

2804/305

TAXATION

March/April 2025

Time: 3 hours



THE KENYA NATIONAL EXAMINATIONS COUNCIL

DIPLOMA IN ACCOUNTANCY

TAXATION

3 hours

INSTRUCTIONS TO CANDIDATES

*This paper consists of **SIX** questions.*

*Answer **FIVE** questions in the answer booklet provided.*

Maximum marks for each part of a question are as indicated.

Candidates should answer the questions in English.

This paper consists of 8 printed pages.

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

1. (a) Highlight four grounds upon which a tax payer may be deregistered from Value Added Tax (VAT). (8 marks)

- (b) Mateka Limited is in the business of soap making.
The following is the income statement of the business for the year ended 31 December 2024.

	Dr Ksh	Cr Ksh
Income		
Profit from sale of investment		890,000
Discounts received		240,000
Gain on sale of motor vehicle		380,000
Bad debts recovered - general		160,000
Gain on foreign exchange		118,000
Operating profit		1,650,000
		3,438,000
Less expenses		
Bad debts	350,000	
Depreciation	179,000	
Director's remuneration	450,000	
Miscellaneous expenses	280,000	
Interest expenses	480,000	1,739,000
Net profit		1,699,000

Additional information:

- (I) Miscellaneous expenses comprise of :

	Ksh
Conveyance fees on land	118,000
Repairs and maintenance	20,000
Legal fees for breach of contract	80,000
Discounts allowed	36,000
Salaries and wages	26,000
	280,000

- (II) Director's remuneration include:

	Ksh
- Director's end year party	160,000
- Compensation for wrongful termination	210,000

1. Adjusted Income
Profit for the year
2.6 of June

Less income from specified sources.

(III) Bad debts include:

	Ksh
- Embezzlement by a director	180,000
- Expired products	36,000

(IV) Interest expenses include:

	Ksh
- Cost of appeal against a tax assessment	190,000
- Legal feed for negotiating a bank loan	36,000

(V) Capital allowances were agreed at Ksh.280,000.

- Prepare a statement of adjusted taxable income for the year of income 2024.
- Determine the tax payable for the year of income 2024.

(12 marks)

2. (a) Highlight **four** reasons for undertaking back-duty investigations.

(8 marks)

- Kaka and Kiiko are in partnership business sharing profits and losses in the ratio 3:2 respectively.
Interest on capital is allowed at 10%.

The following is the income statement of the partnership for the year ended 31 December 2024.

	Ksh	Ksh
Gross profit		1,170,000
Interest drawings		150,000
Discounts received		135,000
		1,455,000
Less expenses		
Impairment loss	280,000	
Commission to Kaka	45,000	
Salaries and wages	360,000	
Discounts allowed	24,000	
Rent and rates	<u>36,000</u>	
VAT paid	220,000	
Legal fees	290,000	
Insurance and interest	310,000	1,625,000
Net loss		170,000

Additional information:

- (I) Salaries and wages include KSh.85,000 and KSh.60,000 paid to Kaka and Kiko, respectively. *(capital allowance - omitted)*
- (II) The partners capital contributions were Ksh.600,000 and Ksh.1,000,000 for Kaka and Kiko respectively.
- (III) 30% of rent and rates relate to Kaka's personal house. *- allowance*
- (IV) Legal fees include:

- less omitted allowable salary
- less non taxable income - profit
income from specified source

	Ksh
Renewal of a 25 year lease contract	70,000
Handling of tax dispute	35,000
Collection of outstanding customer's debts	48,000
Defending Kiko for breach of contract	47,000
Securing a bank loan	90,000
	290,000

Prepare a

- (i) Statement of adjusted partnership profit and loss for tax purposes.
- (ii) Schedule of allocation of taxable income to each of the partners. (12 marks)

3. (a) Explain four canons of taxation. (8 marks)

(b) The following information relates to the employment income of Mr. Tibu for the year of income 2024.

- Basic salary Ksh.2,000,000 per annum (PAYE Ksh.362,000 per annum)
- Medical allowance of Ksh.420,000 per annum. The company has a medical scheme for senior management only.
- The employer paid his son's school fees amounting to Ksh.240,000.
- He is provided with a car of 2000 cc. The cost of the car was Ksh.1,800,000.
- He contributed Ksh.32,000 per month to a registered pension scheme.
- He is housed by the employer. The market rent of a similar house is Ksh.40,000. The house was furnished at a cost of Ksh.120,000. *24*
- He is provided with a commuter allowance of Ksh.3,500 per month.

For the year of income 2024, determine Mr. Tibu's.

- (i) Taxable income.
- (ii) Tax payable. (12 marks)

4. (a) Highlight four costs that may qualify for mining deductions. (8 marks)

(b) Tim Limited is registered for Value Added Taxes (VAT) purposes.
The following transactions relate to the business for the month of October 2024:

- October 2 Paid telephone expenses for Ksh.22,000
3 Sold goods for Ksh.156,000 ✓
6 Exported goods to Malawi for Ksh.250,000
7 Bought printing materials for Ksh.32,000
9 Purchased goods for Ksh.320,000
10 Sold goods for Ksh.420,000
11 Returned goods worth Ksh.110,000 to a supplier
12 Incurred bad debts of Ksh.32,000
13 Issued a debit note of Ksh.24,000 to a customer
14 Paid legal fees Ksh.240,000

(i) Prepare a Value Added Tax (VAT) account. (10 marks)

(ii) State the date when the tax is payable. (2 marks)

