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KIRIRI WOMENS' UNIVERSITY OF SCIENCE AND TECHNOLOGY
UNIVERSITY EXAMINATIONS, 2024/2025 ACADEMIC YEAR
SECOND YEAR, FIRST SEMESTER EXAMINATION
FOR MASTER IN BUSINESS ADMINISTRATION (ACCOUNTING OPTION)

KAC 3206: TAXATION

Date: 6TH DECEMBER, 2024
Time: 11:00 AM – 2:00 PM

INSTRUCTIONS TO CANDIDATES
ANSWER QUESTION ONE (COMPULSORY) AND ANY OTHER THREE QUESTIONS

QUESTION ONE: COMPULSORY (40 MARKS)

a) ABC Traders Limited is a Kenyan-based company involved in the import, manufacture, and export of consumer electronics. The company supplies its products locally and internationally and also earns royalties from licensing proprietary manufacturing processes to affiliated companies in neighboring countries. ABC imports raw materials from Country X (customs duty applicable). It manufactures products in Kenya and exports a significant portion to Country Y, with the remainder sold locally. Licensing income is earned from Country Y affiliates. During the year of income, KRA conducted and audit and come up with the below observations;

- Misclassification of Expenses: ABC claimed deductions for certain marketing and entertainment expenses that KRA argues are non-deductible under the Income Tax Act. KRA disputes the depreciation rates applied to certain assets, reclassifying them as capital in nature.
- Export Sales: KRA disputes the zero-rated VAT status of some export sales, claiming insufficient proof of export.
- Import Transactions: Customs duty was allegedly underpaid due to misclassification of imported raw materials under a lower tariff code.
- Time of Supply: KRA claims that ABC incorrectly accounted for VAT on certain transactions, arguing that the company failed to declare VAT at the correct time of supply.
- Withholding Tax (WHT):ABC made royalty payments to Country Y without deducting WHT, arguing that the Double Taxation Agreement (DTA) with Country Y exempts these payments. KRA asserts that consulting fees paid to a non-resident supplier are subject to WHT.
- Administrative Issues: ABC claims that KRA imposed penalties and interest without giving the company sufficient opportunity to respond to the tax audit findings.

i. Differentiate between deductible and non-deductible expenses under the Income Tax Act. **(2 Marks)**

ii. Evaluate the treatment of ABC's marketing and entertainment expenses. **(2 Marks)**

iii. Assess the criteria for zero-rating exports under the VAT Act. **(2 Marks)**

iv. What evidence must ABC provide to substantiate the zero-rated status of its export sales? **(2 Marks)**

v. Discuss the implications of failing to meet the documentation requirements for zero-rated sales. **(2 Marks)**

vi. Discuss the determination of the time of supply for VAT purposes under Kenyan law. How does this affect ABC's VAT obligations? **(2 Marks)**

vii. Provide recommendations on how ABC can improve its compliance with time of supply rules to avoid future disputes. **(2 Marks)**

viii. Evaluate KRA's claim that royalty payments to Country Y are subject to WHT. How should the DTA provisions be interpreted in this context? **(2 Marks)**

ix. Analyze the tax treatment of consulting fees paid to a non-resident supplier. What steps can ABC take to mitigate WHT risks? **(2 Marks)**

x. Assess the procedural fairness of KRA's audit process under the Tax Procedures Act. What remedies are available to ABC for procedural non-compliance? **(2 Marks)**

b) Suntec Traders is a business registered for value added tax (VAT) purposes. The following transactions were recorded in the month of May 2024:

May 4: Purchases of goods (local)	4,640,000
May 6: Purchase of a computer	162,400
May 8: Return outwards	139,200
May 10: Legal fees	62,640
May 12: Imports Cost, Insurance and Freight (CIF)	300,000
May 14: Advance salaries and wages	580,000
May 16: Sales (local)	5,916,000
May 18: Export sales	600,000
May 20: Exempt sales	1,840,000
May 24: Printing and stationery	27,840
May 28: Electricity	53,940

Additional information:

1. During the month, import duty was at 20% on Cost, Insurance and Freight (CIF) basis.
2. A debtor of goods valued at Sh.121,800 was declared bankrupt on 20 May 2024.
3. Input tax relating to goods sold as exempt sales could not be directly identified and it was found appropriate to restrict deductible import tax.
4. Transactions are inclusive of VAT at the rate of 16% where applicable.

Required:

i. Output tax. **(3 Marks)**

ii. Deductible input tax **(5 Marks)**

iii. VAT payable or refundable. **(2 Marks)**

c) Argue FIVE cases against indirect taxes imposed in your country **(5 Marks)**

d) Name and explain any FIVE principles of taxation **(5 Marks)**

QUESTION TWO: (20 MARKS)

Smartboots Manufacturing Ltd. commenced manufacturing of leather shoes on 2 January 2024 after incurring the following expenditure:

Factory building	14,640,000
Processing machinery	4,712,000
Computers	384,000
Conveyor belts	1,240,000
Staff canteen	2,440,000
Delivery vans (two)	4,160,000
Sewerage system	1,280,000
Generator	400,000
Godown	2,600,000
Heating plant	1,400,000
Lorry	2,948,000
Sports pavilion	1,800,000
Loose tools	144,000

A corporation based in Kenya has made an investment in a commercial building and purchased industrial machinery as given below

Investment cost in commercial building: KSh 20 million

Industrial machinery cost: KSh 5 million

Assume the relevant rates are as per the Kenyan tax laws.

