TAXATION

Is a process through which the government obtains money from the public/eligible person (s) by application of the law.

OR

Taxation is a legal compulsory transfer of money from the public to the government as source of government revenue.

Tax refers to a compulsory charge imposed by the government or any other competent authority on persons/businesses in order to finance government activities.

Basic terms used in taxation

1. **Tax base**. This refers to any item or economic activity that is subject to tax. The tax base in Uganda may include;
   - Income earned from economic activities like trading and manufacturing.
   - Income earned from employment like salaries, wages, commissions etc.
   - Property or assets like houses, land and other investments.
   - Consumption of goods which are a subject of taxation.
2. **Threshold of a tax.** Refers to the amount of money or level of income from which the tax liability begins **or** it refers to the level of income or money earned above which people or businesses must pay tax.
3. **Tax evasion.** This is the deliberate refusal of a tax payer to pay the tax imposed by the tax authority.
4. **Tax avoidance.** This is the deliberate and legal exploitation of the loopholes or weaknesses in the tax laws in order to reduce one's tax liability. This involves taking advantages of the loopholes in the tax laws to reduce one's tax liability.
5. **Tax holiday.** This refers to the period of non-tax payment given by the government to an investor/company.
6. **Tax exemption.** This is where the tax payer/tax paying unit is relieved or excluded from paying tax in order to encourage investment.

7. **Average rate of tax.** This refers to the proportion/fraction of total income that is paid as tax.

$$\text{Average rate of tax} = \frac{(tax\ amount)}{total\ income} X100$$

8. **Marginal rate of tax.** It refers to the proportion/fraction of additional or extra income that is paid as tax.

$$\text{Marginal rate of tax} = \frac{(change\ in\ tax\ )}{change\ in\ income} X100$$

9. **Tax rebate.** This refers to the tax reduction under special consideration.
10. **Tax yield.** This refers to the amount of tax revenue collected from a given number of taxes.
11. **Taxable capacity.** Refers to the ability of a tax payer to pay the tax imposed on him/her without affecting the standards of living.
12. **Tax burden.** This is the effect of a tax on the tax payer.
13. **Tax incidence/incidence of a tax.** This is the final resting place of a tax **or** it refers to the person/business that actually/finally pays the tax imposed.
14. **Tax liability.** This refers to the amount of money a tax payer is expected to pay as a tax in a given period of time **or** it refers to the total amount of money paid as tax by the tax payer.
15. **Tax rate.** This is the proportion/percentage at which an individual or a business is taxed.
16. **Taxable income.** This refers to income that is subject to taxation.

Determining either tax rate or tax liability given taxable income

Example 1: use the information below to determine the tax rates for the following tax payers.

Tax payer	Taxable income (shs)	Tax liability (shs)
Besigye	1,000,000	150,000
Muntu	800,000	80,000
Bobi	600,000	48,000
Mao	400,000	20,000

$$\text{Tax rate} = \frac{Tax\ liability}{Taxable\ income}\ x\ 100$$

Besigye; Tax rate = $\frac{150{,}000}{1{,}000{,}000}\ x\ 100$

= 15%

Muntu; Tax rate = $\frac{80{,}000}{800{,}000}\ x\ 100$

= 10%

Bobi; Tax rate = $\frac{48{,}000}{600{,}000}\ x\ 100$

= 8%

Mao; Tax rate = $\frac{20{,}000}{400{,}000}\ x\ 100$

= 5%

Example 2; Study the following table and answer the questions that follow;

Tax payer	Taxable income (shs)	Tax rate (%)
Saulo	9,000,000	15
Duncan	6,800,000	14
Prossy	5,700,000	13
Sanyu	10,000,000	16

Calculate the tax liability for each tax payer.

Tax liability = Tax rate x Taxable income

Saulo; Tax liability = $\frac{15}{100}\ x\ 9{,}000{,}000$

= shs 1,350,000

Duncan; Tax liability = $\frac{14}{100}\ x\ 6{,}800{,}000$

= shs 952,000

Prossy; Tax liability = $\frac{13}{100}\ x\ 5{,}700{,}000$

= shs 741,000

Sanyu; Tax liability = $\frac{16}{100}\ x\ 10{,}000{,}000$

= shs 1,600,000

Types/forms of taxes

There are two types of taxes i.e. direct taxes and indirect taxes.

Direct taxes; these are taxes levied/imposed on the income or property of individuals and business entities (companies). The burden of tax is directly borne by the individual or business entity hence cannot be shifted to other individuals.

Types/forms/examples of direct taxes

- **Personal income tax**. This is a tax levied/imposed on the income of individuals.
- **Corporation tax/company tax/profit tax**. This is a tax levied on corporations or profits of companies.
- **Wealth tax/property tax.** This is a tax levied on accumulated wealth, savings or capital of an individual or business entity.
- **Capital gains tax.** This is tax levied on profits received from the sale of capital/financial asset(s) **or** it refers to the tax imposed on profits received/realised from the sale of capital/financial assets whose values have increased or appreciated between the time of purchasing and selling them.
- **Estate/death duty.** This is a tax levied on the estate/property of a deceased person. It is normally done before the property of the deceased is distributed to the different named beneficiaries.
- **Gift tax.** This is a tax imposed on gifts from one individual to another.
- **Inheritance tax.** This is a tax imposed on inherited property of a deceased person after the death tax has been charged.

Merits/advantages/positive effects or impact of direct taxes

- **Direct taxes are used to reduce income inequalities/they help to redistribute income.** This is because they are progressive in nature hence high income earners are taxed at a higher rate compared to the low income earners e.g. PAYE.
- **They are used to control inflation.** This is because direct taxes reduce the people's disposable income and thereby reducing aggregate demand for goods and services.
- **Direct taxes are certain.** This is because the tax payers are well informed regarding the amount to pay, the time and method of payment.
- **They are economical.** This is because the cost of collecting direct taxes is generally low especially when deducted from the income or salary of an individual.
- **They are flexible.** This is because the government is able to increase or decrease the tax rates according to the prevailing economic conditions or requirements in the country.
- **They are simple and easy to understand.** This is because there no complicated calculations involved.
- **Direct taxes are convenient.** This is because they are collected at the time when income has been earned/realised.

Demerits/disadvantages/costs/positive effects or impact of direct taxes

- **Direct taxes discourage saving and investment.** This is because high direct taxes reduce people's disposable income hence reducing the amount of money available for saving which limits investment.
- **They make the government unpopular.** This is because they impose a heavy burden on the tax payers hence creating resentment and negative attitude towards government.
- **They are easy to evade**. This is by the tax payers under declaring their incomes.
- **They cause inconvenience to the tax payers**. This is because some direct taxes are payable in advance and lump sum.

- **They are a burden to the tax payers**. This is because they are paid directly out of the income of the tax payers.
- **They are not economical/they are costly**. This is because of the need to employ many people to assess, collect and administer taxes where the population is scattered and the informal sector is big.
- **They discourage hard work and effort**. This is because they are progressive in nature implying that when people work harder and realise higher incomes, they are taxed at higher rates.
- **They are discriminative in nature**. This is because some income groups especially low income earners are exempted from paying some of the direct taxes like PAYE.

Indirect taxes/consumption taxes/expenditure taxes/out lays

These are taxes imposed/levied on goods or services. The burden of the tax can be shifted by the tax payer to another party.

Types/forms/examples of indirect taxes

- **Import duty**. This is a tax imposed on goods entering into the country from other countries **or** tax on imposed on imports
- **Export duty.** This is a tax imposed on goods leaving the country **or** tax imposed on exports.

  NB; Import duty and export duty are referred to as customs duty**. Customs duty** is a tax imposed on imports and exports of a country.
- **Excise duty.** This is a tax imposed on locally/domestically produced or manufactured goods.
- **Specific tax**. This is a tax imposed on each unit of output produced or sold by a firm **or** tax charged per unit of output produced/sold.
- **Octoroi tax**. This is a tax imposed on goods in transit through a given country.
- **Sales tax/turnover tax.** This is a tax imposed on goods or services locally sold **or** tax imposed as a percentage on goods or services sold **or** tax imposed on total sales of goods or services of a business.
- **Advalorem tax.** This is a tax imposed on the value of products.

- **Sumptuary tax.** This is a tax levied on specific consumer goods to discourage their consumption.
- **Lumpsum tax.** This is a tax imposed on total output of a business/firm.
- **Withholding tax.** This is a form of income tax deducted at source by one person making/effecting payment to another person.
- **Value Added Tax (VAT).** This is a tax imposed on the value added at each stage of production or distribution of products.

