

KASNEB

ATD LEVEL III

DCM LEVEL III

PRINCIPLES OF PUBLIC FINANCE AND TAXATION

TUESDAY: 24 May 2016.

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 2015.

| 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 | Excess over - 466,704 | 30% |

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

Prescribed benefit rates of motor vehicles provided by employer

| | Monthly rates (Sh.) | Annual rates (Sh.) |
|--|---|-----------------------|
| Capital allowance: | | |
| Wear and tear allowance: | | |
| Class I | 37.5% | |
| Class II | 30% | |
| Class III | 25% | |
| Class IV | 12.5% | |
| Software | 20% | |
| | (i) Saloons, Hatch Backs and Estates | |
| | Up to 1200 cc | 3,600 |
| | 1201 - 1500 cc | 4,200 |
| | 1501 - 1750 cc | 5,800 |
| | 1751 - 2000 cc | 7,200 |
| | 2001 - 3000 cc | 8,600 |
| | Over 3000 cc | 14,400 |
| | (ii) Pick-ups, Panel Vans (unconverted) | |
| | Up to 1750 cc | 3,600 |
| | Over 1750 cc | 4,200 |
| | (iii) Land Rovers/Cruisers | 7,200 |
| 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%)

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 |

QUESTION ONE

- (a) The Cabinet Secretary for the National Treasury or the State Officer responsible for finance in your country is mandated by law to manage the national budget process. In relation to this function, he issues a circular setting guidelines to be followed to all government entities.

With reference to the above statement, outline four contents of such a circular. (4 marks)

- (b) In managing the national government public finances, the National Treasury or such state organ in your country enforces certain fiscal responsibility principles in accordance with the constitution and the Public Finance Management Act.

In relation to the above statement, explain four fiscal responsibility principles. (8 marks)

- (c) In relation to Public Finance Management, distinguish between the following set of terms:

(i) "Capital expenditure" and "Recurrent expenditure". (4 marks)

(ii) "Eurobond" and "Treasury bond". (4 marks)

(Total: 20 marks)

QUESTION TWO

- (a) Explain the term "Finance Bill" as provided under the Public Finance Management Act. (2 marks)

- (b) Effective oversight and monitoring are crucial to sound governance and Public Finance Management.

With reference to the above statement, discuss four roles of internal audit. (8 marks)

- (c) The Public Finance Management Act requires both the County governments and National government to engage the public in the budget process.

Highlight six advantages of public participation in the County budgeting process. (6 marks)

- (d) State four sources of revenue for County governments apart from the share of revenue from the National government. (4 marks)

(Total: 20 marks)

QUESTION THREE

- (a) Identify three omissions that constitute pay as you earn (PAYE) offences. (3 marks)

- (b) Summarise four challenges faced by the customs department within the East African Community in an effort to improve customs administration. (4 marks)

- (c) James Bekele practises crop and livestock farming. He has provided the following income statement summary for the year ended 31 December 2015:

| Revenue | Sh. | Sh. |
|-------------------------------------|---------|------------------|
| Sale of milk to Maziwa Ltd. | | 642,000 |
| Sale of onions | | 517,200 |
| Sale of mutton and chicken | | 780,000 |
| Sale of tomatoes | | <u>1,200,000</u> |
| Total revenue | | <u>3,139,200</u> |
| Expenditure | | |
| Fertilizers | 40,000 | |
| Pesticides | 15,000 | |
| Seeds | 45,000 | |
| Planting onions and tomatoes | 80,000 | |
| Motor vehicle expenses | 120,000 | |
| Insurance for the farm | 15,000 | |
| Crops destroyed by hailstones | 25,000 | |
| Salaries and wages | 75,000 | |
| Animal feeds | 15,000 | |
| Trade fair expenses | 6,000 | |
| Electricity and water | 5,000 | |
| Subscription to Kenya football club | 18,000 | |
| Purchase of chicks | 52,000 | |

| | | |
|-----------------------------------|---------------|------------------|
| | Sh. | Sh. |
| Value of sheep killed by hyenas | 12,000 | |
| Depreciation of motor vehicles | 15,000 | |
| Life insurance cover | 22,000 | |
| Bad debts written off | 8,000 | |
| Repairs on daily sheds and fences | 3,000 | |
| Loan interest (Mkulima SACCO) | 8,000 | |
| Loan repayment (Mkopo Bank) | 120,000 | |
| Construction of dogs kennels | 15,000 | |
| Construction of water tank | <u>17,200</u> | <u>(731,200)</u> |
| Net profit for the year | | <u>2,408,000</u> |

