



**kasneb**

**ATD LEVEL III**

**DCM LEVEL III**

**PRINCIPLES OF PUBLIC FINANCE AND TAXATION**

**WEDNESDAY: 27 November 2019.**

**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 2018.**

Monthly taxable pay (Sh.)		Annual taxable pay (Sh.)		Rate of tax % in each Sh.
1	- 12,298	1	- 147,580	10%
12,299	- 23,885	147,581	- 286,623	15%
23,886	- 35,472	286,624	- 425,666	20%
35,473	- 47,059	425,667	- 564,709	25%
Excess over	- 47,059	Excess over	- 564,709	30%

**Personal relief Sh.1,408 per month (Sh.16,896 per annum).**

**Prescribed benefit rates of motor vehicles provided by employer**

	Monthly rates (Sh.)	Annual rates (Sh.)
<b>Capital allowance:</b>		
<b>Wear and tear allowance:</b>		
Class I	37.5%	
Class II	30%	
Class III	25%	
Class IV	12.5%	
Software	20%	
<b>Industrial building allowance:</b>		
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%	
<b>Farm works allowance</b>	100%	
<b>Investment deduction allowance</b>	100%	
<b>Shipping investment deduction (Ships over 125 tonnes)</b>	100%	
(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

**Extraction expenditure:**

Written off over 5 years (20%)

**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
<b>Agriculture employees: Reduced rates of benefits</b>		
(i) Water	200	2,400
(ii) Electricity	900	10,800

### QUESTION ONE

- (a) Explain the meaning of the following terms as used in public finance management:
- (i) Contingencies fund. (2 marks)
  - (ii) Intergovernmental budget and economic council. (2 marks)
  - (iii) Recurrent expenditure. (2 marks)
- (b) The responsibilities of the National Treasury with respect to the budget process include preparing annual budget policy statement.
- In light of the above statement, outline three aspects that should be included in the budget policy statement. (6 marks)
- (c) Summarise two similarities based on responsibilities of the following two tiers of government in relation to budget making process:
- (i) The National Treasury and the County Treasury. (4 marks)
  - (ii) The National Assembly and the County Assembly. (4 marks)
- (Total: 20 marks)**

### QUESTION TWO

- (a) The internal audit function plays a vital role in public sector governance. In relation to public finance management, evaluate four roles of the internal audit department or such similar agency in your country. (4 marks)
- (b) Explain the following types of tax assessments:
- (i) Self-assessment. (2 marks)
  - (ii) Default assessment. (2 marks)
  - (iii) Advance assessment. (2 marks)
- (c) The following transactions took place during the month of December 2018 in respect to the operations of Blue Ltd., a company registered for value added tax (VAT) purposes:

	Sh.
Sales at standard rate	12,000,000
Sales at zero rate	2,400,000
Exempt sales	700,000
Purchases at zero rate	1,200,000
Purchases at standard rate	9,600,000
Audit fees	128,000
Legal fees	94,000
Electricity	36,000
Export sales to Zambia	560,000

#### Additional information:

1. The company received credit notes for Sh.40,000 in respect to goods returned to suppliers and debit notes for Sh.28,000 from suppliers.
2. Purchases at standard rate included:
  - Catering services for Sh.140,000.
  - Spare parts for director's official car for Sh.160,000.
  - Hire of motor vehicles for Sh.60,000.
3. The company issued credit notes to customers worth Sh.140,000 in respect to goods sold at standard rate.
4. A debtor of goods valued at Sh.80,000 was declared bankrupt and the commissioner granted bad debt relief in the same month of December 2018.
5. Exempt supplies are not identifiable from taxable supplies.

All transactions are exclusive of VAT. The VAT is at the rate of 16% where applicable.

**Required:**

For the month of December 2018, compute for Blue Ltd:

- (i) Input tax. (5 marks)
- (ii) Output tax. (3 marks)
- (iii) VAT payable or refundable. (2 marks)
- (Total: 20 marks)**

**QUESTION THREE**

(a) Discuss four reasons that could cause the differences between "accounting profit" and "taxable profit". (8 marks)

(b) Kevin Rono works as a production manager of a leading biscuit manufacturing company. He has provided the following information relating to his income for the year ended 31 December 2018:

1. Basic salary of Sh.160,000 per month (PAYE Sh.44,000 per month).
2. He is living in a rented house where he pays a monthly rent of Sh.40,000. The company pays him Sh.50,000 per month as house allowance.
3. During the year, his son was admitted in a private university and the company paid school fees amounting to Sh.240,000. This amount was disallowed for tax purposes in the company's books of accounts.
4. He is a member of a registered pension scheme where he contributes Sh.25,000 per month with the employer contributing an equal amount for him.
5. He was provided with a saloon car of 2,500cc on 1 July 2018 which had cost the company Sh.2,950,000.
6. The company catered for his telephone bills and he was reimbursed Sh.48,500 during the year for the bills.
7. The company has a medical scheme that covers all the senior managers. During the year, the company paid Sh.380,000 as medical bills in respect of his wife's illness.
8. Kevin Rono is a member of a Home ownership saving plan and he contributes Sh.25,000 per month.
9. During the year he was declared the best employee and the company rewarded him with Sh.90,000. He was also entitled to a monthly entertainment allowance of Sh.18,000 with effect from 1 October 2018.
10. Interest on infrastructure bonds that he received during the year was Sh.108,000. In addition to that, he earned an interest of Sh.76,000 (net withholding tax) on fixed deposit from the Bank of Ceylon.
11. He received the following dividend income during the year:
 

	Sh.
Uwezo Ltd.	75,000 (net)
Zawadi Co-operative Society	150,000 (gross)
12. The employer contributed for him Sh.9,000 per month towards his children's education insurance policy.

