Kampala International University Uganda

BACHELOR OF COMMERCE

MODULE

PRINCIPLES OF TAXATION

By

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Unit1
Introduction to Taxation
1.1 Introduction

Taxation is the inherent power of the sovereign, exercised through the legislature, to impose burdens upon subjects and objects within its jurisdiction for the purpose of raising revenues to carry out the legitimate objects of government.

It is also defined as the act of levying a tax, i.e. the process or means by which the sovereign, through its law making body, raises income to defray the necessary expenses of government. It is a method of apportioning the cost of government among those who, in some measure, are privileged to enjoy it benefits and must therefore bear its burdens.

Taxes

Are the enforced proportional contributions from persons and property levied by the law making body of the state by virtue of its sovereignty for the support of the government and all pubic needs.

Tax is to impose a financial charge or other levy upon a **taxpayer** (an individual or legal entity) by a state or the functional equivalent of a state such that failure to pay is punishable by law.

Taxes are also imposed by many subnational entities. Taxes consist of direct tax or indirect tax, and may be paid in money or as its labour equivalent (often but not always unpaid labour).

A tax may be defined as a "pecuniary burden laid upon individuals or property owners to support the government [...] a payment exacted by legislative authority."

A tax "is not a voluntary payment or donation, but an enforced contribution, exacted pursuant to legislative authority" and is "any contribution imposed by government [...] whether under the name of toll, tribute, tallage, gabel, impost, duty, custom, excise, subsidy, aid, supply, or other name."

The legal definition and the economic definition of taxes differ in that economists do not consider many transfers to governments to be taxes. For example, some transfers to the public sector are comparable to prices.

Examples include tuition at public universities and fees for utilities provided by local governments. Governments also obtain resources by creating money (e.g., printing bills and minting coins), through voluntary gifts (e.g., contributions to public universities and museums), by imposing penalties (e.g., traffic fines), by borrowing, and by confiscating wealth. From the view of economists, a tax is a non-penal, yet compulsory transfer of resources from the private to the public sector levied on a basis of predetermined criteria and without reference to specific benefit received.

In modern taxation systems, taxes are levied in money; but, in-kind and *corvée* taxation are characteristic of traditional or pre-capitalist states and their functional equivalents.

The method of taxation and the government expenditure of taxes raised is often highly debated in politics and economics. Tax collection is performed by a government agency such as Canada Revenue Agency, the Internal Revenue Service (IRS) in the United States, or Her Majesty's Revenue and Customs (HMRC) in the UK. When taxes are not fully paid, civil penalties (such as fines or forfeiture) or criminal penalties (such as incarceration)[2] may be imposed on the non-paying entity or individual.

A tax on earnings is a tax on income whether it is salary, inheritance, or profits from investments. This is often contrasted with a consumption tax; where taxes are impose d on those goods and services that are consumed. Some argue that consumption tax would be a better way to go than tax on earnings, since it is argued that people who earn more, would reasonably spend more, thus making the tax structure more equitable.

1.2 Purposes of Taxation

- Revenue or fiscal, the primary purpose of taxation on the part of the government is to provide funds or property with which to promote the general welfare and the protection of its citizens and to enable it to finance its multifarious activities.
- Non-revenue or regulatory, taxation may also be employed for purposes of regulation or control.
    - Imposition of tariffs on imported goods to protect local industries
    - The adoption of progressively higher tax rates to reduce inequalities in wealth and income

- The increase or decrease of taxes to prevent inflation or ward off depression

Essential elements f a tax

- It is an enforced contribution
- It is generally payable in money
- It is proportionate in character
- It is levied on persons, property, or the exercise of a right or privilege
- It is levied by the state which has jurisdiction over the subject or object of taxation
- It is levied by the law making body of the state
- It is levied for public purpose or purposes

1.3 Advantages and disadvantages of taxation

Advantages of imposing a tax on earnings can include the following:

- People are taxed based on total income, thus people who make less theoretically pay less tax on earnings.
- Not all people consume at the same rate, therefore tax on earnings is a more equitable way of assessing tax than with a consumption tax.
- People with lower incomes would be the most impacted by a straight tax on consumption, since even necessary items like cars would be significantly more expensive.
- Income is an easier way to levy taxes and decide deductions. While people may deal with a few pay stubs they have to save, in consumption tax, people might have to save receipts for every purchase they made during a year in order to qualify for tax breaks.

Disadvantages of a tax on earnings include:

- The collection of a tax on earnings is generally thought to more difficult than a consumption tax which would be levied at the point of sale.
- For those in the middle class and lower classes, an earnings tax may be a financial hardship, regardless of the amount.
- Some believe that income tax is a violation of a citizen's individual freedom. Especially Libertarians argue that tax on earnings violates the individual’s right to decide how to use the money he earns.
- People paid “under the table” may be able to evade paying any income taxes.

Both methods of taxation are in use in the United States. Most states and many cities impose consumption or sales taxes on certain items. Many also require people to pay state income tax as well as federal income tax. This leads to the claim that US citizens are disproportionately taxed according to where they live, be it state to state, county to county, or rural versus urban areas. Those who claim that this is a disadvantage of the current system believe that it would be best to have one system in place that assesses taxation more equitably.

An idea that has been garnering increasing support is called Fair Tax. This would be similar to consumption tax, and some feel it would not only benefit individuals but also corporations. In this plan, people would pay a 23% tax on purchases of most goods and services, often excluding food. This would in most cases, along with state sales tax increase taxes on purchases to about 30%. Some argue this method would lower prices and make production less expensive. Others say that the middle class would bear the burden of the majority of taxes under Fair Tax.

The method of taxation is a complex one that requires extraordinary scrutiny. Any change to the method of taxation would require congressional approval and possibly constitutional amendments. On this issue of tax on earnings, abundant and multiple opinions exist which further complicate matters.

1.4 Evolution of taxation law

Evaluation of Tax

Tax is **fee** that is **charged by government** which is **on income, activity or product**. Tax when directly levied on corporate or personal incomes then we call it as direct-tax. Taxes when levied upon cost of service or good then we call it as indirect-tax. **Taxation's purpose** is financing the expenditures of government. Taxes very significant use is financing public services and goods, like cleaning of street and lighting of street. As public services and goods don't permit exclusion of non-payer, or permit exclusion through consumer, so there can't be mart in service or goods, and therefore government provide them, which incline for financing themselves mostly through the taxes.

Standards for Evaluation of Tax

- **Simplicity** – Tax-law must be in such a way that its rules are understood by the tax payers easily.
- **Fairness** – Taxpayers who are situated similarly must be similarly taxed.
- **Economic efficiency and growth** – System of tax must not reduce or impede economies productive efficiency.
- **Neutrality** – Tax-law's effect on decision's of taxpayer of how a specific transaction be carried must be minimum.
- **Transparency** – It should be known by a taxpayer that when and how tax is being imposed upon him.
- **Reducing noncompliance** – Tax must be formed or structured in such a way to reduce noncompliance.
- **Collection being cost effective** – Tax collected by taxpayer and government must be very less.
- **Certainty** – Rules of must include when, how and how much one has to pay tax.

Structures and Tax Rate:

Marginal-Tax	**Household's Head**	**Married separately filing**	**Married jointly Filing / Educated Widow**	**Single**
10%	$0 to $11,950	$0 to $8,375	$0 to $16,750	$0 to $8,375
15%	$11,951 to $45,550	$8,376 to $34,000	$16,751 to $68,000	$8,376 to $34,000
25%	$45,551 to $117,650	$34,001 to $68,650	$68,001 to $137,300	$34,001 to $82,400
28%	$117,651 to $190,550	$68,651 to $104,625	$137,301 to $209,250	$82,401 to $171,850
33%	$190,551 to $373,650	$104,626 to $186,825	$209,251 to $373,650	$171,851 to $373,650
35%	$373,651+	$186,826+	$373,651+	$373,651+

Questions:

Review Questions

1. Define Tax.
2. Explain standards for evaluation a Tax.
3. State Tax rates and structures.

Unit 2
Taxation theory and practice

2.1 Theory and basis of taxation

The power of taxation proceeds upon the theory that the existence of government is a necessity; that it cannot continue without means to pay its expenses; and that for these means, it has a right to compel all its citizens and property within its limits to contribute.

The basis of taxation is found in the reciprocal duties of protection and support between the state and its inhabitants. In return for his contribution, the taxpayer received benefits and protection from the government. This the so-called benefits received principle.

Life blood or necessity theory

The life blood theory constitutes the theory of taxation, which provides that the existence o government is a necessity; that government cannot continue without means to pay its expenses; and that for these means it has a right to compel its citizens and property within its limits to contribute.

