

## **CPE NON-AUDIT**

### **SOLUTIONS TO QUESTION ONE**

#### **APLUS ASSOCIATES**

##### **1) In relation to the various clients of Aplus Associates,**

- a) Compare and contrast with an example each, the difference between tax evasion and tax avoidance (6 marks)

##### **Tax Avoidance**

Tax Avoidance refers to the ethical use of tax planning techniques to reduce tax liability. This involves organizing business affairs and transactions to take advantage of all tax deductions, credits and exemptions through prudent tax planning

An example of tax avoidance is to invest in a designated Multi Facility Economic Zone (MFEZ) where various tax exemptions and benefits are available including tax holiday periods, reduced tax rates and rebates

##### **Tax Evasion**

Tax evasion refers to the use of dishonest and unlawful techniques to avoid paying taxes. Examples include underreporting income, concealing assets, misrepresenting transactions and manipulating records

- b) Explain the ethical and legal implications associated with

**i) Tax avoidance (4 marks)**

Tax avoidance is lawful, but it creates ethical concerns because it denies the government funds that may be used for social welfare programs. Wealthy people and businesses who can afford to retain tax professionals and lawyers to assist them in finding loopholes in tax laws and policies frequently engage in tax avoidance.

Fairness and equity

The practice of tax avoidance may be viewed as undermining the laws of fairness and equity because it burdens others in society who are less well-off and cannot afford to avoid paying taxes. The medium and lower income groups bear a disproportionate amount of the burden of paying taxes because they lack the means to do it legally

**ii) Tax evasion (5 marks)**

It is illegal and unethical to avoid paying taxes.

### **Professional Behaviour**

Tax evasion is against the principle of professional behaviour which requires compliance with all applicable laws and standards. There a number of legal implications for tax evasion:

#### **Civil penalties**

Loss of professional and company license  
Asset seizure

#### **Integrity**

Tax evasion is against the principle which requires members to be honest, truthful and sincere

#### **Fairness and equity**

The idea of fairness and equity in tax collecting is threatened by tax evasion. It burdens individuals who do pay their taxes honestly since they are forced to increase their payments to make up for the revenue lost through tax evasion

As required by the managing director, Mr. Thole, prepare a briefing paper in which you should

**c) As required by the managing director, Mr. Thole, prepare a briefing paper in which you should**

#### **Briefing Note**

**To : Mr Thole – Managing Director**  
**Subject : Ethical and other professional issues**

#### **Introduction**

**As requested, the purpose of this briefing paper is to provide a summary of the acceptance procedures that our firm should follow, including addressing to specific ethical issues raised**

- i) Summary of the procedures which the firm should follow before accepting new clients. (6 marks)
- We must obtain evidence of the clients' identity and his address.

- We must have regard to the fundamental principles of professional ethics. This requires us to consider whether becoming tax advisers to each client would create any threats to compliance with these principles.
- Integrity – we must consider the appropriateness of each client's attitude to complying with the law and the disclosure of information to the tax authorities.
- Professional competence – we must ensure that we have the skills and competence necessary to be able to deal with the matters which may arise in connection with each client's affairs.
- If any such threats are identified, we should not accept the appointment unless the threats can be reduced to an acceptable level via the implementation of safeguards.
- We should contact each client's existing tax adviser(s) in order to ensure that there has been no action by each client which would preclude the acceptance of the assignment

**ii) Summary of the actions which the firm should take, and the matters of which Wanda should be aware, in relation to this income tax refund.  
(6 marks)**

We should assist Wanda in investigating whether or not there was a valid reason for the refund of income tax which has been received.

If we are unable to identify a valid reason, we would have to conclude that the refund was made as a result of an error on the part of ZRA. In these circumstances we should inform Wanda:

- that the amount should be repaid immediately
- that failing to return the money would be an offence
- that ZRA should be informed of their error as soon as possible in order to minimise any interest and/or penalties which may become payable

If Wanda is unwilling to return the money, this poses a threat to the fundamental principle of integrity and we would have to consider ceasing to act as her tax advisers.

We would then have to notify ZRA we no longer act for her, although we would not provide them with any reason for our action. This is in accordance with the fundamental principle of confidentiality. We should also consider whether or not this has money laundering implications and act accordingly.

- iii) **Implications for Plad Ltd, and our firm, of the failure to report the chargeable gain to ZRA. You are NOT required to address money laundering or the possibility of penalties (5 marks)**

#### **Plad Ltd**

The company has a responsibility to report this omission to ZRA and to pay the outstanding tax. It will be committing tax evasion, a criminal offence, if it fails to do so.  
ZRA will charge Plad Ltd interest on any tax which becomes payable.

