MAY 2021 PROFESSIONAL EXAMINATION
PRINCIPLES OF TAXATION (PAPER 2.6)
CHIEF EXAMINER'S REPORT, QUESTIONS AND MARKING SCHEME

EXAMINER'S GENERAL COMMENTS

Though entirely satisfactory, the candidates' performance in this paper was not what was expected based on the standard of the questions. Approximately 23% of the candidates who wrote the paper passed. This was above the pass rates of approximately 20% recorded during November 2020. Tuition providers and students should have been conversant with the trend by now since, more often than not, the questions are normally spread across the syllabus. This is the fourth diet for the paper after the change of the syllabus, and it is still expected that candidates would have the opportunity to make amends by learning the rudiments of the paper.

Candidates are advised, to continuously read and pay more attention to the tax laws and principles. This is so because the Principles of Taxation is built on general knowledge of how the tax laws and principles work and, more significantly, how the law and principles are explained and applied. The principles of taxation paper describe the Ghanaian taxation system, outline the basic principles of taxation of individuals and corporations (entities), and outline key aspects of realisation of assets, VAT, and describe how the Ghana Revenue Authority administers taxes.

Therefore, candidates should desist from specialisation and exert their energies in learning across the broad spectrum of the syllabus since this will easily catapult them to success.

Another general observation made was the fact that there was much improvement in the computational questions. Most of the candidates performed excellently, probably because the instructions and requirements in the questions were straightforward.

STANDARD OF THE PAPER

The standard of the questions was excellent. All the questions did reflect the Principles of Taxation syllabus of which the candidates were expected to have a fair knowledge to pass. The questions fairly covered the entire syllabus, and the expectations were that an average student who wrote the paper should be in the position to pass.

PERFORMANCE OF CANDIDATES

Generally, the performance of the candidates was not *too satisfactory. The* expectations of the Examiner from the candidates were once again *not* met looking at the nature of the questions. Instructions were self-explanatory as to what the candidates were to do. Inadequate preparation and unwillingness of candidates to learn across the syllabus and appreciate the subject's principles continue to remain a bane to the performance of candidates. Any candidate who could not pass cannot blame anyone. Approximately 23% of the candidates passed the paper, and this is NOT good enough.

The reasons could be as follows:
Most of the candidates have still not understood the principles of taxation very well. Tuition providers perhaps are also not covering the syllabus and are also not giving exercises to solicit students as to whether they have grasped the basic principles.
Candidates who passed did well in the computational questions and balanced it with the theories. Candidates need to note that the excellent performance in this paper requires a basic understanding of the principles of taxation. Paper 2.6 of the Study Text of the Institute of Chartered Accountants (Ghana) is a recommended reference guide for the preparation for the examination.
There is evidence that not too many candidates have reasonable tuition. Besides, some of the candidates did not show any evidence of a good understanding of the basics. Taxation is a creature of legislation and must not be based on intuition and feelings but on what the tax laws say. Therefore, it is not advisable to primarily rely on self-tuition since this has not augured well for most candidates.
Those candidates who did not perform well do not understand the objection process as contained in the Revenue Administration Act 2016 (Act 915) as amended, the basic taxation principles on withholding tax as it relates to residential and not residential properties for resident persons and application of Value Added Tax to taxable and non-taxable activities. These areas of taxation continue to be examined, and it seems most of the candidates have little knowledge of these issues.

NOTABLE STRENGTHS & WEAKNESSES OF CANDIDATES
Some of the candidates had an excellent understanding of the syllabus and the subject. This was demonstrated in the answering of the questions. However, the coverage of the syllabus is still low. Candidates still learn only specific aspects of the syllabus. This was evident with some candidates scoring high marks in specific questions and abysmally low marks in other questions, especially those that bothered on the principles.

It is also clear that not too many candidates received very good tuition on the subject and therefore lost valuable marks that could have been grasped with ease. Both lecturers and candidates should pay attention to the law and the basic principles of taxation.
Some candidates proved that they understood the questions' requirements and prepared for the paper, scoring more than half for each question. They thus earned marks above 60%.

Once again, some candidates did not pay attention to the topics such as Fiscal Policy, National Pension Scheme, Partnership, Tax Administration, and Value-Added Taxation. If candidates had given more attention to these topics, the pass rate would have been more than 50% since the questions were pretty straightforward.

QUESTION ONE

a) The location of an entity is of importance in tax planning. How does location inure to the benefit of a young entrepreneur aged 35 years or younger in the manufacturing business?

