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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

THURSDAY: 28 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		Annual rates	
	(Sh.)	(Sh.)	(Sh.)	(Sh.)
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%)				
Commissioner's prescribed benefit rates				
Services				
(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 five roles of the County Assembly in public finance management. (5 marks)
 - (b) Propose five sources of revenue for county governments. (5 marks)
 - (c) Outline the stages to be followed in the budget process for the National Government in any financial year. (10 marks)
- (Total: 20 marks)**

QUESTION TWO

- (a) Identify three ad hoc committees that a county procuring entity could establish to ensure that procurement and asset disposal is done in accordance with the County Governments Procurement Regulations. (3 marks)
- (b) Discuss five roles of the National Treasury in relation to procurement and asset disposal as outlined in the Public Procurement and Asset Disposal Act. (5 marks)
- (c) The following are summaries of the details of the sales day book, purchases day book and the cash book of Kamata Ltd. for the month of December 2018:

Sales Day Book

Date	Details	Folio	Amount (Sh.)
December 4	Mwangaza Ltd.	1002	650,000
7	J. Kamau	1003	520,000
14	Hazina Enterprises (export)	1004	350,000
20	Ministry of Sports	1005	170,000
	Total		1,690,000

Purchases Day Book

Date	Details	Folio	Amount (Sh.)
December 1	Jawabu Enterprise	2004	300,000
6	Sonytec Ltd. (imports)	2006	420,000
12	N. Kaluma	2007	200,000
27	B. Salama	2008	180,000
	Total		1,100,000

Cash Book

DR				CR			
Date	Details	Cash	Bank	Date	Details	Cash	Bank
December		Sh.	Sh.	December		Sh.	Sh.
5	Sales	960,000	450,000	2	Salaries and wages		1,800,000
15	Receipt from debtors	800,000	4,200,000	4	Catering expenses	120,000	
				5	Purchases	580,000	640,000
				7	Furniture		160,000
				9	Electricity	32,000	
				14	Photocopying	24,000	
				22	Refund to customers		176,000
				30	Balance c/d	1,004,000	1,874,000
		1,760,000	4,650,000			1,760,000	4,650,000

Additional information:

1. J. Kamau was declared bankrupt on 18 December 2018 after having paid Sh.400,000 for the goods purchased on 7 December 2018.
2. Ten per cent of the purchase from Jawabu Enterprises were returned by the company due to poor quality.
3. Credit notes amounting to Sh.280,000 were issued to customers during the month.
4. Refund to the customers in the cashbook relates to the excess amounts paid on cash sales.
5. A purchase invoice of Sh.220,000 from Dubai Traders was omitted from the purchases daybook.
6. All the above transactions are exclusive of VAT at the standard rate of 16%.

Required:

Prepare a VAT account for the month of December 2018 showing the VAT payable or refundable, if any. (12 marks)
(Total: 20 marks)

QUESTION THREE

- (a) In a tax seminar one of the facilitators noted that, "The Tax Procedures Act 2015, specifies on information that the Commissioner should include in the default assessment to a taxpayer".

With reference to the above statement, outline five categories of such information. (5 marks)

- (b) Suleiman Kombo is employed as the Managing Director of Utamu Distributors Ltd., a tax exempt company. During the year ended 31 December 2018, he presented the following information:

1. His basic salary was Sh.120,000 per month (PAYE Sh. 48,000 per month).
2. He was provided with lunch by the employer from 1 August 2018 of Sh.4,800 per month.
3. He was provided with a fully furnished house fitted with water and electricity. The employer paid a monthly rent of Sh.45,000. He was deducted 10% of his basic monthly salary for rent. The cost of furniture was Sh.300,000 while the monthly electricity and water bills was Sh.3,500 and Sh.2,800 respectively.
4. The company paid for him life insurance premiums of Sh.6,000 per month for each member of his household from 1 September 2018. He had included himself, his wife and their son in the insurance policy.
5. He contributed 10% of his monthly pay towards a registered pension scheme while the employer contributed 15% of his basic pay towards the same scheme.
6. He enjoyed free medical treatment under a medical scheme operated by the company for all employees. His medical expenses were assessed at Sh.150,000 during the year.
7. During the year the company paid a total of Sh.35,000 as school fees for his son studying in a County School. This amount was not included in the company's income statement during the year.
8. On 1 August 2018, the company provided him with the following:
 - A Land Rover which was acquired at a cost of Sh.1,800,000 with an engine capacity of 3,000cc.
 - A gardener and a night watchman whose monthly salaries was Sh.12,500 and Sh.15,000 respectively.
9. He invested in real estate and earned a net rental income of Sh.72,000 after deducting the following expenditure:

	Sh.
Caretaker's wages	120,000
Fencing	40,000
Loan repayment	320,000
Insurance rent and rates	48,000
Partitions	60,000
Capital allowances	22,000
Gross rental withholding tax paid	68,200

10. He received net dividends of Sh.42,500 from Maziwa Co-operative Society during the year.

Required:

- (i) Total taxable income for Suleiman Kombo for the year ended 31 December 2018. (10 marks)
- (ii) Tax payable (if any) from the income computed in (b) (i) above. (3 marks)
- (iii) Comment on any information not used in your computations under (b) (i) above. (2 marks)

(Total: 20 marks)

QUESTION FOUR

- (a) Dalbir Singh is a retired engineer. He set up a factory complex in industrial area on 30 September 2017 to fabricate mechanical and auto spare parts at a cost of Sh.48 million.

However, operations commenced on 1 January 2018.

The cost comprised the following:

	Sh.
Factory building	18,750,000
Office (within the factory building)	6,250,000
Reinforcement of concrete floor to affix machinery	1,650,000
Land	8,000,000
Architect's fee	2,430,000
Packing bay	990,000
Electrical wiring	1,480,000
Conveyer belt	1,200,000
Lifts and escalators	4,000,000
Special shafts for lifts	3,250,000
	<u>48,000,000</u>

Dalbir Singh provided the following additional information:

1. Additional structures and works constructed and utilised from 1 January 2018 were as follows:

	Sh.
- Residential house	960,000
- Workplace nursery	1,200,000
- Drawing and design room	720,000

2. To improve performance in the factory, an Oracle database that provides cloud service was installed at a cost of Sh.450,000. The computers in the drawing and design room had a Computer Aided Design (CAD) application installed at a cost of Sh.270,000.

3. A building that had been constructed at a cost of Sh.12,000,000 was leased from Jalaam Manufacturers Ltd. for five years. The annual lease rentals were agreed at Sh.2,800,000. Dalbir imported processing machinery from China at a cost of Sh.5,200,000 and installed it in the building.

4. Two warehouses were constructed at a cost of Sh.2,250,000 and utilised from 1 September 2018.

5. The following assets were purchased or constructed during the year:

	Sh.
Furniture and fittings (including of Sh.220,000 for the workplace nursery)	620,000
Library display fixtures (stocked with mechanical engineering volumes)	480,000
Computers and electronic adding machines	840,000
Motor vehicle (a second-hand BMW)	2,300,000
Lorry (four tonnes)	1,800,000
Tuktuk for the messenger	180,000
Backhoe loader	3,680,000
Additional processing machinery	9,000,000
Mobile crane	1,900,000

Required:

Capital allowances due to Dalbir Singh for the year ended 31 December 2018.

(10 marks)

- (b) The following information has been extracted from the records of LathermanCo. Ltd. who are regional suppliers of electronic equipment and appliances, for the year ended 31 December 2018:

	Sh.
Operating profit before tax and other income	3,800,000
Investment income	849,500
Leasing of electronic equipment	50,000
Rental income	346,000

Additional information is provided as follows:

1. Investment income comprises of the following:

	Sh.
Interest income: Post Bank (K) Ltd.	138,000
Fixed deposit accounts with Luanda Bank	246,500 (Net)
Savings accounts	170,000 (Net)
Dividend income: B and M Co. Ltd.	200,000 (Gross)
Kampuni Sacco Society Ltd.	95,000 (Net)
	<u>849,500</u>

2. Rental income is arrived at after deducting the following expenses among others:

	Sh.
Mortgage interest on property	10,000
Purchase of water meters	28,000
Caretaker's salary	36,000
Replacing iron sheet roofing with the tile roofing	120,000
Withholding tax on rental income	60,000

3. The following expenses were considered before arriving at the operating profit before tax and other income:

	Sh.
Salaries and wages	840,000
Retirement fund contribution (with Sh.80,000 to registered funds)	150,000
Depreciation	400,000
Bank interest	180,000
Provision for bad debts	10,000
Legal and professional fees	108,000
Repairs and maintenance	40,000
Sundry expenses	150,000
Donations	150,000
Compensation	92,000
Instalment tax paid for the previous year	900,000
Construction of the watchmen's booth at the gate	240,000

4. Salaries and wages comprised: Directors allowances Sh.300,000, director's watchmen salary Sh.40,000 and salaries to other staff Sh.500,000.

