



MACHAKOS UNIVERSITY

University Examinations for 2021/2022 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING BANKING AND FINANCE

THIRD YEAR SEMESTER EXAMINATION FOR

BACHELOR OF

BAC 304: FUNDAMENTALS OF TAXATION

DATE:

TIME:

INSTRUCTIONS:

Answer Question One and Any Other Two Questions

QUESTION ONE (30 marks)

- a) The following information relates to the transactions of communication solutions ltd for the month of September 2017. The company is registered for VAT.

September 2 purchased goods worth sh.2,400,000 from Japan. Customs duty was paid at 5%.

September 2 sold goods to mobile connections ltd for sh.960,000 on credit. Goods worth sh.60,000 were found to be defective and were returned.

September 5 purchased office furniture for sh.640,000. One desk worth sh.80,000 was defective and was returned to the seller.

September 9 purchased goods worth 4,500,000 on credit from a manufacturing company. Goods worth sh.500,000 were damaged in transit and were thus not salable. it cost the company sh.240,000 to transport the goods.

September 10 sold goods for cash worth sh.960,000

September 12 exported goods worth sh.2,400,000

September 16 imported goods worth 1,500,000 from india. Customs duty was paid at 5% .

September 20 sold goods worth sh.218,000 to XYZ ltd.

September 25 Exported goods worth sh.2,600,000 to kimbo ltd.

September 30 paid the following expenses for the month of September.

Salaries and wages sh.1,400,000

Electricity sh.48,000

Telephone sh.36,000

Water sh.10,000.

Note: where applicable prices are quoted inclusive of VAT.

Required: the VAT payable (or refundable) for the month of September 2017.

(10 marks)

b) The profit and loss account of Kipkorir Kiboen, a trader in Nakuru town show the following details for year ended 31 Dec, 2005.

	Sh.	Sh.
Sales		1,200,000
Opening stock	166,000	
Add: purchases	375,000	
Less: closing stock	<u>(150,000)</u>	<u>391,000</u>
Gross profit		809,000
<u>Other Income:</u>		
Interest: Post Office Savings Bank	120,000	
Baclays Bank Interest (Gross)	20,000	
Sweepstake winnings	35,500	
Sale of a plot at Mathare, Nairobi	<u>16,500</u>	<u>192,000</u>
		1,001,000
Less:-Sundry expenses		<u>(458,000)</u>
Net Profit		<u>543,000</u>

Notes:

Payment from a resident insurance company for trading stock destroyed by fire amounting to Sh.115,000 has been included in drawings account.

A creditor cancelled an amount payable to him by Mr. Kipkorir of Sh.35,000 also included in drawings account.

Sundry expenses in Mr. Kipkorir's profit and loss account include:

- a. A second hand furniture bought during the year Sh.20,500
- b. Alimony paid to former wife he divorced Sh.14,500
- c. Subscription of Sh.8,000 paid to a welfare association of which he is a member
- d. Paid with amount drawn and included in drawings account were:
 - i) Insurance premium of Sh.13,000 against fire in respect of trading stock.
 - ii) Painting of business premises for Sh.5,000
 - iii) Stationary for Sh.3,500

Required: Compute Mr. Kipkorir's taxable income for Year 2005. (17 marks)

c) Explain the features of a tax policy for a developing country. (3 marks)

QUESTION TWO (20 MARKS)

a) A ship of 500 tons was acquired on 1.1.2002 at Ksh.40, 000,000. It was sold in Year 2005 for Kshs.36,000,000.

Required: Compute capital allowances to claim for the years 2002 to 2005. (10 marks)

b) A mining company incurred the following expenditure prior to mining operations:

i. Search for minerals	sh. 300,000
Discovery of the minerals	60,000
Testing of the minerals	240,000
Wining access to deposits	150,000.
ii. Acquisition of patent rights	60,000.

iii. Buildings, machinery other than those

qualifying for wear & tear allowance 540,000.

iv. General administration before commencement.

300,000

1,650,000

Required: Compute mining allowance. (6 marks)

b) what are the factors which govern taxable capacity? (4 marks)

QUESTION THREE (20 MARKS)

a) Mrs Kamau is the owner of a supermarket in Nairobi East. Her accounts clerk has submitted to you the following trading, profit and loss account for the year ended 31 December 2017.

