

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

PRINCIPLES OF TAXATION – PAPER 8

CPA(U) EXAMINATIONS

JUNE 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) Under the VAT Statute 1996, records must be kept for:-
 - (a) 5 years.
 - (b) 6 years.
 - (c) 7 years.
 - (d) 4 years.
- (ii) Which of the following is not an exempt supply under the VAT Statute 1996?
 - (a) Maize flour sold in Kabale.
 - (b) Medical gloves sold to Kabale Secondary School Clinic.
 - (c) Maize flour exported to Nairobi.
 - (d) A supply of meat to Sheraton Kampala Hotel.
- (iii) Which of the following does not form part of gross income under the Income Tax Act 1997?
 - (a) Interest income from treasury bills.
 - (b) Rental income of a company.
 - (c) Income earned outside Uganda by a resident individual.
 - (d) Income earned from exports.
- (iv) Which of the following is an allowable deduction?
 - (a) Income tax payable in Uganda.
 - (b) In case of rental income, 20% of the rental income deducted as expenditure and losses incurred by an individual in the production of such income.
 - (c) A bad debt written off due to delayed payment.
 - (d) Money spent on purchase of a computer for a business.
- (v) Which of the following is a mismatch?
 - (a) Excise duty.
 - (b) Graduated tax.
 - (c) Value Added Tax.
 - (d) Income tax.

- (vi) 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.
- (vii) The rental income of a resident individual is charged to tax as follows:-
- (a) 20% of the amount in excess of Ushs.1,560,000.
 - (b) 20% of the gross rental income.
 - (c) 20% of the gross rent less rental expenses.
 - (d) Out of the gross rent, take off 20%, then take off Ushs.1,560,000, then apply a tax rate of 20% on the balance.
- (viii) Which of the following is not subject to Withholding Tax?
- 1. Interest paid to a financial institution.
 - 2. Interest paid by a financial institution.
 - 3. Royalty paid to a non-resident.
 - 4. Payment of dividends to East African Development Bank.
- (a) 1, 2 and 4 only.
 - (b) 1 and 4 only.
 - (c) 2 and 3 only.
 - (d) 1 and 2 only.
- (ix) 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.

- (x) Which of the following is incorrect about income subject to final Withholding Tax?
- (a) That income is not aggregated with other income for the purpose of ascertaining chargeable income.
 - (b) No deduction is allowed for any expenditure or losses incurred in deriving such income.
 - (c) The taxpayer will need a tax credit certificate to be able to claim tax withheld on such income against final tax liability.
 - (d) No further tax is imposed against the taxpayer in respect of such income.
- (xi) VAT is not chargeable in one of the following cases:-
- (a) Sale of a car to United States Agency for International Development (USAID) by a local VAT registered trader.
 - (b) Import of a car by the Kenyan Embassy.
 - (c) Import of a car by a local government authority.
 - (d) Import of a car by a government ministry.
- (xii) The VAT standard rate is:-
- (a) 17.5%
 - (b) 16%.
 - (c) 17%.
 - (d) 15%.
- (xiii) The Commissioner may require a taxpayer or taxpayer's trustee, to furnish a return of income for the taxpayer, by a specified date, for a period less than 12 months when the tax payer: -
- (a) is about to leave Uganda indefinitely.
 - (b) consistently makes losses from year to year.
 - (c) has not filed a return of income by the due date.
 - (d) is non-resident for the year of income.
- (xiv) A person, for VAT registration purposes means all the following except:-
- (a) An unincorporated body.
 - (b) An association.
 - (c) A sole proprietor.
 - (d) None of the above.

- (xv) Employment services according to the VAT Statute 1996 are:-
- (a) Exempt supplies.
 - (b) Zero rate supplies.
 - (c) Standard rated supplies.
 - (d) None of the above.
- (xvi) Which of the following does not form part of employment income?
- (a) Entertainment allowance.
 - (b) Servants allowance.
 - (c) Reimbursement of employee's medical expenses.
 - (d) Medical allowance.
- (xvii) Musa bought a suit and paid Shs.150,000 cash from a VAT registered trader on Luwum Street. How much VAT did he pay?
- (a) Shs.124,500.
 - (b) Shs. 25,500.
 - (c) Shs. 21,795.
 - (d) Shs. 22,500.
- (xviii) Which of the following is the best definition of taxable value of a taxable supply under the VAT Statute 1996?
- (a) The amount payable for the supply.
 - (b) The amount exclusive of all direct taxes.
 - (c) The tax element of the total value.
 - (d) The total consideration paid or payable in money or in kind by all persons for the supply.
- (xix) Which of the following is not exempt income under Income Tax Act 1997?
- (a) Official employment income of an army officer.
 - (b) Business income of a listed institution.
 - (c) Rental income of an army officer.
 - (d) None of the above.

