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CPA PART I SECTION 2

CS PART I SECTION 2

CIFA PART I SECTION 2

CCP PART I SECTION 2

PUBLIC FINANCE AND TAXATION

WEDNESDAY: 23 May 2018. **Time Allowed: 3 hours.**

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

Year of income 2017.

Monthly taxable pay (Sh.)			Annual taxable pay (Sh.)			Rate of tax % in each Sh.
1	-	11,180	1	-	134,164	10%
11,181	-	21,715	134,165	-	260,567	15%
21,716	-	32,249	260,568	-	386,970	20%
32,250	-	42,782	386,971	-	513,373	25%
Excess over	-	42,782	Excess over	-	513,373	30%

Personal relief Sh.1,280 per month (Sh.15,360 per annum)

Capital allowance:

Wear and tear allowance:

Class I	37.5%
Class II	30%
Class III	25%
Class IV	12.5%
Software	20%

Industrial building allowance:

Up to 2009	2.5%
From 1 January 2010	10%
Hotels	10%
Hostels/Education/Film producers buildings	100%
From 1 January 2010 - Commercial building: (Shop, office or show room)	25%
Farm works allowance	100%
Investment deduction allowance	100%
Shipping investment deduction (Ships over 125 tonnes)	100%

Extraction expenditure:

Written off over 5 years (20%)

Prescribed benefit rates of motor vehicles provided by employer

			Monthly rates (Sh.)	Annual rates (Sh.)
(i)	Saloons, Hatch Backs and Estates			
	Up to	1200 cc	3,600	43,200
	1201	1500 cc	4,200	50,400
	1501	1750 cc	5,800	69,600
	1751	2000 cc	7,200	86,400
	2001	3000 cc	8,600	103,200
	Over	3000 cc	14,400	172,800
(ii)	Pick-ups, Panel Vans (unconverted)			
	Up to	1750 cc	3,600	43,200
	Over	1750 cc	4,200	50,400
(iii)	Land Rovers/Cruisers		7,200	86,400

Commissioner's prescribed benefit rates

Services	**Monthly rates Sh.**	**Annual rates Sh.**
(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

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QUESTION ONE

(a) When the Cabinet Secretary for the National Treasury or equivalent ministry presents the Division of Revenue Bill to Parliament, it should be accompanied by a memorandum explaining various matters.

With reference to the above statement, identify four such matters. (4 marks)

(b) Outline six functions performed by the Controller of Budget in relation to public finance management. (6 marks)

(c) Summarise the steps that each public entity should follow under the e-procurement process. (10 marks)

(Total: 20 marks)

QUESTION TWO

(a) Identify four factors that are considered by the Commission on Revenue Allocation (CRA) or equivalent body while selecting marginalised counties for purposes of allocating the equalisation funds. (4 marks)

(b) Discuss three functions of the Council of Governors in county financial management. (6 marks)

(c) Mwanahawa Hamisi is a trader dealing in fast moving consumer goods and electronics. She is duly registered for value added tax (VAT). Details of her business transactions for the month of October 2017 were as follows:

1. Sales during the month:

	Sh.
Standard rate	1,900,000
Zero rated	418,000
Exempt	342,000

2. Customers for the sales at standard rate are offered a 15% discount if they settle within the same month. From past experience, 40% of the customers take advantage of the discount facility.
3. Purchases of goods constituted Sh.1,200,000 made at the standard rate and Sh.500,000 exempt. All the purchases are made in cash.
4. The exempt sales were all from the batch of exempt purchases with some remaining in inventory at the end of the month.
5. During the month, she paid rent for the business premises for the month of October and the remaining portion of the year. The landlord charges Sh.80,000 per month.
6. The business accountant wrote off debts amounting to Sh.280,000 as irrecoverable and made an allowance for specific irrecoverable debts of Sh.11,600 as the portion for that month.
7. During the month, a supplier from whom the business had made purchases of goods worth Sh.292,000 and a a customer to whom goods were sold at standard rate in July 2017 and still owed Sh.325,000 were declared bankrupt.
8. A pick-up vehicle was acquired at a cost of Sh.870,000 (inclusive of VAT) for business purposes.
9. At the end of every month, Mwanahawa prepays the electricity for the following month using prepaid meter tokens. This is done by establishing her standard usage for the following month. During the month, she paid Sh.42,500 whereas in the previous month she had paid Sh.38,500.
10. Other expenses paid during the month of October 2017 were as follows:

	Sh.
Telephone	13,200
Audit fee (Tax invoice including VAT)	111,070
Stationery	36,000

11. Mwanahawa made donations to registered charities consisting of Sh.100,000 in cash and Sh.280,000 in form of goods.
12. Closing inventory for the month was valued at Sh.340,000.