In commissioner vs. Algue, the supreme court said that taxes are the lifeblood of the government and should be collected without unnecessary hindrance. They are what we pay for a civilized society. Without taxes, the government would be paralyzed for lack of motive power to activate and operate it. The government, of its part, is expected to respond in the form of tangible and intangible benefits intended to improved the lives of the people and enhance their moral and material values.

Illustrations of lifeblood theory

- Collection of taxes cannot be enjoined by injunction
- Taxes could not be the subject of compensation or set off
- A valid tax may result in destruction of the taxpayer's property
- Taxation is a unlimited and plenary power

Benefit received principles

This principle serves as the basis of taxation and is founded on the reciprocal duties of protection and support between the state and its inhabitants. Also called symbiotic relation between the state and its citizens.

In return for his contribution, the taxpayer receives the general advantages and protection which the government affords the taxpayer and his property. One is compensation or consideration for the other, protection for support and support for protection

However it does not mean that only those who are able to and do pay taxes can enjoy the privileges and protection given to a citizen by the government.

In fact, from the contribution received, the government renders no special or commensurate benefit to any particular property or person. The only benefit to which the taxpayer is entitled is that derived from the enjoyment of the privileges of living in an organized society established and safeguarded by the devolution of taxes to public purpose.

Taxes are essential to the existence of the government. The obligation to pay taes rests not upon the privileges enjoyed by or the protection afforded to the citizen by the government, but upon the necessity of money for the support of the state. For this reason, no one is allowed to object to or resist payment of taxes solely because no personal benefit to him can be pointed out as arising from the tax.

2.2 Types of Taxes

Direct and indirect

Taxes are sometimes referred to as "direct taxes" or "indirect taxes". The meaning of these terms can vary in different contexts, which can sometimes lead to confusion. An economic definition, by Atkinson, states that

"...direct taxes may be adjusted to the individual characteristics of the taxpayer, whereas indirect taxes are levied on transactions irrespective of the circumstances of buyer or seller."

According to this definition, for example, income tax is "direct", and sales tax is "indirect". In law, the terms may have different meanings. In U.S. constitutional law, for instance, direct taxes refer to poll taxes and property taxes, which are based on simple existence or ownership. Indirect taxes are imposed on events, rights, privileges, and activities. Thus, a tax on the sale of property would be considered an indirect tax, whereas the tax on simply owning the property itself would be a direct tax. The distinction between direct and indirect taxation can be subtle but can be important under the law.

Direct tax

A direct tax is demanded from the person who also shoulders the burden of the tax. It is a tax which the taxpayer is directly or primarily liable and which he or she cannot shift to another.

Indirect tax

An indirect tax is demanded from a person in the expectation and intention that he or she shall indemnify himself or herself at the expense of another, falling finally upon the ultimate purchaser or consumer. A tax which the taxpayer can shift to another.

Proportional, progressive, and regressive

An important feature of tax systems is the percentage of the tax burden as it relates to income or consumption. The terms progressive, regressive, and proportional are used to describe the way the rate progresses from low to high, from high to low, or proportionally. The terms describe a distribution effect, which can be applied to any type of tax system (income or consumption) that meets the definition.

- A progressive tax is a tax imposed so that the effective tax rate increases as the amount to which the rate is applied increases.
- The opposite of a progressive tax is a regressive tax, where the effective tax rate decreases as the amount to which the rate is applied increases. This effect is commonly produced where means testing is used to withdraw tax allowances or state benefits.
- In between is a proportional tax, where the effective tax rate is fixed, while the amount to which the rate is applied increases.

The terms can also be used to apply meaning to the taxation of select consumption, such as a tax on luxury goods and the exemption of basic necessities may be described as having progressive effects as it increases a tax burden on high end consumption and decreases a tax burden on low end consumption.

Proportional Tax

Tax based on a fixed percentage of the amount of the property receipts or other basis to be taxed. Example real estate tax

Progressive or graduated tax

Tax the rate of which increases as the tax base or bracket increases. Example, income tax

Digressive tax rate

Progressive rate stops at a certain point, progression halts at a particular stage.

Regressive tax

Tax the rate of which decreases as the tax base or bracket increases. There is no such tax in the Philippines.

Other Types of Taxes

Capital Gains taxes are paid on investments that have appreciated. Frequently these investments have been sold. Examples would be stocks, bonds, and real estate. Most losses can be "written off" on the federal income tax level, and like corporate taxes, these are usually best handled by professional tax preparers.

Inheritance or Estate Taxes: Of the 7 types of taxes, this is the only type where a tax can happen because of a death. A certain amount of estate money that may be passed on with no tax consequence. Once that level is met, however, the taxes are usually quite steep. Life insurance is often used to offset inheritance taxes, and is one reason insurance is so critical in estate planning.

- The difference between a direct and indirect tax is complicated because it truly depends on whether you are asking from a “legal” or an “economic” perspective. In economics, a direct tax will refer to any levy that is both imposed and collected
- on a specific group of people or organizations. A sales tax, for instance, would not be considered a direct tax because the money is collected from merchants, not from the people who actually pay the tax (the consumers). An example of direct taxation would be income taxes that are collected from the people who actually earn their income. Indirect taxes are collected from someone or some

organization other than the person or entity that would normally be responsible for the taxes.

In this economic context, the law may actually determine the person or entities from which the tax will be collected, but has nothing to do with how that tax burden is distributed in the market. Who bears the economic burden of the tax itself will be determined by market forces and can be calculated by comparing the price of the goods after the tax has been imposed with the price of the goods prior to the tax being in place. For example, if the price of a gallon of gasoline was $2.50 without taxes and the government suddenly imposed a $0.40 tax, the economic forces of supply and demand would ultimately decide how this new burden is distributed between buyers and sellers. For instance, the price could increase to $2.75 per gallon after the tax, with buyers absorbing $0.25 of the increase and sellers the remaining $0.15. The law may have imposed the tax but the marketplace ultimately decided how it would be distributed.

In a legal sense, the meaning of direct and indirect taxes changes so that a direct tax, according to the U.S. Constitution, applies only to property and poll taxes. These direct taxes are based on simple ownership or existence. Indirect taxes are imposed upon a broad range of abstract ideas, including rights, privileges, and activities. In this sense, a tax on the sale of property would be considered an indirect tax while the tax actually owed on the property would be direct.

The legal distinction between direct and indirect taxes was important enough to warrant the passage of a Constitutional amendment - 16th Amendment - in 1913. Prior to this amendment the law was written in such a way that all direct taxes imposed by the government had to be directly apportioned to the population. In other words, any state having half as many people as another state would only have direct tax revenue that equaled half that of the larger state. The direct tax legal

2.3 Purposes and Effects

Money provided by taxation has been used by states and their functional equivalents throughout history to carry out many functions. Some of these include expenditures on war, the enforcement of law and public order, protection of property, economic infrastructure (roads, legal tender, enforcement of contracts, etc.), public works, social engineering, and the operation of government itself. Governments also use taxes to fund welfare and public services. These services can include education systems, health care systems, pensions for the elderly, unemployment benefits, and public transportation. Energy, water and waste management systems are also common public utilities. Colonial and modernizing states have also used cash taxes to draw or force reluctant subsistence producers into cash economies.

Governments use different kinds of taxes and vary the tax rates. This is done to distribute the tax burden among individuals or classes of the population involved in taxable activities, such as business, or to redistribute resources between individuals or classes in the population. Historically, the nobility were supported by taxes on the poor; modern social security systems are intended to support the poor, the disabled, or the retired by taxes on those who are still working. In addition, taxes are applied to fund foreign aid and military ventures, to influence the macroeconomic performance of the economy (the government's strategy for doing this is called its fiscal policy; see also tax exemption), or to modify patterns of consumption or employment within an economy, by making some classes of transaction more or less attractive.

A nation's tax system is often a reflection of its communal values or/and the values of those in power. To create a system of taxation, a nation must make choices regarding the distribution of the tax burden—who will pay taxes and how much they will pay—and how the taxes collected will be spent. In democratic nations where the public elects those in charge of establishing the tax system, these choices reflect the type of community that the public and/or government wishes to create. In countries where the public does not have a significant amount of influence over the system of taxation, that system may be more of a reflection on the values of those in power.