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

SECTION B

Question 2:

Mr. Abdul Ashraft is a Zimbabwean citizen. He was recruited from Zimbabwe by ABS(U) Ltd. as the company's Marketing Manager from 1 February 2001. Mr. Ashraft is in Uganda solely for the purpose of fulfilling his employment contract with ABS(U) Ltd. The terms of his employment contract include the following:-

- (i) A monthly salary of:-
 - (a) Ushs.4,000,000 paid in Uganda shillings.
 - (b) US\$ 1,500 payable directly to his account in Zimbabwe.
- (ii) Provision of accommodation. The company rents for him a house in Muyenga at Ushs.3,000,000 per month.
- (iii) Provision of a Toyota Prado by the company which was bought on 1 February 2001 for Ushs.45 million.
- (iv) A 2% commission on gross sales if sales exceed Shs 200 million per month. This will be in addition to his salary.
- (v) A bonus of 0.5% of gross sales per month.
- (vi) Medical insurance to National Insurance Corporation of Ushs.1,200,000 per year to cover Mr. Ashraf and his dependants' medical costs.

On further investigation, it was confirmed that ABS (U) Ltd. paid the

following on behalf of Mr. Ashraft although they were not covered in the employment contract:

- (i) Ushs.4,500,000 being the cost of air passage for Mr. Ashraft and his family from Zimbabwe to Uganda on 1 February 2001.
- (ii) Mr. Ashraft was given a furniture loan of Ushs.15 million on 1 February 2001 at an interest rate of 4% per annum. The loan is payable on termination of Mr. Ashraft's contract although the interest is deducted from his salary on a monthly basis.
- (iii) School fees of Ushs.2,500,000 for Mr. Ashraft's children at Mengo Senior School.
- (iv) (a) Security expenses of Shs.350,000 per month.
(b) Electricity and water bills paid at Shs.120,000 per month. The company deducts Shs.50,000 from his monthly salary.
(c) House servants for Shs.150,000 per month.

Other information:-

- (i) The Bank of Uganda discount rates for the months of June and July 2000 and 2001 were as follows:-

	2000	2001
June	17%	22%
July	15%	23%

- (ii) The average exchange rate for the period was US\$ 1 to Ushs.1,700.
- (iii) Sales for January - June 2001 in shillings millions were as follows:-

Jan.	Feb.	Mar.	Apr.	May	June
250	220	180	196	320	340

Required:

Determine Mr. Abdul Ashraft's tax liability for the period to 30 June 2001.

(20 marks)

Question 3

High View Hotel Ltd. located in Tororo operates an approved hotel business. Its results for the year to 31 December 2000 were as follows:-

	Ushs.'000	Ushs.'000
Sales		500,000
Cost of sales		<u>230,000</u>
Gross profit		270,000
Other income:-		
Profit on disposal of assets		100
Interest on Treasury bills		80,000
Foreign exchange gain		<u>46,000</u>
		396,100
Less Expenses:-		
General expenses	84,600	
Repairs and renewals	17,000	
Depreciation	35,000	
Rent	36,000	
Foreign exchange loss	52,000	
Water and electricity	6,200	
Advertising	18,700	
Staff party	4,600	
Donations	2,100	
Entertainment	8,700	
Provision for obsolete stock	13,700	
Bad debts	<u>15,600</u>	
		<u>294,200</u>
Net Profit		<u>101,900</u>

Notes:

(a) The wear and tear balances brought forward from 1999 were as follows:-

Class	Shs '000
I	3,000
II	6,000
III	5,500
IV	<u>12,000</u>
Total	<u>26,500</u>

(b) Additions during the year were as follows:-

Date	Item	Cost Shs '000
01.04.00	Computer	5,500
30.06.00	Electric Fan	90
01.02.00	Photocopier	4,500
31.08.00	Land cruiser station wagon	35,000
31.12.00	Tata lorry (20 tonnes)	50,000
01.12.00	New hotel building.	100,000

Note:

1. Construction of the new hotel building commenced on 1 August 2000.
2. The old hotel building was constructed in May 1999 at Shs 200,000,000.

