

**MERU UNIVERSITY OF SCIENCE AND TECHNOLOGY**

**P.O. Box 972-60200 – Meru-Kenya.**

**Tel: 020-2069349, 061-2309217. 064-30320 Cell phone: +254 712524293, +254 789151411**

**Fax: 064-30321**

**Website:** [**www.mucst.ac.ke**](http://www.mucst.ac.ke) **Email:** [**info@mucst.ac.ke**](mailto:info@mucst.ac.ke)

**University Examinations 2014/2015**

SECOND YEAR, SECOND SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF COMMERCE, BACHELOR OF SCIENCE IN BUSINESS INFORMATION TECHNOLOGY

**HBC 2211: INTRODUCTION TO TAXATION**

**DATE: DECEMBER 2014 TIME: 2 HOURS**

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

**QUESTION ONE**

1. Name and briefly explain four major principles of a good tax system (10 marks)
2. Mr. James Kivuna worked for Maua limited, a company in the horticultural sector, as the general manager on a five year contract commencing 1 January 2011. His contractual salary per annum was sh. 800,000. The contract provided for compensation in case of contract termination before its expiry of sh. 3,000,000. The contract was terminated on 1 January 2013 and he received the compensation on that date. On 31 January 2013, he secured employment with Charter Bank Limited. The following information is relevant for his year of income ended 31 December 2013.
3. His basic salary was sh. 90,000 per month (PAYE sh. 12,000)
4. He was entitled to reimbursement of medical expenses incurred on self and family subject to a maximum of 10% of basic pay. He spent sh. 135,000 on medical costs for the year. The medical scheme covers senior managers only.
5. He obtained a mortgage for Maendeleo Finance Ltd. on 1 July 2005 for sh. 3,500,000 at an interest rate of 10% per annum to purchase a residential house. The house was furnished by his employer at a cost of sh. 60,000. An alarm system was also installed in the house by the employer at a cost of sh. 10,000.
6. He was sponsored for a seminar on banking by the employer at sh. 120,000. 5% of this cost was for private entertainment.
7. He received 1,000 ordinary shares of Charter Bank Ltd. as a performance bonus on 31 December 2013. Each of these shares had a par value of sh.10 but at the time of their issue to Mr. Kivuna, their market price was sh. 8 each.
8. On 1 September 2013, he obtained a sh. 600,000 loan from his employer. The interest payable on this loan was at the rate of 2% per annum.
9. He contributes 5% of his basic pay to a registered pension scheme while the employer contributes an equal amount for him
10. He employed a night watchman on 1 August 2013 at a salary of sh. 3,000 per month Charter Bank Ltd. pay half the salary
11. He received a gross dividend of sh. 8,000 from Akiba Ltd. on 31 October 2013
12. During the year, he paid a total of sh. 35,000 as fees for his children studying in public
13. He won a defamation case against a local newspaper and was awarded sh. 300,000. The amount was paid on 15 November 2013
14. His other income (or losses) for the year ended 31 December 2013 included:

Net income from rent sh. 1,000,000

Profit from retail business sh. 320,000

Loss from farming business sh. 600,000

**Required:**

1. Compute the fringe benefit tax payable. Assume a prescribed interest rate of 12% per annum (5 marks)
2. Compute the total taxable income for Mr. Kivuna for the year ended 31 December 2013. (10 marks)
3. Compute the tax payable on the taxable income in (ii) above (5 marks)

**QUESTION TWO**

The Gitoro food processing industries ltd commenced business on 1 January 2012 and the following are fixed assets of the company which it acquired prior to the commencement of the business:

sh.

Conveyer and sorter (installed in the buildings) 3,120,000

Packing machine 2,625,000

Milling machine 2,580,000

Crashing machine 2,760,000

Forklifts 1,290,000

Farm tractors 5,850,000

Lorry 1,800,000

Saloon car 585,000

Delivery van 1,350,000

Furniture, fittings and partitions 408,000

Land at cost 15,000,000

The building in use was constructed at a cost of sh. 10,200,000 but its value after construction was estimated at sh. 12,600,000 by a professional valuer. In the year, the company bought the following assets:

sh.

