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CPA

Advanced Taxation

December 2025

Level: Advanced Level

Question 1a

 Tax investigations, Tax dispute resolution mechanism

Brightstar Enterprises Ltd., a manufacturing company has been assessed by the Revenue Authority for the year ended 31 December 2023. The assessment alleges that Brightstar Enterprises Ltd. understated sales and issued a reassessment of corporate income tax amounting to Sh.15 million. In addition, the Revenue Authority has imposed penalties and interest for late filing and payment. Separately, a VAT audit adjustment of Sh.5 million has been made on the basis that some supplier invoices claimed for input VAT were not in proper format. Brightstar Enterprises Ltd. insists that its sales records are complete and audited and that the Revenue Authority findings of understatement is incorrect. The company accepts responsibility for the late filing (attributing it to system failures), though it believes the penalties may be mitigated.

With regards to VAT, Brightstar Enterprises Ltd. maintains that the invoices in question are valid under generally accepted accounting practice, despite lacking some formal invoice formalities. Brightstar Enterprises Ltd. wishes to dispute the assessment and resolve the matter in a timely and cost-effective manner.

Required:

(i) Analyse THREE steps Brightstar Enterprises Ltd. should take under tax laws or any other related laws in Kenya to properly object the tax assessment issued.

(ii) Citing THREE benefits that might accrue to the company, advise the management of Brightstar Enterprises Ltd. on how to commence alternative dispute resolution (ADR) process.

(iii) If Brightstar Enterprises Ltd. chooses to appeal before the Tax Appeals Tribunal (TAT), explain FOUR preconditions it must satisfy, under Kenyan tax law to make its appeal valid.

✓ Answer for Question 1a

(i) Three Steps to Properly Object to the Tax Assessment

Under the **Tax Procedures Act, 2015 (TPA)**, Brightstar Enterprises Ltd. must follow a strict, statutory process to formally dispute the assessments. The following three steps are critical for a valid objection:

1. Lodge a Valid Notice of Objection Within 30 Days

The company must file a written notice of objection with the Commissioner of Domestic Taxes within **30 days** of being notified of the assessment. It is crucial that this objection is complete to be considered "validly lodged." Under **Section 51(3) of the TPA**, a valid objection must:

- **State precise grounds:** Clearly explain why the assessment is incorrect, specify the amendments required to correct the decision, and give reasons for those amendments.
- **Pay the undisputed tax or apply for an extension:** The company must pay the entire amount of tax that is **not in dispute**. Since Brightstar Enterprises Ltd. accepts responsibility for the late filing penalty and the underlying tax, it must pay this undisputed amount or formally apply for an extension of time to pay.
- **Submit all relevant documents:** The objection must be accompanied by all relevant supporting documents. For the corporate income tax dispute, this would include audited financial records and sales ledgers. For the VAT dispute, it would include the supplier invoices in question to demonstrate their validity.

2. Wait for the Commissioner's Objection Decision

After a valid objection is lodged, the Commissioner has **60 days** to consider it and issue an "Objection Decision." This decision, which can allow the objection in whole or in part, or disallow it, must include findings of fact and reasons for the decision. If the Commissioner does not issue a decision within 60 days, the law dictates that the objection is **deemed to be allowed** by operation of law. This is an important safeguard for the taxpayer.

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Advanced Taxation

August 2025

Level: Advanced Level

Question 1b

 Value added tax administration

Barani Enterprises Ltd. is a value added tax (VAT) registered business involved in the sale and distribution of both taxable and exempt supplies. The following transactions were recorded in the books of the company for the month of April 2025:

- April 2: Sales at standard rate Sh.1,160,000.
- April 4: Sales made as exempt supply Sh.400,000.
- April 6: Purchase of goods for resale on credit Sh.580,000.
- April 9: Purchase of stationery on credit Sh.116,000.
- April 12: Purchase of fuel for company car Sh.87,000.
- April 15: Payment for entertainment expenses for clients Sh.58,000.
- April 18: Purchase of a saloon car for director Sh.1,160,000.
- April 20: Imported raw materials with customs and VAT paid Sh.232,000.
- April 22: Repairs to delivery truck used exclusively for distribution Sh.58,000.
- April25: Purchase of goods used in both exempt and taxable supplies for Sh.348,000.
- April 28: Rent for business premises to a landlord registered for VAT Sh.116,000.

Additional information:

1. The company uses turnover-based apportionment for input VAT on mixed-use items.
2. Transactions are inclusive of value added tax (VAT) at the rate of 16%where applicable.

Required:

(i) Compute the output VAT for the month of April 2025.

(ii) Determine the total input VAT incurred and identify which amounts are restricted under the VAT Act, 2013.

(iii) Calculate the allowable input VAT claimable.

(iv) Compute the VAT payable or refundable for the month of April 2025.