(5 marks)

b) Public expenditure can be in the form public works and transfer payments. Public Works are expenditure on durable goods, primarily fixed structure that the government produces. They include expenditure on public works such as roads, schools, hospitals, irrigation etc. Transfer payments include interest on public debt, government wages and salaries, pension, insurance and social security benefits, etc.

Required:
Explain **FIVE (5)** goals of public expenditures. **(5 marks)**

c) The Commissioner-General assessed Judah in the 2020 year of assessment, and he is dissatisfied with the assessment. Judah intends to seek redress with the Commissioner-General. He has contacted you for professional advice on objection processes.

Required:
Explain the objection processes as contained in the Revenue Administration Act, 2016 (Act 915) as amended. (**10 marks)**

(Total: 20 marks)

QUESTION TWO

a) MMX Bank, a resident financial institution in Ghana, contracted Crown UK, a specialist in software maintenance. Per the contract, Crown UK is required to come to Ghana to provide the services every two years. The specialist will provide services to the bank's clients in the normal banking operation.

Required:
How will VAT, if any, be accounted for? **(4 marks)**

b) Kuundive Ltd produces fruits that have caught up with childrens' interest. Kuundive Ltd engages Yelawana Ltd to mainly do a distribution of its product and, in turn, receives a commission. Per the arrangement, Yelawana will put a margin on the price for the distribution.

Required:
What is the VAT arrangement between Kuundive and Yelawana? **(6 marks)**

c) A receiver of XX Bank intends to sell assets of the Bank. The receiver wants your guidance on the VAT implication on the sale of the bank's assets. **(5 marks)**

d) Explain the 3-Tier scheme under the National Pension Act**.** **(5 marks)**

(Total: 20 marks)

QUESTION THREE

Amna and Bean are brothers and equal partners in their partnership business, A&B General Wholesale Merchants Limited. The partnership is in its second year of trading and operates from an office premises owned by Amna. The cost of the Premises as at 1 January, 2019 was GH¢200,000. Bean provided all the office furniture and equipment used by the partnership, valued at GH¢80,000 as at 1 January, 2019.

Amna and Bean use their own personally acquired motor vehicles for the partnership business and charge the partnership for the business mileage incurred for fuel and maintenance. The cost of the two motor vehicles as at 1 January, 2019 was GH¢120,000.The partnership has employed three staff in addition to the partners.

The partnership's income statement for the year ended 31 December 2020 is detailed below:

	Notes	**GH¢**
Income		730,000
Less expenses:		
Distribution expenses	1	(160,000)
Administrative expenses	2	(290,000)
Other expenses	3	(30,000)
Profit for the year		**250,000**

Notes:

1. Distribution expenses comprise**:**

		GH¢
Motor vehicle running expenses		70,000
Third Party motor Insurance and licensing		40,000
Parking fines		6,000
Business mileage claim:	Amna	24,000
	Bean	20,000
		160 000

2. Administrative expenses comprise:

	GH¢
Staff salaries	160 000
Cleaning and sanitation	38,000
Income tax paid (arrears and penalty for 2018)	8,000
Electricity and Water	13,000
Depreciation	23,000
Payment for business operating permit	33,000
Printing and Stationery	15,000
	290,000

3. Other expenses comprise penalties for late filing of tax returns and payment of taxes.

Amna and Bean are both married. Amna has two children, both in accredited senior high schools in Ghana. Bean has one child who is currently attending university in the United Kingdom. Amna takes full care of her aged mother. Bean, who is currently undertaking a training course in Wholesaling Risks, is certified as handicapped in one of his legs through accident. Bean paid GH¢3,300 for the training course.

Required:

a) Explain the principles governing partnership taxation. **(2 marks)**

b) Calculate the joint partnership taxable income for the year ended 31 December, 2020. You are required to include capital allowance where necessary. **(12 marks)**

c) Calculate the taxable income of Amna and Bean for the year ended 31 December, 2020. **(4 marks)**

d) What are the taxation rules on payment to causal and temporary staff? **(2 marks)**

(Total: 20 marks)

QUESTION FOUR

a) The following details were taken from the records of KK Company Limited for the 2020 year of assessment.