All large businesses incur administrative costs in the process of delivering revenue collected from customers to the suppliers of the goods or services being purchased. Taxation is no different, the resource collected from the public through taxation is always greater than the amount which can be used by the government. The difference is called *compliance cost*, and includes for example the labour cost and other expenses incurred in complying with tax laws and rules. The collection of a tax in order to spend it on a specified purpose, for example collecting a tax on alcohol to pay directly for alcoholism rehabilitation centres, is called hypothecation. This practice is often disliked by finance ministers, since it reduces their freedom of action. Some economic theorists consider the concept to be intellectually dishonest since, in reality, money is fungible. Furthermore, it often happens that taxes or excises initially levied to fund some specific government programs are then later diverted to the government general fund. In some cases, such taxes are collected in fundamentally inefficient ways, for example highway tolls.

Some economists, especially neo-classical economists, argue that all taxation creates market distortion and results in economic inefficiency. They have therefore sought to identify the kind of tax system that would minimize this distortion.

Since governments also resolve commercial disputes, especially in countries with common law, similar arguments are sometimes used to justify a sales tax or value added tax. Others (e.g. libertarians) argue that most or all forms of taxes are immoral due to their involuntary (and therefore eventually coercive/violent) nature. The most extreme anti-tax view is anarcho-capitalism, in which the provision of *all* social services should be voluntarily bought by the person(s) using them.

2.4 Rationale of Taxation

Acceptance of income taxation as the fairest kind of tax is based on the premise that an individual's income is the best single index of one's ability to contribute to the support of government. Moreover, compared with sales taxes or property taxes, an income tax is easier to change when the taxpayer's ability to pay taxes is affected by various life-course circumstances (such as the number of dependents the taxpayer supports or extraordinary medical expenses).

Another argument for income taxation proceeds from its relation to a nation's economic performance. Compared with the amounts produced by sales taxes or wealth taxes, the receipts from the individual income tax tend to rise more steeply in economic booms and drop more sharply in recessions. This occurs in part because individual income itself is quite sensitive to changes in the level of overall economic activity. In addition, income taxation is regulated by a progressive rate structure (which can be thought to include the personal exemption as a zero tax rate). As a result, a rise in individual income creates additional income that is taxed at a higher rate. Conversely, a drop in individual income causes some taxpayers to be taxed at lower bracket rates. Because of this, taxpayers' tax liabilities fluctuate more than their incomes—the individual income tax actually offsets some effects of expansionary and contractionary forces during business cycles. Exceptions to a tax code—such as deductions, the indexation of exemptions, and the measurement of income from capital for inflation—reduce the potential for stabilization. (See progressive tax; regressive tax.)

The individual income tax reduces the amount of income individuals have available to spend, save, or invest. Of course, any tax has this result. The question is whether other taxes may achieve the same end more efficiently or with fewer undesirable side effects. It has been argued that a tax on income discriminates against saving and is less favourable to economic growth than a tax on spending because an income tax is levied on all income—even that which is saved and made available for investment—while a consumption tax is not levied on moneys that are put into savings.

It is difficult to determine the extent to which an income tax reduces the incentive to work. To the extent that the tax reduces total income after taxes, it may lead some persons to work longer in an effort to maintain an established standard of living (the income effect). To the extent that the tax reduces the reward for an extra hour's work, it may make the taxpayer decide to work less and to indulge in more leisure (the substitution effect); presumably, the larger the income and the more steeply progressive the tax, the greater this substitution effect will be. Finally, a progressive income tax is sometimes said to have an adverse effect on investment, especially in the case of risky ventures, but this has been shown to depend on the provisions a tax law makes for allowing investors to write off their losses.

2.5 Objectives of Taxation

As you are aware, the cold is the hitting book of your **resume objectives**. It tells about your career ambition and how the -to-be employer will get benefited if he selects you as a candidate. So resume cold should be specific for accurate job profile.

Resume cold for position of a tax acquirement beneficiary needs to be accounting because assorted demands of the job

Once you are austere with assorted roles acquirement tax beneficiary has to undertake, you will be bright about how to address assorted sections of the resume of the tax acquirement collector. Resume cold samples are readily available. So accede the activities and address the resume cold accordingly.

Job Demands of a Tax Acquirement Collector

- Tax accumulating from humans as able-bodied as business professionals
- Maintain the records, procedures, cipher changes, accounting procedures. It ultimately is associated with alive on banking information
- Take affliction of the issues accompanying to tax allotment and problems associated with it. If any of the acknowledged issues are raised, plan the band of activity or plan on the band of activity to get out of the litigation. Attend accidental appeals hearings on contested cases from added co professionals
- Coordination and advice with the tax payers to acquaint them the procedures, data transaction accompanying issues or issues accompanying to refund. Acquaint the tax payers about overpayment or underpayment
- Pursue all the activities accompanying to tax returns, i.e. to ample up the accompanying information, action the advice etc.
- Broadly speaking the tax acquirement beneficiary deals with taxes, customs and sales tax returns

There are abounding added activities the acquirement beneficiary has to undergo. It is mentioned in the job requirements or job profile. Go through what the -to-be employer wants. Understand which area you are declared to be added alive in? It may be sales tax, customs or assets tax. So **resume objectives** will alter depending aloft the area in which you are searching for a job.

You can accredit samples on the internet and can address the cold that can actualize an consequence at a glance. In added words you may say that it is the accommodation authoritative account whether the -to-be employer would additional time to apprehend your resume added or not. So beware a acceptable cold account can accomplish or breach the path.

2.6 Tax Planning And Management

Taxes are the money paid by companies to government entities for the privilege of doing business. The amount of taxes paid by companies depends on different business factors, including the amount of sales revenue, assets owned by the business and wealth generated through various equity investments. Most companies spend copious amounts of time determining their tax liabilities to ensure they do not face penalties for the underpayment of taxes.

- Tax planning is a wider term and tax management is narrow term which is a part of tax planning.
- Tax planning emphasizes on tax minimization whereas, tax management is compliance of legal formalities.
- Every person does not require tax planning but tax management is essential for everyone.
- Tax planning is about future benefits and tax management is about present benefits.

Tax planning is essentially the systematic analysis of the differing tax options you have which is aimed at the minimization your tax liability in the current and future tax periods.

If you own a business in Uganda, I would recommend that you convene probably in the middle of the Uganda government's financial year and implementing various strategies that will help you minimize the amount of taxes you will pay to Uganda Revenue Authority.

It would be good to go through this process with the help of a competent Uganda Tax Consultant

Some of the key areas/factors you should look at during your tax planning in Uganda would include:

- The choice of accounting and inventory-valuation methods
- The timing of equipment purchases,
- The spreading of business income among family members and
- The selection of tax-favored benefit plans and investments.

Furthermore, depending on the ownership structure of your Uganda business, you will find some areas of tax planning that are specific to your business form, whether sole proprietorship, partnership, or limited liability company.

Tax planning involves conceiving of and implementing various strategies in order to minimize the amount of taxes paid for a given period. For a small business, minimizing the tax liability can provide more money for expenses, investment, or growth. In this way, tax planning can be a source of working capital. According to *The Entrepreneur Magazine Small Business Advisor,* two basic rules apply to tax planning. First, a small business should never incur additional expenses only to gain a tax deduction. While purchasing necessary equipment prior to the end of the tax year can be a valuable tax planning strategy, making unnecessary purchases is not recommended. Second, a small business should always attempt to defer taxes when possible. Deferring taxes enables the business to use that money interest-free, and sometimes even earn interest on it, until the next time taxes are due.

Experts recommend that entrepreneurs and small business owners conduct formal tax planning sessions in the middle of each tax year. This approach will give them time to apply their strategies to the current year as well as allow them to get a jump on the following year. It is important for small business owners to maintain a personal awareness of tax planning issues in order to save money. Even if they employ a professional bookkeeper or accountant, small business owners should keep careful tabs on their own tax preparation in order to take advantage of all possible opportunities for deductions and tax savings. "Whether or not you enlist the aid of an outsider, you should understand the basic provisions of the tax code," Albert B. Ellentuck wrote in the *Laventhol and Horwath Small Business Tax Planning Guide.* "Just as you would not turn over the management of your money to another person, you should not blindly allow someone else to take complete charge of your tax paying responsibilities." In addition, as Frederick W. Dailey wrote in his book *Tax Savvy for Small Business,* "Tax knowledge has powerful profit potential. Knowing what the tax law has to offer can give you a far better bottom line than your competitors who don't bother to learn."

General Areas of Tax Planning

There are several general areas of tax planning that apply to all sorts of small businesses. These areas include the choice of accounting and inventory-valuation methods, the timing of equipment purchases, the spreading of business income among family members, and the selection of tax-favored benefit plans and investments. There are also some areas of tax planning that are specific to certain business forms—i.e., sole proprietorships, partnerships, C corporations, and S corporations. Some of the general tax planning strategies are described below:

Accounting Methods,

Accounting methods refer to the basic rules and guidelines under which businesses keep their financial records and prepare their financial reports. There are two main accounting methods used for record-keeping: the cash basis and the accrual basis. Small business owners must decide which method to use depending on the legal form of the business, its sales volume, whether it extends credit to customers, and the tax requirements set forth by the Internal Revenue Service (IRS). The choice of accounting method is an issue in tax planning, as it can affect the amount of taxes owed by a small business in a given year.

