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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: 19 May 2021.

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 2020.

Assume that the following rates of tax applied throughout the year of income 2020:

Monthly taxable pay (Sh.)	Annual taxable pay (Sh.)	Rate of tax % in each Sh.
1 - 24,000	1 - 288,000	10%
24,001 - 40,667	288,001 - 488,000	15%
40,668 - 57,334	488,001 - 688,000	20%
Excess over - 57,334	Excess over - 688,000	25%

Personal relief Sh.2,400 per month (Sh.28,800 per annum).

Investment allowance:	Rate of investment allowance	Residual value (per year on reducing balance)	Prescribed benefit rates of motor vehicles provided by employer
Capital expenditure incurred on:			(i) Saloons, Hatch Backs and Estates
			Monthly rates (Sh.) Annual rates (Sh.)
(a) Buildings:			Up to 1200 cc 3,600 43,200
• Hotel building	50% in the first year of use	25%	1201 - 1500 cc 4,200 50,400
• Building used for manufacture	50% in the first year of use	25%	1501 - 1750 cc 5,800 69,600
• Hospital buildings	50% in the first year of use	25%	1751 - 2000 cc 7,200 86,400
• Petroleum or gas storage facilities	50% in the first year of use	25%	2001 - 3000 cc 8,600 103,200
• Educational/hostels building	10% per year on reducing balance		Over - 3000 cc 14,400 172,800
• Commercial building	10% per year on reducing balance		
(b) Machinery:			(ii) Pick-ups, Panel Vans (unconverted)
• Machinery used for manufacture	50% in the first year of use	25%	Up to - 1750 cc 3,600 43,200
• Hospital equipment	50% in the first year of use	25%	Over - 1750 cc 4,200 50,400
• Ships or aircraft	50% in the first year of use	25%	
• Motor vehicles and heavy earth moving equipment	25% per year on reducing balance		
• Computer software, calculators, copiers and duplicating machines	25% per year on reducing balance		
• Furniture and fittings	10% per year on reducing balance		
• Telecommunication equipment	10% per year on reducing balance		
• Film equipment by a local producer	25% per year on reducing balance		
• Machinery used to undertake operations under prospecting rights and exploration under mining rights	50% in the first year of use	25%	
• Other machinery	10% per year on reducing balance		
(c) Purchase/acquisition of right to use fibre optic cable by telecommunication operation	10% per year on reducing balance		(iii) Land Rovers/Cruisers 7,200 86,400
(d) Farm works	50% in the first year of use	25%	

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) Summarise four functions of the National Assembly budget committee as per the Public Finance Management Act, 2012. (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. (8 marks)
- In relation to the above statement, explain four fiscal responsibility principles. (4 marks)
- (c) Citing their information needs, identify four users of the Consolidated Fund reports. (4 marks)
- (d) Highlight four responsibilities of a County Treasury with respect to county public funds. (4 marks)
- (Total: 20 marks)**

QUESTION TWO

- (a) Outline six functions of a disposal committee as provided under the Public Procurement and Asset Disposal Act 2015. (6 marks)
- (b) In a tax seminar, one of the facilitators noted that "Most revenue authorities in developing countries are embarking on tax base expansion programme to raise more revenue through identification of new taxpayers". (4 marks)
- With reference to the above statement, highlight four sources of information in regard to identification of new taxpayers.
- (c) The following summary of transactions were obtained from the books of Zawadi Ltd., a company registered for value added tax (VAT) for the month of October 2020:

	Sh.
Sales at standard rate	1,480,000
Exports to a foreign country	364,000
Audit fees	78,300
Electricity bills	36,400
Imported raw materials	320,000
Purchases at standard rate	624,500
Exempt supplies	700,000
Catering services	94,000
Entertainment services	120,000
Telephone bills	28,000
Car parking services	50,000
Bottled drinking water for staff	64,000
Zero rated supplies (exports)	240,000
Repairs of motor vehicles	76,200

Additional information:

- Sales at standard rate include goods valued at Sh.280,000 purchased at standard rate and sold at the same state.
 - Imported raw materials was exclusive of freight charges of Sh.80,000 and insurance premium of Sh.40,000. Import duty rate was at 20%.
 - A debtor was issued with a credit note for goods valued at Sh.48,000 and this had not been passed through the relevant daybook.
 - The company issued debit notes valued at Sh.164,000 in respect to under invoicing of some customers.
 - Repairs of motor vehicles include Sh.20,000 for fuels and oils supplied to the company.
- Transactions are exclusive of VAT at the rate of 14% where applicable.