✓ Answer for Question 1b

(i) Compute the output VAT for the month of April 2025.

Output VAT is the VAT charged on taxable sales (supplies) made by the business.

Date	Transaction	Sh.
April 2:	Standard Sales 1,160,000@16/116	160,000
April 4:	Exempt Sales 400,000@0%	0
Total Output VAT		160,000

(ii) Determine the total input VAT incurred and identify which amounts are restricted under the VAT Act, 2013.

Input VAT is the VAT paid on purchases (inputs) made by the business. We must calculate the VAT amount for each purchase and then identify which are restricted (non-deductible).

Date	Transaction	Sh.
Apr 6	Goods for resale 580,000@16/116	80,000
Apr 9	Stationery 116,000@16/116	16,000
Apr 12	Fuel 87,000@16/116	12,000
Apr 15	Entertainment 58,000@16/116	8,000
Apr 18	Saloon car 1,160,000@16/116	160,000
Apr 20	Imported raw materials 232,000@16/116	32,000
Apr 22	Repairs(Truck) 58,000@16/116	8,000
Apr 25	Mixed-use goods 348,000@16/116	48,000
Apr 28	Rent 116,000@16/116	16,000

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Advanced Taxation

April 2025

Level: Advanced Level

Question 1c

Limited companies

Marine Shipping Line Ltd. is a Kenyan resident company that carried on the business of transporting cargo, mails and passengers in the various ports of the world. The company reported the following transactions for the year ended 31 December 2024:

Income	Sh"000"
Revenue generated from carriage of passengers from Kenya to other countries	851,580
Revenue generated from carriage of cargo and mails from Kenya to China	1,147,500
Revenue from carriage of passengers and cargo from China to Kenya	2,502,820
Rebate received for meeting destination timelines	12,220
Income from the lease of a ship	362,500

Expenditure:

1. The company started its operations on 1 April 2024 and acquired the following assets:

		Sh.“000”
Ships: MV Border	340 tonnes	89,000
: MV Queen	100 tonnes	28,000
: MV Olympic	490 tonnes	20,000
Tools and implements		6,000
Pick up vans		16,000
Mobile cranes		10,000

2 The following expenses were incurred during the year: **Sh.“000”**

	Sh.“000”
• Business licences and permits	40,000
• Port facilities fee	132,400

• Catering bills for passengers	237,800
• Salaries and wages	1,118,000
• Estimated default by debtors	12,000

3 Out of the revenue generated from carriage of passengers and cargo from China to Kenya, Sh.520,000,000 was in respect of passengers who embarked in Kenya as a result of transshipment.

Required:

Compute the taxable profit or loss and tax payable (if any) for Marine Shipping Line Ltd. for the year ended 31 December 2024.

✓ Answer for Question 1c

Taxable profit or loss and tax payable (if any) for Marine Shipping Line Ltd. for the year ended 31 December 2024.

	Sh."000"
Revenue (W1)	2,893,800
Expenditure:	
Business licences and permits:	(40,000)
Port facilities fee	(132,400)
Catering bills for passengers	(237,800)
Salaries and wages	(1,118,000)
Capital Allowance (W2)	(75,600)
Taxable profit(loss)	**1,290,000**

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Advanced Taxation

December 2024

Level: Advanced Level

Question 2a

 Tax investigations, Professional practice in taxation

Bright Star Electronics Enterprise is a small business operating in the retail sector. The business has experienced steady growth in sales over the years. The owner, John Irungu handles most of the financial and accounting tasks. The revenue authority has noticed discrepancies in the tax returns over the last two years where there are significant variations in the reported income and expenses. The business has also claimed several large deductions that appear unusual for the size of the business. These red flags prompted the revenue authority to issue a notice of tax audit. John Irungu has engaged you as a tax agent to assist him in this matter:

Required:

(i) Explain to John Irungu THREE objectives of a tax audit initiated by the revenue authority.

(ii) Analyse THREE responsibilities of a tax agent to the client during the tax audit process.

✓ Answer for Question 2a

Advice for John Irungu of Bright Star Electronics Enterprise

(i) Objectives of a Tax Audit Initiated by the Revenue Authority

A tax audit is not merely a random check; it is a structured examination of your business records with specific goals. The primary objectives are:

1. **To Verify Compliance with Tax Laws:** The main goal is to check if the information declared in your tax returns (income, expenses, VAT) is accurate and complete. They want to ensure you have paid the correct amount of tax according to the law.
2. **To Detect and Correct Errors or Omissions:** The authority aims to identify any mistakes, whether unintentional (like calculation errors) or intentional (like omitting income or inflating deductions). The audit will reconcile your financial records with your tax declarations.
3. **To Promote Voluntary Compliance:** The audit serves as a deterrent. By conducting audits, the revenue authority encourages all businesses to be more diligent and honest in their tax reporting, knowing their records can be reviewed at any time.