Accounting records prepared using the cash basis recognize income and expenses according to real-time cash flow. Income is recorded upon receipt of funds, rather than based upon when it is actually earned, and expenses are recorded as they are paid, rather than as they are actually incurred. Under this accounting method, therefore, it is possible to defer taxable income by delaying billing so that payment is not received in the current year. Likewise, it is possible to accelerate expenses by paying them as soon as the bills are received, in advance of the due date. The cash method is simpler than the accrual method, it provides a more accurate picture of cash flow, and income is not subject to taxation until the money is actually received.

In contrast, the accrual basis makes a greater effort to recognize income and expenses in the period to which they apply, regardless of whether or not money has changed hands. Under this system, revenue is recorded when it is earned, rather than when payment is received, and expenses recorded when they are incurred, rather than when payment is made. The main advantage of the accrual method is that it provides a more accurate picture of how a business is performing over the long-term than the cash method. The main disadvantages are that it is more complex than the cash basis, and that income taxes may be owed on revenue before payment is actually received. However, the accrual basis may yield favorable tax results for companies that have few receivables and large current liabilities.

Under generally accepted accounting principles (GAAP), the accrual basis of accounting is required for all businesses that handle inventory, from small retailers to large manufacturers. It is also required for corporations and partnerships that have gross sales over $5 million per year, though there are exceptions for farming businesses and qualified personal service corporations—such as doctors, lawyers, accountants, and consultants. Other businesses generally can decide which accounting method to use based on the relative tax savings it provides.

Inventory Valuation Methods

The method a small business chooses for inventory valuation can also lead to substantial tax savings. Inventory valuation is important because businesses are required to reduce the amount they deduct for inventory purchases over the course of a year by the amount remaining in inventory at the end of the year. For example, a business that purchased $10,000 in inventory during the year but had $6,000 remaining in inventory at the end of the year could only count $4,000 as an expense for inventory purchases, even though the actual cash outlay was much larger. Valuing the remaining inventory differently could increase the amount deducted from income and thus reduce the amount of tax owed by the business.

The tax law provides two possible methods for inventory valuation: the first-in, first-out method (FIFO); and the last-in, first-out method (LIFO). As the names suggest, these inventory methods differ in the assumption they make about the way items are sold from inventory. FIFO assumes that the items purchased the earliest are the first to be removed from inventory, while LIFO assumes that the items purchased most recently are the first to be removed from inventory. In this way, FIFO values the remaining inventory at the most current cost, while LIFO values the remaining inventory at the earliest cost paid that year.

LIFO is generally the preferred inventory valuation method during times of rising costs. It places a lower value on the remaining inventory and a higher value on the cost of goods sold, thus reducing income and taxes. On the other hand, FIFO is generally preferred during periods of deflation or in industries where inventory can tend to lose its value rapidly, such as high technology. Companies are allowed to file Form 970 and switch from FIFO to LIFO at any time to take advantage of tax savings. However, they must then either wait ten years or get permission from the IRS to switch back to FIFO.

Equipment Purchases

Under Section 179 of the Internal Revenue Code, businesses are allowed to deduct a total of $18,000 in equipment purchases during the year in which the purchases are made. Any purchases above this amount must be depreciated over several future tax periods. It is often advantageous for small businesses to use this tax incentive to increase their deductions for business expenses, thus reducing their taxable income and their tax liability. Necessary equipment purchases up to the limit can be timed at year end and still be fully deductible for the year. This tax incentive also applies to personal property put into service for business use, with the exception of automobiles and real estate.

Wages Paid To Family Members

Self-employed persons can also reduce their tax burden by paying wages to a spouse or to dependent children. Wages paid to children under the age of 18 are not subject to FICA (Social Security and Medicare) taxes. Under normal circumstances, employers are required to withhold 7.65 percent of the first $62,700 of an employee's income for FICA taxes. Employers are also required to match the 7.65 percent contributed by every employee, so that the total FICA contribution is 15.3 percent. Self-employed persons are required to pay both the employer and employee portions of the FICA tax.

But the FICA taxes are waived when the employee is a dependent child of the small business owner, saving the child and the parent 7.65 percent each. In addition, the child's wages are still considered a tax deductible business expense for the parent—thus reducing the parent's taxable income. Although the child must pay normal income taxes on the wages he or she receives, it is likely to be at a lower tax rate than the parent pays. Some business owners are able to further reduce their tax burden by paying wages to their spouse. If these wages bring the business owner's net income below $62,700—the threshold for FICA taxes—then they may reduce the self-employment tax owed by business owner. It is important to note, however, that the child or spouse must actually work for the business and that the wages must be reasonable for the work performed.

Benefits Plans and Investments

Tax planning also applies to various types of employee benefits that can provide a business with tax deductions, such as contributions to life insurance, health insurance, or retirement plans. As an added bonus, many such benefit programs are not considered taxable income for employees. Finally, tax planning applies to various types of investments that can shift tax liability to future periods, such as treasury bills, bank certificates, savings bonds, and deferred annuities. Companies can avoid paying taxes during the current period for income that is reinvested in such tax-deferred instruments.

Tax Planning for Different Business Forms

"The first step in tax planning—for small business owners and professionals, at least—is to select the right form of organization for your enterprise," according to Albert B. Ellentuck in the *Laventhol and Horwath Small Business TaxPlanning Guide.* "You'll end up paying radically different amounts of income tax depending on the form you select. And your odds of being audited by the IRS will change, too." Many aspects of tax planning are specific to certain business forms; some of these are discussed below:

Sole Proprietorships and Partnerships

Tax planning for sole proprietorships and partnerships is in many ways similar to tax planning for individuals. This is because the owners of businesses organized as sole proprietors and partnerships pay personal income tax rather than business income tax. These small business owners file an informational return for their business with the IRS, and then report any income taken from the business for personal use on their own personal tax return. No special taxes are imposed except for the self-employment tax (SECA), which requires all self-employed persons to pay both the employer and employee portions of the FICA tax, for a total of 15.3 percent.

Since they do not receive an ordinary salary, the owners of sole proprietorships and partnerships are not required to withhold income taxes for themselves. Instead, they are required to estimate their total tax liability and remit it to the IRS in quarterly installments, using Form 1040 ES. It is important that the amount of tax paid in quarterly installments equal either the total amount owed during the previous year or 90 percent of their total current tax liability. Otherwise, the IRS may charge interest and impose a stiff penalty for underpayment of estimated taxes.

Since the IRS calculates the amount owed quarterly, a large lump-sum payment in the fourth quarter will not enable a taxpayer to escape penalties. On the other hand, a significant increase in withholding in the fourth quarter may help, because tax that is withheld by an employer is considered to be paid evenly throughout the year no matter when it was withheld. This leads to a possible tax planning strategy for a self-employed person who falls behind in his or her estimated tax payments. By having an employed spouse increase his or her withholding, the self-employed person can make up for the deficiency and avoid a penalty. The IRS has also been known to waive underpayment penalties for people in special circumstances. For example, they might waive the penalty for newly self-employed taxpayers who underpay their income taxes because they are making estimated tax payments for the first time.

Another possible tax planning strategy applies to partnerships that anticipate a loss. At the end of each tax year, partnerships file the informational Form 1065 (Partnership Statement of Income) with the IRS, and then report the amount of income that accrued to each partner on Schedule K1. This income can be divided in any number of ways, depending on the nature of the partnership agreement. In this way, it is possible to pass all of a partnership's early losses to one partner in order to maximize his or her tax advantages.

Corporations

Tax planning for C corporations is very different than that for sole proprietorships and partnerships. This is because profits earned by C corporations accrue to the corporation rather than to the individual owners, or shareholders. A corporation is a separate, taxable entity under the law, and different corporate tax rates apply based on the amount of net income received. As of 1997, the corporate tax rates were 15 percent on income up to $50,000, 25 percent on income between $50,000 and $75,000, 34 percent on income between $75,000 and $100,000, 39 percent on income between $100,000 and $335,000, and 34 percent on income between $335,000 and $10 million. Personal service corporations, like medical and law practices, pay a flat rate of 35 percent. In addition to the basic corporate tax, corporations may be subject to several special taxes.

