

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

CPA(U) EXAMINATIONS

LEVEL TWO

PRINCIPLES OF TAXATION – PAPER 8

TUESDAY, 18 DECEMBER 2001

INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours**
2. Attempt all questions in Sections **A** and **B**, and only **one** question from Section **C**.
3. Section **A** has **twenty** compulsory questions each carrying 1 mark.
4. Section **B** has **three** compulsory questions, each carrying 20 marks.
5. Section **C** has **two** questions and only **one** question is to be attempted. Each question carries 20 marks.
6. Please read further instructions on the answer book.

SECTION A

Question 1

- (i) Which of the following persons is required to submit a return of income?
- (a) A peasant farmer who sells his surplus food.
 - (b) A resident individual whose only income is rental income from a commercial house located in Nairobi?
 - (c) A listed institution, which earns rental income.
 - (d) A non-resident individual whose only income is consultancy fees earned in Uganda.
- (ii) Which of the following is odd?
- (a) The supply of social welfare services.
 - (b) The supply of seeds, fertilizers, pesticides and hoes.
 - (c) The supply of educational services.
 - (d) The supply of betting, lotteries and games of chance.
- (iii) The following persons are not required to submit a return of income to URA;
- 1. Persons for whom all tax due has been recovered under Withholding Tax.
 - 2. Resident individuals who have not made any profits in the year of income.
 - 3. Resident individuals assessable under the presumptive tax system.
 - 4. Resident individuals whose income is below the threshold.
- (a) 1, 3, and 4 only.
 - (b) 2, 3 and 4 only.
 - (c) 3 only.
 - (d) 1 only.

- (iv) Which of the following is an allowable deduction?
- (a) Income tax payable in Uganda or a foreign country.
 - (b) A contribution or similar payment made to a retirement fund.
 - (c) The amount of pension paid to any person.
 - (d) None of the above.
- (v) Choose the correct statement.
- (a) A business below Shs 50 million turnover per year is not allowed to register for VAT.
 - (b) A business below 20 million turnover per year is not allowed to register for VAT.
 - (c) A business with 13 million turnover in three months must register for VAT.
 - (d) A business with 13 million turnover in three months is not required to register for VAT.
- (vi) Which of the following is not an exempt income?
- (a) The income of a listed institution.
 - (b) The income of a local authority.
 - (c) Interest payable on Treasury Bills.
 - (d) All the above.
- (vii) A credit for input tax is allowed to a taxable person for tax payable in respect of:
- 1. All taxable supplies made to the person during the tax period.
 - 2. All imports of goods made by the person during the tax period.
 - 3. All supplies made to the person during the tax period.
- a) 1 only.
 - b) 1, 2 and 3.
 - c) 1 and 2.
 - d) 2 and 3.

- (viii) Which of the following is false?
- (a) Provisional tax is payable in two installments in case of an individual.
 - (b) Provisional tax is payable in four installments in case of an individual.
 - (c) Provisional tax is payable before the end of the year of income.
 - (d) Provisional tax is offset against tax liability at the year-end.
- (ix) Which of these is not taxable in Uganda?
- (a) Any allowance payable in Uganda to a person working in a Uganda foreign mission.
 - (b) Business income earned by a Uganda Prisons officer.
 - (c) Income earned by a peasant farmer from sale of his surplus food crop production.
 - (d) Interest income earned in Uganda by a non-resident person.
- (x) Which of these is true for a provisional taxpayer who is an individual?
- (a) He is supposed to file two provisional returns, before the sixth and the twelfth month.
 - (b) He is supposed to make four quarterly provisional returns.
 - (c) He is supposed to make two payments, before the sixth and twelfth months.
 - (d) He is supposed to make four quarterly provisional tax payments.
- (xi) Which of the following best defines “tax period” as used in the Value Added Tax Statute?
- (a) The tax payers’ accounting period.
 - (b) The tax year commencing 1 July.
 - (c) The respective month.
 - (d) None of the above.

