

Name \_\_\_\_\_ Index No. \_\_\_\_\_

2804/305  
TAXATION  
November 2014  
Time: 3 hours

Candidate's Signature \_\_\_\_\_

Date \_\_\_\_\_



**THE KENYA NATIONAL EXAMINATIONS COUNCIL**

**DIPLOMA IN ACCOUNTANCY**

**TAXATION**

**3 hours**

**INSTRUCTIONS TO CANDIDATES**

- Write your name and index number in the spaces provided above.*
- Sign and write the date of examination in the spaces provided above.*
- Answer any FIVE questions in the spaces provided after each question.*
- ALL questions carry equal marks.*
- Do NOT remove any pages from this booklet.*
- Candidates should answer the questions in English.*

**For Examiner's Use Only**

Question	1	2	3	4	5	6	TOTAL SCORE
Candidate's Score							

**This paper consists of 20 printed pages.**

**Candidates should check the question paper to ascertain that all the pages are printed as indicated and that no questions are missing.**



2. (a) Outline four factors that may influence tax shifting in the country. (8 marks)

(b) Mr. Kalandi, a businessman, has not kept full records of accounts and has not paid any income tax since he began business. From available records and his explanation, the following information relating to his assets and liabilities were obtained.

	2009	2010	2011	2012	2013
	Ksh '000	Ksh '000	Ksh '000	Ksh '000	Ksh '000
<b>Assets</b>					
Building	1,200	1,200	1,200	1,200	1,200
Furniture and fittings	150	200	200	220	220
Freehold land	-	-	300	300	300
Motor vehicles	-	-	650	650	350
Inventories	100	100	120	150	200
Account Receivables	-	-	500	600	680
Bank	<u>      </u>	<u>      </u>	<u>120</u>	<u>100</u>	<u>100</u>
	<u>1450</u>	<u>1500</u>	<u>3090</u>	<u>3220</u>	<u>3050</u>
<b>Liabilities</b>					
Account payables	-	50	80	85	90
Loan	<u>      </u>	<u>      </u>	<u>30</u>	<u>30</u>	<u>18</u>
	<u>      </u>	<u>50</u>	<u>110</u>	<u>115</u>	<u>108</u>

- Estimated living expenses were Ksh 150,000 in 2009 and had been estimated to be increasing by sh 15,000 each year.
- A motor vehicle that cost Ksh 300,000 was sold for Ksh 350,000 in 2013.

Calculate the taxable income in arrears for each of the years. (12 marks)

3. Mr. Kazi is a registered quantity surveyor and owns Banga Associates, a Consulting firm that is managed by his wife. She draws a monthly salary of Ksh 48,000 (PAYE Ksh 9,600 per month). Mr. Kazi is a full-time employee of Lengo Ltd. During the year ended 31 December 2013 the company provided him with the following:

- Monthly salary of Ksh 82,000 (PAYE Ksh 21,000 per month)
- Provided with an accommodation in a fully furnished house, whose cost of furniture as on 1 January 2013 was sh 300,000. He paid a nominal rent of Ksh 18,000 per month toward house rent.
- Water and electricity; whose monthly bill was Ksh 2,600 and Ksh 6,500 respectively.
- Leave pay equal to 50% of one month's salary.
- Life insurance for his family of Ksh 120,000 per year.
- Pension contribution to a registered pension scheme of Ksh 5,000 per month. He contributed a similar amount to the same.

Benga Associates had made an assessed loss of Ksh 250,000 in the year of income 2012.

Mr. Kazi's other income are rental income whose rent account for the year ended 2013 was as follows:

	Ksh	Ksh
Gross rent		280,000
less: Care takers wages	52,000	
Rent and rates	28,000	
Mortgage repayment	135,000	
Re-painting	20,000	
Mortgage interest	<u>95,000</u>	<u>330,000</u>
Loss carried forward		<u>(50,000)</u>

Calculate:

- (i) Mr. Kazi's taxable income for the year of income 2013.
- (ii) Tax payable by Mr. Kazi for the year of income 2013.

(20 marks)

4. Allan, Ken and Martin are in a partnership sharing profits and losses in the ratio of 2:1:1 respectively. The following information relates to the partnership for the year ended 31 December 2013.

	Ksh
Net loss after charging the following expenses	(1,296,000)
Legal costs	90,000
Salaries and wages	360,000
Donations	67,200
Rent	216,000
Water and electricity	42,000
Stationery and postage	14,400
Repairs to business premises	78,000
Audit and accountancy	28,800
Motor vehicle expenses	108,000
Advertising	78,000
Depreciation	51,600
<b>Salaries to partners:</b>	
Allan -	288,000
Ken -	288,000
Martin -	432,000
<b>Drawings</b> - Martin	6,000
- Allan	14,400
<b>Interest on capital</b>	
Allan -	96,000
Ken -	96,000
Martin -	144,000
Stamp duty paid for Allan's plot	66,000

**Additional information;**

- Salaries and wages include Ksh 36,000 paid to Allan's son for clearing the business premises during school holidays.
- 40% of motor vehicle expenses are personal.
- Wear and tear allowance is agreed at Ksh 19,200 with the commissioner of domestic taxes.
- Rent comprises:

	Ksh
- Business premises	120,000
- Partners residence	96,000

- Legal costs include Ksh 18,000 paid as a tax penalty by the partnership.

