

# THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

*A Committee of Council of ICPAU*

## CPA (U) EXAMINATIONS

### LEVEL TWO

### TAXATION - PAPER 11

**THURSDAY, 10 DECEMBER 2009**

#### INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours 15 minutes.**  
The first 15 minutes of this examination have been designated for reading time. You may not start to write your answer during this time.
2. Section **A** has **one** compulsory question carrying 30 marks.
3. Section **B** has **three** questions and only **two** questions are to be attempted. Each question carries 20 marks.
4. Section **C** has **three** questions and only **two** questions are to be attempted. Each question carries 15 marks.
5. Tax rates are provided on page 10.
6. Please read further instructions on the answer book.

**© 2009 Public Accountants Examinations Board**

## SECTION A

### Question 1

Nguvu Manufacturers Limited is a manufacturing company registered in Uganda with its principal business of manufacturing bags. The factory plant is located in Njeru and the company is registered for all Ugandan taxes. The following is its detailed statement of comprehensive income for the period ended 31st December 2008.

#### Statement of Comprehensive Income for the Year Ended 31 December 2008

	Notes	Shs '000'
Income:		
Turnover		920,300
Less cost of sales	1	<u>523,700</u>
Gross profit		396,600
Unrealized gain		<u>35,000</u>
Total gross profit		<u>431,600</u>
Expenditure:		
Administration costs (see below)		317,020
Finance costs	2	<u>7,500</u>
Total expenditure		<u>324,520</u>
Net profit before tax		<u>107,080</u>
Administration costs:		
Personnel	3	139,800
Utilities	4	26,550
Life insurance premium		18,510
Office repairs and maintenance		10,210
Motor vehicle expenses		12,300
Printing and stationery		20,400
Professional fees	5	15,700
Depreciation	6	50,070
Donations	7	5,200
Office insurance		7,960
Bad debts	8	<u>10,320</u>
		<u>317,020</u>

Notes to the accounts:

1. Cost of Sales: This includes Shs 5 million penalty imposed by government for under-declaration of the value of imported stationery.
2. Finance costs relate to interest on a loan from a related entity which has now made foreign debt to equity ratio of 3:1.

3. Personnel costs include the following:

**Shs '000'**

NSSF employer contribution	25,600
PAYE on directors' fees	3,100
Relocation costs for staff	2,545
Staff travel to and from their homes to place of work	4,600
Staff travel and accommodation out of workstations.	6,560

4. Included in utilities is a water bill for Shs 1.5 million for one of the director's residence but paid for by the company.
5. Professional fees is a provision for expenses to be incurred on a feasibility study to be carried out next year of income for a new manufacturing plant.
6. Included in depreciation is a leasehold amortization for 5 years premises on which the factory was built. The property cost Shs 150 million in 2000 with a remaining lease period of 40 years. The policy of the company is to depreciate leasehold assets over their life time.
7. Expenditure on donations includes the following:

**Shs '000'**

Registered political parties	1,750
Uganda Federation of Employers Association	500
Uganda Golf Club	950
Uganda Manufacturers Association	<u>2,000</u>
	<u>5,200</u>

8. Bad debts include:

**Shs '000'**

Trade bad debts written off	2,100
Sale of company car to staff	3,120
Provision for doubtful debts	4,050
Provision for other trade debtors	<u>1,050</u>
	<u>10,320</u>

Additional information related to non-current assets:

- (a) The company's depreciable assets were as follows:

Written down value as at 31 December 2007

	<b>Shs '000'</b>
Class I	30,000
Class II	200,000
Class III	52,000
Class IV	20,000

Additions:

	<b>Cost Shs '000'</b>
Office furniture	32,000
Computers	15,000
Computer software	60,000
Motor vehicle, pick-up 3 tonnes	45,000
Motor vehicle, Land Cruiser for the managing director at	290,000

A Mitsubishi truck, 9 tonnes, was disposed of during the year for Shs 12.5 million.

