

READING PAPER

APPLIED ZIMBABWE TAXATION 2016

POSTGRADUATE DIPLOMA IN APPLIED ACCOUNTING SCIENCES

CTA Level 2 [CAZ 2]

TEST 2: 26 APRIL 2016

Time allowed 1 hour 15 minutes including reading time

NOTES

- a) Answer all questions, clearly showing workings.
- b) The examination is based on legislation that was in force as at 31 December 2015 (including legislation proposed in December 2015 and that was promulgated as at 1 January 2016).
- c) This paper comprises of 1 question
 - 1. TAXATION OF BUSINESS INCOME [40 MARKS]
- d) Rates of tax, limits and other thresholds (to be used in the examination) are given in the appendix at the end of the question paper.
- e) Except where expressly stated, amounts are in United States Dollars (\$).
- f) Fifteen minutes reading time is allowed before attempting any questions.
- g) This reading paper consists of 8 pages including this top page.

APPLIED ZIMBABWE TAXATION (CAZ 2) LEVEL 2 TEST 2

Question 1

Steel Merchants (Private) Limited is a company registered in Zimbabwe and is involved in the manufacture of steel products which include, roofing sheets, pipes and other steel products used in the construction industry. The company commenced its operations in 2009 after the adoption of the multi-currency system in Zimbabwe and has over the years seen tremendous growth in its product range and market share. Steel Merchant's strategic drive has been the provisioning of low cost steel solutions to consumers in order to combat cheap imports coming in from China.

In March 2015 at a strategic meeting for Steel Merchant's board of directors a resolution was reached to target listing the company on the Zimbabwe Stock Exchange by the end of 2016. One of the measures agreed upon by the board in order for the successful achievement of this objective was that the company hire the service of tax consultants to assist the finance manager in preparing the 2015 tax returns. The directors are of the opinion that once the company is listed they will be more public scrutiny hence they would want the company's tax affairs to be in order.

Your firm MSN Chartered Accountants won the tender to provide tax related services to Steel Merchant's (Private) limited commencing May 2015. The partners within your firm view Steel Merchant as a client which will propel the firm's growth in future and have assigned to work on this client given that you are the most senior and experienced person within MSN's tax department.

In February 2016 Steel Merchant's finance manager sent to your office the audited financial statements for the year ended 31 December 2015 and have requested that you prepare their annual income tax return which was due to be submitted by the 30th of April 2016. All amounts are exclusive of Value Added Tax unless specifically indicated otherwise.

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Detailed below is an extract of statement of comprehensive income for the year ended 31 December 2015:

	Note	US \$000
Sales	1	12,000
Cost of sales	2	(7,200)
Gross Profit		4,800
Other Income	3	400
Administration expenses	4	(800)
Selling and distribution expenses	5	(1,100)
Staff costs	6	(800)
Profit before interest and tax		2,100
Finance Charges	7	(700)
Profit before tax		1,400

Extract of the statement of financial position as at 31 December 2015:

	Note	US \$000
Equity and Liabilities		
Share Capital		10
Retained earnings		2,200
		2,210
Non-Current Liabilities		
Long term interest bearing loan		8,200
Deferred tax		300
		8,500
Current liabilities		
Trade payables		700
Deferred Revenue	1	40
Current portion of long term interest bearing loan		640
		1,380
Total Equity and Liabilities		12,090

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Notes

1. During the 2015 financial year Steel Merchants exported 60% of their production output in quantity to customers within Southern Africa. One of Steel Merchant's customers in Botswana made a prepayment of \$40,000 in December for the supply of steel between January and May 2016. This amount has been recorded as deferred revenue in Steel Merchant's financial statements. After discussions with Steel Merchant's production manager he gave a breakdown of the costs to service the prepaid order, which were as follows:

	\$
Purchase of steel raw materials – Acquired in November 2015*	12,500
Processing and shipping of the steel – to be done in 2016	<u>15,500</u>
	<u>28,000</u>

*The steel purchased for the order was included in closing stock at 31 December 2015.

You were also informed that included in the sales figures were sales made to a customer in Bulawayo under a hire purchase agreement. In terms of the agreement the total sale price was \$18,000 payable in 6 equal monthly installments commencing 1 November 2015. Steel Merchants made a gross profit margin of 45% on this transaction.

2. Included in cost of sales were the following items:

	\$
Depreciation	56,000
Closing stock recorded at Net Realisable Value (Cost \$30,000)	24,000

3. Other income includes the following amounts amongst others:

	\$
Dividend from FirstMed Medical Society	13,000
Unrealised exchange gain on debtors	6,700
Profit on disposal of Motor Vehicles – see note 9	5,000
Dividend for Probeats Limited (South African Company)	14,000(net)*

*Steel Merchants received the dividend of \$14,000 in August 2015 after the deduction of South Africa Withholding tax of \$1,000. You also incurred bank transfer charges of \$300 in respect of this dividend.

4. In June 2015 Steel Merchants was fined \$10,000 by the Environment Agency (EMA) for failing to comply with environmental regulations in their administration process. This amount plus \$1,000 in legal fees incurred in respect of the EMA fine has been expensed in the general administration expenses.

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The company also paid insurance premiums of \$8,000 in December 2015 in respect of insurance cover for the period 1 January 2016 to 31 December 2016. This amount has been capitalised as a prepayment in the financial statements.

