

# THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

*A Committee of the Council of ICPAU*

## CPA(U) EXAMINATIONS

### LEVEL THREE

#### TAXATION – PAPER 13

THURSDAY, 20 JUNE 2002

#### 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

Safeway Trading Company Limited is a Ugandan resident company, which manufactures and bottles soft drinks for sale. The company has always made up its financial statements to 30 June and in the year ended 30 June 2001 the company's profit before tax was Shs 16,500 million arrived at after charging and crediting the items of expenditure and income.

Expenditure:

	<b>Shs '000</b>
(i) Gift to a local charitable organization [Note 1]	16,000
(ii) Contributions to the company's staff provident fund	23,000
(iii) Amortisation of an acquired intangible asset [Note 2]	48,500

Income:

	<b>Shs '000</b>
(iv) Bank interest income [Note 3]	14,000
(v) Income from rental property [Note 4]	25,000
(vi) Dividend income [Note 5]	125,000

### Notes

- 1 The local charitable organization is "an exempt" Non Governmental Organisation.
- 2 The acquired intangible asset is the trademark and rights to bottle the company's products from an international bottling company.
- 3 Bank interest was received net from a local savings account after deduction of withholding tax.
- 4 The income from the rental property is from the company's warehouse let out to a clearing and forwarding company.
- 5 The dividend income was received from the company's 100% resident subsidiary company.
- 6 The tax written down values of the company's plant and machinery as at 30 June 2000 were as follows:

	<b>Shs '000</b>
Class 1	124,000
Class 2	140,000
Class 3	2,360,000

- 7 New plant and machinery additions and disposals during the year were as follows:
- (a) A new machine for the bottling line was bought in March for Shs 80,000,000.
  - (b) A new Nissan Terrano was bought for the Finance Manager in January for Shs 68,000,000.
  - (c) Computer equipment and software of Shs 14,000,000 were bought in December.
  - (d) The company sold an old delivery lorry for Shs 22,000,000.
- 8 The total cumulative cost of the company's industrial buildings as at 1 July 2001 was Shs 6,400,000,000. On 1 September 2001 the company bought a new factory for Shs 132,000,000. The factory was brought immediately into use, and the company wishes to claim maximum allowances during the first year of industrial use.

**Required:**

- (a) Calculate the corporation tax payable by Safeway Trading Company Limited for the year ended 30 June 2001, showing in detail all your workings as well as brief explanatory notes on your tax treatment of the items in notes 1 to 8 above (where applicable).  
**(26 marks)**
  - (b) State the relevant due dates for tax payments for Safeway Trading Company Limited for the 2001 year of income.  
**(3 marks)**
  - (c) Explain what penalties and interest the Commissioner may impose if Safeway Trading Company were not to furnish their return of income and pay the tax due and payable on time.  
**(4 marks)**
  - (d) The provisional tax return filed by Safeway Trading Company Limited for the 2001 year of income showed an estimate of the chargeable income for the year of Shs 12,800 million, and 30% provisional tax was paid thereon. Calculate the penal tax payable by the company for understating its provisional tax estimate.  
**(4 marks)**
  - (e) You believe that the company had genuine reasons for understating their provisional estimate of the chargeable income. How would you advise them in light of the penal tax assessed on them in (d) above.  
**(3 marks)**
- (Total 40 marks)**

## SECTION B

### Question 2

Gloria and Sophia have been in partnership since 1994 dealing in designer clothes, and sharing profits equally. On 31 December 2001, Gloria resigned from the partnership to go for further studies, and Agnes replaced her on 1 January 2002. Profits continued to be shared equally between Sophia and Agnes. The partnership prepares its financial statements to 31 December, and Sophia has approached your firm for tax advice in relation to the following:

- (i) The tax implications of Agnes contributing assets to the partnership.
- (ii) Sophia paying off Gloria for her share of capital and business assets in the partnership.
- (iii) Valuing the business assets of the former partnership and transferring them to the new partnership.
- (iv) The tax disclosure requirements in respect of the change in partnership.
- (v) The partnership tax return filing requirements and tax payment obligations of the individual partners.

**Required:**

Write a brief letter to Sophia explaining by way of bullet points, the tax implications of all the above.

**(15 marks)**

### Question 3

Legends Supermarket, a UK registered company is planning to open up a branch in Uganda. The company's Finance Director has requested a meeting with you at your firm's offices to discuss the following tax issues that are of major concern to him and will ultimately influence the company's final decision on their set up in Uganda.

- (a) How the company's Uganda branch profits will be taxed in Uganda.
- (b) What are the tax implications of the company repatriating all the profits of the Uganda branch back to the UK.
- (c) What are the tax implications of the UK Head Office charging a proportion of its management and administrative costs to the Uganda branch.
- (d) The UK head office will initially second six members of staff to the Uganda branch for a period of two months, to assist with the initial set up of the branch, and the staff's salaries will be paid in the UK by the UK company.

- (e) The implications of the existence of a double tax treaty between Uganda and the UK, and how this may be beneficial to the company.

**Required:**

Prepare brief notes on each of the Finance Director's queries in (i) to (v) above which you would use as the basis of your discussion during the meeting, highlighting all the tax issues which you would want to bring to his attention during the meeting.

