

**SCHOOL OF BUSINESS AND ECONOMICS****DEPARTMENT OF COMMERCE****FINAL EXAM: JANUARY SEMESTER 2019****UNIT: TAXATION 11****CODE: ACC 415A**

INSTRUCTIONS:**TIME: 2.5 HOURS****1 ANSWER QUESTION ONE AND ANY OTHER TWO QUESTIONS****2. SHOW ALL YOUR WORKINGS****QUESTION ONE.**

Mr. Morris is employed by an International Company, Its head office is in South Africa but has a branch in Nairobi. The following information relates to Mr. Morris's employment for the year ended 31 December 2018 (All amounts are stated in Kenya Shillings (Kshs))

1. His basic pay commencing 2 Feb 2018 was Sh.380,000 per month
2. The Company pays for the education of his Children Sh. 500,000 p.a
3. On 6 June the company rented for him a house whose fair rental value is 80,000 p.a. Mr Morris pays sh. 42,000 as monthly rent.
4. He is provided with free air ticket up to a limit of sh.120,000 to his place of choice and family members.
5. Commencing 1 July, he received a monthly entertainment allowance of Ksh.56,000 from the employer which he spent on visiting local tourist sites.
6. He is provided with a motor car of 2500 cc that costed the company sh.3500,000. A comprehensive insurance cover for this motor car for an annual premium of Ksh.80,000.
7. On 30 December he received a cheque of Ksh.150,000 from the employer for being the best employee for the year ended 31 December 2018.
8. Further the company has provided him with the following domestic servants
 - Watchman sh. 6500 per month

- House help sh. 8000 per month
 - Gardener sh.15000 per month
9. The house is fully furnished with the cost of furniture estimated to be 4000,000. Free water and electricity.
10. Telephone bills that amounted to sh.46,000 p.a were paid by the company.
11. He is also provided with medical benefit of sh. 1200,000 p.a
12. He contributes 5% of his basic pay to a registered pension scheme and the company contributes 10%.He pays a life insurance premium of sh. 20,000 every month.

Business income

Mr. Morris, runs a business that deals with repairs of computers and has provided you with the following information for the year ended 31 December 2018:

PROFIT AND LOSS ACCOUNT

	Sh.		Sh.
Rent for premises		Gross profit	1,272,000
– owned by Mr. Morris	180,000	Interest income	48,000
Establishment expenses	600,000	Dividends	80,000
Printing and stationery	135,000	Farming income	226,600
Interest expense	46,000	Profit on sale of shares	533,000
Electricity	40,000	Lottery winnings	733,300
Farm expenses	210,000	Other income	53,300
Repairs to premises	30,000		
Depreciation	196,000		
Salary to Mr. Morris	380,000		
Drawings	200,000		
Donations to children's home	166,000		
Legal expenses	125,000		
Interest on loan	29,000		
Bad debts	180,000		
Staff wages	144,000		
Net profit	<u>285,200</u>		
	<u>2,946,200</u>		<u>2,946,200</u>

Additional information:

1. Capital allowances have been agreed as follows:

	Sh.
Wear and tear allowances	120,000
Industrial building allowances	80,000

2. Legal expenses include Sh.50,000 paid with regard to pursuing a dispute with the VAT department.

1. Establishment expenses include Sh.400,000 incurred in acquiring furniture and equipment for the business before commencement of operations.

Investment Income

Mr. Morris has earned the following Incomes in the course of the year.

Dividends:

Kenya Breweries Ltd	180,000
HFCK Ltd.	90,000
CMC Ltd.	36,000

Interest:

Kenya Commercial Bank Savings Account	208,000
HFCK – Housing Development Bond	63,000
Post Office Savings Bank	200,000
15% 2010 Treasury Bonds.	135,000

Rental income

Mr. Morris has an Apartment in South B Nairobi and he has furnished KRA with the following information

	Sh.	Sh.
Gross rent		300,000
Less:		
Loan repayment	150,000	
Interest on loan	125,000	
Fencing	30,000	
Caretaker wages	55,000	
Insurance, rent and rates	25,000	
Replaced broken doors	<u>85,000</u>	<u>470,000</u>
Loss to be C/F		<u>170,000</u>

Required

For the year ended 31st December 2018, show the taxable income and tax liability of Mr Morris.
(30 marks)

QUESTION TWO

M Ltd. prepares its accounts to 31 December each year. The trading and profit and loss account for the year ended 31 December 2018 is as follows:

	Sh.	Sh.
Gross profit		21,400,000
Less:		
Directors' fees	3,637,500	
Depreciation	5,250,000	
General office expenses	1,950,000	
Salaries and wages	2,365,500	
Donations	412,500	
Dividends paid	2,250,000	
Repairs and maintenance	2,162,500	
Interest expenses	3,050,000	<u>(21,050,000)</u>
Net profit transferred to reserves		<u>322,000</u>