(All the above transactions are quoted exclusive of VAT at a rate of 16% where applicable unless otherwise stated).

Required:

The value added tax (VAT) payable by (or refundable to) Mwanahawa Hamisi for the month of October 2017. (10 marks)

(Total: 20 marks)

QUESTION THREE

(a) Distinguish between "objection" and "appeal" as used in administration of income tax. (4 marks)

(b) Outline four disadvantages of a multiple tax system. (4 marks)

(c) Bonface Huka is a resident individual and a qualified pharmacist who has been employed by Sawa Hospital since his early retirement from the public service in 2016.

The following details were availed to you in respect of his earnings for the year ended 31 December 2017:

1. He received a monthly basic salary of Sh.184,000 from Sawa Hospital. Additional one month's basic salary was paid to him in December 2017 as a bonus. PAYE deducted during the year was Sh.897,600.
2. Pension received from the public service was Sh.540,000 as a lumpsum amount.
3. A commission of Sh.199,000 was paid to him for the promotion of drugs under identified brands during the year.
4. During the year, he was sent to Mombasa for a four day medical conference and was paid daily subsistence allowance of Sh.18,000 by the hospital.
5. He has a fixed deposit account of Sh.1,500,000 at the Broad Bank Ltd. from which he received an interest of Sh.105,000 during the year.
6. He has a life insurance policy where he contributes 40% of the premiums, while the employer contributes 60%. Annual premiums as per the insurance policy during the year was Sh.460,000.
7. He was provided with a saloon car of 2000 cc by the hospital for personal and official duties on 1 July 2017. The saloon car had an initial cost of Sh.2,800,000.
8. The hospital has a medical cover for all staff. He was entitled to a maximum cover of Sh.180,000 per annum while he utilised Sh.74,000 on medical bills during the year.
9. During the year, he was provided with a house. The market value of the house was Sh.120,000 per month and he contributed Sh.20,000 per month as nominal rent.
10. During the year, the hospital settled his bills as follows: telephone Sh.68,000, water Sh18,200 and electricity Sh.24,600.
11. The hospital contributed 5% of his basic salary towards a registered pension scheme while he contributed an equal amount to the scheme.
12. The hospital paid subscription fees on his behalf to the Pharmacy and Poisons Board amounting to Sh.54,000 during the year.
13. He was reimbursed private entertainment expenses of Sh.120,000 by the hospital during the year.

Required:

(i) Taxable income for Bonface Huka for the year ended 31 December 2017. (10 marks)

(ii) Tax payable (if any) on the income computed in (c)(i) above. (2 marks)

(Total: 20 marks)

QUESTION FOUR

(a) The following information was extracted from the books of Fanaka Ltd. for the year ended 31 December 2017:

	Sh.
Sales	4,800,000
Purchases	1,100,000
Bad debts recovered	540,000
Rent received (commercial premises)	280,000
Dividends received (Mkopo Ltd.)	100,000 (net)
Interest received (Hekima Bank Ltd.)	340,000 (net)
Discount allowed	54,000
Discount received	133,000
Salaries	960,000
Electricity	180,000
Advertising	395,000
Provision for bad debts	45,000
Subscriptions to a trade association	65,000
Audit fees	168,000
Legal fees	139,500
Car hire expenses	420,000
Purchase of machinery	1,600,000
Loss of stock	530,000
Installation of machinery	42,000
Foreign exchange gain (realised)	232,000
Donations to a political party	1,050,000
General expenses	52,000

Additional information:

1. Opening stock and closing stock were valued at Sh.912,000 and Sh.840,000 respectively.
2. Included in the sales figure was a sale of Sh.928,000 that was inclusive of VAT at the rate of 16%, while the other sales were recorded net of VAT.
3. Advertising includes an amount of Sh.195,000 spent in the erection of a bill board.
4. Loss of stock includes Sh.120,000 relating to insured stock.

