



MUEO

# **MOI UNIVERSITY**

OFFICE OF THE CHIEF ACADEMIC OFFICER

## **UNIVERSITY EXAMINATIONS 2012/2013 ACADEMIC YEAR**

**THIRD YEAR END OF SEMESTER EXAMINATIONS**

**FOR THE DEGREE OF  
BACHELOR OF BUSINESS MANAGEMENT**

**COURSE CODE: BBM 303**

**EXAM TITLE: TAXATION I**

**DATE: 25<sup>TH</sup> OCTOBER, 2012**

**TIME: 9.00 A.M. – 12.00 NOON.**

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***INSTRUCTION TO CANDIDATES***

**> SEE INSIDE.**

**BBM 303: TAXATION 1**  
**MAIN EXAMINATION**  
**ACADEMIC YEAR 2012/2013**

**INSTRUCTIONS TO CANDIDATES:** Answer any **FOUR** Questions. All Questions carry equal Marks.

**QUESTION ONE**

- Enumerate **FIVE** objectives of raising taxes and discuss how they are achieved by the government (8 Marks)
- Briefly discuss the case for and against direct and indirect taxation. In your own opinion, justify the most appropriate form of taxation in Kenya (8 Marks)
- Define the term "tax avoidance" and identify two ways in which an individual or institution could engage in the practice of "tax avoidance" (4 Marks)

**(Total 20 Marks)**

**QUESTION TWO**

- Income Tax Act Cap 470 (Laws of Kenya) Second Schedule provides for capital deduction in respect of capital expenditure. Discuss various capital deductions available to business enterprises in Kenya. (8 Marks)
- Mulirp Ltd., a company dealing in hardware, prepares its accounts to 30 June each year. The following information relates to the year ended 30 June 2011:

- Written down value of assets brought forward for Income Tax purpose:

	Class I	Class III	Class IV
	37½%	25%	12½%
	<b>Shs</b>	<b>Shs</b>	<b>Shs</b>
Written Down Value 30.6.2010	175,000	180,000	87,000

- Disposals during the year:

	Cost	Net Book Value	Sales proceeds
	<b>Shs</b>	<b>Shs</b>	<b>Shs</b>
Isuzu Lorry	280,000	175,000	260,000
Motor car (purchased in 1.3.2010)	1,160,000	1,015,000	800,000

- Additions during the year:



	Shs
Mercedes Benz sports car for director	4,000,000
Second-hand Tractor	80,000
Trailer occasionally used by tractor	80,000
Shop fittings	60,000
Computers	250,000
Telephone system	72,000
Partitions	30,000
Machinery	100,000
Motorcycle	50,000

- iv) The office safe which cost Shs 30,000, in 2008 was traded-in for a more modern safe costing Shs 40,000. The old safe was valued at Shs 20,000 and the company paid the balance of Sh. 20,000 to acquire the new safe. The net book value of the old safe was Shs 22,968 at 30.6.2010.

**Required**

Calculate the wear and tear deductions due to the company for the year 2009. (12 Marks)  
(Total 20 Marks)

**QUESTION THREE**

- a) Explain the difference between a resident and non resident person for tax purposes. (4 Marks)
- b) Mr. Omondi is an employee of Yara Limited. He has provided you with the following information for the year ended 31<sup>st</sup> December 2011.
- Basic salary per month Shs. 75,000. He also received a bonus of 20% of his basic pay at the end of the year.
  - Staff meals provided by employer 2000/- per month.
  - He is housed by the company which deducts Shs. 13,000 per month from his pay as rent.
  - The employer also pays him Shs. 2,000/- per month as overtime.
  - He receives leave pay of Shs. 17,000 for the year from the employer.
  - He is provided with a company car with an engine capacity of 2,000 cc whose cost as at 1<sup>st</sup> January 2009 was Shs. 560,000.
  - He contributed Shs. 240,000 during the year to a registered pension scheme.
  - He also has a poultry farm which he receives a net profit of Shs. 20,000 per year.
  - Mr. Omondi has a rental house in which he earns a gross rent of Ksh. 105,000. He incurred Ksh. 10,000 to recover rent from the tenants, Ksh. 19,000 for painting, Sh. 30,000 for structural alteration to the building to conform to Municipal plan and Sh. 25,000 for insurance and security.

**Required**

- a) Determine the total taxable income of Mr. Omondi for the year ended 31<sup>st</sup> December 2009. (13Marks)
- b) Calculate the tax payable by Omondi for the year ended 31<sup>st</sup> December 2009. (3 Marks)  
(Total 20 Marks)

#### **QUESTION FOUR**

- (a) Outline the importance of a tax invoice in the administration of VAT. (4 Marks)
- (b) Mr. Otwere is a registered VAT trader dealing in household electronics. On 5<sup>th</sup> August, 2011, he sold the following electronic goods to Mr. Okundi on credit terms.