#### **Our firm:**

We should investigate how this error arose and consider whether there are likely to be further errors.

We will not retain a client which is engaged in deliberate tax evasion, as this poses a threat to the fundamental principles of integrity and professional behaviour. Accordingly, we should not continue to act for Plad Ltd unless the chargeable gain is disclosed to the authorities.

If we were to cease to act for Plad Ltd, we would notify ZRA, although we would not provide them with any reason for our resignation

## **2) In relation to Solar Power Limited**

- a) **Show how the three key ratios were computed based on the draft financial statements (6 marks)**

|                            |   |                                                 |         |
|----------------------------|---|-------------------------------------------------|---------|
| Return on capital employed | = | $\frac{K2,972}{K18,253.5 + K20,450.8} * 100$    | = 7.3%  |
| Net profit margin          | = | $\frac{K2,972 - 1,241}{K31,850} * 100$          | = 5.4%  |
| Gearing                    | = | $\frac{K18,253.5}{K18,253.5 + K22,450.8} * 100$ | = 44.8% |

**b) For each of the three transactions:**

- i) Discuss the accounting treatment of each transactions AND identify any errors that you think have been made in applying accounting principles with references, where appropriate, to IFRS.  
(15 marks)

**Transaction 1: Sale and repurchase agreement**

**Discussion**

This is a case in appropriate revenue recognition in accordance with IFRS 15 – Revenue from Contracts with Customers

Solar Power Limited remains the owner of the item of plant as it retains the risks and rewards of ownership. Solar Power Limited continue to insure the plant and store it on its premises

The transaction is not a true sale but a financing transaction with the asset as collateral. The transaction involves contracting to sell the financial asset with an express contract to buy it back. The right of use and control of the asset has not been transferred. Therefore, SPL should continue recognizing the asset and the amount received should be regarded as a loan.

The price which Solar Power Limited will be required to pay to buy the item of plant back is equivalent to a financing cost and appears to have no relationship to any appreciation in the value of the item.

ZAMBANK is an entity that provides financial services to business and has no use for the plant. As a result of the above, the fundamental principle of substance over form, as identified in the IASB conceptual framework, points clearly to a financial agreement.

Moreover, as an item of plant is involved, even if this was a true sale, it would not have been shown in revenue. IFRS 15 Revenue from contracts with customers, states that it only applies if the counterparty to the contract is a customer. A customer is a party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration. The ordinary business activities of SPL is energy and consultancy and not selling assets

**Adjustments**

The adjusting entries should be as follows, assuming the K1, 000,000 was received in cash and we need details of the accounting entries made to derecognize the asset in order to reverse these

|                          |            |            |
|--------------------------|------------|------------|
| DEBIT Revenue            | K1,000,000 |            |
| CREDIT short - term loan |            | K1,000,000 |
| DEBIT interest expense   | K100,000   |            |
| CREDIT Interest payable  |            | K100,000   |

## Transaction 2

### Discussion

This transaction does not meet the recognition criteria for receivable as per IFRS 9 financial instruments, as Solar Power Limited bears the risk of any uncollectible amounts. The substance of the transaction is a financing agreement with interest of 10% as the fiancé charge secured by Solar Power Limited's receivables. The receivables must be re-instated

### Adjustments

The adjusting entries are:

|                                                 |            |             |
|-------------------------------------------------|------------|-------------|
| DEBIT Receivable (75% x K2,000,000)             | K1,500,000 |             |
| CREDIT Loan                                     |            | K1,500 ,000 |
| To restate receivables and account for the loan |            |             |
| DEBIT Interest expense                          | K150,000   |             |
| CREDIT Loan                                     |            | K150 ,000   |

## Transaction 3

### Discussion

Under IAS 32 *Financial Instruments: Presentation*, redeemable preference shares should be classified as debt. The preference dividends payable should be classified as interest. The fact that the shares are redeemable and the obligation to pay dividends indicate that the financial instruments, in substance, a liability and should be classified as such

### Adjustments

The adjusting entries are:

|                                      |          |          |
|--------------------------------------|----------|----------|
| DEBIT Interest (8% x K2,000,000)     | K160,000 |          |
| CREDIT Dividends – debited to equity |          | K160,000 |

|        |        |            |            |
|--------|--------|------------|------------|
| DEBIT  | Equity | K2,000,000 |            |
| CREDIT | Debt   |            | K2,000,000 |

