



THE MOMBASA POLYTECHNIC UNIVERSITY COLLEGE

Faculty of Business & Social Studies

DEPARTMENT OF BUSINESS STUDIES

BACHELOR OF BUSINESS ADMINISTRATION

HCA 2123: TAXATION I

END OF SEMESTER EXAMS

SERIES: APRIL/MAY 2010.

TIME: 2 HOURS

INSTRUCTIONS TO CANDIDATES

1. The paper consists of **FOUR** questions.
 2. Answer Question **1** and any other **TWO** questions.
 3. Show all your workings.
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Q.1 (a) Discuss the concept of justice in taxation. (10 marks)

- (b) Mr. Bahati is a farmer in Kwale District. For the years 2004, 2005 and 2006 his profits before capital allowances were 800,000, 700,000 and 600,000 respectively.

He erected a farmhouse in January 2004 for sh.360,000 and incurred other expenditure as follows:-

January 2005	Cattle dip	sh.90,000
June 2005	Labour quarters	sh.120,000
September 2005	Irrigation system	sh.150,000
October 2005	Milking machinery	sh.99,000

In 2006 he had the following transactions.

1st January Sold all assets acquired in the previous two years except land and acquired a farm for expansion at a cost of sh.200,000

Required:

Compute taxable profits for the years 2004, 2005 and 2006. (12 marks)

- (c) Write brief notes on the following:
- (i) Arm's length income
 - (ii) Hobby farming
 - (iii) Trading receipt
 - (iv) Permanent establishment
- (8 marks)

Q.2 (a) Explain the four basic principles of a good tax system. (8 marks)

- (b) Mr. Otiende is a professional accountant. During the year 2006, he had the following transactions:

	Shs.
Professional fees received	2,000,000
Purchased personal car	600,000
Purchased professional books	400,000
Computer – office	120,000
Rent paid – office	100,000
Salary from part time job	400,000
Contribution to “Nyumba Ya Wazee”	20,000
ICPAK Subscription	3,000
Professional management expenses	50,000

50% of the car usage was for business.

Required:

Compute professional taxable income. (12 marks)

Q.3 (a) Outline some of the reasons that lead to non tax – compliance in your country and their possible remedies. (5 marks)

- (b) Wanyama and Wanyonyi have been trading in partnership sharing profit and losses in the proportion of three fifths and two fifths. They have prepared accounts for 2006 as follows:

		Sh.
Interest on capital -	Wanyama	20,000
	Wanyonyi	10,000
Goodwill w/o		4,000
Bad debts		20,000
Audit, insurance & legal exp.		20,000
Motor expenses		30,000
Depreciation		60,000
Special expenses		8,000
Withholding tax on dividends		3,000
Salaries – Wanyonyi		60,000
Loss on sale of investments		10,000

Repairs and renewals	6,000
Salaries and wages	100,000
Light, water and electricity	20,000
Net profit	<u>32,000</u>
	<u>403,000</u>
Gross	380,000
Dividend	17,000
Sub-letting	<u>6,000</u>
	<u>403,000</u>

NOTES

1.	Bad debts	
	Bad debts written off	10,000
	Provision c/d - General	80,000
	- Specific	<u>22,000</u>
		<u>102,000</u>
		<u>112,000</u>
	Balance b/d - General	60,000
	Specific	<u>30,000</u>
		90,000
	Profit and Loss	20,000
	Debts recovered	<u>2,000</u>
		<u>112,000</u>
2.	Audit, insurance and legal:	
	Audit exp.	10,000
	Partner's insurance	2,000
	Legal fees-debt collection	500
	Partnership deed	<u>7,500</u>
		<u>20,000</u>
3.	Special expenses:	
	Breach of tax law	4,000
	Redundancy pay	3,000
	Christmas gift to partners wives.	<u>1,000</u>
		8,000
4.	Repairs and renewals	
	Office partitions	2,000
	Office carpet	1,500

Replacement of adding machine	1,000
General repairs	<u>1,500</u>
	<u>6,000</u>

Required:

Calculate the adjusted profit for tax purposes for each partner. (15 marks)

Q.4 (a) Explain any **FOUR** factors that determine taxable capacity of a country. (8 marks)

(b) Mr. Mundumuluma is an employee of Wykem Limited. His basic pay per annum is sh.960,000. He is entitled to the following benefits for the month of October, 2007:

- (i) Housing of which he pays a rent equivalent to 2% of his basic pay (market rent sh.20,000 per month).
- (ii) Life insurance premiums of 12,000 per month.
- (iii) Contribution to a pension scheme of 20,000 p.m. He contributes similar amount of his own to the scheme.
- (iv) He secured a mortgage of which he is paying annual interest of 120,000 per month.
- (v) Other taxable allowances sh.8,000 per month.

Required:

Calculate tax payable in the month of October, 2007. (12 marks)

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

Year of income 2005.

Monthly taxable pay (Shillings)		Annual taxable pay (Shillings)		Rate of tax % in each Shillings	
1	- 10164	1	- 121968	10%	
10165	- 19740	121969	- 236880	15%	
19741	- 29316	236881	- 351792	20%	
29317	- 38892	351793	- 466704	26%	
Excess over	38892	Excess over	466704	30%	

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

Prescribed benefit rates of motor vehicles provided by employer.

Monthly Rates (Shs.)	Annual Rates (Shs.)
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Capital allowances:

Wear and tear allowances:

Class I 37.5%

Class II 30% Saloons, Hatch Backs and

Class III 25% Estates

Class IV 12.5%

Industrial allowances:		Upto	-	1200 cc	3,600	43,200	
	Industrial buildings	2.5%	1201	-	1500 cc	4,200	50,400
	Hotel	4.0%	1501	-	1750 cc	5,800	69,600
Farm works allowances	33.3%	1751	-	2000 cc	7,200	86,400	
Investment deduction allowance:		2001	-	3000 cc	8,600	103,200	
	2003	-	70%				
	2004	-	100%				
	2005	-	100%				