Corporations must prepare an annual corporate tax return on either a calendar-year basis (the tax year ends December 31, and taxes must be filed by March 15) or a fiscal-year basis (the tax year ends whenever the officers determine). Most Subchapter S corporations, as well as C corporations that derive most of their income from the personal services of shareholders, are required to use the calendar-year basis for tax purposes. Most other corporations can choose whichever basis provides them with the most tax benefits. Using a fiscal-year basis to stagger the corporate tax year and the personal one can provide several advantages. For example, many corporations choose to end their fiscal year on January 31 and give their shareholder/employees bonuses at that time. The bonuses are still tax deductible for the corporation, while the individual shareholders enjoy use of that money without owing taxes on it until April 15 of the following year.

Both the owners and employees of C corporations receive salaries for their work, and the corporation must withhold taxes on the wages paid. All such salaries are tax deductible for the corporations, as are fringe benefits supplied to employees. Many smaller corporations can arrange to pay out all corporate income in salaries and benefits, leaving no income subject to the corporate income tax. Of course, the individual shareholder/employees are required to pay personal income taxes. Still, corporations can use tax planning strategies to defer or accrue income between the corporation and individuals in order to pay taxes in the lowest possible tax bracket. The one major disadvantage to corporate taxation is that corporate income is subject to corporate taxes, and then income distributions to shareholders in the form of dividends are also taxable for the shareholders. This situation is known as "double taxation."

S Corporations

Subchapter S corporations avoid the problem of double taxation by passing their earnings (or losses) through directly to shareholders, without having to pay dividends. Experts note that it is often preferable for tax planning purposes to begin a new business as an S corporation rather than a C corporation. Many businesses show a loss for a year or more when they first begin operations. At the same time, individual owners often cash out investments and sell assets in order to accumulate the funds needed to start the business. The owners would have to pay tax on this income unless the corporate losses were passed through to offset it.

Another tax planning strategy available to shareholder/employees of S corporations involves keeping FICA taxes low by setting modest salaries for themselves, below the Social Security base. S corporation shareholder/employees are only required to pay FICA taxes on the income that they receive as salaries, not on income that they receive as dividends or on earnings that are retained in the corporation. It is important to note, however, that unreasonably low salaries may be challenged by the IRS.

Review Questions

1. What are factors considered when carrying out tax planning?

Unit 3
Tax Administration
3.1 Introduction

Administration and enforcement

One type of flat tax taxes all income once at its source. Hall and Rabushka (1995) includes a proposed amendment to the US Revenue Code implementing the variant of the flat tax they advocate.

This amendment, only a few pages long, would replace hundreds of pages of statutory language (although it is important to note that much statutory language in taxation statutes is *not* directed at specifying graduated tax rates). As it now stands, the USA Revenue Code is over 9 million words long and contains many loopholes, deductions, and exemptions which, advocates of flat taxes claim, render the collection of taxes and the enforcement of tax law complicated and inefficient. It is further argued that current tax law retards economic growth by distorting economic incentives, and by allowing, even encouraging, tax avoidance. With a flat tax, there are fewer incentives than in the current system to create tax shelters and to engage in other forms of tax avoidance.

Flat tax critics contend that a flat tax system could be created with many loopholes, or a progressive tax system without loopholes, and that a progressive tax system could be as simple, or simpler, than a flat tax system. A simple progressive tax would also discourage tax avoidance.

Under a pure flat tax without deductions, companies could simply, every period, make a single payment to the government covering the flat tax liabilities of their employees and the taxes owed on their business income. For example, suppose that in a given year, ACME earns a profit of 3 million, pays 2 million in salaries, and spends an added 1 million on other expenses the IRS deems to be taxable income, such as stock options, bonuses, and certain executive privileges. Given a flat rate of 15%, ACME would then owe the IRS $(3M + 2M + 1M) \times 0.15 = 900{,}000$. This payment would, in one fell swoop, settle the tax liabilities of ACME's employees as well as taxes it owed by being a firm. Most employees throughout the economy would never need to interact with the IRS, as all tax owed on wages, interest, dividends, royalties, etc. would be withheld at the source. The main exceptions would be employees with incomes from personal ventures.

The *Economist* claims that such a system would reduce the number of entities required to file returns from about 130 million individuals, households, and businesses, as at present, to a mere 8 million businesses and self-employed.

This simplicity would remain even if realized capital gains were subject to the flat tax. In that case, the law would require brokers and mutual funds to calculate the realized capital gain on all sales and redemptions. If there were a gain, 15% of the gain would be withheld and sent to the IRS. If there were a loss, the amount would be reported to the IRS, which would offset gains with losses and settle up with taxpayers at the end of the period.

Under a flat tax, the government's cost of processing tax returns would become much smaller, and the relevant tax bodies could be abolished or massively downsized. The people freed from working in administering taxes will then be employed in jobs that are more productive. If combined with a provision to allow for negative taxation, the flat tax itself can be implemented in an even simpler way.

Economic efficiency

A common approximation in economics is that the economic distortion or excess burden from a tax is proportional to the square of the tax rate.

Revenues

Theoretically, a flat tax would increase tax revenues, by simplifying the tax code and removing the many loopholes currently exploited to pay less tax.

The Russian Federation is a considered a prime case of the success of a flat tax; the real revenues from its Personal Income Tax rose by 25.2% in the first year after the Federation introduced a flat tax, followed by a 24.6% increase in the second year, and a 15.2% increase in the third year. The Laffer curve predicts such an outcome, attributing the primary reason for the greater revenue to higher levels of economic growth stemming from the introduction of the flat tax.

The Russian example is often used as proof of the validity of this analysis, despite an IMF study in 2006 found that there was no sign "of Laffer-type behavioral responses generating revenue increases from the tax cut elements of these reforms" in Russia or in other countries. Of course, since the flat tax is heavily advocated by supply-side economists, who are often in direct conflict with the IMF, this is not an unexpected result.

3.2 Structure of the Tax Administration System

Overall structure

Some taxes other than the income tax (for example, taxes on sales and payrolls) tend to be regressive. Hence, making the income tax flat could result in a regressive overall tax structure. Under such a structure, those with lower incomes tend to pay a higher proportion of their income in total taxes than the affluent do. The fraction of household income that is a return to capital (dividends, interest, royalties, profits of unincorporated businesses) is positively correlated with total household income. Hence a flat tax limited to wages would seem to leave the wealthy better off. Modifying the tax base can change the effects. A flat tax could be targeted at income (rather than wages), which could place the tax burden equally on all earners, including those who earn income primarily from returns on investment. Tax systems could utilize a flat sales tax to target all consumption, which can be modified with rebates or exemptions to remove regressive effects (such as the proposed Fair Tax in the U.S.

Border adjustable

A flat tax system and income taxes overall are not inherently border-adjustable; meaning the tax component embedded into products via taxes imposed on companies (including corporate taxes and payroll taxes) are not removed when exported to a foreign country (see Effect of taxes and subsidies on price).

Taxation systems such as a sales tax or value added tax can remove the tax component when goods are exported and apply the tax component on imports. The domestic products could be at a disadvantage to foreign products (at home and abroad) that are border-adjustable, which would impact the global competitiveness of a country.

However, it's possible that a flat tax system could be combined with tariffs and credits to act as border adjustments (the proposed Border Tax Equity Act in the U.S. attempts this). Implementing an income tax with a border adjustment tax credit is a violation of the World Trade Organization agreement. Tax exemptions (allowances) on low income wages, a component of most income tax systems could mitigate this issue for high labour content industries like textiles that compete Globally.

In a subsequent section, various proposals for flat tax-like schemes are discussed, these differ mainly on how they approach with the following issues of deductions, defining income, and policy implementation.

3.3 Background to the Uganda and other relevant taxation systems

3.4 Filing returns and policy decision concerning the tax mix

3.5 Tax administration under various acts; VAT computation and management, etc.

The Excise & Taxation Department is revenue department. It administers the various Acts such as the Sales Tax Act, Central Sales Tax Act, Motor Spirit Taxation Act, Passenger & Goods Tax Act, Entertainment & Show Tax Act and Excise Act. Under all these Acts levy of tax is collected by the Assessing Authorities in their respective field consisting of Wards which are seven in number.

Under the above Acts these Assessing Authorities who are AETC/ETOs, ensures the realization of the taxes with the supporting staff deployed in their Wards. The department is headed by the Excise and Taxation Commissioner, who is superintending this office through the Deputy Excise and Taxation Commissioner under various enactments referred to above.

The department contributes a major chunk of revenue to the State exchequer of Union Territory, Chandigarh. Administration of every enactment is being ensured in accordance with the statutory provisions of each Act and Rules framed there under.

Although these enactments are based on a very old system of working being in operation for more than fifty year's earlier stage, yet to maintain a pace with the changed system of working in every field, the department has simplified various procedures to make it a public friendly and self compliance.