5. Bank interest includes that of an overdraft taken by a senior manager of Sh.40,000, on the managing director's residential house mortgage Sh.60,000 and the rest on bank loan.

6. Provision for bad debts is made up as follows:

	Sh.		Sh.
Bad debts written off: Customers	10,000	Balance brought forward: 3% of accounts receivable	8,000
Staff	14,000	Balance brought forward: Specific bad debts	30,000
Balance carried down:			
2% of accounts receivable	9,000	Bad debts recovered	5,000
Specific bad debts	<u>20,000</u>	Income statement	<u>10,000</u>
	<u>53,000</u>		<u>53,000</u>

7. Legal and professional fees comprise:

	Sh.
Collection of trade debts	20,000
Renewal of lease (9 $\frac{1}{2}$ years)	3,000
Accounting fee	35,000
Auditing fee	15,000
Tax appeal	30,000
Staff loan collection	<u>5,000</u>
	<u>108,000</u>

Auditing fee relates to an enquiry by the Revenue Authority which revealed discrepancies that led to higher tax liability and penalties.

8. Sundry expenses constitute staff Christmas party Sh.17,000, tax penalty for late filing Sh.3,000, school fees Sh.40,000 and other allowable expenses of Sh.90,000. School fees was for a director's son and the company agreed not to debit it in the income statement.

9. Donations were to the County Governor's political campaign kitty.

10. Compensation was to a staff member who had not been issued with safety equipment and uniform as he carried out work at a client's premise leading to him being badly injured.

Required:

The adjusted taxable income of Latherman Co. Ltd. for the year ended 31 December 2018.

(10 marks)

(Total: 20 marks)

QUESTION FIVE

- (a) Explain each of the following terms as used under custom taxes: (2 marks)
- (i) Clean report of findings. (2 marks)
- (ii) Import declaration form. (4 marks)
- (b) Summarise four factors which could influence the extent of tax shifting. (4 marks)
- (c) Teddy, Racheal and Michael are partners trading under the name Teram Enterprises. They share profits and losses in the ratio of 4:3:3. The partners have presented the following income statement for the year ended 31 December 2018:

	Sh.		Sh.
Salaries and wages	280,000	Gross profit	2,300,000
Rent, rates and taxes	150,000	Miscellaneous income	150,000
Office expenses	204,000	Discounts	80,000
Printing and stationery	64,000	Farming income	132,000
Instalment tax paid	45,000	Profit on sale of shares	100,000
Advertising	73,000	Interest on deposits	120,000
Interest on capital:			
Teddy	60,000		
Racheal	70,000		
Michael	80,000		
Legal fees	82,000		
Commission to partners:			
Teddy	45,000		
Michael	35,000		
Depreciation	92,000		
Bad debts	68,000		
General expenses	99,000		
Donation to famine relief	100,000		
General reserve	120,000		
Local taxes on property	12,000		
Electricity	46,000		
Showroom expenses	117,000		
Net profit	<u>1,040,000</u>		
	<u>2,882,000</u>		<u>2,882,000</u>

Additional information:

1. It has been the firm's practice to value the stocks at the cost price, however, the closing stock amounting to Sh.180,000 was valued based on net realisable value which is 10% less of its cost price.
2. Salaries and wages include salaries amounting to Sh.40,000 paid to Racheal.
3. Advertising includes Sh.10,000 spent on advertising campaign to introduce a new product in the market.
4. Legal fees include a sum of Sh.12,000 paid as parking fine and penalty to the county government.
5. Capital allowances have been agreed with the Commissioner of Income Tax at Sh.90,000.
6. Teddy's other income includes Sh.120,000 consultancy fee. He has brought forward partnership business loss of Sh.35,000 from the assessment of the year of income 2017.
7. Racheal has income of Sh.200,000 from bet winnings. She has brought forward partnership business loss of Sh.135,000 from assessment of the year of income 2017.

Required:

- (i) Taxable profit or loss of the partnership for the year ended 31 December 2018. (8 marks)
- (ii) Allocation schedule of profit or loss calculated in (c) (i) above. (2 marks)
- (iii) Total taxable income of each of the partners for the year of income 2018. (2 marks)

(Total: 20 marks)

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