

TECHNICAL UNIVERSITY OF MOMBASA
SCHOOL OF BUSINESS
DEPARTMENT OF ACCOUNTING AND FINANCE

BACHELOR OF COMMERCE YEAR 3
BACHELOR OF BUSINESS ADMINISTRATION YEAR 3

BAC 4305: TAXATION II

END OF SEMESTER EXAMINATIONS

SERIES: APRIL 2016

TIME: 2 HOURS

INSTRUCTIONS:

- This paper consists of Sections **A** and **B**.
- Section **A** is Compulsory. Answer any **TWO** questions in Section **B**.
- Mobile phones are not allowed into examination room.
- Cheating leads to disqualification.
- This paper consists of Five printed pages.*

QUESTION ONE

- (a) Give a critical analysis of the benefit theory of taxation (5 marks)
- (b) FKM Ltd. Is a manufacturing firm which has been in operation since 2002. The capital deduction schedule shows that the written down values as at 31st December 2015 were as follows:-

Written down values

Sh.

Plant and machinery	5,261,500
Motor lorry and tractor	72,760
Delivery vans and pick-up (less than 3 tones)	2,025,000
Furniture and fittings	600,000

During the year ended 31st December 2015, FKM Ltd acquired the following assets:

Cost

Sh.

Furniture and fittings	1,600,000
Pick-ups (less than 3 tons)	8,000,000
Lorries	3,600,000

The following items were disposed of during the year:

Written down value

Sh.

Sold for

Sh.

Machinery	1,000,000	900,000
Delivery van (less than 3 tons)	250,000	270,000
Tractor	30,000	20,000

Required:

Calculate the wear and tear deductions to be claimed under the second schedule of the Income Tax Act for the year ended 31 December 2015 and shown the written down values of the assets as at that date. (15 marks)

- (c) The following figures have been extracted from the books of Ahero insurance co. ltd for the year ended 31st December, 2015.

	Shs. '000'
Claims paid	105,200
Claims recoverable from Nyake Re-Insurance Ltd	20,500
Commissions to insurance brokers and agents	48,000
Expenses of Management	53,000
Reserves for unexpired risks brought down	204,000
Shares in companies	249,000
Office equipment(WDV)	30,000
Depreciation	21,000
Premiums less premiums under reinsurance	211,000
Tax deducted at source	9,000
Interest on investment(gross)	90,000
Claims outstanding	14,000
Commission on reinsurance ceded	40,000

Reserves for unexpired risk should be maintained at 50% of the net Premiums.

Required: computed the tax payable by Ahero Insurance co. ltd a resident company that operates only a general insurance business. (10 Marks)

Question Two

Ushuru Mkora who has been in the business for several years does not maintain proper books of account. He pays tax on the basis of estimated income. The tax the tax authority feels that he is not fully taxed and has required him to prepare a capital statement to establish his tax liability. He has provided the following information for this purpose.

Year of income	2011 Shs. '000'	2012 Shs. '000'	2013 Shs. '000'	2014 Shs. '000'	2015 Shs. '000'
Total assets	123,000	156,000	175,000	200,000	216,000
Total liabilities	26,000	40,000	48,000	56,000	52,000
Drawings	1,500	2,000	2,300	3,000	2,900
New capital introduced	-----	4,000	-----	5,000	-----
Depreciation	2,000	2,000	2,000	2,000	2,000
Capital allowances	4,000	4,500	6,000	3,000	2,500
Declared income	3,500	3,500	3,500	3,500	3,500

The net worth for the year ended 2010 was Shs. 90,000,000.

Required:

- Tax arrears for each of the years 2011, 2012, 2013 and 2014.
- Tax penalty for the year 2013
- Interest penalty for the year 2014

(20 Marks)

Question Three

Ochieng, Mutua and Odongo are partners in an engineering firm. They share profits and losses equally. For the year ended 31 December 2015, you have been provided with the following summary of receipts and expenditures:

	Sh.		Sh.
Salaries and wages	10,000,000	Professional fees	35,000,000
Audit and accountancy fees	430,000	Capital introduced: Mutua	6,000,000
Legal fees	160,000	Odongo	4,000,000
Rent and rates	180,000		
Water and electricity	96,000		
Telephone and postage	240,000		
Subscriptions to the Engineering Association	60,000		
Subscriptions to Starehe Sports Club	400,000		
Instalment tax paid	1,000,000		
Donations to women's group	50,000		
Interest on overdraft	136,000		
VAT paid	6,000,000		
Office expenses	240,000		
Sundry expenses	300,000		
Purchase of design materials	2,000,000		
Drawings: Ochieng	2,000,000		
Mutua	3,000,000		
Odongo	500,000		
Interest on capital: Ochieng	170,000		
Mutua	60,000		
Odongo	20,000		
Net Profit	<u>17,958,000</u>		
	<u>45,000,000</u>		<u>45,000,000</u>

Additional information:

1. Salaries and wages include salaries paid to the partners as follows:

Ochieng	Sh.1,440,000
Mutua	Sh.1,200,000
Odongo	Sh. 960,000
2. Legal fees include Sh.100,000 for conducting a VAT appeal.
3. Telephone and postage includes Sh.60,000 paid for Mr. Ochieng's house telephone.
4. Credit notes issued to clients and not included in the accounts amount to Sh.950,000.
5. Agreed capital allowances for the year ended 31 December 2002 amount to Sh.4,000,000.