	GH¢
Profit before tax	132,000

The following were included in arriving at the net profit before tax:

	GH¢
Total Financial Gain from derivatives	42,000
Total Financial Cost from derivatives	300,000

Required:

i) State what constitutes financial cost from derivatives? **(3 marks)**

ii) Explain the tax treatment of financial cost from derivatives under a company such as KK Company Limited that is neither a mining or petroleum company. **(2 marks)**

iii) Compute and explain the allowable financial cost from derivatives. **(3 marks)**

iv) Assume all facts are the same except that Financial gain from derivative is GH¢60,000 and Financial Cost from derivative is GH¢30,000. Compute and explain the allowable financial cost from derivative. **(4 marks)**

b) Fridays Ltd is a resident company. It provides cleaning services across the country. The following is available from its tax returns for the 2020 year of assessment.

	GH¢	GH¢
Revenue		920,000
Cost of Sales		(680,000)
Gross profit		240,000
Add other income:		
Rental income (Gross)	120,000	
Dividend (Gross)	20,000	
Gross interest from treasury bills	41,000	181,000
		421000
Less operating expense		(205,900)
Net Profit		**215,100**

The following additional information has been adjusted to the operating expenses above.

	GH¢
Depreciation	10,000
Penalty	2,000
Fines	500
Refreshment	1,500
Taxes paid	16,500

Other relevant information is as follows:
The dividend was received from Z Ltd, a resident company where Fridays Ltd has 27% shares.

Required:

i) Compute the tax payable assuming its tax rate is 25% **(6 marks)**

ii) Explain the treatment of the following:
Rental Income **(1 marks)**
Dividend **(1 marks)**

(Total: 20 marks)

QUESTION FIVE

a) A resident person who makes a payment to another resident person in respect of the rental of residential or non-residential premises is required to withhold tax in accordance with Income Tax Act, 2015 (Act 896) as amended.

Required:

i) State the taxation principle applicable to rental income and the relevant rates. **(5 marks)**

ii) Given i) above, how will you treat this transaction, where a resident person makes a payment to another resident person conducting a business of sale or renting of residential or non-residential premises. **(5 marks)**

b) On the death or as part of a divorce settlement or bona fide separation agreement, an individual may transfer an asset to a spouse or former spouse. What are the taxation rules on this arrangement? **(5 marks)**

c) Madam Gifty Kums was appointed a Minister of State in 2018. On the occasion of her vetting by parliament, she received the following gifts:

- Cash donation amounting to GH¢80,000 from her party foot soldiers within her constituency
- A Toyota Land Cruiser worth GH¢1,000,000 from the Chief of her village
- Cash of US$ 20,000 from the mother- in-law in Afghanistan. (GH¢1=$5)

Required:
Compute the gift tax payable by Madam Gifty Kums **(5 marks)**

(Total: 20 marks)

SOLUTION TO QUESTIONS

QUESTION ONE

a) One of the variable of tax planning is location. Young entrepreneur aged 35 years or younger that takes advantage of location is sure to reduce their tax liability for the next five years

Accra and Tema	15%
Regional Capitals outside the northern regions	12.5%
Any area outside the Northern Regions	10%
Northern Regions	5%

(2.5 marks)

The following businesses: Manufacturing, farming, agro-processing, ICT, Tourism and creative arts, horticulture and medicinal plant, energy and waste processing.

(2.5 marks)

Alternatively, a candidate may write on the following:

Young entrepreneur that engages in farming, agro-processing, cocoa by product business has locational incentives for the next five years **(2.5 marks)**

Accra and Tema	20%
Regional Capitals outside the northern savanna ecological zone	15%
Any area outside the Northern savanna ecological zone	10%
Northern savanna ecological zone	5%

(2.5 marks)

b)

- During a period of Depression. Deficit financing assumes greater importance when there is the need to recover after a major depression or to reduce the severity of the business cycle. This happens when there is the realisation that private sector activities and traditional monetary policies prove inadequate in restoring economic stability. When economic activities are declining, or stagnant deficit financing may replace deficiency in aggregate demand by injecting funds and providing the necessary stimulant for reducing under-utilisation of resources and increase the deployment of labour and capital through additional spending to finance the budget deficit.
- During Wars: Governments try to raise additional resources to finance tribal conflicts during tribal wars. This may, however, have adverse effects on inflation etc.
- During a Process of Economic Development: Usually, in developing countries, deficit financing is applied to cater for the meagre voluntary investment to progress rapid development to do away with the vicious circle of poverty (low savings, low investment, low income, etc).

