

Chalimbana University

Integrity. Service. Excellence

DIRECTORATE OF DISTANCE EDUCATION

BPT 4101: TAXATION

FIRST EDITION 2021

Chalimbana University

 Private Bag E1

 Lusaka

 Zambia

 Website: www.chau.ac

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**Acknowledgements**

Chalimbana University wishes to thank Alice Chinyama for writing the Taxation module.

Module Overview

Pre-requisite: BMT 1100 AND BCA 2100

Rationale

Understanding Taxation will help the learners to develop a skill of logical reasoning, because it applies to most aspects of everyday life and the company’s well being.

Aim

This course intends to give the students an understanding of the concepts of taxation and how they are applied in tax administration in business

Learning Outcomes

By the end of this course, students should be able to:

* Describe the theoretical and legal framework of taxation.
* Demonstrate the principles of taxation and the role played by taxation in the economy.
* Prepare tax computations and returns for individuals, partnerships and companies.

Study Skills

As an adult learner, your approach to learning will be different to that of your school days: you will choose when you want to study, you will have professional and/or personal motivation for doing so and you will most likely be fitting your study activities around other professional or domestic responsibilities. Essentially you will be taking control of your learning environment. As a consequence, you will need to consider performance issues related to time management, goal setting, stress management, etc. Perhaps you will also need to acquaint yourself with areas such as essay planning, searching for information, writing, coping with examinations and using the internet as a learning resource.

Your most significant considerations will be *time* and *space* i.e. the time you dedicate to your learning and the environment in which you engage in that learning. It is recommended that you take time now before starting your self-study to familiarise yourself with these issues. There are a number of excellent resources on the web. A few suggested links are:

<http://www.how-to-study.com/>

The “How to study” website is dedicated to study skills resources. You will find links to study preparation (a list of nine essentials for a good study place), taking notes, strategies for reading text books, using reference sources, test anxiety.

<http://www.ucc.vt.edu/stdysk/stdyhlp.html>

This is the website of the Virginia Tech, Division of Student Affairs. You will find links to time scheduling (including a “where does time go?” link), a study skill checklist, basic concentration techniques, control of the study environment, note taking, how to read essays for analysis, memory skills (“remembering”).

Timeframe

You are expected to spend at least 18 hours of study time on this module. In addition, there shall be arranged contact sessions with lecturers from the University during residential possibly in April, August and December. You are requested to spend your time judiciously so that you reap maximum benefit from the course.

Need Help

In case you have difficulties during the duration of the course, please get in touch with your lecturer for routine enquiries during working days (Monday-Friday) from 08:00 to 17:00 hours on Cell: +260963804004; E-mail: adsikalumbi@gmail.com; website: [www.chau.ac.zm](http://www.chau.ac.zm).You can also see your lecturer at the office during working hours as stated above.

You are free to utilise the services of the University Library which opens from 07:00 hours to 20:00 hours every working day.

It will be important for you to carry your student identity card for you to access the library and let alone borrow books.

Required Resources

In this module you will need the following tools;

Note Book

Assessment

In this module you will be assessed on the basis of your performance as follows:

Continuous Assessment 50%

Assignment 10%

Project 15%

2 Tests of equal weight 25%

Final Examination 50%

Total 100%

**Prescribed Readings**

1. Mulolani, A. (2013). Foundation Taxation. Lusaka.
2. Alm, J. (2011). *The economics of Taxation*. Edward Elgar Publishing.

**Recommended Reading**

1. JCTR, (2011). The Taxation System in Zambia: Technical Report. JCTR, Lusaka

**UNIT 1 - INTRODUCTION – NATURE AND PURPOSE OF TAXATION IN ZAMBIA**

This unit introduces the nature and purpose of taxation

**1.1 Learning Outcome**

After completing this unit, students should be able to:

* Define the term taxation
* Trace the history of taxation in Zambia
* Understand the principles of taxation
* Explain the classification of tax
* Identify the elements of tax



**1.2 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**1.3 TAX DEFINED**

Taxation may be defined as the process of raising revenue for central government through levies on income and gains of resident persons.

**1.4 BRIEF HISTORY OF TAXATION IN ZAMBIA**

Taxation as we know it today, that is, the legislation and monetary aspect of it began with the coming in of Europeans. As Africans, we had our own version of taxation, which included provision of labor and various gifts and trophies to traditional chiefs including tilling fields of the royalty as well as contribution of food to the traditional leaders. Men enlisting for fighting in tribal warfare may be considered as a form of taxation.

**Note:** To discuss the history of taxation in Zambia, we will do well to identify important dates in our history.

**Period before 1890:**

We were organized in tribal communities and by and large taxation took the form of paying in kind to the traditional chief’s food and labour. It must be stated that in rural communities this continues to this day.

**Period between 1890 (1900) - 1924**

Zambia as we know it today was ruled indirectly by Britain through the British South Africa Company (BSAC). The white settlers imposed taxes such as the hut tax and the head tax etc. Natives who could not find money to pay the taxes were forced to leave their villages to go and look for work in the mines or outside Zambian in particular Southern Rhodesia and South Africa Forced Labour.

**Period between 1924 - 1964**

Direct British Rule the above taxes continue. However, in 1954 we saw the first piece of legislation being introduced the promulgation of the income tax Act, the precursor of today Income Tax Act. It must be stated that this Act borrowed heavily from the British tax system.

**1.4.1 The relationship between the Zambian tax system and that of Britain**

At the time of the Napoleon wars in Europe, the British Government decided to come up with a measure of raising revenue for the Army. This was in the form of tax on income at very low rates. The rate of tax on income was about 5% at most. The introduction of tax on income was intended to be only a temporal measure. The residents were levied this tax without major problems. After the war had ended, the government realized that the system was very efficient as huge amounts of revenue were collected from residents. As a result, the system of tax on income was made permanent and tax rates had to rise gradually to marginal rates of about 98%. The rates then dropped to reasonable rates which are currently prevailing.

When Northern Rhodesia (now Zambia) was colonized by Britain, the system was of tax on income was extended here. Individuals who were in employment were required to pay the tax. After independence, the system of tax on income continued to apply as previously. Apart from income tax, new taxes were introduced in the United Kingdom such as corporation tax and capital gain tax. To date, these other taxes are not available in Zambia. However, if they had come into existence before Zambia became independent, they could have been extended as well.

**Period after Independence (1964)**

In 1966, the Income Tax Act was enacted and has been amended from time to time. In 1994, there was a major revision to the Income Tax Act in Zambia.

**1.5 FUNCTIONS OF TAXATION**

Taxation can be used for the following three functions.

1. Fiscal or budgetary and allocation function
2. Wealth distribution function
3. Economic function

**Budgetary and allocation function**

The fiscal system deals with government revenue to finance government expenditure such as: Financing the education system

* Financing the Health System
* Paying personal emoluments for government employees
* Financing the country's infrastructure development such as roads, bridges etc.
* Financing subsidies
* Providing social benefits etc
* The major items of government expenditure and its source of revenue are clearly shown in the National Annual Budget.
* Apart from taxation, other sources of government revenue include:-
* Donor funding
* Borrowing from the International Financial institution such as the IMF and the IBRD (the World Bank).
* Government domestic borrowing

**Re-distribution of Wealth and Income**

Taxation is one of the Government's ways of removing inequalities i.e. the government will generally collect higher taxes from the well to do and re-distribute the funds collected to the less well to do through the construction of public establishment such as schools, hospitals, public universities etc.

**Economic Function**

Governments may use taxation as a tool to achieve specific economic goals.

**Examples**

* + 1. All governments desire that their national economies experience Growth.

Using taxation as a tool, governments may use money raised through taxation to establish strategic industry such as iron and steel industry, thereby creating employment and facilitating economic growth. Government investment in a national railway system and rural electrification programme with taxpayer's money will achieve the same goal

* + 1. Protection of local Industry the infant industry argument.

Governments have a responsibility to protect local industry from unfair foreign competitions. To protect the local Zambian industries from unfair foreign competition the tariffs levied on imported goods aim at raising the prices of those goods that come from low production cost countries and as such would put local industries at a disadvantage in terms of a pricing if no taxes were levied on them.

**Use of taxation**

1. Economic regulation
2. Macroeconomic stabilization. You may use your knowledge in Economics to answer this question.

**1.6 FEATURES OF A GOOD TAX SYSTEM**

Adam Smith in 1776 coined the following four maxims or properties of good taxation.

1. The tax which each individual is bound to pay' ought To be certain, and not arbitrary. The time of payment, the manner of payment the quantity to be paid, ought all to be clear.
2. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it, e.g., the withholding tax paid on rentals is paid at the time, which is convenient for the contributor.
3. Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state.
4. The subjects of every state ought to contribute towards the support of the Government as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state.

The other maxims were those enunciated by Stieglitz in 1980. Stieglitz characteristics of good taxes can be summarized as follows:-

1. **Economic efficiency** - The tax should not prevent efficient allocation ofresources.
2. **Administrative simplicity**- The tax should be easy and inexpensive to administer.
3. **Flexibility** - The tax system should respond easily to changes in economic conditions.
4. **Transparency** - Individuals should be able to ascertain their tax burdens so that burdens can be politically tailored to what society considers desirable.
5. **Fairness** -The tax system should be fair in its treatment of different individuals observing both horizontal and vertical equity.

Horizontal equity advocates that individuals who are the same in all relevant aspects should be treated equally; and vertical equity advocates that individuals who are better able to pay higher taxes should bear a higher share of total taxes.

The above maxims by the two authors, Adams and Stieglitz can be synthesized and summarized as follows:-

1. **EQUITY**

Equity means fairness. The tax system should be seen to be fair. This would mean that persons with a higher income should pay more tax than those with lower incomes. This is called vertical equity. It also means that given two persons with the same amount of income, the two should pay the same amount of tax this is horizontal equity.

1. **ECONOMY**

The cost of collecting the tax should not exceed the revenue raised or benefit sought.

1. **CONVENIENCE**

A tax system should not unnecessarily cause undue hardship on the taxpayer. It should be convenient to both taxpayer and administer.

One way of making the payment of taxes convenient to the taxpayer is to deduct the taxes at source (withholding tax). For instance, PAYE and other withholding tax schemes in place.

### **SIMPLICITY**

The tax system must be simple and easy to understand by the taxpayer. The tax laws and regulations must be comprehensive to the taxpayer. They must be unambiguous and certain, both to the taxpayer and the tax administrator.

1. The tax system should be able to generate adequate revenue to cover government expenditure at all levels.

**1.7 CLASIFICATION OF TAXES**

Taxes can be classified as direct taxes, indirect taxes, capital taxes, revenue taxes, progressive taxes, regressive taxes and proportional taxes as follows:-

**Direct Taxes**

These are taxes that are levied directly on the income and gains. Normally a percentage of the income or gain is paid in the form of a tax. Examples of Direct taxes in Zambia are:-

* Income Tax such as PAYE
* Mineral Royalty tax
* Property Transfer Tax

In general, direct taxes are Progressive. The amount of tax payable is dependent on the level of income. The higher the income, the higher the tax and the lower the income, the lower the amount of tax. Persons whose income levels are low, therefore, will not pay the same amount of tax as those whose income levels are high.

### **Indirect Taxes**

These are taxes that are imposed indirectly. They are expenditure taxes and therefore, they are borne by consumers. Traders who are registered for charging indirect taxes charge these taxes on the supplies they make and collect the tax on behalf of the Zambia Revenue Authority (ZRA). The indirect tax collected must be paid to ZRA by set date.

The amount of indirect tax payable does not depend upon the level of income of the consumer. Both those who are in the low income group as well as those who are in the high income group pay an equal amount in the form of taxes. Example include Value Added Tax; Excise Duty, Import Duty etc.

**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 a capital tax is Property Transfer Tax.

**Revenue Taxes**

These are taxes which are levied on revenue receipts. A revenue receipt is a receipt arising from a sale of a non-capital item. Items acquired with a view to subsequent resale are non-capital items. When they are sold, the amount received is a revenue receipt or income and is subjected to a revenue tax, e.g. Income Tax.

**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 fall. VAT is a regressive tax because the rate of VAT is the same on the good whether that good is bought by a rich person or by a poor person.

**Progressive Taxes**

These are taxes that represent a larger proportion of the person's income as that person's income rises. The average rate of taxation rises. The rates of tax for lower income levels are less than the tax rates for higher income levels. Income tax is generally an example of a progressive tax where it is levied at different tax rates such that low income is taxable at lower rates. In Zambia, this is the case concerning personal income tax. Lower income is chargeable at lower income tax rates and higher income is chargeable at higher tax rates.

**Proportional taxes**

These are taxes where the percentage of income paid in taxation always stays the same. The average rate of taxation is constant irrespective of the level of income.

**1.8 SOURCES OF TAX LAW IN ZAMBIA**

It is apparently clear that the operation of a tax system requires rules and regulations. These rules and regulations constitute tax law. There are typically three sources of tax law in Zambia, namely:-

1. The statutes
2. Decided Court Cases - Case Law
3. Statutory Instruments

**The Statutes**

These are statutes or Acts of Parliament. They form the principal law. The Main Acts of Parliament, which control the tax affairs of the Republic of Zambia, include the following:-

* + 1. The Zambia Revenue Act;
		2. Income Tax Act, and its Annual

Amendments;

* + 1. The Customs and Excise Act;
		2. The Value Added Tax Act

**Case Law**

There is no common tax law in Zambia. Judges cannot make tax law.

However, decided cases in taxation will assist with the interpretation of a particular statute which relates to the specific circumstances of a case.

**Statutory Instruments**

These are a form of legislation issued by a Government Minister. Statutory instruments related to tax matters are issued from time to time by the Minister of Finance and National Planning.

Other sources of legislation derive directly from the Zambia Revenue Authority. While these do not have a legal effect, they assist in the smooth running of the taxation system. These sources include the following:-

**Practice Notes**

These are issued by the ZRA to indicate the ZRA's interpretation of a statute. The practice notes are normally issued following amendments to Taxes Acts.

**UNIT 2 – TAX ADMINISTRATION IN ZAMBIA**

 **2.1** **Introduction**

This unit introduces you to the operations of the Zambia Revenue Authority, the organ mandated by law to administer and manage taxes on behalf of the Zambian Government.

**2.2 Learning Outcome**

After completing this unit you should be able to: -

* Understand the structure of the Zambia Revenue Authority (ZRA)
* Understand the Operational Activities of the ZRA
* Explain the various tax collection methods such as withholding taxes and provisional tax
* Explain the grievance handling procedure regarding tax disputes.



**1.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**1.4 THE ZAMBIA REVENUE AUTHORITY (ZRA)**

The Zambia Revenue Authority (ZRA) is a corporate body responsible for the imposition and collection of taxes in Zambia. It falls under the Ministry of Finance and Economic Planning. ZRA was established on 1 stApril 1994 by an Act of Parliament. A Board oversees ZRA's operations. The Chief Executive Officer of ZRA is the Commissioner General who is appointed by the Republican President.

The authority was created to redress the serious shortfall in revenues. The goal of the Zambia Revenue Authority is to **maximise tax compliance** and **increase domestic revenue** yield**.**ZRA is expected to **advise the Government on matters of taxation policy**.

**ZRA’S MISSION STATEMENT**

The mission of the Zambia Revenue Authority is to maximise and sustain revenue collection through integrated, efficient, cost effective and transparent systems, professionally managed to meet the expectations of all stakeholders.

ZRA is divided into two operational division namely:

 (a) Domestic Taxes Division

 (b) Customs Services Division

Each of these operational divisions is headed by a Commissioner who reports to the Commissioner General.

**OPERATIONAL STRUCTURE AT ZRA**



### **NOTE**

1. Board of Directors - These oversee ZRA's operations. Board members are appointed by the Minister of Finance and Economic Planning and are predominantly drawn from the private sector. The Board elects its own Chairman thence the Chairman of the Board is elected from among the Board members by the Board members themselves.
2. Commissioner General - Is the Chief Executive Officer who reports to the ZRA Board. He is appointed by the Republican President.
3. Domestic Taxes Division - Headed by a Commissioner. Domestic taxes, this division is responsible for the administration of Income Tax, property transfer tax, mineral royalty tax and domestic value added tax. In as far as VAT is concerned, the division grants registration for VAT purposes to eligible traders so that they are able to charge Vat on their taxable supplies and pay that Vat to ZRA.
4. Customs Services Division - This is the division that has been set up to deal with customs and Excise duties and Import Vat. It is headed by the commissioner - customs services

**OTHER DIVISIONS AND DEPARTMENTS OF THE ZRA**

Apart from the three operational divisions mentioned above, ZRA had three corporate divisions namely:-

* Finance, which incorporate the treasury function
* Human Resource Division
* Support Services Division

There are other three departments:

* Legal Services Department
* Information technology
* Internal Audit Department

**PURPOSE OF THE ZAMBIA REVENUE AUTHORITY**

1. Efficiently collect tax on behalf of government.
2. Assess taxes for the charge year.
3. Ensure compliance

**RESPONSIBILITIES OF ZRA**

To ensure that all relevant statutory provisions are enforced, i.e. the ITA; VAT and customs and Excise Act.

