KASNEB

CPA PART III SECTION 6

ADVANCED PUBLIC FINANCE AND TAXATION

THURSDAY: 26 May 2016.

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 2015.

Monthly t	axa	ble pay	Annual taxable pay			Rate of tax
(5	Sh.)		(Sh.)		% in each Sh.	
1	-	10,164	1	-	121,968	10%
10,165	holes	19,740	121,969	ing:	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 rel	ief S	Sh.1.162 per mo	onth (Sh 13 944 ner	anr	um) ATAC 1945	used teachire teaching

Prescribed	benefit rates	s of motor vehicles	provided by employer
		Monthly ra	

				LONG THE PARTY OF	withing rates	Annual rates	
					(Sh.)	(Sh.)	
Capital allowance:			(i) Saloons, H	latch Backs and Es	tates	he allow with allow	
Wear and tear allows	ance:		Up to	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	103/100	
Software	20%		Over	3000 cc	14,400	72,800	
					1576	And desired	
Industrial building a	llowance:					All Subjects	
Up to 2009		2.5%					
From 1 January 20	010	10%				and the first and the second	
Hotels		10%					
Hostels/Education	/Film producer	S					
buildings		100%					
From 1 January 20	010 -			TABLESS NAME OF STREET		SECTION OF THE SECTION OF	
Commercial build						- 25/ \$66 \$ 66 \$ 400 to	
(Shop, office or sh		25%				NATES MAINTAIN	
		20,0				BUSTE BUILDING	
Farm works allowand	ce	100%	(ii) Pick-ups, P	anel Vans (unconv	verted)	ners i "Stanta" i tera	
Investment deduction	allowance	100%	Up to	1750 cc	3,600	43,200	
			Over	1750 cc	4,200	50,400	
Shipping investment	deduction	100%	THE VIEL OF	1,50 00	1,200	30,700	
(Ships over 125 to			(iii) Land Rove	rs/Cruisers	7,200	86,400	
						and the case of the case of	

Extraction expenditure:

Written off over 5 years (20%)

Commissioner's prescribed benefit rates

		Monthly rates	Annual rates
Serv		Sh.	Sh.
(i)	Electricity (Communal or from a generator)	1,500	18,000
(ii)	Water (Communal or from a borehole)	500	6,000
Agri	culture employees: Reduced rates of benefits		
(i)	Water	200	2,400
(ii)	Electricity	900	10,800

QUESTION ONE

Country Y has recently introduced a number of reforms with regard to public sector financial management. One of the (a) reforms involved the establishment of a debt management office (DMO).

Required:

Discuss four possible roles of the DMO as established in Country Y.

(8 marks)

- (b) Citing four reasons, assess the importance of public investment reports as prepared by the National Treasury or equivalent ministry in your country. (4 marks)
- (c) In the context of the Public Private Partnerships Act, 2013 or equivalent legislation in your country:
 - (i) Explain the nature of public private partnerships (PPPs).

(2 marks)

(ii) Discuss three factors that have motivated the growth of PPPs.

(6 marks) (Total: 20 marks)

QUESTION TWO

Weka Enterprises is a small retail business dealing in fast moving consumer products. The Revenue Authority suspects that the business has been filing fraudulent returns and has requested for financial statements from the business. The business provided the following details for the years ended 31 December 2015 and 31 December 2014:

Income statement for the year ended 31 December 2015

			Sh.	Sh.
Turnover	eore esta	Mey Walley To John 5		27,840,000 -
Less cost of goods sold	d estes in			(15,354,000)
Gross profit	(.62)			12,486,000
Proceeds from sale of	furniture	andrea una estante		240,000
Capital gain on sale of	plot			156,400
				12,882,400
Less expenses:				
Purchase of furniture	000X -	594083	360,000	
General expenses			2,367,800	
Rent and rates			160,000	
Depreciation on motor	vehicle		94,600	
Customs duty			124,200	
Hire purchase cost			226,000	
Salaries and wages			1,680,000	(5,012,600)
Net profit				7,869,800

