



STRATHMORE UNIVERSITY BUSINESS SCHOOL
BACHELOR OF FINANCIAL SERVICES
END OF SEMESTER EXAMINATION
BSF 2103: TAXATION IN BUSINESS

DATE: Tuesday, 2nd August 2022

TIME: 2 Hours

INSTRUCTIONS:

ANSWER QUESTION ONE AND ANY OTHER TWO QUESTIONS

Marks allocated to each question are shown at the end of the question. Show ALL your workings.

Any assumptions made must be clearly and concisely stated.

RATES OF TAX (2022 tax rates) (Including wife's employment, self-employment and professional income rates of tax).

New KRA PAYE Rates Effective 1st January 2022

Monthly Taxable Pay	Annual Taxable Pay	Income Tax Rate
Up to KSh12,298	Up to KSh147,580	10%
KSh12,299 - KSh23,885	KSh147,581 - KSh286,623	15%
KSh23,886 - KSh35,472	KSh286,624 - KSh425,666	20%
KSh35,473 - KSh47,059	KSh425,667 - KSh564,709	25%
Above KSh47,059	Above KSh564,709	30%
Personal Relief: Ksh2,400 Per Month	Personal Relief: Ksh28,800 Per Year	

Prescribed benefit rates of motor vehicles provided by employer:

<i>CC Rating</i>	<i>Monthly (Kes)</i>	<i>Annual (Kes)</i>
Up-to 1200	3,600	43,200
1201-1500	4,200	50,400
1501-1750	5,800	69,600
1751-2000	7,200	86,400
2001-3000	8,600	103,200
Over 3000	14,400	172,800
Pick-Ups and Panel Vans (uncovered)		
<i>CC Rating</i>	<i>Monthly (Kshs)</i>	<i>Annual (Kshs)</i>
Up-to 1750	3,600	43,200
Over 1750	4,200	50,400
Land Rovers and Land Cruisers	7,200	86,400

Commissioner's prescribed benefit rates

<i>Services</i>	<i>Monthly Rates (Kes)</i>	<i>Annual Rates (Kes)</i>
<i>Electricity (Communal or from a generator)</i>	1,500	18,000
<i>Water (Communal or from a borehole)</i>	500	6,000
<i>Agriculture employees: Reduced rates of benefits</i>		
<i>Water</i>	200	2,400
<i>Electricity</i>	900	10,800
<i>Telephone (Landline and Mobile phones)</i>	30% of the bills	

QUESTION ONE

Moses Onyango works for Geo-Sat Solution Ltd. as a technical director. During the year ended 31 December 2020 he received the following incomes and emoluments:

1. Basic salary of Sh. 160,000 per month (PAYE Sh.42,000 per month).
2. He was provided with a 2200cc Land Rover which had cost the company Sh.4,600,000 in the year 2010.

3. In the month of December 2020. he received a sitting allowance of Sh.280,000.
4. He is a member of a registered retirement benefits scheme of which he makes monthly contributions of Sh.30,000.
5. He was housed by the company in a rented house with water, telephone and electricity. The house had a market rental value of Sh.64,000 per month and he paid a nominal rent of Sh 25,000 per month.
6. During the year, the company paid school fees for his son amounting to Sh.280.000. This amount was disallowed for tax purposes on Cleo-Sat Solution Ltd.
7. Geo-Sat Solution Ltd. operates a medical scheme for all staff with Afya Insurance Ltd. In the year 2020, the amount paid for Moses Onyango's cover amounted to Sh.320,000.
8. The company paid his monthly electricity, water and telephone bills averaging to Sh.18,000, Sh.12,500 and Sh.16,000 respectively.
9. He earned interest income of Sh.180,000 during the year from his investments in Housing Development Bonds.
10. The company paid Sh.240,000 to cover for Moses Onyango's family life insurance premiums during the year.
The insurance policy covered Moses Onyango, his wife and son.
11. In December 2020, Moses Onyango received an entertainment allowance of Sh.120,000. Half of this amount was spent on entertaining customers.
12. Moses Onyango received a net rental income of Sh.1.800,000 from his commercial rental premises during the year. This was after deducting the following expenses:

	Sh.
Caretaker's wages	620,000
Building an extension	840,000
Interest on mortgage	120,000
Fixing metallic doors	320,000

