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YOUR WEALTH

**QUESTION A**

**Objective of the question: to demonstrate the ability to convert financial information from the accrual basis of accounting to the cash basis; and to demonstrate the ability to read and extract critical/relevant information from extracts of financial statements and additional information provided that can be used to prepare components of the statement of cash flow.**

Prepare the cash flows from operating activities section of the statement of cash flows for the reporting period ended 30 April 2019. Comparatives are NOT required. Show all workings. The extract must include the following:

(a) Cash received from customers,
(b) Cash paid to suppliers and employees,
(c) Taxation paid, and
(d) Payments to financiers (debt and equity).

[25 marks]

| Statement of cash flow (extract) | | | **Marks** |
|---|---|---|---|
| for the reporting period ended 30 April 2019 | | | |
| Cash flows from operating activities: | | | |
| Cash received from customers | W1 | 8,830,000 | **4** |
| Cash paid to suppliers and employees | W2 | (7,606,000) | **13** |
| Cash generated from operations | | 1,224,000 | |
| Taxation paid | W3 | (750,000) | **1.5** |
| Interest paid | | (22,500) | **0.5** |
| Dividends paid | | (83,000) | **2** |
| Cash generated from operating activities | | 1,592,500 | **0.5** |
| | | | |
| W1: Debtors account | | | |
| Opening balance | 275,000 | | **0.5** |
| Add: Sales | 9,000,000 | | **0.5** |
| Add: Revenue in advance | 5,000 | | **1.5** |
| Less: Closing balance | (450,000) | | **0.5** |
| Cash received | 8,830,000 | | |
| | | | |
| W1.1 Revenue in advance | | | |
| Opening balance | (20,000) | | |
| Less: Closing balance | 25,000 | | |
| Cash received | 5,000 | | |
| | | | |
| W2: Cash paid to supplies & employees | | | |
| Cash paid to suppliers | (4,782,500) | | **5** |
| Expenses paid | (2,823,500) | | **6** |
| Cash paid to suppliers & employees | (7,606,000) | | |

| | | | |
|---|---|---|---|
| W2.1 Inventory | | | |
| Opening balance | 425,000 | | **0.5** |
| Less: Cost of goods sold (9,000,000 x 1/2] | (4,500,000) | | **1** |
| Less: Closing balance | (650,000) | | **0.5** |
| Purchases | (4,725,000) | | |
| | | | |
| W2.2: Supplier | | | |
| Opening balance | (360,000) | | **0.5** |
| Add: Purchases | (4,725,000) | | **0.5** |
| Less: Closing balance | 325,000 | | **0.5** |
| Add: Interest accrued | (22,500) | | **1** |
| Cash paid | (4,782,500) | | |
| | | | |
| W2.3: Operating expenses | Accrued | Prepaid | |
| Opening balance | (18,000) | 6,500 | |
| Less: Closing balance | 15,000 | (8,000) | |
| Movement in expenses | (3,000) | (1,500) | |
| | | | |
| W2.4: Operating expenses | | | |
| Net operating costs | (3,190,000) | | **0.5** |
| Non-cash items adjustments: | | | |
| Depreciation | 277,000 | | **1** |
| Profit on sale of vehicle | (15,000) | | **0.5** |
| Loss on sale of plant | 34,000 | | **0.5** |
| Goodwill written off | 30,000 | | **1** |
| Interest expenses | 45,000 | | **0.5** |
| Movement in prepaid expenses | (1,500) | | **1** |
| Movement in accrued expenses | (3,000) | | **1** |
| Cash expenses paid | (2,823,500) | | |
| | | | |
| W3: Other costs paid | Taxation | Dividends | |
| Opening balance | (310,000) | (48,000) | **0.5** |
| Less: Closing balance | - | 105,000 | **0.5** |
| Add: Provisional tax payments | (440,000) | | **1** |
| Add: Dividends declared | | (175,000) | |
| Less: Dividend in specie | | 35,000 | **1.5** |
| Taxation paid | (750,000) | (83,000) | |
| | | | **Max: 25** |

**QUESTION B**

**Objective of the question: demonstrate the ability to interpret ratios in terms of the context of the business and providing insight and understanding of the financial statements and business in order to provide a report to management.**

Analysing the ratios as per the schedule and comment on the liquidity and cash position of the business. The analysis should focus on:
(a) liquidity ratios

