

**KASNEB
CPA
TAXATION**

Taxation May 2015

Rates of tax(Including wife's employment, self-employment and professional income rates of tax)

Year of income 2014

Monthly taxable pay (Sh.)	Annual taxable pay (Sh.)	Rate of tax % in each Sh
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	466,704	30%

Personal relief Sh. 1,162 per month (Sh. 13, 944 per annum)

Prescribed benefit rates of motor vehicles provided by employer

Capital Allowance		i) Saloons, Hatch Backs and Estates		Monthly rates (Sh.)	Annual rates (Sh.)
Wear and tear allowance					
Class I	37.5%	Up to	1200cc	3,600	43,200
Class II	30%	1201	1500cc	4,200	50,400
Class III	25%	1501	1750cc	5,800	69,600
Class IV	12.5%	1751	2000cc	7,200	86,400
Software	20%	2001	3000cc	8,600	103,200
		Over	3000cc	14,400	172,800

Industrial building allowance

up to 2009	2.50%
From 1 January 2010	10%
Hotels	10%
Hostels/Education Buildings	50%
From 1 January 2010-	
Commercial building (Shop, office or show room)	25%

Farm works allowance

100% ii) Pick-ups, Panel Vans (unconverted)

Investment deduction allowance

100%	Up to	1750cc	3,600
	Over	1750cc	4,200
	iii)	Land Rovers/Cruisers	7,200

Shipping investment deduction	40%
Mining allowance	
Year 1	40%
Years 2-7	10%

Commissioner's prescribed benefits rates

	Monthly Rates	Annual Rates
	Sh.	Sh.
Services		
i) Electricity (Communal or from a generator)	1,500	18,000
ii) Water (Communal or from a borehole)	500	6,000
Agriculture employees: Reduced rates of benefits		
i) Water	200	2,400
ii) Electricity	900	10,800

QUESTION ONE

- a) Explain the significance of the following canons in designing the tax systems of an economy:
- i. Equity (2 marks)
 - ii. Economy (2 marks)
 - iii. Convenience (2marks)
 - iv. Certainty (2 marks)
- b) Gregory Omari, a finance manager with Safi Ltd., has provided the following information on his employment and other income for the year ended 31 December 2014:
1. Basic salary Sh. 225,000 per month (PAYE Sh. 42,500 per month).
 2. The employer provided him with a house during the year. The employer furnished the house on 1 October 2014 at a cost of Sh.240, 000. Prior to this, he was using his own furniture.
 3. He was provided with a company car of 2000cc, which had cost Sh. 1, 200, 000 in 2013
 4. He was paid leave allowance equal to one month's basic salary in March 2014.
 5. He contributed 5% of his monthly basic salary to a registered pension scheme, with the employer contributing an equal amount for him.
 6. During the year the employer paid school fees for Gregory Omari's son amounting to Sh. 85, 000. The amount was disallowed for tax purpose on Safi Ltd.
 7. His wife was hospitalized and the employer paid Sh. 540, 000 towards the medical bill. The employer has a medical cover for senior staff only.
 8. The employer paid life insurance premium of Sh. 50, 000 per annum for him.
 9. During the month of May 2014, he acquired a loan from Delite Bank amounting to Sh. 8,000,000 at an interest rate of 8% per annum and constructed four rental houses. The houses were occupied from 1 September 2014 at a monthly rent of Sh. 40, 000 per house.
 10. He received 2,000 shares in Safi Ltd at the end of December 2014 as a reward for his outstanding performance during the year. The last valuation of the shares was Sh. 50 each.
 11. In December 2014, the employer decided to reimburse him for a third of the cost incurred on water, electricity, internet and cook for the entire year. The annual amounts incurred by him were Sh. 14, 400, Sh 18, 000, Sh 15,000 and Sh 54, 000 respectively.
 12. Other expenditure in relation to the rental houses included

Sh.