Purchase of a water tank 150,000

Required:

- a)
- i) Taxable income of Moses Onyango for the year ended 31 December 2020. Clearly showing your calculations. (17 marks)
 - ii) Tax liability (if any) from the income computed above. (3 marks)
- b) Canon of taxation refers to the characteristics or qualities of a good tax system. Discuss in details FIVE (5) canons of a good taxation system. (10 marks)

QUESTION TWO

- (a) Hazel and Kaka are in partnership operating a hardware shop as Maka enterprises and sharing profits or losses equally. The following is the income statement of the partnership business for the year ended 31 December 2020:

	<i>Kes</i>	<i>Kes</i>
<i>Sales</i>		9,280,000
<i>Capital gain on sale of property</i>		290,000
<i>Rental income</i>		240,000
<i>Dividends from Waki Cooperative (net)</i>		170,000
<i>Unrealized foreign exchange gain</i>		94,000
		10,074,000
<i>Less expenses:</i>		
<i>Cost of goods sold</i>	4,000,000	
<i>Purchase of computers</i>	160,000	
<i>Salaries and wages</i>	360,000	
<i>General expenses</i>	720,000	
<i>Legal expenses</i>	940,000	
<i>Conveyance fees</i>	92,800	
<i>Farm-works at cost</i>	60,000	

<i>Repairs and maintenance</i>	24,500	
<i>Interest on partners' capital</i>	450,000	
<i>Mambo's mortgage interest</i>	65,800	
<i>Donations to Tennis club</i>	34,800	
<i>Commission to Kaka</i>	21,100	(6,929,000)
<i>Net profit</i>		<u>3,145,000</u>

Additional information:

1. General expenses include:

	Sh.
• Embezzlement by Kaka	24,000
• Partition of staff offices	48,000
• Staff catering expenses	50,000
• Pension contributions	180,000
• Prepaid rent and rates	32,400
• Stamp duty on land transfer	64,000
2. Legal expenses include:

	Sh.
• Drafting a partnership deed	42,000
• Negotiating a bank loan	28,400
• Executing a customs bond security	24,600
• Defending the business against breach of contract	38,000
3. Salaries to partners and interest on partners' capital is to be shared according **to** the profit and loss sharing ratio.
4. Salaries and wages include salaries to employees of Sh.160,000 while the balance was paid to partners.
5. Cost of goods sold include purchases valued at Sh.300,000 which had been overstated by 20%.

Required:

- i) Adjusted taxable profit or loss for the partnership for the year ended 31 December 2020. (11 marks)
- ii) A schedule showing distribution of partner's taxable income for the year ended 31 December 2020. (9 marks)

QUESTION THREE

- (a) The Finance Act, 2019 introduced a tax known as digital services tax (DST). With reference to the above statement, describe the DST and identify FOUR types of income that are subject to digital services tax. (6 marks)
- (b) Lulu Ltd. commenced manufacturing operations on 1 May 2020 after having incurred the following capital expenditure:

	<i>Kshs</i>
<i>Factory building (note 1)</i>	20,600,000
<i>Processing machinery</i>	4,800,000
<i>Factory parking bay</i>	1,640,000
<i>Sewerage system</i>	560,000
<i>Industrial effluent treatment plant</i>	2,400,000

Additional information:

1. Factory building included the following:
- | | |
|----------------|-----------|
| | Sh. |
| — Cost of land | 4,400,000 |
| — Godown | 800,000 |
| — Showroom | 520,000 |
| — Offices | 600,000 |
| — Retail shop | 400,000 |
2. On 1 July 2020, the following capital expenditures were incurred:

	Sh.
Photocopier	60,000
Computers	150,000
Motorbike	96,000
Saloon car	3,400,000
Forklift	720,000

Furniture	240,000
Pick-up	920,000
Scanners	56,000
Tractor	1,700,000
Carpets	36,000

- The company imported a portable weighting machine on 1 September 2020 at a cost of Sh.480,000 inclusive of duty of Sh.20,000. The duty was waived by the government.
- The company was also involved in agri-business during the year.

Required:

Investment allowances due to the company for the year ended 31 December 2020. (14 marks)

(Total: 20 marks)

QUESTION FOUR

Ng'ombe Ltd, is a company that is involved in farming and milk processing. It has the following financial statement for the year then ended 31st December 2021. It started operating on 1st January 2021.

