

# THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

*A Committee of the Council of ICPAU*

## CPA(U) EXAMINATIONS

### LEVEL TWO

#### PRINCIPLES OF TAXATION-PAPER 8

**TUESDAY, 22 JUNE 2004**

#### INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours**.
2. Attempt **all** questions in Sections **A** and **B** and **one** question from Section **C**.
3. Section **A** has twenty compulsory multiple-choice 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. **Tax rates** are provided on page 10.
7. Please read further instructions on the answer book.

**SECTION A****Question 1**

- (i) Jane and Joan are partners holding 80:20 interest in LLP Partnership, a law firm based on Nkrumah Road. For purposes of taxation, who are the taxable persons?
  - (a) Jane and the LLP Partnership.
  - (b) LLP Partnership.
  - (c) Jane, Joan and LLP Partnership.
  - (d) Jane and Joan.
- (ii) Financial services offered by banks are ... under the VAT Statute.
  - (a) Standard rated.
  - (b) Partially exempt.
  - (c) Exempt.
  - (d) Zero rated.
- (iii) Which of the following reasons justifies the establishment of Export Processing Zones?
  - (a) Promote weak industries to produce for local consumption.
  - (b) Attract import substitution industries.
  - (c) Promotion of commodity exports through tax incentives.
  - (d) Export of services.
- (iv) ABC Ltd is a Korean company offering services to Kinyara Sugar Works in excess of US \$ 1,000. ABC Ltd is non-resident. What withholding tax rate should Kinyara apply when paying the Korean company?
  - (a) 15%.
  - (b) 4%.
  - (c) 10%.
  - (d) 0%.
- (v) Dairy Corporation had installed a milk processing plant in Ntungamo for the year ended 31 December 2003. What is the tax depreciation rate that will be applicable to this plant in 2004?
  - (a) 20%.
  - (b) 50%.
  - (c) 35%.
  - (d) 75%.

- (vi) Alpha Ltd is a Ugandan company with operations in Sudan and Egypt where it paid foreign tax amounting to Shs 100,000,000 in 2003. What credit is available for foreign tax under the Income Tax Act 1997?
- (a) Claim Shs 100,000,000 as tax payment on the return for 2003 to the extent it does not exceed Uganda tax at 30%.
  - (b) Expense Shs 100,000,000 as a tax deductible expense.
  - (c) Claim for tax refund of Shs 100,000,000 for Year of Income 2003.
  - (d) Income from Sudan and Egyptian sources is not subject to tax.
- (vii) What is the key provision of the East African Customs Union treaty?
- (a) Establishment of export-oriented industries in East Africa.
  - (b) Establishment of a Customs Union.
  - (c) Share Power and Electricity resources in East Africa.
  - (d) Train staff of the three governments using same resources.
- (viii) Jane is a cashier with Muliti Road Parking Ltd with a monthly basic salary of 290,000 and monthly lunch allowance of Shs 100,000. Compute her monthly PAYE.
- (a) Shs 100,000.
  - (b) Shs 117,000.
  - (c) Shs 41,500.
  - (d) Shs 30,000.
- (ix) International Supermarket Ltd operates on William Street in Kampala. Its monthly sales are Shs 12.5 million but it has not registered for VAT after 12 months of trading. What options are open to the Commissioner General of URA?
- (a) Advise the company to pay VAT in future.
  - (b) Impose tax equivalent to 6 months sales.
  - (c) Compulsorily register the company and demand VAT due.
  - (d) Compulsorily register the company and impose a flat penalty of Shs 450,000 per month.
- (x) Yume Ltd is making payments of Shs 200 million (US \$ 102,564) to a Swedish Company which installed a microwave on its premises in Jinja. How much should Yume Ltd pay to URA as withholding tax on the transaction?
- (a) Shs 60 million.
  - (b) Shs 75 million.
  - (c) Shs 30 million.
  - (d) Zero since withholding tax is not applicable.