[6 marks]

| | **Marks** |
|---|---|
| Liquidity Analysis: | |
| Although the current ratio increased significantly in the context of the business which reduce the financial risk to the short-term supplier. However, the current ratio of the business is below that of the industry average indicating that although the business is closing the gap it is still under performing in relation to the industry. | **2** |
| The acid test ratio increased marginally which reduces the payment risk to the short-term supplier. However, the ratio is well below the industry average (approximately half) which indicates that the business may be facing cash flow challenges. | **2** |
| Cash ratio of the business decreased significantly to a negative indicating a significant deterioration of the cash position of the business. The ratio in comparison to the industry average displays a bleak situation for the business. | **2** |
| | **Max: 6** |

(b) operating cash cycle

[10 marks]

| | | | | Marks |
|---|---|---|---|---|
| | 2019 | 2018 | Industry Average | |
| Inventory holding period | 52.7 | 37.8 | 35.6 | |
| Debtors' collection period | 18.2 | 12.2 | 25.9 | |
| Cash conversion period | 70.9 | 50 | 61.5 | **1** |
| Supplier' payment period | 25.1 | 28.3 | 36.8 | |
| Cash operating cycle | 45.8 | 21.7 | 24.7 | **1** |
| The business significantly reduced its ability to convert its goods into sales (more than 50% of previous year performance) which indicates the level of competition the business is facing - business needs to review its strategy objectives and plans. This may also indicate that the business is stock piling which may increase the level of obsolescence and inventory losses - cash is tied up in goods for longer periods. | | | | **2** |
| The debtors' collection period has increased by approximately 6 days which indicates that the business is taking longer to convert its debtors into cash. However, the business collects its cash from customers at a rate faster than the industry average which indicates that the business an excellent debtors' collection system. | | | | **2** |
| The cash conversion period has increased by 20 days which places a significant strain on the operating cash of the business and may place the business at risk in terms of self-financing its operations. The cash conversion performance of the business has deteriorated to a situation where it is below that of the industry average. | | | | **2** |
| The supplier' repayment period declined by 3 days indicating that the short-term supplier are concerned about the credit rating of the business and are demanding payment over shorter periods. The business pays its supplier over periods which as approximately 11 days quicker than the industry average indicating the supplier has regarded the business as a financial risk. | | | | **2** |
| The operating cash cycle has doubled which indicates the operating risk that the business is facing - the business is becoming less self-sustaining and depends more on external funding for its operations. This is double that of the industry average which reflects the deteriorating cash flow position of the business. | | | | **2** |
| | | | | **Max: 9** |

**QUESTION C:**

**Objective of the question: demonstrate the ability to identify the nature and type of supply and select the appropriate provisions of the VAT Act which applies to the transaction.**

Discuss the VAT implications for the sale plan of management to sell the jewellery including the additional services rendered (insurance and transportation) to the foreign customers.

[4 marks]

| | **Marks** |
|---|---|
| The jewellery will be sold to customers outside of South Africa which is classified as an export - the supply of export goods is zero rated. | **2** |
| The rendering of transport services for goods will be zero rated, if it is transported from a place in South Africa to a place in an export country. | **1.5** |
| Where goods are exported and additional services are supplied, in this case the insurance of the goods, it will also be zero rated. | **1.5** |
| | **Max: 4** |

**QUESTION D:**

**Objective of the question: demonstrate the ability to use financial management information to make capital budgeting decisions using the net present value method as wellas understanding the qualitative factors that impacts on investment decision-making.**

Management approved the acquisition of Machine C as it has the longest estimated useful life. Discuss whether management selected the best investment opportunity based on the using the net present value method or annual equivalent when using the net present value method.

[3 marks]

| | **Mark** |
|---|---|
| When applying the net present value method for selecting investment options with different useful live, the selection should be based on the annual equivalent rather than the net present value. Machine B should be selected as it has the highest annual equivalent, but the difference with Machine C which has a longer useful life should also be taken into consideration. Conclusion: based on the net present value method the decision of management is incorrect. | **1**<br>**1**<br>**1** |
| | **Max: 3** |

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**QUESTION E:**

**Objective of the question: demonstrate the ability to apply financing desion-making techniques (calculations) which contribute to minimise the cost to the business (less cost impact and cash flow) taking into account the tax implications of the decision.**

Advise management which option should be selected between the cash purchase and the finance lease, in order to finance the acquisition of Machine C. Support your recommendation with calculations and reasons.