6. Advertising comprises;

	Ksh
- Advertising campaign	33,600
- New bill board	6,000
- Launch of a new product	10,800
- End of year partners party	27,600

7. Bad debts include:

	Ksh
- General	12,000
- Specific	14,400
- Written off	9,600
- Ken's daughter	12,000

8. Other incomes included in the profit and loss account are:

	Ksh
- gain on sale of plot	15,600
- sub-letting rental income	26,400
- dividends from Bora Bank Ltd	22,800

- (i) Compute the partnership adjusted profit or loss for tax purposes. (15 marks)
- (ii) Show the allocation among the partners. (3 marks)
- (iii) Explain the tax treatment of income from partnership. (2 marks)

5. (a) Outline **four** duties of a VAT registered person.

(8 marks)

(b) The following details relate to the transactions of Mzalendo traders for the months of June to November 2013.

	Sales	Purchases
	(Ksh '000)	(Ksh '000)
June	2,640	1,800
July	3,240	2,160
August	2,400	2,040
September	1,080	1,800
October	720	480
November	3,120	2,400

The amounts above are stated inclusive of VAT at a rate of 16%.

Additional information:

1. All sales were made on credit basis with the cash due received in the month following the month of sale while all the purchases were on cash basis.
2. 15% of the purchases made in the month of September were returned to the supplier in the same month.
3. Included in the sales of October was Ksh 240,000 for which the debtor was declared bankrupt in November 2013.

Prepare a VAT account, showing VAT payable or refundable for the six months of 2013.  
(12 marks)

6. (a) Explain four ways through which the government collects tax revenue. (8 marks)
- (b) Mahiga Mining Ltd has been prospecting for diatomite in Kilifi since 2010. On 1<sup>st</sup> September 2012, mining commenced with the following expenditures being incurred.

	Ksh
Payment for mining rights to the government	6,768,000
Purchase of specialized drilling equipment	2,352,000
Transportation of the specialized drilling equipment to the site	540,000
Purchase of tools, spares and implements for mining	108,000
Construction of labour quarters at the site	1,440,000
Purchase of a 5-tonne lorry	2,304,000
Purchase of computers	432,000
Purchase of a Nissan pick-up	1,650,000
Purchase of a mercedes benz for the manager	2,500,000
Purchase of furniture and fittings	1,680,000
Construction of godown	3,216,000
Construction of administration block on site	936,000

Additional information:

- The company had incurred exploration expenses of Ksh 1,800,000 and administration expenses of Ksh 360,000 before 1<sup>st</sup> September 2012.
- In 2013, computers worth Ksh 140,000 were sold.

Calculate capital allowances claimed by the company for the years of income ended 31st December 2012 and 2013. (12 marks)



**RATES OF TAX (Including wife's employment, self-employment and professional income rates of tax).  
Year of income 2013.**

Monthly taxable pay (Sh.)		Annual taxable pay (Sh.)		Rate of tax % in each Sh.
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 Sh.1,162 per month (Sh.13,944 per annum)

**Prescribed benefit rates of motor vehicles provided by employer**

		Monthly rates (Sh.)	Annual rates (Sh.)
<b>Capital allowance:</b>			
<b>Wear and tear allowance:</b>			
Class I	37.5%		
Class II	30%		
Class III	25%		
Class IV	12.5%		
Software	20%		
<b>Industrial building allowance:</b>			
Up to 2009	2.5%		
From 1 January 2010	10%		
Hotels	10%		
Hostels/Education buildings	50%		
<b>Farm works allowance</b>	100%		
<b>Investment deduction allowance</b>	100%		
<b>Shipping investment deduction</b>	40%		
<b>Mining allowance:</b>			
Year 1	40%		
Years 2 - 7	10%		

(i) Saloons, Hatch Backs and Estates		Monthly rates (Sh.)	Annual rates (Sh.)
Up to	1200 cc	3,600	43,200
1201	1500 cc	4,200	50,400
1501	1750 cc	5,800	69,600
1751	2000 cc	7,200	86,400
2001	3000 cc	8,600	103,200
Over	3000 cc	14,400	172,800

  

(ii) Pick-ups, Panel Vans (unconverted)		Monthly rates (Sh.)	Annual rates (Sh.)
Up to	1750 cc	3,600	43,200
Over	1750 cc	4,200	50,400

  

(iii) Land Rovers/Cruisers		Monthly rates (Sh.)	Annual rates (Sh.)
		7,200	86,400

**Commissioner's prescribed benefit rates**

Services	Monthly rates Sh.	Annual rates Sh.
(i) Electricity (Communal or from a generator)	1,500	18,000
(ii) Water (Communal or from a borehole)	500	6,000
<b>Agriculture employees: Reduced rates of benefits</b>		
(i) Water	200	2,400
(ii) Electricity	900	10,800