Required:

a) Compute the allowable capital allowances for the first year of use **(10 Marks)**

b) Discuss FIVE benefits of claiming capital allowance **(10 Marks)**

QUESTION THREE: (20 MARKS)

a) Solomon Chuchuh is employed as the Managing Director of Utamu Millers Ltd. During the year ended 31 December 2023, he presented the following information relating to his income:

Employment income: KSh 1,200,000

Rental income: KSh 600,000

Interest from a fixed deposit: KSh 100,000

Required:

Monthly taxable pay (Sh.)			Annual taxable pay (Sh.)			Rate of tax % in each Sh.
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 Sh.2,400 per month (Sh.28,800 per annum).

Use the above rates for year of income 2023.

Calculate the total taxable income and tax payable for the individual, assuming no other deductions. **(10 Marks)**

b) Describe FIVE types of tax assessments as per the tax procedure act 2015 **(10 Marks)**

QUESTION FOUR: (20 MARKS)

ABC Limited is a company based in Nairobi that operates in the manufacturing sector. The following are the details from their financial statements for the year ended December 31, 2023:

1. Gross Profit: KSh 40,000,000
2. Operating Expenses: KSh 8,000,000 (this includes allowable and disallowed expenses as outlined below)
3. Capital Allowances (as per tax laws): KSh 3,000,000
4. Interest on Loan: KSh 1,500,000 (loan used for business operations)
5. Legal Fees: KSh 500,000 (KSh 100,000 relates to fines and penalties)
6. Entertainment Expenses: KSh 700,000 (KSh 200,000 is personal in nature)
7. Donations: KSh 400,000 (donations made to an approved charitable organization)
8. Dividends Received: KSh 1,000,000 (from shares in another Kenyan company)
9. Bad Debts Written Off: KSh 600,000 (KSh 150,000 is not recoverable)
10. Net Profit Before Tax: KSh 30,000,000

Required:

a) Calculate ABC Limited's taxable income for the year 2023. **(8 Marks)**

b) Based on the taxable income computed, calculate the corporate income tax liability assuming the standard corporate tax rate is 30%. **(2 Marks)**

c) Describe the procedure for objection and appeals against a tax decision by a tax payer in Kenya as per the tax procedure act 2015 **(10 Marks)**

QUESTION FIVE: (20 MARKS)

a) Following the convergence of market economies, most business transactions currently take place through the digital market place. Most countries have come up with ways of taxing the digital economy, although some countries continue to struggle in taxation of this economy.

With reference to the above statement, suggest and discuss FIVE challenges faced by your country in taxing the digital economy. **(10 Marks)**

b) Assume that you have been requested to make a presentation in a tax seminar on measures that should be put in place to curb the problem of tax evasion in your country. Discuss FIVE measures of curbing tax evasion that you would include in your presentation. **(10 Marks)**

Rates on capital allowances

The rates of deduction are as follows:-

Capital Expenditure Incurred on:	Rate of Investment Allowance
(a) Buildings	
i) Hotel Buildings	50% in the first year of use
ii) Buildings used for manufacture	50% in the first year of use
iii)Hospital buildings	50% in the first year of use
iv)Petroleum or gas storage facilities	50% in the first year of use
v) Residual value to item (a)(i) to a(iv)	25% per year, on reducing balance
vi)Educational buildings including student hostels	10% per year, on reducing balance
vii) Commercial building	10% per year, on reducing balance
(b)Machinery	
i) Machinery used for manufacture	50% in the first year of use
ii) Hospital equipment	50% in the first year of use
iii) Ships or aircrafts	50% in the first year of use
iv)Residual value items (b)(i) to (b)(iii)	25% in the first year of use
v) Motor Vehicle and heavy earth moving equipment	25% in the first year of use
vi) Computer and peripheral computer hardware and software calculators, copiers and duplicating machines	25% in the first year of use
vii)Furniture and fittings	10% per year, reducing balance
viii)Telecommunications Equipment	10% per year, reducing balance
ix) Filming equipment by a local film producer licensed by the Cabinet Secretary responsible for filming	25% per year on reducing balance
x) Machinery used to undertake operations under a prospecting right	50% in the first year of use and 25% per year, on reducing balance
xi)Machinery used to undertake exploration operations under a mining right	50% in the first year of use and 25% per year on reducing balance
xii) Other machinery	10% per year, reducing balance
(c) Purchase or an acquisition of an indefeasible right to use fibre optic cable by a telecommunication operator	10% per year, on reducing balance
(d) Farmworks	50% in the first year of use and 25% per year, on reducing balance