[14 marks]

| Cash purchase: | | **Marks** |
|---|---|---|
| Immediate cash outflow | (780,000) | **0.5** |
| Present value of tax saving in respect of wear & tear: [(780,000 x 20% x 28%) @ 15% for 5 period from 2nd period] - 43,680 x 2.9149 | 127,324 | **3.0** |
| Net present value of cash outflows | (652,676) | **0.5** |
| Finance lease: | | |
| Immediate rental payment | (135,000) | **0.5** |
| Present value of rental payments: [135,000 @ 7.5% for 7 periods] - 135,000 x 5,2966 | (715,041) | **3.0** |
| Present value of tax saving for deduction [(270,000 x 28%) @ 15% for 4 years from 2nd year] - 75,600 x 2.4826 | 187,684 | **2.0** |
| Net present value of cash outflows | (662,357) | **0.5** |
| Recommendation: the company should select the finance lease option to acquire Machine C. | | **1** |
| | | **Max: 14** |

**QUESTION F:**

**Objective of the question: demionstrate the ability identify transactions relating to establishing an operating activity for the recognition of the related expenses between capitalisation of costs and expenses.**

Discuss whether the manner in which the financial accountant treated of the operating license and training costs incurred by the company were correctly classified and recognised in the accounting records for the reporting period ended 30 April 2019 in compliance with the accounting records.

[7 marks]

| | **Marks** |
|---|---|
| Operating license:<br>The costs to acquire the operating license was not relating to a specific asset but for the entire operations - cannot be capitalised to the cost of the asset as the estimated useful lives of the machinery and the license differ. The operating license provides the company the right to operate and must be recognised as an intangible asset.<br>Conclusion: the treatment by the accountant is incorrect as operating license should be recognised as an intangible asset. | <br><br><br><br><br>**2.5**<br><br>**1** |
| Training cost:<br>Generally training costs are incurred for the development of the skills utilise the machine effectively and is therefore recognised as expenses. However, as the training was specific to the to the machine which may indicate that the costs should be capitalised to the cost of the machine -the training cost may be treated as a direct cost to make the machine ready for its intended use.<br>Conclusion: the statement is incorrect as the training cost does not relate directly to making the machine available for use, the costs should be expensed. | <br><br><br><br><br>**2.5**<br><br>**1** |
| | **Max: 7** |

**QUESTION G:**

**Objective of the question: demonstrate the ability to correct the journal entries for the capitalisation of the costs are part of an asset – including the correction of the depreciation.**

Record the correcting journal entries if the treatment of the operating license and training costs were incorrectly recorded by the reporting period ended 30 April 2019 in compliance with the accounting standards.

[5 marks]

| | | | Marks |
|---|---|---|---|
| | Debit | Credit | |
| Intangible asset - Operating license | 120,000 | | **1.5** |
| Training expense | 98,000 | | **1** |
| Machinery – cost | | 218,000 | **0.5** |
| [Correction of the costs capitalised to the machine costs] | | | |
| Accumulated depreciation – machinery | 32,700 | | **1.5** |
| Depreciation expense | | 32,700 | **0.5** |
| [Correction of the depreciation relating to the costs capitalised – (218,000 x 20% x 9/12)] | | | |
| | | | **Max: 5** |

**ALTERNATIVE SOLUTION**

| | | | Marks |
|---|---|---|---|
| | Debit | Credit | |
| Intangible asset - Operating license | 120,000 | | **1.5** |
| Training expense | 98,000 | | **1** |
| Input VAT Control | 32,700 | | **1** |
| Bank/Suppliers | | 250,700 | **0.5** |
| [Recognition of expenses incurred relating to the machinery] | | | |
| | | | **Max: 5** |

**QUESTION H:**

**Objective of the question: demonstrate the treatment sales and cost of sales transactions which occur in different year of assessments in respect of transactions with foreign customers.**

Discuss how the sales transaction together with the manufacturing costs should be treated in the calculation of taxable income for the 2019 and 2020 year of assessment.