- Ineffective Financial Management: since budgetary projects in developing countries are unreliable, and management also tends to be ineffective, leading to demand for loans, grants, and aid to finance ineffective programmes.
- Weak Expenditure Control and Monitoring: The annual accounts are usually in arrears in such a way that year by year comparison is difficult. Besides the unpredictable economic and social environment, the government may incur expenditure outside the budget, necessitating the inflow of budget expenditure over expected revenue.
- Low Revenue Mobilization: The revenue or tax net does not encapsulate all taxable enterprises and individuals. Therefore, revenue from taxes tends to be less than what is needed for payments of goods and services and other government current financial obligations.
- Political Pressure: Politicians make electioneering promises which have not been budgeted for. When political pressure becomes unbearable, there are attempts to implement policies (not budgeted for) to earn political integrity. These create an extra burden needing extra funds to finance outside the budget.
- Infrastructural Development
- To keep government workers productive by paying them
- Enhance economic livelihood through LEAP
- Provide social goals
  The theory of social goods is of prime importance to the economies of the public sector. Some economists divide social goods under two heads: Social and economic overheads. Social overheads like hospitals, schools and colleges and technical institutions, economic overheads like roads and railways, irrigation and power projects etc., are all essential for economic development. Public expenditure is responsible for building up sound social and economic overheads as money for these things does not usually come from private sources.
- Increase Production
  Public expenditure contributes to production through a large number of public enterprises both in industries and agriculture. Government incurs a lot of expenditure in the agricultural sector, e.g. on irrigation and power, seed forms, fertiliser factories, warehouses, feeder roads etc., and in the industrial sector by setting up public enterprises like steel plants, heavy electrical, heavy engineering, machine-making factories, etc. All these enterprises are calculated to promote production and, thereby, economic development.
- Promote Price Stability
  An increase in public expenditure relieves the economy from the quagmire of depression. Conversely, public expenditure can be scaled down when there is a fear of an inflationary rise in prices. Thus, public expenditure helps in stabilising prices, especially where the economy is depressed.
- Create employment
  Public expenditure is the most potent weapon to fight unemployment. The level of employment depends upon aggregate demand. The government can influence effective either by making more public expenditure or by resorting to such fiscal methods to raise the level of private expenditure. Thus as the government spends to

revitalise the economy from a depressed state, it tends to create employment opportunities resulting from the multiplier effect of government expenditure.

- Promote Balanced Growth
  There is a tendency to use economic resources for the further development of already developed regions. However, special attention needs to be paid to developing backward areas and underdeveloped regions for overall growth. This requires enormous amounts for which reliance has to be placed on public expenditure.
- Reduce Inequality of Income
  Another objective of public expenditure is to reduce the inequality of income. Expenditure on old age pensions, unemployment relief, free education, free midday meals etc., benefits the poorer classes of the community at the expense of the rich. The above objectives reveal that public expenditure properly made of utmost importance for social welfare and economic prosperity.
- Exploitation and Development of Mineral Resources
  Minerals provide a base for further economic development. The government has to undertake schemes of exploitation and development of essential minerals, e.g. coal and oil. Thus public expenditure has to play its role here too.

(Any 5 points for 5 marks)

c)

- A person who is dissatisfied with a tax decision that directly affects that person may object to the decision with the Commissioner-General within thirty days of being notified of the tax decision.
- An objection to a tax decision shall be in writing and state precisely the grounds upon which the objection is made.
- Before the expiration of the thirty days, a person may apply in writing to the Commissioner-General for an extension of time to file an objection.
- Where the Commissioner-General is satisfied that there are reasonable grounds for the extension, the Commissioner-General may grant the application for extension and shall serve notice of the decision on the applicant. (sick, not in the country or other reasonable grounds).
- An objection will be entertained only when all the import duties have been paid in the case of importation or 30% of the tax due has been paid in the case of other taxes.
- The Commissioner-General may waive, vary or suspend the payment of this amount pending the determination of the objection.
- The Commissioner-General must within 60 days serve the taxpayer with his decision on the objection.
- Where the Commissioner-General does not serve the person with notice of the decision within sixty days, the person may, by notice in writing to the Commissioner-General, elect to treat the Commissioner-General as having decided to disallow the objection.
- A decision is made regarding an objection on the date the person is served with notice of the decision. If a person makes an election, thirty days from the date the person files the election with the Commissioner-General. Act 2020, Act 1029 amended section 44 of the Revenue Administration Act 2016, Act 915 as follows:

- Suppose the person is still not satisfied with the Commissioner-General's decision. In that case, the person may within thirty days, appeal against the decision to the Independent Tax Appeals Board also known as the Appeals Board.
- Therefore, Judah should not seek redress at the High Court but rather raise an objection to the assessment by writing to the Commissioner-General and later appeal to the Independent Appeals Board if still not satisfied with the outcome of the objection decision.
- A person who is dissatisfied with the decision of the Appeals Board may appeal against the decision to the Court within thirty days from the date the decision was served on the person.

