UNIVERSITY EXAMINATIONS

2022/2023 ACADEMIC YEAR

MAIN EXAMINATIONS

BACHELOR OF COMMERCE

COURSE CODE: BCF 322

COURSE TITLE: PUBLIC FINANCE

DATE: 19TH APRIL, 2023 TIME: 9.00AM - 11.00AM

INSTRUCTIONS TO CANDIDATES

1. Answer a total of **three** questions; question **one** and any other **two** questions.
2. Question **one** carries **30** marks and each of the other two questions carry **20** marks each.

SECTION A

Question One (Compulsory)

a) As a branch of economics, public finance is a science of management of money entailing the study of allocation of economic resources for achieving the goals of public affairs. Justify why public finance qualifies to be a science. **{5 marks]**

b) In an attempt to understand the theory of public finance, the newly posted head of accounting unit in Banana Ministry of Uwezo Country who was the Chief Accountant of Zalisha Agricultural Ltd, a private limited company is pondering on how to approach government accounting. You are required to contrast public and private finance. **[8 marks]**

c) The free rider problem is an economic concept of a market failure that occurs when people are benefiting from resources, goods, or services that they do not pay for. Identify the measures that the government can use to minimize this problem. **[5 marks]**

d) James Otieno is a hardware merchant. He purchases cement from Athi Cement Ltd. which he then sells to his customers. Both James Otieno and Athi Cement Ltd. require a profit margin of 20% on cost. Cement attracts 18% VAT. If the cost of production by Athi Cement Ltd. is Sh.220 per bag of 50Kg. At what price should James Otieno sell a bag of cement including VAT? **[5 marks]**

e) The management of Ajabu Limited has presented the following income statement for the year ended 31 December 2022:

	Shs	Shs
Gross profit		5,292,000
Other incomes		
Dividend from subsidiary company	200,000	
Interest from foreign bank account	4,000	
Discount received	28,000	
Refund of VAT	12,000	
Gain on sale of motor vehicle	14,000	258,000
		5,550,000

Expenditure

Salaries and wages	800,000	
NHIF contribution	30,000	
Subscription to trade association	50,000	
Hire purchase interest	15,000	
Bad debts written off	60,000	
General expenses	80,000	
Depreciation	25,000	
Legal expenses	40,000	
Insurance premiums	124,000	
Rent	66,000	
Electricity	34,000	
Purchase of furniture	26,000	1,350,000
Net profit		4,200,000

Additional information:

i) Capital allowances were agreed with the Revenue Authority at Sh.75,000

ii) Included in bad debts is a loan of Sh.15,000 due from a former employee of the company who was dismissed in October 2022.

iii) Legal expenses include Sh.20,000 incurred in defending a manager against a traffic offence.

iv) Insurance premiums include Sh.24,000 paid to the National Hospital Insurance Fund (NHIF) as a penalty for late submission of contribution.

v) The company paid stamp duty of Sh.6,000 relating to a piece of land purchased in August 2022. This payment is included in the rent expense for the year ended 31 December 2022.

Required: Compute the adjusted taxable profit or loss of Ajabu Limited for the year ended 31 December 2022. **[7 marks]**

Question Two

a) The 'Principle of Maximum Social Advantage' was introduced by British economist Hugh Dalton. It is the fundamental principle of Public Finance. It states that: "The best system of public finance is that which secures the maximum social advantage from the operations which it conducts.

Required:

i) Using appropriate diagrams, demonstrate how the maximization of social advantage takes place. **[6 marks]**

ii) Identify the assumptions of the Principle of Maximum Social Advantage **[4 marks]**

b) Market failure is a situation defined by an inefficient distribution of goods and services in the free market. Arising from this situation, the Kenya Government had previously embraced subsidy principle as one of the measures to minimize market failure. You are required to assess the causes of market failure. **[10 marks]**

Question Three

a) While the fiscal policy deals with taxation and expenditure, the monetary policy consists of decisions and actions taken by the Central Bank to ensure that the supply of money in the economy is consistent with growth and price objectives set by the government. Evaluate five monetary policies employed by the Central Bank of Kenya. **[10 marks]**

b) You have recently been appointed as a Finance Manager of Bidii Company Limited, a Semi-Autonomous Government Agency. Part of your duties is to ensure prudent and transparent management of funds of Bidii Company Limited.

Required:
Reference to Public Finance Management Act 2012, discuss five fiscal responsibility principles that you will apply to fulfill your duties. **[10 marks]**

Question Four

a) Reference to incidence of tax, distinguish between forward and backward shifting. **[4 marks}**

b) According to Musgrave "A change in the distribution of income available for private use which arises as a result of changes in budget policy is called incidence.". Discuss five forms of this tax incidence. **[10 marks]**

c) Fiscal policy is the policy of government related to its own expenditure and taxes in order to influence the aggregate demand (AD) by applying the following equation: $Y = C + I + G + (X - M)$.

Required:
Using this equation, demonstrate how the government influences the economic activity. **[6 marks]**

Question Five

a) The Electronic Project Monitoring Information System (e-ProMIS) is the Government of Kenya's main platform for monitoring the performance and implementation of development projects and programs.

Required: Identify the objectives of e-ProMIS **[12 marks]**

b) The Debt Management Strategy paper prepared Mid-term by The National Treasury's Debt Management Department is generally referred to as "The Medium-Term Debt Management Strategy (MTDS) "is one of the important deliverables of the National Treasury as provided under the PFM Act, 2012. Explain how the Kenyan government ensures transparency and accountability in debt management. **[8 marks]**