(xii) Which of the following is not categorized as employment income by the Income Tax Act, 1997?

- (a) Entertainment allowance.
- (b) Servants allowance.
- (c) Reimbursement of the employees' medical expenses.
- (d) Gifts.

(xiii) Which of the following is false?

- (a) A taxpayer can change from one method of accounting to another i.e. cash to accrual method with the permission of his auditors.
- (b) A taxpayer's method of accounting should be in accordance with Generally Accepted Accounting Principles.
- (c) A tax payer can use cash or accrual basis of accounting.
- (d) A tax payer can object to an assessment if he feels he has been unfairly assessed.

(xiv) Which of the following is/ are true?

- 1. A tax payer's method of accounting should be in accordance with Generally Accepted Accounting Principles.
- 2. A tax payer can use either cash or accrual basis of accounting.
- 3. A tax payer can change from one method to the other [in (2) above] with the permission of the Commissioner.
- 4. A tax payer can change from one method of accounting to the other [in (2) above] with the permission of the auditors and owners of the business.

- (a) 1, 2 and 4.
- (b) 1, 2 and 3
- (c) 2 and 4
- (d) 1 only.

(xv) The following persons are not obliged to submit a return of income to URA.

1. Persons for whom all tax due are recovered under withholding tax.
2. Resident individuals who have not made any profit in the year of income.
3. Resident individuals assessable under the Presumptive Tax System.
4. Resident individuals whose income is below the threshold.

- (a) 1, 3 and 4 only.
- (b) 2, 3 and 4 only.
- (c) 3 only.
- (d) 1 only.

(xvi) Which of the following is not exempt income?

- (a) The official employment income of a person employed in the Uganda Police force.
- (b) A lump sum payment made by a resident retirement fund to a member of the fund or a dependant of a member of the fund.
- (c) A contribution or similar payment made to a retirement fund either for the benefit of the person making the payment or for the benefit of any other person.
- (d) The income of a local authority.

(xvii) Business debt in the case of a debtor for tax purposes means;

1. A debt obligation, the proceeds of which are used to acquire a business asset or to incur an expense of a business;
2. A debt obligation arising, as a result of being given time to pay, on the acquisition of a business asset or the incurring of an expense of a business;
3. Any debt obligation of a partnership or company;
4. Any debt obligation owed to the creditor that was entered into or arose in the course of the creditors business.

- (a) 1, 2 and 3
- (b) 1 and 2
- (c) 1 and 4
- (d) all the above.

(xviii) What do you understand by the term tax?

- (1) A statutory contribution to the government.
 - (2) A contribution designed to reduce private expenditure in favour of public expenditure.
 - (3) Any leakage from the circular flow of income into the public sector.
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- (a) 1, 2 and 3
 - (b) 1 and 2
 - (c) 1 and 3
 - (d) none of the above.

(xix) Which of the following statements best defines 'foreign sourced income'?

- (a) Income accruing to Multinational corporations not resident in Uganda
- (b) Income accruing to non-resident persons
- (c) Any income except employment income not derived from sources in Uganda.
- (d) Any income not derived from sources in Uganda.

(xx) A disposal of an asset is deemed to take place when an asset is:

- (1) Sold, exchanged, redeemed, or distributed by the taxpayer.
- (2) Transferred by the taxpayer by way of gift.
- (3) Destroyed or lost.
- (4) Becomes obsolete.