* + 1. To assess and collect taxes and duties at the right time without causing undue burden to the Public.
		2. Encouragement of the public to come forward and pay tax voluntarily
		3. Facilitation of International trade
		4. Give advice to Ministers on aspects of tax policy.

**POWERS OF THE COMMISSIONOR GENERAL**

The Commissioner General has the following powers to:-

* Request a return to be submitted at anytime
* Request accounts and document to be submitted for examination
* Examine any person for the purpose of obtaining information
* Search and seize money, documents and property.

**UNIT 3 - TAXATION OF INDIVIDUAL PERSONS**

**3.1 Introduction**

This unit introduces us to the computation of income tax for individual persons. We look at the calculation of income tax liability to an individual person with various sources of income be it from employment, business profits or investments or indeed any combinations of these.

**3.2 Learning Outcome**

After completing this unit you should be able to:-

* Explain the meaning of the terms:-

Residence, Ordinary Residence and domicile as they relate to individual persons.

* Describe the categories of taxable and exempt persons
* Aggregate an individual's income and compute the total taxable income.
*  Calculate income tax payable by individuals given various sources of income.

In order for us to compute the tax charge for an individual person, we need to be clear on the following terms.

* Charge Year
* Taxable Persons
* Exempt Persons
* Taxable Income
* Exempt Income

**TAXABLE PERSONS**

Income tax is chargeable on the income of persons "**resident"** and "**ordinarily resident** in Zambia.

**INDIVIDUALS**

An individual is resident in Zambia if he or she is physically present in Zambia for a period of not less than 183 days in a charge year.

For example, if Mr Ali is physically present in Zambia for 183 or more days in the charge year 2020, he will be resident in Zambia for that charge year.

**RESIDENCE**

An individual person is resident if:-

(l) He or she is physically present in Zambia for a period of not less than 183 days in a charge year.

1. He or she habitually stays in Zambia for at least 3 months in a year for a consecutive period of three years.
2. He or she has intention to permanently stay in Zambia (Applicable to persons coming to Zambia for the first time- if such persons express intention to stay in Zambia permanently then they are accorded the "residence status" in Zambia under tax law).

**ORDINARY RESIDENCE**

Individuals who **normally live in Zambia** are resident and ordinary resident in Zambia.

Individuals who come to Zambia with the intention of remaining here for more than 12 months are deemed to be resident and ordinarily resident in Zambia from the date of arrival.

**DOMICILE**

A person is domiciled in the country that is his or her permanent home. The two types of domicile are domicile of origin and domicile of choice.

* Domicile of origin is the domicile acquired at birth. This means that individuals are domiciled in the country in which they are born.
* Domicile of choice is the domicile that is acquired by choice. Individuals can make a choice as *to* what country should be their permanent home once they attain the age of sixteen years.

The concept of domicile may affect the amount of income that will be assessed on a taxable individual where such an individual has income from all over the world. Individual who are domiciled in Zambia would be liable to Zambian income Tax on their world wide income whether the foreign income is remitted to Zambia or not, unless the income is specifically exempt from income tax.

**EXEMPT PERSONS**

Persons who are not resident in Zambia are exempt from Zambia Income Tax.

Certain Persons are **exempt** from Zambia income tax although they are resident and ordinarily resident in Zambia. These persons include:

* Republican President on the income received as President
* The Income of Chiefs received from the Government
* Local Authorities
* Commonwealth Development Corporation
* Club, society or association organized only for Social Welfare or recreation and improvement etc. If its income may not be received in any way by a member or shareholder.
* Registered Trade Unions
* Political parties registered as a statutory society under the societies Act.
* Persons receiving social cash transfers

**TAXABLE AND EXEMPT INCOME**

Income that is liable to tax is income that arises from a **source within Zambia** or deemed to be within Zambia.

**TAXABLE INCOME**

Taxable income includes the following:-

* Rental Income from letting of property in Zambia
* Profits or gains derived from Business
* Emoluments from holding an office or from being employed
* Interest from Banks and Building societies
* Loan and Debenture interest
* Dividends
* Royalties received
* Income received by way of annuities

**EXEMPT INCOME**

Certain Income is exempt from tax. These include:-

* Scholarships or bursaries payments for education and maintenance during education.
* The emoluments of the Republican president which are received as a result of holding that office
* The emoluments of chiefs including those of the Litunga
* War disability pensions
* Income received by way of grant as compensation for loss of office or disturbance by an officer admitted to the permanent and pensionable establishment of the government.
* Income received in conjunction with the award of military, police, fire brigade or decoration.
* Income received as an old age pension paid out of public funds.
* Income received as compensation or benefit paid under any written law in respect of injury or disease suffered in employment.

**INTRODUCTION TO PERSONAL TAXATION COMPUTATIONS**

**CHARGE YEAR**

A **charge year** is a year for which tax is chargeable. It is also known as a year of assessment, a fiscal year or an income tax year. Income and gains arising in a particular charge year are taxable in that charge year.

In Zambia, a charge year runs from 1 January to 31 December. For example, the year from 1 January 2020 to 31 December 2020 is the charge year 2020.

**PERSONAL TAX COMPUTATION**

An individual’s income that arises in a given tax year is aggregated to arrive at the total taxable income for that year. Income tax rates applicable to that tax year are then applied on the income to calculate income tax payable. Certain income is not subjected to assessment at the end of the tax year because it is taxable at source.

For the tax year 2020, the income tax rates are as follows:

***Income band Total income Rate***

 K %

First K1 – K39, 600 39,600 0

Next K39, 601 – K49, 200 9,600 25

Next K49, 201 – K74, 400 25,200 30

Over K74, 400 37.5

The rate of income tax on income from **farming is 10%.** This means the excess of farming profits over the tax free amount (the first K39, 600 for the tax year 2020) is taxable at the rate of only 10% for individuals.

**EXAMPLE**

Mr. Chushi has business profit of K79, 000 for the tax year 2020. The turnover of the business for the tax year 2020 was K900, 000.

**Required**

Calculate the income tax payable by Mr. Chushi for the tax year 2020.

**SOLUTIONS**

MR. CHUSHI

PERSONAL INCOME TAX COMPUTATION FOR 2020

Business profit 79, 000

Less tax free income (39, 600)

 39, 400

Income tax

25% $×$ K9,600 2,400

30% $×$ K25,200 7,560

37.5 % $×$ K4, 600 1,725

Income Tax Payable 11,685

**EXAMPLE 2**

Mrs. Tundu runs a farm on a commercial basis in the Central Province of Zambia. The annual turnover from her business has always exceeded K800,000. Her farming profits for the tax year 2020 were KI09,500. She has no other sources of income.

**Required**

Calculate, for Mrs.Tundu, the income tax payable for the tax year 2020.

**SOLUTION**

MRS. TUNDU

PERSONAL INCOME TAX COMPUTATION FOR 2020

 K

Farming profit 109,500

Less tax free income (39,600)

 69,900

Income tax payable: 15%X K69, 900 6,990

**UNIT 4** - **TAXATION OF INDIVIDUALS IN EMPLOYMENT**

**4.1 Introduction**

This unit introduces us to the taxation of individuals in employment and the operation of the PAYE system.

**4.2 Learning Outcome**

After completing this unit you should be able to:

* Explain the tax treatment of various payments made to employees.
* Compute income tax on the payments made on termination of employment.
* Explain the operation of the pay as you earn system.



**4.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**EMOLUMENTS**

The term emoluments include all payments made to an employee or office holder, whether before the commencement of employment or upon the cessation of employment.Such payments include wages and salaries, allowances, bonuses, tips and service charges, overtime pay and payments on termination of employment.

**OFFICE**

Is a position that exists independently of the person presently occupying it. It must be capable of being declared vacant.

**EMPLOYMENT**

Exists where there is a legal relationship of master and servant. The master will be the employer and the servant the employee. The legal relationship of master and servant may be evidenced by a contract or it may be implied by conduct

**EMPLOYMENT VS SELF EMPLOYMENT**

In order to establish whether an individual performing a task is an employee or a hired self-employed person, some factors to be considered are as follows:

1. **Type of contract**

If there is a contract of service it will indicate the existence of relationship of master and servant i.e. (employer-employee relationship). A contract for service will indicate the existence of self-employment.

1. **Work performance**

Employees must perform the duties assigned to them themselves while the self-employed may hire other people to perform the work for them.

1. **Control**

The work of an employee is controlled by the employer who will normally stipulate working hours and other conditions. A self-employed person will decide when to perform the duties and how to perform them.

1. **Payment and financial risk**

Employees are paid an agreed salary on a monthly or weekly basis and incur form of financial risk.

In order to earn an extra sum employers will have to work overtime.

Self-employed persons are normally paid a proportion of the contract price based on the amount of work performed. They will also bear the full financial risk of their business-absorb all the losses and enjoy all the profit whichever maybe the case.

1. **Place of work**

Employees will normally be told where the duties are to be performed from. This is normally at the employer's premises or at the premises of the client.

Self-employed persons will perform the duties at a place of their choice.

1. **Equipment**

An employer will provide the tools and equipment which the employees are to use. Self-employed persons will provide their own tools and equipment.

1. **Correction of work**

Employees will normally rectify any faulty work during the normal working hours and there will still be paid for those hours. Self-employed persons will rectify any faulty work outside the contract time and they will not be paid for that extra work.

1. **Engagement and dismissal**

The employer will take on and dismiss employees. A self-employed person will normally enter into a contract with a client specifying the beginning and end.

1. **Exclusively**

Employees normally work for only one employer. A self-employed person will normally work for a number of clients.

1. **Integration**

An employee's work is fully integrated within an organization.

1. **Insurance**

Employers will normally provide insurance cover for the actions of their employees — Vicarious liability. Self-employed person usually answer for their actions.

**TAXABLE AND EXEMPT EMOLUMENTS**

The following are the tax treatments of the various payments which employees may be entitled to.

**SALARIES, WAGES**

These are taxable emoluments without any exemption, taxable in full on that employee.

The exception is where the salary is equal to or less than the tax free pay, which for the tax year 2020 is K39, 600. If this is the case and the salary is the only entitlement that the employee receives, then that salary will not be taxable. Similarly, if the net amount of emoluments after deducting the pension contributions is not more than the tax free pay, then employee will not pay tax.

**BONUSES**

Like salaries and wages, bonuses are taxable emoluments without any exemption. The actual amount received is taxable in full on the employee.

**ALLOWANCES PAID TO EMPLOYEES**

All allowances qualify as emoluments and as such, they are fully taxable. "If an employee, however, is reimbursed any expenditure incurred while performing the duties of employment, then only the excess of the reimbursed amount over the actual expenditure incurred by the employee shall be taxable. This normally occurs in cases where an employee is required to spend personal money when performing duties and then submit receipts to the employer for reimbursement.'

**BENEFITS IN KIND**

A benefit in kind is a benefit of some sort which is not money. Benefit in kind include the benefits derived from employment through the use of personal to holder vehicles and through the provision of free residential accommodation by the employer.

Benefits which cannot be converted into cash are not treated as emoluments of the employees. These benefits are taxable on the employer instead. They include the accommodation benefit and the personnel to holder car benefit.

Benefits which can be converted into cash are taxable on the employees receiving them.

**MAINTENANCE OF A RESIDENCE BY THE EMPLOYER**

Any amounts paid by the employer to assist an employee in meeting the cost of the upkeep of the residence are, as a general principle, taxable as emoluments of the employee.

If the employer undertakes to pay all the outgoings in respect of the house including rate, rent, taxes, insurance, security, electricity, telephones, entertainment and the general maintenance of the residence including the surrounding, then this constitutes **money's worth** and is taxable on the employee as emoluments.

**CLOTHING OR UNIFORM ALLOWANCE**

If an employee receives an allowance for the purchase of uniforms for official purposes or functions, the allowance received is taxable as an emolument of the employee. Employees may, however, claim for expense relief in respect of any amounts incurred on the purchase of uniforms for use in the performance of official duties.

**MEDICAL EXPENSES**

Expenses incurred by the employer on behalf of an employee, his or her family or household, for the cost of medical treatment are not chargeable emoluments. However, a medical allowance paid to an employee is a taxable emolument.

**CASH VOUCHERS**

A cash voucher is any document or stamp capable of being exchanged, either immediately or after a time for a sum of money equivalent to the stipulated value. Where a cash voucher is provided to an employee by reason of employment, the employee is treated as having received a taxable emolument.

**NON – CASH VOUCHERS**

A non-cash voucher is usually a document capable of being exchanged for goods or services. It may be exchanged immediately or after some time. Examples are: Christmas vouchers, shopping vouchers fuel vouchers etc. Where an employee receives a non-cash voucher, the employee is taxable on the value of the goods which that voucher can obtain.

**BOARD, LODGING AND MEALS**

Where an employee is provided with meals or board and lodging by the employer, there is no taxable emolument on the employee concerned.

If, however, an employee receives an allowance in lieu thereof, the allowance received would be a taxable emolument.

If an employee is required to work late at night such that it would be unreasonable to expect him to use public transport for his journey home, then the cost to the employer of providing such an employee with private transport home is not a taxable emolument of the employee.

**COMPULSORY PAYMENTS FOR BOARD**

Where arrangements exist to pay wages to employees gross, out of which a certain amount must go towards the payment for board, then the gross amount payable to the employee is a taxable emolument

**RESTRICTIVE UNDERTAKINGS**

A payment made by an employer in respect of an agreement entered into by an employee, the effect of which is to restrict the activities of the employee, or the ability of the employee to compete with the employer is a taxable emolument of that employee.

**TIPS AND SERVICE CHARGES**

If an employer operates a scheme under which he pays employees tips from customers or service charges, the amounts paid to employees are taxable emoluments on those employees.

**ALLOWABLE EXPENSES**

Allowable expenses are revenue expenses which are incurred wholly and exclusively for the purposes of the employment and include:

1. Subscription to professional bodies which are relevant to the employment.Subscriptions to professional bodies whose membership is not relevant to the employment are not deductible. Subscriptions which would be deductible are those paid to the Zambia Institute of Chartered Accountants by accountants who are members. Those paid to the Law Association of Zambia by lawyers who are members and subscriptions to all other bodies paid by members.
2. Mortgage Interest in respect of the property acquired for occupation by the employee and his or her family if interest is being payable at the rate at which a building society would charge it.
3. Capital allowances on implements, plant and machinery used wholly and exclusively in the performance of the duties of employment. This is in cases where employees are required to provide their own tools and equipment as in the case of tradespeople.
4. Travelling expenses incurred in the course of employment.These are expenses an employee incurs whilst performing the duties of employment. They include the following:
* Costs incurred in travelling between two places at which the duties are to be performed.
* Costs incurred in travelling between home and work if the duties commence at home, as in the case of medical doctors who are on call. For such Doctors, duties commence when they get a phone call that they are required at the hospital.

The following travelling expenses are not deductible:

* Costs incurred in travelling between two employments, as in the case of employees working on a full time contract with one company and on a part time contract with another. The costs incurred in travelling between the premises of the full time employment and the premises of the part time employment are not deductible.
* Costs incurred in travelling between home and work, unless duties commence at home as explained above.

The distinction between deductible travelling expenses and those which would not be deductible is illustrated in the following cases.

**CONTRIBUTIONS TO PENSION FUNDS**

Employee’s pension contributions to the national pension scheme authority (NAPSA) and any other pension fund are not deductible when computing taxable employment earnings.

Employee’s NAPSA contributions are calculated as 5% of the employee’s earnings subject to the social security contribution ceiling. Employer’s NAPSA contributions are also calculated as 5% of employee’s earnings, again subject to the social security contribution ceiling.

The employer is mandated under the law to remit both the employee’s NAPSA contributions deducted from employee’s earnings and the employer’s NAPSA contribution by the 10th day following the end of the month to which the employee’s earnings relate.

**NATIONAL HEALTH INSURANCE SCHEME CONTRIBUTIONS**

Employee’s contributions to the National Health Insurance Scheme which is managed by National Health Insurance Scheme Authority (NHIMA) or any other medical or health scheme are not deductible when computing taxable employment earnings.

The statutory employee’s National Health Insurance Scheme Contributions (NHISCs) are calculated at the rate 1% of the employee’s monthly basic salary. The statutory employer’s NHISCs are also calculated as 1% of the employee’s monthly basic salary.

The employer is mandated under the law to remit both the employee’s NHISCs deducted from employee’s salaries and the employer’s NHISCs to the NHIMA by the 10th day following the end of the month to which the salaries relate.