In your case, the "significant variations" and "unusual large deductions" are specific red flags the auditor will be investigating to achieve these objectives.

(ii) Responsibilities of a Tax Agent to the Client During the Tax Audit Process

As your tax agent, my responsibilities are to protect your interests, ensure the process is fair, and achieve the best possible outcome. These responsibilities can be analysed as follows:

1. Pre-Audit Preparation and Guidance

- **Analysis:** My first duty is to prepare you thoroughly. This involves reviewing all your financial records for the audit period to identify and rectify any potential issues *before* the auditor arrives.

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Advanced Taxation

August 2024

Level: Advanced Level

Question 2b

 Taxation of business income and specialized business activities

Pelly and Mark have been partners trading as Pama Enterprises from 1 January 2021 having contributed Sh.12,000,000 and Sh.15,000,000 as capital for Pelly and Mark respectively. They prepare their accounts to 31 December every year. Due to the need of expanding their business, they decided to admit Colley on 1 May 2023 and changed the business name to Pamac Enterprise. Colley brought in Sh.18,000,000 as his capital contribution. Prior to the admission of Colley, the profit and loss sharing ratio was 2:3 between Pelly and Mark respectively. However, with the admission of Colley they revised the profit and loss sharing ratio to 2:3:4 for Pelly, Mark and Colley respectively.

The following information was extracted from the business records for the year ended 31 December 2023:

1. Assets and liabilities as at 31 December:

	2022 Sh.“000”	**2023 Sh.“000”**
Payables	7,200	11,050
Accrued salary and wages	1,600	2,300
Accrued rent	1,825	2,100
Prepaid electricity bills	293	245
Furniture and fittings	600	450
Balance at bank	7,910	9,566
Equipment	670	530
Inventory	1,248	897

2. During the year ended 31 December 2023, the partners banked all cash collections after deducting the following monthly expenses:

	Sh.
Repair and maintenance	20,000
Stationery	23,700
Sundry expenses	32,000
Motor vehicle expenses	20,500
Purchase of goods for resale	190,000

3. Payments made through the bank during the year ended 31 December 2023, have been summarised as follows:

	Sh.“000”
Rent	2,250
Motor vehicle expenses	420

Web hosting cost	25
Directors allowance	450
General expenses	10,779
Electricity	1,800
Purchase of goods	52,640
Floatation cost	200
Salaries and wages	8,300
Purchase of saloon car	4,500

4. The partnership business was converted into a limited company by the name Pamac Limited on 1 September 2023 and the partners became the directors of the company. Upon conversion, the company issued 8% debentures of Sh.15,000,000.

5. On average, the business sold all goods at a gross profit margin of 30%.

6. Specific provision for bad and doubtful debts as at 1 January 2023 was Sh.8,300,000 while as at 31 December 2023 was Sh.3,400,000.

7. There was no disposal of fixed assets during the year.

8. The partners were charging interest on capital at the rate of 10% per annum.

9. The partners annual salary was Sh.1,000,000, Sh.2,500,000 and Sh.3,000,000 for Pelly, Mark and Colley respectively. The partners salary was not included in the salary and wages for the year.

10. Sales, purchase and expenses accrued evenly throughout the year.

Required:

(i) In a columnar format, determine the taxable income of the partnership and Pamac Limited for the year ended 31 December 2023.

(ii) Compute taxable income of each partner for the year ended 31 December 2023.

✓ Answer for Question 2b

(i).Taxable income of the partnership and Pamac Limited for the year ended 31 December 2023.

Description	Pama (Jan-Apr)	Pamac Ent. (May-Aug)	Total Partnership (8 months)	Pamac Ltd (Sep-Dec,4 months)	Total (Jan-Dec,12 months)
Sales(W1)	28,152,857	28,152,857	56,305,714	28,152,857	84,458,571
Less: COGS(W1)	(19,707,000)	(19,707,000)	(39,414,000)	(19,707,000)	(59,121,000)
Gross profit	**8,445,857**	**8,445,857**	**16,891,714**	**8,445,857**	**25,337,571**
Less: Expenses					
Salaries and wages(W2)	(3,000,000)	(3,000,000)	(6,000,000)	(3,000,000)	(9,000,000)
Rent	(841,667)	(841,667)	(1,683,333)	(841,667)	(2,525,000)
Electricity	(616,000)	(616,000)	(1,232,000)	(616,000)	(1,848,000)
Repair and maintenance	(6,667)	(6,667)	(13,333)	(6,667)	(20,000)
Stationery	(7,900)	(7,900)	(15,800)	(7,900)	(23,700)
Sundry expenses	(10,667)	(10,667)	(21,333)	(10,667)	(32,000)
Motor vehicle expenses(20,500+420,000)	(146,833)	(146,833)	(293,667)	(146,833)	(440,500)
Web hosting cost	(8,333)	(8,333)	(16,667)	(8,333)	(25,000)
Directors allowance	-	-	-	(450,000)	(450,000)
General expenses	(3,593,000)	(3,593,000)	(7,186,000)	(3,593,000)	(10,779,000)
Floatation cost	-	-	-	(200,000)	(200,000)
Bad debts(Specific)	(1,633,333)	(1,633,333)	(3,266,667)	(1,633,333)	(4,900,000)
Debenture interest(15,000,000*8%*4/12)	-	-	-	(400,000)	(400,000)
Wear & Tear(W3)	(292,333)	(292,333)	(584,667)	(292,333)	(877,000)
Taxable income/(loss)	**(1,710,876)**	**(1,710,876)**	**(3,421,753)**	**(2,760,876)**	**(6,182,629)**