Merits/advantages/benefits/positive effects or impact of indirect taxes

- **They are difficult to avoid and evade**. This is because they are included in the prices of goods or services hence paid willingly.
- **They are comprehensive.** This is because they are imposed on a variety of goods or services/ they cover a wide range of taxable goods or services hence high government revenue**.**
- **They help in income redistribution/they help to reduce income inequalities**. This is through levying high taxes on products consumed by the rich and lower taxes on goods consumed mainly by the poor.
- **Indirect taxes are flexible**. This is because the tax rate can be adjusted either upwards or downwards depending on the country's prevailing economic situation.
- **They are convenient**. This is because they are paid only when a good or a service is bought.
- **They discourage consumption of harmful/undesirable goods.** This is by increasing indirect taxes to make them more expensive hence reduced demand.
- **They are used to protect the domestic infant industries from foreign competition.** This through increasing import duties thereby making imports more expensive than the locally produced goods.
- **They are used to improve the balance of payment position of the country**. This is achieved by imposing high taxes on imported/foreign goods thereby discouraging their importation and eventually reducing the country's expenditure abroad.

- **They encourage hard work.** This is because they are imposed on goods or services that force people to put in more effort to realise enough incomes to pay for them.
- **They are impartial/they do not discriminate the tax payers**. This is because they are paid by all the consumers of goods or services.
- **They are economical**. This is because they involve low cost of collection since producers or sellers are used to collect them.

Demerits/disadvantages/costs/negative effects or impact of indirect taxes

- **They increase income inequalities among the tax payers**. This is because they are regressive in nature hence the burden of tax or sacrifice is heavier on low income groups.
- **They cause inflation**. This is because they increase the costs of production hence rising prices of goods or services.
- **They discourage production/ investment.** This is because they increase the costs of production thereby lowering the profit margin.
- **They are complicated**. This is because some indirect taxes are difficult to calculate or compute **or** they require a lot of documentation especially VAT.
- **They lead to diversion of resources.** This is because the producers tend to shift resources from taxed commodities to non-taxed commodities.
- **They discourage value addition or quality production.** This is because they increase the costs of inputs used to produce products.
- **They encourage trade malpractices like smuggling.** This is because the importers strive to evade the taxes.
- **They lead to a reduction in people's welfare.** This is because of a reduction in consumption due to increase in prices of goods or services.

Reasons/objectives/need/rationale/purpose for taxation (Why government imposes/ levies/charges taxes)

- **To raise government revenue**. This is through imposing different taxes on different tax paying units and the tax revenue realised is used to provide social services.

- **To reduce income inequalities/To help in income redistribution**. This is achieved through progressive tax system where high income earners are taxed at high rates and low income earners at low rates or subsidised**.**
- **To control inflation**. This is through charging high income tax which reduces disposable income leading to a fall in total demand for goods or services hence a fall in prices.
- **To discourage consumption or production of harmful or undesirable products**. This is through charging high taxes on such goods thereby making them expensive and less demanded by the consumers.
- **To create employment opportunities**. This is through using tax revenue for establishing investments that provide job opportunities.
- **To control monopoly power**. This is through taxing the abnormal profits made by monopoly firms.
- **To improve the country's balance of payments position**. This is through imposing high taxes on imports to discourage importation/reduce volume of imports hence reducing expenditure abroad.
- **To encourage forced saving**. This is through taxing income at source before it is passed to the recipient like NSSF contribution.
- **To encourage/promote hard work.** This is because tax payers are forced to put in more/extra effort to realise income to meet the tax obligations as well as the personal requirements.
- **To reduce dependence on foreign aid**. This is because the different taxes imposed increase the tax revenue generated by government hence no need for external borrowing.
- **To protect domestic infant industries**. This is through imposing high taxes on imports to make them more expensive hence less demanded compared to locally produced goods.
- **To discourage dumping.** This is through charging high taxes on goods entering the country making them expensive hence lowering their demand/consumption.
- **To promote economic growth.** This is through imposing high taxes on imported goods to discourage importation hence encouraging domestic production and investment.

Demerits/disadvantages/costs/negative effects or impact or role of taxation

- **Increases/widens income inequalities**. This is because of regressive taxes where the low income earners are taxed at higher rates than the high income earners.
- **Causes inflation**. This is because taxation increases the costs of production hence forcing producers to increase the prices of goods or services.
- **Discourages investment.** This is because it increases the costs of production thereby lowering the profit margin.
- **Discourages saving.** This is because taxation reduces disposable income of individuals and the profit margin of the producers/investors hence limiting saving.
- **Discourages hard work.** This is because some direct taxes are progressive in nature whereby high income earners are taxed at higher rates hence discouraging the effort to work.
- **Causes diversion of resources.** This is because the producers tend to shift resources from taxed commodities to non -taxed commodities.
- **Creates resentment making the government unpopular.** This is because taxation reduces the disposable income of the people and the amount of profits realised by the producers making them turn against the government.
- **Encourages trade malpractices like smuggling.** This is because the importers strive/try to devise means of evading or dodging the payment of taxes.
- **Leads to a reduction in people's welfare.** This is because of a reduction in consumption due to increase in prices of goods or services
- **Reduces the volume and benefits of trade.** This is because high taxes on profits made reduce the ability of producers to expand their businesses hence limiting economies of scale.

Principles/canons/doctrines of taxation or good tax system

Principles of taxation refer to the rules/guidelines followed when devising a tax system. They are the rules that must be observed when administering, assessing and collecting taxes.

Principles of taxation include the following;

- **Simplicity.** The tax should be easy to understand by both the tax payers and the tax officials/administrators.
- **Equity or fairness.** The tax burden should be distributed equally or fairly among the tax payers.
  This can be applied in two different ways;
  - ✓ **Horizontal equity**. This is where people with the same level of income/ taxable income pay the same amount of tax.
  - ✓ **Vertical equity**. This is where people with higher income levels pay more amount of tax than those with lower income levels.
- **Convenience.** The time, place and manner or mode of tax payment should be favourable or conducive to the tax payer.
- **Certainty.** The tax payers and tax officials or collectors should be well aware of the tax amount, manner or mode of tax payment, time and place of paying the tax.
- **Economy/cheapness/efficiency.** The costs involved in administering, assessing and collecting taxes should not exceed the tax revenue/revenue yield.
- **Ability to pay.** The tax imposed should be based on the financial resources of the tax payer to enable him/her meet the tax obligations **or** the tax payer should be able to pay the tax assessed on him/her without difficulties.
- **Flexibility/elasticity/buoyancy.** The tax should be able to increase or decrease depending on the prevailing economic conditions in the country.
- **Productivity.** The tax imposed should generate adequate/sufficient tax revenue to the government without discouraging hard work.
- **Neutrality/impartiality.** The tax imposed should not discriminate the tax payers/it should not favour any group of tax payers.
- **Comprehensiveness/diversity.** Good tax should cover a wide range of tax bases/ it should cover many taxable activities and persons.
- **Consistency.** The tax imposed should be in line with the national development objectives/government policies.
- **Avoidance of double taxation.** The tax payer should not be taxed more than once on the same tax base in the same period.

Characteristics/features/qualities of a good tax/tax system

- It should be simple to understand by both the tax payers and tax officials/collectors.
- It should be equitable in its distribution of the tax burden.
- It should be convenient to both the tax payer and tax collector.
- It should be certain.
- It should be economical/cheap/efficient to administer.
- It should be flexible or elastic.
- It should be productive.
- It should be neutral/impartial.
- It should be comprehensive.
- It should be consistent.
- It should be able to avoid double taxation.

Revision questions;

1. a) Describe the principles of a good tax system. (10 marks)
   b) Explain the need for taxation to the government of your country. (10 marks) **OR** why should the government levy taxes in Uganda?
2. a) Distinguish between corporation tax and value added tax (04 marks)
   b) What is the role of taxation in Uganda? (16 marks)
3. a) Distinguish between direct taxes and indirect taxes. (04 marks)
   b) Discuss the merits and demerits of indirect taxes. (16 marks)
4. a) Describe the different types of indirect taxes paid by entrepreneurs in Uganda. (10 marks)
   b) How does the government of Uganda **benefit** from the **taxes** imposed on entrepreneurs? (10 marks)

Tax compliance

This is the degree to which the tax payer/tax paying community meets the tax obligations, in accordance with the legal and regulatory provisions.

OR

Tax compliance refers to the degree to which the tax payer conforms to the tax rules of the country.

Elements of tax compliance

The tax payer is said to be tax compliant when the following have been done;

- **Registration**. Every tax payer is expected to register with URA for purposes of issuing the tax payer with Taxpayer Identification Number.
- **Filing returns**. Accurate and correct information should be provided about the business to help URA determine the tax payable.
- **Declaration**. The tax payer needs to declare the actual incomes and expenses of the business.
- **Payment**. Correct amount of tax due should be paid in time.
- **Record keeping**. All records relating to incomes and expenditures of the business should be properly kept.

