



MERU UNIVERSITY OF SCIENCE AND TECHNOLOGY

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University Examinations 2023/2024

SECOND YEAR SECOND SEMESTER EXAMINATION FOR THE DEGREE OF
BACHELOR OF COMMERCE, BACHELOR OF BUSINESS ADMINISTRATION AND
BACHELOR OF BUSINESS INFORMATION TECHNOLOGY

BFC 3276: INTRODUCTION TO TAXATION

DATE: APRIL 2024

TIME: 2 HOURS

INSTRUCTIONS: Answer question *one* and any other *two* questions

QUESTION ONE (30 MARKS)

- (a) Differentiate between a "tax" and a "charge" as imposed by the government. (2 marks)
- (b) Distinguish between tax evasion and tax avoidance. (4 marks)
- (c) Mrs. Chagua received pension of Sh. 1,500,000 out of which sh. 450,000 was annual entitlement. Calculate her taxable income. (4 marks)
- (d) The recent debate relating to importation of goods through the port of Mombasa has had one of its issues the amount of tax assessed. Specify and explain clearly at least four ways in which the Government may lose tax revenue on imports. (4 marks)
- (e) Describe two advantages and two disadvantages of direct as opposed to indirect taxation. (4 marks)
- (f) The following information relates to Mr. Kathurima and his wife for the year ended 31st December 2023:
- (i) He was employed by Lipa Ltd as a sales manager on the following terms:
- Basic pay per annum Sh. 1,000,000 (annual PAYE Sh. 300,000)

- Annual bonus of Sh. 30,000
- Monthly commission equal to 2% of monthly basic pay
- Annual medical allowance (non-discriminatory scheme) of Sh. 180,000 paid on reimbursement basis. During the year, he was reimbursed Sh. 120,000 for medical cost incurred on self and family
- Free lunch valued at Sh. 40,000 per annum

(ii) He obtained a loan from the employer amounting to Sh. 600,000 on 1st December 2023. The interest on the loan was specified by the employer as 5% per annum.

Assume a prescribed interest rate of 8% per annum for the month of December 2023.

(iii) He paid life premium amounting to Sh. 80,000 during the year for policies on self and family

(iv) His wife is employed by Mauzo Ltd as a financial analyst at a basic salary Sh. 85,000 per month. Mr. Kathurima owns 25% of the ordinary share capital of Mauzo Ltd.

(v) The following additional income accrued to his wife during the year: - She earned a profit of Sh. 500,000 from a supermarket business registered by her name but managed by her daughter. This profit was after deducting Sh. 150,000 paid as salary to the daughter during the year. The daughter was below eighteen years of age as at 31st December 2023.

- She owns residential houses inherited from her father. The rental income received for the year amounted to Sh. 580,000.

Required:

(i) The taxable incomes of Mr. Kathurima and his wife for the (8 marks)

(ii) The tax liability of Mr and Mrs. Kathurima for the year ended 31st December 2023 (2 Marks)

(iii) Briefly comment on the procedure for the filing of the wife's income tax returns. (2 Marks)

QUESTION TWO (20 MARKS)

Write explanatory notes on the taxes listed below and in each case indicate whether the tax complies with the main principles of a good tax system.

(a) Presumptive tax on agricultural produce. (5 marks)

(b) Cess on agricultural produce. (5 marks)

(c) Trade licence chargeable to professionals. (5 marks)

(d) Stamp duties on transfer of properties. (5 marks)

QUESTION THREE (20 MARKS)

Kenwide Company Ltd. is a distributor of wines and spirits. The profit and loss account for the year ended 31 December 2023 is as follows:

	Sh.		Sh.
Purchases	1,000,000	Sales	3,655,000
Staff wages	850,000	Discounts	355,000
Rent and rates	92,500	Provision for bad and	
Distribution and office		doubtful debts	35,500
expenses	445,500	Profit on sale of assets	65,500
Traveling	256,000	Insurance recovery	170,000
Repairs and maintenance	85,600		
Discount	156,000		
Bad debts	122,100		
Subscription	25,000		
Bank charges & interest	24,000		
Loss on sale of assets	35,500		
Legal fees	95,000		
Audit fees	41,500		
Depreciation	126,000		
Net profit	<u>917 300</u>		<u> </u>
	<u>4,282,000</u>		<u>4,282,000</u>

Additional Information:

- 10% of rent and rates relate to directors.

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|---|--------|
| 2. Distribution and office expenses includes the following expenses: | Sh. |
| Directors personal expenses | 31,550 |
| Contribution to a sports club — employees use it | 30,000 |
| Donations | 22,000 |
| Loss on staff canteen | 12,000 |
| 3. Repairs and maintenance include extension to an office block | 40,000 |
| 4. Subscriptions are to trade associates. | |
| 5. Travelling expenses include business trip to Dubai to attend a trade exhibition. | 56,000 |
| 6. Legal charges include the following: | |
| Acquisition of copyrights | 25,000 |
| Debt collection | 21,000 |
| Renewal of lease for 99 years | 18,000 |
| Fines and defence of legal suits | 11,000 |
| Employment contract | 5,000 |
| 7. Insurance recovery is in connection with stolen stock in the previous year. | |
| 8. Bad debts provision is reduced in general provision. | |

Required:

- (a) Prepare a tax computation. (14 marks)
- (b) Compute the tax liability and indicate the due date. (2 marks)
- (c) Compute the instalment tax payable in 2024 and indicate the respective due date(s). (4 marks)

QUESTION FOUR (20 MARKS)

Ojwang, Awino and Ochieng are partners trading as Okode Enterprises. Ojwang and Awino are active partners while Ochieng is a sleeping partner. The partnership agreement was silent on the profit and loss sharing ratio.

