



MASENO UNIVERSITY

UNIVERSITY EXAMINATIONS 2017/2018

THIRD YEAR FIRST SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF BUSINESS ADMINISTRATION WITH INFORMATION TECHNOLOGY

MAIN CAMPUS

ABA 301: PRINCIPLES OF TAXATION

Date: 19th February, 2018

Time: 3.30 - 6.30pm

INSTRUCTIONS:

- Answer Question ONE and any other THREE
- Show all the workings clearly



VALUE OF TAXABLE BENEFITS PRESCRIBED BY CIT
Taxable Employment Benefits - Year 2015/2016

RATES OF TAX (Including wife's employment, self employment and professional income rates of tax). Year of income 2015.

Monthly taxable pay (shillings)		Annual taxable pay (shillings)		Rates of tax % in each shilling
1	- 10,164	1	- 121,968	10%
10,165	- 19,740	121,969	- 236,880	15%
19,741	- 29,316	236,881	- 351,792	20%
29,317	- 38,892	351,793	- 466,704	25%
Excess over	- 38,892	Excess over	- 466,704	30%

Personal relief Shs. 1,162 per month (Shs. 13,944 per annum)

Prescribed benefit rates of motor vehicles provided by employer

			Monthly rates (Sh.)	Annual rates (Sh.)
Capital allowances:		(i) Saloon, Hatch Backs and Estates		
Wear and tear allowances		Upto - 1200 cc	3,600	43,200
Class I 37.5%		1201 - 1500 cc	4,200	50,400
Class II 30%		1501 - 1750 cc	5,800	69,600
Class III 25%		1751 - 2000 cc	7,200	86,400
Class IV 12.5%		2001 - 3000 cc	8,600	103,200
Industrial building allowance:		Over - 3000 cc	14,400	172,800
Industrial buildings 2.5%		(ii) Pick-ups, Panel Van (Unconverted)		
Hotels 4.0%		Upto 1750 cc	3,600	43,200
Farm works allowance	33.3%	Over 1750 cc	4,200	50,400
Investment deduction allowance:		(iii) Land	7,200	86,400
2014 - 100%		Rovers/Cruisers		
2015 - 100%		OR 2% of the initial capital cost of the vehicle for each month, whichever is higher.		
2016 - 100%				
Shipping investment deduction				
40%				
Mining allowance:				
Year 1 40%				
Year 2 - 7 10%				

QUESTION ONE

(a) Lynette Ochieng works with Kaudo Ltd. and has provided you with the following information for the year ended 31 December 2016.

1. Pension from previous employment Sh.20,000 per month.
2. Salary Sh.120,000 per month (PAYE Shs.42,000 per month)
3. Lynette Ochieng and her husband (Mr. Ochieng) own a company whose taxable income was agreed at Sh.500,000 after charging husband's salary of Sh.250,000 per month (PAYE Sh.60,000 per month).
4. Kaudo Ltd. Provided a company house to Lynette Ochieng in Millimani, where rent of similar houses was Sh.20,000 per month.
5. Lynette Ochieng works over time and her overtime income averages Sh.10,000 per month.
6. Lynette Ochieng enjoyed medical benefit of Sh.160,000 during the year. She is a senior manager and the company has medical cover for all its employees.
7. She obtained free consumables from the company as a Christmas gift worth Sh.30,000 during the year
8. Lynette Ochieng owns rental property at Migosi Estate and receives Sh.50,000 as rental income per month. During the year, she incurred Sh.60,000 in renovations, repairs and painting before letting the property. She had obtained a mortgage loan from Housing Finance Company amounting to Sh.3,000,000. She paid Sh.900,000 during the year of which Sh.500,000 was principal.
9. Lynette Ochieng owns 20% of the shares of Kaudo Ltd.