**ii) Prepare the adjustments that are required to correct those errors (6 marks)**

**Adjustments ('000)**

|                        | As given | Transaction<br>1 | Transaction<br>2 | Transaction<br>3 | Adjusted<br>Figures |
|------------------------|----------|------------------|------------------|------------------|---------------------|
|                        | K        | K                | K                | K                | K                   |
| Revenue                | 31,850   | (1,000)          |                  |                  | 30,850              |
| Profit before interest | 2,972    |                  |                  |                  | 2,972               |
| Interest               | 1,241    | 100              | 150              | 160              | 1,651               |
| Equity                 | 22,450.8 |                  |                  | (2,000)          | 20,450.8            |
| Debt                   | 18,253.5 | 1,000            | 1,500            | 2,000            | 22,753.5            |

**c) Calculate and explain the effect of your adjustments on SPL's key accounting ratios for the year ended 31st December 2024 (9 marks)**

**Calculation of the effect of adjustments**

|                            |   |                                                      |          |
|----------------------------|---|------------------------------------------------------|----------|
| Return on capital employed | = | $\frac{K2,972}{K22,753.5 + K20,450.8} \times 100$    | = 6.88%  |
| Net profit margin          | = | $\frac{K2,972 - K1,641}{K30.850} \times 100$         | = 4.28%  |
| Gearing                    | = | $\frac{K22,753.5}{K22,753.5 + K20,450.8} \times 100$ | = 52.66% |

**Explanation**

If SPL achieves the targets set, Mr. Rogers Sombe, a self-made \$ millionaire has expressed interest in providing additional financing to SPL to allow it to expand its operations to the rest of Zambia.

Based on the draft financial statements, all three targets were achieved with profitability above target and gearing far below the set target of 48%

However, following the adjustments, the results show that the targets were not achieved with the gearing falling far below the target set. **This is shown in appendix 1**

### Appendix 1

|          | Performance Indicator                                                                                      | Target           | Based on draft financial statements | Revised after adjustments |
|----------|------------------------------------------------------------------------------------------------------------|------------------|-------------------------------------|---------------------------|
| <b>1</b> | <b>Return on Capital Employed ( Computed as Profit before interest as a percentage of debt plus equity</b> | <b>7%</b>        | 7.3%                                | <b>6.88%</b>              |
| <b>2</b> | <b>Net profit margin (Computed as profit before tax as percentage of revenue)</b>                          | <b>5%</b>        | 5.4%                                | <b>4.28%</b>              |
| <b>3</b> | <b>Gearing ( Computed as long term and short term debt as a percent of the total debt plus equity)</b>     | <b>Below 48%</b> | 44.8%                               | <b>52.66%</b>             |

### 3) In relation to Charlies and Angels and the type of business

- a) Calculate Charlies' and Angels' income tax payable for 2025 if they run their business as  
i) A partnership (8 marks)

#### PERSONAL INCOME TAX COMPUTATION IF BUSINESS RUN AS A PARTNERSHIP – 2025

|                                   | Total<br>K | Charlies<br>K | Angels<br>K |
|-----------------------------------|------------|---------------|-------------|
| Adjusted profit                   | 4,752,000  |               |             |
| Less capital allowances           |            |               |             |
| - 20% x K450,000 x 2 x 50% - Cars | (90,000)   |               |             |
| - 25% x K600,000 x 2 - Ford Vans  | (300,000)  |               |             |
|                                   | -----      |               |             |
|                                   | 8          |               |             |

|                      |           |           |           |           |
|----------------------|-----------|-----------|-----------|-----------|
| Final trading profit | 4,362,000 |           |           |           |
|                      | =====     |           |           |           |
| Salaries             | 4,000,000 | 2,000,000 | 2,000,000 |           |
| Balances (1:1)       | 362,000   | 181,000   | 181,000   |           |
|                      | -----     | -----     | -----     |           |
|                      |           | 4,362,000 | 2,181,000 | 2,181,000 |
|                      | =====     | =====     | =====     |           |
| Income tax:          |           |           |           |           |
| 0% x K61,200         |           | Nil       | Nil       |           |
| 25% x K24,000        |           | 4,800     | 4,800     |           |
| 30% x K25,200        |           | 7,560     | 7,560     |           |
| 37% x K2,070.600     |           | 766,122   | 766,122   |           |
|                      |           | -----     | -----     |           |
| Income tax payable   |           | 778,482   | 778,482   |           |
|                      |           | =====     | =====     |           |