Insurance	20,000
Salary to self	100,000
Loan repayment	1,162,000
Interest on loan	213,000
Rates	5,000
Caretaker salary	36,000
Computer	55,000

Required:

- i. Taxable income for Gregory Omari for the year ended 31 December 2014 (10 marks)
- ii. Tax payable (if any) on the income computed in (b) (i) above (2 marks)

(Total: 20 marks)

QUESTION TWO

- a) The member states of East African Customs Union have faced certain challenges in their intergartion. Citing relevant example, evaluate four such challenges. (8 marks)
- b) Ashrey and Balak are partners trading as Barrey Enterprises, and sharing profit and losses equally. They have not maintained proper books of account, but have provided the following details for determination of taxable income for the partnership for the year 31 December 2014:
 1. The partners charge interest on drawings at the rate of 10% per annum.
 2. Assets and liabilities as at 31 December:

	2013	2014
	Sh.	Sh.
Stock in trade	860,000	1,680,000
Creditors	740,000	890,000
Prepaid rent	30,000	42,000
Accrued Electricity bills	21,000	16,000
Bank balance	230,000	165,000
Accrued salaries	520,000	480,000

3. The partners banked all cash collections after deducting the following monthly expenses:

Sh	
Cash drawings: Ashrey	15,000
Balak	10,000
Wages	12,000
Purchase of goods for sale	18,000
Sundry expenses	10,000
Motor vehicle expenses	8,000

4. Payments made through the bank during the year ended 31 December 2014 were as follows:

	Sh
General expenses	30,000
Motor vehicle expenses	16,000
Purchase of goods for sale	1,515,000
Rent	504,000
Electricity	139,000
Salaries	4,800,000
Purchase of motor vehicle	3,000,000
Selling and distribution expenses	140,000
Wages	544,000
Cost of meals to employees	123,000

5. On average, the partners sold all goods at a gross profit margin of $\frac{331}{3}$. During the year, Ashrey and Balak had taken goods (at cost price) worth Sh. 250,000 and Sh. 100, 000 respectively.
6. The partners estimate the use of motor vehicle to be 40% for private purposes.
7. On 1 October 2014, the partners admitted Korir as a new partner. He paid Sh. 4,000,000 as his capital contribution. The new profit sharing ration was agreed at 2:2:1 for Ashrey, Balak and Korir respectively.
8. A half of the salaries expenses relate to the partners. Out of these, Korir received Sh. 268, 000 being salary dues to 31 December 2014.
9. It was agreed with the commissioner of tax that wear and tear allowance be provided at Sh. 120, 000 for the year ended 31 December 2014.

Assume that income and expenses accrued evenly throughout the year.

Required:

- i. The adjusted partnership profit or loss for the year ended 31 December 2014. (8 marks)
- ii. Distribution schedule of the profit of loss calculated in (b)(i) (4 marks)
above.

(Total: 20 marks)

a) In the context of taxation of firms in the mining industry, explain the following terms:

- i. Exploration expenditure (2 marks)
- ii. Extraction expenditure (2 marks)

b) Solomon Chacha registered for value added tax on 1 May 2015. During the registration process, he was instructed to ensure that in the course of his business he maintained a full and written record, in electronic or other acceptable form.

He has approached you for more details he is expected to maintain as per the Value Added Tax (VAT) act.

Required:

Advise Solomon Chacha, on six records he is required to maintain as per the VAT Act. (6 marks)

c) Mehta Ltd, a company dealing in electronic items and registered for value added tax (VAT) purposes, provided the following details in respect of the month of September 2014.

September 1: Purchased 10 cameras for a total of Sh. 500,000.

September 2: Purchased flash bulbs for a total of Sh. 200,000.

September 4: Purchased slide projectors for a total of Sh. 1,000,000.
 September 6: Sold 5 cameras each at 35% above cost price
 September 7: Purchased 200 wrist watches at Sh. 1,500
 September 8: Sold 2 slide projectors for a total of Sh. 50,000
 September 9: Sold flash bulbs that had cost Sh. 100,000 for Sh. 150,000
 September 12: Purchased 50 stop watches for a total of Sh. 50,000
 September 15: Purchased 100 alarm clocks at a total cost of Sh. 80,000
 September 18: Sold the remaining 5 cameras each at 25% above cost price
 September 20: Sold 3 slide projectors for a total of Sh. 750,000
 September 22: Sold 100 wrist watches at Sh. 2,000 per watch
 September 25: Sold 70 alarm clocks each at 30% above cost price
 September 27: Sold 50 stop watches for a total of Sh. 75,000
 September 30: Paid - Rent Sh. 20,000
 - Motor vehicle repair Sh. 10,000 (for business)
 - Telephone Expenses Sh. 9,000
 - Catering services Sh. 19,000
 - Audit fee Sh. 35,000

All transactions were inclusive of VAT at the rate of 16% where applicable.

