Solutions

a. In respect to Note 2 discuss with supporting calculations the income tax implications of the installment credit sales assuming that Kudu takes advantage of all the available tax incentives. Your discussion should cover both the 2013 and 2014 tax years.

2013

- In terms of sect 18 to the income tax act, if a tax payer disposes of a movable property where the sale amount is receivable in installments and ownership passes after the payment of the final installment, the whole amount is deemed to have accrued to the tax payer on the date of signing the agreement. 2 marks
- Therefore in respect of the sales of the two vehicles on credit, Kudu should have recognised $36 000 ($1 000 * 36) each as gross income in the 2013 year of assessment. 2 mark
- The $18 000 incurred for the importation of each vehicle would have been allowed as a deduction in terms of sect 15. 2 mark
- However in terms of section 18 Kudu will be allowed an allowance in respect of installments not yet due and receivable as at 31 December 2013. 1 marks
- The allowance is calculates as follows:

	$	
Total sales proceeds ($1 000 * 36 * 2)	72 000	1
Less cost of sales		
Importation costs ($21 600 * 2)	(43 200)	1
Gross Profit	28 800	
Gross Profit % 28 800/72 000 * 100	40%	1
Total installments not yet due and receivable as 31 December 2013:		
(36-8)* $1 000 * 2	56 000	1
Sect 18 Allowance: $56 000 * 40%	22 400	1

2014

- In 2014 the allowance deducted in 2013 is brought into gross income in terms sect 18 and a further allowance is granted in respect of installments not yet due and receivable as at 31 December 2014: 1
- Calculated as follows:

	$	
2013 Sect 18 allowance b/f	22 400	1
Less 2014 sect 14 allowance: (36-20)*1 000 * 2 * 40%)	(12 800)	1

b. Calculate the minimum taxable income and income tax payable by Kudu (Pvt) Ltd for the year ended 31 December 2014. For amounts which require no adjustment provide a brief explanation and indicate by the use of a zero on your tax computation.

	$	$	Marks
Profit before tax		510 000	½
Note 1			
Invoices for bookings made – sect 8 gross income		0	½
Fines charged for damages – compensation for revenue expenses – gross income		0	1
Fuel sales – sect 8 gross income		0	½
Note 2			
Cash sales of new vehicles – sect 8 gross income		0	½
Cash sales of second hand vehicles – sect 8 gross income		0	½
Sect 18 allowance b/f – see part a		22 400	1
Sect 18 allowance 2014 – see part a		(12 800)	1
Note 3			
Opening stock – deductible sect 15 2(		0	½
Purchases – deduction sec 15 2 (a)		0	½
Depreciation – no expense incurred		300 000	1
Closing stock – gross income sect 8		0	½
Note 4			
Fair value gain – no amount received		(13 000)	1
Finance income – taxed in 2013		(5 000)	1
Profit on disposal of vehicles – not received		(15 000)	1
Recoupments Motor vehicles: W1		24 600	6
Profit on disposal of office building – not received		(80 000)	1
Recoupment on disposal of office building :$130 000*2.5%*2 (recoupment limited to capital allowances previously granted)		6 500	2
Capital allowances: New office building: $150 000 * 2.5%		(3 750)	1
Insurance proceeds – gross income received in respect of revenue expenses		0	1
Repair costs – deductible sect 15 2 (b)		0	1
Note 5			
Donation Harare high – sect 15 2 (		0	1
Depreciation – no expense incurred		13 000	1
Entertainment allowance – prohibited sect 16		15 000	1
Staff lunches – entertainment therefore prohibited sect 16		4 500	1
Note 6			
Travel costs to Zambia – deductible sect 15 2(a)		0	1
Advertising costs – deductible sect 15 2(a)		0	½
Bad debts: capital in nature, not in business of giving loans		800	1
Note 7			
Thin capitalisation sect 16 - w2		82 727	3
Note 8			

Recoupment : $110 000 * 2.5% * 2 (recoupment limited to capital allowances previously granted)		5 500	2
Additional information			
Mazda atenza: Accelerated W&T - $80 000*25%		(20 000)	1
Toyota corolla: Accelerated W&T - $25 000*25%		(6 250)	1
Isuzu KB Double cabs: SIA - $125 000 * 25%		(31 250)	1
Office furniture: Accelerated W&T - $15 000* 25%		(3 750)	1
Computer equipment: Accelerated W&T - $10 000* 25%		(2 500)	1
Total taxable income		791 727	
Tax @ 25.75%		203 870	1
Less Payments on QPDs		(145 000)	1
		58 870	
Total			**40**

Workings:

W1 : Recoupments Motor Vehicles

Description	Year of purchase	Cost	ITV	Sale Price	Recoupment	Marks
Mazda 323 sedan	2011	7 000	1 750	3 200	1 450	1
Toyota corolla sedan	2011	6 800	1 700	3 100	1 400	1
Toyota prado (SUV)	2011	45 000	11 250	29 000	17 750	2
Navara twin cab	2012	23 000	11 500	15 500	4 000	2
					24 600	

W2 : Thin capitalisation

Current debt to equity ratio: (4 200 000 + 900 000)/1 160 000
4.4 : 1

Allowable interest: 3/4.4 * $260 0000
$177 273

Disallowed interest: $260 000 - $177 273
$82 727

c. In respect of Note 1 to Note 4 discuss with supporting calculations were relevant the Value Added Tax implications to Kudu of the information provided. 25 marks

