



MUEO

MOI UNIVERSITY

OFFICE OF THE DEPUTY VICE CHANCELLOR
(ACADEMICS, RESEARCH, EXTENSION & STUDENT AFFAIRS)

UNIVERSITY EXAMINATIONS

2022/2023 ACADEMIC YEAR

THIRD YEAR SECOND SEMESTER EXAMINATION

FOR THE DEGREE OF

BACHELOR

OF

BUSINESS MANAGEMENT

COURSE CODE: BBM 303/BPM 414/BSE 414/BHR 205

COURSE TITLE: TAXATION I

DATE: 12TH APRIL, 2023 **TIME:** 2.00 P.M. – 5.00 PM.

INSTRUCTION TO CANDIDATES

- SEE INSIDE.

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BBM 303: TAXATION I

MAIN EXAMINATION – 3rd YEAR, 1st SEMESTER, 2022/2023 ACADEMIC YEAR

Instructions: Answer question ONE and any other THREE

An individual is taxed at graduated scale rates such that the higher the income, the higher the tax as follows: These rates were effective on 1st January, 2021. It include wife's employment, self-employment and professional income rates of tax.

Monthly taxable pay (shillings)		Annual taxable pay (shillings)		Rates of tax (%)
Up to	- 24,000	up to	- 288,000	10%
24,001	- 32,333	288,001	- 388,000	25%
Income above	32,333	income above	388,000	30%

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

Prescribed benefit rates of motor vehicles provided by employer

		Monthly (sh.)		Annual (sh)	
Capital allowances					
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
Software	20%	Over	-	3000 cc	14,400 172,800
Industrial building allowance:					
Up to 2009	2.5%				
From 1 st January 2010	10%				
Hotels	10%	ii. Pick-ups, Panel Van (Unconverted)			
Hostels/educational buildings	100%				
Commercial buildings (Shop, office or show rooms)	25%	Up to	1750 cc	3,600	43,200
		Over	1750 cc	4,200	50,400
Farm works allowance	100%	iii Land Rovers/Cruisers		7,200	86,400
Investment deduction:	100%				

OR 2% of the initial capital cost of the vehicle for each month, whichever is higher.

Shipping investment deduction
(Ships over 125 tonnes) 100%

Extraction expenditure:
Written off over 5 years (20%)

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

The current VAT rate is 16%

QUESTION ONE

- a. Outline any four specified sources of income as detailed in section 3 (2) of the Income Tax Act. **(4 marks)**
- b. State and briefly explain reasons for imposing taxes in a country **(6 marks)**
- c. Lilgaa Agroforestry Ltd. has two operating divisions; Agriculture Division and Forestry Division. The following information relates to the capital expenditure incurred by the two divisions for the year ended 30th September, 2021

Agriculture Division	Kshs
Clearing and ploughing land for planting coffee	1,600,000
Purchase and planting of coffee seedlings	3,200,000
Construction of gabions to prevent soil erosion	1,000,000
Cattle shed and dip	3,000,000
Dairy equipment	360,000
Labour quarters	1,200,000
Farmhouse	7,200,000
Forestry Division	
Sawmill building	4,600,000
Sawmill machinery – fixed machinery for business use	3,800,000
Non – fixed machinery for general use	320,000
Labour quarters utilized from 1 st October 2021	2,400,000

Additional information

- i. The cost of sawmill excluded the following:
- | | |
|--|-----------|
| Architect fees | Kshs. 800 |
| Cost of transportation of building materials | 500,000 |
| Electricity supply | 100,000 |
| Wages for construction of workers | 1,200,000 |
- The sawmill building has a floor area of 4,000 square feet of which 200 square feet is occupied by offices. The cost of constructing the offices, which is included in the total cost of the sawmill building was Kshs. 750,000
- ii. Other assets acquired or constructed during the year were as follows:
- | | |
|---|-----------------|
| Two – 5 tonnes Lorries (Kshs. 2,700,000 each) | Kshs. 5,400,000 |
| Two saloon cars (Kshs. 2,400, 000) | 4,800,000 |
| Tools and equipment | 3,600,000 |
| Pick – up (4 tonnes) | 2,500,000 |
| Computers for monitoring production | 1,000,000 |
- iii. The written down values for assets for tax purposes as at 1st January, 2020 were as follows:
- | CLASS I | CLASS II | CLASS III | CLASS IV |
|-----------|-----------|-----------|-----------|
| 1,400,000 | 1,820,000 | 2,400,000 | 3,400,000 |
- iv. The company had another sawmill building which was constructed for kshs. 4,800,000 and utilized from 1st January, 2016. Due to an oversight the company did not claim for an

investment deduction on this building. The building was assessed by the revenue authority to have an economic life of 20 years. On 1st April, 2021 the company incurred Kshs. 4,200,000 to renovate the building.