**(15 marks)**

**Question 4**

Medi, is a Kampala based businessman who regularly imports office furniture from his suppliers based in Kenya. His average monthly value of imports is about Shs 5 million.

He has recently read in *The New Vision* that the Uganda Revenue Authority (URA) intends to start assessing and collecting Value Added Tax (VAT) on the deemed value added on people who regularly import goods in excess of Shs 4 million on average a month. He has never considered registering for VAT, as he believes that his annual business turnover is below the annual threshold of Shs 50 million.

He is concerned about this new URA notice published in *The New Vision*, and he has approached you for advice.

**Required:**

- a) Explain to Medi when a trader is required to register with the URA for VAT with respect to the VAT registration threshold according to the VAT Statute 1996.

**(3 marks)**

- b) Explain the potential penalties that Medi may face for late registration for VAT.

**(3 marks)**

- c) Explain how the URA will compute (assess) the VAT payable by Medi on his imports.

**(3 marks)**

- d) Briefly explain what records Medi will need to maintain in respect of the imports and the other purchases that he makes once he has registered for VAT?

**(4 marks)**

- e) If Medi were to register for VAT, how often would he be required to file his VAT returns with the URA, and when would he have to make the VAT payments due for each VAT period?

**(2 marks)**

**(Total (15 marks))**

**SECTION C****Question 5**

- (a) Rita is employed by JFK Associates Limited as the firm's Human Resources Manager. The following information relates to Rita's remuneration package, allowances and other income for the year ended 30 June 2001.
- (i) Annual salary of Shs 36 million.
  - (ii) Rita paid 10% of her salary into the company's private pension fund.
  - (iii) The company made a further contribution equivalent to 5% of Rita's salary into the scheme on her behalf.
  - (iv) The company provided Rita with a motor vehicle throughout the year which was valued at Shs 14 million at the time it was first provided to Rita. The motor vehicle was bought two years ago for Shs 50 million.
  - (v) During the 12 months period ended 30 June 2001, Rita drove 19,000 miles of which 4,250 miles were for business purposes.
  - (vi) Rita paid the company Shs 40,000 per month towards the cost of her private fuel.
  - (vii) The company provided Rita with an interest free loan of Shs 30 million, payable over a six year period, and as at 30 June 2001, the balance outstanding on the loan was Shs 20 million.
  - (viii) Rita resides in one of the company's flats of ratable value Shs 500,000 per month.
  - (ix) Rita owns a small house in the affluent suburbs of the city which she lets out for Shs 450,000 per month.

**Required:**

- (a) Calculate the income tax payable by Rita for the year ended 30 June 2001.  
**(9 marks)**
  - (b) Calculate the tax payable on Rita's rental income for the year.  
**(3 marks)**
  - (c) The company has decided to waive the balance outstanding due from Rita on the company loan of the Shs 20 million. Advise Rita on the tax implications of this course of action by her employer.  
**(3 marks)**
- (Total 15 marks)**

**Question 6**

- (a) Owino and Balikudembe both work for a major petroleum company in Uganda. Owino is in charge of the fuels sales (petroleum and diesel) and Balikudembe is responsible for the lubricants and Liquefied Petroleum Gas (LPG) sales. Both Owino and Balikudembe have been notified by the company's internal auditors that the VAT treatment of their respective products differs according to the VAT Statute 1996.

**Required to:**

- (i) Compare and contrast the VAT treatment of a trader making exempt supplies and that of a trader making taxable supplies. **(3 marks)**
- (ii) Differentiate between the partial exemption method and the standard exemption method. **(3 marks)**
- (iii) When are annual adjustments on the VAT account required to be made by a trader making mixed supplies, and how are they made. **(3 marks)**
- (b) During the month of June 2002, the following amounts of VAT were charged on the company's purchases and expenses that related to the following supplies:

Items	Shs million
Petrol	108
Diesel	110
Kerosene	75
Lubricants	83
LPG Gas Cylinders	65
Non – attributable VAT	40

The following supplies were also made during the month. (Amounts exclude VAT where applicable):

Items	Shs million
Petrol	240
Diesel	200
Kerosene	120
Lubricants	140
LPG Gas Cylinders	90

**Required:**

Compute the amount of input tax that the company is able to reclaim in its VAT return for the month of June, based on the above information.

**(6 marks)**  
**(Total 15 marks)**

**Question 7**

Write short notes on the tax treatment of each of the following:

- (a) A company incurs expenditure of Shs 44 million in starting up business to produce income to be included in the company's taxable income.
- (b) A horticultural company incurs expenditure of Shs 12 million in acquiring farm works for use in its business.
- (c) A company with accumulated tax losses of Shs 68 million arising from its trade dealing in the processing and export of coffee is considering changing business to processing and exporting hides and skins.
- (d) A Ugandan resident company wholly owned and controlled by its South African parent company has requested the parent company to cancel its business debt (an amount it owes the parent company) on the grounds that it cannot afford to repay the debt, and the parent company has agreed to forgive the debt.
- (e) A sole trader in the grocery business carried out an end of year inventory take and on realising that most of his inventory was damaged and some had expired, he wrote off inventory of Shs 18 million in his inventory records.
- (f) A Ugandan resident company pays a dividend of Shs 210 million for the year ended 31 December 2001, to its local parent company.

**(15 marks)**