	<i>Kshs</i>	<i>Kshs</i>
<i>Revenue:</i>		
<i>Sale of milk</i>		2,400,000
<i>Sale of livestock</i>		1,800,000
<i>Sale of manure</i>		540,000
<i>Proceeds from sale of an old tractor</i>		820,000
<i>Discount received</i>		180,000
		5,740,000
<i>Expenses:</i>		
<i>General expenses</i>	430,000	
<i>Construction of a water tank</i>	240,000	
<i>(1st January)</i>		

<i>Vaccines for livestock</i>	640,000	
<i>Loan repayment</i>	350,000	
<i>Depreciation</i>	180,000	
<i>Electricity and water</i>	135,000	
<i>Conveyance fees</i>	156,000	
<i>Construction of permanent chicken shed</i>	480,000	
<i>(1st January)</i>		
<i>Animal feeds</i>	200,000	
<i>Salaries and wages</i>	1,240,000	
<i>General bad debt provisions</i>	150,000	
<i>Repair and maintenance</i>	762,000	
<i>Professional fees</i>	620,000	(5,583,000)
<i>Net profit</i>		157,000

Additional information:

1. Farm works acquired on 1st July 2021 comprised of the following:

Kshs

- | | |
|--------------------|-----------|
| a. Granary | 420,000 |
| b. Labour quarters | 1,200,000 |
| c. Cowshed | 160,000 |

2. General expenses include:

Kshs

- | | |
|--|---------|
| a. Subscriptions to Farmers' Association | 96,000 |
| b. Acquisition of a 50-year lease | 180,000 |
| c. Staff Christmas party | 25,000 |
| d. Parking fines | 129,000 |

3. Repairs and maintenance comprise:

Kshs

- | | |
|--------------------------------------|---------|
| a. Provision for fencing expenditure | 145,000 |
| b. Repairs to machinery | 240,000 |

- c. Other repairs 377,000
4. Professional fees include Kshs 500,000 paid in regards to pursuing a dispute with the Kenya Revenue Authority's VAT department.
 5. The loan repayment constituted of the principal payment amounting to Kshs 200,000 and the balance was interest payment.
 6. Assume a corporation tax rate of 30% and no capital gains tax.

Required:

- a) Adjusted taxable profit and loss of Ng'ombe Ltd., for the year ended 31st December 2021. (15 marks)
- b) Tax payable, if any, on the profit or loss you have computed above. (2 marks)
- c) Discuss the differences that exists in the taxation of a resident company has over non-resident company in Kenya. (3 marks)

QUESTION FIVE

Qwetu Home Ltd., specialize in providing students' hostels within the environs of Nairobi County. It had the following financial information for the year ended 31st December 2021.

<i>Kshs.</i>	
<i>Monthly residential rental income:</i>	
<i>Property A: 50 units each earning 12,000</i>	
<i>Property B: 40 units each earning 10,000</i>	
<i>Annual expenses:</i>	
<i>Construction of an building extension</i>	2,000,000
<i>Security cost</i>	1,500,000
<i>Repair and maintenance cost</i>	1,000,000
<i>Land Rent/Rates</i>	180,000
<i>Insurance cost</i>	50,0000
<i>Legal fees</i>	350,000
<i>Rent collection agency fees</i>	200,000
<i>Electricity and water</i>	900,000

Note:

1. The building extension was put into use from 1st January.
2. During the year, the company had taken a 10% Kshs 10,000,000 loan for the construction of the above 40 units (Property B) of residential in nature.
3. A water pump worth Kshs 450,000 was purchased to pump borehole water for the tenants. It was put into use on the 1st September 2021. The borehole was sunk at a cost of Kshs 950,000.
4. The legal fees, above, were paid to the company's defense attorneys for a court case against KRA for disputed court case. However, the firm lost the case on the 1st December 2021.
5. All the rental properties were residential (hostels) for students in nature.

Required:

- i) Estimate the tax payable for the year ended 31st December 2021.
(4 marks)
- ii) Estimate the tax payable assuming Property A units were 100 units (instead of 5) and Property B units 80 (instead of 4). (16 marks)