The following simplification of the procedures involving public interests have been made by the department:-

- Computerisation of all the records, which enables the dealer to have an access to their respective information with regard to Returns filed, payments of tax made and verification of encashment of cheques/drafts etc. This ensures the expeditious disposal of their Assessment cases.
- One of the senior officer has been entrusted the work of Central Public Information Officer, to facilitate the dealers/the persons having any interest in the working of the department, for obtaining any information.
- Some Sampark Centres formulated by the Chandigarh Administration in various parts of the city have been authorized to conduct the business relating to this office such as receipt of taxes and returns. This system facilitates the dealers particularly falling in that area to save their time and energy. The working time of such Sampark Centres is from 8 A.M. to 8 P.M. which is more convenient as compared with office working of the department.

In order to pace with the changed system of implementation and realization of the tax on the sales as well as on the purchases under the VAT Act in Union Territory, Chandigarh, the functioning of the department can be classified into two categories, (1) Regulatory System (2) Service Providing System. The scope of the both fields is detailed below:

Regulatory function

Ensuring the proper realization of the tax on the sales/ purchase of taxable items under the VAT Law, by way of various provisions of the VAT Act, which consists compulsory registration of a person liable to pay tax, making inspections/ raids and roadside checking to detect the tax evasion in the hands of the unscrupulous dealers. The department also conduct the Audit on scrutiny as per the policy of the VAT Act and assess the return filed by the dealer.

Compliance of the VAT provisions with regard to maintenance of books of accounts of the dealer is also enforced by this department failing to which penal action is taken as per the provisions of the VAT Act.

The department also ensures the implementation and realization of the taxes levied under the Punjab Entertainment Tax Act and Punjab Passenger and Goods Taxation Act. In order to ensure the recovery of the tax under these Acts, the department enforces various provisions under these enactments by paying surprise inspections also.

Service providing systems service providing functions

Although the main functioning of the department is to ensure the compliance of various provisions of the VAT Law by the dealers, yet out of those various functions enunciated under the VAT Act/ Rules, the following works can be treated as Service Providing ones:

- **Issuance of various declaration forms**

The department issues to the assesses on their demand preferred by way of application, various declaration forms such as Form 'C', 'F', 'ST XXII', 'H', 'I', 'E1', 'EII', etc. This process is promptly attended to. The application is examined by the Taxation Inspector and the issuance of above declaration forms are ordered by the Excise and Taxation Officer of the Ward concerned and then on the same day the official put on this duty issues the same to the applicant. This system is attended very promptly and it takes hardly one hour for the assesses to collect these forms.

Grant of Registration Certificate

On the receipt of the application on the prescribed Performa under the VAT Law alongwith the required fee, the application is received in the office by the Dairy Clerk and marked to the Taxation Inspector of the area concerned and the later verify the contents of the application and also verify the Sureties if any, and pay the visit to the spot i.e. business premises in order to ascertain the genuineness and bonafide of the dealer before the report is submitted to the E.T.O.

The Excise and Taxation Officer concerned passes the order for the grant of Registration Certificate and the same is prepared and issued by the official in the Establishment Branch. The time earmarked for whole system is one month, where the applications are received with all documents required under the Law.

- **Amendment**

The amendment applications of various kinds as per the request of the dealer is received in the office and the acknowledgement is issued. The

Taxation Inspector of the area concerned examine the same and verify the contents of the application and submit his report to the Excise and Taxation Officer concerned for ordering the amendment.

Where it is necessary to visit the premises of the applicant assesses under the VAT Act/Rules, he also pays visit to the premises to verify the genuineness of the applicant's request. Fifteen days are earmarked to the Taxation Inspector to verify the contents of the application and submit its report to the Excise and Taxation Officer.

On the receipt of the application by the E.T.O., he scrutinizes the application as per provisions of the VAT Law vis-à-vis the report of the Taxation Inspector and the amendment is allowed within 15 days by the E.T.O. The whole process is completed within one month.

General Queries

In case of any doubt with regard to the sales/ purchase transactions for the tax liability, the dealer can file application under Section 85 of the VAT Act addressed to the Excise and Taxation Commissioner, which is decided by giving an opportunity to the applicant of being heard by the Excise and Taxation Commissioner. The clarification is given by way of passing an order as provided under the VAT Act by the later and is communicated to the applicant promptly. The time to decide such cases may vary case to case as it depends upon the nature of the query asked for. However, every effort is made to decide it on priority basis. On an average it takes two months time.

Providing various information on website

The department has uploaded VAT rates, VAT Forms and VAT Rules on the website of the Chandigarh Administration. Any change in the VAT rates is also updated on the website.

Regulatory Functions

VAT Act

- **Proper realization of tax**

Ensuring the proper realization of the tax on the sales/ purchase of taxable items under the VAT Law, by way of various provisions of the VAT Act, which consists compulsory registration of a person liable to pay tax.

- **Inspections**

Making inspections/ raids and roadside checking to detect the tax evasion in the hands of the unscrupulous dealers.

- **Audit of Returns**

The department also conduct the Audit on scrutiny as per the policy of the VAT Act and assess the return filed by the dealer.

- **Compliance of VAT provisions**

Compliance of the VAT provisions with regard to maintenance of books of accounts of the dealer is also enforced by this department failing to which penal action is taken as per the provisions of the VAT Act.

Excise Act

- **Bar Licenses**

A fifteen days notice to general public is required to be given for the grant of (L-3/L-4/L-5/L-12C) these Licenses. These Licenses are granted in less than one month time as the file has to move upto the Excise and Taxation Commissioner, U.T. Chandigarh for consent.

- **Breach Cases**

The disposal of breach cases of licenses within 15 days after given at least 7 days notice to the erring licensee.

Punjab Entertainment Tax Act and Punjab Passenger and Goods Tax Act

The department also ensures the implementation and realization of the taxes levied under the Punjab Entertainment Tax Act and Punjab Passenger and Goods Taxation Act. In order to ensure the recovery of the tax under these Acts, the department enforces various provisions under these enactments by paying surprise inspections also.

Service Providing Functions

VAT Act

- **Grant of Registration Certificate: Total Time 30 days**

    i) Receipt of   One day.

	application	
ii)	Verification and report by the Taxation Inspector	15 days.
iii)	Verification and Issuance of Certificate by the E.T.O./D.O.	10 days.
iv)	Preparation and receipt of R.C. from the S.R.C.	5 days.

- **Amendments: Total Time one month.**

Receipt of application	One day.
Verification and report by the Taxation Inspector	15 days.
Verification and Issuance of Certificate by the E.T.O./D.O.	10 days.
Preparation and receipt of R.C. from the S.R.C.	5 days.

- **Issuance of various declaration Forms: Total Time about one to two hours (depending upon the rush of work).**

i)	Verification and report by the Taxation Inspector	10 to 15 minutes.
ii)	Issue of declaration Forms by the E.T.O./D.O.	15 minutes.
iii)	Receipt of declaration Forms from the S.R.C.	One hour.

- **General Queries: Regarding queries under Section 85 of VAT Act, time taken about one to two months.**

i)	Issue of notice and preparation of case by the office	20

		days.
ii)	Presentation of case before the Excise and Taxation Commissioner and passing of orders after arguments	20 to 30 days.

Excise Act

- **Liquor Possession Permits (L-42 / L-50)**

  Issued within one day of receipt of application.

- **Liquor Permits, Pass Permits, L-32 and L-34)**

  Within one day of the receipt of the applications by the Licensee.

- **Renewal of Licensees :**

Takes 4 to 5 days from the date of announcement of Excise Policy for the year for which the renewal is sought.

- **Export Permission:**

Within one day to the Export Liquors out of U.T. Chandigarh by the Chandigarh Bottling Plants on receipt of their application.

- **Passenger and Goods Tax Act:**

Clearance Certificates are issued on the same day on receipt of application from the Transport Company or the owner.

Liquor possession limits

As per the provisions of the Excise Policy of the year 2008-09, Private Possession limit of liquor to be kept by the citizens in U.T. Chandigarh has been fixed. A citizen of U.T. Chandigarh can keep the following quantity of liquor without any permission:-

Country Liquor	2 Quarts (bottles) of 750 ml
IMFL/IFL	18 Quarts (bottles) of 750 ml

Beer	36 Bottles of 650 ml
Wine	18 Bottles of 750 ml

However, in case any individual wants to keep more liquor than the above-prescribed limit, he can have his possession limit enhanced by obtaining a permit in Form L-50 from the Excise & Taxation Department. The enhanced possession limit on the basis of the L-50 permit has been fixed as under:-

IMFL/IFL	36 Quarts (bottles) of 750 ml
Beer	72 Bottles of 650 ml
Wine	36 Bottles of 750 ml

The possession of liquor in excess of the above mentioned limits by any individual in U.T., Chandigarh can lead to legal action under the provisions of the Punjab Excise Act, (as applicable to U.T.).

