

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

CPA(U) EXAMINATIONS

LEVEL TWO

PRINCIPLES OF TAXATION-PAPER 8

TUESDAY, 13 DECEMBER 2005

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 11.
7. Please read further instructions on the answer book.

SECTION A**Question 1**

- (i) Which of the following statements is false about a valid objection to an income tax assessment?
- (a) It is made within 60 days from the date of service of notice of assessment.
 - (b) It is made in writing.
 - (c) It states the grounds of objection.
 - (d) It is made within 45 days from the date of service of notice of assessment.
- (ii) Who of the following persons are obliged to submit a return of income to Uganda Revenue Authority?
- (i) Persons for whom some taxes are recovered under withholding tax.
 - (ii) Resident individuals who have not made any profit in the year of income.
 - (iii) Resident individuals assessable under the Presumptive Tax System.
 - (iv) Resident individuals who use cash accounting and their income is below Shs 200 million.
- (a) (i), (iii) and (iv).
 - (b) (ii) and (iv).
 - (c) (iii).
 - (d) (i).
- (iii) Which of the following is exempt from income tax?
- (a) Proceeds from the disposal of trading stock.
 - (b) Interest income from Government of Uganda Treasury Bills.
 - (c) The value of a gift in the course of doing business.
 - (d) Any capital gain that is not included in business income.
- (iv) Mr. Katula a trader received a VAT assessment from Uganda Revenue Authority (URA) demanding tax liabilities of Shs 45,000,000 on 1 March 2005. By which date should he object to URA if he is not satisfied with the assessment?
- (a) 30 March 2005.
 - (b) 15 April 2005.
 - (c) 31 March 2005.
 - (d) 30 April 2005.

- (v) Wamasali Ltd made a provisional return for Shs 200 million. It consequently paid the taxes by the end of the year. On submitting the final return by the due date, the company returned Shs 300 million as taxable income. How much money should the company pay to URA in form of taxes and penalties (if any) both inclusive under the Income Tax Act?
- (a) Shs 4,200,000.
 - (b) Shs 30,000,000.
 - (c) Shs 34,200,000.
 - (d) Shs 36,000,000.
- (vi) An investment trader can apply to extend his application to continue trading as one for an additional period of:
- (a) 2 years.
 - (b) 1 year.
 - (c) 4 years.
 - (d) 5 years.
- (vii) Which of the following is true about a resident professional who is not VAT registered?
- (a) All payments made to him / her should be less 6% WHT.
 - (b) All payments made to him / her should be less 30% income tax.
 - (c) He / she should be required to register for VAT and charge VAT on his / her services.
 - (d) He / she should submit output VAT to URA on payments made to him / her.
- (viii) Which of the following is true about Domestic VAT?
- (i) Was introduced effective 1 March 2001?
 - (ii) Charged on all imports by taxpayers above Shs 4 million.
 - (iii) Charged on goods imported by non-registered taxpayers above Shs 4 million.
 - (iv) Charged on all goods imported by non-registered taxpayers.
 - (a) (i), (ii) and (iii).
 - (b) (i) and (ii).
 - (c) (i), (ii) and (iv).
 - (d) (i) and (iii).
- (ix) Mr. Maumbe is a trader who qualifies to pay domestic VAT. He imported goods with C.I.F of Shs 4,550,000 in August 2005. How much tax is he to pay in form of domestic VAT?
- (a) Shs 819,000.
 - (b) Shs 941,850.
 - (c) Shs 773,500.
 - (d) Shs 889,525.

- (x) Newman purchased goods worth Shs 7,080,000, VAT inclusive from a registered trader. She sells her goods at a profit of 25%. What is the minimum amount that she should charge to a buyer, VAT inclusive?
- (a) Shs 8,354,400.
 - (b) Shs 10,443,000.
 - (c) Shs 8,850,000.
 - (d) Shs 8,496,000.
- (xi) A CPA student made the following notes in preparation for the Principles of Taxation examination:
- Is organized under the laws of Uganda.
 - Is operated for the principal purpose of providing retirement benefits to resident individuals.
 - Has its management and control exercised in Uganda at any time during the year of income.
- The notes above refer to a resident:
- (a) trust.
 - (b) retirement fund.
 - (c) company.
 - (d) partnership.
- (xii) A trade agreement between countries that creates close economic and political relationship among them is known as:
- (a) Preferential Trade Area.
 - (b) Economic Union.
 - (c) Customs Union.
 - (d) Trade Market.
- (xiii) What do the following statements relate to under the Income Tax Act?
- The amount of any gain, as determined under Part VI, which deals with gains and losses on disposal of assets, derived, by a person on the disposal of a business asset.
 - Any amount derived by a person as consideration for accepting a restriction on the person's capacity to carry on business.
 - The gross proceeds derived by a person from the disposal of trading stock.
- (a) Business income.
 - (b) Employment income.
 - (c) Property income.
 - (d) None of the above.
- (xiv) Which of the following are not collected by Uganda Revenue Authority?
- (a) Property rates.
 - (b) Stamp duty.
 - (c) Import duties.
 - (d) Withholding tax.