(1 mark each was awarded for any 10 points = 10 marks)

(Total: 20 marks)

EXAMINER'S COMMENT

Question 1a) was not well answered by candidates. Surprisingly, most candidates were not conversant with the location tax incentives that will inure to the benefits of the young entrepreneur aged 35 years or younger in the manufacturing business. They rather spent their energies and time discussing location tax incentives for manufacturing businesses in general. They thus lost valuable marks, mostly zero out of five.

Question 1b) was straightforward and was well handled by the majority of the candidates. The performance was excellent.

Candidates performance in 1c) was mixed. Surprisingly, some candidates were ignorant of the provisions in section 44-47 of the Revenue Administration Act of 2016, Act 915, as amended. The majority did not know that if a person is still not satisfied with the Commissioner-General's decision, the person can now appeal to the Independent Appeals Board. On the whole, it was just an average performance with a sizeable number of candidates losing valuable marks.

QUESTION TWO

a) VAT is charged on consumption. Given that the services will be provided in Ghana, VAT will be charged. This is a case of imported services Section 65 of Act 870 (Act 2013) as amended indicates that if the services are going to be used on activity which are taxable, no VAT will be charged. On the other hand, if it is going to be used on exempt, VAT will be charged. This is, however, the case of reverse charge. **(4 marks**)

b) Under section 32 of the VAT Act 870 Act 2013, a supply of goods or services made by a person as an agent for another person who is a principal is a supply by the Principal. To the extent that it will not be supply of services of an agent to the Principal.
Given that that Yelawana ltd will add a margin to the price makes Yelawana ltd an agent for the Principal and also to earn commission. There is no VAT between the

Principal and the Agent since Yelawana ltd will earn a commission. The additional margin is agreed with the Principal. The agent will invoice the commission vat inclusive and account for the whole amount but will charge VAT to the consumer on behalf of the Principal **(6 marks)**

c) Under section 25 of the VAT Act 870, where a taxable person supplies goods or services and a deduction for input tax paid on the acquisition of the goods or services was denied, the supply of the goods or services by the taxable person is a supply of goods or services other than in the course or furtherance of a taxable activity.
The question to address here is if the input tax was not denied, then the VAT is charged, but if there was a denial, the input tax must not be charged.
In conclusion, without any information to the contrary, the VAT should be charged.
(5 marks)

d) **3-Tier Pension Scheme**

- **The First Tier** is the Basic National Social Security Scheme for all workers in Ghana. It is a defined benefit scheme and mandatory for workers to have 13.5% contributions made on their behalf. The contribution is managed by SSNIT.
- **The Second Tier** is a defined contributory Occupational Pension Scheme mandatory for workers with 5% contribution made on behalf of members. The contribution is managed privately by approved Trustees.
- **The Third Tier** which includes all Provident Funds and all other Pension Funds outside Tiers I and II is a voluntary scheme.
- Under the first two tiers, the employee is required to contribute 5.5% while the employer contributes 13%. Of the total contribution of 18.5%, 13.5% is contributed to the first tier and 5% to the second-tier schemes. These contributions are deductible for tax purposes and are tax free for both the employer and the employee.
- Under the third tier, there are no restrictions on the contributions made to the fund. However, contributions made by an employer and employee of up to 16.5% are exempt from tax on both the employer and the employee to the extent of their respective contributions to an approved fund manager. All contributions in excess of 16.5% are taxable on the employee or employer or both.
- Expatriates, unless exempt, are required to contribute to the mandatory social security schemes. However, expatriate employees of contractors and sub-contractors (of the upstream petroleum industry) are not required to participate in any insurance, compensation, or other employee or social benefit programmes established in Ghana.

(5 marks)

(Total: 20 marks)

EXAMINER'S COMMENT

Question 2a) looked quite technical for the candidates. Only few candidates could recognise that the question relates to VAT on imported service, in which case it is the recipient of the service, that is MMX Bank but not Crown UK, that is supposed to account for the VAT. Besides, candidates could not identify that the question also relates to the case of reverse charge where if the services are going to be used on activity which is taxable by the bank, no VAT will be charged on those activities and if it is going to be used on exempt supply, VAT will instead be charged.

