Any difference between the net worth at the beginning and net worth at the end is the increase in the net worth of the tax payer during the year.

The taxable portion of the income can be reconstructed by adding back the non-deductible items to the increase in the net worth and subtracting that portion of the income which is partially or wholly non-taxable.
(1 mark per valid point up to 4 marks)

(iv) Unit and volume method

This method is based on the theory that the gross receipts may be determined by applying the sales price to the volume of business done by the taxpayer.
The number of units or volume of business done by the tax payer might be determined from the tax payer's books as the records under examination may be adequate as to cost of goods sold or expenses or may come from third parties.

SOLUTION THREE

(a) Importance of audit working papers:

1. They assist the team leaders and other officers who may be dealing with the current audit at a later stage.
2. They are the connecting link between the examination of a tax payer's affairs and the audit report.
3. They can be evaluated as part of the Quality Assurance process.

(b) Meaning of the following terms in the context of auditing

(i) Relevant evidence: An auditor needs to collect evidence that gives a direct relationship between work done and the audit opinion arrived at. Therefore, there should be a clear and logical relationship between audit objectives, evidence and opinion arrived at.

(ii) Reliable evidence: Evidence that is collected should be consistent or credible in order for shareholders to have confidence in the audit opinion arrived at. Therefore, there will be a need to use procedures and international audit standards.

(iii) Sufficient evidence: Sufficient relate mainly to the quantity of audit evidence that has been collected and usually linked to materiality levels of the financial statements. The quantity of the audit evidence relates to the size of the sample and that of the company as well.

(c) PC Bank Limited

Company income tax computation for the tax year 2020.

K'000 K'000

Income before taxes 34,670

Add:

Depreciation 2,500

Loss on disposal of assets 6,200

Personal to holder car 40

8,740

43,410

Less:

Decrease in general provision 2,460

Dividends 95

Unrealized trading gains 1,640

Royalties 2,500

Rental income	1,765		
Capital allowances (w)		4,553	
13,013			
Taxable business profits			30,397
Add:			
Royalties			2,500
Taxable income			32,897
Company income tax: K32,897 x 35%			11,514
Less:			
WHT on royalties (K2,500 x 15%)		(375)	
Provisional income tax payable			(6,000)
Final company income tax payable		3,639	

Workings

Capital Allowances Computation:	K'000	
Office Equipment: (K2,500 – K2,500)	Nil	
ATM Machines: K17, 150,000 x 25%	4,288	
Motor car: K700,000 x 20%	140	
Cash in transit van: K500,000 x 25%		125
Total capital allowances		4,552

SOLUTION FOUR

(a) The tax agencies such as ZRA, undertakes a tax audit whose aim is to ensure compliance with tax laws by the tax payers and develop various initiatives of promoting voluntary compliance.

A tax audit can also be done in order to review a tax return as part of routine of the process of increasing the detection of minor errors that may be present on any return.

It can also be used as a means of checking whether the tax payer has been compliant with the tax payments.

(b) The four auditing theories according to Hayes et al (2005) are described below:

1. Policeman theory.

The theory held the view that that the auditor is responsible for searching, discovering and preventing fraud. However, this view has changed and the auditor is expected to provide reasonable assurance and verify the truth and fairness of the financial statements by way of expressing an opinion.

2. The lending credibility theory.

The theory suggests that the primary function of an audit is to add credibility to the financial statement by way of expressing an opinion that users of financial statements can rely upon. It can also resolve the agency problem as management would know that auditors will audit and scrutinize the books of accounts.

3. The theory of inspired confidence (theory of rational expectations)

This is the theory that satisfies the demand for audit. An audit should be supplied as a service. The demand side for audit services is as a result of demand for audit services by users of financial statements and other third parties such as creditors. Investors have provided capital and would like to see accountability in the use of their investments. On the other side, the supply of audit services, suggested that auditors need to strive to meet the expectations of stake holders in order to reduce the audit expectation gap.

4. Agency theory (Watts and Zimmerman 1986)

This suggested that an auditor acts on behalf of both third parties such as shareholders as well as management. Management are agents who should obtain services such as goods, or other services and sell or transfer these services at a higher value in order to maximize the return on shareholder's investments. Auditing theory has been expanded in order to provide other views on audit perception that auditors are just about detecting audit fraud.

(c) The objective of Compliance Risk Management is to enable a tax administration accomplish its strategic objectives by facilitating management decision making.

It is used to stimulate compliance and prevent non-compliance, based on the knowledge of all taxpayers and related to the available capacity.
This is done through a decision making cycle or continuous loop having the following steps:

1. Identification;
2. Analysis;
3. Prioritization;
4. Treatment; &
5. Evaluation.

The first two steps relate to taxpayer behaviour causing the risks, while the next two relate to treatment planning (making choices) and implementation. The final step relates to measurement, evaluation and learning.

(d) An introductory letter is important to both parties as it lays out the program laying ahead. The letter will indicate assertiveness on the part of the auditor and proper organisation on how to approach issues

The following matters must be communicated to the client before an introductory meeting takes place:

1. Purpose of the main study
2. Time schedule for the main study
3. A list of members who will be on the audit team
4. The types of methods that will be used by the auditor
5. The information that will be requested from the auditee
6. The need to appoint or confirm the contact person

(e) A qualitative tax audit may provide the following assurances:

1. Taxpayer's accounts and records having been reviewed in sufficient depth to reach a supportable conclusion regarding all items of a material tax consequence.
2. Appropriate income test having been performed where necessary to ensure the proper and complete reporting of income regardless of the source.
3. Responsibilities of the tax payer regarding the filling of all tax returns have been ascertained.
4. The conclusions expressed are documented in sufficient details to enable the reader to comprehend the process thereby such a conclusion was reached.

END OF SOLUTION