



TECHNICAL UNIVERSITY OF MOMBASA

SCHOOL OF BUSINESS
DEPARTMENT OF ACCOUNTING & FINANCE
UNIVERSITY EXAMINATION FOR:
BACHELOR OF COMMERCE III
BACHELOR OF IN BUSINESS ADMISTRATION III
BAC 4305: TAXATION 11
END OF SEMESTER EXAMINATION
SERIES: AUGUST, 2019
TIME:2 HOURS
DATE: AUGUST, 2019

Instructions to Candidates

You should have the following for this examination
-Answer Booklet, examination pass and student ID

This paper consists of **FIVE** questions. Attempt question ONE (Compulsory) and any other TWO questions.

Do not write on the question paper.

QUESTION ONE

- a) Justify the imposition of tax by the government of Kenya to its residents **(10 marks)**
b) Mwamba Limited was established in the year 2018 to manufactured soap for the local market. Before commencement of operation on January, 2018, the company spent a total of h.9,760,000 to construct a factory. The cost is analyzed below:

	Sh
Cost of land	1,000,000
Landscaping	200,000
Architect's fees	320,000
Sewage system	240,000
Actual building cost (including showroom)	<u>8,000,000</u>
	<u>9,760,000</u>

Additional information)

- 1) The following assets were constructed or purchased and utilized with effect from 1st July 2018.

	Cost (sh.)
Power transformer	800,000
Processing machinery (including installation costs as sh.200,000)	1,900,000
Bridge (connecting the factory to the main road)	600,000
Fork lift (mobile 2.5 tons)	150,000
Two salon cars (cost sh 2.5 million each)	5,000,000
Computers	3,600,000
Furniture and Fixtures	200,000
Pick-up (1.5 tons)	1,200,000
Tractor	1,500,000
Scanners	1,400,000
Computer software	4,800,000
Labour quarters	3,000,000
Office block	4,200,000

- 2) One of the salon cars was written off following an accident on 23rd December, 2018. The insurance company paid sh.900,000 as compensation to Mwamba Ltd.
- 3) The following assets were purchased on 1st August, 2018.

	Shs
Processing machinery	400,000
Office curtains	160,000
Fax machine	100,000
The process machinery was acquired on hire purchased terms. The cash price was sh.250.000	

Required

Compute the capital allowances due to Mwamba Limited for each of the year ended 31st Dec, 2018.

(20 marks)

Question Two

Kashurutishwa 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	2014	2015	2016	2017	2018
	Shs.	Shs.	Shs.	Shs.	Shs.
	'000'	'000'	'000'	'000'	'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 2013 was Shs. 90,000,000.

Required:

- Tax arrears for each of the years 2015, 2016, 2017 and 2018.
- Tax penalty for the year 2017
- Interest penalty for the year 2018

(20 Marks)

Question Three

- Baraka, Kabaka and Michapo are partners trading as Bakami Enterprises dealing in transport business. They share profit and losses equally after allowing an interest of 10% on their capital contribution. Their income statement for the year ended 31 December 2016 reflected the following:

Income	Sh.	Sh.
Sales revenue		2,800,000
Other income		<u>1,600,000</u>
		4,400,000
<i>Operating expenses:</i>		
Tyres and tubes	480,000	
Stationery	120,000	
Value Add Tax	160,000	
Legal fees	380,000	
Depreciation	90,000	
Subscription to trade association	48,000	
Advertisements costs	250,000	
Partner's medical expenses	140,000	
Fuel and oils	64,000	
Spares, repairs and maintenance	220,000	
Interest expense	940,000	
Commission to Kabaka	120,000	
Salaries and wages	760,000	
Miscellaneous expenses	800,000	<u>(4,572,000)</u>
Reported loss		<u><u>(172,000)</u></u>

Additional information:

- Legal fees comprised the following:

	Sh.
Preparation of employment contracts	125,000
Defending Baraka in private suit	64,000

- Preparation of a 90 year lease agreement 191,000
2. Advertising costs include a neon sign purchased for Sh. 80,000 and erection of a sign post at Sh. 25,000
3. Salaries and wages include those paid to partners as follows:

