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MAASAI MARA UNIVERSITY

**REGULAR UNIVERSITY EXAMINATIONS**

**2016/2017 ACADEMIC YEAR**

**THIRD YEAR FIRST SEMESTER**

**SCHOOL OF BUSINESS AND ECONOMICS**

**BACHELOR OF BUSINESS MANAGEMENT**

**COURSE CODE: BBM 303**

**COURSE TITLE: TAXATION I**

**DATE: 25TH APRIL 2017 TIME: 8.30AM-10.30AM**

**INSTRUCTIONS TO CANDIDATES**

* **Answer question ONE (compulsory) and any other THREE**
* **Question one carries 25 marks**
* **All other questions carry 15 marks**

This paper consists of 8 printed pages. Please turn over

**QUESTION ONE**

1. List and explain any three deductions that may be available against gains or profits from employment. **(3 marks)**
2. Distinguish between tax evasion and tax avoidance. **(3marks)**
3. What are some of the factors a country should take into account in designing its tax policy? Is it possible to accommodate all the factors? **(6marks)**
4. Write brief notes on the following:
   * 1. Specified sources of income.
     2. Income subject to tax at source for resident persons
     3. Wife's employment income. **(3marks)**
5. Mr. Shoma has two offers for employment in two engineering firms. The details of the two offers are as follows:

**Firm A Firm B**

***Shs. Shs.***

Basic pay per month 45,000 41,000

Benefits: Housing

Car 1600cc (cost) 600,000 600,000

Pension scheme which is registered by commissioner of income tax both employer and employee contribute 5% of the basic salary towards the pension scheme.

**Required:**

What offer would you recommend to Mr. Shoma? Explain the reasons for your recommendation **(10marks)**

**QUESTION TWO**

Mr. Matata has approached you with a view to obtaining help in determining his taxable income for 2005. He has supplied the following information:

1. Business Income

He runs a small garage that generates taxable income of Sh.60, 000. In 2004, he had a tax loss of Sh.40, 000 from this business.

2. Wife’s Income

His wife was employed by Mafuta Ltd. as the Finance Director. Her salary was sh.52, 000 p.m. Additional benefits include:

Company car 1800 cc.

House at New Muthaiga (market value of rent Sh.20, 000 per month)

Staff gifts of oil products worth Sh.1000 p.m

3. Capital Gains

In the course of the year, the Matata’s sold one plot they owned in Nairobi for Sh.1, 200,000. This represented a gain of Sh.600, 000 which they used to take a holiday to Mombasa.

4. Investment Income

|  |  |  |
| --- | --- | --- |
|  | Withholding Tax  **Sh.** | Net  **Sh.** |
| Dividends:  Kenya Breweries Ltd  HFCK Ltd.  CMC Ltd.  Interest:  Kenya Commercial Bank Savings Account  HFCK – Housing Development Bond  Post Office Savings Bank 15% 2010 Treasury Bonds. | 2,000  1,000  4,000  2,000  7,000  -  1,500 | 18,000  9,000  36,000  18,000  63,000  20,000  13,500 |

5. Employment Income – Mr. Matata

He was employed by Utajiri Limited as the General Manager – Sales. His salary was Sh.40, 000 per month and a bonus of 2% on total sales revenue. He had a car of 2000cc which he used to visit customers otherwise his wife would pick and drop him at the place of work each day using her official car.

6. Utajiri Limited insures all its sales against default from customers. The cost of the insurance was Sh.10, 000 which represents 0.001 percent of sales. The company also paid sh.20, 000 to cover the life of Matata and his household items.

7. PAYE of Sh.130, 000 was deducted from Matata’s pay but due to an oversight in the part of the Chief Accountant the tax was not paid to the Collector of Income tax. His wife’s PAYE was Sh.180, 000 in the year.

**Required:**

(i) Compute total income chargeable to tax and show the tax payable thereon. **(11 marks)**

(ii) Comment on any information not used for computing taxable income above. **(2 marks)**

(iii) Is Matata to blame for failure of the company to pay his PAYE? Explain. **(2 marks)**

**QUESTION THREE**

Timexa Limited provided the following details with respect to its fixed assets for the year of income 2005.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Building Sh.** | Class I  **Sh.** | Class II  **Sh.** | Class III  **Sh.** | Class IV  **Sh.** |
|  | 1,400,000 | 460,000 | 610,000 | 800,000 | 6,200,000 |

2. The industrial building had been constructed sometimes back in 2000 at a cost of Sh.1, 600,000. Fixed machines were Sh.2, 000,000. Due to an oversight, no investment deduction was claimed.

