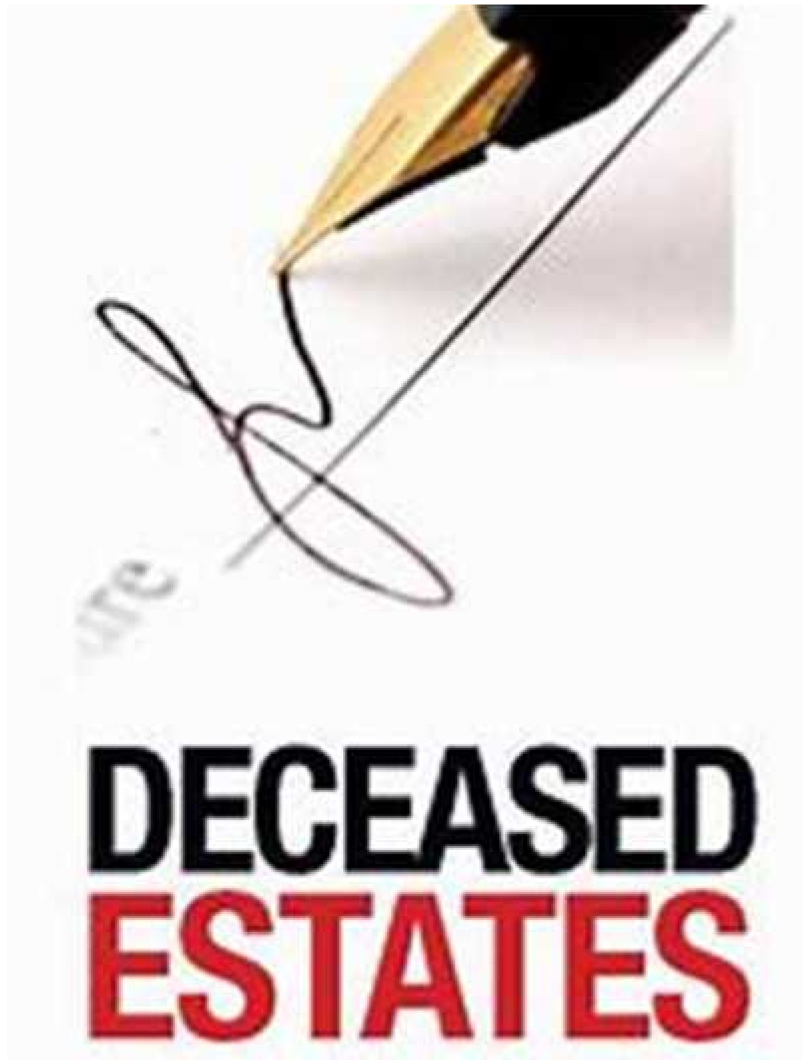
CAA

CHARTERED ACCOUNTANTS ACADEMY

DECEASED ESTATES AND TRUSTS



SECTION 2

Section 2 specifically interprets a person to include:

a. A deceased or insolvent estate; and
b. A trust, in relation to income the subject of a trust to which no beneficiary is entitled

SECTION 11

- Provision deals with INCOME DERIVED from assets in a deceased estate.
- Key terms:
  a. Ascertained beneficiaries S11(1)
  b. Assets in a deceased estate S11(1)
- Pre and Post death income.

  On the death of a taxpayer an assessment is raised on the deceased’s taxable income accruing to the date of death. A new taxpayer i.e. a deceased estate, comes into being after the death. A determination has to be made as to in whose hands post death income accrues.

SECTION 11 – POST DEATH INCOME

There are at least three possible taxpayers that may be liable to income tax after a person has died.

a. The deceased person – where income is determined to have been pre-death.
b. An ascertained beneficiary
c. The deceased estate.

Section 11 provides for the taxation of the post death income

Identifying the tax payer

Terms of a will are very important.

