



GARISSA UNIVERSITY

**UNIVERSITY EXAMINATION 2017/2018 ACADEMIC YEAR THREE
FIRST SEMESTER EXAMINATION**

SCHOOL OF BUSINESS AND ECONOMICS

FOR THE DEGREE OF BACHELOR OF BUSINESS MANAGEMENT

COURSE CODE: BBM 303

COURSE TITLE: TAXATION 1

EXAMINATION DURATION: 3 HOURS

DATE: 01/12/17

TIME: 2.00-5.00 PM

INSTRUCTION TO CANDIDATES

- The examination has SIX (6) questions
- Question ONE (1) is COMPULSORY
- Choose any other THREE (3) questions from the remaining FIVE (5) questions
- Use sketch diagrams to illustrate your answer whenever necessary
- Do not carry mobile phones or any other written materials in examination room
- Do not write on this paper

This paper consists of NINE (9) printed pages

please turn over



QUESTION ONE (COMPULSORY)

- (a) What does the term employer include for PAYE purposes? [2 marks]
- (b) Distinguish between tax evasion and tax avoidance. [4 marks]
- (c) Give five examples of non-taxable income. [5 marks]
- (d) Explain the concept of elasticity with respect to:
- i. Direct Tax [2 marks]
 - ii. Indirect Tax [3 marks]
- (e) Amina is an accountant with Garissa Enterprises Ltd. Details of her employment income for the year ended 31 December 2016 are as follows:
- i. Salary per month – Sh.110,000 (PAYE of Sh.34,600 per month).
 - ii. She contributes 7.5% of her monthly salary to the company's pension scheme which is registered with the Commissioner of Income Tax and her employer pays 15% of her monthly salary.
 - iii. She is paid a bonus of sh.2,000 per month
 - iv. She is housed by her employer in a house where the employer pays a rent of Sh.5,000 per month.
 - v. Her employer pays on her behalf life insurance premium at sh.2,000 per month.
 - vi. Interest received by Amina during the year was as follows:

Post Office Savings Bank	Sh.12,000
Fixed Deposit Account: Euro Bank	Sh. 2,250
Savings Account: National Bank	Sh. 8,400
 - vii. She owns 20,000 ordinary shares of Sh.10 each in CBA Banki Ltd. During the year of income, she received a dividend of Sh.5 per share.

Required:

- i. Compute chargeable income for Amina in 2016. [6 marks]
- ii. Compute Amina's 2016 tax liability. [3 marks]

QUESTON TWO

- (a) Write brief notes on the following:
- i. Taxation of companies operating in export processing zones [3 marks]
 - ii. Taxation of members' clubs [3 marks]
- (b) E-Talk Ltd. has been in the business for many years. The company's profit and loss account for the year ended 31 December 2012 is as follows:



	Sh.	Sh.
Sales		20,450,500
Less: Cost of sales		15,705,000
Gross profit		4,745,500
Less expenses:		
Salaries and wages	1,200,400	
Shop expenses (rent, rates, lighting and telephone)	100,800	
Printing and stationery	40,200	
Motor vehicle expenses	300,000	
Bad and doubtful debts	88,100	
Loss on sale of motor van	105,800	
Depreciation – motor vehicle	115,000	
Interest on loan to purchase investment shares	99,200	
Compensation to ex-directors	250,700	
Sundry expenses (all allowable)	150,500	
Legal expenses	200,000	
Redundancy payments to retrenchment staff	36,400	2,687,100
		2,058,400
Dividend received from Safaritel Ltd.		144,900
Net profit		2,203,300



Additional information:

1. Capital allowances have been agreed with the Commissioner of Income Tax at Sh.99, 200.
2. The bad and doubtful debts for the year is as follows:

Debts written off:	Sh.
Customers	21,200
Staff	1,600
General provision	34,200
Specific provision	<u>31,100</u>
	<u>88,100</u>

3. Legal expenses consist of:

	Sh.
Advice on staff service contracts	23,200
Tax appeals	38,400
Defense against criminal activities	20,200
Acquisition of copy rights	42,500
Preparation and renewal of a lease of more than 99 years	50,000
Debt collection	<u>25,700</u>
	<u>200,000</u>

Required:

- i. Compute the adjusted taxable profit or loss for E-Talk Limited for the year 2012. **[5 marks]**
- ii. Calculate the tax payable thereon. **[2 marks]**
- iii. Assume that the management of E-talk Limited neither paid the tax in (b) above on the due date nor submitted the self-assessment return as required. What are the consequences of this action? **[2 marks]**



QUESTION THREE

(a) Name five objectives of raising taxes and explain how they are achieved by the government

[5 marks]

(b) Ali, Kerow and Maalim are in a partnership of selling imported clothes and shoes. They have provided the following information for the year of income 2015:

Net loss after deducting the following	(1,080,000.00)
Rent	180,000.00
Legal costs	75,000.00
Salaries & Wages	300,000.00
Donations: Dadab Food Relief Fund	100,000.00
Electricity & Water	35,000.00
Repair to business premises	65,000.00
Stationery	12,000.00
Vehicle expenses	90,000.00
Advertising	65,000.00
Depreciation: -Car	10,000.00
-Building	33,000.00
Salaries: -Kerow	240,000.00
-Maalim	240,000.00
-Ali	360,000.00
Interest on capital: -Kerow	80,000.00
-Maalim	80,000.00
-Ali	120,000.00
Bad debts	40,000.00
Political Party membership: Kerow	15,000.00
Dresses taken by Ali for his own use	17,000.00
School fees paid for Ali's Children	90,000.00

Additional information:

- Wear and tear deductions were estimated at Sh. 16,000.
- Salaries and wages include Sh.25,000 paid to Ali's daughter for assisting in the business during the school holidays.
- Legal costs included a payment of Sh.15,000 paid to an arbitrator to settle a personal dispute between Kerow and Maalim.
- Thirty per cent of vehicle expenses was for personal use
- Bad debt analysis: Sh.