Additional information:

1. James Bekele is a member of Wakulima Cooperative Society in which he received a dividend of Sh.85,000 (net) during the year.
2. Insurance for the farm includes James Bekele's wife personal cover of Sh.8,000.
3. Salaries and wages includes Sh.35,000 paid to James Bekele's househelp.
4. Capital allowance has been agreed with the Commissioner of Income Tax to be Sh.86,000.

Required:

- (i) Taxable income for James Bekele for the year ended 31 December 2015. (10 marks)
 - (ii) Tax payable or refundable on the income computed in (c)(i) above. (3 marks)
- (Total: 20 marks)**

QUESTION FOUR

- (a) The following information was obtained from the books of Betatech Ltd., a manufacturing company for the year ended 31 December 2015:

1. The written down values of the various assets as at 1 January 2015 were as follows:

| | |
|---------------------------|------------|
| | Sh. |
| Motor vehicles (Pick-ups) | 1,720,000 |
| Fax machine | 140,000 |
| Office curtains | 38,000 |
| Tractor | 2,800,000 |
| Wheelbarrows | 120,000 |
| Cellphones | 82,000 |
| Computers | 158,000 |
| Furniture and fittings | 246,000 |
| Combine harvester | 1,380,000 |

2. The following assets were purchased and utilised with effect from 1 July 2015:

| | |
|--------------------------|------------|
| | Sh. |
| Processing machinery | 400,000 |
| Trailer for tractor | 380,000 |
| Saloon car | 2,800,000 |
| Sewerage treatment plant | 1,200,000 |

3. The company disposed of the following assets on 1 July 2015:

| Asset | Disposal proceed |
|------------------------|-------------------------|
| | Sh. |
| Fax machine | 48,000 |
| Furniture and fittings | 124,000 |
| Computers | 82,500 |

4. The company constructed the following structures during the year which were utilised from 1 October 2015:

| | |
|------------------|------------|
| | Sh. |
| Factory building | 4,600,000 |
| Staff canteen | 1,800,000 |
| Sports pavilion | 680,000 |
| Parking bay | 420,000 |

5. The factory building includes a showroom and an office block constructed at a cost of Sh.600,000 and Sh.420,000 respectively.
6. The company sunk a borehole at a cost of Sh.1,280,000 which was put in use on 1 November 2015.

Required:

Capital allowances due to Betatech Ltd. for the year ended 31 December 2015. (10 marks)

- (b) The following information was extracted from the books of Juakali Ltd. for the month of February 2016:

Cash book Extract

| Date | Details | Sh. | Date | Details | Sh. |
|---------|-------------------------|------------------|---------|-----------------------------|------------------|
| 1/2/16 | Balance brought forward | 120,000 | 3/2/16 | Cash purchases | 200,000 |
| 2/2/16 | Cash sales | 560,000 | 6/2/16 | Cash purchases | 120,000 |
| 6/2/16 | Cash sales | 750,000 | 8/2/16 | Cash purchases | 240,000 |
| 15/2/16 | Cash sales | 420,000 | 9/2/16 | Electricity bill | 34,000 |
| 23/2/16 | Cash sales | 360,000 | 15/2/16 | Payment – January purchases | 45,000 |
| 25/2/16 | Refund from customer | 240,000 | 19/2/16 | Salary and wages | 520,000 |
| 28/2/16 | Cash sales | 280,000 | 27/2/16 | Sales Commission | 50,000 |
| | | | 27/2/16 | Audit fees | 80,000 |
| | | | 28/2/16 | Balance carried down | <u>1,441,000</u> |
| | | <u>2,730,000</u> | | | <u>2,730,000</u> |