Section 11(2)

a. Where a specific asset is left to a specific person – ascertained beneficiary
b. The ascertained beneficiary is taxable on the income derived from the asset from the day after death of the deceased.

Section 11(3)

a. Residue in a will is taxable in the hands of the estate.
b. This is of income derived from the asset or residue from the day after death until date of distribution by the executor.

Identifying the taxable income in post death period

Section 11(4)

(a). Income by virtue of a right forming part of the assets in a deceased estate which didn't become due and payable before the death of the deceased person shall be **INCOME IF THE AMOUNT WOULD HAVE BEEN INCOME OF THE DECEASED PERSON HAD IT BEEN RECEIVED IN HIS LIFETIME.** This shall therefore be taxable in the hands of either the deceased estate or ascertained beneficiary.

(b). (a) above is not applicable if:

The deceased had no right the amount in his life time;

The amount is received ex gratia.

Expenditure against post death income

- Residence status of an estate
- Medical expenses of a deceased paid after death - claim a credit in the pre-death period.

Tax rates

Think of the identity of the income:

- Employment income
- Trade and investments income

TAXATION OF TRUSTS

- Section 2 includes Trusts in the definition of a person. Unless it has income to which a beneficiary is entitled.
- If a beneficiary has a vested right he then is taxable and the Trust is only a conduit.

Trust Income and expenditure

- Trust income maintains its identity upon distribution to a beneficiary, unless it is distributed by way of an annuity.
- The general deduction formula applies to trust income. However, no expenditure is allowable against exempt income.

Expenditure on exempt income

- In a case where trustees earn a commission on all income they earn for the trust, and part of that income is exempt. Then the commission is only deductible to the extent that it does not relate to the exempt income.

Expenditure on exempt income

- Use the following formula to determine the non-deductible portion of the expenditure:

$$\frac{\quad \times \quad}{\quad}$$

- A – exempt income
- B – direct expenditure in production of trust income
- C – total gross income created by trustees

Beneficiary rights

- Vested right – beneficiary has the right to all of the income in the trust, the trustee(s) have no discretion to distributed. All income taxed in the hands of the beneficiary, whether distributed or not.
- Contingent right – beneficiary only has right to income upon meeting certain conditions, e.g. passing CTA. Only the distributed income is taxed in the beneficiary's hands, the retained income is taxed in the hands of the trust

Beneficiary rights

- Neither vested, nor contingent right – this means that distributions are made at the discretion of the trustees. All income is taxed in the hands of the trust.

PARTNERSHIPS

INTRODUCTION

- What is a partnership?
- Does a partnership have a legal status and how does that differ from its tax status?
- How should a partnership be taxed?
- Would income earned by a partner be remuneration?

Transfer of Assets

- Three forms of transfer that require adjustments:
  - Sole trader converts into a partnership
  - New partner is admitted or partner retires/dies
  - Partnership business converts into a company
- What are the tax effects of these transfers?
- **ITA, CGT & VAT**

PARTNERSHIP TRANSACTIONS

- **Bad Debts** - cannot be claimed where they were not included in the taxpayers income in prior years.
- **Insurance Policies**

  - Joint Life Policy

  Where premiums are expensed to the partnership's account, the deduction is not allowable if the partnership is the beneficiary.

  - **Separate policy on own life ceded to the partnership**

  The partnership has become the beneficiary and therefore the premiums are no longer allowable deductions

  - **Separate policy for own benefit funded by partnership**.

  This is an allocation of partnership profits and so allowable as a deduction in computing the partnership's taxable income and taxable income in the hands of the each partner to the extent the premiums were paid on their behalf by the partnership.

Partnership Expenditure

- **Key matters**
  - In whose hands are we: Partnerships or Partner
  - Taxability of the amount as per ITA
- **Discuss the following expenses**
  - Partner's Salary
  - Interest on Capital
  - Drawings
  - Sports Subscriptions
  - Medical aid contributions
  - Partner's life policy – ceded to the partnership
  - Joint life policy
  - Partner's life policy – partnership is the beneficiary
  - Partner's life policy – partner is the beneficiary

Double Taxation Agreements

Double Taxation Agreements

- What are DTAs?
- Their Purpose?
- S91
- S92
- Where no DTA exists?