- (b) The existing factory building cost Shs 110 million and was constructed in January 2000 and first brought to use on 1 July 2001. During the year under consideration, an extension to the factory building was constructed at a cost of Shs 200 million and brought to use on 1 October 2008.
- (c) The agreed adjusted loss for the year ended 31 December 2007 was Shs 3.65 million.

**Required:**

- (a) Compute the chargeable income or tax loss position for Nguvu Manufacturers Limited for the year ended 31 December 2008.

**(26 marks)**

- (b) State the circumstances under which a taxpayer is deemed to have disposed of an asset.

**(4 marks)**

**(Total 30 marks)**

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

Zulu, a South African citizen, is employed by Zambi Uganda Limited as company secretary, effective 1 July 2008. He was resident in Uganda for a period of 172 days. The terms of his employment contract include the following:

- (i) Monthly salary, Shs 8 million per month.
- (ii) Provision of accommodation in a rented house at Buziga at Shs 1.5 million per month.
- (iii) A bonus of Shs 6 million per annum.
- (iv) Provision of a Toyota Prado motor vehicle by the company which was bought on 1 March 2009 at Shs 60 million.
- (v) Medical insurance to AAF of Shs 1 million per annum for self and immediate family members.
- (vi) The company pays for his subscription to the Institute of Corporate Governance up to a limit of Shs 70,000 per annum.
- (vii) Loan facilities from the company not exceeding Shs 30 million at an interest rate of 7% per annum. The loan would be payable in 3 years time.

During the year the following transactions took place:

- (i) The company paid for his subscription to the Institute of Corporate Governance Shs 900,000.
- (ii) The company paid for his accommodation at Shs 1.5 million per month.
- (iii) Zulu took a furniture loan of Shs 25 million on 1 April 2009.
- (iv) By 30 June 2009, Zulu had privately used the car during that year for approximately 100 days. He had also paid Shs 500,000 towards expenses related to the car.
- (v) The company paid school fees for his children Shs 4.5 million.
- (vi) Utility bills to the tune of Shs 300,000 per month were paid for him by the company.
- (vii) Zulu received alimony from his ex-wife of Shs 20 million on 31 May 2009.

**Note:** Assume that the statutory rate of interest as at 1 July 2008 was 10%.

**Required:**

- (a) Compute Zulu's chargeable employment income for the year ended 30 June 2009. Comment on any information not used.  
(14 marks)
- (b) Compute the tax liability for the period ended 30 June 2009.  
(3 marks)
- (c) Give any **three** circumstances under which income is exempt from tax as provided for in the Income Tax Act.  
(3 marks)

**(Total 20 marks)**

**Question 3**

Manzi Enterprises Ltd commenced business in retailing assorted merchandise in February 2009. The company has not registered for VAT but deals in VAT chargeable supplies. The company's operating statement for the month of March 2009 is as provided below:

	<b>Shs '000'</b>
Sales:	
VAT standard rated	80,500
VAT zero rated	25,600
VAT exempt	<u>30,400</u>
	136,500
Purchases	(65,300)
Opening inventory	(10,200)
Closing inventory	15,700
Other expenses on:	
Standard rated sales	(36,100)
Zero rated sales	(12,000)
Exempt sales	(14,300)
Overheads	<u>(7,500)</u>
Net profit	<u>6,800</u>

**Additional notes:**

- (i) The purchases figure is made up of 70% VAT standard rated, 20% VAT zero rated and the remainder VAT exempt.
- (ii) All VAT exempt purchases were sold during the period.
- (iii) Sales are VAT inclusive and purchases are VAT exclusive.
- (iv) Expenses are VAT exclusive and the company paid VAT on all other expenses.

**Required:**

- (a) Compute Manzi Enterprises Ltd's VAT liability for the month of march 2009.

**(10 marks)**

- (b) Briefly explain any errors arising from input VAT that Manzi Enterprises Ltd is likely to commit.

**(5 marks)**

- (c) Give any **five** transactions listed under exempt supplies.