	Sh.		Sh.
Opening stock	8,640,000	Closing stock	1,004,000
Purchases	96,000,000	Proceeds from sale of land	
Donations to Kenya Chamber of commerce	100,000	allocated to her by government	500,000
Redundancy payments	600,000	Gain on sale of shares	200,000
Contributions to a registered Pension fund	100,000	Gain on sale of residential plot	400,000
Rent, rates and taxes	110,400	General bad debts recovery	36,000
Insurance	14,880	Dividends (net)	43,200
Legal and professional fees	109,200		
Depreciation	363,840		
Advertising	116,800		
Value added tax	247,200		
Customs duty-2017	700,000		
Income tax for 2015	312,000		
Medical expenses (mrs kamau)	28,800		
Interest on bank overdraft	49,920		
Purchase of equipment	25,200		
Christmas gifts to customers	20,160		
General bad debts	55,200		
Household expenses	100,800		
Stationery and postage	33,120		
Net profit	<u>2,905,680</u>		

The following additional information is also provided

- i) Rent, rates and taxes includes sh.20,400 being customs duty for the purchase of equipment.
- ii) Sales include a sum of sh. 120,000 representing the value of goods withdrawn for use by Mrs. Kamau and her children. These goods had been purchased at a cost of sh.96,000

Required: a) Mrs. Kamau's chargeable profit for the year of income 2017

(16 marks)

b) The tax payable on the profit.

(4 marks)

QUESTION FOUR (20 MARKS)

Kip and Limo have been trading in partnership sharing profits and losses in the proportion of three fifths and two-fifths respectively. Their main activity is buying and selling property. Accounts to 31 December 2005 are presented below:

Income	Notes	Sh.
Gross profit from sale of residential houses		4,880,000
Interest from treasury bills (gross)	(1)	270,000
Pre-sale rent income		360,000
Commission on sale of public playground	(2)	<u>2,000,000</u>
		<u>7,510,000</u>
 Expenditure		
Interest on capital – Kip		40,000
Interest on capital - Limo		32,000
Goodwill written off		62,000
Bad debts	(3)	560,000
Audit, insurance and legal fees and expenses	(4)	320,000
Motor vehicle expenses		330,000
Depreciation		118,000
Special expenses	(5)	48,000
Salary to Limo		620,000
Loss on sale of Kenya Airways shares	(6)	280,000
Repairs and renewals	(7)	75,000
Salaries and wages		2,960,000

Light, water and electricity		148,000
Retirement benefits	(8)	240,000
Subscription and donations	(9)	<u>30,000</u>
		<u>5,863,000</u>
Profit for the period		1,647,000

Notes

1. Interest from treasury bills - The partners have informed you that they have heard that, although included in the accounts, the interest is not taxable.
2. Commission on sale of public playground. The commission was earned from a politician who allocated himself the playground irregularly and subsequently the partners found a buyer for the playground.
3. Bad debts: The bad debts are composed as follows:

	Sh.
A customer (through court action)	400,000
Partner's wife	<u>160,000</u>
	<u>560,000</u>

4. Audit, insurance and legal fees and expenses:	Sh.
Audit expenses	120,000
Partner's insurance	80,000
Legal fee - debt collection	80,000
defend action from (2) above	<u>40,000</u>
	<u>320,000</u>

5. Special expenses:	Sh.
Staff redundancy costs	30,000
Commission paid to facilitate transfer at land office	<u>18,000</u>
	<u>48,000</u>

6. Loss on Kenya Airways shares. The partners bought Sh.30,000 shares and sold them after price declined to avoid further loss.

7. Repairs and renewals: Sh.35,000 was used to repair Limo's house.

8. Retirement benefits:	Sh.
NSSF contributions	10,000
Pension to staff	190,000
Provident fund for partners	<u>40,000</u>
	<u>240,000</u>

9. Subscription and donations: They were made to Mukuru Childrens' fund, a national project to help street children.

Required:

- a) Compute the taxable profit of the partnership. (10 marks)
- b) Compute the tax payable by each of the partners, assuming that the partners have no other source of income. (6 marks)
- c) Is the money earned by the politician on sale of a playground taxable? Explain. (4 marks)

QUESTION FIVE (20 MARKS)

- a) Explain the meaning of income from rent and state the deductions allowed against rental income. (5 marks)
- b) Mr. Munene rented out his five houses in Komarock, Nairobi for Sh.35,000 per month for each house from 1st May 2005. Key money for each of Ksh105,000 was paid on assigning a five- year lease. The following expenses were incurred by him during the year:
 - 1) Rates and ground rent Sh.120,000 p.a
 - 2) Plumbing services on repairs Shs.60,000 paid in June 2005.
 - 3) A watchman was provided at a cost of Sh.48,000 p.a
 - 4) Installation of extra toilets in July 2005 for Sh.120,000
 - 5) Insurance premium for the properties sh.35,000 p.a.
 - 6) Fees to estate agent for arranging the lease calculated as 5% of the Gross income payable in October 2005.
 - 7) Interest on mortgage Sh.240,000 p.a.
 - 8) Repairs and maintenance costs incurred in February 2005 amounted to Sh.144,000.
 - 9) Furniture worth Sh.300,000 was provided on 1st July 2005.
 - 10) Cost of rent collection 5% of rent was paid during the year.
 - 11) Cost of wiring one of the toilets in July 2005 amounted to Sh.60,000.
 - 12) Incurred Sh.25,000 in October 2005 on replacing 4 wooden doors with metallic ones.

Required:

Compute Mr. Munenes' taxable rental income for year 2005. (15 marks)