Additional information:

1. Sales were made up of standard, zero-rated and exempt sales in the ratio of 3:2:1 respectively.
2. Sales invoices omitted for goods sold at standard rate for the month of February 2016 amount to Sh.1,500,000.
3. Refund from customers included bad debts recovery of Sh.72,000 which was previously written off and VAT refund claimed and Sh.168,000 being an amount deposited to a customer bank account erroneously.
4. Electricity bill paid relates to months of January and February 2016 and were incurred equally. 25% of the bill relates to domestic use.
5. Credit notes of Sh.35,000 were sent to customers. This relates to goods sold at standard rate.
6. Bad debts written off during the month amount to Sh.24,000.
7. Sales return by customers of goods sold at standard rate amount to Sh.450,000.

The above transactions are stated exclusive of VAT unless otherwise stated.

Required:

A value added tax (VAT) account for the month of February 2016 for Juakali Ltd. (10 marks)
(Total: 20 marks)

QUESTION FIVE

- (a) Outline four reasons why the incidence of tax is important to policy makers in your country. (4 marks)
- (b) List four documents that must accompany an application for a bad debt relief or a refund in the case of VAT. (4 marks)
- (c) The management of Hekima Ltd. has presented the following statement of comprehensive income for the year ended 31 December 2015:

| | Sh. | Sh. |
|--|-----|---------------|
| Gross profit | | 3,980,000 |
| Other income | | |
| Discount received | | 120,000 |
| Gain on sale of equipment | | 82,000 |
| Interest from Biashara Bank Ltd. (net) | | 51,000 |
| Refund of import duty | | 28,000 |
| Gain on foreign exchange transactions (realised) | | <u>49,200</u> |
| Total revenue | | 4,310,200 |

| | Sh. | Sh. |
|-----------------------|----------------|--------------------|
| Expenses: | | |
| Property rates | 112,000 | |
| Insurance | 48,600 | |
| NSSF Contributions | 150,000 | |
| Depreciation | 132,500 | |
| Salaries and wages | 240,000 | |
| Goodwill amortisation | 122,300 | |
| Advertising | 342,000 | |
| Legal fees | 142,000 | |
| Travelling expenses | 180,600 | |
| Donations | 156,200 | |
| General expenses | 426,000 | |
| Bad debts | 176,800 | |
| Furniture | 280,000 | |
| Corporation tax | <u>242,800</u> | <u>(2,751,800)</u> |
| Net profit | | <u>1,558,400</u> |

Additional information:

- Donations relate to the amounts donated to a trade association.
- Legal fees comprised the following:

| | Sh. |
|--|----------------|
| Acquisition of a bank loan | 42,000 |
| Settling customer disputes | 34,000 |
| Conveyance fee for purchase of land | 60,000 |
| Preparation of a Memorandum of Association | <u>6,000</u> |
| | <u>142,000</u> |

- General expenses include:

| | Sh. |
|---|----------------|
| Golden handshake to a retiring director | 220,000 |
| Directors emoluments | 172,000 |
| Christmas gifts to staff | <u>34,000</u> |
| | <u>426,000</u> |

- Advertising expenses include Sh.125,000 spent on acquisition of a neon sign.

- Bad debts comprised the following:

| | Sh. |
|----------------------------------|----------------|
| General provisions for bad debt | 32,800 |
| Embezzlement by the cashier | 117,600 |
| Specific provisions for bad debt | <u>26,400</u> |
| | <u>176,800</u> |

- It is estimated that 15% of the travelling expenses relate to private usage of company motor vehicles by the directors.

Required:

- Adjusted taxable profit or loss for Hekima Ltd. for the year ended 31 December 2015. (10 marks)
- Tax payable by Hekima Ltd. (if any) for the year ended 31 December 2015 from the adjusted income in (c)(i) above. (2 marks)

(Total: 20 marks)

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