

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

TAXATION – PAPER 13

CPA(U) EXAMINATIONS

JUNE 2001

INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours**.
2. Attempt question **one** in Section **A**. It is compulsory and carries 40 marks.
3. Section B has **three** questions and only **two** questions are to be attempted. Each question carries 15 marks.
4. Section C has **three** questions and only **two** questions are to be attempted. Each question carries 15 marks.
5. Please read further instructions on the answer book

SECTION A

Question 1

Agape International Limited is a company that was incorporated in 1998 and has its accounting date as 30 June. The company has the following results for the year ended 30 June 2000.

	Shs '000	Shs '000
Sales		563,000
Factory Cost of sales		<u>267,000</u>
Gross Profit		296,000
Expenses		
General Administration	67,000	
Marketing	48,000	
Distribution	26,000	
Financial	<u>42,000</u>	<u>183,000</u>
		113,000
Other Income		<u>24,000</u>
Profit before Tax		137,000
Corporation Tax		<u>35,000</u>
Profit after Tax		<u>102,000</u>

Additional Information:

	Shs '000
Factory Cost of Sales includes:	
Depreciation	27,000
Partitioning of the office area	6,000
Repairs to premises	2,000
General expenses includes:	
Legal costs of share issue	12,000
Legal costs of tax appeal	300
Stamp duty	2,200
Fines on employees' motor offences	500
Marketing expenses include:	
Sponsorship costs	2,200
Loan to employee written off	500
Increase in general provisions	10,000
Increase in specific provisions	2,000
Advertising on TV	12,800
Promotion	2,800

Financial Expenses include:	Bank interest	2,100
	Bank Charges	400
	Donation to political party	500
	Subscription to UMA	2,500
	Redundancy Payment	21,000
Non-sales Revenue comprises	Profit on sale of fixed assets	600
	Bad debts provisions recovered	1000
	Agency Commission	20,000
	Unrealised exchange surplus on currency dealings	2,400
Capital allowances for the year have already been computed as Shs 109,000,000.		

Required:

- a) Compute the adjusted profit for corporation tax purposes.
(10 Marks)
- (b) Agape International Limited was gazetted in 1999 to account for their chargeable income on the self-assessment system
- Briefly describe your understanding of the self-assessment system.
(5 Marks)
- (c) What are the advantages and disadvantages of the self-assessment system both to the taxpayer, and to the Uganda Revenue Authority?
(5 Marks)
- (d) Agape International Limited is engaged in Research work and has employed one of the company's ex-employees as a Consultant and would like the Consultant to pay his own tax. However, the Consultant would like to know the most tax effective way of structuring this. He would like your advice with particular mention to the following:
- (i) The difference between employment and self-employment.
(5 Marks)
- (ii) The possible criteria which the Commissioner of the Uganda Revenue Authority will be looking at in order to satisfy himself that the Consultant is self employed and therefore responsible for paying his own tax.
(5 Marks)

- (iii) If the Consultant was deemed to be an employee of the company, what are the obligations of the company in respect to the taxation of the employee.

(5 Marks)

- (iv) If the Consultant was deemed to be self-employed, briefly explain how he would be taxed and his obligations with respect of filing his tax returns.

(5 Marks)

(Total 40 Marks)

SECTION B

Question 2

Ms Namutebi, a friend of yours is pursuing a Tourism degree course at the University and she will be qualifying within three months' time. She recently applied to a Tours and Travel Company in Kampala for a job. She was interviewed last month and two weeks later; she received the following letter from Mt Gorilla Tours and Travel Company.

Dear Ms Namutebi

Following the interview with us, we are pleased to offer you a position within our firm at a salary of Shs 26,000,000 per annum. You will be required to contribute 5% of your salary to the National Social Security Fund, the firm contributing a further 10% on your behalf.

The firm provides lunch free of charge at the firm's canteen.

You will have the sole use of a Toyota Camry acquired new on 1 January 1998 at a cost of Shs 14,000,000 for the Assistant Manager. While on official business, you will be paid a mileage allowance of Shs 2,000 per kilometre.

For the first two years of your employment, you may live rent-free in a flat owned by the firm. The estimated market rent for those flats is Shs 4,800,000 per annum. The firm also pays for the electricity and water to the extent of Shs 3,000,000 per annum. However, if you prefer, the firm could pay you Shs 6,000,000 per annum as a housing allowance and rent your own accommodation.

You will be expected to pay your own professional body subscriptions of Shs 750,000 per annum. The firm however will pay for your evening

course fees of Shs 3,500,000 and examination fees of Shs 850,000 for your final examinations.

During the month of August and September, you will be required to spend four weeks in the various parts of the country surveying a number of holiday resorts. Your travel costs are estimated to be Shs 300,000 with your weekly hotel bills of Shs 595,000 per week.

At the end of two years, we would offer you a loan, not exceeding Shs 55,000,000 at a low interest rate, to assist in purchasing a property.

We look forward to hearing from you.

Required:

Ms Namutebi has come to you requesting you to explain to her concisely the taxation position of each part of the above employment package and in particular the following benefits

- (a) Housing (3 Marks)
 - (b) Low interest loan (3 Marks)
 - (c) Reimbursement of expenditure incurred on business entertainment (3 Marks)
 - (d) Electricity and Water Bills (3 Marks)
 - (e) Sole use of the company's car (3 Marks)
- (Total 15 Marks)**

Question 3

The following are copies from the records of **Similar Substitutes Enterprises**, a business owned by Sarah Serwanga.