- (xv) Brian Wantate had rental income of Shs 150,000 per month for the year ended 31 December 2004. How much rental tax should he pay to URA for the year?
- (a) Shs 288,000.
 - (b) Shs 360,000.
 - (c) Nil
 - (d) Shs 48,000.
- (xvi) Which of the following supplies are zero-rated?
- (a) Pesticides.
 - (b) Milk.
 - (c) Maize flour.
 - (d) Medical equipment.
- (xvii) Which of the following form part of taxable employment income?
- (a) Pension received by an employee from a registered fund.
 - (b) Life insurance premium paid by a taxable employer.
 - (c) Payment in respect of change in employment terms.
 - (d) Discharge or re-imbursement of medical expenses.
- (xviii) What is the meaning of the term “services” under the VAT Act?
- (a) An intangible supply.
 - (b) Any thing which is not a good or money.
 - (c) Any thing which is not a good.
 - (d) An import or export of services.
- (xix) Kibuuko Traders is a small taxpayer. What is its income tax on an annual turnover of Shs 50 million?
- (a) Shs 500,000.
 - (b) Shs 450,000.
 - (c) Shs 200,000.
 - (d) Shs 9,000,000.
- (xx) Which of the following statements is true about returns to be submitted by an individual in business with an annual turnover of over Shs 500 million?
- (a) Four provisional returns and one final return per annum.
 - (b) Two provisional returns and one final return.
 - (c) One provisional and one final return.
 - (d) No return since this is an individual.

SECTION B**Question 2**

(a) Explain the meaning of the following terms:

- (i) Balancing charge. **(2 marks)**
- (ii) Balancing deduction. **(2 marks)**
- (iii) Initial allowance. **(2 marks)**
- (iv) Industrial building deduction. **(2 marks)**

(b) Tweheyo Limited brought into use their brick laying factory in Mbarara on 1 January 1996. The factory building had cost Shs. 20,000,000 to construct. On 1 January 2004, the whole business of Tweheyo Limited was transferred to Kapo Limited, as a going concern. Besides all other assets, the factory building was acquired for Shs. 40,000,000.

Required:

Determine the Industrial Building Deduction due to Kapo Limited for the year 2004 (Ignore the effect of other allowances).

(2 marks)

(c) Masaka Enterprises Limited decided to discontinue its manufacturing operations based in Masaka in 2004. The following information relates to the year ended 31 December 2004:

(i) Written down values of assets brought forward for income tax purposes:

	Shs '000
Class I	175,000
Class II	-
Class III	180,000
Class IV	380,000

(ii) Additions during the year:

	Shs '000
Prado motor vehicle	40,000
Lorry	60,000
Computers	20,000
Furniture	12,000
Tools	800

(iii) Disposal proceeds during the year:

	Shs '000
Motor vehicles	60,000
Computers	55,000
Plant and Machinery	80,000
Furniture	18,000

(iv) The rest of the assets remaining unsold as at 31 December 2004 were worthless.

- (v) The Prado was used by the Managing Director throughout the year. He used it for his private affairs 40% of the time.
- (vi) The profit for 2004 before the above transactions has been agreed with URA at Shs. 150 million.

Required:

Determine the taxable profit (loss) for Masaka Enterprises Limited for the year ended 31 December 2004 and state the tax due.

(10 marks)**(Total 20 marks)****Question 3**

Mr Magombe was employed by a micro-finance company from 1 July 2004 as a Finance Manager.

He is entitled to the following monthly emoluments:

- Basic salary of Shs 3,450,000.
- Other allowances of Shs 1,000,000.
- Entertainment allowance of Shs 400,000.

He is also entitled to the following benefits:

- A fully furnished house in Ntinda Ministers' Village.
- Fully serviced car for both official and private use.
- Medical cover for self, spouse and a maximum of six children.
- Gratuity of 20% of his annual basic pay at the end of each year successfully served.

The company incurred the following in relation to Mr. Magombe:

- (i) Purchased a Nissan station wagon at Shs 50 million, which he uses for both official and personal purposes. He used the car throughout the year except during April 2005 when he parked it at the office and went for his annual leave to Japan. He contributed Shs 50,000 per month towards the maintenance of the car.
- (ii) Magombe was given a company loan on 1 January 2005 of Shs 30,000,000 to complete his house in Kabalagala at an interest rate of 12% per annum.

The annual statutory rates given by Bank of Uganda were as follows:

July 2004	20%
December 2004	25%
April 2005	25%

- (iii) The company paid medical insurance of Shs 4,500,000 to AAR to cover Mr. Magombe and his family for the year to 30 June 2005.