(ii). Taxable income of each partner for the year ended 31 December 2023.

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Advanced Taxation

April 2024

Level: Advanced Level

Question 2c

 Value added tax administration

Weddy Associates is a practicing law firm that was registered for VAT in the year 2022. The following transactions were reported by the law firm accountant for the month of October 2023.

October 2:	The firm provided consultation for legal information and advice to Weka Ltd. at a fee of Sh.1,200,000.
October 5:	Offered training services to practicing accountants on alternative dispute resolution during the annual conference and invoiced the Institute of Accountancy Sh.800,000. The payment had not been received at the end of the month.
October 9:	A client by the name Bima Ltd. was declared bankrupt. Weddy Associates had offered arbitration services to the client in April 2023 at a fee of Sh.480,000 but Bima Ltd. had only managed to settle Sh.200,000 by the time it was declared bankrupt.
October 11:	Weddy Associates entered into a contract with Apex Bank Ltd. to review the bank lease agreement following a dispute with the bank's landlord on rent payment. The firm received an advance payment of Sh.400,000 from the bank and the balance of Sh.620,000 was to be received upon submission of the final legal report in November 2023.
October 16:	Royal Ltd. engaged the firm to draft its Memorandum and Articles of Association and register the company with the registrar of companies at a fee of Sh.50,000.
October 21:	Weddy Associates represented RR International Ltd., a diaspora client in arbitration case with a supplier and charged a fee of Sh.2,100,000. The client had only paid 30% of the total fee by end month.
October 25:	Weddy Associates engaged a professional legal firm in the United Kingdom (UK) to train the law firm employees on client mediation and arbitration process at a total fee of Sh.1,800,000 without VAT. The training was conducted just before the end month.
October 30:	The firm represented the following clients in the court in the course of the month and charged the fee as follows:

- Sh. Shakir family on property dispute 620,000
- Bema Ltd. on breach of trade agreement 1,400,000
- Safi hospital on patient negligence 360,000

The following expenses were incurred by Weddy Associates in the course of the month:

- Electricity paid during the month was Sh.120,000 out of which Sh.20,000 was paid as deposit for the electricity meter to the power and lighting company.
- Rent for the office space Sh.480,000.
- Mandatory annual continuing legal education subscriptions for firm lawyers Sh.360,000.
- Training fee for the advocates Sh.420,000.
- Fuel for partners vehicles Sh.90,000.
- Professional indemnity cover Sh.124,000.
- Purchase of law practice management and accounting software Sh.1,620,000.
- Office computers purchase Sh.2,400,000.
- Stationery Sh.300,000.

Unless otherwise stated, all transactions were inclusive of value added tax (VAT) at the rate of 16% where applicable.

Required:
Compute the value added tax (VAT) payable by or refundable to Weddy Associates for the month of October 2023.

✓ Answer for Question 2c

VAT Computation for Weddy Associates for October 2023

Output VAT

Date	Transaction Details	
Oct 2	Legal advice 1,200,000@16/116	165,517
Oct 5	Training 800,000@16/116	110,345
Oct 11	Lease review 400,000@16/116	55,172
Oct 16	Company registration 50,000@16/116	6,897
Oct 21	Arbitration 2,100,000 x 30%@16/116	86,897
Oct 25	Reverse Charge: 1,800,000 × 16%	288,000
Oct 30	Court Representations: - Shakir family 620,000 - Bema Ltd. 1,400,000 - Safi hospital 360,000 2,380,000@16/116	328,276
Total Output VAT		**1,041,104**

Input Vat

Transaction details	Rate	Sh.
Electricity	100,000@16/116	13,793
Office Rent	480,000@16/116	66,207
Training Fee for Advocates	420,000@16/116	57,931
Fuel for Partners' Vehicles	90,000@16/116	12,414
Practice Management Software	1,620,000@16/116	223,448
Office Computers	2,400,000@16/116	331,034