Required

- i) The taxable income for Mr and Mrs Ochieng for the year of income 2016. (10 Marks)
- ii) Tax payable on the income computed above. (10 Marks)
- iii) Lynette Ochieng did not fill her self assessment return form for 2016. State the penalties due, if any. (5 Marks)

QUESTION TWO

Kisumu Enterprises Ltd. is a distributor of Bamburi Cement in Kisumu County. The profit and loss account for the year ended 31 December 2016 is as follows:

	Sh.		Sh.
Purchases	1,000,000	Sales	3,655,000
Staff wages	850,000	Discounts	355,000

Rent and rates	92,500	Provision for bad and	35,500
Distribution and office	445,500	doubtful debts	65,500
expenses	256,000	Profit on sale of assets	170,000
Traveling	85,600	Insurance recovery	
Repairs and maintenance	156,000		
Discount	122,100		
Bad debts	25,000		
Subscription	24,000		
Bank charges & interest	35,500		
Loss on sale of assets	95,000		
Legal fees	41,500		
Audit fees	126,000		
Depreciation	<u>917,300</u>		
Gross profit	<u>4,282,000</u>		<u>4,282,000</u>

Additional information:

- 10% of rent and rates relate to directors.
- Distribution and office expenses includes the following expenses:

Directors personal expenses	Sh.	31,550
Contribution to a sports club – employees use it		30,000
Donations		22,000
Loss on staff canteen		12,000
- Repairs and maintenance include extension to an office block

		40,000
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- Subscriptions are to trade associates.
- Travelling expenses include business trip to Japan to attend a trade exhibition.

		56,000
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- Legal charges include the following:

Acquisition of copyrights		25,000
Debt collection		21,000
Renewal of lease for 99 years		18,000
Fines and defence of legal suits		11,000
Employment contract		5,000

7. Insurance recovery is in connection with stolen stock in the previous year.

8. Bad debts provision is reduced in general provision.

Required:

- (a) Prepare a tax computation. (12 marks)
(b) Compute the tax liability and indicate the due date. (3 marks)

QUESTION THREE

- (a) Explain the term employer and what it include for PAYE purposes. (3marks)
(b) Rachel is an accountant with Aus Enterprises Ltd. Details of employment income for the year ended 31 December 2015 are as follows:

Salary per month – Sh.250,000 (PAYE of Sh.84,600 per month).

She contributes 5% of her monthly salary to the company's pension scheme which is registered with the Commissioner of Income Tax.

She is provided with a company house.

The financial controller has informed you that Aus Enterprises Ltd. has leased the house which Rachel is occupying at a monthly rent of Sh.50,000.

Required:

- (i) Compute chargeable income for Rachel in 2015. (5 marks)
(ii) Compute Rachel's 2015 tax liability. (7 marks)

QUESTION FOUR

Elchico Co. Ltd. a manufacturer, purchases raw materials at Sh.1,000,000. The company then incurs conversion costs which are estimated at 40% of material cost. The profit mark-up is 20% of total cost. The completed product is sold to Pramukh Wholesalers who then incur conversion costs of 50% on cost. The wholesalers mark-up is 10% on cost. The wholesaler sells the product to a retailer, who has no conversion costs but sells at a profit of 30%.

Required:

Assuming VAT is charged at 15% on all products, compute the total VAT payable.

(15 marks)

QUESTION FIVE

Discuss the objectives of raising taxes

(9 marks)

Explain the concept of elasticity with respect to Direct Tax and Indirect Tax giving an example in each case.

(6 marks)

QUESTION SIX

Dan, Ben and Ken are former school mates who were doing business together.

The business is not registered but they registered themselves as equals in it. They keep proper books of account and have been able to provide the following profit and loss account for the year ended 31 December 2015.

Profit and Loss Account

	Sh.		Sh.
Establishment 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
Light and heating	40,000	Gross income from farming	340,000
General farm expenses	294,000	Lottery winnings	800,000
Repair of premises	40,000	Dividend (Gross)	120,000
Depreciation	300,000		
Interest on partner's capital:			
Dan	80,000		
Ken	120,000		
Salary to Ben	160,000		
Commission to partners:			
Dan	96,000		
Ben	96,000		
Ken	96,000		
Bad debts	240,000		
Gifts, present and charity	40,000		
Donation to child welfare	200,000		
Interest on loan taken to pay			

Income tax	20,000	
Legal charges	120,000	
Net profit	<u>398,000</u>	
	<u>3,520,000</u>	<u>3,520,000</u>

Additional information:

1. Capital allowances have been agreed as follows: Wear and Tear allowances sh.180,000; Farm works deductions 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 the loan.
3. Legal charges include Sh.40,000 paid to finish a case in the customs department.
4. In 2005, the partners brought forward losses amounting to Sh.800,000 from this business.

Required:

- (a) Compute taxable income derived from the partnership (15 marks)
- (b) Show allocation among partners. (5 marks)