	Exc. VAT	March 2001	April 2001
		Shs	Shs
1.1	Cash Sales and Credits Sales	38,500,000	46,700,000
1.2	Zero Rated supplies (Credit Sales)	8,500,000	3,250,000
1.3	Credit Purchases	33,000,000	41,800,000
1.4	Zero rated supplies (Cash purchases)	5,000,000	Nil

Notes

- (i) Sarah sold goods for Shs 9,900,000 (tax inclusive) on 1 Sept 1998. The output tax in respect of the supply was paid to the Uganda Revenue Authority. On 3 March 2001, an amount of Shs 6,050,000 in respect of the above mentioned supply was written off as a bad debt, by Sarah.
- (ii) On 30 April 2001, Sarah bought goods for an office function. The value of the goods paid was Shs 825,000 and is included in 1.3 above.
- (iii) Mr. A, an employee of Sarah was compelled to spend 5 days away in Masaka in March 2001 as a result of his duties. The full account below was paid by the taxable person:

Accommodation	Shs 200,000
Meals	Shs 100,000
Transport charges	Shs 50,000
Subsistence Allowance	<u>Shs 250,000</u>
Total	<u>Shs 600,000</u>

Values include VAT at 17% where applicable.

- (iv) An amount in respect of Shs 115,000 of input tax was denied, because the requirement of keeping tax invoices was not complied with. However on 20 April 2001, Sarah obtained a tax invoice for the relevant supply.
- (v) There was an omission to deduct an amount of Shs 150,000 of input tax for the tax period of February 2001 from output tax. Sarah was however entitled to deduct the amount in the next tax period.

Required

- a) Calculate the amount of tax payable/refundable in respect of the two tax periods. Explain the calculation with your *comments*.
(7 Marks)
 - b) Not all input tax paid can be offset against output tax. Give three examples of cases where this may apply.
(3 Marks)
 - c) What requirements must be complied with prior to the deduction of input tax in respect of a taxable supply?
(5 Marks)
- (Total 15 Marks)**

Question 4

Andrew Okot is a self-employed Management Consultant.

On 1 November 1998, he registered for VAT as an Investment trader and his accounting date is 31 December.

He has made the following additions to Fixed Assets:

Date	Item	Gross Cost	VAT	Net Cost
		'000	'000	'000
22 Nov. 1998	Office equipment & furniture	6,450	937	5,513
28 Feb 1999	Toyota Carina	8,250	1,199	7,051
15 June 1999	Photocopier and Equipment	2,180	317	1,863
31 Dec 1999	Toyota Starlet	6,500	944	5,556
01 June 2000	Office Fixtures	290	42	248
31 July 2000	Word Processor	2,185	317	1,868
01 Aug. 2000	BMW Car	13,500	1,962	11,538

The Toyota Carina was sold on 1 August 2000 for Shs. 4,790,000. The photocopier and office equipment were of poor quality and were scrapped in August for no consideration.

Required

- (a) Calculate the capital allowances due for all the years of assessment.
(10 Marks)
- (b) Andrew moved into his offices and started to trade on 1 January 1999. In the same year, he was joined by Moses Njoroge, a former colleague, with whom he studied in Kenya and they formed a partnership during the month of March 1999. The partnership agreed to reimburse Moses all of his removal expenses from Kenya. It was also agreed that the partnership would pay commercial rent to Andrew for use of his building office premises.

Required:

Comment on the deductibility of the payments to Andrew and Moses in the partnership books for tax purposes.

(3 Marks)

- (c) Would your answer under (b) with respect to Moses be different if Moses was an employee rather than a partner? Comment.

(2 Marks)

(Total 15 Marks)

SECTION C

Question 5

Yello and Mango had been directors operating a business of juice extraction and packaging from bananas and mangos. At the beginning of this year, they agreed to dissolve the business and move into cellular phones business. The juice business was registered for VAT since it was started. Their year end is 31 December.

Yello has contacted you as a tax manager in the firm of Certified Public Accountants and would like to know the most tax effective way to dispose either of the assets or the business.

Required

- (a) Give the income tax and VAT implications of such an activity.
(6 Marks)
- (b) What conditions must prevail for the disposal of assets or business to qualify as a going concern?
(4 Marks)
- (c) Each of the directors had use of a Toyota Rav 4 that had been bought at Shs 54 million each in 1998. These vehicles had to be sold off during the year ended 31 December 1999 and the proceeds of Shs 18 million were used to pay some creditors.

Compute the capital gains or loss arising on the disposal of the vehicles.

(5 Marks)

(Total 15 Marks)

Question 6

- a) Discuss briefly what you understand by the following:
 - (i) Double Tax Treaty. **(3 Marks)**
 - (ii) The importance of the Double Tax Treaties agreements in the light of regional cooperation. **(3 Marks)**
- (b) Explain the Reverse Charge concept as it applies to VAT.
(4 Marks)
- (c) The Income Tax Assessor in URA has queried whether remuneration paid to non-executive directors of Matovu & Mukisa Co Limited (who are wives of executive directors) is in the

company's production of income. The wives duties include attending the occasional board meeting, but not much else.

As the accountant who has been handling the tax affairs of Matovu & Mukisa Co Limited, briefly outline the points you would use to explain to the Company's directors of the rationale of URA's enquiry, and how you would respond to the enquiry.

(5 Marks)

(Total 15 Marks)

Question 7

- (a) A Ugandan company has two directors, one UK National and a Ugandan. The company provides IT Services around the world. It proposes to pay salaries in Uganda.

What are the tax implications in relation to the salaries paid to the UK National if the UK National is absent from Uganda for more than a year?

(5 marks)

- (b) It has been suggested that a tax-free allowance of \$60 per diem per day would be paid to either of the directors while on business outside Uganda. This is in addition to a lot of airfares, hotel accommodation, and subsistence as the business is carried out in short assignments around the world.

Briefly outline the tax implications to the company's directors of all the above payments and allowances.

(Please consider both the Corporation tax and PAYE implications)

(10 Marks)

(Total 15 Marks)