

CHUKA



UNIVERSITY

UNIVERSITY EXAMINATIONS

EXAMINATION FOR THE AWARD OF DEGREE OF BACHELOR OF EDUCATION

BUST 422: BUSINESS TAXATION

STREAMS: BED Y4S2

TIME: 2 HOURS

DAY/DATE: THURSDAY 12/04/2018

8.30 A.M. – 10.30 A.M.

INSTRUCTIONS:

- **Attempt question one and any other two questions.**

Question one

- (a) Briefly describe what 'tax' is and outline its features. (3 marks)
- (b) Outline three alternative purposes for which a building may be in use in order to qualify for capital deductions as an industrial building. (3 marks)
- (c) Mark Koech works for Bora Ltd. During the year ended 31st December 2017, he received the following incomes and emoluments.
1. Basic salary of sh. 160,000 per month (PAYE Sh. 42,000 per month)
 2. He was provided with a 2,200 cc Land Rover which had cost the company Sh. 4.6 million in the year 2012.
 3. In the month of December 2017, he received a sitting allowance of Sh. 280,000
 4. He is a member of the registered retirement benefits scheme of which he makes monthly contributions of Sh. 30,000
 5. He was housed by the company in a rented house. The house had a market rental value of Sh. 64,000 per month and he paid a nominal rent of Sh. 25,000 per month.
 6. The company paid annually electricity, water and telephone bills averaging to Sh. 18,000, Sh. 12,500 and Sh. 16,000 respectively.

7. During the year, the company paid school fees for his son amounting to Sh. 280,000. This amount was disallowed for tax purposes on Bora Ltd.
8. In December 2017, Mark Koech received an entertainment allowance of Sh. 120,000. Half of this amount was spent on entertaining customers.
9. Mark Koech has a life insurance policy and contributes a monthly premium of Sh. 15,000 per month.

Required:

- (i) Taxable income for Mark Koech for the year ended 31 December 2017. (12 marks)
- (ii) Tax liability (if any) Mark Koech's for the taxable income. (4 marks)
- (d) Describe the characteristics of excisable goods and services. (4 marks)
- (e) Distinguish between value added tax and turnover tax. (2 marks)

Question Two

- (a) Outline any six (6) expenses that are specifically allowable deductions by the Income Tax Act. (6 marks)
- (b) Ruiru Ltd. Processes meat for sale in the local market. The company started operations on 1st January 2017 after constructing a factory building at a cost of Sh. 18 million. Other assets acquired by the company on commencement of its operations included:

Assets	Cost Sh '000'
Land	2,000
Computer software	300
Photocopier machines	450
Processing machine	4,000
Saloon car	2,400
Office curtains	100
Packaging machines	800
Office furniture	240
Computers hardware	400
Duplicating machines	300
2-lorries (each 5 tonnes)	2,000

Additional information:

1. On 1st March 2017, the company acquired a tuktuk for Sh. 350,000 for use in delivery of customer orders within the factory environs.
2. The company constructed labour quarters for Sh. 720,000 which were occupied from 1 July 2017.
3. The following assets were disposed of during the year ended 31st December 2017.

Assets	Date of disposal	Disposal proceeds Sh. '000'
Computers	5-May-2017	120
Saloon Car	10-Aug-2017	1,800

Required:

The capital allowances due to Ruiru Ltd. for the year ended 31st December 2017. (14 marks)

Question Three

- (a) Explain how the government uses taxation to encourage savings in Kenya. (4 marks)
- (b) Margaret and Grace are in a partnership operating a hardware shop as 'Maga' Enterprises and sharing profit and losses equally. The following is the income statement of the partnership business for the year ended 31 December 2017.

	Sh. '000'	Sh. '000'
Sales		9,280
Less Expenses:		
Cost of goods sold	4,000	
Purchase of computers	160	
Salaries and wages	360	
General expenses	720	
Legal expenses	940	
Repairs and maintenance	25	
Interest on Partners capital	450	
Margaret's mortgage interest	65	
Donations to Tennis club	35	
Commission to Grace	<u>21</u>	<u>(6,776)</u>
Net Profit		<u>2,504</u>
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Additional information:

1. Salaries to partners and interest on partners' capital is to be shared according to the profit and loss sharing ratio.
2. Salaries and wages include salaries to employees of Sh. 160,000 while the balance was paid to.
3. Legal expenses include: Sh'000'

Drafting a partnership deed	42
Negotiating a bank loan	30
Defending the business against breach of contract	38

Required:

- (i) Adjusted taxable profit and loss for the partnership for the year ended 31 December 2017.
- (ii) A schedule showing distribution of partners' taxable income for the year ended 31 December 2017

Question Four

- (a) Outline any four deductions allowed against employment income. (4 marks)
- (b) Excel Enterprises, a registered trader incurred input tax of Sh. 5,000 on purchase of his stock. Out of this stock, he sold as follows: Goods taxable at 16% worth Sh. 20,000, zero rate goods worth Sh. 20,000, and exempt goods worth Sh. 20,000.

Required:

Input Tax claimable: (6 marks)

- (c) The management of Trend Limited has presented the following income statement for the year ended 31 December 2017:

Trend Limited		
Income Statement for the Year ended 31 December 2017		
Gross profit		5,292,000
Other incomes:		
Discount received	28,000	
Refund of VAT	12,000	
Gain on sale of motor vehicle	<u>14,000</u>	<u>54,000</u>
		5,346,000
Expenditure:		
Salaries and wages	800,000	
NIHF contribution	30,000	
Subscription to a trade association	50,000	
Bad debts written off	60,000	
General expenses	80,000	
Depreciation	25,000	
Legal expenses	40,000	
Insurance premiums	124,000	
Rent expense	66,000	
Electricity expense	34,000	
Purchase of furniture	<u>26,000</u>	<u>1,335,000</u>
		4,011,000
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Additional information:

- 1. Capital allowances were agreed with the Revenue Authority at Sh. 75,000
- 2. Included in bad debts is a loan of Sh. 15,000 due from a former employee of the company who was dismissed in October 2017
- 3. Legal expenses include Sh. 20,000 incurred in defending a manager against a traffic offence.

4. Insurance premiums include Sh. 24,000 paid to the National Hospital Insurance Fund (NHIF) as a penalty for late submission of contribution.
5. The company paid stamp duty of Sh. 6,000 relating to a piece of land purchased in August 2017. This payment is included in the rent expense for the year ended 31 December 2017.

Required:

- (i) Compute the adjusted taxable profit or loss of Trend Limited for the year ended 31 December 2017. (12 marks)
 - (ii) Calculate the tax liability (if any) of the company for the year ended 31 December 2017. (2 marks)
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