**(5 marks)****(Total 20 marks)**

**Question 4**

- (a) Mukasa Enterprises Uganda Ltd deals in cosmetics on Luwum Street, Kampala, with branches in Kenya, Rwanda and Tanzania. For the year of income 2008, Mukasa Enterprises Uganda Ltd had a chargeable income of Shs 150 million. The following additional information is also relevant:

- Included in the above chargeable income is Shs 35 million derived from sales through the Kenyan branch of which tax of Shs 14,875,000 had been paid.
- The Rwanda branch returned sales of Shs 27 million on which tax of Shs 6,750,000 had been paid.
- Interest on deposits with Standard Bank in Tanzania was Shs 15 million. No tax is payable on the interest earned from the deposits in Tanzania.

**Required:**

Determine the amount of foreign tax credit allowed from the Kenyan, Rwanda and Tanzanian branches.

**(5 marks)**

- (b) Zambi Technology Ltd is a company registered in Zambia dealing in computers and accessories. The company has a branch in Uganda, registered as Zambi Technology Ltd – Uganda Branch.

The following transactions from the branch relate to the year of income ended 30 June 2009:

1 July 2008:	<b>Shs million</b>
Total cost base of assets	750
Total liabilities	340
30 June 2009:	<b>Shs million</b>
Total cost base of assets	680
Total liabilities	295

The net profit of the branch for the year of income calculated according to generally acceptable accounting principles was Shs 170 million.

**Required:**

Determine the repatriated income of the branch and the tax there on.

**(9 marks)**

- (c) Commercial Plaza is a commercial building in Jinja that was constructed at Shs 850 million and put to first use in January 2001. The net book value at the point of its disposal on 31 December 2008 was Shs 465 million. The proceeds from sale were Shs 950 million. The tax written down value as at 1 January 2008 on the commercial building was Shs 580 million.

**Required:**

Determine the tax implications of the sale of the commercial property above.

**(6 marks)**

**(Total 20 marks)**

**SECTION C**

**Question 5**

- (a) The Income Tax Act provides for double taxation agreements between the government of Uganda and other foreign governments.

**Required:**

Define the term 'double taxation agreement' and identify the factors that should be considered in determining the location of a company in a double taxation agreement zone.

**(4 marks)**

- (b) The East African countries have come together to facilitate social integration, a common market, a monetary union and a political federation:

**Required:**

- (i) Briefly explain the meaning of the term 'customs union' clearly describing the three classes of tariffs under a customs union.

**(4 marks)**

- (ii) Discuss any **four** challenges of a customs union.

**(4 marks)**

- (c) Discuss **three** ingredients of a good tax system.

**(3 marks)**

**(Total 15 marks)**

**Question 6**

- (a) Briefly explain the following terms under the Income Tax Act:

- (i) Resident individual.

**(3 marks)**

- (ii) Resident company.

**(3 marks)**

- (b) Distinguish between the requirements for payment of provisional tax for an individual from that of a company as per the Income Tax Act.

**(4 marks)**

- (c) Explain the determinants of existence of employer-employee relationship in order to enforce pay as you earn (PAYE) under the Income Tax Act.

**(5 marks)**

**(Total 15 marks)**



**Question 7**

- (a) Distinguish between a finance lease and an operating lease for income tax purposes clearly discussing the resulting tax implications.

**(6 marks)**

- (b) Explain what is meant by a substituted year of income and outline the procedures a taxpayer has to follow to apply for a substituted year of income.

**(3 marks)**

- (c) Discuss the objections and appeals procedures under the income tax laws of Uganda.

**(6 marks)**

**(Total 15 marks)**

## TAX RATES

### Resident Individual Income Tax Rates

Annual chargeable Income	Rate of Tax
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*

Annual chargeable Income	Rate of Tax
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 Rates

Gross Turnover	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 plus 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 plus 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 a year.	Shs 450,000 plus 1% of gross turnover, whichever is the lower.