Levels of tax compliance

There are four levels of tax compliance;

- Tax payers who are fully compliant. These tax payers are willing to fulfill their tax obligations voluntarily.
- Tax payers who reluctantly comply. These tax payers know that non-compliance would be expensive hence comply accordingly.
- Tax payers who show slight resistance to compliance. These tax payers are always ignorant about tax compliance hence when advised and some pressure exerted on them, they tend to comply.
- Tax payers who are non-compliant and show/exhibit a lot of resistance to meeting their tax obligations. These tax payers take pride in failing the tax authority.

Procedures/steps/stages of tax compliance

1. Registering of the taxpayer with Uganda Revenue Authority (URA).
2. Obtaining of the Taxpayer Identification Number (TIN).

3. Preparing the tax records that is income statements, cash flow statements among others.
4. Getting assessed for tax payment.
5. Submitting timely tax returns.
6. Paying the taxes imposed.
7. Receiving of feedback from the tax authority for example short message services, tax certificates etc.

Factors that affect/determine/influence tax compliance

- **The tax rate.** A high tax rate discourages tax compliance due to low taxable capacity which increases tax evasion while a low tax rate encourages tax compliance due to high taxable capacity.
- **Quality of business management by the tax payers.** Proper/good business management by the tax payers through proper record keeping ensures declaration of actual incomes and expenses hence encouraging tax compliance while improper/poor business management by the tax payers leads to under declaration of incomes and expenses which limit tax compliance.
- **The quality of tax administration.** A good tax administration reflected by high level of professionalism like integrity, good customer care among others promotes tax compliance while a poor tax administration reflected by unprofessional behaviour such as poor customer care, harsh methods of tax collection etc discourages tax compliance.
- **The popularity of the government and quality of governance.** A popular government because of good governance ensures proper accountability of tax revenue hence encouraging tax compliance while unpopular government because of poor governance promotes misuse of tax revenue limiting tax compliance.
- **The level of consistence and fairness in application of the tax laws and rules.** Consistent and fair application of tax laws and rules ensure equality among the tax payers hence promoting tax compliance while inconsistent and unfair application of tax laws and rules promote favouritism among the tax payers hence low level of tax compliance.

- **Simplicity of tax laws.** Simple tax laws are easily understood by the tax payers hence encouraging tax compliance while complicated tax laws are difficult to be understood by the tax payers hence low level of tax compliance.
- **The extent to which the tax system is equitable.** Equitable/fair tax system encourages tax compliance because of the fair distribution of the tax burden while inequitable/unfair tax system discourages tax compliance because of the unfair distribution of the tax burden.
- **The extent to which the tax burden is spread to all potential taxpayers.** Fair/proportional distribution of the tax burden makes taxpayers willingly meet their tax obligations hence high level of tax compliance while unfair distribution of the tax burden makes some taxpayers resist meeting their tax obligations hence low level of tax compliance.
- **The level of income.** A high level of income leads to high taxable capacity among the tax payers hence high level of tax compliance while a low level of income leads to low level of taxable capacity hence low tax compliance.
- **Level of tax education.** A high level of education increases taxpayers' awareness about importance of paying taxes hence high level of tax compliance while a low level of education leads to low level of tax compliance because of ignorance about importance of paying taxes.

Importance/benefits/significance of tax compliance (paying taxes promptly) to a business/an entrepreneur

- Promotes continuity in business activities since there is limited interference from the government/tax authorities.
- Helps to attract government support and sympathy in times of need like subsidies.
- Creates good business image/reputation hence different stakeholders are willing to deal with the business.
- Government uses the tax revenue for infrastructural development which benefits the business/entrepreneur.
- Encourages hard work/work effort since it makes the entrepreneur responsible and self-reliant.

- Import duties help to safeguard the domestic market for the local industries.
- Government uses tax revenue for paying salaries/wages and allowances of its workers hence increasing the demand for the products of the business.
- Enables easy access to business opportunities like government procurements or contracts or tenders.
- Enables the business to access financial resources like loans.

Factors limiting tax compliance/causes of low tax compliance in Uganda

- **High tax rate.** This leads to high rates of tax evasion and avoidance caused by low taxable capacity.
- **Poor management of the business.** This is leads to under declaration of incomes and expenses due to inability of the tax payer to keep proper business records for tax purposes.
- **Limited skilled personnel/ staff.** This makes proper tax assessment and collection difficult.
- **Unpopularity of the government in power due to poor governance.** This discourages tax payers from paying the tax since the tax revenue in most cases is misused.
- **Inconsistent application of tax laws/ rules.** This promotes discrimination among the tax payers hence low level of tax compliance.
- **Complicated tax laws/tax system.** These cause low tax compliance because the tax payers find difficulty in understanding or interpreting the tax laws.
- **Inequitable tax system.** This leads to unequal/unfair distribution of the tax burden hence limiting tax compliance.
- **Low income level of the tax payers.** This leads to low taxable capacity among the tax payers hence low tax compliance.
- **Inconvenient tax system/inconvenient time of tax collection.** This leads to low tax compliance since the tax dues are collected at unfavourable time to the tax payers.
- **Inadequate tax education.** This makes the tax payers ignorant about the benefits/importance of paying taxes.

- **Political instability.** This creates fear among the people which limits economic activities/ income generating activities hence low/no incomes realised.
- **Poor infrastructure.** This makes it difficult for the tax officials to move with ease to different parts of the country to assess or collect taxes.
- **Long procedures involved in paying the tax.** This creates inconvenience to the tax payers when clearing taxes.

Forms of non-tax compliances

- **Tax avoidance.** This refers to the <u>exploitation</u> of the <u>loopholes/weaknesses</u> in the <u>tax laws or tax system</u> in order to reduce the tax liability. It involves taking advantages of the loopholes in the tax laws to reduce one's tax liability.
- **Tax evasion.** This refers to the <u>deliberate refusal</u> of the tax payer/tax paying unit to <u>pay the tax</u> imposed or levied on him/her/it.It is an illegal act.

Forms/ ways/ examples of tax evasion

- Smuggling i.e. failure to declare entry or exit of goods.
- Under declaration of income ie under declaration of business income or personal income.
- Under valuation of the goods/services ie giving lower value of the goods/services imported or exported by the business.
- Refusal of the business to register for Value Added Tax/failure to register the business for taxation.
- Overstating of business expenses so as to declare less profits.
- Bribing tax collectors.
- Hiding from tax collectors at the time of collecting the tax.
- Failure to declare wealth, income and property for tax assessment.

Penalties/consequences/costs/effects of tax evasion/non-tax compliance to the business

- Temporary or permanent closure of the business by relevant tax authorities hence loss of business income.

- Denial of government support to a business where tax compliance is considered as a necessary condition for receiving the support.
- Penalty or surcharge on all the outstanding tax dues (unpaid taxes).
- Forceful payment of tax arrears/unpaid taxes from the business profits or entrepreneur's income.
- Publishing the business name in the shame list hence bad public image.
- Loss of smuggled goods that are confiscated by relevant tax authorities.
- Taking court action which may lead to imprisonment over non-paid tax obligations/ Imprisonment of tax defaulter(s) after court ruling.
- Blacklisting of the non-tax compliant business by the tax authorities hence bad public image.
- Denial of public/government contracts or tenders as the business may be blacklisted by the relevant tax authorities.
- Taking over the management of the business by the tax authority.

Measures that can be undertaken by the government to encourage tax compliance (how to minimise tax evasion) in Uganda

- **Maintaining/charging low tax rate.** This enables the tax payers to retain enough disposable income to support reasonable/decent standard of living which encourages tax compliance.
- **Improving the quality of business management in terms of record keeping.** This ensures proper tax assessment on businesses **or** it ensures proper and accurate estimation of the tax liabilities.
- **Strengthening or improving tax administration/employing or using skilled personnel.** This ensures proper assessment and collection of taxes.
- **Making the government popular and improving the quality of governance.** This ensures proper accountability of the tax payers' money/tax revenue which encourages tax compliance.
- **Ensuring consistency and fairness in application of tax laws/ rules.** This ensures equal treatment of all the tax payers hence minimising tax evasion.
- **Simplifying the tax laws.** This enables all the tax payers to easily understand or interprete the tax laws hence avoiding tax evasion.

