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ATD LEVEL III

DCM LEVEL III

PRINCIPLES OF PUBLIC FINANCE AND TAXATION

TUESDAY: 22 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)

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

### QUESTION ONE

- (a) Outline six roles of county assembly in relation to management of public finance. (6 marks)
- (b) Citing four reasons, justify why the national government might borrow a loan within the country or outside the country as envisaged by the Public Finance Management Act. (4 marks)
- (c) It is the responsibility of the National Treasury to manage national government public finance in accordance with the Constitution. In doing so, it has to enforce fiscal responsibility principles.
- In relation to the above statement, describe six such fiscal principles. (6 marks)
- (d) Summarise four roles of the senate as an oversight function in public finance management. (4 marks)
- (Total: 20 marks)**

### QUESTION TWO

- (a) (i) Explain the meaning of the term "budget circular" as used in public finance management. (2 marks)
- (ii) The National Treasury is mandated with the preparation of annual estimates and coordinating preparation of the national government's budget. Towards this function, the Cabinet Secretary issues out a circular.
- In relation to the above statement, summarise four contents of Treasury budget circular. (4 marks)
- (b) Outline four responsibilities of an accounting officer of a public entity in relation to the preparation of annual estimates of expenditure in the budget preparation process. (4 marks)
- (c) Pie General Merchant Ltd. is registered for value added tax (VAT) purpose. During the month of November 2017, the company made the following transactions:

November 1:	Sold goods to Keita Ltd. for Sh.300,000 on credit
November 2:	Purchased goods on credit from Hawa Traders for Sh.150,000
November 3:	Keita Ltd. returned goods valued at Sh.45,000 and received a credit note
November 4:	Exported goods to Upendo Ltd. a company based in Tanzania for Sh.225,000
November 5:	Purchased goods for Sh.600,000 from Katunda Ltd. on credit
November 6:	Imported goods from China exclusive of import duty and VAT for Sh.675,000
November 7:	Received debit note from Katunda Ltd. worth Sh.36,000
November 8:	Bought spare parts for repair of motor vehicle for use in business for Sh.90,000
November 9:	Sold goods to John on credit amounting to Sh.600,000
November 15:	Sold goods to various customers on cash for Sh.150,000
November 20:	Paid the following expenses:
	<b>Sh.</b>
	Catering 51,000
	Stationery 63,000
	Electricity bills 18,000
	Audit fee 45,000
November 25:	Received cash Sh.255,000 from Keita Ltd. in full settlement of debt
November 30:	Closing stock was valued at Sh.560,000

All transactions are stated inclusive of VAT at the rate of 16% where applicable unless otherwise stated. Import duty was agreed to be 25% of the value of the goods imported.

#### Required:

A value added tax (VAT) account for the month of November 2017.

(10 marks)  
**(Total: 20 marks)**

### QUESTION THREE

- (a) Mwangaza Ltd. manufactures candles for the local market and export to neighboring countries. The company has submitted the following income statement for the year ended 31 December 2017:

	<b>Sh.</b>	<b>Sh.</b>
Gross profit		6,608,000
Dividends (net)		360,000
Rental income		820,000
Foreign exchange gains realised		760,000
Insurance compensation for stolen inventory		480,000
		9,028,000

**Less expenses:**

Salaries and wages	2,440,000	
Subscriptions and donations	120,000	
Bank charges	340,000	
Depreciation	280,000	
Office rent	1,720,000	
Electricity and water	960,000	
Advertisement costs	130,000	
Amortisation of goodwill	420,000	
Repairs and maintenance	640,000	
Audit fees	320,000	
General expenses	2,400,000	
Provision for corporation tax	<u>180,000</u>	(9,950,000)
Net loss		(922,000)

**Additional information:**

1. General expenses comprised the following:

	<b>Sh.</b>
Legal fees for breach of contract	180,000
Stamp duty on land	1,200,000
Passages to one of the directors	420,000
General provision for bad debts	600,000

