



(Knowledge for Development)
KIBABII UNIVERSITY

UNIVERSITY EXAMINATIONS

2019/2020 ACADEMIC YEAR

FOURTH YEAR SECOND SEMESTER

SPECIAL/SUPPLEMENTARY EXAMINATION

FOR THE DEGREE OF BACHELOR OF BUSINESS MANAGEMENT

COURSE CODE: BBF 421

COURSE TITLE: PUBLIC FINANCE AND TAXATION

DATE: 2ND FEBRUARY, 2021 **TIME: 2.00PM – 4.00PM**

INSTRUCTIONS TO CANDIDATES

Answer Question One in Section A and Any other TWO (2) Questions in Section B

TIME: 2 HOURS

KIBU observes ZERO tolerance to examination cheating

This Paper Consists of 11 Printed Pages. Please Turn Over. ►

RATES OF TAX (Including wife's employment, self-employment and professional income rates of tax)

YEAR OF INCOME 2019

Taxable Employment Benefits - Year 2019

Monthly taxable pay (shillings)			Annual taxable pay (shillings)			Rates of tax % in each shilling
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 Shs. 1,162 per month (Shs. 13,944 per annum)

Prescribed benefit rates of motor vehicles provided by employer

			Monthly rates (Sh.)	Annual rates (Sh.)
Capital allowances:	(i)	Saloon, Hatch Backs and Estates		
Wear and tear allowances		Upto - 1200 cc	3,600	43,200
Class I	37.5%	1201 - 1500 cc	4,200	50,400
Class II	30%	1501 - 1750 cc	5,800	69,600
Class III	25%	1751 - 2000 cc	7,200	86,400
Class IV	12.5%	2001 - 3000 cc	8,600	103,200
Industrial building allowance:		Over - 3000 cc	14,400	172,800

Industrial buildings	2.5%	(ii)	Pick-ups, Panel Van (Unconverted)		
Hotels	4.0%				
Farm works allowance	33.3%		Upto 1750 cc	3,600	43,200
Investment deduction allowance:			Over 1750 cc	4,200	50,400
2013	- 70%	(iii)	Land Rovers/Cruisers	7,200	86,400
2014	- 100%		OR 2% of the initial capital cost of the vehicle for each month, whichever is higher.		
2014	- 100%				

**Shipping investment deduction
40%**

Mining allowance:

Year 1	40%
Year 2 - 7	10%

Commissioner's prescribed benefit rates

Services	Monthly rates	Annual rates
	Sh.	Sh.
(i) Electricity (Communal or from a generator)	1,500	18,000
(ii) Water (Communal or from a borehole)	500	6,000
(iii) Provision of furniture (1% of cost to employer) If hired, the cost of hire should be brought to charge		
(iv) Telephone (Landline and mobile phones)	30% of bills	

Agricultural employees: Reduced rates of benefits

(i)	Water	200	2,400
(ii)	Electricity	900	10,800

Low interest rate employment benefit:

The benefit is the difference between the interest charged by the employer and the prescribed rate of interest.

Other benefits:

Other benefits, for example servants, security, staff meals etc are taxable at the higher of fair market value and actual cost to employer.

The current VAT rate is 16%

Marks allocated to each questions are shown at the end of the question. Show ALL your workings. Any assumptions made must be stated.

SECTION A

QUESTION ONE (COMPULSORY)

Mr. John Kiogora is employed by Meru Distributors Ltd. During the year of income 2013, he presented to you the following information:

1. Mr.Kiogora owns 10,000 ordinary shares of Sh.50 each in Benki Ltd. During the year of income, he received a dividend of Sh.2 per share.

2. His employment earnings include:

Salary sh.60,000 per month (P.A.Y.E Sh.16,000 per month)

He received an end of the year bonus payable to executive staff: sh.20,000

He used his own car to travel during the course of duty and the following costs were met by the employer:

Petrol paid for by Mr Kiogora and reimbursed by his employer in full Sh.12,000.

Maintenance and repair costs Sh.14,000.

Road licence and insurance sh.28,000.

Mr.Kiogora spent Sh.17,000 on entertainment of customers which was fully reimbursed by the employer.

Mr.Kiogora is housed by his employer, in a house where the employer pays Sh.5,000 per month.

His employer pays on his behalf life insurance premium at sh.2,000 per month.

The employer paid Sh.2,000 per month for Mr.Kiogora's approved pension scheme.

3. Interest received by Mr.Kiogora during the year was as follows:

Post Office Savings Bank

Sh.12,000

Fixed Deposit Account: Euro Bank Sh. 2,250

Savings Account: National Bank Sh. 8,400

4. Mr.Kiogora paid interest of Sh.20,000 per month, on a loan from HFCK for the purchase of his residence.

	Sh.	Sh.
5. Rental income:		
Gross rent		43,000
Less: Mortgage interest:	8,000	
Cost of building extension	120,000	
Painting extension	<u>10,000</u>	<u>138,000</u>
Net loss on rent		<u>95,000</u>

6. Mrs. Mary Kiogora earned the following income for the year of income 2013:

Salary: Malima Manufacturers sh.72,000 per month (P.A.Y.E. Sh.25,000 per month)

Free lunches by his employer Sh.2,400 per month

Part-time business Sh.10,000 per month.

Required:

- (a) Calculate the total taxable and tax payable income for Mr.Kiogora for the year of income 2013.

