PAN AFRICA CHRISTIAN UNIVERSITY

END OF SEMESTER EXAMINATION FOR THE DEGREE OF

MAY- AUGUST 2023

CAMPUS: ROYSAMBU

DEPARTMENT: BUSINESS

COURSE CODE: BCM 301 BUA 4123

COURSE TITLE: PRINCIPLES OF TAXATION

EXAM DATE:

TIME:

INSTRUCTIONS

- This examination script consists of **six (6)** questions.
- Answer question **ONE** and ANY other **four** Questions.
- Read all questions carefully before attempting.
- Write your **student number** on the answer booklet provided.

Question One **(Compulsory= 10 marks)**

a. Discuss **three** practical problems experienced by a Kenyan in complying with the VAT Act. Suggest ways in which these problems can be overcome. (6 marks)

b. The value for VAT of a supply is the consideration paid. Indicate the value for VAT under each of the following circumstances:

   i. The price of a radio cassette was Sh.17,500. A cash discount of 10% was given to the customer.

   ii. Ushonaji Architects provided a free service to a community-based project. The value of the service was Sh.125,000.

   iii. Dubai Kenya Ltd. imported electricals valued for Sh.2,000,000. A duty of 25% was charged by customs department.

   iv. Kupenda Company Ltd. sold furniture by instalments. The first instalment of Sh.5,000 was received immediately. The sales price of the furniture is Sh.20,000 and the remaining balance is to be paid in three equal monthly instalments. (4 marks)

Question Two (10 Marks)

Miss Nyuki's contract of employment for five years was terminated on 31 December 2005 after it had run for three years. Compensation for Sh.300,000 was paid. Her salary at the date of termination was Sh.90,000 per year. If the contract had run its full term, a total of Sh.180,000 would have been paid as salary for both 2006 and 2007.

Required:

a. Determine income assessable on Miss Nyuki (4 marks)

b. Assume that Nyakio's contract was not specific, calculate income is assessable on Miss Nyuki (3 marks)

c. Assume Miss Nyuki was a director in the company paying her compensation. Her shareholding in the company was 5% of the share capital. Explain the tax treatment in (i) and (ii) above. (3 marks)

Question Three (10 Marks)

"Governments in developing countries tend to overtax individuals in formal employment".

a. Using suitable illustrations, explain **three** reasons why Governments find it convenient to continually raise higher taxes on earnings from formal employment. (6 marks)

b. Discuss any **two** proposals on how the Government can be able to generate tax revenue from the informal sector (4 marks)

Question Four (10 Marks)

J. Selina is an accountant with Kamau Enterprises Ltd. Details of employment income for the year ended 31 December 2005 are as follows:

Salary per month – Sh.250,000 (PAYE of Sh.84,600 per month).

She contributes 5% of her monthly salary to the company's pension scheme which is registered with the Commissioner of Income Tax.

She is provided with a company house.

The financial controller has informed you that Kamau Enterprises Ltd. has leased the house which J. Selina is occupying at the monthly rent of Sh.50,000

Required:

(i) Compute chargeable income for J. Selina in 2005. (5 marks)

(ii) Compute J. Selina's 2005 tax liability. (5 marks)

Question Five **(10 Marks)**

Explain **five** major principles of a good tax system using suitable illustrations. (10 marks)

Question Six **(10 Marks)**

a. Define the term "tax avoidance." (2 marks)
b. Identify **two** ways in which an individual or institution could engage in the practice of "tax avoidance." (2 marks)
c. Explain the concept of the "incidence of a tax" clearly outlining its importance to policy makers (6 marks)

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

Taxable Employment Benefits -

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%