[10 marks]

| | **Marks** |
|---|---|
| Sale transaction:<br>Gross income should be recognised on the earlier of the cash received or receivable (accrued to). Furthermore, a sales transaction is received when the risks and rewards associated with ownership of the goods are transferred from the seller to the buyer and the amount of the sales can be quantified - if the amount cannot be quantified, the recognition as gross income is postponed until it can be quantified (s24M).<br>Year of assessment 2019: the deposit of R 500,000 will be recognised based on the actual cash received.<br>Year of assessment 2020: the balance of the amount quantified R 850,000 (1,350,000 - 500,000) will be recognised as gross income. | <br><br>**1**<br><br>**1**<br><br>**1**<br><br>**1**<br><br>**1** |

| | |
|---|---|
| Manufacturing costs:<br>Amounts can be treated as deductions when they were actually incurred or the goods when delivered to the buyer - not treated as part of closing inventory. Year of assessment 2019: as the goods are not held by the seller the manufacturing costs can be treated as a deduction.<br>However, as the deductions must be income to generate income, the deduction must be limited to the gross income recognised - cannot create a loss on the transaction (s23F).<br>Year of assessment 2019: the deduction is limited to gross income R 500,000 recognised.<br>Year of assessment 2020: the loss OF R 150,000 (amount not treated as a deduction) is carried forward and treated as a deduction when the balance of sale is treated as gross income. | **1**<br>**1**<br>**1**<br>**1**<br>**1** |
| | **Max: 10** |

**Alternative answer:**

| | |
|---|---|
| 2019 year of assessment: | |
| In terms of **s22**, the cost of inventory is R650 000.<br>The cost of the inventory can be claimed as a deduction under **s 11(a)**. | 1<br>1 |
| The sale of the piece of jewellery to the customer was concluded in the 2019 year of assessment but the final selling price of the jewellery could not be determined during the 2019 year of assessment as the appraiser only did the valuation on 3 March 2019.<br>**Section 24M(1)** provides that if a person disposes of an asset for a consideration that cannot be quantified in that year of assessment,<br>• **the unquantified portion of the price will be deemed not to have accrued in that year of assessment; and**<br>• **it is deemed to accrue in the year it becomes quantifiable.**<br>The final selling price of the piece of jewellery could only be determined after the 2019 year of assessment. **The provisions of s24M are applicable and the portion of the final selling price that cannot be quantified (R850 000) did not accrue to MFTW during the 2019 year of assessment.** | 1<br>1<br>1<br>1 |

| | |
|---|---|
| **The R500 000 deposit received by MFTW will be included in MFTW's gross income for the 2019 year of assessment as it received the amount for its own behalf and for its own benefit.** | 1 |
| **Section 23F(2)** provides that:<br>• **where a taxpayer has during any year of assessment disposed of trading stock in the ordinary course of his trade,**<br>• **and the full consideration does not accrue to him during such year,**<br>• **any expenditure incurred in respect of the acquisition of such stock during such year which would otherwise be deducted must, to the extent that it exceeds any amount received or accrued from the disposal of that stock be disregarded**<br>A portion of the selling price of the piece of jewellery did not accrue to MFTW due to the provisions of s24M. **The provisions of s23F(2) will, therefore, apply in limiting the deduction allowable under s11(a) for the expenses incurred in the production of the piece of jewellery.** | 1<br>1<br>1 |
| The amounts included in taxable income will be determined as follows: | |
| Gross income (deposit received) — 500 000 | |
| Purchases — **(650 000)** | 1 |
| Loss — (150 000) | |
| The loss is disregarded under s23F(2) — **150 000** | 1 |
| Taxable income — - | |
| In the **2020 year of assessment, the amount of deduction that was limited under s23F(2) will be allowed as a deduction** | 1 |
| Gross Income (balance of purchase price) — **850 000** | 1 |
| Disregarded deduction s23F(2A) — **(150 000)** | 1 |
| Taxable Income — **700 000** | 1 |
| **Available** | **16** |
| **Maximum** | **10** |

**QUESTION I:**

**Objective of the question: demonstrate the ability to apply the provisions of the Income Tax Act to gratuity amounts paid to employees or their dependants.**

Discuss the income tax implications of the gratutious amount paid by the company for:

(a) the company, and

[4 marks]

| | **Marks** |
|---|---|

| | |
|---|---|
| Any amount paid by the company can only be treated as a deduction (s11(a)) if it is directly incurred to generate income or (s23(g)) if it is a necessary cost to carry out the activities of the business.<br>The gratuity amount was paid in relationship to the employee of the business and can therefore be treated as a deduction.<br>The possible risk is that the amount may be regarded as being capital in nature as it was not incurred in respect of the services rendered by the employee. | **1**<br>**1**<br><br>**1**<br><br>**1** |
| | **Max: 4** |

