

# KASNEB

CPA PART I SECTION 2

CS PART I SECTION 2

CIFA PART I SECTION 2

CCP PART I SECTION 2

PUBLIC FINANCE AND TAXATION

PILOT PAPER

September 2015.

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 2014.

Monthly taxable pay (Sh.)		Annual taxable pay (Sh.)		Rate of tax % in each Sh.
1	- 10,164	1	- 121,968	10%
10,165	- 19,740	121,969	- 236,880	15%
19,741	- 29,316	236,881	- 351,792	20%
29,317	- 38,892	351,793	- 466,704	25%
Excess over	- 38,892	Excess over	- 466,704	30%

Personal relief Sh.1,162 per month (Sh.13,944 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 buildings	50%	
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</b>	40%	
<b>Mining allowance:</b>		
Year 1	- 40%	
Years 2 - 7	- 10%	
(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

**Commissioner's prescribed benefit rates**

	Monthly rates Sh.	Annual rates Sh.
<b>Services</b>		
(i) Electricity (Communal or from a generator)	1,500	18,000
(ii) Water (Communal or from a borehole)	500	6,000
<b>Agriculture employees: Reduced rates of benefits</b>		
(i) Water	200	2,400
(ii) Electricity	900	10,800

Rent and rates	240,000	
Salaries to partners: Carter	180,000	
Mortgage interest	240,000	
Repairs on computers	60,000	
Furniture purchased (cost)	84,000	
Bank charges	80,000	(7,845,260)
Reported loss		<u>(452,660)</u>

**Additional information:**

1. General expenses comprise:

	<b>Sh.</b>
Embezzlement by accountant	1,200,000
Staff Christmas party	800,000
Amount paid to retrenched staff	760,000
Replacement of car engine	140,000
Partition of an office	<u>600,000</u>
	<u>3,500,000</u>

2. Salaries and wages include Sh.700,000 and Sh.800,000 paid to Asafa and Bon respectively during the year.  
3. Interest on capital was provided at 45% of the capital contributions.  
4. Legal expenses include:

	<b>Sh.</b>
Parking fines paid to county government	15,200
Legal fees for breach of contract	200,000
Drafting of tender documents	18,000
Drafting of lease agreements (99 years)	9,000
Defending a partner in a tax case	12,000
Legal cost of debt collection	233,300

5. Mortgage interest relates to a partner's residential house.  
6. Assume that the income accrued evenly throughout the year.  
7. Ignore capital allowances.

**Required:**

- (i) The adjusted partnership profit or loss for the year ended 31 December 2014. (9 marks)  
(ii) Allocation of the profits or losses in (c) (i) above to the partners. (4 marks)  
**(Total: 20 marks)**

**QUESTION FOUR**

- (a) Outline any five specified sources of income as detailed in Section 3 (2) of the Income Tax Act. (5 marks)  
(b) Compare and contrast the provisions of the Income Tax Act as relates to "Wear and Tear" and "Farm Works Deduction".

Your analysis should be guided by the following key aspects:

- (i) Acquisition of items previously used by another person for the same qualifying business.  
(ii) New items acquired during the year of income. (4 marks)  
(c) Hal Meat Processing Company (HMPC) was established on 1 January 2014 to process meat products for the local market. The company incurred the following costs in constructing relevant structures which were utilised from 1 January 2014:

	<b>Sh.</b>
Factory building	72,000,000
Labour quarters	24,000,000
Show room	950,000
Staff recreation facility	4,500,000
Retail shop	700,000
Perimeter wall	1,550,000
Administrative offices	1,600,000
Driveway	800,000

Sports pavilion	2,600,000
Drainage system	900,000
Loading bay	1,200,000
Weigh bridge	600,000

**Additional information:**

- A borehole was drilled at a cost of Sh.1,300,000 and utilised with effect from 1 November 2014.
- On 1 December 2014, the company constructed a factory extension at a cost of Sh.2,650,000 and put to use immediately.
- The following items were purchased on 1 December 2014:
 

	Sh:
Pick-up	2,400,000
Conveyor belt	600,000
Scanners	250,000
Mobile phones	260,000
Digital weighing machines	90,000
Computers	300,000
- The following assets were disposed of during the year:

	Disposal Date	Initial Cost (Sh.)	Disposal proceed (Sh.)
Computers	30 December 2014	100,000	60,000
Mobile phones	20 December 2014	60,000	20,000

**Required:**

Capital allowances due to Hal Meat Processing Company (HMPC) for the year ended 31 December 2014. (11 marks)  
(Total: 20 marks)

**QUESTION FIVE**

- Explain any two cases in which a business can close the year with a negative balance in any class of wear and tear elaborating on how such a balance would be treated. (2 marks)
- Regressive taxes present an unmatched opportunity for any developing country to increase its revenue collection from taxes.

Explain the validity or otherwise of this assertion. (5 marks)

- The following is the trading, profit and loss account of Cobalt Ltd. for the year of income 2014. The company is engaged in furniture making both for the local market and the foreign market:

	Sh. "000"		Sh. "000"
Stock (1 January 2014)	450,000	Sales	3,490,000
Purchases	1,400,500	Stock (31 December 2014)	423,000
Bank charges	30,200	Interest from Post Bank	4,800
Wages to casual workers	588,000	Insurance recovery - van	88,000
Insurances	78,000	Profit on sale of shares	54,000
Salaries to permanent staff	144,000	Dividend (net)	32,000
NSSF contributions - workers	13,000	Income from sale of saw dtst	250,000
NHIF contributions - workers	14,000		
Legal expenses	20,400		
Bad debts	50,600		
Commissions	30,200		
Repairs and maintenance	120,200		
General expenses	53,800		
Listing expenses - NSE	147,600		
Delivery van scrapped	22,400		
Depreciation	193,400		
Donations	8,800		
Rent and rates	83,000		
Electricity and water	28,100		

Travelling expenses	560,300	
Pension paid to retired staff	48,700	
Entertainment	17,100	
Purchase of office calculator	3,600	
Telephone expenses	11,900	
Net profit	<u>224,000</u>	
	<u>4,341,800</u>	<u>4,341,800</u>

**Additional information:**

1. Sales of saw dust require a payment of 20% commission on the income to the hawkers who pick up the items from the company premises and deliver them to the market. Such commission has not yet been included in the company books.

2. Legal expenses analysis:

	<b>Sh. '000'</b>
Preparing a lease for 50 years	1,200
Collection of business debts	2,200
Purchase of directors house	<u>17,000</u>
	<u>20,400</u>

3. Entertainment expenses relate to customers and staff.

4. The company was listed at the Nato Securities Exchange (NSE) at the beginning of the year, a process that led to 42% of the company's shares being offered to the public.

5. The capital allowances were agreed at Sh.2,000,000 for the year.

**Required:**

(i) Adjusted taxable income for the year ended 31 December 2014. (10 marks)

(ii) Compute the tax payable (if any) on the income in (c) (i) above. (3 marks)

**(Total: 20 marks)**

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