**EXAMPLE**

Chilu has been employed as a Sales Representative at a Zambian resident company for many years. In the tax year 2020, he was entitled to the following benefits:

Annual basic salary K180,000

Lunch allowance per month K1,200

Housing allowance per month K3,500

Throughout the tax year 2020, he was provided with a company owned Toyota Camry Motor car (with a cylinder of 1,800cc) on a personal to holder basis. The company paid all the motor car running expenses relating to the car which amounted to K4, 000 per month.

On 1 May 2020, he was given a labour day award compromising K3,000 cash and a television set worth K5,000, for being the most hard working Sales Representative in the country.

In December 2020, Chilu received bonus of 2% of his annual basic salary for meeting his sales targets for the year.

During the year to 31 December 2020, the company deducted employee’s NHICs from his earnings at the rate of 1% of his basic salary and paid employer’s NHICs at the rate of 1% of his basic salary on his behalf. The company additionally deducted employee’s NAPSA contributions at the rate of 5% of his earnings on his behalf.

Chilu made the following payments from his employment earnings in the tax year 2020:

Donations to political party K2,000

Professional subscriptions relevant to the duties of his employment K2,500

**Required:**

1. Calculate Chilu’s employee’s NHICs and employer’s NHICs paid in the tax year 2020.
2. Calculate Chilu’s employee’s NAPSA contributions and employer’s contribution paid in the tax year 2020.
3. Compute the income tax payable by Chilu for the tax year 2020. ( clearly indicate in your computation by the use of zero 0 any items of income or expense which are not taxable or not allowable)

**SOLUTION**

1. Employee’s NHISCs = 1% $×$ K180,000 = K1,800

Employer’s NHISCs = 1% $×$ K180, 000 = K1, 800

1. Employee’s NAPSA contributions = 5% $×$ K240,000(W) = K12,000

Employer’s NHISCs = 5% $×$ K240, 000(W) = K12, 000

COMPUTATION OF GROSS EARNINGS

Gross earnings for NAPSA contribution purposes comprises the basic salary plus all allowances, bonuses, commission, overtime pay, leave pay, commuted leave days, severance pay etc

Chilu’s gross earnings for the tax year 2020 will be computed as:

 K

Annual basic salary 180,000

Lunch allowance (K1,200$×$ K12) 14,400

Housing allowance (K3,500$×$ K12) 42,000

Bonus (K180,000$×$ 2%) 3,600

Gross earnings 240,000

1. **CHILU**

PERSONAL INCOME TAX COMPUTATION FOR THE YEAR 2020

 K K

Salary 180,000

Lunch allowance (K1,200$×$ K12) 14,400

Housing allowance (K3, 500$×$ K12) 42,000

Bonus (K180,000$×$ 2%) 3,600

Personal to holder motor car benefit 0

Payment of motor car running expenses

Personal to holder motor car 0

Labourday award (cash & TV set) 0

Employer’s NHISCs 0

Employer’s NAPSA 0

Gross earnings 240,000

Less allowable deductions:

Professional subscriptions 2000

Donation to political party 0

Employee’s NHISCs 0

Employer’s NAPSA contributions 0

 (2,000)

Taxable earnings 238,000

Income Tax

K39,600$×$ 0% 0

K9,600$×$ 25% 2,400

K25,200$×$ 30% 7,560

K163,600$×$ 37.5% 61,350

Income tax payable 71,310

**PAYMENTS MADE ON TERMINANTION OF EMPLOYMENT**

Employment ceases when the employee or employer terminates it. Employment may cease by way of dismissal, resignation, end of contract term, redundancy/retrenchment, retirement or death. Certain payments may be made to the ex-employee as a result of the termination of employment. Some of these payments are taxable while others may be exempt.

**THE PAY AS YOU EARN (PAYE) SYSTEM**

PAYE is the system that is used for collecting income tax on the emoluments from holding an office or from employment.

Under the PAYE system, the procedures relating to tax compliance are transferred from the employees to the employer. The employees receive their emoluments net of income tax.This reduces the number of problems that would be encountered if employees where required to pay income tax on the emoluments several months after those emoluments had been earned and consumed.

**DOCUMENTATION REQUIRED TO OPERATE PAYE**

A person who sets up in business is required to contact ZRA if he is going to engage some people. The inspector will then provide a package containing the following:

* The employer's guide to PAYE
* Tax tables

The main documents and forms required to operate PAYE which include:

* The tax deduction cards, known as form ITF/P8
* Employee leaving forms known as form ITF/P 13 (part I)
* Details of old employment known as form ITF/P 13 (part 11)
* Particulars of employee commencing employment, known as form ITF/P20
* Certificate of pay and tax deducted known as form ITF/P22
* Remittance card known as form CF/P 16
* Employer's annual declaration and certificate known as form CF/P 18

**CALCULATION OF TAX PAYABLE UNDER PAYE**

The following steps are followed in order to calculate income tax payable under the PAYE system each time that emoluments are paid:

1. The total amount payable to the employee for the month should be calculated. This is an employee's gross pay for the month.
2. Contributions to approved pension funds and other allowable expenses are then deducted from the gross pay for the month.
3. The total chargeable emoluments paid to the employee since the commencement of the tax year are added to the taxable emoluments for the month in order to arrive at the chargeable emoluments for the year to date.
4. The proportion of the employee's free pay to date should be determined from the tax tables.This is the proportion of the total free pay applicable since the beginning of the tax year on 1st January.
5. The amount of tax on the chargeable income to date is then worked out using the tax tables.
6. The amount of tax already paid should then be deducted from the result determined instep 5 above to arrive at the amount of tax payable for the current month. The amount of tax payable for the current month is the tax that should be deducted from the employee's pay for the current month.

**PAYMENT OF TAX DEDUCTED UNDER PAYE**

Tax deducted under the PAYE system is payable by the tenth day of the end of the month in which the emoluments were paid.

If the tax is not paid by that date, penalties and interest on overdue tax are charged. These are borne by the employer and not by the individual employees.

**PAYE PENALTIES**

Penalties are charged under PAYE when all the procedures concerning payments of tax and submission of the returns are not complied with.

If 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%.

If there is a loss of tax due to fraud, will ful default or negligence of an employer, the employer may be liable to penalties mounting to 52.5%, 35% or 17.5% respectively of the omitted income**.**

**UNIT 5 - TAXATION OF BUSINESS PROFITS-THE CASE OF A SOLE PROPRIETOR**

**5.1 Introduction**

This unit will introduce you to the taxation of business profits as regards a sole proprietor. Business organizations may be operated as a company or partnership or sole trading/proprietorship. In this course we shall study how each of these business forms are taxed. We start here with a case of sole proprietor i.e. taxation of business profits of a sole trader.

**5.2 Learning Outcome**

After completing this unit you should be able to:-

* Explain the badges of trade
* Explain the general rule used to determine whether expenses are deductible for tax purposes or not.
* Compute the taxable business profits for sole traders.
* Computation of Taxable Business Profit



**5.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

BUSINESS STATUTORY DEFINITION

BUSINESS STATUTORY has been defined in S.2 of the Act as any profession, vocation or trade and includes: Any adventure or concern in the nature of trade whether singular or otherwise, manufacturing, and farming

A PROFESSION was defined in the case of IRC v Maxse as an occupation requiring either the use of purely intellectual skill or manual skill directed by the intellectual skill of the operator.

A VOCATION was defined in the case of Partridge v Mallandaine as the way in which a person passes his or her life.

The statutory definition cannot be relied upon to establish whether a trade exists or not. In order to establish whether a trade exists, the badges of trade are used. These were developed in the UK by the royal commission on taxation.

THE BADGES OF TRADE

The main badges of trade are as follows:

The subject matter of realisation

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 being conducted will be greater.

The length of the period of ownership

Guidance has been provided that trading stock is not normally held for a long period of time. As a result if a person disposes off an asset that he/she held for a long period of time it will be quite difficult to determine whether the asset had been held as trading stock. Assets held for long periods of time are normally investments.

The frequency of similar transactions

If the frequency of similar transactions is high, chances of classifying a taxpayer as a trader are high. In Pickford v Quirke, the taxpayer was one of the syndicates who purchased the shares of companies, liquidated them and sold the assets at a profit. The taxpayer had entered into four transactions each resulting in a profit. It was held that he was trading.

Supplementary work and marketing

If an asset is acquired when it is in a poor state and supplementary work is carried out to improve the asset by making it more marketable, then such an asset when sold will give rise to trading profit. The argument is that supplementary work is performed so that the assets could be sold at a higher price than its value just acquired.

Circumstances giving rise to realisation

It is not always that whenever an asset has been sold, that asset will give rise to taxable profits.

Circumstances that gave rise to the sale are also taken into account. If a taxpayer disposes off an asset in order to raise money to help solve some financial problems it will be difficult to establish whether the asset was trading stock.

The Tax payer's intention

Intention to trade clearly constitutes trading. However, intention to make a profit may not constitute trading. As such it has to been established as to whether a taxpayer sold an asset because the intention was to trade. In addition to the six badges of trade there are additional factors which have to be taken into, account. These are as follows:

The Tax payer's other circumstances/activities

If the other activities of a taxpayer indicate the existence of a trade then even the current transaction is likely to be interpreted as an indication of the existence of the trade

The way the asset sold was acquired

If the asset sold was acquired by inheritance or by way of gift, the transaction may not be considered to be a trading transaction.

The method of finance:

If the asset sold was bought using some borrowed money the presumption that the asset was trading stock is high. The presumption is even greater if some interest was paid on the amount of money borrowed at a high interest rate. All the above factors are applied in trying to determine whether there is a trade in existence.

**COMPUTATION OF TAXABLE BUSINESS PROFITS**

 **K’000 K’000**

Net profit as per accounts X

Add:

Expenses charged in the A/Cs but not deductible for tax purposes X

Taxable income not credited to A/Cs X

 X

Less:

Income credited to accounts but not taxable X

Expenses for tax purposes not deducted in the A/Cs X

 (X)

Taxable business profits X

**RULES FOR DETERMINING DEDUCTABLE EXPENSES WHEN COMPUTING TAXABLE PROFITS.**

**THE GENERAL RULE FOR DEDUCTION OF EXPENSES**

1. It must be Revenue not Capital Expenditure.
2. It must be incurred in the year wholly and exclusively for the purpose of the business.

**CAPITAL EXPENDITURE**

This is specifically disallowed. There are three main points to remember when computing taxable profits.

1. All expenditure incurred on the improvement of fixed assets cannot be deducted in the computation of taxable profits.
2. Depreciation of fixed assets and losses on disposal of fixed assets are non-deductible expenses.
3. Profits on disposals of fixed assets are also not taxable income.

When expenditure is made once and for all but with a view to bringing into existence an asset or advantage for the enduring benefit of a business, that expenditure will reasonably be treated as capital Loses suffered expenditure.

**ALLOWABLE EXPENSES**

This list is extracted from M. Kamanga (1994), income Tax in Zambia.

l . The cost of materials, components and goods purchased for resale.

1. Gross wages and salaries.
2. Redundancy payments
3. Compensation for loss of office
4. Business rates, rent and telephone
5. Business fuel, water and electricity
6. Maintenance and repair expenses
7. Printing and stationery expenses
8. Bank and loan interest used for business purposes
9. Hire purchase interest and payments

11. Advertising which is Revenue in natlile and not permanent advertising considered as capital

1. Training expenditure usually' related to staff training.
2. Bad debts and debt collection costs
3. Research expenditure that considered as Revenue..
4. Insurance
5. Legal expenses arising from trading
6. Other allowable deduction specifically mention bv ITA are;
	* Donation to charity
	* Handicap person allowance Employment of a handicapped person would entitle the business to claim a handicapped person's allowance which is Kl 000 000 per annum per handicapped person employed as long as such person are registered with the association of the handicapped.
7. Gifts such as calendars carrying advertisements, provided it does not exceed Kl 00 000 per gift per individual.
8. Normal business losses
9. Employer's contributions to an approved fund (National

Pension Scheme Authority and such others

21. Staff welfare expenses

1. Licence renewal costs but not application fee for the first time.
2. Specific provisions
3. Losses of stock in trade
4. Capital allowances
5. Travelling and accommodation expenses for business purposes, but not those concerned with the acquisition of an asset which should be capitalized.
6. Losses and defalcation of employees

**DISALLOWABLE EXPENSES**

1.Depreciation of Fixed Assets

* + 1. General provision such as bad debts and preventive maintenance.
		2. Legal expenses in connection with acquisition of capital items.
		3. Entertainment and hospitality expenses other than for purely staff function
		4. Capital improvement costs
		5. Fines for illegal acts
		6. Donations unless specifically approved
		7. Any tax or penalty charged — Statutory penalties
		8. Costs associated with the purchase of assets e.g. carriage and installation charges
		9. Cost of registration of trademarks, copyrights patents etc.

11. Defalcation and misappropriation by senior officers of the business.

* + 1. Drawings by sole trader or partner
		2. The costs of acquisition of a main agency including travelling expenses incurred in that connection.
		3. Goodwill of a business
		4. Costs incurred for increase of share capital
		5. Licence application costs except for renewable costs
		6. Loans to employees of the business
		7. Bad debts incurred before incorporation
		8. Private and domestic expenses of the business officers
		9. Legal expense incurred in defending the tax payer from a charge of breaking the law.
		10. The cost of tax case appeal to the Revenue Appeals Tribunal
		11. The cost of refresher course for sole trader/partnership
		12. Bad debts of a subsidiary
		13. Entrance fees paid to Association such as Manufacturers Association of Zambia.
		14. Any loss or expense which is recoverable under any insurance contract or indemnity

**INCOME NOT TAXABLE AS BUSINESS PROFITS**

Examples of income taxable at source through the withholding tax system are:

* Rental income
* Interest income such as debenture interest, bank interest and building society interest
* Royalties
* Dividends

If such amounts are credited to the profit and loss account, they have to be deducted and if they are taxable, the gross amount is to be included in the final personal tax computation, as will be seen later under personal income tax computations.

**EXAMPLE**

Mulongoti has been in business on his own account as a retail grocery for many years. His business Premises consist of a shop with living accommodation above, which houses Mulongoti and his family. For the year ended 31 December 2020, his income statement showed the following:

 K K

Staff wages 74,160 Gross profit 303,260

Wife’s wages 6,240 Profit on sale of plant 2,400

Rent and rates 6,300

Light and heat 21,720 profit on sale of investments 10,320

Motor car expenses 3,360

Telephone 780 bank interest received 540

Postage, Stationery and wrapping 10,800

Repairs and renewals 4,760

Bad debts written off 1,000

Miscellaneous expenses 3,460

Advertising 10,240

Loan interest 11,300

Depreciation – plant 4,800

 Motor car 1,200

Net profit 156,400

 316,520 316,520

The following information is also relevant:

1. The Zambia Revenue Authority has agreed that one – third of the expenditure on rent, rates, heat and light is applicable to the living accommodation.
2. One – seventh of the motor car expenses relates to private motoring.
3. Repairs and renewals comprise:

 K

Painting shop internally 1,550

Plant repairs 1,010

Constructing extension to stock room 2,200

 4,760

1. Bad debts amount

 K K

Bad debts written off 1,020 Balances b/f

 General reserve 2,000

Balances c/f Specific reserve 3,600

General reserve 4,000 Bad debts recovered 2,400

Specific reserve 3,980 Profit and Loss 1,000

 9,000 9,000

1. Miscellaneous expenses included:

 K

Donation to local charity 100

Subscriptions to the Zambia Chamber of Commerce and Industry 180

Entertaining customers 900

Christmas gifts to customers – bottles of gin and whisky (each costing K50) 700

Payment to employee in lieu of notice 200

Legal expenses – debt collecting 150

Sundry allowable expenses 1,230

 3,460

The charity to which the donation was made is an approved one.

1. The profit on the sale of investment relates to the sale of a holding or ordinary shares in a company quoted on the Lusaka Securities Exchange. These shares were acquired by Mulongoti on 1 January 2020 for K84,600 and sold on 30 June 2020 for K94,920.
2. Mulongoti estimates that during the year, he has withdrawn goods from stock costing K3,400 for the use of himself and his family.
3. Mulongoti estimates that his gross profit percentage on turnover is 15%.
4. Mulongoti is entitled to a nominal salary of K4,000 per annum. This amount is included in the figure for staff wages. Mrs Mulongoti worked full time in the business.

**Required:**

Compute Mulongoti’s income tax payable on the tax adjusted business profits for the year ended 31 December 2020 giving reasons for any adjustment made by you.