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5. Two thirds of the bad debts recovered relate to bad debts which were previously written off from the company's books.
6. Legal fees relate to the following:

	Sh.
Conveyance of land	42,000
Trade dispute	27,000
Breach of contract	36,500
Preparation of employment contracts	34,000

Required:
Adjusted taxable income for Fanaka Ltd. for the year ended 31 December 2017. (8 marks)

(b) Zuret Products Ltd. which is engaged in the business of manufacturing and selling of canned fish commenced its operations on 1 January 2014 after incurring the following expenditure:

	Sh.
Land	4,800,000
Processing machinery	3,200,000
Factory buildings	2,800,000
Staff canteen	860,000
Generator	250,000
Labour quarters	3,600,000
Staff clinic	960,000

Details of property, plant and equipment schedule reflected the following as at 31 December 2017:

Assets	Written Down Value 1 January 2017	Additions during the year (at cost)	Depreciation for the year	Disposal proceeds during the year
	Sh.	Sh.	Sh.	Sh.
Computers	525,000	345,400	131,250	250,000
Water pump	-	280,000	56,000	-
Furniture	360,000	140,000	82,000	-
Conveyor belts	-	960,000	-	-
Delivery vans	2,500,000	1,420,000	180,000	620,000
Cash registers	620,000	-	58,000	-
Printers	120,000	60,000	42,000	-
Tractors	2,500,000	1,800,000	360,000	-
Motorcycles	380,000	-	68,000	-
Packaging machine	-	860,000	-	-
Non-processing machinery	960,000	-	62,000	-

Additional information:
1. A perimeter wall was constructed at a cost of Sh.960,000 during the year ended 31 December 2017.
2. A godown and a drainage system were constructed at a cost of Sh.2,860,000 and Sh.1,780,000 respectively and put into use on 1 October 2017.
3. The company constructed a borehole at a cost of Sh.1,500,000 during the year which was put in use on 1 July 2017.

Required:
Capital allowances due to Zuret Products Ltd. for the year ended 31 December 2017. (12 marks)
(Total: 20 marks)

QUESTION FIVE

(a) Highlight four circumstances under which duty paid on imported goods may be refunded by the commissioner. (4 marks)

(b) Argue four cases against capital gains tax or equivalent tax in your country. (4 marks)

(c) Chege and Telek have been partners trading as Chetel Traders. On 1 September 2017, they admitted Lopez in the business and changed the partnership name to Chetelop Traders. Prior to the admission of Lopez, the profit and loss sharing ratio was 2:3 between Chege and Telek respectively. However, with the admission of Lopez, they revised the profit and loss sharing ratio to 2:3:1 for Chege, Telek and Lopez respectively.

The partners have presented the following income statement for the year ended 31 December 2017:

Income	**Sh.**	**Sh.**
Gross profit		4,500,000
Foreign exchange gain		234,000

	Sh.	Sh.
Interest on bank deposit (net)		90,000
Insurance compensation for stolen vehicle		300,000
Profit on disposal of computers		160,000
		5,284,000
Expenditure		
General expenses	2,625,000	
Salaries and wages	1,800,000	
Interest on capital: Chege	120,000	
Telek	105,000	
Lopez	22,500	
Legal expenses	365,625	
Loss on sale of assets	11,400	
Stamp duty on lease agreements	6,120	
Licenses and permits	10,800	
Subscriptions to trade association	42,000	
Conveyance fees	112,500	
Rent and rates	180,000	
Mortgage interest	180,000	
Repairs on computers	45,000	
Furniture purchased (cost)	63,000	
Bank charges	60,000	
Repair and maintenance	560,000	
Bad and doubtful debts	123,750	
Depreciation	193,400	(6,626,095)
Net profit (loss)		(1,342,095)

Additional information:

1. General expenses comprise:

	Sh.
Embezzlement by a cashier	900,000
Staff christmas party	600,000
Replacement of car engine	105,000
Partition of an office	450,000
Partners private insurance policy	570,000

2. Salaries and wages include Sh.525,000, Sh.600,000 and Sh.235,000 paid to Chege, Telek and Lopez respectively.
3. Mortgage interest relates to a partner's residential house.
4. Assume that the income accrued evenly throughout the year.
5. Legal expenses comprise:

	Sh.
Parking fines paid to county government	11,400
Legal fees for breach of contract	150,000
Drafting a tender document	13,500
Drafting a lease agreement (100 years)	6,750
Defending a partner in a tax case	9,000
Legal cost of debt collection	174,975

6. Repair and maintenance costs comprise:

	Sh.
Purchase of weighing scale	252,000
Installation of CCTV cameras	224,000
Fixing a leaking roof	84,000

7. Bad and doubtful debts comprise:

	Sh.
Specific bad debts	74,250
General provision	49,500

8. Capital allowance was agreed with the commissioner of revenue authority at Sh.260,800.

Required:

(i) Adjusted taxable profit or loss for the partnership for the year ended 31 December 2017. (8 marks)

(ii) Allocation of profit or loss to the partners. (4 marks)

(Total: 20 marks)

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