- (a) 1 and 2
- (b) 2 and 4
- (c) 1,3 and 4
- (d) 1,2 and 3

SECTION B

Question 2

Konde is employed with BB Bank (U) Ltd as a middle manager. Her salary structure is as follows: -

- Monthly basic salary of Shs. 4,400,000
- Annual bonus of 3% of annual basic salary.
- She received payment in lieu of leave, which she did not take in financial year 1999/2000. Payment was made in May 2001, being basic salary for 60 days out of the 249 working days in a year.
- BB Bank also pays her domestic servants allowance at the rate of Shs. 450,000 per month. Konde also receives Shs. 200,000 per month as refund of mobile telephone airtime expense upon presenting her accountability. This is to facilitate her work.
- The company encourages employee share ownership. In 1999 Konde bought 10,000 shares at Shs. 20,000 each. The price quoted by the Securities Market was Shs. 28,000 per share. She received dividend of Shs. 160,000(net) in January 2001.
- Food is provided to all staff in two categories; Middle and senior management at the zone A where buffet is served; category B for the rest of the staff where a la carte menu is provided. In both cases the meal is charged to each staff at Shs.84, 000 per month. BB Bank meets all the expenses and charges to the corporation's expenditure statement, as allowable deduction.
- BB Bank pays life insurance premium for Konde and her family of Shs. 6,200,000 per annum.
- Konde is provided a company car, which cost Shs.45 million in 1998 when it was first provided to her. The market value has now come down to Shs. 20 million.
- A house is also provided at a monthly rental of Shs. 980,000. BB Bank pays the rent directly to the landlord.
- During the financial year 2000/2001 Konde also received interest from her investment in treasury bills of Shs. 510,000.
- On 1 January 2001 her account in Uganda Commercial Bank was credited with Shs.12 million as rent from her houses in Kisumu (Kenya) for the period January 2001 to December 2002. Total expenses towards repairs and maintenance is Shs 1,150,000. Uganda shillings is used all through.

Required:

- (a) Compute the total taxable income for the year 2000/2001 for Mrs. Konde based on the above facts.
- (b) Compute the tax liability for the year 2000/2001 and state when it is due.
State any assumptions made

(20 marks)

Question 3

JASON (U) Limited is a company incorporated in Uganda. The company's offices are located in Kampala, Uganda. The company deals in buying and selling of agricultural produce such as beans, posho and groundnuts.

JASON (U) Limited commenced business on 1 July 1999. The start up costs of the company then amounted to Shs. 12,000,000.

During the first year of operation, the company incurred a tax loss of Shs. 35,000,000. The tax loss has been agreed with the Uganda Revenue Authority.

The company has produced its audited financial statements for the year ended 30 June 2001 and has asked you, as their Tax Advisor, to prepare the tax computation for submission to the Uganda Revenue Authority.

Your Tax Manager has already reviewed the company's tax file and has passed it to you with the following comments:

1. The company made a net profit before tax of Shs. 40,000,000 during the year ended 30 June 2001.
2. The depreciation charged in the financial statements was Shs. 10,000,000
3. The company made contributions to the National Social Security Fund amounting to Shs. 8,000,000. This amount is the 10% contribution made by the company to the Fund.
4. The company spent Shs. 15,000,000 as housing to its Senior Staff who are entitled to housing allowance.
5. The company incurred Shs. 10,000,000 for legal fees. Of this amount, Shs. 7,000,000 was spent on Debt collection activities while Shs.

- 3,000,000 was spent on registering the title for the company's property bought at Bunga, a suburb of Kampala.
6. The company spent Shs. 3,000,000 on donations. The donation was made towards the Kabaka's coronation anniversary.
 7. The training costs of Shs. 5,000,000 was spent towards the Managing Director's tuition for the Masters of Business Administration degree he is undertaking at the Makerere University Business School.
 8. The company made provision for bad debts during the year as follows:
 Specific Shs. 30,000,000
 General Shs. 20,000,000.
 9. Included in the company's income statement was unrealised foreign exchange loss amounting to Shs. 5,000,000, realised exchange gains of Shs. 2,000,000.
 10. The company made a profit on sale of fixed assets of Shs. 5,000,000.
 11. The company received interest on treasury bills amounting to Shs 1,250,000.
 12. The company paid Withholding tax of Shs 2,300,000 and made two provisional tax payments amounting to Shs 6,000,000.