Double Taxation Agreements

- If the Zimbabwean tax is less than or equal to the foreign tax withheld the DTR = the Zimbabwean tax
- If the Zimbabwean tax is more than the foreign tax withheld the DTR = the foreign tax withheld such that the additional Zimbabwean tax chargeable will be equal to the Zimbabwean tax less foreign tax paid.

FARMING

Farming

- Why do farmers have special provisions that apply only to them?

Farming

FARMER

- Any person who derives income from pastoral, agricultural or other farming activities including income from the letting of a farm used for such purposes . Sect 2

Farming – Staff housing

- **4TH Schedule par 1**
- Buildings used mainly for the purposes of a trade wholly or mainly for the housing of his employees
- It does not include any building comprising a residential unit which exceeds US$25,000;
- Staff housing does not include a beer hall forming part of a farm compound. (ITC 1511 (1992) 54 SATC 39)

Farming – Farm Improvements

- **4th schedule par 1**
- Building, structure or work of a permanent nature (including a water furrow) used in farming operations; includes sheds, canals, permanent roads , bridges, cattle dips (not beer halls)
- It includes any building used for the purposes of a school; hospital or clinic , in connection with the taxpayer's farming operations; Limitation of cost US$10,000. 50% rule.
- It excludes any dwelling used by the taxpayer as a homestead for himself and his family;
- Also excludes farm assets covered by other specific provisions e.g. staff housing, tobacco barns, 2nd Schedule assets.

Farming - Tobacco Barn

- **4th schedule par 1**
- means any building used for the curing of tobacco;

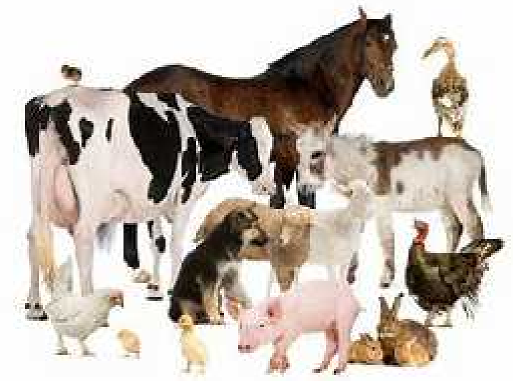
Farming – 7th Schedule deductions

A farmer shall be entitled to deduct expenditure incurred on :

1) Water conservation works. Expenditure is deductible in the year incurred notwithstanding that work might be in progress.
2) The sinking of boreholes and wells;
3) Fencing: Expenditure must not only be incurred by the taxpayer but the fencing must be used in farming operations.
4) Stumping and clearing of land;
5) Works for the prevention of soil erosion
6) Aerial and geophysical surveys.

Livestock valuation

- For ordinary livestock, the farmer may elect – in his first return – between fixed standard value (FSV), and cost maintenance value (CMV); and
- For stud livestock, the farmer may elect to use purchase price value (PPV) or FSV



Livestock Valuation

Livestock acquired without payment.

Valuation of livestock acquired by inheritance or donations:

i. If heir or donee merely sells the livestock without conducting farming operations , the proceeds are of a capital nature;
ii. If livestock farming is commenced or livestock introduced into existing farming operations a deduction is allowed.

Livestock Valuation

Livestock acquired without payment.

