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University Examinations 2023/2024

SECOND YEAR SECOND SEMESTER EXAMINATION FOR THE DEGREE OF
BACHELOR OF SCIENCE IN APPLIED ACCOUNTING

BFH 3251: ADVANCED TAXATION THEORY AND PRACTICE

DATE: APRIL 2024

TIME: 2 HOURS

INSTRUCTIONS: Answer question *one* and any other *two* questions

QUESTION ONE (30 MARKS)

- a) Explain the main theories of tax shifting (5 marks)
- b) With an aid of a diagram, explain the concept of forward shifting of tax (5 marks)
- c) Discuss the functions of commission of revenue allocation (5 marks)
- d) Amaco Insurance Ltd underwrites three classes of insurance. The management has provided you with the details shown below on their operations for the year ended 31 December 2017:

Class of insurance	Fire	Motor vehicle	Theft
	Sh. '000'	Sh. '000'	Sh. '000'
Gross premium written	23,088	24,664	9,780
Reinsurance ceded	14,747	15,007	4,822
Unearned premium brought forward	4,205	6,293	1,466
Unearned premium carried forward	2,035	9,259	668
Claims aid	2,216	5,538	1,215
Claims outstanding brought forward	2,781	10,325	4,532
Claims outstanding carried forward	2,755	9,416	8,756
Legal expenses on claims	645		125
Depreciation	60	125	65
Gain on sale of motor vehicles previously	-	50	-
Specific bad debts	80	35	62
Management expenses	1,606	2,350	876
Commissions (net)	1,606	1,546	890

Additional information:

1. Wear and tear deductions have been agreed with the Income Tax Department at sh.454,000.
2. The company invested surplus funds and earned investment income as follows:

	Sh.
Interest from Treasury bills (net)	2,040,000
Interest from fixed deposits in local bank(net)	762,450
Gross dividends from Zim-re of Zimbabwe (a foreign company)	450,000
Dividends from KELP Ltd.	912,000

3. The company paid sh.745,000 to ABC Investment Management Services, their fund management for professional services for the year ended 31 December 2017.
4. The company owns Afro House which houses its offices. Part of the office space is rented out to other tenants. In the year to 30 December 2014, the company received sh. 2,200,000 net rental income from their estate agents. Property management fees amounting to sh. 2,400,000 for the year to 31 December 2017 had been deducted.
5. Afro Insurance Ltd owns 80% of the ordinary shares in KELP ltd a locally incorporated company.

Required:

- (i) Compute the taxable profit or loss for Afro Insurance Ltd for the year ended 31 December 2017. (10 marks)
- (ii) Compute the tax payable in (a) above. (2 marks)
- (iii) Comment on any information you have not used in your computations (3 marks)

QUESTION TWO (20 MARKS)

- a) Discuss the main provisions regarding the authority to grant double taxation in Kenya (10 marks)
- b) Explain with relevance to tax legislation the implications of this Treaty (5 marks)
- c) Mrs. Mugambi is a Kenyan resident. In 2023, she earned income of shs 2,400,000 in Kenya and taxable income from Canada shs 600,000. Tax deducted in Canada was shs. 400,000. Kenya has a double taxation treaty with Canada. Required:
 - i. Double taxation relief due to Mrs Makena in Kenya (3 marks)
 - ii. Her total tax Liability for the year of income 2023 (2 marks)

QUESTION THREE (20 MARKS)

Explain the main provisions regarding the taxation of the following special businesses as outlined by the income tax Act CAP 470

- i. Amateur sporting clubs (4 marks)
- ii. Consolidated financial statements (4 marks)
- iii. Trade associations (2 marks)
- iv. Companies under liquidation (2 marks)
- v. Residential rental income (4 marks)
- vi. Commercial rental income (4 marks)

QUESTION FOUR (20 MARKS)

The following information was extracted from the books of Majani Mingi imited Ltd, for the year ended 31 December 2017:

- Profit before tax Sh. 8,000,000
- Import duty refunded by tax authority Sh. 800,000
- Dividend distributed by the company Sh. 17,600,000
- Dividend received by the company Sh. 6,000,000

The corporation tax is 30%

Required:

Compensating tax payable by the company for the year ended 31 December 2017 (5 marks)

- b) Discuss the provisions of the Income Tax Act (Cap 470) relating to shortfall tax on non-distribution of dividend. (5 marks)
- c) With reference to section 18 (3) of the Income Tax Act (Cap. 470):
- (i) Outline the characteristics of transactions that may constitute transfer pricing (5 marks)
- (ii) Identify four methods of determining an appropriate transfer price as provided in the organization for Economic Co-operation and Development (OECD) model (5 marks)

QUESTION FIVE (20 MARKS)

- a) Discuss the professional ethics of a Tax Professional (5 marks)
- b) You are the head of the team from the revenue authority conducting this investigation. Mr. Magufuli has submitted to you records of his private and business assets and liabilities from 1 January 2013 to 31 December 2017 as shown below:

	1 Jan 2013 Sh. '000'	31 Dec 2014 Sh. '000'	31 Dec 2015 Sh. '000'	31 Dec 2016 Sh. '000'	31 Dec 2017 Sh. '000'
Assets and Liabilities					
Facto building	36,000	48,000	48,000	52,000	54,000
Plant and machine	24,000	28,000	36,000	36,000	38,000
Commercial vehicles	9,000	12,000	12,000	15,000	18,000
Stock in trade	3,600	4,200	8,000	9,000	7,000
Trade debtors	2,960	3,540	2,640	2,530	2,980
Private residence		13,600	13,600	13,600	13,600
Trade creditors	7,280	8,640	9,420	8,360	7,890
Bank loan	10,900	10,000	9,870	7,640	9,840
Loan from an uncle	800	700	600	870	640
Mortgage loan	3,780	3,780	3,780	3,780	3,780
Bank balance	3,400	5,400	3,600	3,760	4,670

Additional information:

- There were no disposals of fixed assets during the period under investigation.
- The bank balance on 31 December 2015 included Sh. 400,000 inherited from a relative on 31 October 2015
- His living expenses for each of the four years were as follows:

		Year Ended 31 December:		
Living expenses (Sh)	2014	2015	2016	2017
	70,000	120,000	90,000	150,000

4. Interest on the mortgage is at a rate of 10%.

Required:

- a) The taxable income of Mr. Magufuli for each of the four years ended 31 December 2014, 2015, 2016 and 2017. Ignore capital allowances (12 marks).
- b) Comment on any four areas on which you would further clarification from Mr. Magufuli before concluding your investigation (3 marks)