**Alternative answer:**

| | |
|---|---|
| For an expenditure to be deductible, it needs to meet all the requirements of the **section 11(a), read with section 23** | 1 |
| For an amount to be deductible **it needs to meet all the requirements of s11(a)** which requires a deduction from income of such person so derived | 1 |
| **Expenditure and losses** | |
| **Actually incurred** | |
| **During the year of assessment** | |
| **In the production of income** | |
| **Not of a capital nature** | 2.5 |
| **Either in part or full laid out or expended for the purposes of trade - s 23(g)** | 1 |
| The **onus of proof** is on the taxpayer in terms of **section 102 of the Tax Administration Act, to prove the amount is deductible.** | 1 |
| | |
| Damages to driver | |
| | |
| **The issue** is whether the amount is in the **production of income** | 1 |
| There must be a very **close connection between the trade or business carried on and the cause of liability for damages**. ***(PE Electric Tramway)*** | 1 |
| For an amount to be in the production of income, it needs to be a **necessary concomitant** of business operations. (***Joffe)*** | 1 |
| The **employment of drivers was necessary for carrying on of the business of the company and it is therefore a necessary concomitant of trade**. | 1 |
| Therefore the amount of R120 000 is **deductible in terms of s11(a)** | 1C |
| **AVAILABLE** | 9.5 |
| **MAXIMUM** | 4 |

(b) the driver and/or his family.

[3 marks]

| | **Marks** |
|---|---|

| | |
|---|---|
| An amount received should be included in gross income even if it not received directly by the taxpayer - but was for the benefit of the taxpayer. | **1** |
| As the amount was received by the family in respect the employee (sole bread winner) who was injured during working hours, the amount was received in respect of him being employed by the company. | **1** |
| The gratuity received by the family will be included in the gross income of the employee. | **1** |
| | **Max: 3** |

**QUESTION J:**

**Objective of the question: demonstrate the ability to apply the provisions of the VAT Act to the amount received from insurance claims.**

Discuss the VAT implications in respect of the indemity payment received from the insurance company.

[3 marks]

| | **Marks** |
|---|---|
| Indemnity received in respect of insurance claims must be viewed as an independent from the asset or activity that is insurance - must be viewed in respect of the insurance transaction.<br>If the input tax was claimed on insurance payments, then the insurance claim will be regarded as a deemed supply even though it represents a cash/finance transaction (exempt supply).<br>Output tax will be payable on the total indemnity received - even though the items insured may not all be taxable supplies. | **1**<br><br>**1**<br>**1**<br><br>**1** |
| | **Max: 3** |

**QUESTION K:**

**Objective of the question: demonstrate the ability to recognise the acquisition of an asset to replace a damaged one – de-recognition and acquisition.**

Record the transacton relating to the replacement of the motor vehichle that was damaged during the hi-jacking including the insurance claim recived in compliance with the accounting standards.

[6 marks]

| | | | **Marks** |
|---|---|---|---|
| | Debit | Credit | |
| Asset disposal account | 195,000 | | **0.5** |
| Accumulated depreciation | 175,000 | | **1** |
| Motor vehicle - cost | | 370,000 | **0.5** |
| [De-recognition of the motor vehicle destroyed] | | | |
| Bank | 500,000 | | **0.5** |
| Output VAT Control | | 65,217 | **1** |
| Asset disposal account | | 434,783 | **0.5** |
| [Recording the insurance claim received] | | | |
| Motor vehicle - cost | 486,957 | | **0.5** |
| Input VAT Control | 73,043 | | **1** |
| Bank | | 560,000 | **0.5** |
| [Acquisition of the replacement motor vehicle] | | | |
| | | | **Max: 6** |

**QUESTION L:**

**Objective of the question: demonstrate the ability to identiofy the conduct of a Professional Accountant (SA) that may violate the Code of Conduct and Ethical behaviour.**

Discuss the three possible areas where Mr. Sibaba violated any of the principles of the Code of Ethics in fulfilling his professional responsibilities as the chief accountant of the division.