5. Included in selling and distribution expenses are the following amounts:

	\$
Cost of steel samples given to a customer from Lesotho	5,600
Advertising costs at the Zimbabwe International Trade Fair	8,300
Depreciation	80,000
Lunches with clients	9,200

6. Included in staff costs is an amount of \$1,500 paid to a former employee who was injured at work. The employee was permanently injured when a steel casing fell on his legs and he was forced to retire as a result of those injuries. Upon his retirement Steel Merchants decided to pay the former employee an amount of \$300 per month commencing 28 August 2015.

Also recorded under staff costs are the following donations made during the year:

	\$
Donation to University of Zimbabwe: Construction of library	120,000
Donation to the February 1 st celebrations	<u>8,000</u>
	<u><u>128,000</u></u>

7. The finance charge relate to interest paid in respect of the long term interest bearing loan. The loan was used to finance Steel Merchant's working capital requirements.
8. Steel Merchants carry out their manufacturing operations from the Southerton industrial area in Harare. The company also has a sales office in the Central Business District of Harare. The Southerton Land and buildings were acquired in 2010 for an amount of \$160,000 (\$40,000 being for the land and \$120,000 for the building). In 2015 Improvements to the tune of \$50,000 were made to the Southerton building and these were put to use as from 1 October 2015.
The sales office in the Harare CBD was acquired and brought into use in 2012. The purchase price for this building was \$90,000.
9. In May 2015 the company sold two Toyota Corolla sedan vehicles for \$8,000 each. These vehicles had been initially acquired in 2012 for \$18,000 each and have always been used in Steel Merchant's trading operations.

In your discussions with the finance manager he indicated to you that Steel Merchants has always claimed the maximum possible capital allowances where applicable.

APPENDIX

APPLIED ZIMBABWE TAXATION (CAZ 2) LEVEL 2 TEST 2

1. Annual Tax Rates

Individuals

Employment Income – 1 January to 31 December 2015

Segment of Income per annum	Amount	Rate within segment (%)	Tax	Cumulative Tax
Up to 3 600	3 600	0%		0
3 601 – 18 000	14 400	20%	2 880	2 880
18 001 – 36 000	18 000	25%	4 500	7 380
36 001 – 60 000	24 000	30%	7 200	14 580
60 001 – 120 000	60 000	35%	21 000	35 580
120 001 – 180 000	60 000	40%	24 000	59 580
180 001 – 240 000	60 000	45%	27 000	86 580
240 001 and above		50%		

- Income from trade or investments – 25 %
- The AIDS Levy of 3% applies on Income tax chargeable after tax credits.

2. Companies

- Basic Income Tax Rate – 25%*
- Manufacturing company exporting at least:
 - 30% of output (by quantity or volume) – 20%
 - 41% of output (by quantity or volume) - 17.5%
 - 51% of output (by quantity or volume) - 15%
- Mining companies – 25% *
- Special mining lease companies – 15%*
- *Plus 3% AIDS levy

3. Allowable pension deductions

	US\$
In relation to employers: in respect of each member	5 400
In relation to employees: by each member of a pension fund	5 400
In relation to each contributor to a retirement annuity fund or funds	2 700
National Social Security contributions (on a maximum monthly gross salary of US\$700)	3.5% of gross salary
<i>Aggregate maximum contributions to all the above per employee per year US\$5 400</i>	

4. Bonus exemption - \$1 000

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5. Retrenchment package

The first \$10 000 or one third of the approved retrenchment package whichever is greater, subject to a maximum exemption of \$20 000

6. Credits

- Credit for taxpayers over 55 years of age - \$900*
- Credit for blind or disabled persons - \$900

*The amounts relate to 12 months and should be reduced proportionately, if the period of assessment is less than 12 months.

7. Deemed monthly motoring benefit

Engine capacity	Benefit (\$)
0 – 1 500 cc	300
1 501 – 2 000 cc	400
2 001 – 3 000 cc	600
3 001 – and above	800

8. Capital allowances

Maximum deemed costs to be used in determining capital allowances

Asset	Deemed cost (\$)
Passenger Motor Vehicle	10 000
Staff House (actual cost not to exceed \$25 0000	10 000
School, clinic, hospital, nursing home	10 000

9. Capital Allowances: Mining

Maximum deemed costs to be used in determining the capital redemption allowance.

Asset	Deemed cost (\$)
Passenger motor vehicle	10 000
Staff housing , occupied by shareholder	10 000
School, clinic, hospital, nursing home	50 000

10. Rates of capital allowances

- Special Initial Allowance(SIA) – 25%
- Accelerated Wear and Tear – 25%
- Wear and Tear on:
 - Industrial buildings – 5%
 - Farm Buildings – 5%
 - Commercial buildings – 2.5%
 - Motor Vehicles – 20%
 - Movable assets (general rate) – 10%
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11. Capital Gains Tax

- On all listed marketable securities – exempt
- On unlisted marketable securities and acquired after 01/02/2009 – 20%
- On other immovable property acquired after 01/02/2009 – 20%
- On unlisted marketable securities acquired before 01/02/2009 – 5% (on gross proceeds)
- On other immovable property acquired before 01/02/2009 – 5% (on gross proceeds)

12. Capital Gains withholding tax on sales proceeds

- On other immovable property acquired after 01/02/2009 – 15%
- On immovable property acquired before 01/02/2009 – 5%
- On all listed marketable securities – 1%
- On unlisted marketable securities acquired before 01/02/2009 – 5%
- On unlisted marketable securities and acquired after 01/02/2009 – 5%

13. Loans

The deemed benefit per annum is calculated at the rate of LIBOR plus 5% of the amount of the loan.
The LIBOR rate for 2015 is assumed at 1% unless stated otherwise in the scenario/required.

..... **End**