Statement of financial position as at 31 December		
	2015	2014
Non-current assets:	Sh.	Sh.
Furniture at cost	348,000	460,000
Motor vehicle at cost	1,660,000	1,565,400
(barrycroam) and /	2,008,000	2,025,400
Current assets:		
Inventories 1995.4	4,389,600	2,881,000
Accounts receivable	740,400	1,640,000
Prepaid general expenses	178,200	98,000
Prepaid rent and rates	72,800	24,600
Cash and cash equivalents	_300,000	183,000
Total assets	7,689,000	<u>6,852,000</u>
Financed by:		
Capital	1,000,000	800,000
Add net brottt	7,869,800	_5,780,000
	8,869,800	6,580,000
Less drawings	(2,200,000)	(1,320,000)
	6,669,800	5,260,000
Current liabilities:		
Accounts payable	979,200	1,528,000
Accrued rent and rates	24,000	36,000
Interest due on hire purchase	<u>16,000</u>	28,000
Total capital and liabilities	7,689,000	6,852,000

Additional information:

- 1. Turnover and purchases were inclusive of VAT at the rate of 16%.
- 2. The turnover excludes cash sales. During the year ended 31 December 2015, the business paid the following expenses out of cash sales:

	Sh.
Telephone and postage	48,000
School fees	142,800
Repairs and maintenance	94,600
Insurance	36,600

3. The bank balance is included in the cash and cash equivalents. The following details were included in the bank statement:

	Sh.
Personal expenses	294,000
General expenses	792,800
Rent and rates	68,400
Hire purchase interest	29,600
Payments to creditors	2,460,000
Receipts from debtors	5,890,000

4. The following assets used by the business were not included in the assets register:

	Sh.
Computers	368,000
Fax machine	120,000
Saloon car	2,800,000
Delivery van	720,000
Computer software	150,000

The Revenue Authority has established that the statement of financial position forms a good basis for recomputing the profit. All expenses are to be adjusted on the basis of the statement of financial position.

Required:

- (a) Using suitable computations, confirm the accuracy or otherwise of the taxable profit of West Enterprises for the year ended 31 December 2015. (15 marks)
- (b) Summarise five types of preliminary information that you might require from the business in order to further ascertain the accuracy of the taxable profit. (5 marks)

(Total: 20 marks)

QUESTION THREE

- (a) Tax information exchange agreements (TIEAs) are increasingly forming part of the agenda during bilateral and multilateral trade discussions among various countries.
 - (i) Explain the nature of tax information exchange agreements.

(2 marks)

(ii) Citing three reasons, discuss the purpose of TIEAs.

(6 marks)

(b) Zawadi Ltd. has been in operation since 1 January 2014. The company is under a tax investigation relating to value added tax (VAT) transactions.

The following details were obtained from the company's records for the month of September 2015:

- Stock in trade brought down in the month of September 2015 was valued at Sh.719,200.
- Sales ledger records in the company's books showed an amount of Sh.1,786,400 while as per VAT returns, it was Sh.1,429,120.
- The company had not claimed input tax on a building put into use on 1 January 2014 at a cost of Sh.2,784,000. However, in September 2015, the company set-off the input tax against the output tax for the month.
- Purchases amounting to Sh.174,000 did not have supporting fiscal receipts. The total purchases amounted to Sh.928,000.
- Since 1 January 2014, the company had not been filing VAT returns on time and all the penalties are outstanding.

- The company had imported goods on cost, insurance and freight (CIF) terms of Sh.450,000. The clearing and transport costs amounted to Sh.80,000 and Sh.60,000 respectively. The goods were later sold at a mark up of 20%. Import duty on these goods was at a rate of 20%.
- Tax officers established that imports were understated by Sh.150,000 as per import documents.
- Input tax on fuels and oils for motor vehicles used in the business amounted to Sh.51,200.
- Returns outward journal was understated by Sh.139,200 while the purchases ledger was overstated by Sh.174,000.
- Debit notes received by the company were overstated by Sh.232,000.
- Credit notes issued to customers were overstated by Sh.162.400.
- Input tax on catering services amounting to Sh.12,800 had been debited in the VAT account.
- Further examination revealed that VAT records needed recomputation to establish the correct VAT position.