- ii) Taxation payable by Charlies and Angels if run as a limited company and they withdraw gross director's emoluments of K4,000,000  
(4 marks)

|                    |           |           |           |
|--------------------|-----------|-----------|-----------|
|                    | Total     | Charlies  | Angels    |
|                    | K         | K         | K         |
| Salaries           | 4,000,000 | 2,000,000 | 2,000,000 |
|                    | =====     | =====     | =====     |
| Income tax:        |           |           |           |
| 0% x K61,200       |           | Nil       | Nil       |
| 25% x K24,000      |           | 4,800     | 4,800     |
| 30% x K25,200      |           | 7,560     | 7,560     |
| 37% x K1,889,600   |           | 699,152   | 699,152   |
|                    |           | -----     | -----     |
| Income tax payable |           | 711,512   | 711,512   |
|                    |           | =====     | =====     |

- iii) **Taxation payable by Charlies and Angels if they run as a limited company and withdraw dividends of K4,000,000**  
(4 marks)

if the business is run as a limited company and the Directors draw dividends of K4,000,000, withholding tax payable of 15% x K4,000,000 = K600,000 will be the final tax. Therefore, no further income tax will be paid by Charlies and Angels

- b) Calculate the income tax payable by Charge Rite Limited for the year ended 31<sup>st</sup> 2025 if they run their business as a limited company and  
(6 marks)

**i) Withdrew gross remunerations of K4,000,000 – gross remuneration is deductible-  
Capital allowances not restricted**

|                                  |             |
|----------------------------------|-------------|
| Adjusted profit                  | 4,752,000   |
| Less gross remuneration          | (4,000,000) |
| Less capital allowances          |             |
| - 20% x K450,000 x 2 - Cars      | (180,000)   |
| - 25% x K600,000 x 2 - Ford Vans | (300,000)   |
|                                  | -----       |
| Taxable income                   | 272,000     |
|                                  | =====       |
| Tax @ 30%                        | 81,600      |
|                                  | =====       |

**ii) Withdrew as dividends K4,000,000 – Dividend is an appropriation and is not deductible**

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|                                  |           |
|----------------------------------|-----------|
| Adjusted profit                  | 4,752,000 |
| Less capital allowances          |           |
| - 20% x K450,000 x 2 - Cars      | (180,000) |
| - 25% x K600,000 x 2 - Ford Vans | (300,000) |
|                                  | -----     |
| Taxable income                   | 4.272,000 |
|                                  | =====     |
| Tax @ 30%                        | 1,281,600 |
|                                  | =====     |

- c) Based on your calculations in parts (a) and (b), advise Charlies and Angels whether it will be beneficial to run their business as a partnership or whether they should run it as a limited company  
(6 marks)

**Limited Company**

|                               | <b>Partnership</b> | <b>Emoluments</b> | <b>Dividends</b> |
|-------------------------------|--------------------|-------------------|------------------|
|                               | <b>K</b>           | <b>K</b>          | <b>K</b>         |
| Total income                  | 4,752,000          | 4,752,000         | 4,752,000        |
| Less:                         |                    |                   |                  |
| Total personal income tax     |                    |                   |                  |
| (778,482 x 2)/ (K711,512 x 2) | (1,556,964)        | (1,423,024)       |                  |
| Company income tax            |                    | (81,600)          | (1,281,600)      |
| Withholding tax               |                    |                   | (600,000)        |
|                               | -                  | -----             | -----            |
| Net income                    | 3,195,036          | 3,247,376         | 2,870,400        |
|                               | =====              | =====             | =====            |

Base on the above calculations, it would be beneficial for the business to be run as a limited company with Charlies and Angels rewarding themselves by way of emoluments

## QUESTION TWO - SOLUTIONS

### 1) In relation to Mone Ltd:

- a) Explain the tax implications of the following expected investment returns
- (i) Interest from treasury bills (2 marks)
  - (ii) Royalties (2 marks)
  - (iii) Dividends (2 marks)

### THE WITHHOLDING TAX SYSTEM

This is a system of collecting tax at source. Persons making payments of investment income are required to deduct withholding tax and only pay the net amount to the recipient of the income. This is where the person making the payment is the one who is required to make the payment net of withholding tax

Certain payments of investment income are paid gross by most mining companies. Withholding tax is also to be deducted from payments of management and consultancy fees, public entertainment fees and commissions.