Required:

- (a) Adjusted profit and loss account for the partnership. (12 marks)
- (b) Allocation of the profit to the partners (4 marks)
- (c) Tax payable by each Ochieng'. (4 marks)

(Total: 20 marks)

Question Four

- (a) With regards to capital gain tax, discuss SEVEN transactions that are exempted from capital gain tax. (7 Marks)
- (b) Write short notes on the following:
- (i) Motor vehicle licenses and taxes
 - (ii) Poll tax
 - (iii) Property rates
 - (iv) Community charges (8 marks)
- (c) Discuss the requirements that must be fulfilled before VAT becomes chargeable on goods and services. (5 Marks)

Question Five

- (a) Tax planning is defined as the methods used by a tax payer to reduce his burden of taxes in a legal manner. Discuss five strategies that can be used to achieve tax planning goals. (10 Marks)
- (b) Mr. Joe Kamuzu is a practicing accountant operating under the name Kamuzu and Associates. His firm is registered for value added tax (VAT). During the month of March 2015, he undertook and completed the following assignments”

March 2: Tax consultancy work for Base Ltd., at a fee of Sh.240,000.

March 4: Audit for Mwanza Ltd., a company based in Tanzania for Sh.840,000.

March 10: Management consultancy services for Zeal Ltd., for a fee of Sh.360,000.

March 15: The firm was engaged by ABC Ltd., to undertake a review of the internal control systems of the company. His fees were Sh.1,200,000.

March 17: The firm provided audit services to Afro Ltd. for the year ended 30 June 2015 at Sh.480,000.

March 18: Conducted a survey on power consumption for Mwema Enterprises Ltd., at a fee of Sh.2,400,000.

March 19: His firm audited the accounts of Soul Harvester Ministries, a church where he serves as a volunteer auditor. He estimated that his fees would have been Shs.720,000.

March 20: The firm billed Afro Ltd. Sh.136,000 for debt collection services.

March 21: The firm undertook a financial consultancy assignment for World Net South Africa, a company based in South Africa. The fees were Sh.420,000.

March 23: Conducted audit of Matuu Ltd., at a fee of Sh.180,000.

March 27: Provided accountancy services to Githiga Children's home on a voluntary basis. The estimated value of the services was Sh.90,000.

March 30: Performed audit services for Mengo County Council. The fees earned was Sh.860,000.

During the month of March 2015, the firm paid for the following expenses:

	Sh.
Electricity	42,500
Water	42,000
Rent	120,000
Garbage collection	36,000
Stationery	960,000
Catering services	48,000
Computer repair	240,000
Telephone	330,400

All transactions are inclusive of VAT at a rate of 16% where applicable.

Required:

A VAT account for Kamuzu and Associates for the month of March 2015.

(10 marks)

(Total: 20 marks)

RATES OF TAX (Including wife's employment and professional income rates of tax)
year of income 2015.

Monthly taxable pay (Sh.)		Annual taxable pay (Sh.)		Rate of tax % in each Sh.
1	- 10,164	1	- 121,968	10%
	10,165 - 19,740		121,969 - 236,880	15%
	19,741 - 29,316		236,881 - 351,792	20%
	29,317 - 38,892		351,793 - 466,704	25%
	Excess over 38,892		Excess over - 466,704	30%

Personal relief Sh.1,162 per month (Sh.13,944 per annum)

Prescribed benefit rates of motor vehicles provided by employer

		Monthly rates (Sh.)	Annual rates (Sh.)
Capital allowance:	(i) Saloons, Hatch Backs and Estates		
Wear and tear allowance:	Upto 1200cc	3,600	43,200
Class I 37.5%	1201 1500cc	4,200	50,400
Class II 30%	1501 1750cc	5,800	69,600
Class III 25%	1751 2000cc	7,200	86,400
Class IV 12.5%	2001 3000cc	8,600	103,200
Software 20%	Over 3000cc	14,400	172,800
Industrial building allowance:			
Upto 2009	2.5%		
From 1 January 2010	10%		
Hotels	10%		
Hostels/Education buildings	50%		
From 1 January 2010 –			
Commercial building:			
Shop, office or show room)	25%		
Farm works allowance	100%		
Investment deduction allowance	100%		
	(ii) Pick-ups, Panel Vans (unconverted)		
	Upto 1750cc	3,600	43,200
	Over 1750cc	4,200	50,400
	(iii) land Rovers/Cruisers	7,200	86,400
Shipping investment deduction	40%		
Mining allowance:			
Year 1	- 40%		
Years 2 – 7	- 10%		

Commissioner's prescribed benefit rates

	Monthly rates Sh.	Annual rates Sh.
Services		
(i) Electricity (Communal or from a generator)	1,500	18,000
(ii) Water (Communal or from a borehole)	500	6,000
Agriculture employees: Reduced rates of benefits		
(i) Water	200	2,400
(ii) Electricity	900	10,800

