

MURANG'A UNIVERSITY COLLEGE (MRUC)
(A Constituent College of Jomo Kenyatta university of Agriculture & Technology)

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF COMMERCE

BACHELOR OF COMMERCE

SPECIAL/SUPPLEMENTARY EXAMINATION 2014

THIRD YEAR, SECOND SEMESTER

MAIN CAMPUS

2014/2015 ACADEMIC YEAR

HBC 2302: ADVANCED TAXATION

DATE:

TIME: 3 HOURS

INSTRUCTIONS

Answer Question *ONE* and any *OTHER TWO* Questions.

COMPULSORY QUESTION (30 MARKS)

QUESTION ONE

(a) A Degree class was involved in a heated debate on whether taxes are necessary or not. One group was for the idea that taxes were good whereas the other group was opposed to the idea. Which group, in your view, would you join and why, State **Five** reasons to support your choice of the group. (5 Marks)

(b) State and explain whether or not the following were residents of Kenya;

(i) Mr. Charles has a permanent house in Kenya. He works for a company based in the United Kingdom (UK) where he lives. On September 2013 he came to Kenya for one month holiday. He had not returned to UK by December 31, 2013. (2 Marks)

(ii) Mapato Ltd is registered in South Africa where its headquarters are based. The company opened a branch in Kenya on March 2012. (2 Marks)

(iii) Mrs Farida Aloo, a Kenyan citizen is married to a Canadian citizen. She was employed in Kenya until August 30, 2013 when she resigned to join her husband in Canada. (2 Marks)

(iv) Zawadi Limited was registered in Kenya where the company operated until July 21, 2013.

The company thereafter relocated its operations to Kampala, Uganda. (2 Marks)

(c) State two Disadvantages of VAT (2 Marks)

(d) Miss Ochola reported the following information relating to her business for the year ended 31 December 2013.

(1) She was employed by Ndemwa Ltd as an assistant accountant at a monthly basic salary of sh 80,000 (P.A.Y.E sh 15,000 p.m)

(2) She received the following benefits from employment;

- A furnished house (cost of furniture sh 80,000). The market rental value of the house was sh14,000 per month. The employer deducted 5% of her basic salary per month to cover for the rent.

- The following utility bill and wages were paid by the employer during the year.

	Sh
Telephone	40,000
Electricity	20,000
House servant	66,000
Watchman	60,000

- She was reimbursed a sum of sh 70,000 for medical expenses incurred during the year. The medical scheme covered only employees with basic salary of less than sh.100,000 per month
- Her contribution to a registered pension scheme amounted to sh 6,000 per month. The employer contributed sh 12,000 for her to the pension scheme.
- The employer paid sh 15,000 per month for her university education and sh 10,000 for her during the year representing entrance fees and annual subscription to a professional association.

(3) She received the following additional income during the year;

	sh
• Profit from second-hand clothes managed by her brother	18,000
• Farming income (deductible expenses sh12,000)	42,000

Required;

(i) Taxable income for Miss Ochola for the year ended 31 December 2013 (10 Marks)

(ii) Tax payable on the income computed in (i) above (5 Marks)

(Total;30 Marks)

Question 2

- (a) Identify **four** ways in which an individual or firm could engage in “tax avoidance” (4 marks)
 - (b) Suggest **four** ways in which a Government can act in order to reduce incidences of “Tax evasion” (4 marks)
 - (c) Briefly explain how the PAYE system operates in Kenya. What are its advantages? (6 marks)
 - (d) State the meaning of the term “Tax Amnesty”. State its importance in relation to tax administration (6 marks)
- (Total;20 Marks)**

Question 3

- (a) Discuss **four** factors that influence the shifting of tax in an economy. (4 Marks)
- (b) Explain the **four** bases of classifying taxes. (4 Marks)
- (c) Mapema Ltd is registered for VAT. The company’s accounts for the month of April 2013 showed the following transactions.

Month	Purchases Sh.	Sales Sh.
January	4,470,000	5,960,500
February	5,091,200	6,320,250
March	3,490,600	2,950,000
April	7,143,200	9,280,700

The sales and purchases are inclusive of the VAT where applicable.