Where WHT is the final tax, the recipient individual is not subject to further assessment on the investment income received. In cases where the WHT is not the final tax, the recipient is subjected to a further assessment in respect of the investment income received and the WHT is given as a tax credit against the final income tax for the year

#### Bank Interest

WTH charged at 15% but regarded as final tax. The interest will not be included in the taxable income

#### Royalties

WTH charged at 15% but regarded as not final tax. The gross royalties will be included as taxable and the WTH paid deducted from final taxation payable

#### Dividends

Dividends from listed companies - 0% WHT – Exempt and not included as part of income

### b) Assuming that Mone Ltd registered for VAT on 1<sup>st</sup> January 2024,

- (i) Compute the amount of Value Added Tax (VAT) payable for the year ended 31 December 2024. You should indicate zero where VAT is not chargeable or recoverable (12 marks)

#### MONE LIMITED

#### VAT payable for the year ended 31 December 2024

|                                    | K | K |
|------------------------------------|---|---|
| <b>Output VAT</b>                  |   |   |
| Exempt sales (K300,000 x 10% x 12) |   | 0 |

|                             |                |
|-----------------------------|----------------|
| Standard-rated sales        |                |
| (K300,000 x 90% x 12 x 16%) | <u>518,400</u> |
|                             | 518,400        |

### Input VAT

|                                              |          |                  |
|----------------------------------------------|----------|------------------|
| Exempt purchases (K116,000 x 10% x 12)       | 0        |                  |
| Standard-rated purchases                     |          |                  |
| (K116,000 x 90% x 12 x 16%)                  | 200,448  |                  |
| Entertaining customers                       | 0        |                  |
| Entertaining suppliers                       | 0        |                  |
| Motor vehicle servicing (K6,960 x 4/29 x 12) | 11,520   |                  |
| Overheads (K24,592) x 12 x 4/29 x 90%)       | 36,633   |                  |
| Computers (pre-registration)                 | 0        |                  |
| Equipment (K143,840 x 4/29)                  | 19,840   |                  |
| Light truck (K208,800 x 4/29)                | 28,800   |                  |
| Mazda Cars                                   | <u>0</u> |                  |
|                                              |          | <u>(297,241)</u> |
| VAT payable                                  |          | <u>221,159</u>   |

- (ii) Compute the amount of income tax payable by the company for the tax year 2024  
(12 marks)

### MONE LIMITED

#### INCOME TAX PAYABLE FOR THE TAX YEAR 2024

|                                       | K             | K                  |
|---------------------------------------|---------------|--------------------|
| Sales (K300,000 x 12)                 |               | 3,600,000          |
| Add:                                  |               |                    |
| Personal-to-holder car benefit        |               |                    |
| (K30,000 + K30,000)                   |               | <u>60,000</u>      |
|                                       |               | 3,660,000          |
| Less:                                 |               |                    |
| Purchases (K116,000 x 12)             | 1,392,000     | Salaries           |
| (K647,826 + K607,826)                 | 1,255,652     |                    |
| Other expenses                        |               |                    |
| - Motor vehicle servicing (6,960X 12) | 83,520        |                    |
| - Overheads (K24,592 X 12)            | 295,104       |                    |
| Capital allowances:                   |               |                    |
| Computers (K46,400 x 25/29 x 25%)     | 10,000        |                    |
| Equipment (K143,840 x 25/29 x 25%)    | 31,000        |                    |
| Light truck (K208,800 x 25/29 x 25%)  | 45,000        |                    |
| Mazda cars (K150,000 x 20% x 2)       | <u>60,000</u> |                    |
|                                       |               | <u>(3,172,276)</u> |

Taxable business profit 487,724

Income tax @30% 146,317

**2) In relation to Buluwe Holdings request for professional services**

a) Evaluate EIGHT ethical and other professional issues arising (12 marks)

b) For each issue above suggest suitable action that your firm should take (8 marks)