- **Making the tax system equitable.** This ensures fair distribution of the tax burden to all the tax payers.
- **Ensuring application of the principle of convenience.** This enables collection of taxes at a time favourable to the tax payers.
- **Carrying out tax education.** This helps to create awareness among the tax payers about the benefits or importance of paying taxes.
- **Ensuring political stability.** This encourages more economic activities hence realisation of incomes for payment of tax.
- **Developing infrastructure.** This makes it easy for the tax collectors to move to different parties of the country to assess or collect taxes.
- **Making tax payment procedures short.** This gives tax payers convenience when clearing taxes.
- **Rewarding compliant tax payers.** This motivates other tax payers to pay the tax voluntarily.
- **Ensuring proper accountability of tax revenue.** This ensures provision of quality services out of the tax revenue collected.
- **Publishing names of tax defaulters in the media/press.** This encourages tax payers to be compliant to avoid bad public image.
- **Promoting whistle blower's policy.** This helps the tax authority to identify or track non- compliant tax collectors.

Revision questions;

1) a) Describe the procedure involved in tax compliance. (06 marks)
b) Examine the factors that determine the level of tax compliance in your country. (14 marks)

2) a) Account for the low level of tax compliance in Uganda. (10 marks)

b) Explain measures that should be taken to improve the level of tax compliance in Uganda/In what ways can tax evasion be minimised in Uganda? (10 marks)

Uganda Revenue Authority (URA)

Is a body/organisation responsible for collection of revenue for the central government.

It was formed by the government on 5th September 1991 to modernise the process of tax administration and minimise the loss of tax revenue and corruption.

Roles /responsibilities/functions of Uganda Revenue Authority (URA)

- **Assessing taxes**. This is through determining the correct taxes to be paid by the tax payers.
- **Collecting taxes**. This by ensuring that assessed taxes are paid by the tax payer(s) by the due date.
- **Accounting for all the revenue collected**. This is by giving accountability to the ministry responsible for finance (Ministry of Finance, Planning and Economic Development) for the revenue collected.
- **Facilitating trade and investment**. This is by providing tax incentives to the traders/investors **or** this is by coordinating with other government agencies like Uganda Investment Authority.
- **Advising the government on policy matters related to taxation.** This helps the government in making informed decisions in relation to tax administration in the country.
- **Providing tax education.** This is through stakeholder engagements, the media, workshops etc to promote tax compliance.
- **Influencing resource allocation**. This by imposing high taxes on investments on particular sectors hence discouraging resource allocation to such sectors while low taxes imposed on investments in other sectors or areas which promote or encourage resource allocation in those areas.
- **Protecting infant /domestic industries or firms from unfair foreign competition**. This is by imposing heavy taxes on imported commodities.
- **Reducing /controlling dumping of goods in the country.** This is by imposing heavy taxes on imported goods.
- **Increasing government revenue/diversifying the tax system**. This is by introducing new taxes e.g. rental income tax.

- **Redistributing income and wealth among individuals/firms/sectors (reducing income inequality in the country).** This is through progressive taxation.
- **Discouraging the importation, production and consumption of socially undesirable products like alcohol, cigarettes etc.** This is through imposing high taxes on such harmful products that may have negative effects on the health of the citizens.
- **Issuing of Tax Identification Number (TIN).**This is through the registration of the tax payers.

NB: **Tax Identification Number** is a unique number assigned to each tax payer that differentiates one tax payer from the other.

Purposes of allocating Tax Identification Number to a tax payer

- Making references.
- Filing returns.
- Assessing the tax obligation for each tax payer.
- Making inquiries.
- Paying or clearing tax.

Taxes collected by Uganda Revenue Authority

(I) International trade taxes/customs taxes. These are taxes collected from both imports and exports ie taxes collected from goods entering or leaving the country.

They include;

- Import duty.
- Export duty.
- Value Added Tax on imports.
- Withholding tax on imports.
- Excise duty.

- Environmental levy ie tax imposed on used imported products with negative environmental impact like second hand motor vehicles.
- Infrastructural levy.

(II) **Domestic taxes.** These are taxes collected from within the boundaries of the country. They are collected by URA under domestic taxes department. **They include**;

- Individual income tax.
- Corporation tax.
- Rental income tax.
- Capital gains tax.
- Value Added Tax on local goods and services.
- Excise duty.
- Gaming and pool betting tax ie tax imposed on gaming and sports betting activities.

Challenges faced by tax authorities in Uganda/challenges of taxation in Uganda

- **Low taxable capacity.** This is because of low income levels/high levels of poverty which limit the ability of tax payers to pay the tax levied on them.
- **Narrow tax base.** This is because of limited taxable activities.
- **High level/degree of tax evasion.** This is because some tax payers deliberately refuse to pay the taxes levied on them.
- **High level/degree of tax avoidance.** This is because the tax payers exploit the weaknesses in the tax system/tax laws hence paying less tax or no tax at all.
- **High rate of corruption and embezzlement.** This leads to loss of revenue that would have been raised from taxation.
- **Shortage of skilled manpower/limited skills in tax administration.** This leads to inefficiency in tax assessment and collection hence loss of tax revenue by the government.

- **Difficulty in identifying taxable sources.** This is because some tax payers have sources of income which are not cleared defined or are not known to the tax authority.
- **Underdeveloped infrastructure.** This increases the cost of collecting taxes since it limits accessibility to some areas for proper tax assessment and collection.
- **Political instability.** This discourages the tax collectors from reaching the affected areas to assess and collect taxes for fear of losing their lives.
- **Political interference**. This lowers the tax bases because some investors or businesses are offered tax incentives like tax holidays, tax exemptions etc.
- **Large informal sector**. This makes it difficult for the tax authorities to assess tax due to absence of proper book keeping or accounting records by most businesses.
- **Limited facilities like computers**. This makes the process of tax assessment and collection difficult.
- **High rate of inflation**. This reduces the real value of nominal tax revenue making government planning/budgeting difficult.

Measures to improve tax revenue in Uganda/possible solutions to the problems of taxation in Uganda

- **Educating/sensitizing the masses on the role of taxation.** This enables the masses pay taxes willingly.
- **Fighting corruption in tax assessment and collection.** This helps to minimise on the loss of government tax revenue by prosecuting corrupt tax officials in the courts of law.
- **Training of more tax officials.** This helps to fill the manpower gaps in tax administration.
- **Ensuring political stability in all parts of the country.** This encourages more economic activities and also enables the tax collectors easily access tax payers.
- **Developing/improving infrastructure.** This enables tax collectors easily access the tax payers.
- **Widening the tax base.** This is through introduction of new taxes.

- **Improving implementation of the tax laws.** This helps to minimise tax evasion.
- **Putting in place facilities required to facilitate tax assessment and collection.** This improves efficiency in tax administration.
- **Putting in place the anti-smuggling unit.** This helps to reduce smuggling of goods in and outside the country.

Obligations and rights of a tax payer

(i) **Obligations of a tax payer;** these are the responsibilities/duties of a taxpayer. They include;

- Filing returns and entries. Every tax payer is required by law to file correct tax returns and customs entries at the right time.
- Paying tax. The tax payer is required to pay the correct amount of tax at the right time.
- Cooperating with the tax authority. The tax payer is expected to deal and cooperate only with the authorised staff of the tax authority (URA).
- Being aware of and comply with customs, quarantine, wildlife, currency and passenger concession requirements when travelling.
- Using the services of a licensed customs agent to complete customs entries and related clearance formalities when importing and exporting goods or cargo.
- Registration. A tax payer is required to register voluntarily with URA in order to obtain a TIN.
- Disclosure/declaration. The taxpayer is required to provide all the relevant information and make correct declaration of all transactions at all times to the tax authority.
- Completing accurately all the necessary forms before reaching the arrival or departure processing point(s) in case of travelling.

(ii) **Rights of a tax payer;** refer to list of the protections available to the taxpayer when dealing with taxation. They include;

- Right to equity. The tax laws and procedures should be applied fairly or consistently to the tax payer **or** taxpayer needs to pay fair and correct taxes.

- Right to prior notices. The tax payer has a right to receive notifications in advance from the tax authorities whenever the premises are to be subjected to routine inspection or audit.
- Right to tax refunds. The taxpayer has a right to receive tax refund from tax authority where applicable within the prescribed time limit.
- Right to confidentiality. Maintaining the secrecy of the tax affairs of the taxpayer and the tax information used in accordance with the law.
- Right to facilitation of tax compliance. The taxpayer has a right to be sensitised/educated about his/her tax obligations.
- Objections and appeals. The complaints raised by the taxpayer have to be attended to by the tax authority in accordance with the relevant laws and procedures.
- Right to accountability. The taxpayer needs to be promptly updated for any tax paid.
- Right to customer care. The taxpayer has a right to receive excellent services from the tax authority at all times.
- Right to immediate attention concerning processing tax returns, customs entries and other documents relating to tax affairs as stipulated by the relevant laws.

Revision questions;

1 a) Explain the roles of Uganda Revenue Authority (10 marks)

b) What challenges are being faced by tax authorities in Uganda? (10 marks)

2 a) Distinguish between tax evasion and tax avoidance. (04 marks)

b) Explain the rights and obligations of tax payers in Uganda. (16 marks)

Basic tax computations

Tax computations deal with establishing taxes/ duties payable. It focuses on how taxes are determined, based on relevant laws in Uganda.