	Sh.
Baraka	140,000
Kabaka	160,000
Michapo	100,000

4. Capital allowances at Sh. 195,000 had been agreed with the commissioner of Income Tax.
5. Miscellaneous expenses include:

	Sh.
Registration of trade mark	140,000
Cash embezzled by cashier	280,000
Parking fines	150,000
Staff catering services	230,000

6. Interest expense comprised the following:

	Sh.
Interest charged on hire purchase	340,000
Interest on partners' capital accounts	
Baraka	250,000
Kabaka	180,000
Michapo	170,000

7. Other incomes comprised the following:

	Sh.
Recovered specific bad debts	240,000
VAT refund	600,000
Profit on disposal of motor vehicles	240,000
Discount received	180,000
Interest charged to Kabaka on drawings	340,000

8. Spare parts and maintenance included **Sh.** 180,000 spent on replacement of a motor vehicle engine.

Required:

- (a) Adjusted profit and loss account for the partnership. **(9 marks)**
- (b) Allocation of the profit to the partners **(9 marks)**
- (c) Tax payable by each Kabaka **(2 marks)**

Question Four

- (a) With regards to capital gain tax, discuss SEVEN transactions that are exempted from capital gain tax. **(7 Marks)**

(b) Bima Insurance Company provided the following information for the year ended 31st December 2018

	Ksh '000
Gross premium received	30,000
Claims paid	4,000
Commission on reinsurance ceded	800
Commission on reinsurance accepted	20
Claims recovered on re-insurance	900
Foreign exchange gains	3,500
Dividends from life assurance fund	2,000
Rental income	1,600
Bad debts provision	500
Investment income	1,200
Reserves for unexpired risk (1 Jan 2018)	1,000
Legal expenses relating to claims	400
Agency fees	400
Management fees	120
Repairs of rented properties	200
Entertainment expenses	400
Purchase of furniture	600
Purchase of computers	300
Re-insurance premiums paid	4,000
Return premiums	5,000

Additional information;

- i. Reserves for unexpired risk on 31st December 2018 Ksh 200,000
- ii. Claims outstanding on 1st January 2018 and 31st December 2018 were Ksh 600,000 and Ksh 900,000 respectively
- iii. Premiums outstanding on 1st January 2018 and 31st December 2018 were Ksh 6,000,000 and Ksh 12,000,000 respectively
- iv. Agency fees included Ksh 200,000 relating to the life assurance business
- v. Legal expenses included 100,000 relating to settlement of a tax dispute
- vi. Investment income comprised interest from bank Ksh 850,000 net of tax and interest from treasury bonds Ksh 350,000 gross

Required:

Prepare a statement of taxable profits or loss of Bima Insurance Company from the general insurance business for the year ended 31st Dec 2018. (13 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.

(8 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 2019, 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 30: Performed audit services for Mengo County Council. The fees earned was Sh.860,000.

During the month of March 2019, 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 net of VAT at a rate of 16% where applicable.

Required:

A VAT account for Kamuzu and Associates for the month of March 2019.

(12 marks)

RATES OF TAX (Including wife’s employment and professional income rates of tax) year of income 2018.

Monthly taxable pay (Sh.)	Annual taxable pay (Sh.)	Rate of tax % in each Sh.
0 - 12,298	1 - 147,580	10%
12,298 - 23,885	147,580 - 286,623	15%

23,885 -	35,472	286,623 -	425,666	20%
35,472 -	47,059	425,666 -	564,709	25%
Excess over	47,059	Excess over -	564,709	30%

Personal relief Sh. 1,408 per month (Sh. 16,896 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
Class II	30%	1501	1750cc	5,800
Class III	25%	1751	2000cc	7,200
Class IV	12.5%	2001	3000cc	8,600
Software(straight-line) 20%	Over	3000cc	14,400	172,800
Telecommunication equipment (straight-line) 20%				
Loose tools and implements (straight-line) 33.3%				

Industrial building allowance:

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

Services	Monthly rates Sh.	Annual rates Sh.
(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