Additional information

- (i) 20% of the monthly purchases and sales relate to exempt goods respectively
 - (ii) Credit notes amounting to sh 68,000 were issued to customers in the month of April 2013
 - (iii) Debit notes amounting to sh 45,000 were received from suppliers in the month of April 2013
- (The VAT standard rate is 16% where applicable)

Required

The VAT account for the four months period ended 30 April 2013 (12 Marks)

(Total;20 Marks)

Question 4

Kimani, Kipng’etich and Kidum have been in partnership as Tripple K Enterprises sharing profits in the ratio of 2:2:1 respectively. They have presented the following profit and loss account of their business for the year ended 31 Dec 2013

	Sh.’000’	Sh.’000’
Gross profit		24,800
Investment income (gross)		450
Rent from Property		132

Miscellaneous Income		<u>315</u>
		25,697

Deduct expenses

Depreciation	110	
Salaries and Wages	28	
Office equipment	1568	
Legal expenses	360	
Sundry expenses	630	
Trade expenses	380	
Bad debts	86	
Local taxes on property	21	
Electricity	64	
Partner' salaries, interest on capital and drawings	13,350	<u>(16,597)</u>
		<u>9,100</u>

Additional information

1. Investment income comprises:		sh 000
Interest on Post office savings Bank (POSB) deposits		210
Dividend on shares in quoted companies		130
Interest charged on partners' drawings:	Sh '000'	
Kimani	50	
Kipng'etich	40	
kidum	<u>20</u>	<u>110</u>
		<u>450</u>
2. Miscellaneous income comprises		sh '000'
Gain on the sale of furniture and fittings		195

Insurance recoveries for stolen stock		100
Bad debts not previously written off		<u>20</u>
		<u>315</u>
3. Office expenses include the following		sh 000
Advertisements on the bill boards		250
Rent and Rates		700
Printing and Stationery		64
Installment tax paid		45
Provisions;	Sh '000'	
Specific	40	
General	<u>60</u>	100
General expenses (allowable)		<u>518</u>
		<u>1568</u>

4. legal fees include sh 150,000 incurred on successful defense of a partner legal suit and further sh60,000 incurred as parking fine.

5. Sundry expenses comprise;

	Sh '000'
Cash donations to Palpsy Care center	420
Debt recovery charges	90
Motor vehicle maintenance costs	<u>120</u>
	<u>630</u>

6. Trade expenses include;

	Sh '000'
Subscriptions to a trade association	150
Value Added Tax (VAT) paid	170

Repairs to Building	<u>60</u>
	<u>380</u>

7. Partners' Salaries, interest on capital and drawings are analyzed as follows;

	Kimani	Kipng'etich	kidum	Total
	Sh'000'	Sh'000'	Sh'000'	Sh'000'
Salaries	4,000	4,500	3,700	12,200
Interest on capital	200	300	330	830
Drawings	<u>60</u>	<u>100</u>	<u>160</u>	<u>320</u>
	<u>4260</u>	<u>4900</u>	<u>4190</u>	<u>13,350</u>

8. Capital allowances for the year ended 31 December 2013 was agreed with the tax authority to be at sh 480,000.

Required

- (i) Adjusted Partnership profit and loss for the ended 31 December 2013 (11 Marks)
 - (ii) Distribution of the adjusted profits or loss among the partners (9 marks)
- (Total;20 Marks)**

Question 5

(a)The following is an extract from a recent working paper published by the International Monetary Fund (IMF) titled "Tax Policy for emerging markets".

"Setting up an efficient and fair tax system is far from simple, particularly for developing countries that want to be integrated in the international economy .The ideal tax system in the countries should raise essential revenue without excessive government borrowing and should do so without discouraging economic activity and without deviating too much from the tax systems in other countries."

In the light of the above extract, Discuss;

- (i) The principles to be considered when introducing a new tax Policy for emerging markets. (4 Marks)
- (ii) **Four** challenges faced by developing countries in introducing and establishing efficient tax systems

(4 Marks)

(b)"The tax policy in a developing country must be different from those of a developed country." Citing **four** reasons elucidate this statement

(4 Marks)

(c) Distinguish between an objection and an appeal in the context of administration of taxes (4 Marks)

(d) Taxes form the main revenue base for a government. Briefly explain other **four** sources of government revenue. (4 Marks)

(Total;20 Marks)