**Required:**

- (i) Taxable income of Kevin Rono for the year of income 2018. (10 marks)
- (ii) Tax payable on the computed income in (b) (i) above if any. (2 marks)
- (Total: 20 marks)**

**QUESTION FOUR**

(a) Kalashaka Ltd., commenced manufacturing business on 2 January 2018 after incurring the following expenditure:

Assets	Cost (Sh)
Factory building	4,800,000
Processing machinery	3,900,000
Tractors	2,000,000
Computers	800,000
Partitions	400,000
Scanners	300,000
Staff quarters	525,000
Saloon car	1,800,000
Sports pavillion	612,000
Photocopiers	250,000

**Additional information:**

1. The following assets were acquired during the year:

Date	Asset	Cost (Sh.)
1 March	Computers	400,000
4 May	Saloon cars (two)	2,200,000 (each)
24 July	Trailer	400,000
13 October	Lorry (4 tonnes)	1,200,000
19 November	Curtains and carpets	100,000

2. The following assets were disposed of during the year:
- | Date        | Asset      | Original cost (Sh.) | Sales proceeds (Sh.) |
|-------------|------------|---------------------|----------------------|
| 2 June      | Computer   | 120,000             | 80,000               |
| 5 August    | Saloon car | 1,800,000           | 735,000              |
| 9 September | Tractor    | 700,000             | 450,000              |
3. Not included in the cost of assets at commencement is import duty on processing machinery and computers amounting to Sh.360,000 and Sh.186,000 respectively.
4. A flat-screen colour television was acquired for Sh.195,000 and affixed in the company's waiting lounge.

**Required:**

Capital allowance due to Kalashaka Ltd. for the year ended 31 December 2018.

(10 marks)

- (b) The management of Angaza Ltd. Has presented the following income statement for the year ended 31 December 2018:

	Sh.	Sh.
Gross profit		12,800,000
Import duty refund		4,500,000
Discount received		200,000
Foreign exchange gain		342,000
Insurance compensation		2,500,000
Gain on sale of motor vehicles		<u>180,000</u>
		20,522,000
<b>Expenditure</b>		
Stationery and postage	920,000	
Amortisation of goodwill	360,000	
Interest on bank overdrafts	130,000	
Legal fees	1,580,000	
Depreciation	240,000	
Licenses and permits	284,000	
Loss on sale of financial assets	168,000	
Conveyance fees	348,000	
General expenses	1,980,000	
Stamp duty	150,2000	
Rent and rates	<u>280,000</u>	(6,440,200)
Net profit		<u>14,081,800</u>

**Additional information:**

- The insurance compensation relates to the amount received from Haki Insurance Company Ltd. as compensation for the company's stolen motor vehicle.
- Rent and rates includes Sh.120,000 for the month of January and February 2019.
- Legal fees comprised the following:

	Sh.
Drafting a 100 year's lease agreement	420,000
Facilitating collection of debts from customers	140,000
Compensation for breach of a contract	280,000
City County parking fees for the company	82,000
Preparation of tender documents	550,000
Drafting of loan agreements with banks	<u>108,000</u>
	<u>1,580,000</u>

4. General expenses comprised the following:

	Sh.
Office partitions	360,000
Cost of relocating to the new offices	170,000
Director's christmas party	480,000
Repairs on machinery	250,000
Redundancy payments to employees	300,000
Compensation to insured employee while on duty	<u>420,000</u>
	<u>1,980,000</u>

**Required:**

Adjusted taxable profit or loss for Angaza Ltd. for the year ended 31 December 2018.

(10 marks)

(Total: 20 marks)

**QUESTION FIVE**

- (a) Summarise four advantages of multiple tax systems over a single tax system. (4 marks)
- (b) Explain four circumstances under which duty paid on imports is refundable to an importer. (4 marks)
- (c) Unity Traders is a multi-business partnership of three brothers Abel, Ben and Charles. The partners share the profits and losses equally.

The following is the income statement for the partnership business for the year ended 31 December 2018:

	Sh.	Sh.
Gross profit		14,000,000
<b>Other income:</b>		
Profit on sale of machinery		1,780,000
Discount received		960,000
Interest from Abel on overdue account		620,000
VAT refund		82,000
Interest from bank savings		<u>240,600</u>
		17,682,600
<b>Less expenses:</b>		
Salaries and wages	2,300,000	
Sundry expenses	4,200,000	
Office rent	320,000	
Medical expenses	1,250,000	
Depreciation	480,000	
Donations to a charity walk	620,000	
Income tax	96,000	
Drawings by Ben	140,600	
Specific provision for bad debts	280,000	
Interest on capital:		
Abel	100,000	
Ben	175,000	
Charles	140,000	
Repairs and maintenance	520,000	
Loan repayment	<u>1,200,000</u>	<u>(11,821,600)</u>
Net profit		<u>5,861,000</u>

**Additional information:**

1. The office rent was paid to the partners who owned the building.
2. Salaries and wages include salaries paid to partners as follows:
 

	Sh.
Abel	650,000
Charles	520,000
Ben	480,000
3. Half of medical expenses were incurred for the treatment of the partners and their families.
4. Sundry expenses comprised of the following:
 

	Sh.
Conveyance fee for purchase of land	800,000
Settling customer disputes	720,000
General provision for bad debts	880,000
Drafting tender documents	440,000
Parking fines paid to county authority	220,000
Drafting lease documents (90 years lease)	140,000
5. Capital allowances were agreed with the commissioner of tax at Sh.284,000.

**Required;**

- (i) Adjusted taxable profit or loss for the partnership for the year ended 31 December 2018. (8 marks)
- (ii) A schedule showing the allocation of the adjusted profit or loss in (c) (i) above. (4 marks)

**(Total: 20 marks)**

.....