|   | ETHICAL AND PROFESSIONAL ISSUE                                                                                                                                                                                                                                                                 | SUITABLE ACTION                                                                                                                                                                                                                                                                                                                                     |
|---|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | Familiarity – Friends with brother<br>Mr. Eli Malasha's brother appear to be a close friend of Mr. Buluwe, the managing director of Buluwe Holdings. Additionally, Mr. Malasha's desire to chat over a glass of red wine indicates another level of familiarity with Mr. Buluwe                | Mr. Eli should not be involved in this assignment. It be appropriate to have a second review by an independent director before any reports are issued                                                                                                                                                                                               |
| 2 | Advocacy – tax return<br>The request to complete the tax return and submit it to ZRA generates an advocacy threat                                                                                                                                                                              | According to ZICA ethical guidelines, the risk of advocacy cannot be reduced to an acceptable level. The suitable action is not to accept the request to handle the tax return on behalf of Buluwe Holdings. This should be explained to the client. The auditor may wish to provide the information but not take responsibility for the tax return |
| 3 | Loan Guarantee – self-interest<br>The request to guarantee the loan with Afrique Bank creates a conflict or threat of self-interest. The firm will be unwilling to expose any issue that may threaten the ability of Buluwe Holdings to repay the loan. The firm will not act with objectivity | The self-interest created by the loan guarantee is too significant and cannot be reduced. The only suitable action is for the firm to decline the request, explain the ethical and professional implications to the client                                                                                                                          |
| 4 | Buluwe to be seen generating enough cash flows – integrity and intimidation<br>This statement seems to suggest that when the cash flows statement extract is prepared, it should show a favourable position. This may not be the true and fair view position and                               | The firm should explain to Mr. Buluwe that the cash flow extract will be based on the figures included in the financial statement, regardless of whether the position is favourable or not. This should be explained to Mr. Buluwe including clarification as to whether the appointment depends on the firm showing a favourable cash position.    |

|   |                                                                                                                                                                                                                                                                                                                                                                                                                                                               |                                                                                                                                                                                                                                                                                                                                                                                                           |
|---|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|   | may also suggest intimidation. This may also question the integrity of Mr. Buluwe                                                                                                                                                                                                                                                                                                                                                                             | Intimidation is a serious threat and the firm should consider not accepting the assignment if this is confirmed to be intimidation                                                                                                                                                                                                                                                                        |
| 5 | Holiday offer – self-interest, familiarity<br>The holiday offer constitutes gift and hospitality and generates a self-interest as well as a familiarity threat.                                                                                                                                                                                                                                                                                               | This offer appears significant and should be declined, especially that it also increases the familiarity threat<br><br>Alternatively, Mr. Eli Malasha could offer to pay for the expenses – but this will still not deal with the increased threat of familiarity                                                                                                                                         |
| 6 | Competitive Charges –low balling - misleading<br>This is misleading as it implies that the charges or fees levied by Malasha Associates are less than competition. This also suggests low-balling – i.e. charging fees below market rates<br><br>The practice of low balling may create a self- interest as the firm may be attempting to get the assignment with a view of either increasing the rates at a later stage or obtain other services as a result | The fees charged by the firm should be based on the time and relative qualifications and experience of staff to be allocated to the assignment, including taking into account the complexity and reporting requirements of the assignment. The firm should make this clear to the client<br><br>Low balling is allowed only if there are no ulterior motives but undertaken as a normal business practice |
| 7 | Exceptional quality – Exceeding expectations - integrity - misleading<br>This is misleading the client of the quality expected                                                                                                                                                                                                                                                                                                                                | All firms licensed to carry out professional services are expected to provide these services in accordance with stated standards and laws and regulations. This the standard expected of them. This is misleading and the firm should not have asserted this to the client                                                                                                                                |
| 8 | No saving – no fee – contingent fee – self interest<br>The statement no saving no fee seem imply that the fees is dependent on the amount of tax saved for the client. This suggests a contingent fees based on the tax saved and creates a self-interest threat                                                                                                                                                                                              | Contingent fees are not allowed in the provision of professional services. The fee should be based on time and requisite qualifications and experience to be allocated to the assignment.<br><br>For assurance services, a professional can only provide reasonable assurance. For other non-assurance services, only limited or no assurance                                                             |

|  |                                                                                                      |                                                                                  |
|--|------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------|
|  | This also implies that firm is able to provide 100%. It is not possible for the firm to provide 100% | can be provided. This is misleading and the firm should withdrawal the assertion |
|--|------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------|

### 3) In relation to the preparation of the cash flow statement and leasing arrangement for Buluwe Holdings:

- a) Prepare the adjusted net cash generated from operating activities (9 marks)

#### Buluwe Holdings

#### Adjusted net cash flow from generated from operating activities

|                                                   | K'000    | K'000  |
|---------------------------------------------------|----------|--------|
| Profit before tax                                 |          | 15,600 |
| Add back:                                         |          |        |
| ○ Depreciation on buildings – (wkg 1)             | 1,800    |        |
| ○ Depreciation on plant – (wkg 2)                 | 26,600   |        |
| ○ Loss on disposal of plant                       | 4,200    |        |
| ○ Decrease in Inventories (57,400 – 43,300)       | 14,100   |        |
| ○ Increase in trade receivables (50,400 – 28,600) | (21,800) |        |
| ○ Decrease in trade payables (31,400 – 26,700)    | (4,700)  |        |
|                                                   | -----    |        |
|                                                   |          | 20,200 |
|                                                   |          | -----  |
|                                                   |          | 35,800 |
|                                                   |          | =====  |