1**. Individual Income Tax**. This is a tax imposed on the chargeable income/ taxable income of an individual.

Chargeable/ taxable income is derived from gross income.

Gross income is the income earned by an individual from all sources excluding tax exempt income ie the total amount of **business income, employment income and property income** earned by an individual excluding **tax exempt income**.

Tax exempt income/ exempt income this is income not taxed by law.

Gross income = Business income + employment income + property income – Tax exempt income

OR

Gross income = Total income/Income from all sources – Tax exempt income

According to the **Income Tax Act,** there are three sources of income to an individual i.e.

(i) Business income.
(ii) Employment income.
(iii) Property income.

Business income; this refers to any income earned/realised by an individual from carrying out a business activity e.g. gains/ profits from sale of any business asset, sales revenue/ gross sales etc.

Employment income; this refers to any income earned/realised by an individual from any form of employment e.g. wages or salaries earned, commission received, gratuity, allowances, compensation for termination of employment contract etc.

Property income; this refers to income received by an individual from the use or hiring of property by other individuals or business enterprises e.g. property interest received, rent income etc.

Chargeable/taxable income; this is gross income less expenses and losses incurred in earning the income.

Chargeable income = Gross income – Total expenses and losses.

Example 1; Jero earned income from different sources for the year 2020 as shown below;

Business income shs 2,000,000
Employment income shs 4,800,000
Property income shs 1,000,000
In addition, he incurred expenses and losses amounting to shs 2,400,000 while a total of shs 300,000 out of the gross income was tax exempt.

Determine jero's;

(i) Gross income
(ii) Chargeable income

Solution:

(i) Gross income = Total income/ income from all sources – Tax exempt income.
= Business income + employment income + property income – Tax exempt income.
= 2,000,000 + 4,800,000 + 1,000,000 – 300,000
=7,800,000 – 300,000
= shs 7,500,000

(ii) Chargeable income = Gross income – Expenses and losses.
= 7,500,000 – 2,400,000
= shs 5,100,000

Example 2: Musobya earned the following incomes from various sources during a given year.

Profit made on sale of business machinery	shs 6,000,000
Salaries earned	shs 6,000,000
Property interest received	shs 4,000,000
Transport allowance	shs 2,400,000
Rent income	shs 12,000,000
Gross sales	shs 9,000,000

In addition, he incurred total expenses and losses of shs 12,400,000 while tax exempt income for the year amounted to shs 7,080,000.

Calculate musobya's;

(i) Gross income

(ii) Chargeable income

Solution;

(i) Gross income = Total income/ income from all sources – Tax exempt income.

Total income = Profit made on sale of business machinery.

+ Salaries earned

+ Property interest received.

+ Transport allowance

+ Rent income

+ Gross sales.

= 6,000,000 + 6,000,000 + 4,000,000 + 2,400,000 + 12,000,000 + 9,000,000

Total income = shs 39,400,000

Gross income = 39,400,000 – 7,080,000

= shs 32,320,000

(ii) Chargeable income = Gross income – Total expenses and losses.

= 32,320,000 – 12,400,000

= shs 19,920,000

Example 3; Study the table below and answer the questions that follow;

Income earner	**Business income (Shs)**	**Employment (shs)**	**Property income (Shs)**
Onya	1,400,000	800,000	2,300,000
Okile	2,100,000	1,200,000	3,000,000
Okumu	2,500,000	1,600,000	3,400,000
Odoi	2,900,000	1,800,000	3,750,000

For all the above income earners, tax exempt income takes 10% of the total income and expenses and losses incurred while earning the income take 15% of the total income.

Calculate each income earner's;

(i) Gross income
(ii) Chargeable income

Solution;

Gross income = Total income – Tax exempt income

= (Business income + Employment income + property income) - Tax exempt income

• Total income for Onya	=	1,400,000 + 800,000 + 2,300,000
	=	**shs. 4,500,000**
Tax exempt income	=	$\frac{10}{100}\, x\ 4{,}500{,}000$
	=	**shs 450,000**
Gross income for Onya	=	4,500,000 – 450,000
	=	**shs. 4,050,000**
• Total income for Okile	=	2,100,000 + 1,200,000 + 3,000,000
	=	**shs. 6,300,000**
Tax exempt income	=	$\frac{10}{100}\, x\ 6{,}300{,}000$
	=	**shs 630,000**
Gross income for Okile	=	6,300,000-630,000
	=	**shs 5,670,000**
• Total income for Okumu	=	2,500,000 + 1,600,000 + 3,400,000
	=	**shs 7,500,000**
Tax exempt income	=	$\frac{10}{100}\, x\ 7{,}500{,}000$
	=	**shs 750,000**
Gross income for Okumu	=	7,500,000 – 750,000
	=	**6,750,000**
• Total income for Odoi	=	2,900,000 + 1,800,000 + 3,750,000
	=	**shs 8,450,000**

Tax exempt income = $\frac{10}{100}\ x\ 8{,}450{,}000S$

= **shs 845,000**

Gross income for Odoi = 8,450,000 – 845,000

= **shs 7,605,000**

(ii) Chargeable income = Gross income – Expenses and losses incurred in earning the income.

Expenses and losses incurred to earn income = 15% of the total income earned

- Chargeable income for Onya = 4,050,000 – ($\frac{15}{100}\ x\ 4{,}500{,}000$)

  = 4,050,000 – 675,000

  = **shs 3,375,000**

- Chargeable income for Okile = 5,670,000 – ($\frac{15}{100}\ x\ 6{,}300{,}000$)

  = 5,670,000 - 945,000

  = **shs. 4,725,000**

- Chargeable income for Okumu = 6,750,000 –($\frac{15}{100}\ x\ 7{,}500{,}000$)

  = 6,750,000 – 1,125,000

  = **shs. 5,625,000**

- Chargeable income for Odoi = 7,605,000 – ($\frac{15}{100}\ x\ 8{,}450{,}000$)

  = 7,605,000 – 1,267,000

  = **shs 6,337,500.**

Trial exercise 1; Sekitto earned income from different sources for the year 2021

Business income	shs 4,000,000
Employment income	shs 3,800,000
Property income	shs 3,000,000

Tax exempt income shs 800,000
Expenses and losses for the year shs 420,000

Calculate sekitto's;
(i) Gross annual income
(ii) Chargeable income for the year.

Trial exercise 2; Study the table below and answer the questions that follow;

INCOME EARNER	BUSINESS INCOME (Monthly) (SHS)	EMPLOYMENT INCOME (Monthly) (SHS)	PROPERTY INCOME (Monthly) (SHS)
FRESH KID	1,000,000	600,000	1,500,000
FRESH UNCLE	1,200,000	800,000	1,000,000
FRESH MUMMY	2,200,000	800,000	1,400,000
FRESH DADDY	3,000,000	1,300,000	1,700,000

Note: For all the above income earners, tax exempt income takes 10% of the business income while expenses and losses incurred while earning income take 5% of the gross income.

Calculate each income earner's monthly;
(i) Gross income
(ii) Chargeable income.

Individual income tax on employment income (Pay As You Earn)
Most people paying individual income tax earn income from employment and the tax is recovered from them at source through the PAYE system:
The individual income tax on employment income is charged as **a withholding tax**

PAYE is collected by employers who remit it to URA. The employers are authorised by the **Income Tax Act** to withhold the appropriate amount from the employees' monthly employment incomes and remit to URA by the 15th day of the following month.

The tax rate for PAYE

Income is usually taxed in relation to a defined year of income. The tax rate therefore is based on annual figures. However, for PAYE or individual income tax on employment income, the rates are administratively reduced to monthly rates since PAYE is paid on monthly basis.

(A) **PAYE monthly tax rates:**

Monthly chargeable income	Tax rate
Below shs 235,000	NIL
Above shs 235,000 but not exceeding shs 335,000	10% of the amount exceeding shs 235,000.
Above shs 335,000 but not exceeding shs 410,000	Shs 10,000 plus 20% of the amount exceeding shs 335,000.
Above shs 410,000	(a) Shs 25,000 plus 30% of the amount exceeding shs 410,000.
	(b) Where chargeable income exceeds shs 10,000,000, an additional 10% is charged on the amount by which chargeable income exceeds shs 10,000,000.

Example 1:

The following are the gross monthly salaries for the employees of Ekas Enterprises Ltd.

Malaika shs 200,000
Madaraka shs 300,000
Mkubwa shs 600,000
Mkuu shs 11,000,000

Required; Using the PAYE tax rates provided above: calculate the amount of PAYE payable monthly by each employee.

