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**University Examinations 2015/2016**

THIRD YEAR FIRST SEMESTER EXAMINATION FOR THE DEGREE

OF

 BACHELOR OF COMMERCE

**BFC 3326: ADVANCED TAXATION**

**DATE: APRIL 2016 TIME: 2 HOURS**

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

**QUESTION ONE (30 MARKS)**

1. Explain the qualifying expenditure for mining investment allowance (10 marks)
2. KK Ltd are manufactured of belts, hats and shoes. The company has given the following information to be used in the self assessment return for the year of income 2014.

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Sh.** |  | **Sh.** |
| Stock (opening balance) | 1,500,000 | Gross sales  | 30,000,000 |
| Purchases | 12,000,000 | Stock (closing) | 1,900,000 |
| Salaries and wages  | 6,500,000 | Profit on exchange  | 120,000 |
| Electricity and water  | 654,000 | Profit on sales of shares | 77,000 |
| Insurance  | 346,000 | Dividends  | 100,000 |
| Rent, rates and taxes  | 1,230,000 | Interest  | 150,000 |
| Vehicle running expenses  | 3,670,000 |  |  |
| Traveling expenses  | 429,500 | Net loss for the year  | 2,128,500 |
| NSSF | 190,500 |  |  |
| Bank charges and interest  | 139,000 |  |  |
| Donations  | 41,000 |  |  |
| Sales returns  | 4,000,000 |  |  |
| Postage and telephone  | 126,000 |  |  |
| Bad debts  | 354,000 |  |  |
| Depreciation  | 916,000 |  |  |
| General expenses  | 1,300,000 |  |  |
| Repairs and Renewals  | 980,000 |  |  |
| Legal Expenses  | 99,500 |  |  |
|  | 34,475,500 |  | 34,475,500 |
| Net loss brought down  | 2,128,500 |  | 9,000,000 |
| Directors fees  | 6,000,000 |  | 2,628,500 |
| Proposed dividends | 3,500,000 |  |  |
|  | 11,628,500 |  | 11,628,500 |

The following information is further obtained from the company.

1. Legal expenses were analyzed as follows:

|  |  |
| --- | --- |
|  | Sh. |
| Renewal of factory lease for 10 years  | 12,500 |
| Notices to defaulting debtors  | 37,000 |
| Letters of authentication for overdraft  | 25,000 |
| Purchases of director’s private house  | 25,000 |
|  | 99,500 |

1. Bad debts analysis:

**BAD DEBTS ACCOUNT**

|  |  |  |  |
| --- | --- | --- | --- |
| Bad debts  | 154,000 | Balances brought forward: |  |
| Balances carried forward: |  |  | 1,000,000 |
| Specific provisions  | 4,500,000 |  | 354,000 |
| General provisions  |  |  |  |
|  |  |  |  |

1. The profits on exchange was from an amount payable on 1 February 2014 to a foreign creditor of 10,000 US dollar.
2. Rent, rates and taxes include Sh.421,000 paid to Kenya Revenue Authority as installment tax for the year 2014.
3. The interest of Sh.150,000 was earned from deposits held in Swiss account.
4. Donations analysis:

|  |  |
| --- | --- |
| Annual fees paid to association of leather goods manufacturers | 12,000 |
| National Chamber of Commerce and Industry  | 9,000 |
| Home and Salvation Army | 20,000 |
|  |  |

1. Included in general expenses was the cost of renovations to the old factory costing Sh.1,000,000 done on 1 July 2014.
2. The company’s writers down values of assets as at 31 December 2013 were as shown below:

|  |  |
| --- | --- |
|  | Sh. |
| Class I | 12,000 |
| Class II | 9,000 |
| Class III | 20,000 |
| Class IV | 41,000 |

Required:

1. Taxable income of J.T. Ltd for the year ended 31 December 2014. (15 marks)
2. Indicate when the installment tax is payable (5 marks)