#### Workings (K'000)

- (i) Land and buildings - cost

|                                   |        |             |
|-----------------------------------|--------|-------------|
|                                   | DR     | CR          |
| Balance b/d                       | 49,200 | Balance c/d |
| Revaluation – note 1              | 6,000  | 62,300      |
| Acquisition during the year – bal | 7,100  |             |
|                                   | -----  | -----       |
|                                   | 62,300 | 62,300      |

#### Land and buildings – Accumulated depreciation

|             |       |             |
|-------------|-------|-------------|
|             | DR    | CR          |
| Balance b/d | 6,800 | Balance b/d |
|             | 16    | 5,000       |

|                                                    |         |                            |
|----------------------------------------------------|---------|----------------------------|
|                                                    | Dep P/L | 1,800                      |
|                                                    | -----   | -----                      |
|                                                    | 6,800   | 6,800                      |
| <br>(ii) Plant and machinery - cost                |         |                            |
|                                                    | DR      | CR                         |
| Balance b/d                                        | 70,000  | Balance c/d 84,600         |
| Acquisition during the year – bal                  | 38,100  | Disposal – note 2 23,500   |
|                                                    | -----   | -----                      |
|                                                    | 108,100 | 108,100                    |
| <br>Plant and machinery – accumulated depreciation |         |                            |
|                                                    | DR      | CR                         |
| Balance c/d                                        | 37,600  | Balance c/d 22,500         |
| Disposal                                           | 11,500  | Depr- bal - Dep P/L 26,600 |
|                                                    | -----   | -----                      |
|                                                    | 49,100  | 49,100                     |
| <br>Plant and machinery - Disposal                 |         |                            |
|                                                    | DR      | CR                         |
| Plant                                              | 23,500  | Proceeds 7,800             |
|                                                    |         | Acc depreciation 11,500    |
|                                                    |         | Loss Dep P/L 4,200         |
|                                                    | -----   | -----                      |
|                                                    | 23,500  | 23,500                     |

## b) In relation to the leasing arrangement:

- (i) Discuss the accounting treatment to be applied by Buluwe Holdings (5 marks)

### Discussion

#### Initial Measurement

According to IFRS 16 – Leases - at the commencement of the lease, the lessee should recognise

DR Right of use of asset  
CR Liability

Based on the net present value of the instalments payable on the lease using the rate of interest implicit in the lease.

DR Right of use of asset  
CR Bank or payable

The present value of any direct costs incurred in respect of the lease

### **Subsequent measurement**

#### **Right of use of asset**

Under the cost model a right-of-use asset is measured at cost less accumulated depreciation and accumulated impairment. IAS 16 will be applied with asset being depreciated over the lease term

#### **Liability**

The liability will be accounted for using amortised cost and amount payable split between payable within one year and after one year

### **(ii) Prepare financial statement extracts for the year ended 31<sup>st</sup> December 2025 (6 marks)**

#### **Financial statement extracts**

|                                                                | <b>K'000</b> |
|----------------------------------------------------------------|--------------|
| <b>Profit and Loss</b>                                         |              |
| Depreciation – working 1                                       | 4,646        |
| Lease interest receivable – working 2                          | 1,136        |
| <b>Statement of financial position</b>                         |              |
| ○ <b>Non-current assets</b>                                    |              |
| ▪ PPE – Cost less depreciation (23,230 – 4,646) – working 1    | 18,584       |
| ○ <b>Non-current liabilities</b>                               |              |
| ▪ Lease liability – Payable after more than 1 year – working 2 | 13,865       |
| ○ <b>Current liabilities</b>                                   |              |
| ▪ Lease liability – payable within 1 year                      | 5,000        |

#### **WORKINGS**

##### **Working 1**

### Right of use of asset

|                                      |        |
|--------------------------------------|--------|
| ○ NPV of instalments                 | 22,730 |
| ○ Direct costs                       | 500    |
|                                      | -----  |
|                                      | 23,230 |
|                                      | -----  |
| ○ Depreciation $23230/5 = 4,646,000$ |        |