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Advanced Taxation

December 2023

Level: Advanced Level

Question 2d

 Limited companies

The following incomes and expenses were extracted from the accounting records of Turkanah Oil Ltd. for the year ended 31 December 2022:

Income	**Sh.“million”**
Proceeds from sale of oil (2,800,000 barrels at Sh.15,000 per barrel)	42,000
Value of chargeable oil disposed of to local refineries	21,000
Value of chargeable natural gas and other incomes	26,500
Freight charges received from other oil transport	22,800
Expenses:	
Royalties paid for crude oil exported	4,800
Staff accommodation expenses	2,820
Royalties incurred in respect of natural gas disposed of to local refineries	3,420
Interest on loan from foreign subsidiary company	1,890
Employee salaries and emoluments	8,200
Specific bad debts	240
Exploration and drilling costs of oil wells	12,960
Contribution to approved pension schemes	720
Customs duties on drilling machines	1,500
General expenses	7,800
Petroleum oil tankers (ships)	1,800
Cost of generator	500
Intangible drilling cost	1,380
Administration expenses	750
Exploration costs	1,680
Pipeline and storage tank	16,920

Buildings-onshore-factory	5,400
Fixtures and fittings	630
Purchase of drilling machines	5,500

Required:

(i) Prepare a statement of taxable profit or loss of Turkanah Oil Ltd. for the year ended 31 December 2022.

(ii) Identify the clarifications that the tax authority may seek from the company concerning exploration and drilling costs.

✓ Answer for Question 2d

Particulars	**Sh. "million"**
Chargeable/Taxable Incomes:	
Proceeds from sale of oil	42,000
Value of chargeable oil disposed of to local refineries	21,000
Value of chargeable natural gas and other incomes	26,500
Freight charges received from other oil transport	22,800
Total Gross Income	**112,300**
Less: Allowable Deductions:	
Royalties paid for crude oil exported	(4,800)
Staff accommodation expenses	(2,820)
Royalties incurred for natural gas disposed of	(3,420)
Interest on loan from foreign subsidiary	(1,890)
Employee salaries and emoluments	(8,200)
Specific bad debts	(240)
Exploration and drilling costs of oil wells	(12,960)
Contribution to approved pension schemes	(720)
Intangible drilling cost	(1,380)
Administration expenses	(750)
Exploration costs	(1,680)
General expenses	(7,800)
Capital allowance(W1)	(15,873)
Adjusted Taxable Profit from Petroleum Operations	**49,767**

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Advanced Taxation

August 2023

Level: Advanced Level

Question 3a

 Taxation of cross border activities, Professional practice in taxation

Evaluate FOUR methods that multinational companies operating in Kenya can use in order to adjust transfer prices for purposes of computing taxable income as provided under the Transfer Pricing Rules (2006).

✓ Answer for Question 3a

The Kenyan Transfer Pricing Rules, 2006 (largely aligned with the OECD Guidelines), mandate that transactions between associated enterprises must be priced at Arm's Length Principle. This means the terms and conditions should be those that would have been agreed upon by independent enterprises in comparable circumstances.

To compute taxable income in compliance with this principle, MNCs can use the following prescribed methods to set and justify their transfer prices. The Rules do not prescribe a hierarchy, but the selection must be justified as the most appropriate.

Evaluation of Transfer Pricing Methods

1. Comparable Uncontrolled Price (CUP) Method

- **How it Works:** This method compares the price charged for property or services transferred in a controlled transaction to the price charged for comparable property or services in an uncontrolled transaction between independent parties.
- **Evaluation:**
  - **Advantages:** It is the most **direct and reliable** method when highly comparable uncontrolled transactions exist. It provides a clear benchmark and is strongly preferred by tax authorities if reliable data is available.
  - **Disadvantages:** Finding truly comparable transactions is often **difficult or impossible**. Differences in product quality, contractual terms, geographic markets, or timing can render comparisons unreliable. It is most suited for transactions involving generic commodities or well-defined services.

2. Resale Price Method

- **How it Works:** This method begins with the price at which a product purchased from an associated enterprise is resold to an independent enterprise. An appropriate gross margin (the "resale price margin") is then subtracted from this resale price. This margin is intended to cover the reseller's selling and operating expenses and provide an appropriate profit.

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Advanced Taxation

April 2023

Level: Advanced Level

Question 3b

 Limited companies

Saika Ltd. is a company engaged in real estate development. The company constructed eight, two-bedroomed residential houses for sale and three commercial buildings in different locations in the country.

The company has presented the following information relating to the properties development as at 31 December 2022:

Residential houses:

1. Cost of acquisition of land where the houses were constructed was Sh.10,000,000. The company had incurred the following costs in relation to land acquisition; stamp duty Sh.1,800,000, brokerage fees Sh.800,000 and legal fees to facilitate the purchase Sh.360,000.