[7 marks]

| | **Marks** |
|---|---|
| Mr. Sibaba may not be competent to perform the responsibility of appointing service providers which violates the fundamental principle of objectivity. | **1** |
| Mr. Sibaba process transactions without ensure that adequate supporting documentation are maintained and that internal control procedures are complied with - lack of reliability of maintaining reliable accounting records. | **2** |
| The large number of correcting journal entries may be an indication that Mr. Sibaba does not exercise due care when performing his responsibility as the accountant. | **1** |
| The appointment of family members may result in them not being qualified for the position which indicate a lack of integrity by Mr. Sibaba. | **1** |
| The preparation of different reports and set of financial statements indicate that Mr. Sibaba does not apply due care and diligence when fulfilling his responsibilities as a professional accountant. | **2** |
| | **Max: 7** |

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**QUESTION M:**

**Object of the question: to demonstrate the ability to draft a report in a logical and presentable form for management.**

Draft a report to senior management considering at least six items from the areas listed 1 – 9 by the internal auditors (KanKam), where the risks were identified and provide recommendations to mitigate the risks highlighted.

[8 marks]

| | | **Marks** |
|---|---|---|
| To: Management<br>Made-for-the-World (Pty) Limited | | **0.5** |
| re: Investigation of the risks in the Accounting Department | | **0.5** |
| We have been appointed to review and investigate the the activities and processes in the accounting division headed by Mr. Sibaba in terms of ISRS - 4400 (Agreed upon engagement). We have applied procedures during our investigation which are recommended by the engagement and internal auditing standards. The following schedule highlights the risks identifies together with recommendations to mitigate such risks. | | **2** |
| **Risks identifies** | **Mitigating plan** | |
| Appointment of approved suppliers were made at the discretion of Mr. Sibaba. | The risk of appointing suppliers at the discretion of Mr. Sibaba could give rise to the appointment of suppliers who are not suitably qualified or regarded as nepotrism. The appointment of suppliers should be made in terms of the procurement policy and procedures. The appointment of suppliers should made based on the procurement criteria and approved by a panel or senior official. | **2** |
| The lack of supporting documents for payment authorisation. | The risk of authorising payments without supporting documents/evidence increases the risk of payments for invalid transactions or fraud. Payments should be accompanied with supporting documents before they are authorised - a payment schedule together with supporting documents should be submitted to the official authorising the payments. | **2** |

| | | |
|---|---|---|
| There were a large number of journal entries to correct payment transactions. | Journal entries to rectify payments is an indication that all internal checks were not complied with and give rise to the covering up of unathorised and invalid payments or the employment of staff who are not competent for the task - increases the risk of the integrity and qualifity of the accounting information. Correcting journal entries should be supported with appropriate diocumentation and explanations. | **2** |
| An amount of R 1 000 000 was unaccounted for. | Any amounts which cannot be accounted is an indication of unauthorised payments or fraud. All payment made should be supported by supporting documents and compoly with all internal controls of the business. | **2** |
| The appointment of family members in the finance department by Mr. Sibaba. | The appointment of family members may increase the risk of not have qualified staff or the risk of collusion within the department. The appointment of staff should comply with the policies and procedures of the business under the management of the HR department. | **2** |
| A range of different financial reports circulated internally. | The risk of present different sets of financial reports may give an indication of the manipulation of reports and increase the quality and integrity of the accounting information. All reports must be prepared from a single financial information database, even though the manner of presenting the information may change for different users. | **2** |
| Different set of accounting standards and princples used to present reports. | The risk of using different accounting standards to present financial statements/reports results in the lack of consistency. All financial reports presented to external users should be based on the accounting standards which are applied consistency over consecutive periods - this ensures comparability. | **2** |
| Set of fabricated management accounts was presented to the bank. | The risk of presenting fabricated financial staatements to bankers is contrary to the governance and fiduciary responsibility of management. All financial reports must be based on the accounting records of the business. | **2** |
| Fear of staff members in the department. | The fear of staff in the department represent a governance and ethical risk in the organisation. In terms of governance management must provide channels of communication to address ethical dilemmas in the organisation. | **2** |

| | |
|---|---|
| This report was drafted in terms of the engagement standards and is based on the facts and evidence examined. This report can only be used for internal purposes and by the management of the business and cannot be used by parties not mentioned in this report. The report reflects on the activities and processes implemented in the accounting division up to an including date this report has been signed. | **2** |
| Yours faithfully | |
| Jonny Break-Through<br><br>Registered ACFE and IIA<br>12-Apr-19 | **1** |
| | **Max: 8** |

**QUESTION N:**

**Objective of the question: demonstrate the ability to advise clients as to the action that can be taken against a Professional Accountant for misconduct and unethical behaviour.**

Advise management what action should be taken by the company against Mr. Sibaba as he is a member of a local professional accountancy organisation.