Other sources of income for Mr. Magombe included the following:

- Rental income from 4 houses in Muyenga of Shs 4,000,000 per month, for which he incurred the following monthly expenses:

	Shs
Electricity bills per month	600,000
Water per month	250,000
Salary to attendants per month	250,000
Boundary wall	2,000,000
- Interest income from Standard Chartered Bank Kampala Shs 4,000,000 net.
- While in Japan, he was employed for one month and earned the equivalent of Shs 10,000,000, which was taxed at 20% in Japan.

Required:

Compute Mr. Magombe's taxable income for the year ended 30 June 2005 and tax payable thereon.

(20 marks)

Question 4

Mr Walusimbi, a prominent trader in Kampala started business on 1 July 2005. After establishing that his turnover will be Shs 200 million per annum, he registered for VAT on 1 November 2005. His accountant has consulted you on issues relating to the transactions for the month of November 2005. During the month of November, the following transactions took place:

- Imported goods from Dubai whose customs value for VAT was Shs 23,450,000 and sold merchandise from the shop for cash Shs 12,000,000.
- Sold 100 cows that were on his farm in Kalisiizo for Shs 465,000 per cow.
- Paid Shs 9,000,000 to Samaki, Certified Public Accountants which designed the accounting system for his business.
- He paid Shs 16,400,000 to Trancargo Ltd, a transporter, for transporting his goods from Mombasa to Kampala.
- He sold some of his goods to Rwanda Telcom Ltd, a telecommunication company in Kigali Rwanda of Shs 34,765,000 by cash.
- He bought office stationery for Shs 1,500,000.
- During the month of July 2005. He sold goods worth Shs 20,000,000, VAT exclusive to Mwana Ltd on credit. He was served with notice in November 2005 from the High Court that Mwana Ltd has been declared bankrupt and insolvent before receiving his payment.
- Sold goods worth Shs 17,000,000 to Muko Industries Ltd on credit.
- Local purchases of Shs 24,000,000 were made.
- Returned some of the goods worth Shs 2,400,000 to suppliers.
- Rwanda Telcom Ltd returned some defective goods amounting to Shs 3,400,000.

12. Fire gutted the stores and stock worth Shs 18,000,000 was destroyed. The insurance company agreed to pay up to the maximum of Shs 13,500,000 only.

He further made the following payments during the month of November 2005:

- Electricity bills Shs 350,000.
- Water and sewerage Shs 400,000.
- Medical bills for staff Shs 2,000,000.
- Salaries Shs 45,000,000.
- Telephone bills Shs 435,000.
- Repairs for the 3 cars amounting to Shs 3,435,000. The cars are in the names of the company.

All sales are VAT exclusive but all purchases and bills paid are VAT inclusive except where specifically stated.

Required

- (a) Compute the input and output tax to be accounted for to URA. State any necessary assumptions / reasons for your treatment of items. **(14 marks)**
- (b) Advise on the treatment of the supply made to Mwana Ltd. **(3 marks)**
- (c) Compute VAT payable / claimable and state the due date. **(3 marks)**
- (Total 20 marks)**

SECTION C

Question 5

- (a) Explain the following:
- (i) Taxable capacity. **(4 marks)**
 - (ii) The problems of justice in taxation. **(5 marks)**
- (b) Define the following:
- (i) Short-term resident individual. **(2 marks)**
 - (ii) Resident company. **(3 marks)**
- (c) Give three advantages and three disadvantages of the customs union to Uganda. **(6 marks)**
- (Total 20 marks)**

Question 6

During the budget speech on 15 June 2005, Mr. Walugembe heard the following words being said by the Minister of Finance:

“Uganda is a growing economy with a small tax base. We should struggle so hard and widen our tax base. There is no way we can run away from taxes. For this country to grow, each and every individual should pay tax. We have a lot to cover, as government; we need money to do this. The major source of revenue is definitely taxation, ladies and gentlemen”.

Required:

Explain to Mr. Walugembe the following:

- (a) Why people in Uganda should pay taxes to government. **(5 marks)**
 - (b) Five other sources of revenue to the Government of Uganda, giving examples of each. **(5 marks)**
 - (c) Adam Smith’s cannons of taxation. **(6 marks)**
 - (d) The case for and against the suspension of graduated tax in Uganda. **(4 marks)**
- (Total 20 marks)**

TAX RATES**RESIDENT INDIVIDUAL INCOME TAX RATES**

Chargeable Income	Tax Rate
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.

NON-RESIDENT INDIVIDUAL INCOME TAX RATES

Chargeable Income	Tax Rate
Not exceeding Shs. 2,820,000	10%
Exceeding Shs. 2,820,000 but not exceeding Shs . 4,920,000	Shs 282,000 plus 20% of the amount by which chargeable income exceeds Shs 2,820,000
Exceeding Shs 4,920,000	Shs 702,000 plus 30% of the amount by which chargeable income exceeds Shs 4,920,000.

SMALL BUSINESS TAXPAYERS TAX RATE

Gross Turn Over	Tax Payable
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.