**SOLUTION**

MULONGOTI

COMPUTATION OF TAX ADJUSTED BUSINESS PROFITS FOR THE YEAR ENDED 31 DECEMBER 2020

 Note K K

Net profit as per accounts 156,400

Add:

Rent and rates (1/3 $×$ K6,300) 1 2,100

Heat and lighting (1/3 $×$ K21,720) 1 7,240

Motor car expenses (1/7 $×$ K3,360) 1 480

Building extension to stock room 2 2,200

Increase in general bad debt provision 3 2,000

Entertaining customers 4 900

Christmas gifts – bottles of gin and whiskey 4 700

Goods for personal use (100/85 $×$ K3,400) 5 4,000

Mulongoti’s nominal salary 6 4,000

Depreciation of motor car 7 1,200

Depreciation of plant 7 4,800

 29,620

 186,020

Less:

Profit on sale of plant 8 2,400

Profit on sale of investments 8 10,320

Bank interest received 9 540

 (13,260)

Taxable business profits 172,760

Less tax – free income 39,600

 133,160

Income tax

25% $×$ K9, 600 2,400

30% $×$ K25, 200 7,560

37.5% $×$ K98, 360 38,885

Income tax payable 46,845

**UNIT 6 - CAPITAL ALLOWANCES**

**6.1 INTRODUCTION**

This unit introduces you to capital allowances. Business houses that incur capital expenditure on certain capital assets are entitled to claim capital allowances. Capital allowances reduce the taxable profit of an entity.

**6.2 Learning Outcome**

After completing this unit you will be able to:

* Compute capital allowances to be claimed given the capital expenditure.
* Describe the various capital allowances that are claimable when certain capital expenditure is incurred.



**6.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**6.4 NATURE OF CAPITAL ALLOWANCES**

Capital allowances are a form of tax relief given for capital expenditure. They replace accounting depreciation because they are given in a standard manner according to the tax legislation.

Capital expenditure is not an allowable deduction in the computation of taxable business profits. Amounts written off the capital expenditure are the capital allowances.

Capital allowances are not given on all the types of capital expenditure. The income tax act contains the types of capital expenditure on which capital allowances may be claimed.

The qualifying expenditure includes expenditure on:

• Implements, plant and machinery,

• Industrial buildings,

• Commercial buildings,

• Farm works and improvements etc

The income tax act provides that when ascertaining the profits or gains of a business, a deduction in the form of capital allowances shall be allowed based on the cost of any implements, plant and machinery used in that business.

There is no definition of plant in the act. Case law provides some guidance as to what is plant and what is not plant.

**THE ALLOWANCES AVAILABLE**

Capital allowances on implements, plant and machinery are available in the form of wear and tear allowances. The wear and tear allowances are based on the cost of any qualifying expenditure.

The rates at which the wear and tear allowances are available are:

• Implements, plant and machinery as well as commercial vehicles qualify for wear and tear allowances at the rate of 25% on cost.

• Non-commercial vehicles qualify for wear and tear allowances at the rate of 20% on cost.

• Implements, plant and machinery used in farming, manufacturing, tourism and leasing qualify for increased wear and tear allowances at the rate of 50%.

**QUALIFYING PERIODS**

* Capital allowances on implements, plant and machinery are available for charge years.
* Each item of qualifying expenditure qualifies for capital allowances individually. There is no time when the expenditure should be pooled.

**EXAMPLE**

Phiri is in business preparing accounts annually to 31 December. He has acquired the following assets since the commencement of his business:

*Date Asset Cost*

K

1 February 2019 Toyota car 17,500

1 March 2019 Equipment 12,000

31 October 2019 TATA truck 45,000

1 January 2020 Furniture 11,000

All of the above assets were used wholly and exclusively in the business. Phiri’s business does not include any aspect of manufacturing.

**Required:**

Calculate the capital allowances claimable by Phiri for the charge years 2019 and 2020, showing the income tax values at the start and end of each year.

**SOLUTION**

**PHIRI**

**COMPUTATION OF CAPITAL ALLOWABLES ON IMPLEMENTS, PLANT AND MACHINERY**

*Charge year 2019 Values Capital allowable*

 *K K*

**Toyota car**

Purchase cost 17,500

Wear and tear allowable

(20% $×$ K17,500) (3,500) 3,500

Income tax value c/f 14,000

**Equipment**

Purchase cost 12,000

Wear and tear allowable

(25% $×$ K12,000) (3,000) 3,000

Income tax value c/f 9,000

**TATA truck**

Purchase cost 45,000

Wear and tear allowable

(25% $×$ K45,000) (11,250) 11,250

Income tax value c/f 33,750 -

*Total capital allowances for the charge year* 17,750

*Charge year 2020Values Capital allowable*

 *K K*

**Toyota car**

Purchase cost 14,000

Wear and tear allowable

(20% $×$ K17,500) (3,500) 3,500

Income tax value c/f 10,500

**Equipment**

Purchase cost 9,000

Wear and tear allowable

(25% $×$ K12,000) (3,000) 3,000

Income tax value c/f 6,000

**TATA truck**

Purchase cost 33,750

Wear and tear allowable

(25% $×$ K45,000) (11,250) 11,250

Income tax value c/f 22,500

**Furniture**

Purchase cost 11,000

Wear and tear allowable

(25% $×$ K11,000) (2,750) 2,750

Income tax value c/f 8,250

Total capital allowances for the charge year **20,500**

**DISPOSALS OF IMPLEMENTS, PLANT AND MACHINERY**

* When there is a disposal of implements, plant and machinery, the disposal proceeds should be deducted Mitsubishi from the income tax value at the start of the charge year in which the disposal is made. The result maybe a balancing allowance or a balancing charge. W*ear and Tear allowances are not available in the year* when an asset is disposed of.
* If an asset is disposed of in the year of acquisition, there is no wear and tear allowance. The disposed values proceeds are matched with acquisition cost of that asset.

**BALANCING ALLOWANCE**

* This arises when the disposal proceeds are less than the income tax value being matched with those proceeds.
* Balancing allowance are capital allowances in the same way that wear and tear allowances are. They should be added to the wear and tear allowances and the total treated as the capital allowances for the year. If the asset sold has an element of private use by the trader, then the balancing allowance is restricted to the proportion of business use of the asset.

**BALANCING CHARGE**

* This arises when the disposal proceeds are more than the income tax value being matched with the proceeds.
* The balancing charges are also referred to as capital recoveries. The capital recoveries are restricted 0 the actual capital allowances given on the asset sold in the form of wear and tear allowances.
* Balancing charges or capital recoveries reduce the capital allowances. It the net result is a balancing charge, then that amount should' be added to the profits to arrive at the amount of taxable business profits. If the asset sold has an element of private use by the trader, then the balancing allowance is restricted to the proportion of business use of the asset.

**EXAMPLE**

Miyoba runs a small business buying and selling goods to households. He acquired a Nissan motor car at a cost of K18,000 in the tax year 2019. At 1 January 2020, the income tax value of the motor car was K14,400. It has been agreed with the commissioner General tatMiyoba’s private use of the motor car is 25%. Miyoba also owns a pick – up – truck whose income tax value at 1 January 2020 was K15,000. Miyoba acquired the pick – up – truck at a cost K30,000.

During the tax year 2020, Miyoba acquired a computer for K6,000 and sold the Nissan motor car for K20,000. He also sold the pick – up – truck for K13,000. Miyoba replaced the two motor vehicles in the same tax year 2020.

As a result of disposing of the pick – up – truck, Miyoba bought a Toyota truck for K35,000. He replaced the Nissan car with a Mitsubishi motor car costing K21,000. Miyoba’s private use of the Mitsubishi motor car continued to be 25%.

**Required:**

Calculate Miyoba’s capital allowances for the tax year 2020, showing clearly the income tax values at the start and end of each charge year.

**SOLUTION**

MIYOBA

CAPITAL ALLOWANCES COMPUTATION FOR THE TAX YEAR 2020

*Values Capital allowable*

*K K*

**Nissan car**

Income tax value b/f 14,400

Disposal proceeds (limited to cost) (18,000)

Balancing charge (3,600) $×$ 75% (2,700)

**Pick – up – truck**

Income tax value b/f 15,000

Disposal proceeds (limited to cost) (13,000)

Balancing charge (2,000) 2,000

**Computer**

Purchase cost 6,000

Wear and tear allowance

25% $×$ K6,000 (1,500) 1,500

Income tax value c/f (4,500)

**Toyota truck**

Purchase cost 35,000

Wear and tear allowance

25% $×$ K35,000 (8,750) 8750

Income tax value c/f 26,250

**Mitsubishi motor car**

Purchase cost 21,000

Wear and tear allowance

20% $×$ K21,000 (4,200)$×$ 75% 3,150

Income tax value c/f 16,000

Total capital allowances for the tax year 12,700

**CAPITAL ALLOWANCES ON BUILDINGS**

Capital allowances are available on various types of expenditure on buildings. The types of building which qualify for capital allowances include industrial buildings (including low cost housing) and Retail commercial buildings.

**Industrial buildings**

Capital allowances on Industrial buildings may also be referred to as the Industrial Building Allowance (IBA).

**QUALIFYING BUILDINGS**

**BUILDINGS USED FOR INDUSTRIAL PURPOSES**

Unlike plant and machinery that is not defined, the Income tax act defines an industrial building in part of the fifth schedule as to mean 'a building or structure that is used for the purposes of any electricity gas, water, inland navigation, transport, hydraulic power, bridge or tunnel undertaking, or an undertaking of public utility, or is in the use for the purposes of any trade which:

* Is carried on in a mill, factory or similar premises
* Consists of the shortage of goods import or for export

**HOTELS**

Expenditure incurred on the construction or extension of a hotel on or after 1 April 1966 may qualify. The hotel should be certified by the government body that is responsible for the hotel industry as meeting the relevant government standards.

**LOW COST HOUSING**

Low cost housing will qualify as an industrial building if the cost of each housing unit does not exceed K20, 000. The cost of any housing unit that exceeds K20, 000 will not qualify for an IBA.

**NON QUALIFYING BUILDINGS**

The following do not qualify as industrial buildings:

* Dwelling houses
* Retail shops
* Showrooms
* Offices
* Buildings which are used for the purposes of:
* A retail trade
* A repair or servicing trade

**QUALIFYING EXPENDITURE AND ALLOWANCES**

Capital allowances are only available on the actual expenditure incurred in the construction of a building less amounts of any subsidy or grant received from public funds towards the expenditure incurred.

The cost of land does not qualify. However, incidental expenditure may qualify. Incidental expenditure that may qualify includes:

• Expenditure incurred on digging foundations;

• Expenditure incurred on preparing the land

• Architect fees

**EXAMPLE**

Champemba, who has been running a small business, constructed a building at a cost of K2,250,000 made up as shown below:

 K

Land 150,000

General administrative office 200,000

Engineering drawing office 600,000

Staff canteen 400,000

Factory unit 900,000

Total cost 2,250,000

**Required:**

Calculate the cost qualifying for Industrial Buildings Allowances.

**SOLUTION**

1. The construction cost of the building is:

 K

Total cost 2,250,000

Less cost of land (150,000)

Total construction cost 2,100,000

1. 10% $×$ K2,100,000 = K210,000
2. The cost of the general administrative office does not exceed 10% of the total construction cost of the building. As such, the general administrative office will qualify as an industrial building. The qualifying cost will therefore be K2,100,000 consisting of all the buildings, which excludes the cost of land.

**THE ALLOWANCES AVAILABLE**

There are three types of allowances available on the expenditure qualifying to be on industrial building as follows:

**THE INITIAL ALLOWANCE**

This is available only in the first year when the industrial building is first put to use. The rate of initial **allowance** is 10% of the qualifying expenditure.

The initial allowance is deductible from the qualifying cost in arriving at the income tax value at the end of the first year.

**THE INVESTMENT ALLOWANCE**

This is available also only in the first year at the rate of 10% of the qualifying expenditure. The allowance is given against the profits of the first year. It is not deductible from the qualifying cost in arriving at the income tax value at the end of the first year. Only newly constructed buildings qualify for this allowance.

**THE WEAR AND TEAR ALLOWANCE**

This is available at the rate of 5% on the qualifying expenditure. The allowance is available starting from the first year to the year immediately before that in which the building is disposed off.

Where a building is used for qualifying purposes for part of the year and for non-qualifying purposes of the other part, then that building should be treated as if it were in use for only qualifying purpose throughout the year. The wear and tear atk5Wance would then be given in the normal way.

Buildings are not pooled in any way. Each building is dealt with on an individual basis.

**EXAMPLE**

Alex Chisha constructed a new building at a cost of K500,000 including land costingK90, 000 at the start of the tax year 2020. The building qualities as an Industrial building for income tax purposes.

During the charge year 2020, Mr Chisaha’s tax adjusted business profit before capital allowances was K106,000.

**Required:**

Calculate the capital allowances claimable by Mr Chisha for 2020 and the final amount of taxable business profit for the same year.

**SOLUTION**

The qualifying cost of the building is:

 K

Total cost including land 500,000

Less cost of land (90,000)

Qualifying cost 410,000

**COMPUTATION OF INDUSTRIAL BUILDINGS ALLOWABLE FOR 2020**

 **Industrial Buildings**

 **Value Allowance**

 K K

Qualifying cost 410,000

Wear and tear allowance

(5% $×$ K410,000) (20,500) 20,500

Initial allowance

(10% $×$ K410,000) (41,000) 41,000

Investment allowance

(10% $×$ K410,000) 41,000

Income tax value c/f 348,500

Total capital allowance 102,500

**LOW COST HOUSING ALLOWANCES**

Low cost housing qualifies for IBAs in the form wear and tear allowances. The rate of wear and tear allowance is 10% on cost. The initial allowances and investment allowances are available at the rate of 10% on cost in the first year only on newly constructed low cost housing.

A housing unit may be a separate building complete in itself or part of a larger building. Where the housing units are flats. Then each flat would be a housing unit for capital allowances purposes.

**DISPOSAL OF INDUSTRIAL BUILDINGS**

When an industrial building is disposed of, the disposal value should be matched with the income tax value at the start of the tax year in which the disposal takes place. The wear and tear allowance is not available in the year of disposal like in the case of implements, plant and machinery, the result will, be a balancing allowance or a balancing charge. The balancing allowance arises when the disposal proceeds are less than the income tax value at the start of the tax year in which the disposal takes place, On the other hand, a balancing charge arises when the disposal proceeds are more than the income tax value at the start of the tax year in which the disposal takes place.

The buyer of a used building gets only wear and tear allowances at 5% on the cost of the building to him or her. Initial ---allowances and investment allowances are not available on used buildings. These two allowances are only available on newly constructed buildings.

**DISPOSAL OF LOW COST HOUSING**

When there is a disposal of low cost housing, a balancing allowance or charge is computed in the same way as in the case of any other industrial building. The buyer of used low cost housing gets wear a tear allowances on the purchase price paid. Initial allowances and investment allowances are available on used low cost housing.

**COMMERCIAL BUILDINGS**

A commercial building has been defined as to mean a building or structure or part thereof, which is an industrial building, or farm improvement or farm works, and which is in use for the purposes of business, provided that the construction of such a building or structure is completed for first use on after I April 1969.

Most buildings which do not qualify as industrial buildings are commercial buildings for the purpose of capital allowances. Examples of commercial buildings are warehouses used in a retail or wholesale trade, showrooms, sales offices. administration offices, and retail shops.

Commercial building qualify for wear and tear allowances at the rate of 2% of cost. The cost that qualifies is any expenditure that is incurred on the construction or extension of an existing building structure.

**DISPOSAL OF COMMERCIAL BUILDINGS**

A balancing allowance or balancing charge arises when there is a disposal of a commercial building. They are calculated in the same way as for any other building or plant.

**UNIT 7 – PARTNERSHIPS**

**7.1 Introduction**

This unit introduces you to Business Partnership.

**7.2 Learning Outcome**

After completing this unit you will be able to:

* Compute taxable profits for Partnership and allocation to individual partners.



**7.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**7.4** **Definition**

**A PARTNERSHIP** is created when two or more people join together in business with a view to profit. The people who join together are known as partners. However, the **partnership does not pay income tax** on these profits. Instead, the individual partners pay income tax on their share of the taxable business profits.

**COMPUTING PARTNERSHIP TAXABLE PROFITS**

Taxable business profits of partnerships are computed in the **same way as for sole traders**. The net profit figure appearing in the accounts is adjusted using the same rules for adjustments of profits as are applicable to sole traders. Revenue expenses, which are incurred wholly and exclusively for the purposes of the trade, profession or vocation, are allowed as business expenses.If a partner incurs an expense that is partly for the purposes of the business and partly for private purpose, only the business proportion would be allowed for tax purposes.

**Partners’ appropriations of profits are not deductible** in the computation of the taxable business profits which are available for appropriations. The partners’ appropriations are, in fact, part of the taxable income of the individual partners. Partners’ appropriations generally include partnership salaries and interest on capital account balances.

After the profits have been adjusted, **capital allowances** on all assets which are owned by the partnership should be deducted, after any adjustment is made for any private use. In some cases, the individual partners will use their **private assets** in the partnership business. Capital allowances on these assets should be deducted from the individual partners’ shares of the partnerships profits. In order to arrive at the final taxable business profit of a partnership, capital allowances on all partnership assets that qualify are deducted from the tax adjusted business profit. The rules for computing these capital allowances are the same as for sole traders.

