

PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of Council of ICPAU

CPA(U) EXAMINATIONS

LEVEL TWO

TAXATION - PAPER 11

FRIDAY, 30 NOVEMBER 2012

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 9.
6. Write your answer to each question on a fresh page in your answer booklet.
7. Please read further instructions on the answer booklet, before attempting any question.

SECTION A

This section has one compulsory question to be attempted.

Question 1

Spirits Distillers Ltd is a resident company in Uganda located in Mukono municipality. It deals in the distillation and distribution of spirits across the country. The company's statement of comprehensive income for the year ended 31 December 2011 is provided below:

	Notes	Shs '000'
Turnover		16,200,500
Cost of sales		<u>(8,500,000)</u>
Gross profit		7,700,500
Other income	1	<u>89,000</u>
Total operating income		7,789,500
Operating costs:		
Distribution costs	2	(1,800,600)
Administration costs	3	(2,409,000)
Finance cost	4	<u>(156,000)</u>
Profit before tax		<u>3,423,900</u>

Notes	Shs '000'
1 Other income:	
Interest earned on Treasury bills net of related expenses	65,200
Unrealised gains on fixed deposit with Standard Bank	21,600
Gains on disposal of distribution truck in Class II	<u>2,200</u>
	<u>89,000</u>
2 Distribution costs include the following among other items:	
Bribes for overloaded distribution trucks	26,500
Billboards for marketing signage	156,400
3 Administration costs include the following among other items:	
Depreciation	165,400
Specific bad and doubtful debts on trade receivables	25,400
Repairs to the CEO's residence not included in his taxable benefits	6,300
Dividends paid	578,900
Life assurance for employees	96,700
Loss on disposal of CEO's old vehicle	5,600
Cost of acquisition of distribution trucks less than 7 tonnes	246,000
4 Finance cost:	
Finance cost of Shs 156 million is interest paid on a loan extended to the directors for personal use and this was not taxed as part of directors' remuneration	

Notes	Shs '000'
5 Details relating to non-current assets:	
Written down values 1 January 2011	
Class I	189,000
Class II	194,000
Class III	256,000
Class IV	74,500
Qualifying cost net of initial allowance of an industrial building acquired in 2003	980,700
Additions to depreciable assets during the year:	
Computers	15,500
Furniture	25,600
Mercedes Benz for CEO	180,000
Cost of new industrial building brought to into use on 1 January 2011	3,080,000
Cost of adjacent land	200,000
Others:	
Disposal of truck in Class II	36,500
Disposal of CEO's old vehicle which had cost Shs 130 million in 2005	28,900
6 Provisional tax paid	689,000
Withholding tax paid	64,300
VAT paid	150,640

Required:

Compute the chargeable income and the tax payable by Spirits Distillers Ltd for the year ended 31 December 2011.

(30 marks)

SECTION B

Attempt two of the three questions in this section.

Question 2

John Kimotho is a Certified Public Accountant from Tanzania and is currently employed by Tropicana Bank as head of finance. The appointment was effective 1 January 2011 with a 3-year contract. As part of his entitlement, he is provided with a vehicle for use on both employment and private duties. The vehicle is a brand new BMW purchased from a car dealer at Shs 50 million. He is charged a monthly fee of Shs 600,000 for the benefit by the employer.

He also earns the following income:

- (i) Basic salary Shs 5 million per month.
- (ii) Children's school fees at International School of Uganda at Shs 5 million per child per annum for his 2 children.
- (iii) His club membership at Kampala Club is also paid for the employer totaling Shs 4 million per annum.
- (iv) He also receives medical allowance of Shs 2 million per month.
- (v) He was reimbursed Shs 4 million being cost of passage to Uganda when taking up his job.
- (vi) He was immediately provided with a house whose estimated market rent is Shs 600,000 per month for which he contributes Shs 100,000 per month.
- (vii) Travel allowance for his spouse of Shs 2 million.
- (viii) The company pays his housekeeper Shs 200,000 per month.
- (ix) He was offered a loan by the employer of Shs 100 million at an interest rate of 5%. He paid back the loan after one year on 31 December 2011. The statutory Bank of Uganda rate applicable over the 12 months was 10%.
- (x) The company contributes 10% of his basic salary towards the National Retirement Fund every month.

Required:

- (a) Compute John's employment income for the year ended 31 December 2011.

(16 marks)

- (b) Compute the PAYE that should be withheld for the year ended 31 December 2011.

(4 marks)

(Total 20 marks)

Question 3

Mundu and Sera are in partnership dealing in transportation business with their firm located in Kampala. Their partnership deed provides for the following:

- Profit sharing ratio of 3:2 respectively.
- Each partner earns interest on capital of 6% per annum based on the opening balance of each partner's capital account.
- Partners' salaries are paid in respect to their profit sharing ratio.
- Partners are charged interest of 3% per annum on any drawings made during the year of income.