Tax and Revenue Administration (TRA)

Alberta Finance and Enterprise

Act: Alberta Corporate Tax Act, Fuel Tax Act, Tobacco Tax Act, Tourism Levy Act

Regulation: Various
Individuals, trusts, corporations, tax professionals and other interested parties.

Tax and Revenue Administration is responsible for the administration of the **Alberta Corporate Tax Act, Fuel Tax Act, Tobacco Tax Act, Tourism Levy Act,** as well as the Health Cost Recovery programs.

The **Alberta Corporate Tax Act** contains provisions for determining the Alberta income tax of corporations, the Alberta Royalty Tax Credit for corporations, the Alberta Royalty Credit for individuals and trusts and the Insurance Corporations Tax. Fuel tax, tobacco tax and tourism levy provisions are contained in the respective acts.

Administration
The administration and enforcement of the acts are under the control and direction of the Minister of Finance and Enterprise. **TRA** operates out of a full-services office in Edmonton.

Information Services

General information concerning the acts administered by **TRA** is provided by the Tax Services branch. The following services are provided to individuals, corporate representatives, tax professionals and other interested parties on request:

- providing information about the nature of, and eligibility requirements for, the various tax and tax incentive programs under the acts;
- providing information on procedural matters such as the completion and filing of returns and other forms;
- conducting information sessions or client group discussions; and
- Forwarding specific forms and publications to interested parties.

More information including Alberta corporate tax rates, small business deduction rates, fuel tax, tobacco tax and tourism levy rates, and other services, publications and forms can be obtained by visiting the Finance and Enterprise website.

Information contained in this section is of a general nature only and is not intended to constitute advice for any specific fact situation. For particular questions, the users are invited to contact their lawyer. For additional information, see the contact listed below.

Unit 4
Personal Income Tax Computations (Taxable Income)
4.1 Introduction

Taxable income is your assessable income for tax purposes minus all deductions allowed under Division 8 of the Income Tax Assessment Act 1997. These deductions include any loss or outgoing (eg an expense) incurred in gaining or producing assessable income or necessarily incurred in running a business for the purpose of producing your assessable income.

Taxable income is not used to calculate pension and allowance rates, but it is used for Family Tax Benefit and the Commonwealth Seniors Health Card and for assessing Youth Allowance and ABSTUDY entitlements if you are dependent. It also applies to the Assistance for Isolated Children Scheme in assessing entitlement to the Additional Boarding Allowance component. For Family Tax Benefit, Youth Allowance, ABSTUDY and Assistance for Isolated Children, income is made up of taxable income, the value of net rental property losses, certain employer provided fringe benefits, foreign income and tax free pensions and benefits.

The income test for the Commonwealth Seniors Health Card is based on adjusted taxable income. This includes taxable income, foreign income and employer provided fringe benefits. You must include your Tax Notice of Assessment when claiming Commonwealth Seniors Health Card.

Adjusted taxable income

Adjusted taxable income is used to calculate your entitlement to Family Assistance for the current financial year. It is determined based on an estimate of family income for you (and/or your partner) and consists of:

- taxable income
- reportable fringe benefits
- reportable superannuation contributions
- total net investment loss
- tax free pensions or benefits
- foreign income
- tax exempt foreign income
- **less** child support you have paid.

The amount of Family Tax Benefit and/or Child Care Benefit you received throughout the year will be checked against the amount you should have received, based on your actual adjusted taxable income. This is determined after you (and/or your partner) have lodged a tax return.

4.2 Personal allowances

Income tax allowances and amounts

This information applies to England, Wales, Scotland and Northern Ireland

What are allowances against income tax

This information gives details of the different types of allowances and when they can be claimed.

Personal allowance and blind person's allowance are fixed amounts that are set against your income, allowing you to receive that much income free of tax in any one tax year. Married couple's allowance works as a deduction from your tax bill. You may be entitled to receive more than one allowance.

Most taxpayers living in the UK on a day to day basis are entitled to personal allowance. Some taxpayers can claim Blind Person's Allowance and Married Couple's Allowance as well.

If you have paid some tax on your income and are entitled to an allowance and are not getting it, you should claim it from your tax office. If you have not received all the allowances to which you are entitled, you can make a backdated claim for them but there is a time limit for doing this. You can find more information about the time limit that applies in Tax refunds

In practice, if you receive earnings or an occupational pension, this income is taxed through the Pay As You Earn (PAYE) system. Depending on how you are paid, you will either get 1/52 of your personal allowance if you are paid weekly, or 1/12 of your personal allowance if you are paid monthly, as tax free pay every payday. After taking into account any other allowances or reliefs, the amount you earn or receive as pension above this level will be taxed. This means that allowances are spread equally over the year rather than you starting to pay tax only once earnings/pensions exceed the amounts of your allowances.

What allowances are available?

The following tax allowances can be given:

- Personal Allowance - see under heading Personal Allowance
- Blind Person’s Allowance - see under heading Blind Person’s Allowance
- Married Couple’s Allowance for couples where at least one member was born before 6 April 1935 - see under heading Married Couple’s Allowance.

Personal allowance

Most people get the basic personal tax allowance automatically, but people with incomes over £100,000 get a reduced allowance or none at all. The personal allowance can be set against all types of income. There are three amounts of Personal Allowance, but only the basic allowance is given automatically:

- a standard amount (the basic allowance) for most people under 65 (and includes most people over 65 whose income is too high for the increased age allowances – see below)
- a higher amount for people aged 65 to 74 and which is available for the whole tax year to anyone who reaches the age of 65 at some point during the tax year
- The highest amount for people aged 75 or over and which is available for the whole tax year to anyone who reaches the age of 75 at some point during the tax year.

If you have income over a certain limit, the higher amounts for people aged 65 or over are reduced. However, they are not reduced below the standard amount (basic allowance) for people under 65, unless, from 6 April 2010, your income is more than £100,000 in the tax year.

Allowances for older people can be complex. For more information on personal allowances and to work out whether you should be paying tax in retirement.

If you are aged 60 or over and on a low income and have a problem with your tax allowances you may wish to contact TaxHelp for Older People (TOP) for advice on their Helpline on 0845 601 3321 (Mon-Fri 9.00am-5.00pm). TOP can arrange for a home visit, if your problem is better sorted out by a face-to-face meeting.

Personal Allowance amounts

This table gives details of personal tax allowances for all in date tax years. These allowances are deducted from total taxable income before the amount of tax payable is calculated.

Basic personal allowance	2005/06 tax year	2006/07 tax year	2007/08 tax year	2008/09 tax year	2009/10 tax year	2010/11 tax year	2011/12 tax year

Age under 65	£4,895	£5,035	£5,225	£6,035	£6,475	£6,475	£7,475
Age 65-74	£7,090	£7,280	£7,550	£9,030	£9,490	£9,490	£9,940
Age 75 and over	£7,220	£7,420	£7,690	£9,180	£9,640	£9,640	£10,090
Income limit for personal allowances 65-74 and 75 and over	£19,500	£20,100	£20,900	£21,800	£22,900	£22,900	£24,000
Income limit for basic personal allowance under 65	No limit	No limit	No limit	No limit	No limit	£100,000	£100,000

If your income is over the income limit for age-related allowances, HM Revenue and Customs (HMRC) will reduce the age-related allowance by half of the amount, £1 for every £2, you have over that limit, until the basic rate allowance is reached. You'll always get the basic allowance, whatever the level of your income, unless, from 6 April 2011, your income is more than £100,000 in the tax year.

So if, for example, you're 66 and have an income of £24,500, £500 over the limit of £24,000 in 2011/12, HMRC would reduce your age-related allowance by £250 from £9,940 to £9,690.

4.3 Employment income

Income that a person receives as the holder of an office or employment is charged to tax as "employment income".

Employment income consists of:

- "general earnings" and
- "specific employment income"

Most of the payments and benefits covered in this manual count as general earnings. But the distinction between general earnings and specific employment income is important. There are special rules for taxing the general earnings of people who are not resident, or not ordinarily resident, or not domiciled in the United Kingdom for tax purposes. Those special rules do not apply to specific employment income.

Shows you where to find guidance about particular items of employment income

Employment income: general earnings

In very many cases, a person's employment income will consist wholly or mainly of general earnings. General earnings are:

- Earnings as defined as principal tax charge on earnings from an office or employment. It normally takes precedence over any other tax charge.
- Any amount that is treated as earnings by any other provision of the Act. There is a list of those provisions.