**APPROPRIATION OF PROFITS AND LOSSES**

The profits of the partnership should be divided among the partners on the basis of the partnership agreement that is in existence in the accounting period.

**EXAMPLE**

Alpha, Beta and Gamma are in partnership sharing profits and losses in the ratio of 1:2:3 after allowing for annual partnership salaries of K15,000 for Alpha, K12,500 for Beta and K11,000 for Gamma.

The partnership made taxable profits for the two accounting periods as follows:

Year ended 31 December 2019 Profit K75,000

Year ended 31 December 2020 Profit K70,250

**Required:**

Show how the partnership profit will be shared between the partners.

**SOLUTION**

ALPHA, BETA AND GAMMA

DIVISION OF PARTNERSHIP PROFITS

 *Total Alpha Beta Gamma*

 K K K K

Y/e 31 Decemebr 2019

Partnership salaries 38,500 15,000 12,500 11,000

Share of balance (1:2:3) 36,500 6,083 12,167 18,250

Total 75,000 21,083 24,667 29,250

Y/e 31 Decemebr 2020

Partnership salaries 38,500 15,000 12,500 11,000

Share of balance (1:2:3) 31,750 5,292 10,583 15,875

Total 70,250 20,292 23,083 26,875

**CHANGES IN THE PARTNERSHIP AGREEMENT**

If there is a change in partnership agreement during the accounting period, then the following steps should be taken in order to arrive at the profits to be assessed on each other.

Step 1 – the accounting period should be **divided into two periods** on the date when the partnership agreement was changed so as to have a period before the change and a period after the change.

Step 2 – the total profits should then be allocated to each of these two periods on a time basis. For example, if the period before the change is made up of four months and the period after the change is made up of eight months, then four – twelfths of the profit for the year should be allocated to the period before the change so that eight – twelfths is allocated to the period after the change.

Step 3 – the profits allocated to each period are finally divided between the partners on the basis of the partnership agreement that is in existence in each period.

**EXAMPLE**

Alick and Nancy are in partnership as property consultants preparing accounts to 31 December each year. On 1 October 2020 Emmanuel joined Alick and Nancy as a new partner and the partnership agreement was changed.

The partnership agreement has been as follows:

 *Alick Nancy Emmanuel*

Period up to 30 September 2020

Annual salaries (K) 120,000 65,000 -

Share of balance 3 2

Period from 1 October 2020

Annual salaries (K) 80,000 90,000 100,000

Share of balance 5 3 2

The partnership’s taxable profit for the year ended 31 December 2020 was K300,000.

**Required:**

Show how the partnership’s profit for the year ended 31 December 2020 will be shared by the three partners and calculate the income tax payable by each partner.

**SOLUTION**

ALICK, NANCY AND EMMANUEL

DIVISION OF PARTNERSHIP PROFIT FOR THE YEAR ENDED 31 DECEMBER 2020

 *Total Alick Nancy Emmanuel*

 K K K K

1.1.2020 to 30.9.2020

Salaries 138,750 90,000 48,750 Nil

Balance (3:2) 86,250 51,750 34,500 Nil

 225,000 141,750 83,250 Nil

1.10.2020 to 31.12.2020

Salaries 67,500 20,000 22,500 25,000

Balance (5;3:2) 7,500 3,750 2,250 1,500

 75,000 23,750 24,750 26,500

Total profit 300,000 165,500 108,000 26,500

Less tax – free income (39,600) (39,600) (26,500)

 125,900 68,400 Nil

Income tax

K9,600$×$ 25% 2,400 2,400

K25,000$×$ 30% 7,560 7,560

K91,100/K33,600 $×$ K37.5% 34,163 12,600

Income tax payable 44,123 22,560 Nil

**INCOME TAX ASSESSMENT**

The rules for making income tax assessments on commencement of businesses are applied on new partners who join the partnership. Similarly, the rules for making assessments on cessation are applied on retiring partners.

**LOSS RELIEF**

A trading loss should be **carried forward** by each partner and be relieved against **future partnership profits** arising from the **same trade**.

**EXAMPLE**

Gorge and Valley are in partnership sharing profits and losses in the ratio of 1:3 respectively. On 1 April 2020, River was admitted to the partnership and the profits and losses were to be shared between Gorge, Valley and River in the ratio of 2:5:3 respectively. Partnership salaries were K50,000 per annum for each partner up to 31 March 2020. From 1 April 2020, the partners’ salaries were K20,000 per annum for each of Gorge and Valley and K13,333 per annum for River.

The profits and losses for the recent years have been as follows:

Year ended 31 December 2019 Profit K150,000

Year ended 31 December 2020 Loss (K250,000)

**Required:**

Show how the profits and losses will be shared between the partners for each of the two accounting periods.

**SOLUTION**

GORGE, VALLEY AND RIVER

DIVISION OF PARTNERSHIP PROFITS

 *Total Gorge Valley River*

 K K K K

Year ended 31.12.2019

Salaries 100,000 50,000 50,000 Nil

Balance (1:3) 50,000 12,500 37,500 Nil

Total 150,000 62,500 87,500 Nil

Year ended 31.12.2020

1.1.18 – 31.3.2020

Salaries 25,000 12,500 12,500 Nil

Balance (87,500) (21,875) (65,625) Nil

 (62,500) (9,375) (53,125) Nil

1.4.13 – 31.12.2020

Salaries 40,000 15,000 15,000 10,000

Balance (227,500) (45,500) (113,750) (68,250)

 (187,500) (30,500) (98,750) (58,250)

Total (250,000) (39,875) (151,875) (58,250)

**UNIT 8 – BASIS PERIODS AND ACCOUNTING DATES**

**8.1 Introduction**

This unit introduces you to the basis period of assessment

**8.2 Learning Outcome**

After completing this unit you will be able to:

* Understand the accounting dates and basis of assessment
* Understand the commencement and cessation of business



**8.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**8.4 Basis Periods and Basis of Assessment**

A basis period for a given tax year is an accounting period whose profits are to be assessed in the particular tax year.

The bases of assessment applicable are as follows:

**ACCOUNTS PREPARED TO A DATE FALLING BETWEEN 1ST APRIL AND 31ST DECEMBER (INCLUSIVE)**

If accounts are prepared to a date between the above dates inclusive, then the basis of assessment is the current year basis. This means that the tax year in which the accounting period ends is the year in which enquired any resulting profits are to be assessed.

**EXAMPLE**

Mr Chisi, who has been in business for many years, prepares accounts to 31 December each year. He has provided the following tax adjusted trading results for the most recent accounting periods:

 Profit

 K

Year ended 31 December 2018 45,850

Year ended 31 December 2019 51,200

Year ended 31 December 2020 55,650

**Required:**

Show the income tax assessments for all the relevant tax years, identifying the basis periods.

**SOLUTION**

Mr Chisi prepares accounts to a date falling between 1 April and 31 December. Therefore the earliest of the three periods given falls between 1 April 2018 and 31 December 2018, which is in the tax year 2018.

The income tax assessments for Mr Chisi based on the current year basis are as follows:

*Tax year Basis period Profit*

 *K*

2018 y/e 31.12.2018 45,850

2019 y/e 31.12.2019 51,200

2020 y/e 31.12.2020 55,650

**ACCOUNTS PREPARED TO A DATE FALLING BETWEEN 1 JANUARY AND 31 ST MARCH OF THE SAME YEAR (INCLUSIVE)**

If accounts are prepared to a date falling between the above dates, then the basis of assessment appliedis the **preceding year basis**. This means that the profits of the accounting period ending at any time between the dates stated are to be assessed in the preceding tax year.

**EXAMPLE**

Mr Kateule is a businessman who prepares accounts to 31 March each year. The following are the recent tax adjusted trading profits:

 K

Year ended 31 March 2019 65,980

Year ended 31 March 2020 72,450

**SOLUTION**

Accounts are being prepared to 31 March. When this is the case, the preceding year basis is the applicable basis of assessment. The earliest of the accounting periods ends on 31 March 2019. This date falls between 1 January 2019 and 31 March 2019. The tax year in which the profits for the period will be assessed is therefore the tax year 2018, being the preceding tax year.

The income tax assessments for Mr Chisi based on the current year basis are as follows:

*Tax year Basis period Profit*

 *K*

2019 y/e 31.3.2019 65,980

2020 y/e 31.3.2020 72,450

**COMMENCEMENT OF BUSINESS**

In the first period of trading, it may not be possible to prepare accounts for a period of twelve months.As such, the basis of assessment for the first tax year may not be determined using the above running without modification.

The rules applicable on commencement of business are as follows:

1. If the first accounting period is made up of exactly twelve months or less, then the normal rules specified above apply. That is, the current year basis or the preceding year basis may apply depending on when the period ends.
2. If the first accounting period is made up of more than twelve months, then that period should be split into two notional accounting periods for tax purposes. The first period should consist of lessthan twelve months while the second period should consist of exactly twelve months. The profits for the whole period should be allocated to the two notional accounting periods on a time basis.

**EXAMPLE**

Joy Banda commenced to trade on her own account on 1 September 2018. She prepared the first accounts for the 16 month period ended 31 December 2019. She then prepared the next accounts for the year ended 31 December 2020. Her tax adjusted results for the periods of trading are as follows:

 *Profit*

 K

Period ended 31 December 2019 96,000

Year ended 31 December 2020 84,000

**Required:**

Show the income tax assessments for the first three tax years of trading.

**SOLUTION**

Joyce prepares accounts to a date falling between 1 April and 31 December inclusive. Therefore, assessments will be based on the current year basis. The first accounting period exceeds 12 months: it should be split into 2 notional accounting periods for tax purposes. The first period should consist of less than 12 months, while the second period should consist of exactly 12 months ending on the normal accounting date, and then profits should be allocated to each period on a time basis. This will be done as follows:

Period from 1.9.2018 to 31.12.2018 = 4/16 $×$ K96,000 = K24,000

Period from 1.1.2019 to 31.12.2019 = 12/16 $×$ K96,000 = K72,000

Now the position is that there are three accounting periods as shown below:

*Profit*

 K

P/e 31.12.2018 24,000

Y/e 31.12.2019 72,000

Y/e 31.12.2020 84,000

As the earliest accounting period ends in the tax year 2018 and the current year basis is in use, that tax year is the first tax year. The income tax assessments based on the current year basis are as follows:

*Tax year Basis period Profit*

 K

2018 P/e 31.12.2018 24,000

2019 Y/e 31.12.2019 72,000

2020 Y/e 31.12.202 84,000

**CESSATION OF BUSINESS**

This occurs when a business permanently comes to an end. Like in the case of commencement, it not be possible to apply the normal rules without modification.

The rules which are applied are as follows:

1. If the **last accounting period is exactly twelve months** long, then the normal rules will apply.
2. If the last accounting period is **less than twelve months**, then the profits of that accounting period are assessed in the tax year following the one in which the profits of the second last accounting period are assessed.
3. If the last accounting period is made up of **more than twelve months**, then that period should split into a twelve months' period ending on the normal accounting date and a short accounting period ending on the date of cessation. The profits of the long accounting period should be allocation to the two resulting periods on a time basis. The tax year in which the profits of the twelve m period are to be assessed is determined using the normal rules. The profits of the last accounting period (the one with less than twelve months) are to be assessed in the **following tax year**.

**EXAMPLE**

Munshya, who has been running a retail business, ceases to trade on 30 June 2020. He prepared the last accounts for a period of 15 months ended 30 June 2020. Recent tax adjusted trading profits have been as follows:

*Profit*

 K

Y/e 31.3.2018 48,900

Y/e 31.3.2019 58,700

P/e 30.6.2020 74,500

**Required**

Show the income tax assessments for all the relevant tax years.

**SOLUTION**

Accounts have been prepared to 31 March so the preceding year basis applies. Since the last period exceeds 12 months, it should be split into a 12 – month period ending on the normal accounting date of 31 March and a period ending on the date of cessation. The profit for the last period will be assessed in the tax year following that whose basis period is the year ended 31 March 2020.

The last period is split as follows:

Period from 1.4.2019 to 31.3.2020 = 12/15 $×$ K74,500 = K59,600

Period from 1.4.2020 to 30.6.2020 = 3/15 $×$ K74,500 = K14,900

The periods and their respective taxable profits are as follows:

*Profit*

 K

Y/e 31.3.2018 48,900

Y/e 31.3.2019 58,700

Y/e 31.3.2020 59,600

P/e 30.6.2020 14,900

The income tax assessments are as follows:

*Tax year Basis period Profit*

 K

2017 Y/e 31.3.2018 48,900

2018 Y/e 31.3.2019 58,700

2019 Y/e 31.3.2020 59,600

2020 P/e 30.6.2020 14,900

**CAPITAL ALLOWANCES AND BASIS PERIODS**

The capital allowances should be given in full for all the charge years. In the last charge year, there be balancing allowances and balancing charges only as all the assets may have to be disposed of on cessation of business

**EXAMPLE**

Jim Banda began trading on 1 January 2019. He prepared the first accounts for the period from that date to 31 March 2020. The tax adjusted profit figures before capital allowances were as follows:

P/e 31 March 2020 K99,500

Y/e 31 March 2021 K85,000

Jim Banda had the following transactions in non – current assets:

1 January 2019 Bought motor car Cost K15,000

1 June 2020 Bought plant Cost K18,000

1 March 2021 Bought fixtures Cost K20,000

**Required**

1. Calculate the capital allowances for the relevant charge years in question.
2. Calculate the amount of profits chargeable for each of the relevant charge years.

**SOLUTION**

The basis period for the three respective tax years 2018, 2019 and 2020 will be identified using the preceding year basis as the accounts are prepared to 31 March. Since the first period of account is made up of 15 months from 1 January 2019 to 31 March 2020, it will be split into the first 3 months and the last 12 months with the tax adjusted profit before capital allowances being apportioned on a time basis. Capital allowances will then be deducted from the tax adjusted profits as shown below.

2018 Profits 3/15 $×$ 99,500 = K19,900

2019 Profits 12/15 $×$ 99,500 = K79,600

2020 Profits = K85,000

1. CAPITAL ALLOWANCES COMPUTATION

2018

No capital allowances as no assets were acquired in the tax year 2017.

2019

 K

**Motor car**

Wear and tear allowance

20% $×$ K15,000 3,000

**Plant**

Wear and tear allowance

25% $×$ K18,000 4,500

 7,500

2020

**Motor car**

Wear and tear allowance

20% $×$ K15,000 3,000

**Plant**

Wear and tear allowance

25% $×$ K18,000 4,500

**Fixtures**

Wear and tear allowance

25% $×$ K20,000 5,000

Total capital allowances 12,500

1. Final taxable profits

 *2018 2019 2020*

 K K K

Tax adjusted profit 19,900 79,600 85,000

Less capital allowances nil (7,500) (12,500)

Final taxable profits 19,900 72,100 72,500

**UNIT 9 – COMPANY INCOME TAXATION**

**9.1 Introduction**

This unit introduces you to company income tax.

**9.2 Learning Outcome**

After completing this unit you will be able to:

Compute taxable income for companies



**9.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

A company that is resident in the republic of Zambia is liable to company income tax in Zambia on its worldwide income

A company is resident in Zambia for taxation purposes if:

1. The company is **incorporated or formed** in Zambia
2. The **place of effective management** of that company’s business or affairs in Zambia for that year.

**TAXABLE INCOME FOR COMPANIES**

In order to calculate a company’s income tax payable, the income is aggregated and any deductions are made from the aggregate income to arrive at the final amount of taxable income.

Company income tax is then charged on the total taxable income. The income tax is then reduced by any tax withheld from income taxed at source (withholding tax) and any provisional income tax already paid to arrive at the final income tax payable or repayable.

It is a responsibility of the company to compute the appropriate amount of company income tax payable and remit it to the commissioner general

The income of a company includes the following:

* Business profits
* Rental income
* Royalties
* Interest received
* Dividends

Unlike individuals, a company does not have emoluments from employment. All of the income arising in cases where a company offers a service to other companies is taxable business income as opposed to being emoluments from employment. For tax purposes, a company cannot be treated as an employee of any other person.

The format of the computation is as follows:

COMPANY INCOME TAX COMPUTATION FOR THE CHARGE YEAR 2020

 K K

Business profits X

Interest income X

Royalties received X

Total income X

Less allowable deductions (X)

Taxable income X

Income tax on chargeable income X

Less income tax already paid (X)

Income tax payable X

**THE RATES OF COMPANY INCOME TAX**

The standard rate of company income tax is 35%, while income from farming is taxable at the rate of 10%.

Companies that list their shares on the Lusaka Securities Exchange have the tax rate reduced by 2% in the year when they list their shares on the Exchange. If such companies offer one – third of their shares to indigenous Zambians, there is a further reduction in the tax rate by 5%. The reduction for listing shares applies only in the year when shares are listed, while the share offer reduction applies to all the tax years where the shareholding threshold is met.