Solution:

(i) Malaika's monthly PAYE is **NIL**. This is because the monthly gross pay is below the monthly tax threshold of shs 235,000

(ii) Madaraka's monthly PAYE = 10% of the amount exceeding shs 235.000

$$=\frac{10}{100}(300,000 - 235,000)$$

$$=\frac{10}{100} \text{ x}65,000$$

$$= \text{shs } 6,500$$

(iii) Mkubwa's monthly PAYE = shs 25,000 plus 30% of the amount exceeding shs 410,000

$$= 25,000 + \frac{30}{100} \text{ x}(600,000 - 410,000)$$

$$= 25,000 + \frac{30}{100} \text{ x } 190,000$$

$$= 25,000 + 57,000$$

$$= \text{shs } 82,000$$

(iv) Mkuu's monthly PAYE

= shs 25,000 plus 30% of the amount exceeding shs 410,000 plus 10% of the amount exceeding shs 10,000,000

$$= 25,000 + \frac{30}{100} \text{ x } (11,000,000 - 410,000) + \frac{10}{100} \text{ x } (11,000,000 - 10,000,000)$$

$$= 25,000 + \frac{30}{100} \text{ x } 10,590,000 + \frac{10}{100} \text{ x}1, 000,000$$

= 25,000+3,177,000+100,000

= shs 3,302,000.

Example 2: Blessed Construction Company employs five categories of workers and managers. The respective payment for each category is as follows:

No	Category	Number of	Monthly gross pay

		employees	
			shs
1	Cleaners	4	200,000
2	Drivers	2	320,000
3	Machine operators	5	400,000
4	Technicians	2	3,800,000
5	Managers	1	12,400,000

Using the monthly PAYE tax rates, calculate the amount of PAYE payable monthly by:

(a) Each category of employees.

(b) Blessed Construction Company to URA.

a (i) Cleaners monthly PAYE = Number of employee x Tax rate

$$= 4 \text{ x } 0$$

$$= 0$$

This is because the cleaners' income/ monthly gross pay is below the monthly threshold of shs 235,000.

(ii)Drivers monthly PAYE = Number of employees x Tax rate

$$= 2\left[\frac{10}{100}(320{,}000 - 235{,}000)\right]$$

$$=2\left(\frac{10}{100} \text{ x } 85{,}000\right)$$

$$= 2 \text{ x } 8{,}500$$

$$= \text{shs}17{,}\ 000$$

(iii)Machine operators monthly PAYE = Number of employees x Tax rate

$$= 5\left[10{,}000 + \frac{20}{100} \text{x}(400{,}000 - 335{,}000)\right]$$

$$= 5\left[10{,}000 + \frac{20}{100} \text{x}65{,}000\right]$$

$= 5\ (10{,}000 + 13{,}000)$

$= 5 \times 23{,}000$

= shs 115,000

(iv)Technicians monthly PAYE = Number of employees x Tax rate

$= 2\left[250{,}000 + \frac{30}{100} x(3{,}800{,}000 - 410{,}000)\right]$

$=2\left[25{,}000 + \frac{30}{100} \times 3{,}390{,}000\right]$

$= 2\ (25{,}000 + 1{,}017{,}000)$

$= 2 \times 1{,}042{,}000$

=shs 2,084,000

(v)Managers monthly PAYE = Number of employees x Tax rate.

a)$= 1\left[250{,}000 + \frac{30}{100}(12{,}400{,}000 - 410{,}000)\right]$

$=25{,}000 + \frac{30}{100} \times 11{,}990{,}000$

$= 25{,}000 + 3{,}597{,}000$

= shs 3,622,000

b) $= \frac{10}{100}(12{,}400{,}000 - 10{,}000{,}000)$

$= \frac{10}{100} \times 2{,}400{,}000$

= shs 240,000

Total PAYE =a +b

$= 3{,}622{,}000 + 240{,}000$

= shs 3,862,000

(b) Monthly PAYE paid to URA = Total PAYE for all categories.

= Cleaners PAYE + Drivers PAYE

+ Machine operators PAYE + Technicians PAYE + Managers PAYE

= 0 + 17,000 + 115,000 + 2,084,000 + 3,862,000.

= shs 6,078,000.

1. **Trial exercise;** the following are the gross monthly salaries for the employees of Baba bakery.

Billy	shs 235,000
Berna	shs 400,000
Happy	shs 900,000
Hope	shs 11, 400,000

Using the monthly PAYE tax rates, determine the income tax payable by each employee of Baba bakery per month.

(B) **The PAYE annual tax rates;**

Annual chargeable income	Tax rate
Not exceeding shs 2,820,000	NIL
Exceeding shs 2,820,000 but not exceeding shs 4,020,000	10% of the amount by which chargeable income exceeds shs 2,820,000
Exceeding shs 4,020,000 but not exceeding shs 4,920,000	Shs 120,000 plus 20% of the amount by which chargeable income exceeds shs 4,020,000
Exceeding shs 4,920,000	(a) Shs 300,000 plus 30% of the amount by which chargeable income exceeds shs 4,920,000

	(b) Where chargeable income exceeds shs 120,000,000 ,an additional 10% is charged on income above shs 120,000,000

Example 1; Using annual PAYE tax rates, calculate the amount of PAYE payable annually by following employees

Employee	Gross annual salary(shs)
Opio	2,700,000
Opito	3,900,000
Opus	4,600,000
Okitoi	40,000,000
Onyait	140,000,000

(i) Opio: PAYE payable is **Nil/Zero**. This is because his gross annual salary of shs 2,700,000 is below the annual tax threshold of shs 2,820,000

(ii) Opito ; PAYE payable = 10% of the amount by which chargeable income exceeds shs 2,820,000

$$=\frac{10}{100} \text{ x } (3,900,000 – 2,820,000)$$

$$= \frac{10}{100} \text{ x } 1,080,000$$

= shs 108,000

(iii) Opus; PAYE payable = shs 120,000 plus 20% of the amount by which chargeable income exceeds shs 4,020,000

$$= 120,000 + \frac{20}{100} \text{ x } (4,600,000 – 4,020,000)$$

$$= 120,000 + \frac{20}{100} \text{ x } 580,000$$

$= 120,000 + 116,000$

$= \text{shs } 236,000$

(iv) Okitoi; PAYE payable = shs 300,000 plus 30% of the amount by which chargeable income exceeds shs 4,920,000

$= 300,000 + \frac{30}{100} \text{ x } (40,000,000 – 4,920,000)$

$= 300,000 + \frac{30}{100} \text{ x } 35,080,000$

$= 300,000 + 10,524,000$

$= \text{shs } 10,824,000$

(iv) Onyait ; PAYE payable = shs 300,000 plus 30% of the amount by which chargeable income exceeds shs 4,920,000 + 10% of the amount exceeding shs 120,000,000

$= 300,000 + \frac{30}{100} \text{ x } (140,000,000 – 4,920,000)$

$+ \frac{10}{100} (140,000,000 – 120,000,000$

$= 300,000 + \frac{30}{100} \text{ x } 135,080,000 + \frac{10}{100} \text{x } 20,000,000$

$= 300,000 + 40,524,000 + 2,000,000$

$= \text{shs } 42,824,000$

Exercise; Ekas Jero is an employee of unique enterprises where he earns a total gross salary of shs 8,400,000 per year. This means that Jero's earnings fall under the forth income tax bracket indicated below:

4^{th} income tax bracket	Tax rate per month
Shs 410,000 per month and above	Shs 25,000 + 30% of amount exceeding shs 410,000

Calculate the amount of Pay As You Earn (PAYE) expected to be paid by Ekas Jero for a year.

2. **Rental income Tax;** this is a tax imposed on every individual or business entity that earns rental income in a given year.
This tax is charged on rental income received from immovable property (land, building and royalties)

Sources of rental income

- Commercial buildings
- Land (plot, gardens or swamps)
- Royalties (murram, minerals, stones/ rocks etc.)

The Income Tax Act provides the following;

(i) 20% is allowed as a deduction from gross rental income/rental income to cater for expenses/costs incurred.
(ii) A tax free allowance/ tax threshold of shs 2,820,000 is deducted per annum.
(iii) The tax rate is 20% of taxable/ chargeable rental income.

Example 1: Tajiri is a landlord who owns four (4) rental houses and he charges monthly rent of shs 370,000 per house. All tenants stayed for the whole of a given year. The Income Tax Act provides the following:

(i) 20% allowance is deducted from gross rental income to cater for expenses incurred.

(ii) A tax free allowance of shs 2,820,000 is deducted.

(iii) The tax rate is 20% of chargeable rental income

Required; Compute tajiri's;

(a) Gross annual rental income.
(b) Net rental income.
(c) Taxable rental income.
(d) Rental income tax/rental income tax liability paid to URA.