General provision	10,000
Specific provision	12,000
Written-off	8,000
Ali's son (defaulter)	<u>10,000</u>
	<u>40,000</u>



vi.	Advertising:	Sh.
	Advertising campaign	28,000
	Cost of new sign board	5,000
	Sale of clothes	9,000
	Ali's birthday expenses	<u>23,000</u>
		<u>65,000</u>
vii.	Rent analysis:	
	Payment for Partners residence	Sh. 100,000
	Business	Sh. 80,000
viii.	Other incomes (included in trading profit)	Sh.
	Dividends from shares KCB Ltd.	19,000
	Rental income: sub-letting business premises	22,000
	Gain on sale of furniture	<u>13,000</u>
		<u>54,000</u>

Required:

- i. Taxable income (loss) for the partnership business and distribution among Ali, Kerow & Maalim for 2015 if they share profits and losses in the ratio 2:1:1 respectively. **[8 marks]**
- ii. Determine the taxable income of each partner. **[2 marks]**

QUESTION FOUR

- (a) With regard to Value Added Tax, Outline circumstances which may lead to deregistration from VAT. **[3 marks]**
- (b) A tax invoice is often regarded as one of the important documents in the operation of VAT. State the items, which must be contained in such an invoice **[2 marks]**
- (c) Marian operates an electronics shop along Luthuli Avenue in Nairobi. She undertook the following transactions for the month of March 2016:



1 March 2016	Purchased 10 cameras for a total of Sh.500,000
4 March 2016	Purchased flashbulbs for a total of Sh.200,000
4 March 2016	Purchased 5 slide projectors for a total of sh.1,000,000
5 March 2016	Sold 5 cameras each at 25% above cost price.
6 March 2016	Purchased 200 wrist-watches at Sh.1,500 each.
8 March 2016	Sold 2 slide projectors for a total of Sh.500,000.
9 March 2016	Sold flashbulbs that cost sh.100,000 for Sh.150,000.
12 March 2016	Purchased 50 stop watches for a total of Sh.50,000
15 March 2016	Purchased 100 alarm clocks at a total value of sh.80,000
18 March 2016	Sold the remaining 5 cameras each at 15% above cost price.
20 March 2016	Sold 3 slide projectors for a total of sh.550,000.
22 March 2016	Sold 100 wrist-watches at sh.2,000 per watch.
25 March 2016	Sold 70 alarm clocks each at 30% above cost.
27 March 2016	Sold 500 stop watches for a total of Sh.75,000.

Required:

- i. Given that the prices are inclusive of VAT, calculate Marian's:
 - a. Input Tax [3 marks]
 - b. Output Tax [3 marks]
- ii. Prepare the VAT account for Marian clearly showing the VAT (refundable). [2 marks]
- iii. State when the above tax is due, and the penalties payable if the tax is not paid on the due date. [2 marks]

QUESTION FIVE

- (a) Explain three reasons why Capital Allowances are guaranteed [3 marks]
- (b) Briefly explain types of Capital Allowances [4 marks]
- (c) On 1 January 2003, Jamra Manufacturers Limited commenced business at Masalani District with the following assets:



	Sh.
Goodwill	600,000
Land	24,000,000
Buildings (industrial)	51,000,000
Plant fixed to the buildings	7,200,000
Heavy duty fork lifts	4,950,000
Three transit goods prime movers	5,910,000
Mitsubishi Pajero vehicle for use by the Managing Director	3,960,000
Peugeot 504 pick-up	1,750,000
Security wall	1,200,000
Workers quarters	18,000,000
Boilers	6,000,000
Furniture and fittings	3,600,000
Milling machines	37,500,000

Additional information:

- The following assets were acquired in the year ended 31 December 2004:

	Sh.
V W Passat car for the Finance Manager	2,200,000
Toyota Hilux Pick-up	2,300,000
One tractor	3,200,000
Executive desks for departmental heads	900,000

- In the year ended 31 December 2004, the following assets were sold:



	Sales proceeds (Sh.)
One fork lift	1,200,000
One transit goods prime mover	1,500,000
Furniture	600,000
Milling machines	8,000,000

3. In the year ended 31 December 2005, the following assets were acquired or constructed:

	Sh.
Land	6,000,000
Buildings extensions	12,000,000
Additional conveyor fixed to the building	1,000,000
Staff bus	5,500,000
Drilled borehole	1,900,000
Computers	3,600,000

Required:

Capital allowances for the years ended 31 December 2003, 2004 and 2005 **[8 marks]**

QUESTION SIX

(a) Write brief notes on the following:

- i. Installment Tax **[2 marks]**
- ii. Self-assessment **[2 marks]**
- iii. Notice of Objection **[2 marks]**

(b) Explain three (3) purpose of taxation in Kenya **[6 marks]**

(c) What is the tax treatment of school fees? **[3 marks]**