Required:

The VAT payable by or refundable to Zawadi Ltd. for the month of October 2020.

(10 marks)
(Total: 20 marks)

QUESTION THREE

- (a) Propose four measures that the revenue collection agency in your country could employ, to reduce instances of tax evasion. (4 marks)
- (b) Explain four grounds under which the commissioner might suspend or cancel a licence to manufacture excisable goods. (4 marks)

c) Benson Kapila is the manager for Daity Ltd., a company incorporated in Kenya. He has approached you to assist him in filing income tax returns for the year of income 2020. He has provided the following details relating to his income during the year:

1. Basic salary per month (Net of PAYE of Sh.18,600 per month) Sh.61,400.
2. He was provided with a house by the employer which was furnished at a cost of Sh.200,000.
3. He is a member of a registered retirement pension scheme. His monthly contribution was Sh.30,000. The employer contributed Sh.32,000 per month.
4. He was provided with a company car of 2000 cc whose cost as at 1 January 2019 was Sh.800,000.
5. He was given per diem of Sh.10,000 for five days he was out of work station on official duties in the month of June 2020.
6. He is a pensioner and received a monthly pension of Sh.35,000.
7. He is a member of home ownership savings plan (HOSP) where he contributed Sh.16,000 per month up to 30 September 2020.
8. On 1 October 2020, he moved to his own house which he acquired through a 12% mortgage loan of Sh.3,600,000.
9. He has an education insurance policy for his children where he pays premiums of Sh.7,000 per month.
10. He enjoyed free company products during the year whose value was estimated at Sh.56,000.
11. The company gave him a 5% loan of Sh.2,000,000 on 1 December 2020 to assist in off-setting the mortgage loan. The market interest rate was at 12% per annum.
12. The company paid him monthly telephone allowance of Sh.5,000.
13. His other incomes included:
 - Farming loss of Sh.140,000.
 - Rental income (commercial building) Sh.96,000.
 - Dividends (net of tax) of Sh.47,600 from Hazita Cooperative Society.
 - Professional fees Sh.78,000.

Required:

- (i) Total taxable income for Benson Kapila for the year ended 31 December 2020. (10 marks)
 - (ii) Tax payable (if any) from the income computed under (c) (i) above. (2 marks)
- (Total: 20 marks)**

QUESTION FOUR

(a) Excel Communications Ltd. is the regional dealer and distributor of communications equipment. They have provided you with the following statement of profit or loss for the year ended 31 December 2020:

	Sh.	Sh.
Sales		15,300,000
Closing inventory		2,000,000
Disposal gain on asset sold		180,000
Discount received		300,000
Compensation from insurance		<u>105,000</u>
		17,885,000
Less: Expenses:		
Purchases	9,000,000	
Opening inventory	1,500,000	
Repairs and maintenance	528,750	
Rent and rates	93,750	
Bad debts	311,250	
Subscriptions and donations	37,500	
Permits and licences	150,000	
Depreciation	670,000	
Office and distribution expenses	360,000	
Travelling and transport	252,000	
Legal fees	327,000	
Accountancy fees	97,500	
Disposal loss on assets	180,000	
Discount allowed	200,000	
Salaries and wages	1,500,000	
Bank ledger fees	<u>67,500</u>	
Net profit		<u>(15,275,250)</u> <u>2,609,750</u>

Additional information:

1. Insurance compensation is in relation to communications equipment stolen during the year while being shipped to a client.
2. Office and distribution expenses comprise of the following:

	Sh.
Club membership fee subscriptions for employees	135,000
Private expenditure of directors	102,000
3. 10% of the rent and rates relates to directors' private residences.
4. Subscriptions and donations include:

	Sh.
To the communications equipment traders association	22,500
To the Kenya Red Cross-donations	5,500
To the street children feeding program	<u>9,500</u>
	<u>37,500</u>
5. Legal fees include the following:

	Sh.
Renewal of lease – 100 years	45,000
Staff employment contracts	60,000
Counterfeit equipment suit in the High Court	87,000
Debt collection	50,000
6. Capital deductions have been agreed at Sh.645,000 with the Commissioner of Domestic Taxes.
7. Bad debts include an increase in general provision for bad debts of Sh.21,250.
8. Salaries and wages include directors emoluments of Sh.500,000.
9. Repairs and maintenance includes the cost of erecting a signboard outside the dealership shop of Sh.28,750.