Required:

Calculate for Mehta Ltd for the month of September 2014:

- i. Input tax (5 marks)
- ii. Output tax (4 marks)
- iii. VAT payable or refundable (1 mark)

(Total)

QUESTION FOUR

- a) Humphrey Wanjohi constructed five rental houses in the year 2013. The houses were fully occupied with effect from 1 January 2014. He intends to file tax return for the year ended 31 December 2014. He has approached you for advice on the various deductions allowed against rental income.

Required:

Advice Humphrey Wanjohi on six deductions allowed against rental income. (6 marks)

- b) Quality Meat Ltd was established on 1 January 2013 to process meat products for the local market. The company incurred the following costs on constructing relevant structures which were utilized from 1 January 2013.

	Sh
Factory building	8,200,000
labour quarters	2,400,000
Showroom	960,000
Staff recreation facility	4,800,000
Retail shop	720,000
Perimeter wall	1,400,000
Administrative offices	620,000

Drive way	580,000
Sports pavilion	3,200,000
Drainage system	840,000

Other assets acquired prior to 2 January 2013 comprised:

	Sh
Heating plant	3,400,000
Delivery Vans	2,200,000
Computers	680,000
Lorry (tonnes)	4,200,000
Factory machinery	1,800,000
Fax machines	420,000
Water pump	740,000

Additional information:

1. A borehole was drilled at a cost of Sh. 920,000 and utilized from 1 September 2013.
2. On 1 July 2014, the company constructed a factory extension and a loading bay at the cost of Sh. 2,400,000 and Sh. 560,000 respectively. The structures were utilized with effect from 1 October 2014.
3. The following assets were acquired on 1 August 2014:

	Sh.
Pick-up	2,000,000
Conveyor belts	640,000
Scanners	220,000
Mobile phones	156,000
Electronic weighing machines	720,000

4. The following assets were disposed off during the year:

Asset	Disposal date	Cost of the asset		Disposal Proceeds	
		Sh.		Sh.	
Computers	02-Feb-14	120,000		420,000	
Delivery van	04-Apr-14	1,100,000		760,000	
Fax machine	30-Sep-14	86,000		54,000	

5. The company had not claimed capital allowances since it commenced operations.

Required:

Capital allowances due to Quality Meat Ltd for each of the years ended 31 December 2013 and 2014.

(14 marks)

(Total: 20 marks)

QUESTION FIVE

- a) Outline four benefits of turnover tax. (4 marks)
- b) In a tax seminar, one of the facilities noted that, "there is a global shift from export processing zones (EPZs) to special economic zones (SEZs), where countries are deriving immense benefits from the trend"

Required:

- i. Explain the meaning of special economic zones (SEZs) (2 marks)
- ii. Argue four cases in favour of special economic zones (SEZs) (8 marks)
- c) John Amanda bought a residential house for Sh. 7,000,000 in the years 2006. Legal fees and stamp duties amounted to Sh. 300,000. In the year 2008, he added three bedrooms at a cost of Sh. 920,000 and received an improvement grant of Sh. 1,000,000. In the year 2009, a strong wind damaged the roof and he incurred repair costs amounting to Sh.480,000. In the year 2011, a boundary dispute arose with a neighbour and legal costs amounting to Sh. 34,000 were incurred in settling the dispute. In the year 2012, a further extension was planned and architect's fees of Sh. 650,000 incurred, however, the plan was not approved by the County Council and the extension was abandoned.

The residential house was sold in the year 2015. He incurred conveyancing costs of Sh.60, 000, advertising costs of Sh.15, 000 and estate agent commission of Sh. 24,000.

Required:

- i. With respect to capital gains tax, calculate the adjusted cost of the residential home at the point of sale. (4 marks)
- ii. Comment on information not used in (c) (i) above. (2 marks)

(Total: 20 marks)