The partners have presented

Income:	Sh."000"	Sh '000'
Gross profit		12,000
Foreign exchange gain (realized)		364
Farming income		836

2. Salaries and wages included Sh. 1,200,000 and paid shs. 1,400,000 to Ojwang and Awino respectively during the year.

3. Legal expenses included:

	Sh''000''
Legal fees for breach of contract	250
Parking fines paid to the city council	280
Drafting lender documents	19
Drafting lease documents - 100 years	128
Defending a partner in a local committee	97

4. Mortgage interest related to a partner's residential house

Required:

- (i) The adjusted partnership profit or loss for the year ended 31st December 2023 (12 marks)
- (ii) Distribution schedule of the profit or loss calculated (i) above (4 marks)
- (iii) The tax payable by each partner (4marks)

QUESTION FIVE (20 MARKS)

- (a) Distinguish between single and multiple tax systems (2 marks)
- (b) Explain four reasons why a country might prefer a multiple tax system over a single tax system (4 marks)
- (c) Dellite Ltd. is a manufacturing company which commenced business on 1st October 2022 after inculTing the following capital expenditure:

	Sh.
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Factory building	9,600,000
Processing machinery	1,800,000
Generator	400,000
Godown	600,000
Delivery van	800,000
Staff canteen	700,000
Showroom	840,000
Drainage	

Additional information:

1. The factory building includes cost of office space Sh.360, 000, staff dwelling house Sh.500, 000, and a store for finished goods Sh.400, 000.
2. The godown was put into use on 1 July 2023 after the installation of an alarm system costing Sh.300, 000 and shelves for Sh. 100, 000 all fixed in the godown.
3. Production monitoring computers costing Sh.400, 000 were fixed into the processing machinery. The installation costs of the computers amounted to Sh.50, 000.
4. On 1 May 2023, a weighing scale was purchased for Sh.80, 000 and a motorcycle for the office messenger was purchased for Sh.96, 000.
5. On 1 July 2023, a saloon car was purchased for Sh.2, 300,000 for official use by the company's director.
6. During the year, the company imported a tractor for Sh.800, 000 before VAT and import duty. The duty charged was at the rate of 20% while the VAT rate was 16%.
7. On 1 April 2023, the company obtained a bank loan of Sh.5, 000,000 at a fixed interest rate of 15% per annum for constructing a parking bay. The parking bay was completed and used from 1st August 2023. The loan was repaid in full on 30 September 2023.

Required:

Capital allowances due to Dellite Ltd. for the year ended 30 September 2023. (14 marks)

TAX BANDS

Monthly Gross Pay (ICES.)	Annual Taxable Income	Tax Rate
Up to 24,000	Up to 288,000	10%
24,001 - 32,333	288,001 - 388,000	25%

32,334 - 500,000	388,001 -6,000,000	30%
500,001 - 800,000	6,000,001 – 9,600,000	32.5%
Above 800,000	Above 9,600,000	35%
Personal Relief is 2,400	Personal Relief is 28,800	

PRESCRIBED BENEFIT RATES OF MOTOR VEHICLES PROVIDED BY EMPLOYER

(i) Saloon, Hatch Backs and Estate

	Monthly Rates Sh.	Annual Rates Sh.
Up to - 1200cc	3,600	43,200
1201 - 1500cc	4,200	50,400
1501 - 1700cc	5,800	69,600
1751 -2000cc	7,200	86,400
2001 - 3000cc	8,600	103,200
Over —3000cc	14,400	172,800

(ii) Pick-ups, Panel Van (Unconverted)

Upto - 1750cc	3,600	43,200
Over - 1750cc	4,200	50,400

(iii) Land Rovers/Cruisers: 7,200 86,400

OR 2% of the initial capital cost of the vehicles each month, whichever is higher.

COMMISSIONER'S PRESCRIBED BENEFIT RATES

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

Investment allowance:	Rate of investment allowance	Residual value (per year on reducing balance)
(a) Buildings: • Hotel building ° Building used for manufacture ° Hospital building • Petroleum or gas storage facilities ° Educational/hostels building • Commercial building	50% in the first year of use 50% in the first year of use 10% per year on reducing balance 10% per year on reducing balance	25% 25% 25% 25%
(b) Machinery: Machinery used for manufacture • Hospital equipment • Ships or aircraft • Motor vehicles and heavy earth moving equipment • Computer software, calculators, copiers and duplicating machines • Furniture and fittings • Telecommunication equipment • Film equipment by a local producer • Machinery used to undertake operations under prospecting rights and exploration under mining rights	0% in the first year of use 50% in the first year of use 50% in the first year of use 5% per year on reducing balance 5% per year on reducing balance 10% per year on reducing balance 10% per year on reducing balance	25% 25% 25% 25%

<ul style="list-style-type: none"> Other machinery 	5% per year on reducing balance 0% in the first year of use 10% per year on reducing balance	
(c) Purchase/acquisition of right to use fibre optic cable by telecommunication operation	10% per year on reducing balance	
(d) Farm works	0% in the first year of use	25%