**EXAMPLE**

Neil Plc is a Zambian company that produces motor vehicle spares. The company prepares accounts to 31 December each year. On 1 January 2020, the company listed its shares on the Lusaka Securities Exchange. For the year ended 31 December 2020, the company had taxable business profits of K987,000.

**REQUIRED:**

Calculate the company income tax payable by Neil Plc for the year ended 31 December 2020.

**SOLUTION**

Since Neil listed its shares on LuSE, the company’s income tax rate should be reduced by 2% only for the current year.

35% - 2% = 33%

NEIL PLC

COMPANY INCOME TAX COMPUTATION FOR THE YEAR 2020

Taxable profit 987,000

Company income tax (33% $×$ K987,000) 325,710

**COMPUTING TAXABLE INCOME**

**BUSINESS PROFITS**

A company’s business profits are computed in the same way as for individual sole traders and partnerships. The taxable business profit is the tax adjusted profit after deducting capital allowances on the assets that are used wholly and exclusively for the purposes of the business.

**COMPUTATION OF TAXABLE BUSINESS PROFITS FOR THE CHARGE YEAR 2020**

 **K K**

Profit before taxation as per accounts X

**Add:**

1. Expenses charged in the accounts but not X

Deductible for tax purposes

1. Taxable income not credited to accounts XX

 X

**Less:**

1. Income credited to accounts but X

Not taxable

1. Capital allowances X

 (X)

Taxable business profits X

The **expenses** that would be allowed if incurred by an individual sole trader would also generally be allowed if incurred by a company. There are some specific examples of the expenses where the treatment for individuals **differs** from the treatment for individual sole traders.

1. There is no apportionment of expenses between business and private use
2. Where the company employs an individual who is differently abled, then company will be allowed to deduct from its business profits the allowance for employing a differently abled person. For the tax year 2020, this allowance is K1,000.
3. If employees/directors are provided with free accommodation by the company, the amount the company is assessed in respect of each employee or director who is accommodated is 30% of the taxable emoluments of that employee or director.
4. The amount of interest that is allowable is limited or restricted to 30% of the Tax Earnings Before Interest, Tax, Depreciation and Amortization (EBITDA) of the company.

**EXAMPLE**

Zora Plc is a Zambian resident company that is listed on the Lusaka Securities Exchange (LuSE). The company obtained a listing on the LuSE on 1 May 2015.

For the year ended 31 December 2020, the company reported a profit figure before taxation of K956,000. This profit figure was arrived at after charging the following expenses:

1. Depreciation of plant and machinery of K23,000
2. Wages, salaries and other labour related costs for employees of K198,000
3. The Managing Director’s emoluments of K224,000 and the Finance Director’s emoluments of K216,000.
4. Motoring expenses, including serving and insurance of motor vehicles of K90,000
5. General expenses of a revenue nature which are all allowable for taxation purposes

The following additional information has also been made available:

1. The company’s Managing Director and the Finance Director are each accommodated in company – owned houses. They do not pay any rent to the company. If the houses were let, the gross rent payable would be K18,000 per annum for each house.
2. The company’s Managing Director has been provided with a company – owned motor car for both business and private use. The motor car is a Nissan Maxima that has a cylinder capacity of 3,000 cc. The Managing Director’s private mileage in the car for 2020 was 70% of the total mileage done.

The Finance Director has been provided with a Nissan Cefiro car for both business and private use. The car has a cylinder capacity of 2,000 cc. The Finance Director’s private mileage in the tax year was 65% of the total mileage done.

The cost of maintaining the motor cars is incurred bybthe company and is included in the motoring expenses of K90,000 charged to the income statement. Of the total motoring expenses, K24,000 relates to the Nissan Maxima while K22,000 relates to the Nissan Cefiro.

1. The company has employed one differently abled person who has been working as its telephone operator since 2015. His salary is included in the figure of K198,000 for wages and salaries for employees.
2. Capital allowances on the company’s assets used in the trade have been agreed at K25,000 for the tax year 2020.

**SOLUTION**

Some challenges here include the treatment of the private element of the motoring expenses relating to personal to holder motor cars. As a matter of fact, when computing tax adjusted profits for companies, there are no expenses which are partly allowable and partly disallowable as is the case with sole traders and partnerships. For companies, it is either that the whole expense is allowed, or it is entirely disallowed. As a result, the whole expenditure incurred by the directors as motoring expenses are allowed in full and therefore no adjustment will be made when computing taxable profits for the company.

In the case of provision of free accommodation by the employer, the amount chargeable on the employer is 30% of the chargeable emoluments payable to the two directors who were accommodated by the company.

The allowable deduction for employing differently abled persons is a straightforward adjustment.

**ZORA PLC**

**COMPANY INCOME TAX COMPUTATION FOR THE TAX YEAR 2020**

 K K K

Profit before taxation as per accounts 956,000

Add back:

Depreciation 23,000

Accommodation benefit:

Managing Director (30% $×$ K224,000) 67,200

Finance Director (30% $×$ K216,000 ) 64,800

 132,000

Personal to holder car benefit

Managing Director 40,000

Finance Director 30,000

 70,000

 225,000

 1,181,000

Less:

Differently abled person deduction 1,000

Capital allowances 25,000

 (26,000)

Taxable profit 1,150,000

Company income tax payable (35% $×$ 1,150,000) 404,250

**CAPITAL ALLOWANCES**

These are available on qualifying assets that are used wholly and exclusively for the purposes of the business. They include:

1. Implements, plants and machinery where a wear and tear allowance of 25% on cost applies, the rate of 20% apply on non – commercial vehicles

There is no adjustment for private use of motor vehicles and other assets owned by the company.

1. Industrial buildings including low cost housing on which annual wear and tear allowance of 5% on cost applies, 10% on cost applies for low cost housing. Investment allowances are available on newly constructed buildings at the rate of 10% on cost.
2. Commercial buildings on which annual wear and tear allowances are claimed at the rate of 2% on cost.

**INVESTMENT INCOME**

This is income from savings and financial investments. It includes bank interest, building society interest, Treasury bill discounts, interest on government bonds (GRZ bonds), dividends from Zambian companies, royalties and rent and premiums from letting of property.

When a Zambian company receives bank interest, building society interest, treasury bill interest, GRZ bond interest and royalties, withholding tax of 15% will usually have been deducted, so the amount received is grossed up and included in the computation of the total taxable income.

Income from the letting of property shall be subject to withholding tax of 10% which represents the final tax.

Dividends received from Zambian companies are net of final withholding tax of either 0% for mining companies and companies listed on LuSE or 15% for all other types of company, so no further assessment should be made.

**RELIEF FOR TAX LOSSES INCURRED BY COMPANIES**

A tax loss is a tax adjusted loss incurred by a taxable person. When a company incurs a tax loss, that loss is carried forward and set off against the first available profits of the company arising from the same source as that which produced the loss. That loss can be carried forward for a maximum of five years. If at the end of the fifth year there is still an outstanding loss, that outstanding loss cannot be relieved in any other way.

**UNIT 10 - TAXATION OF MINING OPERATIONS**

**10.1 Introduction**

This unit introduces you to taxation of mining operations

**10.2 Learning Outcome**

After completing this unit you will be able to:

* Calculate taxation of company income dealing with taxation of mining operations.



**10.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**10.4 Introduction to Mining Operations**

Mining is defined in the Act as the extraction of solid, liquid or gaseous material from beneath the surface of the earth in order to win minerals, or any operations directly or indirectly necessary or incidental thereto.

Minerals – is any substance occurring naturally in /on earth or in/under water formed by or subjected to geological process excluding

1. Water
2. Petroleum

Mining operations are only permitted after obtaining a mining rights. Rights to be granted are:

* Exploration license
* Mining license

Non –Mining rights to be granted:

* Mineral processing license
* Mineral trading permit
* Mineral import permit
* Mineral export permit

**MINERAL ROYALTY**

Is a payment received as consideration for the extraction of minerals.

It’s charged on the quantity of mineral extracted and sold per month rather than profit.Its payable as soon as production begins.

**LIABLE PERSONS FOR MINERAL ROYALTY**

Holders of the following mining rights on minerals produced under their respective licenses:

* Large scale mining license
* Large scale gemstone license
* Small scale mining and gemstone license
* Artisans mining right

The following are the liable persons for mineral royalty:

* Any person in possession of minerals (mineral royalty not paid by suppliers) but without mining rights.
* All persons carrying out quarrying of industrial minerals (include quarrying gravel, clay and sand).
* All persons that use the minerals as inputs or raw materials in their manufacturing process.

**CLASSIFICATION FOR TAX PURPOSES**

* Minerals are classified in 5 categories:
1. Base metals - non precious metal common and chemically active (iron ,copper, Lead etc)
2. Energy minerals – naturally occurring substance in the earth’s crust used as source of energy (coal, uranium) but not petroleum.
3. Gemstones – nonmetallic substances used in jewelry (diamond, emerald, garnet, ruby etc)
4. Industrial minerals – are rocks or minerals other than the mentioned used in their natural state or after a transformation (sands, clay , gravel, salt, talc etc)
5. Precious metals – high value but not defined in the Act (gold, silver, platinum etc)

**MINERAL ROYALTY RATES**

Mineral royalty rates effective 1st January 2019:

* Base metals (other than copper) – 5% on norm value
* Energy and Industrial minerals – 5% on gross value
* Gemstones – 6% on gross value
* Precious metals – 6% on norm value

**Five tier regime for copper based on norm value:**

1. Less than $4,500 - 5.5%
2. $4,500 but less than $6,000 – 6.5%
3. $6,000 but less than $7,500 – 7.5%
4. $7,500 but less than $9,000 – 8.5%
5. $9,000 and above – 10%

**CALCULATION OF MINERAL ROYALTY IS BASED ON:**

1. **GROSS VALUE**- is the realized price for sale free on board (FOB), at point of export in Zambia or point of delivery within Zambia.

It’s applicable to: industrial and energy minerals, gemstones

1. **NORM VALUE**
* The monthly average London metal exchange cash price per metric ton multiplied by the quantity of the metal or recoverable metal sold
* The monthly average Metal Bulletin cash price per tonne multiplied by the quantity of the metal sold or recoverable metal sold to the extent that the metal price is not quoted on the London Metal Exchange
* The monthly average cash price per metric tonne of any other exchange market approved by the Commissioner General multiplied by the quantity of the metal or recoverable metal sold to the extent that the metal price is not quoted on the London Metal Exchange or Metal Bulletin

NB: For the purposes of calculating the norm value, the metal price and monthly BOZ mid-rate can be obtained from large taxpayer or nearest domestic taxes office

**DUE DATE OF PAYMENT**

Mineral royalty is due and payable within 14 days after the end of the month in which the sale of minerals is done.

Failure or late payment attracts penalty and interest. A penalty of 5% per month or part is charged on late payments of mineral royalty. Interest is charged on the overdue at the rate of 2% above the BOZ discount rate per annum.

Monthly royalty returns are due within 14 days after end of the month to which the return relates.

**EXAMPLE**

PAC PLC is a mining company engaged in the mining of copper in Zambia. The company extracted and sold the following quantities of copper each month, in the first quarter of 2020:

Month Quantity (tonnes)

January 2020 15,000

February 2020 20,000

March 2020 25,000

The norm price of copper was $4,000 per tonne in January 2020, $4,600 in February 2020 and $6,500 in March 2020. The relevant exchange rates were as follows:

Month ZMW/Per $

January 2020 K9.95

February 2020 K9.90

March 2020 K9.80

**Required:**

Compute the amount of mineral royalty paid by PAC PLC for each month.

**SOLUTION**

1. Mineral royalty for January 2020

The norm price US$ 4,000 per tonne in January 2020 was less than US$ 4,500, and therefore the relevant rate of mineral royalty is 5.5% of norm value.

Norm Value = US$ 4,000 per tonne$×$ 15,000 tonnes

 = US$60 million

Mineral royalty = ($60,000,000 $×$ 5.5%) $×$ K9.95

 = K32,835 million

1. Mineral royalty for February 2020

The norm price US$ 4,600 per tonne in February 2020 was between US$ 4,500, and US$ 6,000 ,therefore the relevant rate of mineral royalty is 6.5% of norm value.

Norm Value = US$ 4,600 per tonne$×$ 20,000 tonnes

 = US92 million

Mineral royalty = ($92,000,000 $×$ 6.5%) $×$ K9.90

 = K59,202 million

1. Mineral royalty for March 2020

The norm price US$ 6,500 per tonne in March 2020 was above US$ 6,000 but less than US$7,500 and therefore the relevant rate of mineral royalty is 5.5% of norm value.

Norm Value = US$ 6,500 per tonne$×$ 25,000 tonnes

 = US$162.5 million

Mineral royalty = ($162,500,000 $×$ 7.5%) $×$ K9.80

 = K119,44 million

**TAX INCENTIVES IN THE MINING COMPANIES**

1. Reduced standard rate of company income at 30%.
2. 20% deduction of capital expenditure incurred for the purposes of mining in capital allowances.
3. 20% on cost of capital expenditure incurred on the provision of services in mining township (construction of roads, schools etc.)
4. Input tax claim for 10years on pre- production expenditure for exploration companies.
5. Dividends paid are subjected to WHT at a rate of 0%.
6. 10 year period carry forward of tax losses.
7. Remission of duty on special mining vehicles and machinery specified as
8. Mine – locomotives , Dump trucks – off high way

**CAPITAL EXPENDITURE**

Capital allowances in form of wear and tear allowances for mining companies are available at the rate of exp20% on all capital expenditure that is incurred for the purposes of mining as long as the expenditure has not been written off elsewhere.

**INDEXATION OF CAPITAL ALLOWANCES**

If the accounting records are maintained by a mining company in USD then capital allowances may be indexed using the following formula:

 1 + $\frac{(R₂ -R₁)}{R₁}×$ Capital allowances

𝑹₁ is the average BOZ kwacha per $ mid-rate for the accounting period preceding that in which capital allowances is being claimed.

𝑹₂ is the average BOZ kwacha per $ mid-rate for the accounting period in which capital allowances is being claimed.

**EXPENDITURE IN MINING TOWNSHIPS**

Mining companies can also claim capital allowances at the rate of 20% on the cost of any capital expenditure that is incurred in mining townships to provide services to the mining communities, such as:

* The construction or rehabilitation of roads
* Street lighting systems
* The construction of community schools

**MINING LOSSES**

Losses are carried forward and relieved against future profits arising from the same business.

However, the loss is restricted to 50% of the mining income, if it exceeds 50%, it is deducted from the mining income in the following charge year.

**INDEXATION OF LOSSES**

To maintain real values of losses to be carried forward, the losses are indexed using the formula:

 1 + $\frac{(R₂ -R₁)}{R₁}×$ Mining loss brought forward

𝑹₁ is the average BOZ kwacha per $ mid-rate for the accounting period preceding that in which loss relief is being claimed

𝑹₂ is the average BOZ kwacha per $ mid-rate for the accounting period in which the loss relief is being claimed

**EXAMPLE**

Mangochi mining company involved in industrial mining operations incurred a loss from mining of K9,560,000 in the year ended 31 December 2019 and average BOZ $ to kwacha mid-rate for the period was K5.40. During the year 31 December 2020, Mangochi mining company earned a tax adjusted profit from mining of K3, 350,000 and the average BOZ $ to kwacha mid-rate was K6.35 for the year ended 31 December 2020.

**Required:**

Calculate the amount of mining loss that will be relieved against the mining profits of the year ended 31 December 2020, and the amount of unrelieved loss to be carried forward as at 31 December 2020

**SOLUTION**

The indexed mining loss is =1 + $\frac{(R₂ -R₁)}{R₁}×$ Mining loss brought forward

 = 1 + $\frac{(6.35 - 5.40)}{5.40}×$ K9,560,000

 =K11,241,852

**MANGOCHI MINING COMPANY**

 K’000

Mining profits for the year 3,350

Less mining loss relief (W) (1,675)

Taxable income 1,675

The mining loss still being carried forward is:

K

Indexed mining loss brought forward 11,241,852

Less loss relieved in 2020 restricted to (50% $×$ K3,350,000) (1,675,000)

Mining loss carried forward as at 31 December 2020 9,566,852

**COMPANY INCOME TAX FOR MINING OPERATIONS**

Mining companies are expected to contribute a great amount of revenue to the Zambian economy. This is so because the country had always depend on copper when all the mines were state owned and controlled. As a result of privatization, taxes from mining companies are expected to be substantial.

In the tax year 2020, income from mining operations is taxable at a flat rate of 30%. Income generated by businesses engaged in mineral processing is also taxable at the rate 30%.

**EXAMPLE**

Zondwa Mining Limited is a zambian resident mining company, engaged in the extraction and sale of copper. The company made a profit before taxation of K3,920,000 for the year ended 31 December, 2020. The gross sales revenue of the company for the year was K19,500,000. Mineral royalty was paid at the appropriate rates on the relevant due dates during the year and has been properly accounted for.