[4 marks]

| | **Marks** |
|---|---|
| Management can deal with Mr. Sibaba through their internal disciplinary policies and procedures. | **1** |
| Management can report Mr. Sibaba to the PAO of which he is a member for misconduct - lay a charge against the member for investigation. | **1** |
| Management can report Mr. Sibaba to the regulatory organisation for misconduct - report the matter for investigation - report the member to SAQA if the PAO does not respond to the matter. | **1** |
| Management can institute a criminal case against Mr. Sibaba is the business suffered financial losses or damages. | **1** |
| | **Max: 4** |

**QUESTION O:**

Discuss the procedures that should be followed when conducting substantive tests on payments to suppliers

| Audit Objectives | Descriptions | Example procedures |
|---|---|---|
| Existence | The accounts payable balances shown on the trade supplier list should actually exist, i.e. genuine supplier and transactions. | Select balances from the supplier' list and trace them to the individual vendors' invoices and statements.<br>Confirm balances by sending confirmation letters to the vendors selected, emphasizing large amount of balance. |
| Completeness | All supplier balances outstanding at balance sheet date have been included in the supplier' list. | Perform out-of-liability tests. |
| Accuracy | The list of trade supplier balances and the total should be accurate. | Select the balances and agree to vendors' statement.<br>Perform out-of-liability tests. |
| Classification | The balances on the supplier' list are properly classified. | Review the suppliers' list to note any balance that is of interest-bearing, long term or debit nature. |
| Cut-off | The transactions in the purchases and payment cycle are included in the proper period. | Perform out-of-liability tests.<br>Perform cu-off tests. |
| Detail tie-in | The list of trade supplier balances should agree with purchase ledger accounts | Check the footing of the list and trace the total to the general ledger control account.<br>Select balances and trace them to individual |

| | | |
|---|---|---|
| | and general ledger control accounts. | vendors' ledger accounts for names and amounts. |
| Valid obligation | Client has the obligation to pay for the amount of liability shown on the balance of trade supplier. | Same as existence above. |
| Presentation and disclosure | The balances arising from transactions of purchases and payment cycle are properly presented and disclosed. | Review the financial statements to make sure that proper segregation has been done for interest bearing liabilities, current or long-term liabilities, and whether additional information has to be disclosed as note to the accounts, e.g. related party disclosures. |

**QUESTION P:**

**Objective of the question: demonstrate the ability to apply the provisions of the VAT Act to the acquisition of property.**

Discuss, supported with calculations, the VAT implications arising from the purchase of the building. Your answer must include the timing (periods) for claiming the input tax, if any.

[8 marks]

| | | Marks |
|---|---|---|
| The property was acquired from a registered VAT vendor thus the company will pay input tax rather than transfer duty. | | **1** |
| The input tax can only be claimed if the property is used to produce taxable supplies - company taxable and exempt supplies. If the taxable supplies (standard and zero rated) is below the threshold of 95%, then the input tax must be apportioned - can only claim 85% of the amount paid. | | **2** |
| The input tax becomes payable when the property is transferred into the name of the buyer or when the payment is made, but the amount than can be claimed is limited to the cash paid if the parties are not connected. | | **2** |
| Input tax that can be claimed: | | |
| - 30 June 2017: [17,250,000/2 x 15/115 x 87%] | 978,750 | **1** |
| - 31 July 2017: [17,250,000/2 x 15/115 x 87%] | 978,750 | **1** |
| | | **Max: 8** |

**Alternative answer:**

| | Marks |
|---|---|
| VAT Implications | |
| The purchase of the property represents the purchase **of goods by a vendor from a vendor who is not a connected person**, which will **be used to make taxable supplies.** | **1**<br>**1** |
| Since the building was acquired from a VAT vendor, **actual VAT was levied on the transaction** (and no transfer duties) therefore **MFTW can claim actual VAT as input tax.** | **1** |

| | |
|---|---|
| The time of supply in terms of s9(3)(d) is the **earlier of**: | **1** |
| • **The date the fixed property is registered in the name of the vendor** ( 15 July 2017) or | **1** |
| • **The date on which any payments is made in respect of the consideration for such supply.** | **1** |
| However, **as they are not connected persons, the input tax may only be claimed in proportion to the amount paid.** | |
| Therefore, MFTW can claim the input tax credit in the following VAT periods to the **extent of taxable supplies as the administration building is used for both making taxable(retail) and non-taxable supplies(financing):** | **1** |
| 30 June 2017 – R2 250 000 *1/2 or R2 250 000 *R8 625 000 /R17 250 000 = R1 125 000 x 87% = **R978 750** | **1** |
| 31 July 2017 - R2 250 000 *1/2 or R2 250 000 *R8 625 000 /R17 250 000= R1 125 000 x 87% = **R978 750** | **1** |
| **Available** | **9** |
| **Maximum** | **8** |