Valuation of livestock acquired by inheritance or donations:

i. to an heir, the fair market value, for which the valuation in the estate concerned would be used;
ii. to a donee, an amount not exceeding what would have been deductible in the donor’s hands had he sold the livestock: this is normally the FSV of livestock

Taxable Income from Drought sales – 7th schedule par 5

Proceeds from drought sales		XX
Less :		
(a)	number sold * fixed standard value	XX
(b)	total no. sold * livestock expenses Average stock#	XX
Taxable income from drought sales		XX
Relief (carried forward) [2/3 x taxable income]		XX

#Average stock = (opening stock + closing stock) / 2

Farming – Restocking Allowance – 7th schedule par 6

- Provided on the cost of restocking a herd which has been depleted by forced sales;
- The cost of purchases is allowable
- A further deduction of 50% of the purchase price granted as a restocking allowance.
- Restocking allowance subject to a restriction based on the assessed carrying capacity of the land (ACCL).

MINING

Mining

- Miners assessed in the same manner as any other taxpayer;
- Main difference is the method of claiming capital allowances;
- The capital redemption allowance(CRA) replaces SIA, W&T, scrapping allowance.
- 6 year prescription on loss carryovers not applicable to miners. Why?

Mining

In terms of Section 2 "mineral" includes any valuable crystalline or earthy substance forming part of or found within the earth's surface and produced or deposited there by natural agencies but does not include petroleum or any clay (other than fire-clay), gravel, sand, stone (other than limestone) or other like substance ordinarily won by the method of surface working known as quarrying;

Mining operation

- Includes:
  i. Any operation for the purpose of winning a mineral from the earth.
  ii. subsequent smelting and refining , by the same taxpayer of minerals won from the earth
  iii. any other operation recognised by the Commissioner , such as the re-working of mine – dumps.

Mining- Prospecting expenses

PROSPECTING (S15(2)(f)(ii))

- Refers to expenditure incurred by a person on operations either in searching for a potential claim or in searching for minerals after a claim has been pegged.
- A binding election is available to claim such expenditure from current income from any source or carry forward the expenditure to be allowed against income from mining operations in any subsequent year.
- Expenditure may include;
  - Survey costs
  - Sinking of boreholes
  - Digging of trenches and pits
  - Any other prospecting and other exploratory works undertaken for the purposes of acquiring rights to mine minerals

Capital Redemption Allowance (CRA) – Sect 15 (2) (f) (i) a.r.w 5th schedule

Definition of Capex: 5th Schedule–

Capital expenditure for mining purposes is defined as :-

(i) Expenditure on buildings, works or equipment, lease premiums,

(ii) shaft sinking (including sumps, pump chambers, stations and ore bins accessory to a shaft) ;

(iii) expenditure incurred prior to commencement of trade on preliminary surveys, boreholes, development, general administration and management, interest on loans ;

(iv) and, expenditure incurred on or after the 1st April, 1988, on any permanent building used for the purposes of—mine schools, nursing homes and clinics.

NB:

Capital expenditure does not include cost of claims and goodwill or company flotation expenses

CRA (cont.)

- Recoupment

  Amount accruing from sale , damage , destruction or other disposal of asset on which capital redemption allowance or an allowance on replacement of asset has been claimed;

  it does not include in the case of damage / destruction of assets an amount exceeding original cost.

Methods of Calculating CRA

- The redemption allowance can be calculated using either of three methods commonly referred to as
- Life of mine
- Mixed method
- New mine method
- The taxpayer has to make an election of the method preferred.

Life of mine – 5th sched para 2

- The current year's capital expenditure is added to the balance of unredeemed capital expenditure brought forward at the commencement of the current year of assessment. The total capital expenditure is then divided by the approved estimate life of the mine (in years), counting from the beginning of the current year of assessment.
- CRA = CCE + UBCE – Recoupment / Estimate of life (years)

$$CRA = \frac{CCE + UBCE - Recoupment}{\text{Estimate of life (years)}}$$

- A taxpayer who adopts the life of the mine basis in respect of a particular mine is permitted to change subsequently to the 'mixed basis'.