Required:

- (a) Compute JASON (U) Ltd's corporation tax for the year ended 30 June 2001.
- (b) The due date for payment of the final tax liability for the year then ended.

Additional information:

- (a) The Written Down Values of the fixed assets agreed with the Uganda Revenue Authority as at 30 June 2000 were as follows:

Class	Amount in Shs.
1	25,000,000
2	15,000,000
3	Nil
4	10,000,000

- (b) The Company made several purchases of fixed assets during the year as follows; Computers Shs. 15,000,000; Second hand pick up van Shs. 10,000,000; A luxury Toyota Prado car for the Managing Director at Shs 50,000,000; furniture Shs. 5,000,000 and equipment Shs. 9,000,000.

- (c) The company also made the following asset disposals during the year; Computers which had a net book value of Shs. 15,000,000 were sold at Shs. 20,000,000; The sale of motor vehicles realised Shs. 18,000,000. Included in the proceeds for motor vehicle sales was Shs. 8,000,000 which related to the sale of the Pajero Mitsubishi car which was previously used by the Managing Director. The Pajero car was bought on 1 July 1999 at the cost of Shs. 40,000,000.

Question 4

- (a) (i) Under what circumstances does a company deregister for VAT?
What is the procedure for such deregistration

(3 marks)

- (ii) What is the usefulness of VAT threshold levels?

(2 marks)

- (iii) Namata is a retailer and is registered for VAT. She buys her supplies of photocopying paper from Mr. Kazinga who is registered for VAT. Mr. Kazinga acquired the supplies from Computer Point Ltd whose price is Shs 8,500,000 VAT (exclusive).

If all parties are to charge VAT at the standard rate and Namata and Kazinga both require a profit margin of sh500,000 on the photocopying paper, what is the minimum price that Namata should charge?

(3 marks)

- (iv) A trader makes a supply of standard rated goods of Shs.300,000(excluding VAT); zero-rated supply of Shs.150,000 and exempt supply of Shs. 200,000.

What is the output VAT?

(2 marks)

- (b) Kiconco (U) Ltd. is VAT registered company which deals in various goods. The company's transactions for a period were as follows:-

Purchases

- 01/12/01 Bought a motor car for business use at Shs 8,000,000 and paid in cash to Top company (U) Ltd.
- 02/12/01 Imported a pick-up for business use and paid Shs 4,200,000 as VAT.
- 03/12/01 Bought 125 sacks of maize flour for resale and paid cash Shs 3,700,000.
- 03/12/01 Received UTL telephone bill for the month of November 2001 of Shs 197,000.
- 06/12/01 Paid MTN telephone bill for the month of December 2001.
- 07/12/01 Paid November 2001 housing allowances to staff of Shs 2,500,000.
- 11/12/01 Bought 145 bags of Rice from Kibimba Rice scheme for Shs 3,125,000 and paid cash.
- 18/12/01 Paid rent for the shop for Shs, 3,200,000. The rent invoice were received in October 2001. All prices for local purchases are VAT inclusive where applicable and the company had received tax invoices for them.

Sales:

- 08/12/01 Sold 50 sacks of maize flour to Kitante Hill School for Shs. 2,100,000.
- 09/12/01 Exported 50 bags of rice to Rwanda for Shs 710,000 cash.
- 12/12/01 Sold 20 dozens of soap on credit to Kikubo traders for Shs 800,000.
- 15/12/01 Sold 30 bags of salt to Nakasero market for Shs 1,500,000 cash.
- 18/12/01 Sold 140 bags of dry beans to City High School for Shs 7,500,000 on credit.
- 18/12/01 Exported 50 bags of Rice to Rwanda for Shs. 2,800,000 cash.
- 18/12/01 Received Shs 1,800,000 for maize flour sold in November 2001 to Kikuubo Traders.

All prices are VAT inclusive where applicable.

