MACHAKOS UNIVERSITY

University Examinations for 2017/2018 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF BANKING, ACCOUNTING & FINANCE

THIRD YEAR SECOND SEMESTER EXAMINATION FOR BACHELOR COMMERCE

BAC 304: FUNDAMENTAL OF TAXATION

DATE: 15/12/2017 **TIME: 8:30 – 10:30 AM**

INSTRUCTIONS:

Answer Question One and Any Other Two Questions

1. a) Citing four reasons justify the need for levying taxes in Kenya. (8 marks)

b) Outline four types of qualifying capital expenditure for mining allowance. (4 marks)

c) Distinguish between forward tax shifting and backward tax shifting. (4 marks)

d) Many developing countries are faced with increasing budget deficit. Other than taxes, explain four ways in which a government could raise revenue to bridge the budget deficit (6 marks)

e) (i) Define the "term resident person" in relation to a corporate entity (3 marks)

(ii) Outline five factors which determine the taxable capacity of a company (5 marks)

QUESTION TWO (20 MARKS)

a) Miss Zainabu Musu reported the following information relating to her income for the year ended 31st December, 2016.

1. Shewas employed by Tausi Limited as an assistant accountant at a basic salary of sh 80,000(pay as you earn tax was deducted at sh.15, 000 per month)

2. She received the following benefits from her employer

- A furnished house (cost of furniture sh 80,000) The market rental value of the house was sh 14,000 per month. The employer deducted 5% of her basic salary per month to cover for rent.
- The following utility bills and wages were paid by the employer during the year

	sh
Telephone	40,000
Electricity	20,000
House servant	66,000
Watchman	60,000

- She was reimbursed a sum of sh 70,000 for medical expenses incurred during the year. The medical scheme only covered employee with basic salary of less than sh 100,000 per month.
- Her contribution to registered pension scheme amounted to sh.6, 000 per month. The employer contributed sh.12, 000 for her to the pension scheme.
- The employer paid sh.10,000 for her during the year representing entrance fees and annual subscription to a professional association.

She received the following additional income during the year

	sh
Profit from second-hand clothes business managed by her brother	18,000
Farming income	42,000
Lottery wins on a short message service (sms) based competition	100,000

Required

i) Taxable income for miss Zainabu Musa for the year ended 31st December 2016 (10 marks)

ii) Tax payable on the income computed in (i) above.

b) Distinguish between an objection and appeal in the context of tax administration in Kenya

(6 marks)

QUESTION THREE (20 MARKS)

Mambo and Kaka are in partnership operating, a hardware shop as Maka enterprises and sharing profits & loss equally. The following is the income statement of the partnership business for the year ended31st December 2016.

		sh
Sales inclusive of V.A.T on the rate of 16%		9,280,000
Capital gain on sale of property		290,000
Rental income		240,000
Dividends from Waki Cooperative (Net)		170,000
Unrealized foreign exchange gain		94,000
		10,074,000
Less:Expenses		
Cost of goods sold	4,000,000	
Purchase of computers	160,000	
Salaries and wages	360,000	
General expenses	720,000	
Legal expenses	940,000	
Conveyance fees	92,800	
Farm work at cost	60,000	
Repairs and maintenance	24,500	
Interest on partners capital	450,000	
Mambos Mortgage interest	63,800	
Donations to Tennis Club	34,800	
Commission to Kaka	21,000	6,929,000
		3,145,000

Additional information

1. General expenses include

	sh
• Embezzlement by Kaka	24,000
• Partition of staff services	48,000
• Staff catering expenses	50,000
• Pension contributions	180,000
• Prepaid rent and rates	32,000
• Stamp duty on land transfer	64,000

2. Legal expenses include

	sh
• Drafting a partnership deed	42,000
• Negotiating a bank loan	28,400
• Executing a customs bonds security	24,600
• Defending the business against	
Breach of contract	38,000

3. Salaries to partners and interest on partners capital is to be shared according to the profit and loss sharing ratio

4. Salaries and wages include salaries to employees of sh 160,000 while the balance was paid to partners

5. Cost of goods sold include purchase valued at sh 300,000 which had been over stated by 30%.

Required

i. Adjusted taxable profit or loss for the partnership for the year ended 31st December 2016 (12 marks)
ii. A schedule showing distribution of partners taxable income for the year ended 31st December 2016 (8 marks)

QUESTION FOUR (20 MARKS)

a) Explain the following terms as used in taxation
   i. Accounting period (2 marks)
   ii. Year of income (2 marks)
b) Distinguish between impact of a tax and incidence of a tax (4 marks)
c) Summarize four tax incentives available to landlord in Kenya (4 marks)
d) Citing four reasons justify why many countries are shifting from direct to indirect taxes (8 marks)

QUESTION FIVE (20 MARKS)

Onyango operates an electronic shop along Luthuli Avenue in Nairobi. He took the following transactions for the month of March 2017.

1st March 2017:	Purchased 10cameras for a total of shs 500,000
4th March 2017:	Purchased flash bulbs for a total of shs 200,000
4thMarch 2017:	Purchased 5 slides projectors for a total of sh 100,000
5thMarch 2017:	Sold 5 cameras each at 25% above cost price
6th March 2017:	Purchased 200 wrist watches at sh 1500 each
8th March 2017:	Sold 2 slide projectors for a total of sh 500,000
9th March 2017:	Sold flush bulbs that cost sh 100,000 for sh 150,000
12th March 2017:	Purchased 50 stop watches for a total of sh 50,000
15th March 2017:	Purchased 100 alarm clocks at a total of sh 80,000
18th March 2017:	Sold the remaining 5 cameras each at 25% above cost price
20th March 2017:	Sold 3 slide projectors for a total of sh 750,000
22nd March 2017:	Sold 100 wrist watches at 2000 per watch
25th March 2017:	Sold 70 alarm clocks each at 30% above cost
27thMarch 2017:	Sold 50 stop watches for a total of sh 75,000

The prices are inclusive of VAT.

Required

i. Calculate:
   - Input Tax
   - Output Tax (10 marks)

ii. Prepare the V.A.T account for Onyango clearly showing the V.A.T payable/refundable (6 marks)

iii. State when the above tax is due and the penalties payable if the tax is not paid on the due date (4 marks)