Disposals were as follows:-

Item	Cost Shs '000	Accumulated Depreciation. Shs '000	Sale Proceeds Shs '000	Profit / (loss) Shs '000
Old computer	2,500	700	1,900	100
Saloon car	17,000	12,000	4,000	(1,000)
Photocopier	6,000	5,800	1,200	<u>1,000</u>
Profit on disposal				<u><u>100</u></u>

(c) Extra information relating to the year is as follows:-

(i) General expenses are broken down as follows:

	U Shs '000
Salaries and wages	54,000
NSSF company contribution	5,400
Office cleaning, telephone and postage.	<u>25,200</u>
	<u>84,600</u>

(ii) Rent expenses are broken down as follows:-

	U Shs '000
Office rent.	27,000
House rent for Managing Director.	5,000
Car rentals for business use.	<u>4,000</u>
	<u>36,000</u>

(iii) Repairs and renewals include Ushs.4,300,000 for putting up a new reception area. The difference relates to polishing the business premises and replacing broken windows and a door.

- (iv) Foreign exchange gain was recognised on translation of debtors denominated in foreign currency at the year-end.
- (v) Ushs.22,000,000 of the foreign exchange loss was recognised on translation of creditors denominated in foreign currency at the year-end. The balance was on actual payments made during the year to clear trade creditors denominated in foreign currency.
- (vi) Advertising includes Ushs.6,900,000 spent on installing a billboard on Entebbe road on 1 August 2000 to advertise the company's products. The balance was media advertising.
- (vii) The break down of bad debts is as follows:

	Shs '000
Irrecoverable bad debts (Debtors no longer traceable)	6,500
Bad debts overdue by over one year	4,100
Increase in bad debts provision.	<u>5,000</u>
	<u>15,600</u>

Required:

Calculate the tax liability for High View Hotel Ltd. for the year ended 31 December 2000.

(20 marks)

Question 4:

K & J (U) Ltd. is a VAT registered company which deals in various goods. The company's transactions for the month of June 2000 were as follows:-

Purchases

- 1.6.00 Bought a passenger car for business use. The price was Ushs 15,000,000 paid in cash to Lohnro Motors (U) Ltd.
- 3.6.00 Imported a delivery van for business use and paid Ushs. 3,000,000 as VAT to Customs Department.
- 6.6.00 Bought 100 bunches of matooke for resale and paid cash Shs.400,000.
- 11.6.00 Received Celtel telephone bill for the month of May 2000 of Shs.125,000.
- 12.6.00 Paid Celtel telephone bill for the month of April 2000 for Ushs.155,000. The bill was received in May 2000.
- 15.6.00 Paid May 2000 salaries to staff of Ushs.2,500,000.
- 17.6.00 Bought 100 bags of sugar from Kakira Sugar Works for Ushs.4,500,000 and paid cash.
- 30.6.00 ▪ Paid rent for the shop for Ushs.2,000,000.

- Paid rent for the Director's apartment Ushs.1,500,000.
The rent invoices were received in April 2000.

All prices for local purchases are VAT inclusive where applicable and the company has received tax invoices for them.

Sales:

- 7.6.00 Sold 50 bunches of Matooke to Makerere University for Ushs.300,000 cash.
- 8.6.00 Exported 50 bunches of Matooke to Rwanda for Ushs.350,000 cash.
- 11.6.00 Sold 20 bags of sugar on credit to Kawempe traders for Ushs.1,000,000.
- 15.6.00 Sold 30 bags of sugar to Kawempe traders for Ushs 1,620,000 cash.
- 18.6.00 Sold 100 bags of dry beans to Makerere University for Ushs.8,000,000 on credit.
- 20.6.00 Exported 80 bags of sugar to Rwanda for Ushs.4,400,000 cash.

All prices are VAT inclusive where applicable.

Required:

- (a) Compute the company's June 2000 VAT liability if the company uses cash basis accounting.

(10 marks)
- (b) Compute the company's June 2000 VAT liability if the company uses invoices basis accounting.

(10 marks)

(Total 20 marks)

SECTION C

Question 5:

- (a) Why is taxation necessary? Give examples to illustrate your answer. (6 marks)
- (b) Write short notes on:
- (i) The term residence when applied to individuals and companies. (6 marks)
 - (ii) Objection to an income tax assessment. (4 marks)
- (c) Describe the role of the Tax Appeals Tribunal in Uganda. (6 marks)
- (Total 20 marks)**

Question 6:

- (a) State the tax considerations you would take into account while advising your friend who would like to start a business as either a sole proprietor or a limited company. (5 marks)
- (b) Explain six principles of a good tax system citing relevant examples in Uganda. (12 marks)
- (c) Explain the difference between a comprehensive tax system and an efficient tax system. (3 marks)
- (Total 20 marks)**