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UNIVERSITY EXAMINATIONS

2022/2023 ACADEMIC YEAR

**FOURTH YEAR SECOND SEMESTER
MAIN EXAM**

FOR THE DEGREE OF BACHELOR OF COMMERCE

COURSE CODE: BCA 421

COURSE TITLE: TAXATION THEORY AND PRACTICE

DATE: 19TH APRIL, 2023

TIME: 9.00AM - 11.00AM

INSTRUCTIONS TO CANDIDATES

1. Answer a total of **three** questions; question **one** and any other **two** questions.
2. Question **one** carries **30** marks and each of the other two questions carry **20** marks each.

TIME: 2 Hours

QUESTION ONE

- a) State any five reasons why government levies taxes (5mks)
- b) Give advantages of direct taxes (3mks)
- c) Distinguish between Absolute taxable capacity and Relative taxable capacity (3mks)
- d) List any three instruments chargeable to stamp duty (3mks)
- e) Describe dumping in the context of taxation (3mks)
- f) Mrs Janet Mbugua is a professional medical doctor practicing in Nairobi. Given below are the financial details of her clinic for the year ended 31 December 2020.

	KShs.
Gross professional fees received	3,000,000
Director fees received (deductions at source)	360,000
Interest income from AJ Bank Ltd-Gross	72,000
Dividend income (net)	102,000
Subscriptions to professional association and publications	60,000
Donations to destitute children's home	30,000
Subscription to wildlife Magazine	6,000
Debt collection (patients) expenses	18,000
Wages for clinic assistant	360,000
Replacement of clinic instruments	120,000
Rent for clinic premises	420,000
Electricity and water for clinic	120,000
General expenses - clinic	210,000
Car hire expenses for use in practice	150,000
Uniform for staff	115,000
Payment of school fees for own children	120,000
Terminal benefits paid to retired receptionists	50,000
Contributions to registered provident fund-self	180,000
Payment of life insurance premium - self	60,000
Depreciation on furniture - clinic	36,000
Rents received from sub-rentals	42,000
Rent collection expenses	6,000
Wages paid to cleaners and watchman - clinic	150,000
Tarmacking of drive-way-personal residence	240,000
Additional servant quarters residence	420,000

Required:

- a) Taxable income of Mrs. Janet Mbugua for the year ended 31 December 2016(8 Mrks)
- b) Tax liability of Mrs Janet Mbugua (4Mrks)

QUESTION TWO

a) Under what situations can tax be avoided

- Cess
- Passenger service charge
- Road maintenance levy

c) A notice of assessment is a standard form issued by the commissioner and contains specific information. Highlight the contents of assessment (7mks)

(3mks)

(3mks)

(3mks)

(4mks)

(Total 30mks)

QUESTION THREE

a) Give a list of taxable supplies under VAT law (4mks)

b) Write short notes on wife's income (6mks)

c) Mr. Bannu Shah provided the following for the year ended 2014. He was employed as a fulltime Director of Latex Ltd. At a salary of Ksh 80000 per month (P.A.Y.E Ksh 31,200 per month)

- Free goods were received sh. 50,000 from the company
- He enjoyed free medical treatment under the medical scheme operated by the company which was assessed at Ksh 50,000
- Mr. Bannu Shah and wife operate a company fully owned by them whose taxable income has been assessed at Ksh 200,000 (P.A.Y.E 22000 p.a)
- Latex provides him with housing from 1st August 2013. Before this He lived in his own house.
- His wife works as a nurse in a private hospital and she earns Ksh20,000 p.m (P.A.Y.E sh 4000 p.m from August 2014
- Repairs and painting costs on the property were Ksh 11,500.
- The house he was living in before had a mortgage of Ksh.2,000,000 and Ksh600,000 was paid and of which Ksh.330,000 was capital sum

Required

a) Mr Bannu Shah taxable income for 2014. (3mks)

b) Tax liability for 2014. (3mks)

(Total 20mks)

QUESTION FOUR (a)
The directors of PQR limited have presented you with the following profit and loss account for the year ended 31 December 2014

	Sh.	Sh.
Gross profit		20,326,000
Less: Opening expenses		
Salaries and wages,	8,000,000	
Reserve for contingencies	1,580,000	
Hire purchase interest	413,000	
Laundry Expenses	434,000	
Legal and professional fees	400,000	
Depreciation	2,450,000	
Dividends paid	1,600,000	
Repairs and maintenance	872,000	
Insurance premium	320,000	
VAT Paid	168,000	
Bad and doubtful debts	228,000	
Advertising	1,200,000	
Bank charges	170,000	
Water and electricity	1,200,000	
Rent and rates	3,020,000	
Subscriptions and donations	371,000	
Telephone and postage	1,204,000	
Sundry expenses	600,000	
Motor Vehicle expenses	2,300,000	
Net Profit		3,296,000

