MACHAKOS UNIVERSITY

University Examinations for 2018/2019 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BANKING, ACCOUNTING & FINANCE

FOURTH YEAR SPECIAL/SUPPLEMENTARY EXAMINATION FOR

BACHELOR OF COMMERCE

BAC 400: TAX LAWS AND PRACTICE

DATE: 26/7/2019 **TIME: 2.00-4.00 PM**

INSTRUCTIONS:

i. Answer question one and any other two questions.
ii. Marks allocated for each question are shown at the end of the question.
iii. Show your working where necessary.

QUESTION ONE (30 MARKS): COMPULSORY

(a) Explain THREE roles of the Kenya Revenue Authority in achieving the country's development agenda. (6 marks)

(b) Explain FOUR benefits of Integrated Tax Management System (ITMS). (8 marks)

(c) The following information was provided by Singida Ltd for the year ended 31 December 2017.

	Shs. "000"
Dividend paid	52,500
Dividend received	8,750
Profit after tax	17,500
Tax refund	5,000

Corporation tax rate is 30 %.

Required: Dividend Tax Account to determine the compensating tax (if any) payable by Singida Ltd for the year ended 31 December 2017. (4 marks)

(d) Explain THREE benefits of Export Processing Zones (EPZ) tax incentives to the Kenyan economy. (6 marks)

(e) Samia Ltd reported the following income for the year ended 31 December 2017.

	Shs.
Operating income (before tax)	12,000,000
Investment income	650,000
Rental income (gross)	1,600,000

Investment income comprised:

	Shs.
Dividend from a company in which Samia holds 20% of the share capital	100,000
Interest from fixed deposit account (net)	50,000
Interest from Treasury bills (net)	500,000

Required: Determine the shortfall distribution tax (if any) payable by Samia Ltd for the year ended 31 December 2017. (6 marks)

QUESTION TWO (20 MARKS)

The management of Kiboko Ltd presented the following income statement for the year ended 31 December 2017.

	Sh. "000"	Sh. "000"
Sales		46,250
Less: Cost of sales		
Opening Stock	10,500	
Purchases	14,000	
Closing Stock	(6,000)	18,500
Gross Profit		27,750
Other Incomes:		
Gain on sale of equipment		300
Interest on savings account		100
Refund of import duty		200
Gain on foreign exchange transactions		250

		28,600
Expenditure:		
Goodwill amortization	62.5	
Legal expenses	1,050	
Salaries	5,000	
Bad debts	1,250	
NSSF contribution	150	
General expenses	1,500	
Advertising	750	
Staff meals	475	
Travelling expenses	450	
Donations to trade associations	100	
Property rates	112.5	
Depreciation	375	
Interest on long term loan	750	
Interest on bank overdraft	200	
Insurance	310	
Cost of stolen stock	50	
Branch closure costs	250	(12,835)
Net profit		15,765

Additional information:

i) Closing stock was valued at cost plus mark up of 20%.

ii) Legal expenses relate to:

	Sh.
Preparation of a Memorandum of Association	375,000
Conveyance fees on purchase of land	150,000
Acquisition of leasehold property	225,000
Settling customer disputes	250,000
Acquisition of a bank loan	50,000
	1,050,000

iii) The directors had withdrawn goods costing Sh. 1.5 million (selling price Sh.1.8 million) for their personal use. These goods have been included in both purchases and sales for the year ended 31 December 2017.

iv) Salaries expense included the following:

	Sh.
Directors allowances	1,800,000
Christmas gifts to staff	1,500,000
Golden handshake to a retiring director	1,000,000

v) Bad debts include:

	Sh.
Loan to directors	500,000
Estimated defaults by trade debtors	300,000

vi) Advertising expense includes Sh.250, 000 for a neon sign.

vii) Twenty percent of the travelling expenses relate to private usage of company motor vehicles.

viii) Capital allowances were agreed with the revenue authority at Sh. 500,000

Required:

Adjusted taxable profit or loss for Kiboko Ltd for the year ended 31 December 2017.

The tax payable by the firm (if any) for the year ended 31 December 2017. (20 marks)

QUESTION THREE (20 MARKS)

Kinga insurance company Ltd underwrites three classes of insurance namely; Motor Vehicle, Theft and Fire. The following details were obtained from the company for the year ended 31 December 2017.