2. The following costs were incurred on construction:

   - Material cost for each house was Sh.4,350,000 inclusive of value added tax (VAT) at a rate of 16%.
   - Architectural and surveying fee was Sh.1,624,000 inclusive of VAT. The company paid Sh.50,000 for each house to the county government for approval of the construction.
   - Professional fees for engineers amounted to Sh.3,480,000 inclusive of VAT.
   - Labour cost was Sh.400,000 for each house per month. It took the company nine months to complete the construction.
   - The construction was financed by Ujenzi Housing Bank with a loan of Sh.80,000,000 at an interest rate of 12% per annum. The loan was to be repaid at year end when all houses were sold. Only 70% of the loan was used on the houses. The balance was used to finance construction of the commercial buildings.
   - Drainage system and sewerage line cost Sh.960,000 for all houses.
   - The company leased equipment for construction at a total lease charge of Sh.2,000,000.

3. Other costs incurred included:

   - Cost of landscaping the entire land where the houses were constructed Sh.300,000.
   - Legal fees of Sh.180,000 to settle disputes in relation to the title deed of the land.

4. All the houses were sold by 31 December 2022 at a selling price of Sh.12,500,000 per house. The following costs were incurred in selling the houses:

   - Legal fees Sh.120,000 per house.

- Valuation fee for all houses Sh.1,200,000
- Advertising to find a buyer Sh.1,000,000 for all houses.

Commercial buildings:

- The commercial buildings were constructed at a total cost of Sh.30,000,000 each. This included shops at Sh.2,200,000, gym and steam bath Sh.1,450,000 and a swimming pool for the tenants at Sh.2,400,000.
- The commercial buildings were leased on 1 October 2022 at a monthly rent of Sh.1,200,000 each. Key money received on signing the lease agreement amounted to Sh.1,000,000 per building.
- The tenants were required to pay a monthly premium charge for extra services provided of Sh.200,000 per house.
- Maintenance expenses per month amounted to Sh.300,000.
- The company incurred advertising costs of Sh.400,000 of which Sh.120,000 was incurred before leasing the buildings.
- Installation of CCTV cameras cost. Sh.180,000 on each building and insurance for the whole year amounted to Sh.480,000 for all the buildings.

Required:

Compute the total taxable income and tax payable (if any) by Saika Ltd. for the year ended 31 December 2022.

✓ Answer for Question 3b

1. Residential Houses (Trading Stock – Sold during year)

Item	Sh.
Sales Revenue $12,500,000 \times 8$	100,000,000
Less: Cost of Sales	(85,040,000)
Gross Profit	14,960,000
Less: Selling Expenses (Allowable)	
Legal fees (selling) $120,000 \times 8$	(960,000)
Valuation fee	(1,200,000)
Advertising (selling)	(1,000,000)
Less: Finance Cost	
Interest 80,000,000×12%× 3 /12×70%	(1,680,000)
Trading Income (A)	**10,120,000**

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Advanced Taxation

December 2022

Level: Advanced Level

Question 4a

 Taxation of cross border activities

The African Growth and Opportunity Act (AGOA) is a United States Trade Act enacted in year 2000 as a legislation that significantly enhances market access to the United States for qualifying Sub-Sahara African countries. Analyse THREE conditions that the above countries must meet in order to qualify and be eligible for AGOA consideration.

✓ Answer for Question 4a

Analysis of AGOA Eligibility Conditions

The eligibility criteria for AGOA can be broadly categorized into **Mandatory Conditions** (explicitly stated in the law) and **Discretionary Conditions** (which the U.S. President considers). Failure to meet these conditions can lead to a country's suspension or termination from the program.

1. Mandatory Eligibility Requirements

These are non-negotiable conditions explicitly laid out in the AGOA legislation. A country **must** be making continuous progress toward each of these to qualify.

- **Establishment of a Market-Based Economy:** The country must be moving towards a economy where prices and production are determined by market forces, not government planning.
    - **What it entails:** Reduction of trade barriers, protection of private property rights, minimization of government interference in the economy, and establishment of a transparent and open rules-based trading system.
- **Rule of Law and Political Pluralism:** The country must have a political system that supports democratic principles.
    - **What it entails:** Fair and transparent elections, a functioning multi-party system, and laws that are applied equally to all citizens. This condition aims to combat corruption and nepotism.
- **Elimination of Barriers to U.S. Trade and Investment:** The country must work to remove unfair trade practices that disadvantage U.S. businesses.
    - **What it entails:** Lowering tariffs, eliminating non-tariff barriers (like complex quotas or standards), and providing adequate and effective intellectual property (IP) protection for U.S. companies.
- **Economic Policies to Reduce Poverty:** The country must implement policies that directly aim to improve the living standards of its poorest citizens.