On 1 January 2018, M Ltd. purchased its current factory from K Ltd., a registered contractor, for Sh.240 million. K Ltd. availed the following details concerning the cost of construction of the factory:

	Sh.
Acquisition of land	12,880,000
Demolition and clearing of old factory from the site	8,640,000
Labour quarters built on site	28,800,000
Factory building	89,280,000
Stone wall around the factory	14,400,000
Bank interest during period of construction	<u>11,520,000</u>
	165,520,000

The factory building houses administrative offices worth sh.23, 040,000 and a raw materials and finished goods store worth Sh.8, 640,000. M Limited installed machinery worth sh.120, 000,000 on 3 January 2018 and started manufacturing drugs for human and animal use

The following assets were acquired in the course of the year in addition to those mentioned above:

Date	Asset	Cost
		Sh.
10 January 2018	New computers	1,120,000
11 January 2018	Furniture	360,000
11 January 2018	Photocopier	240,000
11 January 2018	Scanner	80,000
11 January 2018	Television set (colour)	20,000
15 January 2018	3 saloon cars (Sh.1.2 million each)	3,600,000
17 January 2018	2 lorries (4 tonnes at Sh.2 million each)	4,000,000

The following assets were disposed of during the year:

Date	Asset	Proceeds
		Sh.
5 February 2018	Machinery (original cost	
6 March 2018	sh.960,000)	640,000
7 March 2018	Saloon car (original cost	

Sh.920,000)	400,000
Furniture (original cost	
Sh.820,000)	360,000

The balances brought forward for capital allowances purposes as at 1 January 2018 were as follows:

Class I	Class II	Class III	Class IV
Sh.	Sh.	Sh.	Sh.
5,780,000	1,340,000	2,650,000	3,650,000

Required:

- (a) Capital allowances available to M. Ltd. in 2018. (20 marks)
- (b) The company's taxable profit (or loss) and tax payable (if any) (5 marks)

QUESTION THREE

Mr Morris is a practicing accountant working under the style and name of Morris and Associates. His firm is registered for Value Added Tax (VAT). During the month of September 2018, he undertook and completed the following assignments:

- 2 September - Tax consultancy work for ABC Ltd. his fees was sh.240,000 inclusive of VAT.
- 4 September - Audit for Rwandacell, a company based in Rwanda. His fees amounted to Sh.840,000 exclusive of VAT.
- 10 September - Management consultancy services for Kikwetu Ltd. He billed them for sh.360,000 inclusive of VAT.
- 15 September - His firm was appointed by XYZ Ltd. to undertake a review of the internal control systems of the company. His fees were Sh.1,200,000 exclusive of VAT.
- 17 September - The firm conducted the audit of Kikwetu Ltd. for the year ended 31

December 2017. Charges were Sh.480,000 inclusive of VAT.

- 18 September - The firm was appointed by Stima Ltd to conduct a survey on power consumption at a fee of Sh.2,400,000 (exclusive of VAT).
- 19 September - His firm audited the accounts of Miracle Ministries, a church where he serves as a volunteer auditor. He estimated that his fees would have been Sh.720,000 exclusive of VAT.
- 21 September - The firm bill Kikwetu Limited Sh.136,000 (inclusive of VAT) for debt collection services.
- 22 September - The firm undertook a financial consultancy assignment for Worldnet South Africa, a company based in South Africa. The fees were Sh.420,000 exclusive of VAT.
- 24 September - Conducted audit of Lengo Ltd. at a fee of Sh.180,000 inclusive of VAT.
- 26 September - Provided accountancy services to Rehema Children's Home on a volunteer basis. The estimated value of the services was Sh.90,000 inclusive of VAT.
- 30 September - Performed audit services for Ujamaa County Council. The fees earned were Sh.860,000 exclusive of VAT.

During the month of September 2018, the firm paid for the following services:

Electricity	Sh.42,500
Water	Sh.2,400
Rent	Sh.120,000
Garbage collection	Sh.36,000
Stationery	Sh.960,000
Computer repairs and maintenance	Sh. 240,000
Telephone	Sh.330,000

(where applicable, the above payments were VAT inclusive)

Required:

Prepare a VAT Account for Morris and Associates for the month of September 2018.

(25 marks)

QUESTION FOUR

Write short notes on the following

- a) Tax planning (5 marks)
- b) Tax investigation (5 marks)
- c) Tax evasion and tax avoidance (5 marks)
- d) Double taxation (5 marks)
- e) Tax administration in Kenya (5 marks)

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