Required:

- (i) Excel Communications Ltd. taxable profit or loss for the year ended 31 December 2020. (9 marks)
- (ii) The tax payable (if any) on the profit or loss computed in (a) (i) above. (1 mark)

- (b) Plasticom Ltd. is a company established in year 2020 to manufacture plastic products. Before commencing its operations on 1 May 2020, the company incurred a total of Sh.8,760,000 in construction of a factory building which included:

	Cost (Sh.)	Date of first use
Godown	320,000	1 July 2020
Showroom	240,000	1 September 2020
Administration offices	680,000	1 October 2020

Additional information:

1. The following assets were constructed or purchased and utilised with effect from 1 July 2020:

	Cost (Sh.)
Water pump	540,000
Labour quarters	920,000
Processing machinery	2,600,000
Tractor	1,800,000
Scanners	320,000
Two saloon cars	7,000,000
Mobile forklift	1,500,000
Computers	250,000
Power transformer	820,000
Office cabinets	180,000
Boilers	960,000
Bridge (connecting the factory to main road)	1,200,000

2. The following costs were incurred by the company on 1 September 2020:

	Cost (Sh.)
Sinking a borehole	720,000
Construction of a parking bay	630,000

3. One of the computers traded in on 10 November 2020 for a new one costing Sh.68,000. The trade in value was Sh.40,000 and the balance was settled in cash.
4. The company constructed a Sports Pavilion and additional staff quarters during the year at the cost of Sh.890,000 and Sh.1,200,000 respectively. These structures were utilised from 1 October 2020.

Required:

- Investment allowances due to Plasticom Ltd. for the year ended 31 December 2020. (10 marks)
- (Total: 20 marks)**

QUESTION FIVE

- (a) Explain four reasons for the declining trend in tax revenue in most developing countries. (4 marks)
- (b) Summarise four objectives of fiscal policies in your country. (4 marks)
- (c) Mark and Wanguh are in a trading partnership operating as Mawah Enterprises and sharing profits or losses in the ratio of 2:3 respectively.

The following statement of profit or loss was prepared by the business for the year ended 31 December 2020:

**Mawah Enterprises
Statement of profit or loss for the year ended 31 December 2020**

	Sh.	Sh.
Gross sales		2,736,000
Unrealised foreign exchange gain		16,000
Insurance recovery on stolen good		300,000
Overprovision for bad debts		34,000
Dividends from Haki Cooperative Society		42,500
L Interest on drawings		<u>45,000</u>
		3,173,500
Less expenses:		
General expenses	324,000	
^ Legal expenses	678,600	
^ Salaries to partners	450,000	
^ Drawings by partners	100,000	
^ Commission to partners	180,000	
^ Interest on partners' capital	250,000	
Purchase of furniture	96,000	
L Donations to poverty commission	64,000	
Construction of fire exit	<u>36,400</u>	<u>(2,179,000)</u>
Net profit		<u>994,500</u>

Additional information:

1. Gross sales include VAT at 14%. In addition, 10% of sales before VAT represents closing stock. The stock had been overstated by 20%.
2. The amounts due to partners are to be apportioned according to profit or loss sharing ratios.
3. General expenses comprise:

	Sh.
• Partition of business premises	64,000
• Debt collection expenses	36,000
• Purchase of office stationery	14,000
• Cash embezzled by partner's wife	48,000
• Bad debts written off	24,800
• Business premises rent	31,200
• Salaries to employees	<u>106,000</u>
	<u>324,000</u>
4. Legal expenses include:

	Sh.
• Acquisition of patent rights	24,800
• Drafting of sales agreement	34,200
• Negotiating sales contract	60,000
• Defending the business against trade dispute	42,600
• Mortgage interest for Mark	140,000
• Defending partners against wrong tax assessment	94,600
• Conveyance fees for business premises	125,800
• Tax consultancy fees	72,500
5. The purchases represent 40% of the gross sales figure Sh.2,736,000. The purchases had been understated by 25% and were omitted from the income statement.

Required:

- (i) Adjusted partnership statement of profit or loss for the year ended 31 December 2020. (8 marks)
- (ii) The allocation of profit or loss computed in (c) (i) above to each partner. (4 marks)

(Total: 20 marks)