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Advanced Taxation

August 2022

Level: Advanced Level

Question 4b

 Value added tax administration

Zawadi Associates provides consultancy services to various clients whose terms of contract allow clients to pay for the services either before or after the provision of the service. The following information is provided regarding the firm's transactions for the months of October, November and December in year 2021.

Nature of service	Value of service	Service provision date	Payment date
Audit services to XL Supermarkets	700,000	25 October 2021	5 November 2021
Training services to Kyle Securities	240,000	3 November 2021	Not yet paid
Accountancy services: Watoto Children's Home	600,000	5 December 2021	20 November 2021
Debt collection services to Zuwela Computers	820,000	9 November 2021	30 November 2021
Strategic Plan development: Bazo (Rwanda) Ltd.	2,150,000	10 November 2021	Not yet paid
Management consultancy: Sylok Investments	1,440,000	13 November 2021	40% paid on 13 November 2021
Internal controls reviewed: Lema Ltd.	960,000	18 November 2021	10% paid on 7 October 2021
Financial consultancy to W Ltd.	1,200,000	20 November 2021	1 December 2021

Additional information:

1. Sylok Investments was declared bankrupt on 30 November 2021.
2. On 5 November 2021, Zawadi Associates renewed its national industrial training license for Sh.30,000 and paid for legal fees Sh.360,000 to follow up on clients who were not paying as per the agreed date.
3. Electricity bill paid on 10 November 2021 was Sh.270,000 out of which Sh.100,000 was payment for outstanding bill for October 2021 and Sh.20,000 was in respect of additional deposits as demanded by the power company.

4. Fuel consumed for partners' vehicles amounted to Sh.90,000 during the month of November 2021.
5. Computers purchased for business use cost Sh.240,000 in November 2021.
6. Zawadi Associates paid rent for the month of November 2021 amounting to Sh.180,000 on 5 November 2021.
7. Transactions have been stated inclusive of VAT at the rate of 16% where applicable, unless otherwise stated.

Required:

(i) Compute the VAT payable by (or refundable to) Zawadi Associates for the month of November 2021.

(ii) Zawadi Associates is planning to engage a firm of financial management consultants from South Africa to facilitate online training on financial management assignments.

Advise Zawadi Associates on the tax point in respect of such services.

✓ Answer for Question 4b

(i) VAT Payable/Refundable for the Month of November 2021

Output VAT	**Sh.**
Training (Kyle Securities) 240,000 * 16/116	33,103
Accountancy (Watoto Home) 600,000 * 16/116	82,759
Debt Collection (Zuwela) 820,000 * 16/116	113,103
Strategic Plan (Bazo-Rwanda) 2,150,000 Export	0
Management Consult. (Sylok) 1,440,000*16/116	198,621
Financial Consult. (W Ltd.) 1,200,000*16/116	165,517
Lema Ltd. (90%*960,000)*16/116	119,172
Bad debt 1,440,000*16/116*60%	(119,172)
Total Output VAT	**593,103**

Input VAT	**Sh.**
Legal Fees 360,000 * 16/116	49,655
Electricity Bill (Net of Deposit) (270,000-20,000) * 16/116	34,483
Rent 180,000 * 16/116	24,828
Computer 240,000*16/116	33,103
Total Input VAT	**142,069**

VAT Payable (or Refundable) = 593,103 - 142,069 = 451,034

Zawadi Associates has a **VAT Payable** of **Sh. 451,034** for the month of November 2021.

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Advanced Taxation

April 2022

Level: Advanced Level

Question 4c

 Value added tax administration

Define the term "reverse charge" and indicate when it would apply (if at all) to Supa Bread Ltd.

✓ Answer for Question 4c

Definition of "Reverse Charge"

The **reverse charge** is a mechanism in Value Added Tax (VAT) where the **recipient (the buyer) of the goods or services is responsible for accounting for the VAT**, instead of the supplier.

Under a normal VAT transaction:

- The supplier charges VAT (output tax) and the customer claims it as input VAT (if eligible).

Under a **reverse charge**:

- The supplier does **not** charge VAT on the invoice.
- The recipient calculates the VAT that would have been due, declares it as their **output VAT**, and simultaneously claims it as their **input VAT** (if the service is used for making taxable supplies).
- The net effect on the VAT payable is often zero, but it ensures the transaction is recorded in the country where the service is consumed.

Application to Supa Bread Ltd.

The reverse charge mechanism **does apply** to Supa Bread Ltd. in the scenario provided.

When it applies:
It applies specifically to the **imported advisory services** billed at Sh. 1,000,000 (VAT inclusive) from the overseas company.