**QUESTION TWO (20 MARKS)**

1. Identify and explain instances when a capital statement may be required: (4 marks)
2. Mr. J.J. has not been keeping proper books of account since the inception of the business in 2002. The following balances relate to JJ’s business for the period 2009 to 2014.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|  | Sh. | Sh. | Sh. | Sh. | Sh. | Sh. |
| Leasehold land | 15,000,000 | 15,000,000 | 15,000,000 | 15,000,000 | 15,000,000 | 15,000,000 |
| Lorries (cost) | 5,000,000 | 7,000,000 | 4,000,000 | 3,000,000 | 6,000,000 | 6,000,000 |
| Saloon cars (cost) | 2,000,000 | 2,000,000 | 2,000,000 | 2,000,000 | 2,000,000 | 2,000,000 |
| Swimming pool | 800,000 | 800,000 | 800,000 | 800,000 | 800,000 | 800,000 |
| Stocks  | 1,200,000 | 2,300,000 | 2,000,000 | 1,800,000 | 1,800,000 | 1,400,000 |
| Computers  | 500,000 | 500,000 | 500,000 | 400,000 | 400,000 | 400,000 |
| Bank account  | 400,000 | 300,000 | 20,000 | 20,000 | 20,000 | 20,000 |
| Business deposit Account  | 2,200,000 | 2,200,000 | 2,200,000 | 2,200,000 | 2,200,000 | 2,200,000 |
| Treasury bills  | 3,000,000 | 3,000,000 | 3,000,000 | 4,500,000 | 4,000,000 | 3,000,000 |
| Investment debtors  | 200,000 | 150,000 | 250,000 | 300,000 | 280,000 | 520,000 |
| House mortgage  | - | - | - | 7,000,000 | 7,000,000 | 7,000,000 |
| Crediros  | 340,000 | - | - | 400,000 | - | - |
| Bank overdraft  | 20,000 | 60,000 | 80,000 | 120,000 | 160,000 | 200,000 |
| Interest on bank deposit  | 10,000 | 5,000 | 8,000 | 7,000 | 6,000 | 3,000 |
| Loss on sale of investment  | 150,000 | 120,000 | - | - | 200,000 | 160,000 |
| Gain on foreign exchange  | 50,000 | 60,000 | 40,000 | 30,000 | 20,000 | 10,000 |

Required:

1. Estimate the taxable income for each of the three years 2010 to 2014, 2007. (15 marks)
2. Itemize and briefly explain other information which may be required in assessing the tax liability of a taxpayer. (5 marks)

**QUESTION THREE (20 MARKS)**

Explain the following terms as used in Customs and Excise Act CAP 472:

1. Drawback
2. Remission
3. Refund
4. Rebate
5. Sufferance wharf (20 marks)

**QUESTION FOUR (20 MARKS)**

Jackson and Ireri are partners running a glass making profit and losses in the year ended 31 December 2014

|  |  |
| --- | --- |
|  | Shs. |
| Income: |  |
| Sales | 4,882,000 |
| Sales of old plant (Sh.30,750 and lorry sh. 150,000) | 180,750 |
| Refund of VAT  | 21,250 |
| Post office saving bank interest  | 5,750 |
| Dividend (net) |  |
|  |  |
| Expenses  |  |
| Purchases  | 1,491,500 |
| Wages  | 408,750 |
| National Hospital Insurance (NHIF) | 35,500 |
| Rent  | 620,500 |
| Lorry maintenance expense  | 1,165,750 |
| Salaries to partners  | 1,200,000 |
| Ireri’s household expenses  | 86,000 |
| Repairs and maintenance (plant) | 233,750 |
| Advertising  | 75,000 |
| Insurance premiums  | 156,750 |
| Interest on loan  | 125,000 |
| Subscription – glass makers Association  | 25,000 |
| Donations to bursary fund  | 8,000 |
| Legal expense  | 89,000 |
| Bad debts  | 298,000 |
| Water and electricity  | 86,250 |
| Depreciation: furniture and fittings  | 111,500 |
|  Plant | 61,750 |
| Total expenses  | 8,000 |
|  |  |
| Net loss for the year  |  |