The following is the income statement for the partnership for the year ended 31 December 2011:

	Shs '000'	Shs '000'
Income:		
Turnover		350,000
Cost of sales		<u>(106,000)</u>
Gross income		244,000
Expenses:		
Staff salaries	15,000	
Partner's salaries	45,000	
Rent for office space	7,000	
Repairs to office equipment	2,500	
Office upkeep	3,200	
Depreciation	7,600	
Bad debts written off	600	
Donation to charity	900	
Legal and professional fees	6,200	
Rent for Mundu's residence	4,600	
Bribes to traffic officers	700	<u>93,300</u>
Net profit		<u>150,700</u>

Additional information:

(a) Capital accounts:

	Mundu Shs '000'	Sera Shs '000'
Balances 1 January 2011	60,000	52,000
Balances 31 December 2011	65,000	53,500

(b) Mundu made drawings from the business of Shs 3.5 million for his personal expenses.

- (c) The capital allowances due to the partnership during the year were as follows:

	Shs '000'
Initial allowance:	3,000
Wear and Tear:	2,640

- (d) PAYE on the partners salaries paid during the year was as follows:

	Shs '000'
Mundu:	7,170
Sera:	4,470

Required:

- (a) Prepare a statement to determine the partnership chargeable income.
(15 marks)
- (b) Determine the tax due for each partner for the year ended 31 December 2011.

(5 marks)

(Total 20 marks)

Question 4

Choncod Ltd, a company resident in Uganda dealing in engineering consultancy, is fully registered for all Ugandan taxes. During the year ended 31 December 2011, the company was involved in various transactions. The managing director of Choncod Ltd is afraid of tax implications that the given transactions might generate. He has hired your services as a tax consultant. Your preliminary review reveals that all the transactions have VAT implications.

Required:

- (a) Advise the company on the VAT implications of each of the following transactions:
- Management has made a provision for income from technical fees of Shs 10 million. The company has not issued any invoices, and the amount is based on management estimates.
 - VAT charged on the purchase of a private passenger motor vehicle and the related repairs.
 - Trade bad debts written off of Shs 15 million which were more than 3 years old.
 - In the month of February 2011, the company paid a rental invoice of Shs 94.4 million inclusive of VAT.

- (v) Disallowed input VAT of Shs 150 million following a URA tax audit of which the company is disputing disallowance of Shs 50 million.
- (vi) Disposal of improved land located in Jinja at Shs 250 million.
- (vii) VAT on entertainment expenses.

(14 marks)

- (a) State the fines and penalties for the following offences as provided for under the VAT Act:

- (i) failure to lodge a return. **(2 marks)**
- (ii) failure to maintain proper records **(2 marks)**
- (ii) improper use of tax identification number **(2 marks)**

(Total 20 marks)

SECTION C

Attempt two of the three questions from this section.

Question 5

- (a) With examples, distinguish between direct and indirect tax systems as applied in the Uganda tax system. **(6 marks)**
- (b) Outline any **six** circumstances under which the income of a person may be exempted from income tax under the Income Tax Act of Uganda. **(3 marks)**
- (c) Mr. Wampamba is dissatisfied with the income tax assessed on his business income. He has sought your advice as a tax consultant.

Required:

Advise Mr. Wampamba on the objection and appeal procedure under the Income Tax Act.

(6 marks)

(Total 15 marks)

Question 6

- (a) Distinguish between an operating lease and a finance lease for income tax purposes. In your discussion include the resulting tax implications. **(5 marks)**
- (b) Discuss the opportunities and challenges presented by the customs union for the East African countries.

(10 marks)

(Total 15 marks)

Question 7

Mr. Grant is a citizen of the United Kingdom (UK) and has lived in Uganda since 1998. He has progressively acquired several assets including a residential house in Ntinda, a warehouse in Nakawa, land at Kiwatule, a flat in UK and three commercial trucks in Uganda.

Mr. Grant would like to return to his homeland, UK and has approached you as a tax consultant to advise him on the following:

- He has no intentions of disposing of the warehouse, trucks and all movable belongings in his residential house at Ntinda.
- He intends to enter into an agreement with his friend Speke who will run the operations of the warehouse and manage the trucks.
- Speke will remit the proceeds from the warehouse and the trucks to Mr. Grant's account in UK on a monthly basis.

Required:

- (a) (i) Discuss how the proposed relocation will affect the residence status of Mr. Grant in Uganda for tax purposes. **(3 marks)**
- (ii) Discuss the tax implications of Mr. Grant's relocation on his assets both personal and business and whether he is liable for any taxes in Uganda. **(4 marks)**
- (iii) Advise Mr. Grant on any requirement to file income tax returns with the Uganda Revenue Authority when he has left the country. **(2 marks)**
- (iv) In light of your answer in (a) (iii) above, under what circumstances would this requirement change? **(2 marks)**
- (b) State persons not required to file income tax returns to Uganda Revenue Authority in accordance with the Income Tax Act. **(4 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.