3. During the year the following assets were purchased:

- Patents Sh.200, 000

- Computers Sh.390, 000

- Stamping machine Sh.800, 000

- Land Sh.530, 000

4. A car for use by the directors was involved in an accident and written off. No recoveries were made.

5. In December, all computers were sold as one lot for Sh.1, 220,000.

6. Assume 60% as the rate of investment deductions. For year 2000.

**Required:**

* + - 1. Capital allowances for Timexa Limited for year of Income 2005 **(10marks)**
      2. State five alternative purposes for which a building may be in use in order to qualify for capital deductions as an industrial building. **(5marks)**

**QUESTION FOUR**

The following purchases and sales were made by Pepo Limited (VAT No.00012Y) during the first two weeks of January 2006. Prices shown are inclusive of VAT at the standard rate of 16 percent.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  |  | **P U R C H A S E S** | | **S A L E S** | |
|  |  | **Unit** | **Price per Unit**  **Sh.** | Unit | **Price per Unit**  **Sh.** |
| January | 1  2  5  7  10  12 | 100  75  -  175 | 1,400  1,600 | 10  20  50  20  50  150 | 1,800  1,800  1,800  1,800  2,000 |

There were no opening stocks at the beginning of the month.

The physical inventory confirmed that there were 25 units in stock as at 31 January 2006.

**Required:**

(i) The VAT account for Pepo Limited **(8marks)**

(ii) What are the requirements with respect to any sales made by Pepo Limited? **(5 marks)**

(iii)Specify when and how VAT computed under (i) is payable  **(2 marks)**

**QUESTION FIVE**

You have been invited by a group of students to discuss the matters listed below:

In each of the cases provide explanatory notes and computations for use in your discussions with students.

(i) A manager who is on full-time employment where he draws sh.80, 000 per month. He is housed by the employer in a rented house where rent payable to the landlord is Sh.720, 000 per annum. **(4 marks)**

(ii) The manager makes an annual contribution of Sh.84, 000 to a registered pension fund**. (3 marks)**

(iii) The manager is provided with a motor car whose purchase cost was Sh.1, 200,000**. (2 marks)**

(iv) A high school boy aged 15 years inherits Sh.300, 000 from his grandfather and wins Sh.100, 000 in the national lottery. **(3 marks)**

(v) A retired civil servant on an annual pension of Sh.180, 000 per annum signed a service contract with effect from 1 January 2005. The contract was for three years at an annual salary of Sh.440, 000. The contract was terminated by the employer on 31 December 2005. The employee was paid compensation amounting to Sh.560, 000. **(3marks)**

APPENDIX 1

**RATES OF TAX** (Including wife’s employment, self employment and professional income rates of tax).

YEAR OF INCOME 2005.

**Taxable Employment Benefits - Year 2005**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **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% |  |  |  |  |  |  |  |
| **Farm works allowance** | | 33.3% |  | Upto |  | 1750 cc |  | 3,600 | 43,200 |
| **Investment deduction allowance:** | | |  | Over |  | 1750 cc |  | 4,200 | 50,400 |
| 2003 - | | 70% | (iii) | Land Rovers/Cruisers | | |  | 7,200 | 86,400 |
| 2004 - | | 100% |  | OR 2% of the initial capital cost of the vehicle for each month, whichever is higher. | | | | | |
| 2005 - | | 100% |  |  |  |  |  |  |  |
| **Shipping investment deduction 40%** | | |  |  |  |  |  |  |  |
| **Mining allowance:** | | |  |  |  |  |  |  |  |
| Year 1 | | 40% |  |  |  |  |  |  |  |
| Year 2 – 7 | | 10% |  |  |  |  |  |  |  |

**Commissioner’s prescribed benefit rates**

**Services**  **Monthly rates Annual rates**

**Sh. Sh.**

(i) Electricity (Communal or from a generator) 1,500 18,000

(ii) Water (Communal or from a borehole) 500 6,000

(iii) Provision of furniture (1% of cost to employer)

If hired, the cost of hire should be brought to charge

(iv) Telephone (Landline and mobile phones) 30% of bills

**Agricultural employees: Reduced rates of benefits**

(i) Water 200 2,400

(ii) Electricity 900 10,800

**Low interest rate employment benefit:**

The benefit is the difference between the interest charged by the employer and the prescribed rate of interest.

**Other benefits:**

Other benefits, for example servants, security, staff meals etc are taxable at the higher of fair market value and actual cost to employer.

**The current VAT rate is 16%**