



CPA INTERMEDIATE LEVEL
CIFA INTERMEDIATE LEVEL
PILOT PAPER
PUBLIC FINANCE AND TAXATION

December 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:	Monthly rates (Sh.)	Annual rates (Sh.)
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) Discuss three roles played by the National Assembly budget committee or equivalent institution in your country in relation to public finance management. (6 marks)
- (b) The national and county governments engage in a number of projects. For the purpose of monitoring these projects the governments have developed an electronic project monitoring information system (e-ProMIS) to capture information on projects implemented by the ministries, state corporations and counties.

Required:

Discuss four specific objectives that the National and County governments might realise from the e-ProMIS (8 marks)

- (c) Discuss three reasons why Public Sector Finance is important in your country (3 marks)
- (d) Discuss three roles of the National Treasury in public procurement and assets disposal. (3 marks)

(Total: 20 marks)

QUESTION TWO

- (a) Highlight the steps followed by your county government or equivalent in developing its annual budget. (9 marks)
- (b) The County Treasury is required to submit to the county assembly a statement setting out the debt management strategy of the county government over the medium term with regard to its actual liability and potential liability in respect of loans and its plans for dealing with those liabilities.

Required:

Identify the information to be included in the statement of debt management strategy (5 marks)

- (c) Discuss three roles of taxation in achieving budgetary objectives. (3 marks)
- (d) During a devolution seminar in your country, one of the key speakers noted that county governments should be allocated national government share of revenue based on the ability of a county to enhance its revenue raising measures.

Required:

Identify three sources of revenue to the county governments. (3 marks)

(Total: 20 marks)

QUESTION THREE

Mr. Japheth Murunga is employed as a finance manager by Top Notch Ltd. He reported the following details on his income and that of his wife for the year ended 31 December 2020:

1. He was entitled to a basic salary of Sh.2,500,000 per annum (PAYE Sh.250,000 per annum).
2. The employer provided him with a motor vehicle (2600 cc) which was leased from Unique Car Hire Services at Sh.32,000 per month. The cost of the vehicle was Sh.2800,000 in 2018.
3. His annual mortgage repayment of Sh.576,000 (including interest of Sh.120,000) was paid by the employer. The loan was obtained from UNA Bank in 2019 for the purpose of constructing own residential house.
4. He was entitled to a bonus of Sh.120,000 per annum, The bonus for 2020 was however not paid until February 2021.
5. The following deductions were made from his salary during the year:

	Sh.
Life insurance premiums	96,000
Subscription to Railway Golf Club	56,000
Subscription to accountants professional body	90,000
Contributions to registered pension scheme	300,000

6. During the year he received a dividend from Top Notch Ltd. of Sh.120,000 (gross) since he holds 2% of the company's share capital. The employer paid the withholding tax on his behalf.
7. His wife Truphena Murunga works for a taxation consultancy firm where she received a basic salary of Sh.80,000 per month. She is housed by the firm together with her family in a house where she contributes 3% of her basic pay as rent. She received the following additional benefits for the year ended 31 December 2020:
 - Subsistence allowance of Sh.6,000 per day. In total she worked out of the office station for 21 days in the year.
 - Medical allowance of Sh.10, 000 per month. The firm has a medical scheme for all senior managers.

- She enrolled for a seminar on women empowerment in Kenya at Sh.120,000. 30% of this cost was met by the employer.
- She received 10,000 shares from the company at a price of Sh.50 per share. The par value per share is Sh.72 while the market price at the time was Sh.79 per share.

Her other income comprised:

	Sh.
Interest income:	
Housing development bonds	200,000
Treasury bonds	120,000
Investment fund	85,000 (net)
Dividend income: Mapato Sacco Ltd.	95,000 (net)
Wezo Co-operative Society	150,000 (gross)
Rental income from residential property	290,000 per month

Reported farming income was Sh.48,000 after deducting own consumption of Sh.20,000 which was equivalent to 18% of total farm produce.

8. Mr. Japheth and his wife have agreed that each files his or her returns to the revenue authority.

Required:

- (a) Taxable income of Mr. Japheth and his wife. (16 marks)
- (b) Tax due on the income(s) computed in (a) above. (4 marks)

(Total: 20 marks)

QUESTION FOUR

- (a) Ernest, a citizen of USA has been assigned to work for his company's branch located in your country for the next ten years. He has approached you to assist him in understanding the Kenyan tax system especially on the basis of taxing an income in Kenya.