For question 2b) candidates could not identify that if an agent acts on behalf of the Principal, VAT will be deemed to have been charged by the Principal and not the agent. There is no VAT between the Principal and the Agent since Yelawana Ltd (Agent) will earn commission for the services rendered on behalf of the Principal. The agent will only have to invoice the commission VAT inclusive and account for the whole amount but will charge VAT to the consumer on behalf of the Principal. It was a below-average performance.

Candidates struggled to apply the VAT laws to practical situations and performed poorly in questions on VAT. Both tuition providers and students are advised to revise VAT well since it contributed to the poor performance of candidates.
It was also quite surprising that most candidates could still not explain the 3-Tier scheme under the National Pension Act even though the question keeps repeating itself with the introduction of the new syllabus in November 2019. It is mind-boggling why some students still take the 3-Tier Pension Scheme to mean Tier 3. Once again, students will be advised to abreast themselves with past questions and suggested solutions in their preparations.

QUESTION THREE

a) Partnership income is taxed in the hands of the individual partners in accordance with their profit-sharing ratios. Therefore, the partnership is not a taxable person.
A partnership is not liable to pay income tax with respect to its chargeable income and is not entitled to any tax credit with respect to that income, but is liable to pay income tax with respect to find withholding payments.

Each partner is required to report his or her share of the partnership's taxable profit or loss in his or her individual tax return and pay income tax on this. Apart from the profit share, all other incomes received by the partner would have to be taken into account to determine the chargeable income. Each partner will claim his/her reliefs.
(2 marks for any two relevant principles)

Amna and Bean

b) **Computation of Capital Allowance for Relevant Years**

Year of assessment 2019	**Class 2**	**Class 3**	**Class 4**	**Total**
	GH¢	**GH¢**	**GH¢**	**GH¢**
Cost / Depreciation Basis	120,000	80,000	200,000	400,000
Capital allowance	36,000	16,000	20,000	72,000
Depreciation Basis (2020)	84,000	64,000	180,000	328,000
Capital Allowance	**25,200**	**12,800**	**20,000**	**58,000**
	58,800	51,200	160,000	270,000

(14 ticks @ 0.5 each = 7 marks)

Amna and Bean
Computation of Joint Partnership Income for 2020 Y/A
01/01/2020 - 31/12/2020

	GH¢
Net profit per accounts	250,000
Parking fines	6,000
Income tax paid (arrears and penalty for 2018)	8,000
Depreciation	23,000
Late filing of tax returns	30,000
Mileage claim Amna	24,000
Bean	20,000
Capital Allowance	(58,000)
	303,000

(10 ticks @ 0.5 each = 5 marks)

c) **Computation of Taxable income of partners for 2020 Y/A**
01/01/2020 -31/12/2020

	Amna GH¢	Bean GH¢
Share of profits	151,500	151,500
Mileage claim	24,000	20,000
	175,500	**171,500**
Less reliefs:		
Marriage Responsibility	(1,200)	(1,200)
Child Education	(1,200)	-
Aged dependence	(1,000)	-
Self-education	-	(2,000)
Disability allowance (25% x 171,500)	-	(48,875)
Chargeable income	**172,100**	**119 ,425**

(12 ticks @ 0.333 = 4 marks)

d) **Payment to Casual Workers**

Where a person makes payment to a casual worker, that payments shall be treated as income earned by that casual worker, and the person shall withhold tax from the gross income paid to the casual worker at the rate of **five percent (5%).** Tax **withheld shall be treated as final tax.**

A casual worker means a worker engaged in seasonal or intermittent work and not for a continuous period of more than six months and whose remuneration is calculated on a daily basis.

(1 mark)

Payment to a Temporary Worker

Where a person makes payment to a temporary worker, that payment shall be treated as income earned by the temporary worker, and the person shall withhold tax from that income in accordance with the **graduated rates for individuals.**

A temporary worker means a worker employed for a continuous period of not less than one month and is not a permanent worker or employed for a seasonal work in character. **(1 mark)**

(Total: 20 marks)

EXAMINER'S COMMENT

Question three tested candidates understanding of Taxation of Partnerships. It mainly was computational interspersed with simple capital allowance computation, computation of both partnership and individual partners' taxable income. This is the usual attributes of taxation of partnership questions. Candidates were only to explain the principles governing partnership taxation for 2 marks and identify the taxation rules on payment to casual and temporary staff also for 2 marks.

The details given to the candidates were very clear and any average candidates should be in the position to provide good answers to the questions. The marks were fairly allocated to the questions.

