



MERU UNIVERSITY COLLEGE OF SCIENCE & TECHNOLOGY

P.O. Box 972-60200 Meru - Kenya. Tel: 020-2092048, 020 2069349
Fax: 020-8027449

University Examinations 2012/2013

SECOND YEAR, SECOND SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF
COMMERCE

HBC 2123: INTRODUCTION TO TAXATION

DATE: DECEMBER 2012

TIME: 2HOURS

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

QUESTION ONE (30 MARKS)

- a) Briefly explain the rationale behind the 'benefit theory' of taxation. (5 Marks)
- b) Giving appropriate examples, distinguish between customs duty and exercise duty. (5 Marks)
- c) Mr. Kamau is a married person. He and his wife had the following income for the year ended 2006.
 - i) Mr. Kamau: Salary Ksh. 170,000 p.a (PAYE 20,000)
Dividends 32,000 (Withholding tax sh. 4,000)
Free company car (1500 c.c)
 - ii) Mrs. Kamau – sh. 10,000 pm (PAYE shs. 2500)
 - iii) She also runs a small business. Its net income from the business was sh. 60,000 during the year.

Required:

- a) Compute the tax payable by Mr. Kamau for the year ended 31st December, 2005 (10 Marks)
- b) Based on the impact and the incidence of tax burden, tax can be classified as direct or indirect tax. Give and explain merits of indirect taxes over direct taxes. (10 Marks)

QUESTION TWO (20 MARKS)

- a) Explain the meaning of the term “Residence” when applied to a company under Kenya income tax laws. (5 Marks)
- b) Bidii limited makes its accounts to 31st December of each year and has prepared the following profit and loss account for 2005.

	Ksh		Ksh.
General administration expenses	40,000	Gross profit b/d	200,000
.....	12,000	Bad debts previously	
Depreciation	10,000	Written off	1,000
Subscriptions	2,000	Dividends (Gross)	5,000
Directors fees and expenses	5,000	Possible interest	6,000
Patents written off	2,500	Gains sale of	
Preliminary expenses	3,000	Plant and machinery	10,000
Retirement benefits	50,000	Tax refund	20,000
Rents, rate and insurances	30,000		
Legal and accountancy	41,500		
Interest in lieu of dividends	5,000		
Net profit before taxation	30,000		
	<u>242,000</u>		<u> </u>
242,000	<u> </u>		<u> </u>

Additional information:

- i) Analysis of repairs and rewards revels the following expenses:

	Ksh.
- Redecoration of an existing business	3,000
- Renovating new building	5,000
- Partition and carpeting officer	<u>4,000</u>

- ii) Subscriptions:

- Natinal chamber of commerce and industry	1000
- N.E.P Refugee fund	<u>1000</u>

iii) Bad debts was incurred in respect of previous employee of the company who cannot now be traced.

iv) Preliminary expenses:

- Legal fees on issue of share on stock exchange amounted to shs. 2000 and the rest was spent for payment for stationery before commencement of business.

v) Retirement benefits

- N.S.SF. Contribution	5,000
- Registered pension scheme for senior management	40,000
- Legal fee- plot acquisition	
- Gift to retiring staff	5,000
	<u>50,000</u>

vi) Legal and accountancy

- Staff services agreement	2,000
- Audit fees	30,000
- Legal fees for lease	4,000
- Legal fees plot acquisitions	5,500
	<u>41,500</u>

vii) Dividends were from subsidiary company where Bidii company controls 60% of the shares

viii) Capital allowances agreed at Sh. 30,000

Required:

Calculate corporation tax liability for 2005. (15 Marks)

QUESTION THREE (20 MARKS)

Explain the following:

- i) Regressive taxes (5 Marks)
- ii) Appeals to income tax tribunal (5 Marks)
- iii) Instalments tax (5 Marks)
- iv) Taxable capacity (5 Marks)

QUESTION FOUR (20 MARKS)

Chaka tea limited has presented the following information relating to its affairs for the year ended 2006, December.

Income	Ksh. (000)
Sales of tea	60,000
Sale of surplus furniture	600
Gear and bonus from KTDA	<u>6,000</u>
	<u>66,600</u>
Expenses	
Purchases	28,000
Wages to staff (Net of PAYE)	19,700
NSSF	2,800
PAYE	1,100
Electricity	420
Staff uniform	110
Repairs and renewals	205
Insurance	96
Legal expenses	72
Motor vehicle expenses	160
Cost of construction of gabions	128
Depreciation	5,250
Tax penalty	41
Efficiency tracking computers	184
Dividends	<u>200</u>
	<u>57,466</u>

Additional Information

- i) The company incurred the following capital expenditure for which it claims deductions under second schedule. All items were in use with effect from 1st January, 2006.

	Shs.
Agriculture land for planting tea bushes	4,000
Irrigation plant	1800
Nursery shed for transplanting seedlings	840
Labour lines for tea pickers	2400
Land for Tea factory	2500
Factory building (Including office block costing (sh. 1000,000))	15,000
Dehydrating Plant(new)	3,600
Conveyor belt fixed to the dehydrating plant	1200
Grading machine (new) and fixed	2800

Movable weighting scale	200
Mobile fork lift (20 tons)	600
Lorries for transporting Tea to factory	5,400
4 Toyota cars for managers	3200
Furniture and Fittings	1000

- ii) The future sold was part of the furniture bought under (i) above.
- iii) Repairs and renewals include purchase of loose tools worth 35,000.
- iv) Legal expenses include an amount 40,000 paid to a lawyer to facilitate “passing” of the tea during tasting.
- v) Motor vehicle expenses include sh. 92,000 incurred on petrol for saloon cars.
- vi) Gabions were constructed by waterways on contract to prevent flooding of the tea plantation during rainy season.
- vii) Tax penalties resulted from breach of VAT regulations.

Required:

Calculate the relevant capital deductions. (20 Marks)

QUESTION FIVE (20 MARKS)

Explain five objectives of raising taxes and explain how they are achieved by the government. (20 Marks)