5. (a) Highlight four sources of information for tax assessment. (8 marks)

value of property

(b) Jilipe has been in business for the last four years without maintaining proper books of account. The following information relates to his assets and liabilities for the last three years

	2022 Ksh '000'	2023 Ksh '000'	2024 Ksh '000'
Accounts payable - <i>liab</i>	135	142	156
Bank - <i>asset</i>	220	180	170
Investment in shares	430	480	520
Motor vehicles	390	430	120
Plant and machinery	1400	1500	1830
Accounts receivable - <i>asset</i>	680	720	700
Inventory - <i>asset</i>	225	220	240

*Total Assets = Total Liab
Net asset - net liab*

Net profit = Total Asset - Total Liab

Additional information:

- (i) The net assets in the year 2021 amounted to Ksh.5,450,000.
- (ii) Capital allowance for the year 2021 were agreed with the commissioner of Domestic Taxes at Ksh.260,000.
The allowances reduced by 12% per annum in the subsequent years.
- (iii) Jilipe's living expenses were estimated at Ksh.420,000 in the year 2021.
The expenses increased by 12 % per annum in subsequent years.
- (iv) During the year 2023, a motor vehicle with a net book value of Ksh.380,000 was sold for Ksh.260,000.

Determine the taxable income of Mr. Jilipe for each of the years 2022, 2023 and 2024.

(12 marks)

6. (a) Explain **four** measures that should be taken by the Kenya Revenue Authority to enhance revenue collection. (8 marks)
- (b) The following information relates to Tek Tek Farmers Cooperative Society.

	Ksh	Ksh
Operating income		
Dairy activity	1,300,000	
Crop activity	260,000	
Non operating income		
Dipping fees	16,000	
Dividend income	11,000	
Rent income	14,000	1,601,000
Expenses		
Bank charges	4,000	
Salaries and wages	120,000	
Mashujaa day celebrations	4,500	
Depreciation on buildings	70,000	
General expenses	96,000	
Donations	24,000	
Legal expenses	68,000	
Entertainment	1,600	(388,100)
Surplus		1,212,900

Net AS - Total Asset - Total
Liability

Additional information

(I) Donations comprised of:

	Ksh
Local church	7,000
ABC research on tomato disease	9,000
Co-operative journal	<u>8,000</u>
	<u>24,000</u>

(II) Salaries and wages comprise:

	Ksh
Staff salaries	72,000
NSSF contributions	9,000
Members retirement fund contributions	<u>39,000</u>
	<u>120,000</u>

(III) Entertainment expenses comprise:

	Ksh
Customers entertainment	1,100
Management committee	<u>500</u>
	<u>1,600</u>

(IV) Legal fees comprise:

	Ksh
Ushirika day celebrations	15,000
Collection of society's debts	29,000
Defending society in civil suit	24,000
	<u>68,000</u>

(V) Capital allowances were agreed with the commissioner for Domestic Taxes at Ksh.377,000.

Determine the:

- (i) Taxable income of the society for the year of income 2024.
- (ii) Tax payable.

(12 marks)

RATE OF TAX (including wife's employment, self employment and professional income rate of tax).
Year of income 2022.

Monthly taxable pay (Ksh)	Annual taxable pay (Ksh)	Rate of tax % in each (Ksh)
1 - 24,000	1 - 288,000	10%
24,001 - 32,333	288,001 - 388,000	25%
Excess over - 32,333	Excess over - 388,000	30%

Personal relief Ksh.2,400 per month (Ksh.28,800 per annum)

Investment allowance:	Rate of investment allowance	Residual value (per year on reducing balance)	Prescribed benefit rates of motor vehicles provided (i) Saloons, Hatch Backs and Estates
Capital expenditure incurred on:			Monthly rates (Sh) Annual rates (Sh)
(a) Buildings:	50% in the first year of use	25%	Upto 1200 cc 2,600 43,200
• Hotel building	50% in the first year of use	25%	1201 - 1500 cc 4,200 50,400
• Building used for manufacture	50% in the first year of use	25%	1501 - 1750 cc 5,800 69,600
• Hospital buildings	10% per year on reducing balance	25%	1751 - 2000 cc 7,200 86,400
• Petroleum or gas storage facilities	10% per year on reducing balance		2001 - 3000 cc 8,600 103,200
• Educational/hostels building			Over - 3000 cc 14,400 172,800
• Commercial building			
(b) Machinery:	50% in the first year of use	25%	(ii) Pick-ups, Panel
• Machinery used for manufacture	50% in the first year of use	25%	Vans (unconverted)
• Hospital equipment	50% in the first year of use	25%	Upto - 1750 cc 3,600 43,200
• Ships or aircraft	25% per year on reducing balance		Over - 1750 cc 4,200 50,400
• Motor vehicles and heavy earth moving equipment	25% per year on reducing balance		
• Computer software, calculators, copiers and duplicating machines	10% per year on reducing balance		
• Furniture and fittings	10% per year on reducing balance		
• Telecommunication equipment	25% per year on reducing balance	25%	
• Film equipment by a local producer operations under prospecting rights and exploration under mining rights	50% in the first year		
• Other machinery			
(c) Purchase/acquisition of rights to use fibre optic cable by telecommunication operations	10% per year on reducing balance		(iii) Land Rovers/ cruisers 7,200 86,400
(d) Farm works	50% in the first year of use		

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
Agricultural employees: Reduced rates of benefits		
(i) Water	200	2,400
(ii) Electricity	900	10,800

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