Required:

Explain to Ernest the cardinal rules of taxing an income in your country. (5 marks)

- (b) Jessica and Mbatha established a partnership business sharing profits and losses in the ratio of 3:2 respectively. The following is the income statement of the partnership for the year ended 31 December 2020:

	Sh.	Sh.
Sales		8,678,000
General bad debts reduction		112,000
Unrealized foreign exchange gain		270,000
Capital gain on sale of shares		528,000
Recovery from insurance on stock stolen		480,000
Discount received		184,000
Dividends from Safari Cooperative Society		<u>51,000</u>
Total income		10,303,000
Less Expenses:		
Purchases	4,263,000	
Purchase of computers software	324,000	
Partners salaries	1,296,000	
Legal expenses	1,224,000	
Repairs expenses	1,023,400	
Rent and rates	366,900	
Interest on loan	249,300	
General expenses	964,000	
Motor vehicles expenses	840,000	
Insurance	280,800	
Preliminary expenses	473,000	
Directors fees	1,080,000	
Audit and accountancy fees	142,000	
Debenture interest	1,800,000	
Travelling expenses	<u>96,000</u>	<u>(14,422,400)</u>
Net loss		<u>(4,119,400)</u>

Additional information:

- Purchases and sales were inclusive of value added tax at a rate of 16%.
- Closing stock was valued at Sh. 1,840,000 while opening stock was at 10% of sales net of value added tax. Both stocks were undervalued by 10%.
- Legal expenses comprised:**

	Sh.
Legal fee on defense against alleged breach of trade contract	180,000
Legal fee on tax objection and appeals	164,800
Conveyance fees of business premises	72,400
Stamp duty	136,600
Negotiating a business loan	120,800
Recovery of bad debts	145,000
Signing a 100-year lease agreement	128,400
Purchase of partner's private residence - Jessica	150,000
Legal fee on renewal of patents	<u>126,000</u>
	<u>1,224,000</u>
- Repairs expenses comprised:**

	Sh.
Purchase of furniture	460,000
Installation of neon sign	260,000
Designing an office block	140,000
Cost of partitioning office block	141,000
Repainting of office block	<u>22,400</u>
	<u>1,023,400</u>
- General expenses included, impairment of patent rights Sh.144,000, provision for general bad debts Sh.148,000 and drawings of goods by partners Sh.568,000.
- Interest on loan includes interest on partners' capital of Sh.420,000 which was shared according to profit and loss sharing ratio.

Required:

Compute the total taxable income for each partner for the year ended 31 December 2020.

(15 marks)

(Total: 20 marks)**QUESTION FIVE**

- (a) Johari Ltd., a manufacturer of leather products commenced operations on 1 January 2020. The following information relates to the assets that the company purchased or constructed before commencement of operations.

	(Sh.)
Asset	Cost
Factory building (including godown Sh.700,000)	3,800,000
Parking bay	480,000
Drainage systems	240,000
Delivery van	420,000
Processing machine	1,680,000
Security wall	720,000
Office block (including staff canteen Sh.380,000)	980,000

Additional information:

- Processing machine was imported and includes customs duty and VAT of Sh.120,000 and Sh.100,000 respectively which was waived by the government.
- On 1 September 2020, the company sunk a borehole at a cost of Sh.1,600,000 and installed a water pump for Sh.200,000.
- Spots pavilion was constructed at a cost of Sh.1,200,000 and put to use from 1 May 2020.

Required:

Compute the investment allowances due to Johari Ltd for the year ended 31 December 2020.

(5 marks)

- (b) Bitech Ltd. is registered for VAT. In May 2021, the company imported goods costing Sh. 2,600,000 excluding freight charges of Sh.180,000.

The company then incurred Sh.400,000 to transport the goods from the port to its warehouse.

The conversion costs were 25% of the relevant costs incurred up to the point of processing.

The goods were subsequently sold at a profit margin of 33 1/3%.

Required:

The VAT payable on the above transaction. Use a VAT rate of 16% and customs duty rate of 25%.

(5 marks)

- (c) Analyse three circumstances where the revenue authority might cancel a taxpayer's personal identification number. (3 marks)
- (d) Write brief notes on the following terms as used in taxation:
- (i) Tax agents. (2 marks)
 - (ii) Excisable Goods Management System. (2 marks)
 - (iii) Warehousing of goods. (2 marks)
 - (iv) Railway development levy. (1 mark)
- (Total: 20 marks)**
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