2. Repairs and maintenance included:

	<b>Sh.</b>
Replacement of an old computer	82,000
Re-roofing the factory with tiles	420,000
General repairs	138,000

3. Advertisement costs included the following:

	<b>Sh.</b>
Placing advertisements in media	48,000
Erection of a new billboard	24,000
Publicity for Christmas sales	58,000

4. Subscriptions and donations related to the following:

	<b>Sh.</b>
Donations to political parties	90,000
Subscription to Federation of Employers	30,000

**Required:**

- (i) Adjusted taxable profit or loss of Mwangaza Ltd. for the year ended 31 December 2017. (8 marks)
- (ii) Tax payable (if any) by Mwangaza Ltd. for the year ended 31 December 2017 from the adjusted income in (a)(i) above. (2 marks)
- (b) Nandy Ltd. is a meat processing company that was incorporated on 30 December 2014. The company started its operations on 10 January 2015 after incurring the following capital expenditure:

<b>Assets</b>	<b>Cost</b>
	<b>Sh.</b>
Land	6,500,000
Processing machinery	4,200,000
Factory building	2,800,000
Tractors	4,600,000
Trailer for the tractor	1,200,000
Furniture	860,000
Labour quarters	3,200,000
Computer software	280,000
Photocopiers	160,000
Air conditioners	980,000
Isuzu pick-up	1,800,000
Sports pavilion	640,000
Lorry (3 tonnes)	3,800,000
Staff canteen	960,000

**Additional information:**

1. A new pick-up was purchased for business travelling on 1 November 2017 at a cost of Sh.2,400,000 after disposing the old Isuzu pick-up to one of the directors for Sh.960,000.
2. During the year ended 31 December 2017 the company expanded its operations and incurred the following additional expenditures:

Assets	Cost Sh.	Date of first use
Factory extension	3,800,000	2 February 2017
Saloon car (3,000cc)	2,500,000	1 April 2017
Generator	580,000	2 May 2017
Warehouse	800,000	1 July 2017
Water tank	180,000	10 August 2017
Forklifts	920,000	10 August 2017
Cash registers	180,000	1 September 2017
Office partitions	340,000	10 December 2017

3. The company sunk a borehole at a cost of Sh.1,500,000 which was utilised from 1 September 2017. A water pump costing Sh.180,000 was purchased and utilised from the same date.
4. A perimeter wall was constructed at a cost of Sh.620,000 and put in use on 1 December 2017.

**Required:**

Capital allowances due to Nandy Ltd. for the year ended 31 December 2017.

(10 marks)

**(Total: 20 marks)**

**QUESTION FOUR**

- (a) Outline four measures that the National Revenue Authority in your country could use to enhance tax compliance. (4 marks)
- (b) Identify four transactions for which personal identification number (PIN) is mandatory in your country. (4 marks)
- (c) Bonnie Ekeno is employed by Afropos Group Limited as the chef. The group runs a chain of five star hotels both locally and in foreign countries. Information relating to his earnings for the year ended 31 December 2017 was as follows:

1. Basic salary Sh.120,000 per month (PAYE Sh.32,500 per month).
2. The company provides him with a 2650cc vehicle for his private use. The car was acquired at a cost of Sh.2,300,000 on 1 January 2015.
3. He earned bonus pay of Sh.180,000 and overtime allowance of Sh.140,000 as per the terms of his contract, during the year.
4. Bonnie contributes Sh.18,000 per month towards a registered defined benefit fund that is operated by the employer. The employer contributes Sh.20,000 per month on his behalf towards the fund.
5. He contributed Sh.8,000 per month toward a home ownership savings plan (HOSP) with effect from 1 March 2017. The plan was registered and the funds were deposited in an approved institution.
6. Afropos Ltd. runs a scheme providing free medical services to all employees and their dependants. During the year, Bonnie and his wife received services worth Sh.90,000 while their three children (aged fourteen, eighteen and twenty two years) received medical services amounting to Sh.60,000 each.
7. He was provided with a self-contained house by the employer in the staff quarters. He also takes free meals at the hotel.
8. As part of the terms of his employment he was paid a holiday allowance of Sh.70,000 for his holiday to a foreign destination and back home.
9. Bonnie Ekeno has a rental business whose details for the year ended 31 December 2017 were as follows:

	Sh.
Gross rent	1,200,000
Repairs and maintenance	90,000
Renovations and renewals so as to increase rent	420,000
Interest on mortgage	250,000
Purchase of furniture for use by tenants	530,000
Withholding tax paid on gross rent	120,000

10. In the month of August 2017, Afropos Ltd. sent Bonnie Ekeno to their hotel in Cairo for a three-week training course to further his culinary skills. Towards this end, they paid for his return ticket Sh.97,000 and Sh.320,000 for his upkeep.

**Required:**

- (i) The total taxable income of Bonnie Ekeno for the year ended 31 December 2017.

(8 marks)

- (ii) The tax liability (if any) from the income computed in (c)(i) above. (2 marks)
- (iii) Comment on information not utilised in your computations under (c)(i) and (c)(ii) above. (2 marks)
- (Total: 20 marks)**

**QUESTION FIVE**

- (a) Propose four measures that could be used by the customs and excise duty departments of your country to prevent dumping. (4 marks)
- (b) Summarise four circumstances under which a tax payer dissatisfied with the commissioner's decision could appeal to the local committees. (4 marks)
- (c) Karara and Katoo are in partnership trading as Kaka Traders. They share profits and losses in the ratio of 2:3 respectively. The partnership statement of income for the year ended 31 December 2017 was as follows:

	Sh.	Sh.
Gross profit		5,130,600
Sale of motor vehicle		136,700
Foreign exchange gain		<u>72,800</u>
		5,340,100
<b>Less expenses:</b>		
Purchase of furniture	147,000	
Depreciation	180,000	
Conveyance fee for a plot	369,600	
Excise tax	23,100	
Salaries and wages	1,050,000	
Travelling expenses	112,200	
Legal expenses	540,000	
Loss on disposal of shares	60,000	
Stamp duty	96,750	
Interest expense	420,000	
Subscriptions to a social club	36,900	
General expenses	1,320,000	
Katoo farming expenses	141,900	
Bad debts	<u>121,300</u>	<u>(4,618,750)</u>
Net profit		<u>721,350</u>

**Additional information:**

1. Interest expense comprised the following:
 

	Sh.
Interest on capital: Karara	120,000
: Katoo	90,000
Farm loan expenses	54,600
Negotiation fees for loans	33,900
2. General expenses comprised:
 

	Sh.
Partners end of year party	180,000
Purchase of photocopier	225,000
Foreign exchange losses	33,000
Embezzlement by cashier	360,000
Staff catering services	450,000
Printing and stationery	72,000
3. Salaries and wages included:
 

	Sh.
Salaries to: Karara	222,000
: Katoo	123,000
Accrued wages for year 2016	210,000
4. Legal expenses comprised:
 

	Sh.
Parking fines by County Council	27,600
Breach of contract	51,900
Drafting tender documents	40,200
Preparation of lease documents	22,500
Traffic offence	12,000

5. Conveyance fees include mortgage interest of Sh.183,000 in respect of a house acquired by Karara for residential purpose.
6. It was estimated that 40% of bad debts related to specific bad debts.
7. Capital allowances were agreed with the Commissioner of revenue authority at Sh.279,575 for the year.

**Required:**

(i) Adjusted taxable profit or loss for the partnership business for the year ended 31 December 2017. (10 marks)

(ii) The allocation of the taxable profit or loss in (c)(i) above to the partners. (2 marks)

**(Total: 20 marks)**

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