Note 1

Invoices for bookings made

- The supply of a motor vehicle under a rental agreement is a deemed supply in terms of sect 7 (10). 1
- The time of supply would be the earlier of a payment being received or customer making use of the vehicle. 1
- The output tax would be calculated as follows: $1 050 000 * 15% = $157 500 1

Fines for damages to vehicles

- The fine has been charged by Kudu in the furtherance of trade hence subject to VAT. 1
- The amount of output tax would be : $100 000 * 15% = $15 000 1

Fuel

- Fuel is an exempt supply in terms of sect 11 therefore no output tax charged. 1

Note 2

Cash sales of new vehicles

- The supply of new vehicles has been made in the furtherance of trade therefore subject to VAT. 1
- The time of supply would be the earlier of delivery of the vehicle and the receipt of the cash. 1
- The value of supply would be the cash price of the motor vehicles 1
- Output tax: $1 400 000 * 15% = $210 000 1

Cash sales of second hand motor vehicles

- In terms of sect 6 1 (a), the sale of second hand motor vehicles is not subject to VAT. 2

Installment credit sale

- The value of supply for sales under installment credit sale agreement is the cash price of the vehicles, which in this case is $28 000 each. 1
- The time of supply is the earlier of delivery and signing of the sale agreement, therefore in this case the time of supply is 1 May 2013. 1
- Output tax that should have been charged: $28 000 * 2 * 15% = $8 400 1

Note 3

Opening stock

- Kudu would have claimed an input tax deduction in respect of the stock in the year of purchase. 1

- Therefore in 2014 no further input tax deduction.

Purchases: Imported vehicles

- Goods imported into Zimbabwe are subject import VAT in terms of sect 6 1(b) 1
- Since Kudu is a motor dealer the company will be able to claim an input tax deduction in respect of the import VAT regardless of the fact that some of the vehicles may be passenger motor vehicles as defined. Sect 16 2 d(i). 2

Depreciation

- No supply received hence no input tax deduction allowed. 1

Closing stock

- Not a supply since the stock is yet to be sold. 1

Note 4

Fair value gain on shares

- No supply made hence no output tax chargeable 1

Finance income: on vehicles on credit sale

- Finance income is an exempt supply in terms of sect 11 hence no output VAT chargeable. 1

Disposal of motor vehicles.

- These are second hand vehicles hence no Output VAT charged as per sect 6 1(a). 2

Disposal of office building.

- Since the building was being used in the making of taxable supplies the sale of the building attracts output tax at the standard rate of 15%. 1
- Time of supply is the earlier of receipt of the $210 000 or transfer of ownership 1
- Therefore Kudu should have charged output tax of $210 000 * 15% = $31 500 1
- The new building in Newlands was bought from a registered operator and is being used for the purposes of making taxable supplies. Kudu will be able to claim an input tax deduction of $150 000 * 15% = $22 500. 2

Insurance proceeds:

- In terms of sect 7 (7) insurance proceeds are a deemed supply, therefore Kudu should account for the related output tax. 1
- Therefore Kudu should remit output tax of $7 000* 15/115 = $913. 2

d. With reference to the information provided in Note 4 calculate the capital gains tax payable on the disposal of the office building in Southerton by Kudu (Pvt) Ltd. 5 marks

	$	
Proceeds	210 000	1/2
Less Recoupment – refer to part b	(6 500)	1/2
	203 500	
Less Allowable deductions		
Cost	(130 000)	1
Capital allowances previously granted	6 500	1/2
Inflation allowance: $130 000* 2.5% *3	(9 750)	1
	70 250	
Roll forward relief: $70 250*150/210	(50 179)	2
	20 071	
Tax @ 20%	4 014	½

e. With reference to the information in note 8 discuss with supporting calculations the capital gains tax implications of the insurance proceeds received in 2012 and the subsequent disposal in 2014 of the bonded warehouse. 15 marks

2012:

- The compensation from the insurance company constitutes a deemed sale in terms of sect 8 2(b). 1
- Since the proceeds from the insurance company were used to construct a replacement asset the proceeds from the insurance company will taxed to the extent of proceeds not used in the construction of the replacement asset. Sect 13 3(b). 2

	$	
Proceeds	120 000	1/2
Recoupment - $80 000*2.5%	(2 000)	1
	118 000	
Less allowable deductions		
Cost	(80 000)	1
Capital allowances previously granted	2 000	1/2
Inflation allowance: $80 000*2.5%*2	(4 000)	1
	36 000	
Less Gain not taxable: 110/120*36 000- sect 13 3(b)	(33 000)	2
Taxable Gain	3 000	

Tax @ 20%	600	1/2

- However the $110 000 incurred in constructing the replacement warehouse will not be allowable as a deduction on the subsequent disposal of the new warehouse sect 13 (4). 1

2014

- In 2014 on the disposal of the warehouse the deductible cost would be $80 000 being the cost of the warehouse which was initially purchased in 2011. Sect 13 (4). 1

	$	
Proceeds	140 000	1/2
Recoupment: see part b	(5 500)	1/2
	134 500	
Less allowable deductions		
Cost	(80 000)	2
Capital allowances previously granted	5 500	1/2
Inflation allowance: $80 000*2.5%*4	(8 000)	2
	52 000	
Tax @ 20%	10 400	