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ATD LEVEL III

DCM LEVEL III

PRINCIPLES OF PUBLIC FINANCE AND TAXATION

TUESDAY: 27 November 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.)
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	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

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) Explain the term “financial regulations” as used in public finance management. (2 marks)
- (b) Describe the stages of the annual budget process for the county government. (8 marks)
- (c) Discuss five roles played by the controller of budget as envisaged by the Constitution and the Public Finance Management Act. (10 marks)

(Total: 20 marks)

QUESTION TWO

- (a) Financial controls in public sector entities involve the overall process of reviewing and controlling financial resources. In relation to the above statement, highlight four benefits of financial controls in public finance management. (4 marks)
- (b) Outline six factors that determine taxable capacity in your country. (6 marks)
- (c) The following information was extracted from the records of Kuza Enterprises a registered business for value added tax (VAT) purposes for the month of May 2018:

Bank Account			
	Sh.		Sh.
Trade receivables	1,740,000	Balance b/f	260,000
Loan proceeds	4,200,000	Stationery	125,280
Balance c/d	1,332,760	Trade payables	1,102,000
		Audit fee	232,000
		Salaries and wages	4,408,000
		Consultancy fee	116,000
		Loan repayment	270,840
		Garbage collection	62,640
		Purchase of furniture	696,000
	<u>7,272,760</u>		<u>7,272,760</u>

Additional information:

- Cash sales and purchases during the month of May 2018 amounted to Sh.1,740,000 and Sh.1,566,000 respectively.
- Trade receivables and trade payables balances were as follows:

	1 May 2018	31 May 2018
	Sh.	Sh.
Trade receivables	139,200	278,400
Trade payables	275,500	435,000
- During the month of May 2018, goods worth Sh.928,000 were exported to Rwanda. The export sales were not recorded in books of account.
- Electricity and water bills paid in cash during the month amounted to Sh.8,700 and Sh.6,960 respectively.
- Goods worth Sh.38,080 were returned to suppliers by Kuza Enterprises during the month of May 2018.
- All transactions are inclusive of value added tax (VAT) at the rate of 16% where applicable.

Required:

- A value added tax (VAT) account for the month of May 2018 for Kuza Enterprises. (10 marks)
- (Total: 20 marks)

QUESTION THREE

- (a) In a tax seminar, one of the facilitators noted that “modern tax practice and laws provide aggrieved taxpayers with an opportunity to appeal decisions made by the tax administration and ensure that the laws are applied consistently and fairly”.

With reference to the above statement, describe three appeal bodies available to an aggrieved taxpayer. (6 marks)

- (b) Bickam Okabo works for Baraka Trust Ltd. as an operations manager. He has provided the following information relating to his income for the year ended 31 December 2017:
- Basic salary Sh.180,000 per month (PAYE Sh.52,000 per month).
 - He was provided with a fully furnished house, rented by the company for Sh.45,000 per month. The cost of furniture was Sh.120,000 and the company deducted him Sh.15,000 per month as the rent for the house.

3. He was entitled to the company Land Rover of 3000cc for both official and private use. The car had been bought at a cost of Sh.2,500,000 in June 2010.
4. During the year, he contributed 15% of his monthly basic salary towards the company's Provident Fund which has been approved by the National Pension Authority.
5. He was provided with two house servants each on a monthly salary of Sh.18,000. The amount was paid directly to the house servants' account by the company.
6. He was entitled to meals in the company's cafeteria up to a limit of Sh.3,800 per month. During the year, he spent Sh.38,400 on meals at the cafeteria.
7. The company paid for his insurance policies as indicated below:

Policy	Effective date	Sum assured Sh.	Monthly premiums Sh.
Education	1 July 2017	820,000	5,200
Life Assurance	1 October 2017	1,600,000	9,000

8. On 1 October 2017, he was promoted to the Regional Head of Operations position and was entitled to the following allowances per month:

	Sh.
Responsibility allowance	25,000
Entertainment allowance	15,000
Travelling allowance	18,000

9. The company operates a medical scheme for all employees. The company paid Sh.180,000 as medical bills for Bickam Okabo's daughter during the year.
10. The company paid Bickam Okabo's children school fees amounting to Sh.150,000 during the year. This amount was expensed in the company's books of account.
11. During the first week of October 2017, he was sent outside the Head Office on official duties. He was paid daily subsistence allowance amounting to Sh.45,000 for the five days. The Commissioner was not satisfied that the per diem solely represented reimbursement of cost incurred by the employee.
12. He is a member of a home ownership saving plan and he contributed Sh.15,000 per month towards the scheme.
13. During the year, the company paid Bickam Okabo's monthly utility bills as follows:

	Sh.
Electricity	8,000
Telephone	4,200
Cooking gas	7,500

Required:

- (i) Taxable income for Bickam Okabo for the year ended 31 December 2017. (12 marks)
 - (ii) Tax payable (if any) on the income computed in (b) (i) above. (2 marks)
- (Total: 20 marks)**

QUESTION FOUR

- (a) Outline four grounds under which the Commissioner might cancel the personal identification number (PIN) in your country. (4 marks)

- (b) Tosha Ltd., a manufacturing company, presented the following information for the year ended 31 December 2017:

Net profit for the year was Sh.5,850,000 after deducting the following expenses:

	Sh.
Salaries and wages	1,480,000
Depreciation	65,000
Rent	1,020,000
Goodwill amortisation	289,000
Value added tax	36,000
General expenses	535,000
Donations to a political party	1,120,000
General provisions for bad debts	175,000
Advertising	301,000
Bad debts written off	180,000

Additional information:

1. The written down value of assets for tax purposes as at 1 January 2017 were as follows:

CLASS I	CLASS II	CLASS III	CLASS IV
Sh.	Sh.	Sh.	Sh.
1,950,000	350,000	1,800,000	235,000

2. Included as income while computing the net profit was a major renovation of Sh.450,000 undertaken on a factory building acquired on 1 January 2015 at a cost of Sh.2,000,000.

3. Included in advertising expense is a cost of installing a neon sign Sh.54,000.

4. A saloon motor vehicle purchased on 2 February 2016 at a cost of Sh.2,400,000 was involved in an accident on 1 July 2017. An insurance claim of Sh.1,200,000 was received in relation to the vehicle. This has been included as income while computing the net profit for the year.

5. The following assets were acquired on 1 March 2017:

	Sh.
Delivery van	1,700,000
Duplicating machine	62,000
Processing machinery	600,000
Calculators	38,000
Generator	52,000
Saloon motor vehicle	1,800,000
Water pump	27,000
Carpet	21,000
Boiler	29,000

6. The following buildings were constructed and put to use on 4 April 2017:

	Sh.
Godown	510,000
Factory extension	1,970,000
Staff quarters	910,000

7. The cost of factory extension included cost of a warehouse Sh.630,000 and showroom Sh.540,000.

8. All assets in CLASS II were sold for Sh.500,000 during the year.

Required:

(i) Capital allowances due to Tosha Ltd. for the year ended 31 December 2017. (10 marks)

(ii) Statement of taxable income or loss for the year ended 31 December 2017. (5 marks)

(iii) Tax payable (if any) from the income computed in (b) (ii) above. (1 mark)

(Total: 20 marks)

QUESTION FIVE

(a) Explain the following terms in the context of customs duty and excise duty:

(i) Prohibited goods. (2 marks)

(ii) Restricted goods. (2 marks)

(b) Identify four ways in which an individual or firm could engage in tax avoidance. (4 marks)

(c) Rudop and Jutoh are partners trading as Subline Enterprises.

The partnership agreement provided for the following:

	Rudop	Jutoh
Share of profits	2/3	1/3
Capital	Sh.500,000	Sh.250,000
Interest on capital (per annum)	10%	5%
Salaries to partners (per month)	Sh.35,000	Sh.25,000
Interest on drawings	5%	5%

The accounts of Subline Enterprises for the year ended 31 December 2017 were as follows:

	Sh.	Sh.
Gross profit		2,800,000
Discount received		120,000
Bad debts recovered		<u>140,000</u>
		3,060,000
Less expenses:		
Salaries and wages	1,430,200	
Electricity and water	160,000	
Purchase of furniture	120,000	
Bank charges	30,000	
Maintenance costs	180,200	
Depreciation	410,000	
Income tax paid	230,000	
Legal expenses	340,000	
General expenses	420,000	
Interest expense	360,000	
Drawings - Rudop	<u>100,000</u>	<u>(3,780,400)</u>
Net loss		<u>(720,400)</u>

Additional information:

1. Salaries and wages include the salaries paid to the partners and other staff.
2. Electricity and water includes Sh.90,000 paid in relation to Jutoh's residential house.
3. Legal expenses include Sh.180,000 incurred in defending Rudop in an assault case.
4. Bad debts recovered were in respect to bad debts written off in the last financial period.
5. Interest expense includes interest paid on the partners' capital contribution during the year.
6. General expenses included the following:

	Sh.
Partitioning of the shop	120,000
Cash embezzled by the cashier	60,000
Donations to National Disaster Council	240,000

Required:

- (i) Adjusted partnership taxable profit or loss for the year ended 31 December 2017. (10 marks)
 - (ii) Allocation of the taxable partnership profit or loss computed in (c) (i) above (2 marks)
- (Total: 20 marks)**
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