The profit before taxation was arrived at after crediting a dividend received from a Zambian company which is listed on the Lusaka Securities Exchange, of K90,000 (gross) and also after charging the following expenses:

 K

Depreciation of non – current assets (fixed assets) 1,350,000

Gifts of Zondwa calendars, costing K90 per calendar 125,000

Irrecoverable trade debts, written off 850,000

Other operating expenses 5,400,000

Other operating expenses include expenditure of K1,200,000 incurred on constructing boreholes for the local community, in the mine township. The remaining balance comprises general operating expenses which are allowable for tax purposes.

**Additional information:**

1. The company purchased new mining equipment at a cost K7,750,00, in February 2020, which was immediately brought into use
2. Capital allowances on other assets used wholly and exclusively for business purposes have been determined to be K850,000 for the tax year 2020.
3. The provisional income tax paid during the tax year 2020 was K939,000.

Required

Calculate the company income tax payable on the mining profits for the tax year 2020.

**SOLUTION**

**ZONDWA MINING LIMITED**

**COMPUTATION OF TAXABLE PROFIT FOR THE YEAR 2020**

 K K

Profit before taxation as per accounts 3,920,000

Add:

Depreciation 1,350,000

Construction of boreholes 1,200,000

 2,500,000

 6,470,000

Less:

Dividend received 90,000

Capital allowances (W) 2,640,000

 (2,730,000)

Taxable mining income 3,740,000

COMPUTATION OF COMPANY INCOME TAX PAYABLE

 K

Company income tax 1,122,000

(K3,740,00$×$ 30%)

Less provisional income tax paid (939,000)

Company income tax payable 183,000

Workings

COMPUTATION OF CAPITAL ALLOWANCES

 K

**Boreholes**

Wear and tear allowance (K1,200,000$×$ 20%) 240,000

**Mining equipment**

Wear and tear allowance (K7,750,000$×$ 20%) 1,550,000

Other capital allowance 850,000

Total 2,640,000

**UNIT 11 – FARMING ENTERPRISES**

**11.1 Introduction**

This unit introduces you to farming and agro – processing businesses

**11.2 Learning Outcome**

After completing this unit you will be able to:

* Explain the characteristics of farming and fishing enterprises
* Compute farming profits for individuals and companies
* Explain the capital allowances for farming enterprises
* Explain the relief losses from farming
* Calculate average of farming income



**11.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**FARMING** is defined in the income tax act as:

The cultivation of crops and plants, raising of livestock or poultry, beekeeping and rearing fish but excludes letting of any property or provision of a service ancillary to farming. The only income that arise from the various activities as mentioned in the definition above qualifies as farming/fishing income. Tax provisions relating to farming are also extended to agro-processing business.

**AGRO PROCESSING**is any farming produce produced in Zambia to any process which materially changes the farming produce in substance, character or appearance there by making it a food product.

**COMPUTING FARMING PROFITS**

* Tax adjusted profits for farming enterprises are calculated in the same way as for other business enterprises.
* Expenses incurred are allowed if they are of a revenue nature and they are incurred wholly and exclusively for the purposes of farming.
* Capital expenditure and all other expenses which are disallowed in respect of any other business are also disallowed when they are incurred by a farmer.

**CAPITAL ALLOWNACES FOR FARMING ENTERPRISES**

Farming enterprises are entitled to capital allowances on the qualifying assets which are used wholly and exclusively for the purposes of farming.

Farming can claim these capital allowances in the following ways.

**FARM IMPLEMENTS**

These include the implements, plants and machinery which are used by a farmer for the purposes of farming.

Any implements, plant and machinery directly used in farming qualify for a 100% wear and tear allowance.

Such implements are only those directly used in farming such as:

* Tractors
* Ploughs
* Farming implements
* Irrigation and harvesting implements

Implements, plant and machinery directly used in farming qualify for a 100% wear and tear allowance. Implements which are not directly used in farming qualify for an allowance of 25% of cost and 20%on cost in case of non-commercial vehicles.

**FARM IMPROVEMENTS**

Is any permanent work including a farm dwelling and fencing appropriate to farming and any building constructed for and used for the welfare of employees in relation to farming land owned or occupied by the farmer claiming allowance for profit ascertainment.

Farm improvement allowance is given at 100% of the expenditure on the cost of farm improvements.

Expenditure that qualifies for farm improvement allowance are as follows:

* Expenditure on construction of barns and other storage buildings
* Expenditure on the construction of farm dwellings( so long it’s not used by the farmer claiming allowance)
* Expenditure incurred on fencing
* Expenditure on the construction of buildings for the welfare of employees.

A **farm dwelling** is any permanent building that is used as a dwelling, which is not used by the farmer claiming the allowance as the homestead for themselves and their family.

For tax year 2020, the **maximum amount** qualifying for farm improvement allowance in respect of expenditure incurred on construction farm dwelling is K20,000. Therefore, if the cost of a farm dwelling exceeds K20,000 , the farm improvement allowance of K20,000 should be given.

**FARM WORKS**

Are all works which are carried out on the farm. They don’t include improvements or industrial or commercial buildings.

Farm works allowance is given at 100% on the expenditure incurred on farm works.

Qualifying expenditure includes:

* Expenditure incurred on works for the prevention of soil erosion
* Expenditure incurred on carrying out aerial or geographical survey
* Wells
* Boreholes
* Stumping and clearing
* Expenditure incurred on water conservation

**DEVELOPMENT ALLOWANCE**

Any capital expenditure incurred on the development of a plantation qualifies for an allowance.

It’s given at a rate of 10% of the expenditure.

Examples

* Tea plantation
* Coffee and cocoa plantation
* Orange and other citrus fruit plantations

Expenditure incurred in the growing of rose flowers also qualifies for the development allowance.

**EXAMPLE**

MrJuka is a farmer who always prepares accounts to 30 September each year. For the tax year 2020, he incurred the following capital expenditure:

Bought a Toyota Hilux single cab for 90,000

Constructed a farm dwelling for use

by an employee costing 28,000

Bought a tractor for 39,000

Bought furniture for use in his farm office 25,000

Expenditure on stumping 11,000

Digging a well at a cost of 3,000

Fencing the farm at a cost of 22,000

The tax adjusted profit before deducting capital allowances for the tax year 2020 amounted to K509, 000.

**REQUIRED:**

Calculate the final taxable farming profits chargeable on MrJuka for the tax year 2020.

**SOLUTION**

**MR JUKA**

**COMPUTATION OF THE FINAL TAXABLE FARMING PROFIT FOR THE TAX YEAR 2020**

 K K K

Tax adjusted profit before capital allowances 509,000

Less Capital allowances:

Implements, plant and machinery

Toyota Hilux 25% $×$K90,000 22,500

Furniture 25% $×$ K25,000 6,250

Tractor 100% $×$ K39,000 39,000

Total capital allowances on P&M 67,750

 Farm improvement allowances:

Farm dwelling (restricted) 20,000

Fencing the farm 22,000

Total farm improvement allowances 42,000

Farm works allowance:

Cost of stumping 11,000

Cost of digging a well 3,000

Total farm works allowance 14,000

Total capital allowances (123,750)

Final taxable farming income 385,250

**AVERAGING OF FARMING AND FISH PROFITS**

A farmer can make irrevocable elections to have the farming and fishing income of two consecutive years averaged. The averaged income becomes chargeable in both years.

This election is made if one year has produced a loss while the other year has produced a profit or if one year is lower than the other year. I.e. before the year end

A trader cannot make an election on an averaged income.

**EXAMPLE**

The following are the farming profits as adjusted for taxation purposes for MrsNjongolo, a farmer:

 Tax year Profits

 K’000

 2018 567

 2019 215

 2020 633

Mrs Njongolo has made an irrevocable election to average the income of the tax year 2019 with that of 2020.

**Required:**

1. Calculate the final taxable profits for the tax years 2018, 2019 and 2020.
2. Explain whether Mrs Njongolo can make a further election to have the result for 2019 in part (a) above averaged with that of 2018.

**SOLUTION**

1. The average profit is:

 K

Income for 2019 215,000

Income for 2020 633,000

Total income 848,000

Average profit is = $\frac{Total income }{2}$

 = K848,000

 = K424,000

The final chargeable profits for the tax years mentioned are:

Tax year Profit

 K

2018 Actual profit made 567,000

2019 Averaged with 2020 424,000

2020 Averaged with 2020 424,000

1. Mrs Njongolo cannot make a further election to average the profit for the tax year 2018 with the averaged amount for 2019. Such an election is not allowed. Furthermore, the tax year following the second consecutive tax year after 2019, which is 2020, will have ended.

**PERSONAL INCOME TAX ON FARMING PROFITS**

The maximum rate of income tax on farming profits made by individual farmers is 10% for the tax year 2020. If a farmer has only farming profits, then the first K39, 600 will be taxed free and any excess over K39, 600 will be taxed at the rate of 10%.

**EXAMPLES**

Mrs Chikwakwa , a farmer, has farming profits of K98,000 for the tax year 2020. her only other income is dividend of K33,000 (net) received from a Zambian company.

**Required:**

Calculate the income tax payable by Mrs Chikwakwa for the tax year 2020.

**SOLUTION**

**MRS CHIKWAKWA**

**PERSONAL INCOME TAX COMPUTATION FOR THE TAX YEAR 2020**

 K

Farming profits 98,000

Less tax free amount (39,600)

 58,400

Income tax payable

10% $×$ K58, 400 5,840

If a farmer has farming income and non-farming income, then the tax free band should be allocated to non-farming income first.

**EXAMPLE**

Kasongo has been running a farm for some time now. The average turnover in the last 3 years has been around K900, 000. For the tax year 2020, he made a tax adjusted farming profits of K55, 000, after deducting capital allowances. He also received employment income of K51, 600 from part time employment. Income tax deducted from part time employment income under the pay as you earn system was K7, 000.

**Required:**

Calculate the income tax payable by Kasongo for the tax year 2020.

**SOLUTION**

**KASONGO**

**PERSONAL INCOME TAX COMPUTATION FOR THE TAX YEAR 2020**

 Non – farming Farming

 Total income income

 K K K

Income from part- time employment 51,600 51,600

Farming profits 55,000 55,000

 106,600 51,600 55,000

Less tax free income (39,600) (39,600)

 67,000 12,000 55,000

Income tax on non – farming income

25%$×$ K9,600 2,400

30%$×$ K2,400 720

Income tax on farming income

10%$×$ K55,000 5,500

 8,620

Less Pay As You Earn (7,000)

Final income tax payable 1,620

**COMPANY INCOME TAX ON FARMING PROFITS**

A company with farming profits pays income tax at the rate of 10% on its farming profits.

All non-farming income will be charged at income tax rate of 35 %.

**EXAMPLE**

Phil Ltd is a Zambian resident company for taxation purposes. For the tax year 2020, the company has produced the following results:

 K

Profits from farming 809,000

Profits from manufacturing 402,550

Interest income 90,000

The actual gross interest for the tax year 2020 was K90,000. Withholding tax had been deducted at 15% at source.

The company does not have any other income apart from the ones stated above.

Required

Calculate the company income tax payable by Phil Ltd for the tax year 2020.

**SOLUTION**

**PHIL LTD**

**COMPANY INCOME TAX COMPUTATION FOR THE TAX YEAR 2020**

 K

Profits from manufacturing 402,550

Interest income 90,000

Total non – farming income 492,550

Farming profits 809,000

Total taxable income 1,302,550

Company income tax on non – farming income

35% $×$ K492,550 172,393

Company income tax on farming income

10% $×$ K809,000 80,900

 253,293

Less withholding tax on interest

15% $×$ K90,000 (13,500)

Final company income tax payable 239,793

**RELIEF FOR LOSSES FROM FARMING AND FISHING ENTERPRISES.**

If farming or fishing business incurs a tax loss, that loss can be carried forward and set off against the first available profits of that business arising from the same source as that which produced the loss. That loss can be carried forward for a maximum of five years.

**UNIT 12 – PROPERTY TRANSFER TAX**

**12.1 INTRODUCTION**

This unit introduces you to property transfer tax which is chargeable on any person who transfers property to another person.

**12.2 Learning Output**

After completing this unit you will be able to:

Explain the meaning of transfer and realized value

* Calculate property transfer tax



**12.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**Property transfer tax** (PTT) is chargeable on any person who transfers property to another person.

It is chargeable at the rate of 5% of the realized value of the property (10 % for mining rights). This tax is payable by the transferor of property. It’s not payable by the transferee. The tax should be paid within 14 days from the date when the transaction is completed. There are no penalties or interest for late payment of PTT.

For the purpose of PTT, there are four categories of assets that qualify as property. They are all immovable property, which means that PTT does not apply on the transfer of chattels.

Chattels are tangible movable property.

The categories of property chargeable are:

* Any land in Zambia (including any building on that land.
* Any building ,structure , or other improvements
* Any share issued by a company in Zambia that is not listed on the Lusaka Securities Exchange (LuSE); all LuSE listed shares are therefore exempt from PTT
* Any mining right or an interest in a mining right
* Any Intellectual Property such as trademarks, patents and brands.

**TRANSFER OF PROPERTY**

A transfer of property occurs when there is a change in the ownership of that property. Therefore, a transfer includes the following:

* A disposal of property
* A disposal of a part of the property (a part disposal in case of shares)
* A gift of the property (in the case of family members generally)

**REALISED VALUE**

Is the amount on which PTT is charged. It is the price at which the property could, at the time of the transfer, be sold for on the open market.

As a general rule, the realized value of any **property** is the **higher** of:

1. The **contract price** agreed upon by the transferor and the transferee; and
2. The **open market value**

For shares, the realized value is the higher of:

1. The **open market value** of those shares
2. The **nominal value** of the shares.

For a transfer of **mining rights** or an interest in mining rights, the realized value shall be the higher of:

1. The actual price of the mining right or an interest in mining rights at the time of the transfer; and
2. The value as determined by the commissioner general

**TRANSFERS TO IMMEDIATE FAMILY MEMBERS**

A member of the immediate family is any of the following:

* A spouse
* Own blood child
* Duly adopted child
* Step – child

Where a person transfers property to a member of the immediate family, the realized value of such property is the actual price received by the transferor, if any.

**EXEMPT ORGANISATIONS**

The following are exempt from PTT:

1. The government
2. Any foreign government
3. Local authorities
4. Registered trade unions
5. Approved pension fund or medical aid society etc

**EXEMPT TRANSACTIONS**

The following are not liable to PTT:

1. The transactions as a result of the sale or other disposal of any stock or share listed on the LuSE.
2. Contribution towards the equity for a company.
3. A transfer is not liable to PTT if it is occasioned by death of the transferor to a member of the immediate family.

**EXAMPLE**

Julie Mumbi made disposals of assets as follows during the tax year 2020.

**Shares in Muzo Plc**

He sold 100,000 ordinary shares of K1.00 each in MuzoPlc for K250,000 on 31 October 2020. He had acquired 200,000 ordinary shares of K1.00 each in MuzoPlc through a public offer for sale at a price of K1.20 per share in May 2007. Muzo Plc was listed on the Lusaka Securities Exchange in May 2007.

**Farming plot in Mkushi**

He sold a five arce plot of land in October 2020 for K225,000. This plot was of a 20 – acre farming plot that he bought for K400,000 in January 2013. The plot was sold at a price that the government values estimated as the open market value.

**Shares in JM Ltd**

He sold 2,000,000 ordinary shares of K1.00 each in JM Ltd for K10,000,000 during December 2020. He had bought 5,000,000 ordinary shares of K1.00 each in the company in May 2007 when the company was formed by him with a friend. Julius paid K5,000,000 for the shares on acquisition.

**Required**

Calculate the property transfer tax paid by Julie Mumbi and state when it should have been paid.

**SOLUTION**

When determining the amount of PTT paid, the first thing to determine is whether that property is chargeable and then the amount of realized value for each property.

**Shares in MuzoPlc**

MuzoPlc is a company that has listed its shares on the LuSE. Shares that are listed on the LuSE are not chargeable property. Therefore, property transfer tax is not payable on the disposal of shares in Muzo Plc.

**Farming plot in Mkushi**

Land is a chargeable property. The realized value is the greater of the open market value and the actual sales price. As the plot was sold at the open market value, the price paid by the buyer is the realized value.

Property transfer tax paid is = 5% $×$ K225,000

 = K11,250

The amount of PTT of K11,250 should have been paid within 14 days following the conclusion of the transaction.

**Shares in JM Ltd**

Shares in JM Ltd are chargeable as this company is not listed on the LuSE. The realized value is the greater of the nominal value and the open market. It is difficult to value unlisted shares. The sales price can be assumed to be the open market value as it is more than the nominal value.