Required:

Compute the company's December 2001 VAT liability under:

- (i) Cash accounting basis
- (ii) Invoice accounting basis

(10 marks)
(Total 20 marks)

SECTION C

Question 5

Briefly comment and advice on the tax position of each of the following cases:

- (a) Francis runs a business supplying exempt goods. Mary, his sister, runs a business supplying Zero-rated goods. Neither of them charges any VAT to customers though each of them has a turnover in excess of Shs. 50 million per annum. How, if at all, do their VAT positions differ?

(4 marks)

- (b) Rashid, a close friend of yours, has informed you that he is aware that some businesses are registered for VAT whilst others are not registered. Rashid has only recently commenced trading and considers that it will take him 5 years to reach full potential sales, which he projects to rise from the current Shs. 25 million per annum to Shs. 250 million in that period. Could you please advise Rashid on the position regarding VAT registration?

(4 marks)

- (c) Mr. Mujuni, a prominent lawyer in Kampala, traveled to South Africa on a holiday. Upon return to Uganda he brought with him six suits which he intended to use as part of his professional attire. With persuasion from his wife, he sold all six suits and made a profit of Shs. 6,000,000. He has informed you, as his tax advisor, that he does not intend to include the profit in his return, since he does not trade in clothing.

(4 marks)

- (d) Mr. Kalebo was appointed caretaker for the Workers' House, a twenty storey building in Kampala on 1 November 2001. The building has a flat on the roof where Mr. Kalebo resides because he has to be available in the premises all the time in case of an emergency. Mr. Kalebo earns a gross salary of Shs. 1,000,000 per month exclusive of the housing. Mr. Kalebo has approached you, after a hot argument with his accountant who wants to tax him for the housing benefit. Mr. Kalebo is of the view that he does not receive any housing allowance and should not be taxed on housing.

(4 marks)

- (e) Mr. Wafula, your General Manager, tuned onto the Uganda Television last night and listened to a Tax Focus program presented by the Uganda Revenue Authority. He has asked you to explain to him certain issues which he could not follow on the program. Please prepare an outline to help Mr. Wafula understand the difference between the

following terms which were used by the Assistant Commissioner Public Relations and Taxpayer Education at the Uganda Revenue Authority:

- i. Direct and indirect taxes
- ii. Tax evasion and tax avoidance

(4 marks)

(Total 20 marks)

Question 6

- (a) Kakwano Industries Limited, is a local manufacturing company producing a wide range of products such as soap, edible oil, and detergents. The company's production has been increasing over the years and they decided to construct an industrial building in the Industrial Area, Kampala. Move International Uganda Limited, a construction company, was contracted to do the work. The building was originally constructed and put to use on 1 July 1999 at a cost of Shs. 100,000,000. The cost on the extension made during the year to 30 June 2001 was Shs. 50,000,000. The extension was put to use immediately.

Required:

Compute the Industrial Building Allowances that Kakwano Industries Limited is entitled to claim during the years ended 30 June 2000 and 30 June 2001.

(6 marks)

- b) Move International Uganda Limited, a local construction company, prepares accounts to 31 December each year. For the year ended 31 December 2000, the company submitted the provisional tax estimate on 30 June 2000 and paid the first installment of Shs. 10,000,000. The second and last installment of Shs. 10,000,000 was paid on 23 December 2000. However, the company failed to submit the final tax return on time and was issued with a notice of estimated assessment on estimated income of Shs. 90,000,000 on 30 June 2001. The self-assessment return and accounts were submitted on 31 July 2001. The self-assessment return reflected chargeable income of Shs. 120,000,000.

Required:

- i. What action would you advice Move International Uganda Limited to take on receipt of the estimated assessment?
- ii. What action will the Commissioner take since the self-assessment return and accounts reflect a higher income than his/her estimate?

(2 marks)

(1 mark)

- iii. Calculate the tax payable and state the date tax was payable
(5 marks)
- iv. Assume the tax is not paid by 31 July 2001. Calculate late filing penalty and interest payable by 31 July 2001.

(6 marks)

(Total 20 marks)