- (xi) Mwine has a small shop whose turnover for the 2003 year of income was Shs 49 million. What tax should be imposed on him?
- (a) Presumptive tax of Shs 500,000.
  - (b) Income tax on chargeable income for the year.
  - (c) Shs 490,000.
  - (d) Shs 14.7 million.
- (xii) Ninya and Mwanga Company has been trading for the last 10 years. The company is loss making but has paid Shs 4 million as provisional tax over the years to 31 December 2002. What should the company's tax consultant include in 2003 tax return?
- (a) Tax payable of Shs 4 million.
  - (b) Loss for the year and that for previous years and no tax payable/claimable.
  - (c) Accumulated tax losses and tax loss for the year only.
  - (d) A return of income with taxable loss and overpaid tax over the 10 years.
- (xiii) Musa Flower Exporters Ltd imported a Landcruiser Station Wagon worth Shs 60 million and paid duties at Malaba Border. Included in the duties was withholding tax of Shs 490,000 and VAT of Shs 1,200,000. The company also paid excise duty of Shs 2 million and penalties of Shs 1.5 million for under declaration. How should the expenses incurred be treated?
- (a) Expense them in their income statement.
  - (b) Capitalise all expenses incurred.
  - (c) Claim for withholding tax paid in their annual return and capitalise all the other expenses to claim wear and tear allowances on the vehicle.
  - (d) Capitalise all the expenses with the exception of withholding tax and penalties.
- (xiv) Which of the following is not an exempt supply?
- (a) The supply of exports of goods and services.
  - (b) The supply of postage stamps.
  - (c) The supply of insurance services.
  - (d) The supply of goods as part of the transfer of a business as a going concern by one taxable person to another taxable person.
- (xv) Which of the following supplies is liable to VAT?
- (a) Hire or loan of goods to someone.
  - (b) Goods drawn from a shop for personal use.
  - (c) Commission received in return for selling something on behalf of someone else.
  - (d) All the above.

- (xvi) Which of the following provisions is not meant to assist small taxpayers to account for VAT?
- (a) Accounting for VAT on cash basis.
  - (b) Issuance of simplified tax invoices to VAT registered customers subject to certain conditions.
  - (c) Special schemes to help assist taxpayers account for VAT.
  - (d) Accounting for VAT on a quarterly basis.
- (xvii) Which of the following is a supply of a good under the VAT Statute?
- (a) Supply of electrical energy.
  - (b) Supply of construction services.
  - (c) Supply of accountancy services.
  - (d) Supply of medical services.
- (xviii) Benard Musinguzi incurred start up costs of Shs 15,000,000 to start his business in July 2003. He is expected to expense the start up costs over ... years.
- (a) 20.
  - (b) 3.
  - (c) 4
  - (d) 5.
- (xix) Mr. Farmer incurred farm works expenditure of Shs 35,000,000 during the year ending 31 December 2002, when he was starting his farming business. Compute the capital deductions Mr. Farmer is expected to claim for the year of income ended 31 December 2002.
- (a) Shs 8,750,000.
  - (b) Shs 1,750,000.
  - (c) Shs 12,250,000.
  - (d) Shs 7,000,000.
- (xx) Define the term “tax period” as used in the Valued Added Tax Statute 1996 as amended.
- (a) The accounting period.
  - (b) The year commencing 1 July and ending on 30 June.
  - (c) A calendar month.
  - (d) The period from 15<sup>th</sup> of one month to 14<sup>th</sup> of the following month.

**SECTION B****Question 2**

DC Ltd has been trading since January 2002 and today 30 June 2004, they have prepared an 18 month income statement for the period ended 30 June 2004 as follows:

- (a) Income from rental of a property on Plot 200A Acacia Avenue, Kampala of Shs 250 million. It cost the company Shs 1.5 billion.
- (b) Sales of the agricultural products from Kigo Farm of Shs 150 million. Farm works utilised, cost Shs 200 million at the beginning of the year while the operational expenditure was Shs 76 million.
- (c) Received Shs 27 million as legal compensation after a long battle with a competitor. This amount had been subject of an out of court settlement.
- (d) Has received Shs 200 million as estimated commission fees for the period January 2004 to December 2004. The Chief Accountant does not know how to treat deferred income.
- (e) Other than the above, the company's mainstream business which is merchandizing soft drinks posted the following results:

	<b>Notes</b>	<b>Shs '000</b>	<b>Shs '000</b>
Gross profit for the 18 months to June 2004			<b>450,000</b>
Depreciation	(i)	125,000	
Provision for bad debts	(ii)	29,000	
Insurance premium		30,000	
Motorcycle write off		2,500	
Thefts and shortages		41,000	
Non-current assets purchases	(iii)	24,000	
Accident compensation		5,000	
Other operational expenses		150,000	

**Note:**

- (i) Of the depreciation figure, 50% is leasehold amortisation. The cost base of the leasehold was established to be Shs 400 million and the lease period to be 15 years.
- (ii) Shs 29 million is the additional provision for the year. In addition to this, there was a recovery of bad debts amounting to Shs 130 million, of which Shs 70 million was disallowed in 2002 tax computation. The bad debts recovered were not posted in the accounts.
- (iii) Non-current assets purchases included only assets whose cost was below Shs 100,000. Other non-current assets purchases were as follows:
  - Computers and software link for Kampala operations of Shs 300 million.
  - Landcruiser for the managing director at Shs 70 million.
  - Double cabin Toyota pick-up for Shs 55 million.

(iv) Tax written down values at 31 December 2002 were:

Class	Shs'000
I	45,000
II	119,900
III	640,000
IV	51,000

**Required:**

Compute DC's chargeable income and the tax payable for the 18 months to June 2004.

**(20 marks)**

**Question 3**

- (a) Kaisha has a small business in Kikuubo to supplement her employment income. Following her interview with the District Revenue Officer of Bwaise, below are her key transactions for the year ended 31 December 2003:

**Employment:**

- (i) Salary from her consultancy job with Bwaise University was Shs 500,000 per month. She is also provided with a Flat in the University with a market value of Shs 400,000 per month.
- (ii) She was paid a performance bonus of Shs 1,500,000 and Shs 3,500,000 mileage for her business trips to the field at the rate Shs 1,200 per kilometre.
- (iii) Her three year contract with Bwaise University ended on 30 December 2003 and was paid a gratuity of Shs 5,000,000 on 31 December 2003. On the same day, she successfully negotiated a renewal of her contract for the next three years.
- (iv) She is provided with a telephone by the University whose monthly bill is Shs 100,000. The Revenue Officer has analysed the telephone calls print out and it was agreed with her that 75% of the bills are personal.
- (v) Her employer paid Shs 2,300,000 to Kombe International School for her two children as an educational loan. The loan was subsequently written off on 31 December 2003.
- (vi) As an exception, she was paid medical allowance of Shs 450,000 per month and a thirteenth cheque of Shs 500,000 in December 2003.

**Note:** PAYE was only deducted on Shs 500,000 monthly basic pay.

**Business:**

- (b) (i) The monthly turnover from her Kikuubo business is on average Shs 45,000,000 and at no point during the year did it exceed Shs 50,000,000.
- (ii) The gross margin on her sole commodity sold i.e. supermatch cigarettes is 20% of the sales revenue.

- (iii) A trading loan of Shs 10 million which her business owed the University was written off during the year.
- (iv) Other payments made in the year 2003 were as follows:
  - Rent of Shs 500,000 per month.
  - Salaries of Shs 36 million.
  - VAT penalties of Shs 4.6 million and unpaid output VAT of Shs 9.7 million. This was due to the fact she had not charged VAT on sales made to the Uganda Peoples Defence Forces.

**Required:**

Compute her tax payable for the year 2003.