Life of Mine - cont

"estimate of the life of the mine" means the number of years not exceeding –

(a) In the case of a mine operated for the purpose of producing lead or zinc or lead and zinc, <u>ten years;</u>
(b) In the case of a mine operated for the purpose of producing iron, <u>five years;</u>
(c) In the case of any other mine, <u>twenty years</u>
(d) Where a taxpayer adopts this basis , he submits to ZIMRA an estimate of the number of years for which operations are expected to continue based on the certified estimates of ore reserves.
(e) The capital expenditure ranking for CRA (less recoupments) is divided by the life of mine calculated from the commencement of year of assessment concerned.

New Mine Method

New Mine Method (paragraph 4(4))

- This method is only available to those carrying on operations in a new mine as defined. This method allows the taxpayer to deduct all capital expenditure brought forward and current in the first year of production. Thereafter, capital expenditure is allowed in the year in which it is incurred.
- A new mine is defined as an undertaking which commenced regular production on or after 1/04/1968, or recommencement of a mine which has changed ownership and has been reorganised with substantially new development and new plant.
- CRA = CCE + UBCE- Recoupment.

Mixed Method

Mixed Method (paragraph 4(2))

- Under this method this method the taxpayer can make an election to claim a portion of unredeemed capital expenditure brought forward at the beginning of the year, by applying the life of the mine method to it. In addition to that portion, the whole of the capital expenditure incurred in the current year is allowed in full.
- $$CRA = CCE + \frac{(UBCE - Recoupment)}{\text{Life of mine (years)}}$$

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Restrictions on certain assets

- **Passenger Motor vehicle**

  USD 10,000

- **Staff housing**

- **US$10 000** on a building used mainly as a dwelling by an individual shareholder where he is one of not more than four individuals who control the company, where the building was erected on or after the **1st January, 2009;**
- **US$50 000** in respect of any building used mainly as a dwelling by staff employed at the school, hospital, nursing home or clinic—
- No restrictions on dwellings for mine employees

- **US$50 000** on a building used mainly as a school, hospital, clinic or nursing home in connection with the taxpayer's mining operations

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Recoupment (Sect 8(1) j

- A miner's recoupment is generally the proceeds on disposal
- A recovery (insurance proceeds) in respect of damage or destruction of an asset restricted to deductions claimed.
- Restriction if the asset sold has been subject to a limit.

  e.g. A motor vehicle acquired for $20,000 is sold for $15,000

$$\text{Recoupment} = \frac{15\,000 \times 10{,}000}{20{,}000}$$

$$= \$7{,}500$$

Transfer of assets

- Where assets are transferred between companies under the same control, or between husband and wife or in a scheme of localization if the taxpayer so elect, that the amount of capital expenditure ranking for redemption in the hands of the transferor at the time transfer is made shall rank as capital expenditure for redemption in the hands of the transferee and be deemed to be a recoupment from capital expenditure in the hands of the transferor.

General Administration and Management fees

Section 16 (1) r

- To be prohibited as a deduction is general administration and management fees paid by a subsidiary or holding company or a local branch (where the parent is a foreign company engaging in local mining operations). In respect of such expenditure as is paid before commencement of production to the extent that is exceeds 0.75% of:
  - A – (B + C)

Where,

- A – Represents the total expenditure qualifying for deduction in terms of s 15.
- B – Represents general administration and management fees paid outside Zimbabwe.
- C – Capital redemption allowance (section 15 (2) (f) (i))

- In the case of such expenditure as is paid after commencement of production to the extent that it exceeds 1% of the above formula.

2.6 Example

- The following expenses were incurred by A Ltd during the year ended 31 December 2012:

Administration fees paid outside Zimbabwe	$120,000
Depreciation	60,000
Other tax deductible expenses	420,000
Total	600,000

Capital redemption allowances = $50,000.

Allowable fees = 1% [A - (B+C)]

= 1% [600,000 – 60,000 + 50 000) - (120,000 + 50,000)

= **$4,200**

Disallowable s 16(1) r = 120,000 – 4,200

= **115,800**

QUESTIONS ?

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