Reason for Application:

1. **Service is Imported:** The service provider is a non-resident company located outside Kenya.
2. **Recipient is in Kenya:** Supa Bread Ltd. is a VAT-registered business in Kenya and the recipient of the service.

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Advanced Taxation

December 2021

Level: Advanced Level

Question 5a

 Professional practice in taxation

As a tax manager at the revenue authority in your country, prepare a brief on the following:

(i) Process of being appointed a tax agent.

(ii) Requirements for recognition as a tax expert by the revenue authority.

✓ Answer for Question 5a

INTERNAL BRIEFING NOTE

To: All Staff, Compliance and Registration Departments
From: Tax Manager, [Name of Revenue Authority, e.g., Kenya Revenue Authority]
Date: 24th May 2024
Subject: Official Guidelines: Appointment of a Tax Agent and Recognition as a Tax Expert

Topic: Professional Practice in Taxation & Tax Systems and Policies

This brief outlines the official process and requirements for individuals seeking to act as formal representatives for taxpayers. Adherence to these guidelines ensures that only competent and reputable professionals are authorized, thereby enhancing voluntary compliance and the integrity of the tax system.

(i) Process of Being Appointed a Tax Agent

A Tax Agent is an individual or firm authorized by a taxpayer to act on their behalf in specified tax matters. The process is as follows:

1. **Prerequisite: Recognition as a Tax Expert:** The individual must first be recognized by the Revenue Authority as a **Tax Expert** (see requirements in section (ii) below). A firm must have at least one partner/director who is a recognized Tax Expert.
2. **Application by the Taxpayer (The Principal):**
    - The taxpayer seeking representation must complete the official **Appointment of Tax Agent Form** (e.g., KRA Form A).
    - The form must be signed by an authorized official of the taxpayer (e.g., Director for a company, sole proprietor for a business).
3. **Acceptance by the Proposed Tax Agent:**
    - The proposed Tax Agent must also sign the form, accepting the appointment and declaring that they meet the requirements to practice.

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Advanced Taxation

May 2021

Level: Advanced Level

Question 5b

 Taxation of cross border activities

Safari Aviators Ltd. is an air transport company registered in the United Kingdom. On their scheduled flights to East Africa, the company's planes land in Nairobi to connect passengers to other destinations in Africa. Ticketing and other transactions are done through an airline agent in Nairobi, Kenya, who would sell tickets and meet other necessary obligations on behalf of Safari Aviators Ltd.

The agent sold Sh.12,690,000 worth of tickets on behalf of the company in year 2020. The following expenses were incurred in carrying out airline operations in Kenya.

	Sh.
• Salaries for security officers	1,480,000
• Furniture for Agency offices	240,000
• Trade subscriptions	96,000
• Computers	180,000
• Purchase of Aircraft (UK) cost	126,000,000
• Jet fuel	4,900,000
• Covid-19 tests for staff members	148,000
• Upgrading Agency website	60,000
• Airline Authority clearance fees	360,000
• Purchase of saloon car	3,500,000

Additional information:

1. 15% of ticket sales are allowed annually by the Tax Authority in UK to cover for depreciation of other office equipment.
2. 2% of total ticket sales are allowed annually to cover head office expenses relating to the agency.
3. Operating expenses for the agency are allowed in full.
4. 5% of the investment allowance is allowable to the agent for tax purposes on investment in aircrafts.

Required:

(i) A statement of adjusted taxable income or loss for the year ended 31 December 2020.

(ii) Comment on any further information you may seek from the airline agency to facilitate accuracy of tax liability.

✓ Answer for Question 5b

(i) Statement of Adjusted Taxable Income (Loss) for the Year Ended 31 December 2020

Details	**Sh.**
Gross Receipts (Ticket Sales - Kenya Source)	12,690,000
DEDUCT: Allowable Expenses and Allowances	
Operating Expenses (Note 3: Allowed in Full)	
Salaries for security officers	(1,480,000)
Trade subscriptions	(96,000)
Jet fuel	(4,900,000)
Covid-19 tests for staff members	(148,000)
Upgrading Agency website	(60,000)
Airline Authority clearance fees	(360,000)
Head Office Expenses (Note 2) 2% of 12,690,000	(253,800)
Investment Allowance (Note 4) 5% of Aircraft Cost (126,000,000)	(6,300,000)
Wear and Tear Allowance (WTA):	
Computers 180,000@25%	(45,000)
Furniture for Agency offices 240,000@10%	(24,000)
Saloon car - Max 3,000,000@25%	(750,000)
Adjusted Taxable Loss	**(1,726,800)**

Note:**The WTA claimable on a saloon car (a non-commercial road vehicle used for passenger transport) is restricted to the cost of Sh. 3,000,000. Therefore, the WTA is 3,000,000 x 25% = 750,000.*