(a) Gross annual rental income =Number of houses x rent per month x number of months in a year.

$= 4 \times 370,000 \times 12$

$= \text{shs } 17,760,000$

(b) Net rental income = Gross annual rental income – provision for expenses and losses

Provision for expenses and losses= 20% of gross annual rental income

$= \frac{20}{100} \times 17,760,000$

$= \text{shs } 3,552,000$

Net rental income $= 17,760,000 - 3,552,000$

$= \text{shs } 14,208,000$

(c) Taxable rental income = Net rental income – Tax free allowance (tax threshold)

$= 14,208,000 - 2,820,000$

$= \text{shs } 11,388,000$

(d) Rental income tax paid to URA = 20% of taxable rental income

$= \frac{20}{100} \times 11,388,000$

$= \text{shs } 2,277,600$

Example 2: Masikini, a resident individual operates rental properties. In the financial year ended December, 2018 he received shs 17,500,000 as rent revenue.

The Income Tax Act provides the following;

(i) 20% allowance is deducted from gross rental income to cater for expenses incurred.

(ii) A tax free allowance/tax threshold of shs 2,820,000 is deducted.

(iii) The tax rate is 20% of chargeable /taxable rental income.

Determine Masikini’s;

(i) Gross rental income
(ii) Taxable rental income
(iii) Tax liability for the year 2018

(i) Gross rental income/rental income = shs 17,500,000

(ii) Taxable rental income = Net rental income – Tax free allowance

Net rental income = Gross rental income – Provision for expenses and losses.

Provision for expenses and losses=20% of gross rental income

$$=\frac{20}{100}x17{,}500{,}000$$

= shs 3,500,000

Net rental income = 17,500,000 – 3,500,000

= shs 14,000,000

Taxable rental income = 14,000,000 – 2,820,000

=shs 11,180,000

(iii) Tax liability = 20% of taxable rental income

$$= \frac{20}{100} \text{ x } 11{,}180{,}000$$

= shs 2,236,000

Exercise; Among Queen owns two rental houses. She earned monthly rental income of shs 300,000 from each house in a given year. Both houses had tenants for the entire year. The Income Tax Act provides the following;

- Provision for expenses and losses is 20% of gross rental income.
- The annual tax threshold is shs 2,820,000.
- The tax rate is 20% of taxable rental income.

Compute among's;

(i) Annual rental income
(ii) Net rental income.
(iii) Taxable rental income.
(iv) Rental income tax payable to URA

3. **Value Added Tax (VAT)**

This is a taxed imposed on value added at each stage of production or distribution of products.

Key terms used in VAT assessment.

1. **Taxable person**; refers to a person who is registered or is required to register to pay VAT.
2. **Taxable supplies**; these are supplies of goods/services which are liable for VAT at either standard or zero rates.
3. **Zero-rated supplies;** these are business transactions or supplies of goods/services where VAT is charged at zero rate (0%)
4. **Standard rated supplies**; these are business transactions or supplies of goods/services that are liable for VAT payment. VAT is charged at 18%.
5. **Exempt supplies**; these are supplies of goods/services on which VAT is not charged either at standard or zero rate.
6. **Taxable value**; this refers to the price/value of a product that is subject to tax. It is the tax base upon which the VAT rate is applied when computing VAT.
7. **Input VAT/Input tax**; this is VAT on purchases.
8. **Output VAT/Output tax;** this is VAT on sales.
9. **VAT liability** is the difference between Output VAT and Input VAT.
10. **VAT exclusive transaction**; is one where the price of the commodity or taxable value does not include VAT. For such a transaction, the VAT rate is $18\%=\frac{18}{100}$
11. **VAT inclusive transaction**; is one where the price of the commodity or taxable value includes VAT. For such a transaction, the VAT rate = $\frac{R}{R+100}$ where R is the rate of tax

$$= \frac{18}{18 + 100}$$

$$= \frac{18}{118}$$

12. **VAT refund**; this is the excess of Input tax over the Output tax; hence the tax payer claims the difference as VAT refund from URA. **VAT refund=Input tax-Output tax.**

Methods/approaches used for calculating Value Added Tax (VAT).

1. **Using stages**. This involves first calculating the value added to the product at each stage (apart from the first stage) by getting the difference between the selling price and buying/cost price and then applying the VAT rate on the value added.

   A: VAT exclusive transactions

   Example I; the following VAT exclusive transactions were carried out by VAT registered businesses at various stages of distribution for the month of May 2016.

   (i) Super traders bought goods worth shs 9,000,000.
   (ii) Super traders sold all the goods to Ben for shs 14,000,000.
   (iii) Ben sold the same goods to Joy, a retailer at shs 20,000,000.
   (iv) Joy sold all the goods to a final consumer at shs 28,000,000.

   Using a VAT rate of 18%;

(a) Calculate the VAT chargeable at each stage.
(b) Determine the gross sales value the consumer paid for the goods (VAT inclusive)

Solution;

(a) Stage I; VAT chargeable = VAT rate x Purchase price

$$= \frac{18}{100} \text{ x } 9{,}000{,}000$$

$$= \text{Shs } 1{,}620{,}000$$

Stage II; VAT chargeable = VAT rate x Value added.

$= \frac{18}{100}$ x (14,000,000 – 9,000,000)

$= \frac{18}{100}$ x 5,000,000

= Shs 900,000

Stage III; VAT chargeable = VAT rate x Value added.

$= \frac{18}{100}$ x (20,000,000 – 14,000,000

$= \frac{18}{100}$ x 6,000,000

= Shs 1,080,000

Stage IV; VAT chargeable = VAT rate x Value added

$= \frac{18}{100}$ x (28,000,000 – 20,000,000)

$= \frac{18}{100}$ x 8,000,000

= Shs 1,440,000

(b) Gross sales value the consumer paid

= Sales value at stage IV + VAT on sales value at stage IV

= 28,000,000 + $\frac{18}{100}$ x 28,000,000

= 28,000,000 + 5,040,000

= Shs 33,040,000

OR

Gross sales value the consumer paid

= Sales value at stage IV + Total VAT (stages I –IV)

Total VAT = VAT stage I + VAT stage II + VAT stage III + VAT stage IV

= 1,620,000 + 900,000 + 1,080,000 + 1,440,000

=Shs 5,040,000

Gross sales value = 28,000,000 + 5,040,000

= Shs 33,040,000

Example 2; Toto Enterprises had the following VAT exclusive transactions with VAT registered enterprises for one month

Purchases Shs 236,000,000

Sales Shs 259,600,000

(i) Calculate VAT paid by Toto enterprises to URA for that period (use 18% as VAT rate).

VAT paid = VAT rate x Value added

= VAT rate x (sales – purchases)

$= \frac{18}{100}$ x (259,600,000 – 236,000,000)

$= \frac{18}{100}$ x 23,600,000

= Shs 4,248,000.

(ii) Determine Toto enterprises' total sales value (VAT inclusive)

Total sales value = Sales value + VAT on sales value.

$= 259{,}600{,}000 + \frac{18}{100}$ x 259,600,000

= 259,600,000 + 46,728,000

= Shs 306,328,000

Example 3; AVAT registered manufacturer pays shs 100,000 (exclusive of VAT) to purchase raw materials from a VAT registered tax payer. He incurs another 25% on cost for processing raw materials into a finished product. Further, he includes a mark-up of 40%

Given the VAT rate as 18%, calculate;

(i) Input tax
(ii) Output tax at each of the two stages.
(iii) VAT payable to URA

Solution;

(i) Input tax = 18% x cost of raw materials.

$= \frac{18}{100}\ x\ 100{,}000$

= shs 18,000

(ii) Output tax

Stage I

Cost of processing raw materials = 25% of cost of raw materials

$= \frac{25}{100}\ x\ 100{,}000$

= shs 25,000

Value of goods = cost of raw materials + cost of processing raw materials

= 100,000 + 25,000

= shs 125,000

Output tax = 18% x value of goods

$= \frac{18}{100}\ x\ 125{,}000$

= shs 22,500

Stage II;

Mark-up = 40% of value of goods (stage I)

$= \frac{40}{100}\ x\ 125{,}000$

= shs 50,000

Value of goods at stage II = mark-up + value of goods at stage I

= 50,000 + 125,000

= shs 175,000

Output tax = 18% of 175,000

$= \frac{18}{100}\ x\ shs\ 175{,}000$

= shs 31,500

(iii) VAT payable to URA = Output tax – Input tax

= 31,500 – 18,000

= shs 13,500

Exercise 1; Unique Enterprise is VAT registered and it carried out the following VAT exclusive transactions with other VAT registered businesses at various stages of distribution.