- v. A motor vehicle which had cost Kshs. 2,200,000 in year 2017 was sold in August 2021 for Kshs 890,000
- vi. The company reported of Kshs. 36,000,000 before capital allowances for the year of income 2021

Required:

- i. Capital deductions due for the company during the year of income 2021 (10 Marks)
 - ii. Adjusted taxable profit for the year of income 2021 (5 Marks)
- (Total: 25 Marks)**

QUESTION TWO

- a) Explain the meaning of the following terms and state their effects on taxable income.
 - i. Trading receipts. (2 marks)
 - ii. Balancing charge (2 marks)
 - iii. Trading loss (2 marks)
 - iv. Balancing deduction. (2 marks)
 - b) State and briefly explain the factors that influence tax shifting (7 marks)
- (Total 15 marks)**

QUESTION THREE

- a. Elucidate *Three* theories devised to address the problem of justice of taxation in Kenya (6 Marks)
- b. With respect to the recent changes in tax in Kenya, explain the following amendments
 - i. Minimum tax (3 Marks)
 - ii. Beneficial ownership (3 Marks)
 - iii. Digital service tax (3 Marks)

QUESTION FOUR

- a. Explain the effects of Value Added Tax on business (5 marks)
- a) Mr. Sonko is employed by Family Bank Ltd. as an accountant. He has presented the following details for the year ended 31st December 2022:
 - 1. Basic salary of Sh. 80,000 per month (PAYE Sh. 20,000). He also received an overtime allowance equivalent to 10% of his monthly pay.
 - 2. A motor vehicle which was acquired at a cost of Sh. 700, 000. This vehicle has an engine capacity of 2500 cc.
 - 3. Provided a house that had a market value of the house is Sh. 35, 000 per month. The house was well furnished at a cost of Kshs 400,000
 - 4. He contributes Sh. 8,000 per month to a registered pension scheme while the employer contributes an equal amount.
 - 5. For the year ended 31st December 2022, the employer provided him with tea and snacks valued at Sh. 6,000 per month.
 - 6. During the year the employer paid insurance premium worth Kshs 60, 000

7. He incurred Kshs 30, 000 as an entertainment allowance for visitors which was fully reimbursed by the employer
8. Mr. Kuria received Sh. 25,000 from his employer as allowances of a five-day seminar outside his work place. He donated 5% of this amount to a charity.
9. He was nominated the employee of the year and awarded a cash gift of Sh. 85,000.
10. Mr. Sonko operates a savings account with Post Bank Ltd. During the year the bank credited his account with Sh. 6,000 being interest on the balance in his account.
11. In the month of November 2022, he received compensation from an insurance company amounting to Sh.120,000. This was in relation to household furniture destroyed by fire.
12. On 5 November 2022, he made a profit of Sh. 140,000 for providing tax consultancy services. This was before deducting operating expenses of Sh. 18,000 and Sh. 4,000 relating to the acquisition of furniture.
13. His wife, Mrs. Sonko, operates a grocery. She made a net-profit of Sh. 50,000 after deducting the following:

	Sh.
Rent of stall	10,000
Hire of van	22,000
School fees for children	108,000
Advertisement expenses	6, 000

Required:

- i. Mr. Sonko taxable income for the year of income 31 December 2021 (7 marks)
- ii. Tax payable on the taxable income computed in (i) above and comment on any information not used. (3 marks)

(Total: 15 Marks)

QUESTION FIVE

- a. Discuss the various incentives that Kenya Revenue Authority offers to tax payers in Kenya (5 marks)
- b. A businessman, provided the following information to the year of income 2019

	Kshs		Kshs
Rent expenses	180,000	Gross Profit	1,272,000
Establishment expenses	600,000	Interest income	48,000
Printing and stationery	135,000	Dividends (Gross)	80,000
Interest expense	46,000	Farming income (Gross)	226,600
Electricity	40,000	Profit on sale of shares	533,000
Farm expenses	210,000	Lottery winnings	733,300
Repairs to premises	30,000	Other incomes	53,300
Depreciation	196,000		
Salary to Mr. Diplomat	380,000		
Drawings by Mr. Diplomat	200,000		
Donations to registered children's home	166,000		
Legal expenses	125,000		
Interest loan – to pay income tax	29,000		
Bad debts	180,000		
Staff wages	144,000		

Net Profit	285,200	
	2,946,200	2,946,200

Additional information:

- i. Capital allowances has been agreed at Kshs 200,000
- ii. Legal expenses include Kshs. 50,000 paid with regard to pursuing a dispute with the tax authority
- iii. Establishment expenses include Kshs. 400,000 incurred in acquisition of an asset for the business before commencement of operations

Required:

- i. Taxable income for the year of income ended 31st December, 2019 **(7 Marks)**
- ii. Tax payable on the taxable income in (a) above **(3 marks)**

(Total: 15 Marks)

QUESTION SIX

- a. Discuss the cannons of optimal tax system as devised by Adams Smith **(9 Marks)**
- a) Clearly explain the following item are treated for the purposes of Wear and Tear deductions:
 - i. Trade in or part exchange **(2 marks)**
 - ii. Hire purchase **(2 marks)**
 - iii. Assets brought into the business without being purchased **(2 marks)**

(Total: 15 Marks)