Tractor 2,655,000

Lorry 3,900,000

Toyota-Land-Cruiser 2,025,000

Furniture 210,000

Partitions 408,000

Land 4,680,000

3 computers 450,000

The following assets were disposed off in the year:

Forklift 360,000

Saloon car 690,000

Requires:

1. Compute the capital allowances for the company for the years 2012 and 2013

(18 marks)

1. Comment on any information not used in (a) ab0ve (2 marks)

**Total: (20 marks)**

**QUESTION THREE**

Omondi, Onyango and Kimani are partners operating a wholesale shop in Kisumu. They share profits and losses in the ration 2:2:1 respectively. During the year ended 31 December 2013, the partners reported a loss of sh. 10,325,000 after deducting the following:

sh.

Interest on capital Omondi 406,000

Onyango 406,000

Kimani 609,000

Motor vehicle running expenses 532,000

Office expenses 420,000

Goodwill 700,000

Repairs and maintenance 168,000

Loss on investment 55,000

Postage and telephone 297,000

Water and electricity 238,000

Salaries and wages 1,246,000

Donations and charitable institutions 525,000

Subscriptions to KNCCI (Trade Association) 224,000

Bad debts expense 605,500

Rent, rates and licenses 280,000

Professional fees 760,000

Depreciation 960,000

Purchase of lorry 2,329,250

Salary to partners Omondi 700,000

Onyango 735,000

Kimani 1,008,000

Additional information:

1. Office expenses included cost of office cabinet of sh. 192,500
2. The partnership received dividends amounting to sh. 462,000 (net) from various stocks held in different companies. This was excluded from the above computation
3. The partnership received sh. 910,000 being insurance recovery for stocks which were destroyed by fire in 2004. This was omitted in arriving at the reported loss above.
4. Motor vehicle running expenses included sh. 21,000 per month related to personal travel by the partners
5. Provision for bad and doubtful debts account for the year was as follows:

sh. sh.

Bad debts written off 430,500 General brought forward 577,500

Specific carried forward 336,000 Specific brought forward 266,000

General carried forward 682,500 Profit and loss account 605,500

1,449,000 1,449,000

1. Omondi had taken goods worth sh. 122,500 for his own use. This was not recorded in the books of account
2. Included in repairs and maintenance is sh. 140,000 paid for office partitions during the year
3. The partners had other incomes as follows:

Omondi Onyango Kimani

sh. sh. sh

Rent (net) 200,000 - 350,000

Farming income - 750,000 (745,000)

Interest (net) 191,250 81,600 -\_\_\_\_\_\_\_

391,230 831,600 (495,000)

1. Capital allowances have been agreed with the commissioner at sh. 906,000

Required:

1. The taxable profit/(loss) for the partnership business for the year 2013 (8 marks)
2. Show the allocation of the profit/(loss) among the partners (6 marks)
3. Compute tax payable by each partner (6 marks)

**QUESTION FOUR**

Mutuma Kamu operates an electronics shop along Luthuli Avenue in Nairobi. He undertook the following transactions for the month of March 2013.

1 March 2013 Purchased 10 cameras for a total of sh. 500,000

4 March 2013 Purchased flashbulbs for a total of sh. 200,000

4 March 2013 Purchased 5 slide projectors for a total of sh. 1,000,000

5 March 2013 Sold 5 cameras each at 25% above cost price

6 March 2013 Purchased 200 wrist-watches at sh. 1,500 each

8 March 2013 Sold 2 slide projectors for a total of sh. 500,000

9 March 2013 Sold flashbulbs that cost sh. 100,000 for sh. 150,000

12 March 2013 Purchased 50 stop watches for total of sh. 50,000

15 March 2013 Purchased 100 alarm clock at a total value of sh. 80,000

18 March 2013 Sold the remaining 5 cameras each at 25% above cost price

20 March 2013 Sold 3 slide projectors for a total of sh. 750,000

22 March 2013 Sold 100 wrist-watches at sh. 2,000 per watch

25 March 2013 sold 70 alarm clocks each at 30% above cost

27 March 2013 Sold 500 stop watches for a total of sh. 75,000

Required:

1. VAT account (18 marks)
2. State the dates when VAT is available (2 marks)

**QUESTION FIVE**

1. Distinguish between the tax treatment of rent income on resident and non-resident individuals (4 marks)
2. With reference to the Customs and Excise Act (Cap. 472), write short notes on the following:
3. Import declaration form (4 marks)
4. Clean report of findings (2 marks)
5. Four categories of goods liable to forfeiture to the customs department

(4 marks)

1. Four privileged persons or institutions exempted from pre-shipment inspection of imports (4 marks)
2. Identify and briefly explain the operation of any two instruments of fiscal policy

(4 marks)