(i) Unique Enterprises bought goods worth shs 40,000,000.
(ii) Unique Enterprises sold all the goods for cash to Anisha for shs 64,000,000.
(iii) Anisha sold the same goods for cash to a final consumer at shs 85,000,000

Using the VAT rate of 18%

(a) Compute VAT payable at each stage

(b) Determine the amount the consumer paid.

Exercise 2; An illustration below shows the various stages that are involved in the distribution of goods

Stage	Activity	Purchase price (Shs) (VAT exclusive)	Selling price (Shs) (VAT exclusive)
1	Importer at customs	10,000,000	
2	Importer at local distribution	10,000,000	12,000,000
3	Wholesaler	12,000,000	16,000,000
4	Retailer	16,000,000	19,000,000

Required; Compute the VAT paid at each stage of distribution (use 18% as VAT rate)

Exercise 3; Ekas Jero an entrepreneur sold clothes that cost shs 1,500,000 to Unique Enterprises at shs 2,000,000. The transactions were VAT exclusive.

Use 18% VAT rate to calculate;

(i) VAT on purchases (Input tax)
(ii) VAT on sales (Output tax)
(iii) VAT payable to URA

B: **VAT inclusive transactions**

Example 1: Alpha shop had the following VAT inclusive transactions with other VAT registered businesses in a given month.

Product	Purchases (shs)	Sales (shs)
Biscuits Soft drinks	29,500,000 70,800,000	47,200,000 106,200,000

Required to compute;

(i) VAT paid on each product for the month.

VAT paid $= \frac{18}{118}$ x Value added (sales – purchases)

VAT paid on biscuits $= \frac{18}{118}$ x (47,200,000 – 29,500,000)

$= \frac{18}{118}$ x 17,700,000

= shs 2,700,000

VAT paid on soft drinks $= \frac{18}{118}$ x (106,200,000 – 70,800,000)

$= \frac{18}{118}$ 35,400,000

= shs 5,400,000

(ii) Sales value of soft drinks (VAT exclusive)

=Sales value of soft drinks – VAT on sales value.

=106,200,000 - $\frac{18}{118}$ x 106,200,000

=106,200,000 - 16,200,000

=Shs 90,000,000

Example 2: Super wholesalers had the following VAT inclusive transactions with other VAT registered businesses during the month of June, 2021.

Product	Purchases (shs)	Sales (shs)
Watches	35,400,000	42,480,000
Radios	47,200,000	59,000,000

Compute the following;

(i) VAT paid on each product for the month of June, 2021

VAT paid = $\frac{18}{118}$ x Value added (sales – purchases)

VAT paid on watches = $\frac{18}{118}$ x (42,480,000 – 35,400,000)

= $\frac{18}{118}$ 7,080,000

= shs 1,080,000

VAT paid on radios = $\frac{18}{118}$ x (59,000,000 – 47,200,000)

= $\frac{18}{118}$ x 11,800,000

=shs 1,800,000.

(ii) Sales value of watches (VAT exclusive)

=Sales value of watches – VAT on sales value

=42,480,000 - $\frac{18}{118}$ x 42,480,000

=42,480,000 – 6,480,000

=shs 36,000,000

2. **Using Input VAT and Output VAT approach**. This approach involves first calculating Output VAT and Input VAT which eventually helps to determine the VAT liability by getting the difference between Output VAT and Input VAT.

NB: When calculating VAT Using **Input VAT and Output VAT approach**, the VAT rate is applied on the purchase value to obtain the Input VAT and on sales value to obtain Output VAT but not on **value added**.

Example; Malingumu a trader dealing in general merchandise made the following transactions during the month of December 2020.

Products	Purchase price (VAT inclusive) shs	Selling price (VAT inclusive) shs
Biscuits	29,500,000	47,200,000
Soft drinks	70,800,000	106,200,000
Watches	35,400,000	42,480,000
Radios	47,200,000	59,000,000

Using the VAT Input and VAT Output approach,

a) Determine VAT liability on each product.

VAT liability = Output VAT – Input VAT

(i) Biscuits;

Output VAT = $\frac{18}{118}$ x sales value/selling price

= $\frac{18}{118}$ x 47,200,000

= shs 7,200,000

Input VAT = $\frac{18}{118}$ x purchase value/purchase price.

= $\frac{18}{118}$ x 29,500,000

= shs 4,500,000

VAT liability = 7,200,000 – 4,500,000

=shs 2,700,000

(ii) **Soft drinks**;

Output VAT = $\frac{18}{118}$ x 106,200,000

= shs 16,200,000

Input VAT = $\frac{18}{118}$ x 70,800,000

= shs 10,800,000

VAT liability = Output VAT – Input VAT

= 16,200,000 – 10,800,000

= Shs 5,400,000

(iii) Watches;

Output VAT = $\frac{18}{118}$ x 42,480,000
= shs 6,480,000

Input VAT = $\frac{18}{118}$ x 35,400,000
= shs 5,400,000

VAT liability = output VAT – input VAT
= 6,480,000 – 5,400,000
= shs 1,080,000

(iv) Radios;

Output VAT = $\frac{18}{118}$ x 59,000,000
= shs 9,000,000

Input VAT = $\frac{18}{118}$ x 47,200,000
= shs 7,200,000

VAT liability = Output VAT – Input VAT
= 9,000,000 – 7,200,000
=Shs 1,800,000

(b) Compute total VAT liability to URA

VAT liability to URA = Total Output VAT – Total Input VAT

Total Output VAT = 7,200,000 + 16,200,000 + 6,480,000 + 9,000,000
= Shs 38,880,000

Total Input VAT= 4,500,000 + 10,800,000 + 5,400,000 + 7,200,000
= shs 27,900,000

Total VAT liability to URA = 38,880,000 – 27,900,000

= Shs 10,980,000

4. **Customs duties/International trade taxes collected by URA**.

International trade taxes collected by URA include;

- Import duty
- Export duty
- Value Added Tax (VAT)
- Withholding tax
- Excise duty
- Environmental levy/tax

Steps to determine tax liability

Step I. **Determining customs value**; customs value is the cost of goods, Insurance and Freight (cost of transporting goods). This is usually quoted as CIF value.

The customs value can either be in foreign or local currency. If the customs value is in foreign currency, apply the provided exchange rate to convert the customs value to local currency i.e.
Customs value = CIF value x exchange rate.

Step II**. Computing the duties/taxes applicable on imported goods** i.e.

- Import duty = Import duty rate x Customs value.
- Excise duty = Excise duty rate x Excise duty value.
  Excise duty value = Customs value + Import duty.
- Value Added Tax = VAT rate x VAT value.
  VAT value = Customs value + Import duty + Excise duty.
- Withholding Tax = Withholding tax rate x Customs value
- Environmental levy = Environmental levy rate x customs value

NB: The total tax liability/ Total tax payable is equal to the sum of all taxes/duties calculated or involved.

Example: Blessed Auto Care Ltd imports motor vehicle spare parts from Japan worth CIF value \$3000 attracting an import duty of 25%, an excise duty of 60%, VAT of 18% and withholding tax of 6%. Using an exchange rate of 1 dollar = shs 3600, calculate;

(i) Import duty
(ii) Excise duty
(iii) Value Added Tax
(iv) Withholding Tax
(v) Total tax payable to URA

(i) Import duty = Import duty rate x Customs value

Customs value = CIF value x Exchange rate

= 3000 x 3600

= shs 10,800,000

Import duty = $\frac{25}{100}$ x 10,800,000

= shs 2,700,000

(ii) Excise duty = Excise duty rate x Excise duty value

Excise duty value = Customs value + Import duty.

= 10,800,000 + 2,700,000

= shs 13,500,000

Excise duty = $\frac{60}{100}$ x 13,500,000

= shs 8,100,000

(iii) Value Added Tax = VAT rate x VAT value.

VAT value = Customs value + Import duty + Excise duty

= 10,800,000 + 2,700,000 + 8,100,000

= shs 21,600,000

Value Added Tax = $\frac{18}{100} x\ 21{,}6000{,}000$

= shs 3,888,000

(iv) Withholding tax = Withholding tax rate x Customs value

$= \frac{6}{100}\ x\ 10{,}800{,}000$

= shs 648,000

(v) Total tax payable to URA=Import duty+ Excise duty+ VAT+ Withholding tax.

= 27,000,000 + 8,100,000 + 3,888,000 + 648,000.

= shs 15,336,000

Exercise; Azimio a company dealing in the selling of chemicals for making detergents imports its inputs from India at a CIF value of $ 2800 with 25% import duty, 60% excise duty, 18% VAT and 6% withholding tax. If the exchange rate is 1$ =shs 3700. Calculate;

(i) Import duty
(ii) Excise duty
(iii) VAT
(iv) Withholding tax
(v) Tax payable