Item	Quantity Sold	Selling Price per Unit (Before VAT)
Radio	2	15,000
Television	1	30,000
Fridge	1	40,000

The goods were subject to VAT at the standard rate of 16%.

#### **Required**

Prepare a tax invoice in the books of Mr. Otwere relating to the above transactions.

(6 Marks)

- (c) Explain any FIVE benefits of VAT as a tax. (5 Marks)
- (d) Do you support the governments push to subject VAT on foodstuff and necessities at the standard rate? Discuss. (5 Marks)

**(Total 20 Marks)**

#### **QUESTION FIVE**

Mwende, Kwende and Twende are former schoolmates who are doing business together. The business is conducted as a partnership firm in which they share profits and losses equally. They keep proper books of account and have been able to provide the following profit and loss account for the year ended 31 December 2011.

#### **Profit and Loss Account**

	Shs		
Operation expenses	800,000	Gross Profit	1,908,000
Rent of business premises owned by all of them jointly	180,000	Sundry receipts	80,000
Interest expense	80,000	Interest income	72,000
Stationery and printing	120,000	Profit on sale of shares	200,000
Lighting and heating	40,000	Gross income from farming	800,000
General farm expenses	294,000	Lottery winnings	340,000
Repair of premises	40,000	Dividend (Gross)	120,000
Depreciation	300,000		
Interest on partner's capital:			
Mwende	80,000		
Twende	120,000		
Salary to Kwende	160,000		
Commission to partners:			
Mwende	96,000		
Kwende	96,000		
Twende	96,000		
Bad debts	240,000		
Gifts, present and charity	40,000		
Donation to child welfare	200,000		



Interest on loan taken to pay tax	20,000
Legal charges	120,000
Net Profit	<u>398,000</u>
	<u><u>3,520,000</u></u>

3,520,000

#### **Additional information**

1. Capital allowances have been agreed as follows: Wear and Tear allowance Sh.180,000; Farm works deduction Sh.120,000
2. The partners had borrowed Sh.400,000 with a hope of investing it on fixed securities to earn more income. Interest rates nevertheless declined. Interest expense of Sh.80,000 and interest income of Sh.72,000 relate to this loan.
3. Legal charges include Sh.40,000 paid to finish a case in the customs department.
4. In 2011, the partners brought forward losses amounting to Sh.800,000 from this business.

#### **Required:**

- (a) Compute taxable income derived from the partnership. (16 marks)
- (b) Show allocation among partners. (4 marks)

**(Total 20 Marks)**

#### **Question Six**

Explain the meaning of the following terms as used in respective tax legislations:

- i. Fringe benefit tax (3 Marks)
- ii. Stamp duty (2 Marks)
- iii. Excise duty (2 Marks)
- iv. Pension income (2 Marks)
- v. Residential status (3 Marks)
- vi. Personal relief (2 Marks)
- vii. Tax Invoice (2 Marks)
- viii. Impact of tax (2 Marks)
- ix. Incidence of tax (2 Marks)

**(Total 20 Marks)**

\*\*\*\*\***END**\*\*\*\*\*

**RATES OF TAX** (Including wife's employment, self employment and professional income rates of tax).  
Year of income 2011.

Monthly Taxable Pay (Shillings)	Annual Taxable Pay (Shillings)	Rates of Tax % in each Shilling
1 - 10164	1 - 121968	10%
10165 - 19740	121969 - 236880	15%
19741 - 29316	236881 - 351792	20%
29317 - 38892	351793 - 466704	25%
Excess over 38892	Excess over 466704	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.)
<b>Capital Allowances:</b>		
Wear and tear allowances:		
Class I	37.5%	
Class II	30%	
Class III	25%	
Class IV	12.5%	
<b>Industrial Building Allowances:</b>		
Industrial buildings	10%	
Hotels	10%	
<b>Farm Works Allowances</b>	50%	
<b>Investment Deduction Allowance:</b>		
2009 - 100%		
2010 - 100%		
2011 - 100%		
Shipping investment deduction	40%	
<b>Mining allowance:</b>		
Year 1 - 40%		
Year 2-7 - 10%		
<b>OR 2% of the initial capital cost of the vehicle for each month.</b>		

**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
iii. Provision of furniture (1% of cost to employer)		
If hired, the cost of hire should be brought to charge		
iv. Telephone (Landline a and mobile phones)	30% of bills	
<b>Agricultural Employees: Reduced Rates of Benefits</b>		
(i) Water	200	2,400
(ii) Electricity	900	10,800

**Other Benefits:**

Other benefits for example, servants, security, staff meals etc are taxable at the higher of fair market value and actual cost to employer.