The partnership question perhaps was the best answered question simply because it was pretty straightforward. The computation of the capital allowance was well done since the depreciable assets were few and not diverse. However, some candidates have still not been able to clearly appreciate how to compute the taxable income of the partnership firm from that of the individual partners**.** Question three was very well answered by the majority of the candidates.

QUESTION FOUR

a)

i) The financial cost here is interest or losses with respect to a ***financial instrument***, and it is tax-deductible up to the limit defined by Act 896 as amended.

The term financial instrument means:

A debt claims or debt obligation. Debt claim means a right to receive a payment under a debt obligation. Debt obligation means an obligation to make a payment to another person denominated in money. Debt obligations includes accounts payable and the obligations arising under debentures, shares, treasury bills, promissory notes, bills of exchange and bonds.

A derivative instrument. A derivative instrument is a financial instrument or other contract with all three of the following characteristics:

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying')

- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and
- It is settled at a future date.

  A foreign currency instrument; and

  Any other instrument prescribed by regulations or, in the absence of regulations, treated as a financial instrument by generally accepted accounting principles.

(3 marks for a good explanation)

ii) The amount of financial costs should not exceed the total of:
Financial gains derived by the person that is to be included in calculating the person's income from the business or investment for the year of assessment; and
Fifty percent of the chargeable income of the person for the year from the business or investment calculated without:

- Including a financial gain derived by the person; or
- Deducting a financial cost incurred by the person.

Financial costs for which a deduction is denied as a result of the above rules may be carried forward and treated as incurred during any of the following five years of assessment. Carryforwards are used in the order in which they are incurred.

(2 marks)

iii)

	GH¢
Net profit before tax	132,000
Add Financial Cost	300,000
Less Financial Gain	(42,000)
CI after adjusting for financial cost & gain	390,000

Allowable Financial Cost	**GH¢**
Financial gain	42,000
Add 50% x GH¢390,000	195,000
Allowable financial cost	237,000

(8 ticks @ 0.25 = 2 marks)

The allowable financial cost is GH¢237,000. However, the total financial cost was GH¢300,000. Therefore, only 300,000 – 237,000 = GH¢63,000 would not be allowed and may be carried forward for the next five years.

(1 mark for the explanation)

(Total: 3 marks)

iv)

	GH¢
Net profit before tax	132,000
Add Financial Cost	30,000
Less Financial Gain	(60,000)
CI after adjusting for financial cost & gain	102,000

Allowable Financial Cost	**GH¢**
Financial gain	60,000
Add 50% x GH¢102,000	51,000
Allowable financial cost	111,000

(6 ticks @ 0.5 = 3 marks)

The allowable financial cost is GH¢111,000. The total financial cost was GH¢30,000. This means all the GH¢30,000 would be allowed as financial cost for the assessment year. **(1 mark for the explanation)**

(Total: 4 marks)

b)

i) **FRIDAYS LTD**
COMPUTATION OF TAX PAYABLE
Y/A 2020

BASIS PERIOD JANUARY 1-DECEMBER 31, 2020		**GH¢**
Net Profit	**GH¢**	215,100
Deduct the following:		
Rental Income	120,000	
Dividend	20,000	
Gross Interest (T bills)	41,000	
		181,000
Adjusted Profit		34,100
Add Back Non-allowable Deduction		
Depreciation	10,000	
Penalty	2,000	
Fines	500	
Refreshment	1,500	
Taxes Paid	16,500	
		30,500
Chargeable Income		64,600
Add Interest on T. bills		41,000
Total Chargeable Income		105,600
Tax Charged @25%		26,400
Less WHT @ 8% (8% *41,000)		3,280
Tax Payable		**23,120**

(15 ticks @ 0.4 = 6 marks)

ii) **Rental income** is treated as final withholding tax if it is considered as investment income. Residential is 8% final while commercial is taxed @ 15%. In the case of Real Estate, it is 7.5% not final. **(1 mark)**

Dividend income paid by a resident entity to another resident entity is exempt from tax where the recipient holds a minimum of 25% voting rights of the paying entity. **(1 mark)**

(Total: 20 marks)

EXAMINER'S COMMENT

Question four examined the tax treatment of financial cost as it applies to businesses other than mining and upstream petroleum companies. It was, therefore, relevant to the paper. In fact, the topic was one of the modifications in the Income Tax Act 2015, Act 896 as amended and it was to be expected at any time. Twelve marks in all were awarded to both the tax treatment and related computational issues on financial cost. Few candidates who did not revise the topic completely lost out. More than half of the candidates provided excellent answers, especially the tax treatment of financial cost and thus earned above the average mark.