**(20 marks)**

**Question 4**

Alfred Kabuzi is a sole proprietor in Mbale Market. He properly registered his shop for VAT. He maintains a cash register from which the following sales were extracted for the month of May 2004:

<b>Sales</b>	<b>Shs</b>
Maize flour	500,000
Fresh tomatoes	400,000
Cabbages	600,000
Stationery	1,000,000
Candles	200,000
Blue Band	350,000
Used cookers and fridges	1,500,000
Proceeds from sale of his 10 year old pick-up	2,500,000
Sale of drugs	1,200,000
Rent from his land and residential houses	700,000
Goats from his Bubulo Farm	2,900,000

He had also made numerous payments during the month as follows:

	<b>Shs</b>
Rent for the shop	1,900,000
Used fridges and cookers	2,400,000
Purchase of double cabin pick-up for business	5,000,000
Fuel for his pick-up	200,000
Motor vehicle repair for wife's saloon car	150,000
Lubricants for pick-up	70,000
Lubricants for his wife's saloon car	50,000
Reams of paper, pens and exercise books	450,000
Travel ticket for his son to South Africa	800,000

**Notes:**

- Included in his cashbook is Shs 50 million from Uganda Government as compensation for his animals that were lost during NRM/A liberation war.



Associated with this are related costs namely payment of Lawyers fees of 10% of the amount received, his accommodation in a Kampala Hotel of Shs 300,000 and arbitrators fees of Shs 2,000,000.

- The sales figures are VAT inclusive while the purchases are VAT exclusive but are supported with proper tax invoices, were appropriate.

**Required:**

- (a) Determine the amount payable/claimable from URA by Alfred Kabuzi stating any assumptions made. **(15 marks)**
- (b) What would be the VAT payable (claimable) if he had an offset of Shs 200,000 at the end of April 2004? **(5 marks)**
- (Total 20 marks)**

**SECTION C**

**Question 5**

The Government of Uganda expects to finance 52% of her budget of 2003/2004 and 54% of 2004/2005 from internally generated revenue. With donors contributing the difference, it is imperative that Uganda needs to improve her tax base and other revenue sources.

**Required:**

- (a) Briefly explain four non-tax revenues in Uganda. **(4 marks)**
- (b) Why does Uganda have a narrow tax base? **(6 marks)**
- (c) How can Uganda widen her tax base? **(6 marks)**
- (d) Give two merits and two demerits of taxation financing. **(4 marks)**
- (Total 20 marks)**

**Question 6**

- (a) Explain the following:
- (i) Whole time service director.
  - (ii) Exempt organisations under the Income Tax Act.
  - (iii) Resident when applied to an individual.
  - (iv) Self-assessment system.
- (12 marks)**
- (b) Define the term “customs union”. Give three benefits and three demerits that Uganda may derive from being a member of East African Customs Union. **(8 marks)**
- (Total 20 marks)**

**TAX RATES****RESIDENT INDIVIDUAL INCOME TAX RATES**

<b>Chargeable Income</b>	<b>Tax Rate</b>
Not exceeding Shs. 1,560,000	Nil
Exceeding Shs. 1,560,000 but not exceeding Shs. 2,820,000	10% of the amount by which chargeable income exceeds Shs 1,560,000
Exceeding Shs. 2,820,000 but not exceeding Shs. 4,920,000	Shs. 126,000 plus 20% of the amount by which chargeable income exceeds Shs 2,820,000.
Exceeding Shs 4,920,000	Shs 546,000 plus 30% of the amount by which chargeable income exceeds Shs 4,920,000.

**SMALL BUSINESS TAXPAYERS TAX RATE**

<b>Gross Turn Over</b>	<b>Tax Payable</b>
Where gross turnover of a taxpayer does not exceed Shs. 5,000,000 a year.	Nil.
Where gross turnover of a taxpayer exceeds Shs. 5,000,000 but does not exceed Shs. 20,000,000 a year.	Shs 100,000.
Where gross turnover of a taxpayer exceeds Shs. 20,000,000 but does not exceed Shs. 30,000,000 a year.	Shs. 250,000 or 1% of gross turnover, whichever is the lower.
Where gross turnover of a taxpayer exceeds Shs. 30,000,000 but does not exceed Shs. 40,000,000 a year.	Shs. 350,000 or 1% of gross turnover, whichever is the lower.
Where gross turnover of a taxpayer exceeds Shs. 40,000,000 but does not exceed Shs. 50,000,000 per annum.	Shs. 450,000 or 1% of gross turnover, whichever is the lower.