Additional information:

- 1) Salaries and wages include sh. 66,000 paid to the income Tax Department as penalties and the interest on delayed submission of PAYE deduction.
 - 2) Hire purchase interest relates to loans obtained to purchase a delivery Van Sh146,000 and the Chairman's personal car Sh. 267,000.
 - 3) The company directors and senior managers are given free laundry services at the company's laundry. The cost of cleaning their personal clothing for the year ended 31 December 2014 was Sh. 133,000.
 - 4) Legal and professional expenses include Sh. 146,000 incurred while defending the Managing Director in a private suit against him.
 - 5) Repairs and maintenance include the cost of acquiring a second hand laundry machine for sh. 167,000.
- 5) Bad and doubtful debts are made up of a 10% general provision against the debtors balance as at 31 December 2014 and full provision of Sh. 93,000 owed by Oriented Finance Ltd. That

c) Notes on information used.

(3mks)

has been placed under receivership. The Debtors balance as at 31 December 2014 was Sh. 1,350,000.

7) Subscriptions and donations comprise:

Subscription to Rhino Golf Club for the Managing Director 260,000

Subscription to the chamber of Manufacturing and Commerce 63,500

Donation of books to the Watoto School for the Handicapped 35,000

Annual subscription for Finance Manager paid to the Institute of Certified Public Accountants of Kenya 12,000

8) Sundry expenses include Sh. 263,000 paid to Health Africa for the Managing Director's medical cover. He is the only one in the company covered by the medical scheme.

9) Wear and tear allowances for the year ended 31 December 2014 have been agreed at Sh.

4,320,000.

Required

- i) PQR Ltd's adjusted profit/loss (for tax purposes) for the year ended 31 December 2013. (8marks)
 ii) Corporation tax (if any) payable by PQR Ltd. For the year ended 31 December 2013. (2 marks)

QUESTION FOUR (b)

Write short notes on the following)

- | | |
|-----------------------------------|--------|
| i. Diminutive in value allowance | (2mks) |
| ii. Shipping deduction | (2mks) |
| iii. Investment allowance | (3mks) |
| iv. Industrial building allowance | (3mks) |

QUESTION FIVE

a) John Mwau practices mixed farming and closes his books on 31st December every year. He has provided the following income and expenses summary for the year ended 31st December 2020

Income:	sh
Sale of milk to Maziwa Dairies	154,750
Sale of vegetables	136,500
Sale of broilers to Chicken World Ltd.	457,500
Sale of sheep and heifers	138,000
Sale of firewood	<u>116,500</u>
Total income	<u>403,250</u>
Expenses:	Sh.
Fertilizers	19000
Pesticides	15500
Seeds	13600
Planting of tea seedlings	111100

Motor vehicle expenses (pick-up)	118000
Insurance for farm works	16900
Agricultural shows expenses	113300
Salaries and wages for employees	142000
Vaccines for livestock	18800
Electricity and water	16600
Purchase of chicks	158500
Animal Wood shavings and saw dust (for poultry)	12400
Construct of water storage tank	123500
Construction of chicken sheds	190000
Loan repayment - Famers SACCO Ltd	131200
Interest on loan - Farmers SACCO Ltd	110680
Repairs on dairy sheds and fences	16,000
Value of goats killed by a leopard	111,000
Wages for Mwau's house girl	13,300
Mwau's personal accident insurance	12,300
Bad debts written off	17,750
School fees for Mr. Mwau's children	300,00
Depreciation - motor vehicles	<u>28,550</u>
Total expenses	<u>49,3140</u>
Net loss	<u>(39,890)</u>

Additional information:

1. Insurance for farm works includes cover for Mwau's household items amounting to Sh. 11,900
2. Mr. Mwau received Sh.12,500 dividend, net of withholding tax from Majani Ltd.
3. Farm produce consumed by Mr, Mwau's family was valued at Sh.126,500
4. Mr. Mwau received Sh. 200000 from the local farmers' co-operative society as consultancy fees. The farmers' co-operative society uses his farm as demonstration farm from training other farmers.
5. Salaries and wages include Sh. 100,000 paid to Mwau wife.
6. Capital allowances for the year ended 31 December 2020 have been agreed with the Commissioner of Income Tax at Sh. 39,400

Required:

Mr. Mwau's taxable income an tax liability for 2020 (14 marks)

- b) PQ Ltd purchased 600 units at sh.960 each and sold 590 units at sh.1320 each
prices are inclusive of VAT of 16%

Required

- i. VAT a/c
- ii. Purchases a/c
- iii. Sales a/c

(6mks)