MACHAKOS UNIVERSITY

University Examinations for 2017/2018 Academic Year

SCHOOL OF BUSINESS AND ECONOMICS

DEPARTMENT OF ECONOMICS

THIRD YEAR SECOND SEMESTER EXAMS FOR

BACHELOR OF ECONOMICS AND STATISTICS

EAE 301: TAXATION ECONOMICS AND POLICY

DATE: 15/12/2017   **TIME: 2:00 – 4:00 PM**

INSTRUCTIONS

Answer Question ONE and any other TWO questions

QUESTION ONE (COMPULSORY) (30 MARKS)

(a)   Using Kenya as an examples, explain the factors that increase its taxable capacity and those that reduce it .   (10 marks)

(b)   State and explain difference between a tax and fee.   (5 marks)

(c)   The government is interested in taxing sugar in order to increase its tax revenue. The market is currently at equilibrium at a price of Ksh. 10 per kg and sales of 1000 kgs per month. Suppose that own price elasticity of demand at the equilibrium point is 0.1 and the own price elasticity of supply at this point is 0.2. The government announces that the tax measure with the new market price to be maintained at Ksh 15 per kg.

Required

         (i) Compute and show the suppliers and buyers tax burden.   (5 marks)
         (ii) How much will the government get from the new tax measure?   (5 marks)
         (iii)Calculate the deadweight loss of the tax (excess burden of the tax).(5 marks)

QUESTION TWO (20 MARKS)

(a)   In which ways are taxes shifted to others in taxed transactions in your country (5 marks)
(b)   Using appropriate examples of taxes, explain the differences in the extent of tax shifting
                                               (5 marks)

(c)   The demand curve and total cost curve for a firm are as follows

Q = 200 – 2P
C = 10Q + 0.25Q2

Derive the price and output effects under Perfect competition and under monopoly:

(10 marks)

    (i) When a sh 5 is imposed as tax
    (ii) When advalorem tax of 10% of the price is imposed.

QUESTION THREE (20 MARKS)

(a)   Distinguish between the following.   (6 marks)
    (i) Incentive effect and disincentive effect of income tax
    (ii)   Substitution effect and Income effect of income tax on Savings

(b)   Suppose the labour supply curve for an economy is given as: $L_s = -100 + 200W_t$,

where w_t is the after tax wage rate. Assuming the before tax wage rate is fixed at

Sh.10.   (14 marks)

    (i) Determine an expression for Tax revenues as a function of the tax rate (t)
    (ii) Sketch the Tax function and determine the optimal tax rate
    (iii)Suppose the tax rate was set at 70%, what advice would you give to the state

QUESTION FOUR (20 MARKS)

(a)   Distinguish between tax evasion and tax avoidance.   (5 marks)
(b)   Using the case of your country, Identify the various ways in which people commit tax
        fraud.   (10 marks)
(c)   Explain the various strategies your government could use to minimise tax evasion
        and avoidance.   (5 marks)

QUESTION FIVE (20 MARKS)

"Complete decentralization may not be very optimal for a country" Discuss.   (20 marks)