The candidates performance in question 4a) was above average. Most candidates, however, could not state what constitutes financial cost from derivatives. It is instructive for tutors and facilitators to explain this better to students. Besides, the question was clear that the company such as KK Company Limited is neither a mining nor petroleum company, yet some few candidates explained the tax implication of financial cost related to mining and petroleum companies.

Question 4 b of the question related to the usual examination of accounts, a topical issue in the principle of taxation paper. Candidates are expected to have a fair idea of all the principles governing the computation of taxation of business profit. The question on business profit was well done and earned candidates' valuable marks.

QUESTION FIVE

a)

i) A resident person who makes a payment to another resident person in respect of the rental of residential or non-residential premises shall withhold tax as an investment return, and the tax to be withheld is **8% and 15% for residential premises and non-residential (commercial) premises respectively and shall be treated as a final withholding tax.** **(5 marks)**

ii) Where a resident person makes payment to another resident person conducting a business of the sale or letting of residential or non-residential premises, the payment shall be treated as a payment for the supply of services and not as a payment on investment return, and tax shall be **withheld at 7.5% and shall be treated non-final withholding tax.** The amount withheld shall be treated as tax withheld on the account and not as a final withholding tax. (**5 marks)**

b) Where on the death or as part of a divorce settlement or bona fide separation agreement, an individual transfer an asset to a spouse or former spouse:

- That individual is treated as having derived an amount in respect of the realisation equal to the **net cost of the asset immediately before the realisation; and**
- **The spouse or former spouse is treated as incurring an expenditure of the amount equal to the net cost of the asset in acquiring the asset.**

The effect of the above is that there will be no gain or profit on the realisation or disposal of the assets. Therefore, the net cost for an asset at a particular time is:

- In the case of a depreciable asset, the share of the written down value of the pool to which it belongs at that time apportioned according to the market value of all the assets in the pool; and
- In the case of any other asset, the amount by which cumulative costs for the asset exceed cumulative consideration received for the asset to the time.

(5 marks)

c) Computation of gift tax for Madam Gifty Kums for 2018 year of assessment.

	GH¢
Cash donation	80,000
Toyota Land Cruiser	1,000,000
Cash ($ 20,000/5)	4,000
	1,084,000
Gift tax @15%	**162, 600**

(5 ticks @ 1 mark = 5 marks)

(Total: 20 marks)

EXAMINER'S COMMENT

Question five was made up of three parts: withholding taxes as it applies to rental income pertaining to investment returns and to resident persons whose businesses are into a sale and letting of residential and non-residential properties; capital gains, specifically taxation rules on the death or as part of a divorce settlement or bona fide separation agreement of an individual upon the transfer of an asset to a spouse or former spouse and Gift Tax in line with syllabus grid.

Questions on withholding tax continue to pose problems to candidates at this level. The marks awarded to the question should have boosted the students' performance, but shockingly, most candidates could not identify that withholding tax rates for rent is a final tax. Besides, they could not identify that the withholding tax rate on residential premises is 8% whilst that of non-residential premises is 15%. They spent precious time discussing the rates for non-resident even though the question stated the taxable person as a resident person.

Question 5b) was woefully answered. Candidates were not familiar with the fact that where a resident person makes payment to another resident person conducting a business of sale or letting of residential or non-residential premises, the payment shall be treated as a payment for the supply of services and not as a payment on investment returns and for that matter tax shall be withheld at 7.5% on the account and not a final withholding tax. In addition, candidates could not identify that the resident person would have to account for the corporate tax using the company tax rate, and withholding tax on the account could offset the corporate tax liability for the year of assessment.

The c) part of this question was very poorly answered. Only a few candidates were able to identify the taxation rules. Facilitators and students are advised to spend time on the topic "gain on assets and liabilities" so as to improve student performance.

The candidates' performance in 5d) was excellent. The question was simple with no tricks and ambiguity. Very few students could, however not identify that where a gift does not arise as a result of employment, business or investment, the total taxable gifts received by the individual was to be taxed at a flat rate of 15% and the GH¢50 exemption for the year of assessment is not enshrined in the Income Tax Act of 2015, Act 896 as amended.

Candidates have still not taken much interest in the capital gain tax and withholding taxes even though questions under these topics keep recurring. Tuition providers and students are advised to pay attention to every aspect of the syllabus. The gift tax question was excellently done because there were no complications.