(13 marks)

- (b) State the tax position of Mrs.Kiogora. (2 marks)

- (c) Comment on any information that you did not use in computation of Mr.Kiogora's taxable income.

- (d) State and briefly explain three factors which influence the taxable capacity in a country. (6 marks)

(e) "Governments in developing countries tend to overtax individuals in formal employment".

(I) Using suitable explain why Governments find it convenient to continually raise higher taxes

on earnings from formal employment. (5 marks)

(ii) Suggest and explain one proposal on how the Government can be able to generate tax revenue from the informal sector. (2 marks)

(f) Normally in Kenya a trader is required to pay for a variety of licences in order to conduct trade.

(i) Do you consider a licence to be a tax? Explain. (1 mark)

(iii) In Kenya there is a proposal for the Government to issue a single licence to a trader in preference to the practice of issuing a variety of licences. Would you support this proposal? Why (1 mark)

(Total: 30 marks)

SECTION B (CHOOSE TWO QUESTIONS)

QUESTION TWO

(a) State and briefly explain four factors which influence the taxable capacity in a country. (6 marks)

(b) "Governments in developing countries tend to overtax individuals in formal employment".

(I) Using suitable explain why Governments find it convenient to continually raise higher taxes

on earnings from formal employment. (6 marks)

- (ii) Suggest and explain one proposal on how the Government can be able to generate tax revenue from the informal sector. (2 marks)
- (c) Normally in Kenya a trader is required to pay for a variety of licences in order to conduct trade.
- (i) Do you consider a licence to be a tax? Explain. (1 mark)
- (ii) Specify four of such licences. (4 marks)
- (iii) In Kenya there is a proposal for the Government to issue a single licence to a trader in preference to the practice of issuing a variety of licences. Would you support this proposal? Why (1 mark)

(Total: 20 marks)

QUESTION THREE

- (a) Give a brief definition of value added tax (VAT). (2 marks)
- (b) Explain in numbered paragraph the case for and against VAT in your country. (8 marks)
- (c) Saika Co. Ltd. a manufacturer, purchases raw materials at Sh.1,000,000. The company then incurs conversion costs which are estimated at 40% of material cost. The profit mark-up is 20% of total cost. The completed product is sold to Chemuka Wholesalers who then incur conversion costs of 50% on cost. The wholesalers mark-up is 10% on cost. The wholesaler sells the product to a retailer, who has no conversion costs but sells at a profit of 30%.

Required:

Assuming VAT is charged at 15% on all products, compute the total VAT payable.
(10 marks)

(Total: 20 marks)

QUESTION FOUR

(a) Explain the concept of elasticity with respect to:

- (i) Direct Tax (2 marks)
- (ii) Indirect Tax. (3 marks)

(b) Name five objectives of raising taxes and explain how they are achieved by the government.

(15 marks)

(Total: 20 marks)

QUESTION FIVE

(a) Explain the meaning of the term "Residence" when applied to a company under Kenya Income Tax Act.

(5 marks)

(b) Chumex Limited makes its accounts to 31 December of each year and has prepared the following profit and loss account for 2013:

	Notes	Sh.	Notes	Sh.
General administrative expenses		40,000	Gross profit b/d	200,000
Repairs and renewals	(i)	12,000	Bad debts previously written off	1,000
Depreciation	(ii)	2,000	Dividends (Gross) (vii)	5,000
Subscriptions and donations	(iii)	8,000	POSB interest	6,000
Bad debts		5,000	Gain on sale of plant and machinery	10,000
Directors' fees and expenses		2,500	Tax refunded	20,000
Patents written-off	(iv)	3,000		
Preliminary expenses	(v)	50,000		

Retirement benefits	30,000	
Rent, rates and insurances (vi)	41,500	
Legal and accountancy	2,500	
Interest on overdue tax	5,000	
Interest in lieu of dividends	<u>30,500</u>	
Net profit before taxation	<u>242,000</u>	<u>242,000</u>

Notes

(i)	Repairs and renewals:	Sh.
	Redecoration of an existing business	3,000
	Renovation to new building	5,000
	Partition and carpeting offices	<u>4,000</u>
		<u>12,000</u>
(ii)	Subscriptions and donations	Sh.
	National Chamber of Commerce and industry	1,000
	NE Refugee Fund	<u>1,000</u>
		<u>2,000</u>
(iii)	Bad debts:	
	This is on account of a previous company employee who cannot now be traced.	
(iv)	Preliminary expenses:	Sh.
	Legal fee on issue of shares on stock exchange	2,000
	Payment for stationery before commencement of business	<u>1,000</u>

		<u>3,000</u>
(v)	Retirement benefits:	Sh.
	NSSF Contribution	5,000
	Registered Pension Scheme for senior management	40,000
	Gifts to retiring staff	<u>5,000</u>
		<u>50,000</u>
(vi)	Legal and Accountancy:	Sh.
	Staff service agreement	2,000
	Audit fees	30,000
	Legal fee for lease (non-renewable)	4,000
	Legal fee – Plot acquisition	<u>5,500</u>
		<u>41,500</u>
(vii)	Dividends:	
	These were from a subsidiary company where Chumex owns 60% of the shares.	
(viii)	Capital Allowances for 2013 have been agreed at Sh.30,000	

Required:

- (a) Compute Corporation tax liability for 2013.
- (b) State the dates when such tax should be paid. (15 marks)

(Total: 20 marks)