**Additional information:**

1. Glass worth sh.65,000 was used by Jackson and Ireri for their private purposes. This amount should be apportioned to the partners in their profit sharing ratio.
2. Lorry maintenance expense includes cost of new lorry shs.750,000 and depreciation charge for the year of Sh.162, 500.
3. Annual rent for Jackson’s house was shs. 300,000. This was paid for by the business.
4. During the year ended 31 December 2014, new plant was acquired for sh. 200,000. This has been included in the repairs and maintenance costs plant.
5. Jackson’s personal car insurance was paid for the business. It amounted to sh. 90,000.
6. Interest on loan and the legal expenses relate to Ireri’s mortgage loan
7. Bad debts were made up of:

Specific provision Sh. 50,000

General provisions Sh. 61,500

1. Write down where as at 31 December 2013 were as follows:

Furniture and fittings Sh. 49, 500

Motor vehicles Sh. 107, 000

Plant Sh. 9, 000

1. Ireri and Jackson received salaries of Sh. 800, 000 and shs. 400, 000 respectively.

**Required:**

1. The adjusted profit or loss for tax purposes for the year ended 31 December 2014. (10 marks)
2. Division of profit (or loss) between the partners (6 marks)
3. Tax payable for each partner for the year ended 31 December 2014. (4 marks)

**QUESTION FIVE (20 MARKS)**

APA Insurance Company Limited is registered in Kenya to carry out life and general insurance business. From its general ledger and other records for the year ended 31 December 2014, you have been able to extract the following:

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Life business**  | **General business**  | **Total**  |
|  | **Sh.**  | **Sh.**  | **Sh.**  |
| Insurance premises received  | 360,000,000 | 740,000,000 | 1,1000,000,000 |
| Interest on fixed deposits (net) | 119,000,000 | 63,000,000 | 182,000,000 |
| Dividends received (net) | 26,000,000 | 8,000,000 | 34,000,000 |
| Interest on loans to policy holders  | 3,000,000 | - | 3,000,000 |
| Interest paid on maturity of policies  | 27,000,000 | - | 27,000,000 |
| Premiums returned  | 8,000,000 | 17,000,000 | 25,000,000 |
| Interest on premiums returned  | 700,000 | - | 700,000 |
| Premiums paid to reinsurance company  | 36,000,000 | 74,000,000 | 110,000,000 |
| Commission received from reinsurance company  | 3,600,000 | 7,400,000 | 11,000,000 |
| Agency expenses  | 36,000,000 | 88,800,000 | 124,800,000 |
| Management expenses  | 15,160,000 | 74,000,000 | 89,160,000 |
| Depreciation of fixed assets  | 22,000,000 | 33,000,000 | 55,000,000 |
| Traveling expenses  | 6,000,000 | 11,000,000 | 17,000,000 |
| Postage and telephone expenses  | 3,500,000 | 6,200,000 | 9,700,000 |
| Advertising expenses  | 2,200,000 | 3,400,000 | 5,600,000 |
| Bad debts (specific)  | 1,300,000 | 800,000 | 2,100,000 |
| Rent income – Bima Apartments  | 9,000,000 | - | 9,000,000 |
| Rent expenses (office)  | 10,000,000 | 14,000,000 | 24,000,000 |

**Additional information:**

1. Reserves for unexpired risks as determined by Mr. Wafula mengo, a registered actuary, were as follows:

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Life business**  | **General business**  | **Total**  |
|  | **Sh.**  | **Sh.**  | **Sh.**  |
| 1 January 2014  | 29,000,000 | 89,000,000 | 118,000,000 |
| 31 December 2014 | 17,000,000 | 91,000,000 | 108,000,000 |

1. Claims

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Life business**  | **General business**  | **Total**  |
|  | **Sh.**  | **Sh.**  | **Sh.**  |
| Claims outstanding – 1 January 2004 | 23,000,000 | 16,000,000 | 39,000,000 |
| Claim paid during the year  | 39,000,000 | 113,000,000 | 152,000,000 |
| Claims outstanding – 31 December 2014 | 32,000,000 | 9,000,000 | 41,000,000 |

1. Wear and tear allowances for the year ended 31 December 2014, have been agreed with the commissioner for Income Tax at Sh 26, million for the general business respectively.

**Required:**

1. Taxable income of APA Insurance Company Ltd, for the year ended 31 December 2014. (14 marks)
2. Tax payable (if any) on the taxable income computed in (i) above (6 marks)