**QUESTION Q:**

**Objective of the question: demonstrate the ability to record the journal entries for the implementation of the revaluation of an asset including the deferred tax implications.**

Record the journal entries, including narrations, reflecting the implementation of the revaluation of the premises together with deferred taxation for the reporting period ended 30 April 2019 in compliance with the accounting standards.

[15 marks]

| | | | | | **Marks** |
|---|---|---|---|---|---|
| | Cost | Revalued | Surplus | Tax | |
| Cost | 15,000,000 | 20,000,000 | 5,000,000 | 15,000,000 | |
| Accumulated depreciation - 30 April 2018 [(15,292,500 - 250,000)/15 x 9/12] | 737,500 | 987,500 | -250,000 | 750,000 | |
| Carrying amount - 30 April 2018 | 14,262,500 | 19,012,500 | 4,750,000 | 14,250,000 | |
| Depreciation - 30 April 2019 | 983,333 | 1,316,667 | | 750,000 | |
| Carrying amount - 30 April 2019 | 13,279,167 | 17,695,833 | | 13,500,000 | |
| Deferred tax: | | | | | |
| | Difference | Deferred tax | | | |
| 30 April 2018 (historical cost) | 12,500 | 3,500 | | | |
| 30 April 2018 (revaluation) | 4,762,500 | 1,333,500 | | | |
| Adjustment for revaluation | | 1,330,000 | | | |
| 30 April 2019 (revaluation) | 4,195,833 | 1,174,833 | | | |
| Adjustment for the period | | (155,167) | | | |
| | | | Debit | Credit | |
| PPE – building | | | 5,000,000 | | **1.5** |
| Accumulated depreciation | | | | 250,000 | **2** |
| Revaluation surplus (OCI) | | | | 4,750,000 | **1.5** |

| | | | | | |
|---|---|---|---|---|---|
| [Revaluation of property using GRC method] | | | | | |
| Deferred tax expense (OCI) | | | 1,330,000 | | **3.5** |
| Deferred tax liability (SFP) | | | | 1,330,000 | **0.5** |
| [Deferred tax adjustment relating to revaluation] | | | | | |
| Depreciation expense (P&L) | | | 1,316,667 | | **1.5** |
| Accumulated depreciation (SFP) | | | | 1,316,667 | **0.5** |
| [Depreciation for the period] | | | | | |
| Deferred tax liability (SFP) | | | 158,667 | | **2.5** |
| Deferred tax expense (P&L) | | | | 158,667 | **0.5** |
| [Deferred tax provision for the period] | | | | | |
| | | | | | **Max: 15** |

**<u>QUESTION R:</u>**

**Objective of the question: demonstrate the ability to apply the provisions of the Income Tax and VAT Acts for the treatment of discounts granted to customers.**

Discuss whether the statement made by Regella that both discount schemes will results in a reduction in the VAT and income tax liabilities of the company when the sales transaction occur.

[5 marks]

| | **Marks** |
|---|---|
| Bulk Discount:<br>Bulk discount is granted to the customer when the sale is concluded, and therefore reduces the consideration of the sales transaction. For both VAT and income tax purposes, the bulk discount reduces the consideration on which output tax is calculated, and similarly the gross income will be based on the amount excluding the discount. | **1**<br><br>**1** |
| Settlement discount:<br>Settlement discount occur when the payment is received and should be treated as separate transaction from the sale. The settlement discount will result in the reduction of the output tax charged and is recognised as an output tax adjustment of input tax - provided appropriate documents are maintained. The settlement discount is treated as a deduction for income tax purposes when the transaction occurs. | **1**<br>**1**<br>**1** |
| Conclusion: the statement made by Regella is correct for the bulk discount but incorrect for the settlement discount. | **1** |
| | **Max: 5** |