	Class of Insurance		
	Motor Vehicle	Theft	Fire
	Sh. "000"	Sh. "000"	Sh. "000"
Gross Premium	94,640	485,000	378,680

Claims paid	14,320	94,360	12,450
Management expenses	3,490	8,500	6,320
Provision for bad debts	1,250	200	364
Reserve for unexpired risk:			
- 1 Jan 2017	1,380	1,096	484
Claims owing:-1 Jan 2017	12,360	83,700	9,850
-31 Dec 2017	9,870	73,760	7,560
Legal expenses	752	840	640
Reserve for unexpired risk:			
-31 Dec 2017	780	670	358
Interest on policyholders' outstanding premiums	285	180	120
Telephone and postage	94	300	150
Premiums returned	485	470	348
Interest income	336	540	680
Rent expenses	345	420	560
Commission on re-insurance ceded	480	400	342
Commission on re-insurance accepted	336	574	300
Agency expenses	200	248	172
Re-insurance commission	100	96	60
Premium paid to re insurance firm	1,680	1,720	2,360

Additional information:

i) The company also operates a Life Assurance business. Of the total agency expenses, 40% relate to life assurance business.

ii) Furniture and fittings amounting to shillings 1,560,000 were used for all businesses. It was estimated that the value of furniture and fittings relating to life assurance business was sh. 560,000

iii) Dividends from a collective investment scheme of sh. 850,000(net) were included in the total of interest income.

iv) A motor vehicle used by the general business valued at sh. 800,000 was disposed off at sh.960,000. It was purchased on 1 January 2016 for sh. 1.2 million.

v) Management expenses include sh. 3.68 million for life assurance business.

Required:

a) A statement of taxable profit or loss for Kinga Insurance company ltd for the year ended 31 December 2017.

b) Tax payable if any, from your computation of (a) above. (20 marks)

QUESTION FOUR (20 MARKS)

(a) The following information relates to Akiba Savings and Credit Co-operative Society for the year ended 31 December 2017.

Income Statement for the year ended 31 December 2017

	Sh. "000"	Sh. "000"
Income:		
Interest from members' loans		9,600
Interest from fixed deposit accounts		2,400
Interest from government infrastructure bonds		3,600
Other investment income		1,500
Rental income		3,200
Interest from Front Office Saving Activity (FOSA)		1,000
Dividends from Supa Co-operative Society		800
Gross income		22,100
Expenditure:		
Administrative expenses	5,600	
Capital allowances	1,400	
Operating expenses	3,000	10,000
Surplus		12,100

Additional information:

i) The society paid dividends and bonuses to members amounting to sh 6.5 million for the year ended 31 December 2017.

ii) Administrative expenses included:

Sh.

- Salaries to officers directly involved in the processing of members' loans 1,400,000
- Salary to the caretaker of rental property 200,000
- Purchase of comput

iii) Operating expenses included depreciation of sh. 84,000 and non-performing loans to members of sh. 120,000 which were written off.

iv) Other investment income includes income from saving account of sh. 500,000.

Required:

i. Adjusted taxable profit or loss for the year ended 31 December 2017.
   Hint: You may start with the reported surplus.

ii. Tax liability (if any) due for the year ended 31 December 2017. (12 marks)

b) Explain FOUR circumstances under which a tax payer can get Value Added Tax (VAT) refund. (8 marks)

QUESTION FIVE (20 MARKS)

a) Ujenzi limited which is registered for VAT made the following supplies to Uzima limited.

Date	Rate	Amount (Shs.)
2017		(Exclusive of VAT)
January 20	0	800,000
February 3	Standard rate	2,500,000
March 5	Exempt	1,200,000
March 22	Standard rate	3,000,000
April 2	Standard rate	1,600,000

April 10	Standard rate	1,400,000

Ujenzi ltd received the following payments on account from Uzima ltd.

Date	Amount
2017	Shs.
April 11	1,800,000
May 11	900,000
May 27	2,100,000

Uzima ltd decided to wind up operations on August 30, 2017.

Required: Compute the VAT claimable i.e bad debts relief by ujenzi ltd. (10 marks)

b) Distinguish between tax evasion and tax avoidance. (4 marks)

c) Explain SIX events that may trigger a tax investigation by the revenue authority. (6 marks)