Property transfer tax paid = 5% $×$ K10,000,000

 = K500,000

PTT of K500,000 should have been paid within 14 days after completion of the transaction.

**UNIT 13 – VALUE ADDED TAX**

**13.1 Introduction**

This unit introduces you to Value Added Tax. It provides an overview of the scope of VAT, the accounting procedures and the special schemes

**13.2 Learning Outcome**

After completing this unit you will be able to:

* Explain the taxable and exempt supplies
* Calculate Value Added tax payable
* Understand the registration and deregistration
* Explain tax invoice, tax point and tax period.



**13.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**Value Added Tax (VAT)**is a tax on the turnover of taxable supplies of goods and services made in Zambia by a taxable person in the course or furtherance of any business carried on by them. A non-registered trader cannot charge VAT. Only those traders who make taxable supplies can register for VAT.

**TAXABLE SUPPLIES**

Taxable supplies are those on which VAT is charged. They consist of standard rated supplies and zero rated supplies.

**STANDARD RATED SUPPLIES** – are those on which VAT is added at the rate 16% on the VAT exclusive amount. If the amount is VAT inclusive, the VAT fraction is used to calculate the tax.

The VAT fraction is 4/29. If the figure is VAT inclusive, the amount of VAT is calculated at the rate of 4/29. The VAT fraction of 4/29 is the simplified form of the fraction 16/116.

**ZERO RATED SUPPLIES**–are those on which VAT is charged at the rate of 0%. For zero rated supplies, the VAT inclusive and VAT exclusive amount are the same.

**EXEMPT SUPPLIES**

These are supplies of goods and services to which the following apply:

1. No VAT is charged on them
2. They are not taken into account in determining whether a trader is taxable person
3. Input tax attributed to them is not normally available for credit.

**INPUT AND OUTPUT TAX**

**OUTPUT TAX –** is VAT on the turnover. It is the potential amount of VAT payable by a VAT registered trader.

**INPUT TAX**–is VAT incurred on expenses. It is normally recoverable by way of credit against output tax if that input tax is incurred on supplies used to make taxable supplies. The amount of VAT payable by a VAT registered trader is therefore the excess of output tax over input tax.

**EXAMPLE**

Alinani has been trading for many years and is registered for VAT. For the month of January 2020, he had the following transactions

* Sales 58,000
* Purchases 20,000
* Expenses 11,000

The sales are made up of standard rated supplies and are VAT inclusive. Only 70% of the purchases are standard rated and are VAT exclusive. The remaining amount of purchases are zero rated supplies. All the expenses are standard rated and are VAT exclusive.

**Required:**

Calculate the amount of VAT payable by Alinani for the month of January 2020.

**SOLUTION**

In respect of supplies that are VAT inclusive as in the case of sales, VAT will be computed at the VAT fraction of 4/29. In the case of purchases and expenses, VAT will be calculated using the standard rate of 16% as these amounts are VAT exclusive.

 K K

Output tax

Sales (K58,000$×$ 4/29) 8,000

Less recoverable input tax

Purchases (K20,000$×$ 70% $×$ 16%) 2,240

Expenses (K11,000$×$ 16%) 1,760

Total recoverable tax (4,000)

VAT payable 4,000

**REGISTRATION FOR VALUE ADDED TAX (VAT)**

1. **Compulsory registration**

A trader is required to compulsory register for VAT if the turnover of their taxable supplies, excluding VAT, for the 12 months or three month period just ended exceeds the registration threshold. The current threshold is K800,000 per 12 months or K200,000 per 3 months.

Late registration for VAT attracts automatic penalties consisting of 10,000 fee units for each standard tax period the supplier remains unregistered after meeting the registration threshold.

1. **Voluntary registration**

A trader who makes taxable supplies whose VAT exclusive taxable turnover is below the registration threshold can register for VAT voluntarily

**DEREGISTRATION**

Deregistration is the cancellation for a trader’s VAT registration. A trader can be deregistered if any of the following occur, while that trader is registered for VAT:

1. If the business is sold or ceases to trade permanently.
2. If a trader submits nil returns for 12 consecutive standard periods.

**THE TAX INVOICE**

Registered traders are required to issue **tax invoices** when they make supplies of goods and services not later than 30 days after the time when the supply of goods is made.

**TAX POINT**

Is the time of supply deemed to have taken place.It’s important to establish the tax point in respect of supplies for VAT purposes, because it’s used for determining the tax period and also deciding the scheme or VAT rate to use to supply when there is a change in VAT scheme.

**Basic tax point** – is the time when goods are delivered, collected or made available to the customer, or when the services are performed.

Input VAT is **recoverable** from the commissioners if certain conditions are satisfied. i.e

* The trader is registered for VAT purposes
* Supply must be made to the taxable person making the claim
* Supply must be supported by evidence e.g in form of tax invoice
* Person making the claim must use the goods and services for the business.
* The VAT should not be that which is irrecoverable

Irrecoverable input VAT. Its cant be claimed and its excluded from the credit.

Input vat on any of the following:

* Business entertainment
* Motor cars that are not wholly for business unless that car is
1. Acquired for resale
2. Acquired for use in taxi business
3. Acquired for a hire business or driving school
* Telephone bills
* Cost of petrol - unless if it bought for resale then its recoverable
* Cost of diesel (90% of input vat incurred is recovered the 10% is not recoverable
* Domestic refrigeration equipment, air conditioners, mobile phones, vehicle parts, TV sets, decoders , video players
* Additionally input on consumables such as stationary, lubricants and spare parts is not recoverable

However where such products are meant for resale or are a main input in the business, then input VAT can be claimed.

**DUE DATES AND PENALTIES**

The due date for payment of VAT and submission of the VAT returns is the 18th day following the end of the tax period to which the VAT and the return relate if the return has 10 or more transactions.

The daily penalty for late submission of VAT returns is the higher of:

* 1,000 penalty units (K300)
* 0.5% of the amount of VAT payable

Interest is charged on overdue tax at a prescribed rate of interest. The rate is normally BOZ discount rate plus 2%.

**UNIT 14 – CUSTOMS AND EXCISE DUTY**

**14.1 Introduction**

This unit introduces you to the duties which apply on the import and export of goods.

**14.2 Learning Outcome**

After completing this unit you will be able to:

* Understand the tariffs, the customs value (VDP), customs duty and excise duty
* Compute the customs value (VDP), customs duty and excise duty
* Explain the importation and clearance of motor vehicles



**14.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**Customs duty** is administered by the **Customs Services Division** while **excise duty** is administered by the **Domestic Taxes Division**of the **Zambia Revenue Authority (ZRA).**

**CUSTOMS DUTY**

Is a **duty on imported goods**. The customs duty rates fall within the following bands depending on the type of goods imported:

1. For raw material, medicines and most capital equipment 0% - 5%
2. For intermediate goods and semi – finished goods 15%
3. For finished goods 25%

**IMPORTATION OF GOODS**

It is legal requirement that all goods imported are fully declared at the point of entry

**DOCUMENTATION**

A bill of entry with supporting documents must be submitted to effect customs clearance. However, the clearance of motor vehicles involves payment of all appropriate taxes and duties.

The following documents are required to be submitted at the time of importation:

1. Invoice or contract of sale indicating the price paid
2. Insurance certificate
3. Freight statement (overland costs from port)
4. Bill of lading
5. Any other documents relevant to the purchase, shipments etc like police clearance certificate and certificate of registration.

**VALUE FOR DUTY PURPOSES**

Is always based on the total cost of the vehicle up to the point of entry into Zambia. This includes:

* The price paid (sometimes referred to as Free on Board (FOB).
* The insurance charges
* The transport costs
* Any other incidental costs incurred in importing the vehicle into Zambia. Customs value is based on Cost, Insurance and Freight (CIF).

Value for Duty Purpose is **kwacha equivalent of the CIF**. The commissioner general determines the rate of exchange to be used.

**VALUATION OF IMPORTS**

ZRA reserves the right to revalue vehicles to determine the equitable transaction value in the country of supply under the following circumstances

1. If the importer or customs clearing agent provides insufficient information.
2. If the vehicle is acquired other than in the ordinary course of trade.

**DUTY RATES**

In order to arrive at the customs duty payable, Customs duty rate are applied on the VDP.

The rates applicable depend on the type of motor vehicle. Specifics duties for motor vehicles are provided in the Customs and Excise Amendment Act No.14 of 2017.

USED motor vehicles have been split into two categories namely:

1. Vehicles aged between 2 to 5 years
2. Vehicles above 5 years

The two categories have specific applicable duty rates.

NEW motor vehicles apply different rates of customs duty

**CLEARANCE PROCEDURE**

Customs clearance of motor vehicles is complete and granted after all requirements under the customs law have been fulfilled. This includes:

1. Presentation of genuine import documents
2. Revaluation by customs, if any
3. Payments of customs duty, VAT and processing fee
4. Processing of the declaration in form CE 20 by customs

**EXAMPLE**

Mr Chiimba imported a second hand Toyota light truck with gross weight of 16 tonnes from japan costing $1,500 in January 2020 for the transport of goods. The truck was manufactured in January 2014. The charge for insurance was $100 and freight up to the point of entry was $2000. The freight charge from point of entry to Mr Chiimbas premises was K1,950.

The Commissioner General advised that the exchange rate ruling at the time was K10.10 per $1

**Required:**

Determine the light truck:

1. The VDP for customs duty.
2. The amount of total import taxes paid on the importation.

**SOLUTION**

**Import taxes:**

1. Value for Duty Purposes (VDP) for customs duty:

 $

Cost 1,500

Insurance 100

Freight 2,000

CIF 3,600

VDP (for customs) = $3,600 $×$ K10.10

 = K36,360

1. Total import duties payable

Since the truck is more than 5 years old from the date of manufacture and has a gross weight of 16 tonnes, the total amount of import taxes payable will be determined as follows:

 Values Taxes

 K K

VDP 36,360

Customs duty (specific duty) 11,744 11,744

 48,104

Excise duty (specific duty) 9,004 9,004

 57,108

Value Added Tax @ 16% $×$ 57,108 9,137 9,137

Total value 66,245

Carbon surtax (coach over 5 year old) 2000

Total import taxes paid 31,885

**CLASS WORK**

The company imported a saloon car with a cylinder capacity of 1500 cc from overseas in January 2017, at a cost of $9,400. the company paid insurance charges of $1,300 and freight charges of $600 in transit to the port of Dar la Salam .the transportation and other costs from Nakonde boarder post to company’s premises amounted to $1,800. Motor car registration was K12, 000. The car was manufactured in 2016.

The exchange rate issued by commissioner General at that time was K9.20 per $1.

*However the exchange rate at the company’s bank when the company paid for the saloon car was K9.10 per $1.*

**Required:**

1. Compute the VDP of the car
2. Compute the total import taxes paid

**EXCISE DUTY**

Is a tax on particular goods or products whether imported or produced domestically, imposed at any stage of production or distribution, by reference to weight, strength or quantity of the goods or by reference to their value.

It’s administered by the domestic division taxes of ZRA.

Excise duty is levied on the following goods:

* Clear beer
* Opaque beer
* Pipe tobacco
* Hydrocarbon oils such as petrol, diesel, fuel oils etc
* Spirits and wines
* Airtime
* Cosmetics
* Plastic bags
* Carbonated drinks

**EXCISE DUTY RATES**

The rates range from 3% on electricity to 125 % on ethyl alcohol and spirits.

125 % is also applied to tobacco and wine.

15% is charged on services provided by mobile phone service providers.

**LICENSING**

One must apply to the commissioner general for a License, in order for any person to manufacture any of the goods set out in the excise tariff in quantities specified in the Customs and Excise Act.

However, any person may produce without a license and without payment of duty for domestic use but not for sale for profit, the following

1. Fermented Liquor (other than opaque) containing not more than 2% of alcohol by volume.
2. Tobacco in the form of cigars, cigarettes, pipe tobacco or sniff when made from manufactured tobacco duty was already charged or raw tobacco.
3. Opaque beer being not more than 23 decalitres in volume in any period of 4 consecutive days

**WHO APPLIES FOR THE LICENCE**

Any person manufacturing, distilling, mixing, brewing or packaging the following:

1. Any portable liquid (containing not more than 2% volume)
2. All types of spirits /wine
3. Opaque beer in containers exceeding 23 decalitres
4. Hydrocarbon oils and their by products
5. Electrical energy
6. Cosmetics

**ASSESSMENT OF EXCISE DUTY**

Excise duty is chargeable on the VDP for excise duty purposes. This is the VDP for customs duty plus customs duty payable, if any.

**PAYMENT OF EXCISE DUTY**

Returns should be submitted on or before the 15th day of the month and payments should be made within five days i.e by the 20th

**METHODS USED TO DETERMINE VDP**

1. **Transaction value**

Is based on the price actually paid including insurance, freight and other incidental costs to the extent that they are paid.

1. **Transaction value of identical goods**

Is based on the price of identical goods imported by another importer into Zambia from the same source

1. **Transaction value of similar goods**

Is based on the price of similar goods imported by another importer into Zambia from the same source

1. **Deductive value**

Is the price at which identical or similar goods are sold in their quantity in Zambia.

1. **Computed value**

Is priced based on cost of production, insurance, freight and other costs incurred in the delivery of the goods in Zambia.

**6. Residual basis of value (fall – back)**

Is the price arrived at by going through the above five methods flexibly.

**UNIT 15 – TAX PLANNING**

**15.1 Introduction**

This unit introduces you to Tax Planning.

**15.2 Learning Outcome**

After completing this unit you will be able to:

* Explain the nature and differences between tax avoidance and tax evasion.



**15.3 Time Frame:**

You will cover the following time;

* 2 hour 30 minutes’ study time
* 1 hours in class

**TAX PLANNING**

Can be defined as the **minimizing or deferring of tax liabilities** by utilizing various provisions of the law.

Government in many cases provides various deductions and exemptions which can be used to minimize or reduce a tax payer’s tax liability. Tax planning is often achieved by utilizing such exemptions and/or reliefs but it can also be achieved by structuring a transaction in a different way. Examples of this would be:

* Trading through a limited company rather than an unincorporated entity
* Gifting into trust rather than direct to an individual
* Leasing rather than buying an asset
* Running a business partnership with a family member rather than employing them

Tax planning ensures an individual uses their financial resources most efficiently by minimizing their tax liabilities while complying wholly with the law and applying the law in the way it was intended.

**TAX AVOIDANCE**

Can be defined as acting within the law, sometimes at the edge of legality, t**o minimize, eliminate or defer tax** that would otherwise be legally owned. It involves a taxpayer **taking advantage of loopholes** or weaknesses and mismatches in tax law to minimize or defer tax liabilities, thereby **obtaining a tax advantage that was not originally intended** by tax legislation.

Tax avoidance is legal and not an offence, but it defeats the intention or purpose of the law and therefore, to discourage its practice, the government may issue anti – avoidance tax legislation. Anti – avoidance legislation aims at sealing the loopholes in the tax legislation so as to prevent taxpayers from taking advantage of them, and thereby reducing their tax liabilities lawfully.

**TAX EVASION**

Is the use of **illegal** means to avoid or reduce tax liabilities. The aim of the taxpayer practicing tax evasion is to **defraud** the Government of the revenue

Such illegal means of reducing tax liabilities may include but are not limited to the following:

1. **Deliberate concealment of income**, including overstatement of tax credits or exemptions and suppression of profits. This results in the disclosure of income which is not the actual income earned by the taxpayer.
2. **Deliberate misrepresentation** of material fact, manipulation of accounts, disclosure of unreal expenses for deductions, showing personal expenditure as business expenses etc.
3. **Hiding** relevant documents
4. **Not maintaining complete records** of all the transactions.
5. **Not reporting taxes** such as value added tax, pay as you earn and withholding tax. These taxes are collected from others by the taxpayer and held in trust by the business, to be reported and paid to the Zambia revenue authority. Willfully using such taxes to fund a business instead of reporting the collection and paying the taxes when they are due is tax fraud.

The distinction between tax avoidance and tax evasion is not always that clear. For example, a tax avoidance scheme comprising a series of transactions solely designed to reduce the tax liability with no commercial gain to the taxpayer may be taken as illegal and therefore amount to tax evasion.

**THE CAUSES AND CONSEQUENCES OF TAX EVASION**

Tax evasion arises when taxes are perceived to be too high or unfair on taxpayers. However, it can also be just deliberate where the taxpayer intentionally hides some income. Tax evasion is an offence and may be punishable by fines and/or imprisonment.

The consequences of tax evasion include:

1. Loss of revenue for government: the Government sustains enormous revenue losses that directly affect its debt level and jeopardize its capacity to provide services and fund programmes that meet the needs of our ever – changing society.
2. Some people have to pay for others: people who comply with the law shoulder a heavier tax burden than they should because they must compensate for others who participate in the underground economy.
3. Tax compliant businesses face unfair competition: businesses that fulfill their tax obligations face unfair competition from those that do not.