Transactions are inclusive of VAT at a rate of 16% where applicable.

Required:

Analyse the above records and compute the correct VAT position for Zawadi Ltd. for the month of September 2015.

(12 marks)

(Total: 20 marks)

QUESTION FOUR

(a) Evaluate four features that distinguish tax havens from other taxation regimes.

(8 marks)

(b) Salama Insurance Company Ltd. provided the following financial records for the year ended 31 December 2015:

	Sh. of the
Gross premium	14,890,000
Reserves for unexpired risk (1 January 2015)	
Re-insurance premiums paid	384,000
Claims paid	9,364,000
Claims due: 1 January 2015	670,000
31 December 2015	800,000
Life assurance fund	1,240,800
Commission on reinsurance ceded	760,200
Commission on reinsurance accepted	1,940,000
Foreign exchange loss	342,500
Rent income	678,300
Purchase of computers	300,000
Cost of computer software .	150,000
Claims recovered on reinsurance	562,800
Agency expenses	1,380,700
Investment income	1,824,300
Management salaries	948,200
Repair of rented property	28,800
Neon signs	48,000
Depreciation	150,400
Legal expenses relating to claims	64,800
Rent and rates	760,400

Additional information:

- 1. The company operates both general insurance business and life insurance business in the same building where rent and rates are shared in the ratio of 2:3 respectively.
- 2. Agency expenses include general manager's salary of Sh.280,000 working in the life insurance business.
- 3. Investment income includes dividends of Sh.114,000 net of tax from a subsidiary company and Sh.78,400 from proceeds of sale of a car involved in an accident.
- 4. Gross premium includes sale of insurance policies to life insurance company amounting to Sh.748,400.
- 5. The company constructed a commercial building with shops, offices and showroom at a cost of Sh.6,400,000 on 1 January 2015. Rent income from the property amounted to Sh.5,536,400 before deducting capital allowances and expenses amounting to Sh.84,600.

Required:

(i) A statement of taxable profit or loss for the year ended 31 December 2015.

(10 marks)

(ii) Tax payable (if any).

(2 marks) (Total: 20 marks)

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QUESTION FIVE

(a) Country Z has recently been admitted into a regional economic block. As part of the country's full integration into the economic block, it is required to undertake certain legislative and other reforms.

Required:

Advise Country Z on four fundamental reforms that could be considered in the process of integration into the economic block. (8 marks)

- (b) Mjengo Ltd. is a real estate development company. In the year ended 31 December 2015, the company provided the following information:
 - Bought 100 acres at Sh.6,000,000 each for building low cost houses in an approved development area.
 - Cost of surveying was Sh.4,600,000 and conveyance fees amounted to Sh.6,960,000.
 - The cost of constructing each unit was Sh.1,450,000. The company constructed 240 units on a 20 acre piece of land.
 - All the units were sold at a price of Sh.1,600,000 in the year 2015.
 - Building materials for constructing each unit amounted to Sh.742,400 inclusive of VAT at the rate of 16%.
 - Professional fees paid to quantity surveyors inclusive of VAT was Sh.417,600 and for civil engineers was Sh.243,600.
 - Drainage system and sewerage line cost Sh.960,000 for connecting all units built and to be built on 100 acres.
 - The interest on loan to acquire the 100 acres was Sh.7,800,000.
 - Hire expenses for bulldozers used in the construction was Sh.600,000 for each of the three months used for the construction.
 - Charges paid to the government in respect of approval of plans were Sh.678,000.
 - Cost of constructing a site office was Sh.800,000.
 - Hire cost for a saloon car for the site manager was Sh.40,000 per month.
 - A commercial building was also constructed at a cost of Sh.5,600,000 in a part of the land. The building was rented at a monthly rent of Sh.480,000 with effect from 1 May 2015.
 - The costs relating to the total 100 acres are to be apportioned according to the acreage used.

Required:

(i)	tatement of adjusted taxable profit or loss for Mjengo Ltd. for the year ended 31 December 2015, AN tha	irks)

marks)	ii) Tax payable by Mjengo Ltd. (if any) for the year ended 31 December 2015.	(ii
w marks)		