An employee or office holder who is resident, ordinarily resident and domiciled in the United Kingdom is taxed on the full amount of their general earnings for the tax year (Section 15 ITEPA 2003).

Employment income: earnings from an office or employment

For 2003/04 onwards, the main tax charge on employment income is in respect of the "earnings" from an office or employment. This is the income that was previously taxed under Section 19(1)1 ICTA 1988 as "emoluments there from".

Employment income: specific employment income

Specific employment income is part of a person's employment income for tax purposes.

t includes anything that the Act says is to be taxed as employment income **except** anything that counts as general earnings.

Specific employment income is not subject to the special rules about residence, ordinary residence and domicile. Those rules only apply to general earnings.

The main types of specific employment income are:

- payments and benefits on termination of employment, etc onwards)
- payments and benefits in respect of non-approved pension schemes onwards)
- Share related income (including share options) (see Share Schemes Manual).

4.4 Employee incentive schemes

4.5 Other charges on income

4.6 Benefits In Kind

Taxable benefits in kind and expenses payments

There are a wide range of benefits in kind received by employees, most of which are taxable, though there are some statutory exemptions. Most directors of companies are liable to pay Income Tax on the value of the benefit in kind and expense payments provided. Their employers (or in certain cases other third parties who provide benefits in kind) are liable to pay Class 1 or Class 1A National Insurance contributions. Employees who earn less than £8,500 a year are only liable to pay tax on certain benefits in kind.

The National Statistics available through this page will be assessed by the UK Statistics Authority in May 2011. As part of the assessment the UK Statistics Authority will be seeking feedback from users on these statistics, for example regarding their quality and usefulness. If you would like to be contacted by the Authority please provide your name and contact details to the statistical contacts provided in the release and HM Revenue & Customs (HMRC) shall pass these on to the Authority.

HMRC have removed older tables for table 4.5 due to an error in the treatment of National Insurance contributions in years prior to 2002-03. HMRC are not replacing them as years from 2002-03 are fully covered in the latest version of table 4.5, and earlier years are of limited public interest. Tables for years up to and including 2001-02 can however be provided on application.

4.7 Personal pension schemes

4.8 Tax relief

Unit 5

Capital Gains Tax

5.1 Capital deductions

Capital expenses are the costs of purchasing specific assets, such as property or equipment that usually have a life of one year or more and increase the quality and quantity of products and services you can provide. For example, if you own a landscaping business and you purchase mowers and excavating equipment, these costs are capital expenses and do not qualify as deductible business expenses. However, you can recover the money you spent on capital expenses through **depreciation**, **amortization**, or **depletion**. These recovery methods allow you to deduct part of your cost each year so that you are able to recover your capital expenses over time.

Figuring out whether a purchase is a business expense or a capital expense is not always clear cut. Consider taking advantage of free tax training opportunities offered by the U.S. Internal Revenue Service (IRS). If you have hired an accountant, you should also seek his or her advice regarding tax deductions.

The following information provides a brief overview of expenses that qualify as tax deductions, with links to resources that provide clear guidance on deducting and capitalizing your expenses.

There are two ways to deduct capital expenses. You can "depreciate" them by deducting a portion of the total cost each year over the useful life of an asset, or you might be able to deduct the cost in one year as a Section 179 deduction.

Depreciation

If property you acquire to use in your business is expected to last more than one year, you generally cannot deduct the entire cost as a business expense in the year you acquire it. You must spread the cost over more than one tax year and deduct part of it each year on Form 1040, Schedule C. This method of deducting the cost of business property is called **depreciation**.

What property can be depreciated?

You can depreciate property if it meets *all* the following requirements:

- It must be property you own
- It must be used in business or held to produce income. You never can depreciate inventory because it is not held for use in your business
- It must have a useful life that extends substantially beyond the year it is placed in service
- It must have a determinable useful life, which means that it must be something that wears out, decays, gets used up, becomes obsolete, or loses its value from natural causes. You never can depreciate the cost of land
- It must not be excepted property. This includes property placed in service and disposed of in the same year

Repairs

You cannot depreciate repairs and replacements that do not increase the value of your property, make it more useful, or lengthen its useful life. You can deduct these amounts on line 21 Form 1040, Schedule C or line 2 of Schedule C-EZ.

Depreciation Method

The method for depreciating most business and investment property placed in service after 1986 is called the Modified Accelerated Cost Recovery System (MACRS). MACRS is discussed in detail in How to Depreciate Property (IRS Publication 946).

Section 179 Deduction

Purchasing such things as office equipment and computer software would seem like ordinary and necessary expenses, however, the IRS considers these costs to be capital expenses.

Unlike assets that are acquired for the production of income (such as investment property), Section 179 of the IRS Code gives you the option to deduct the costs of assets acquired for business use as expenses in the year you purchased the assets, instead of requiring them to be capitalized and depreciated. Eligible property is generally limited to tangible, depreciable property which is acquired for use in the active conducting of a trade or business. Section 179 deductions are subject to dollar amount and deductible limitations.

Deducting Business Expenses

To be deductible, a business expense must be both "ordinary" and "necessary." An ordinary expense is one that is common and accepted in your field of business. A necessary expense is one that is helpful and appropriate for your business.

Personal Versus Business Expenses

Generally, you cannot deduct personal, living or family expenses. However, if you have an expense for something that is used partly for business and partly for personal purposes, divide the total cost between the business and personal portions. You can deduct the business portion. For example, if you borrow money and use 70 percent of it for business and the other 30 percent for a family vacation, you can deduct 70 percent of the interest as a business expense. The remaining 30 percent is personal interest and is not deductible.

Home Office Deduction

Are you a home-based business? If you are using part of your home for business, you may be able to deduct some expenses for the business use of your home. These expenses may include mortgage interest, insurance, utilities, repairs, and depreciation. If you are a homeowner or renter, the home office deduction is available and applies to all types of homes, from apartments to mobile homes. There are two basic requirements for your home to qualify as a deduction:

1. **Regular and Exclusive Use.** You must regularly use part of your home exclusively for conducting business. For example, if you use an extra bedroom to run your online business, you can take a home office deduction for the extra bedroom.
2. **Principal Place of Your Business.** You must show that you use your home as your principal place of business. If you conduct business at a location outside of your home, but also use your home substantially and regularly to conduct business, you may qualify for a home office deduction. For example, if you have in-person meetings with patients, clients or customers in your home in the normal course of your business, even though you also carry on business at another location, you can deduct your expenses for the part of your home used exclusively and regularly for business. You can deduct expenses for a separate free-standing structure, such as a studio, garage or barn, if you use it exclusively and regularly for your business. The structure does not have to be your principal place of business or the only place where you meet patients, clients or customers.

Generally, deductions for a home office are based on the percentage of your home devoted to business use. So, if you use a whole room or part of a room for conducting your business, you need to figure out the percentage of your home devoted to your business activities.

Visit the IRS page on Home Office Deductions for a full explanation of tax deductions for your home office.

Other Types of Deductible Business Expenses

There are numerous other costs of doing business that qualify as deductions. These include, but are not limited, to the following:

- **Employees' Pay** - You can generally deduct the pay you give your employees for the services they perform for your business.
- **Interest** - Business interest expense is an amount charged for the use of money you borrowed for business activities.

- **Retirement Plans** - Retirement plans are savings plans that offer you tax advantages to set aside money for your own, and your employees', retirement.
- **Rent Expense** - Rent is any amount you pay for the use of property you do not own. In general, you can deduct rent as an expense only if the rent is for property you use in your trade or business. If you have or will receive equity in or title to the property, the rent is not deductible.
- **Taxes** - You can deduct various federal, state, local, and foreign taxes directly attributable to your trade or business as business expenses.
- **Insurance** - Generally, you can deduct the ordinary and necessary cost of insurance as a business expense, if it is for your trade, business or profession.
- **Business-Related Education** - You can deduct seminars, classes, educational tapes or CDs, and convention fees.

Listed Property

You must follow special rules and record keeping requirements when depreciating listed property. Listed property is any of the following:

- Most passenger automobiles
- Most other property used for transportation
- Any property of a type generally used for entertainment, recreation or amusement
- Certain computers and related peripheral equipment
- Any cellular telephone (or similar telecommunications equipment)

- Gains/losses on disposal of Assets
- Computation of chargeable gains and allowable losses.

Unit 6

Legal processes (tax appeal tribunal)

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Read more: http://www.answers.com/topic/tax-planning-in-accounting#ixzz1TJxZaJ00