### Working 2 - Liability

|                                                                   |                |
|-------------------------------------------------------------------|----------------|
|                                                                   | <b>K'000</b>   |
| Balance at at 1 <sup>st</sup> January 2025 – discounted/amortised | 22,730         |
| Effective interest @ 5%                                           | 1,136          |
|                                                                   | -----          |
|                                                                   | 23,866         |
| Less instalments received                                         | <u>(5,000)</u> |
|                                                                   | 18,865         |
|                                                                   | ====           |

### c) Option under IFRS 16

Instead of applying the recognition requirements of IFRS 16, a lessee may elect to account for lease payments as an expense on a straight-line basis over the lease term or another systematic basis for the following two types of leases:

- leases with a lease term of 12 months or less and containing no purchase options – this election is made by class of underlying asset; and
- leases where the underlying asset has a low value when new (such as personal computers or small items of office furniture) – this election can be made on a lease-by-lease basis.

According to IFRS 16 such leases will be accounted for on a straight line basis, with installments payable during the lease charged to the profit and loss on a straight line basis. The justification for are two fold

- i) It simplifies the accounting aspects. Applying IFRS in full is expensive in terms of time and expertise required
- ii) Since the amounts are not material and both the asset and the liability will be derecognized at the end of an accounting period, the impact on the financial statements is insignificant

### 4) In relation to Mr. Shoes Nsapato:

- a) Calculate the amount of provisional income tax paid by Mr. Nsapato in respect of the tax year 2024 and state the due dates and amounts on each due date (5 marks)

(a) COMPUTATION OF PROVISIONAL INCOME TAX

|                          |           |
|--------------------------|-----------|
|                          | K         |
| Estimated taxable profit | 1,290,000 |

Provisional Income Tax

|                  |                |
|------------------|----------------|
| K61,200 x 0%     | 0              |
| K1,228,800 x 10% | <u>122,880</u> |
|                  | <u>122,880</u> |

|                                                    |               |
|----------------------------------------------------|---------------|
| Amount of provisional income tax paid each quarter | <u>30,720</u> |
|----------------------------------------------------|---------------|

|                |   |
|----------------|---|
| (K122,880 ÷ 4) | 1 |
|----------------|---|

| Instalment                 | Due Date                                        | Amount<br>K |
|----------------------------|-------------------------------------------------|-------------|
| 1 <sup>st</sup> Instalment | 31 March but not later than 10 April 2024       | 30,720      |
| 2 <sup>nd</sup> Instalment | 30 June but not later than 10 July 2024         | 30,720      |
| 3 <sup>rd</sup> Instalment | 30 September but not later than 10 October 2024 | 30,720      |
| 4 <sup>th</sup> Instalment | 31 December but not later than 10 January 2025  | 30,720      |

I

**b) Compute the capital allowances for Mr. Nsapato farm for the tax year 2024 (6 marks)**

(a) COMPUTATION OF MAXIMUM CAPITAL ALLOWANCES

|                                                   | K              |
|---------------------------------------------------|----------------|
| <u>Stumping and clearing Expenditure</u>          |                |
| Farm works allowance<br>(K14,550 x 100%)          | 14,550         |
| <u>Construction of Fence</u>                      |                |
| Farm improvement allowance<br>(K24,450 x 100%)    | 24,450         |
| <u>Expenditure for Prevention of Soil Erosion</u> |                |
| Farm works allowance<br>(K27,750 x 100%)          | 27,750         |
| <u>Motor van</u>                                  |                |
| wear and tear allowance<br>(K135,000 x 25%) x 80% | 27,000         |
| <u>Tractor</u>                                    |                |
| Wear and tear allowance<br>(K195,000 x 100%)      | 195,000        |
| <u>Farm implements</u>                            |                |
| Balancing charge<br>(0 – K9,600)                  | <u>(9,600)</u> |
|                                                   | <u>279,150</u> |

**c) Compute the taxable profits for Mr. Nsapato farm for the tax year 2024 (10 marks)**

|                                                   | K       | K         |
|---------------------------------------------------|---------|-----------|
| Profit for the year                               |         | 1,020,000 |
| Add:                                              |         |           |
| Nsapato's salary                                  | 135,000 |           |
| Loans to former employees written off             | 18,000  |           |
| Repairs and fuel for motor van<br>(K14,250 x 20%) | 2,850   |           |
| Depreciation                                      | 21,600  |           |
| Increase in general provision                     | 3,900   |           |
| Loss on disposal of farm implements               | 10,650  |           |
| Stumping and clearing                             | 14,550  |           |

|                                           |              |                |
|-------------------------------------------|--------------|----------------|
| Constructing wire fence                   | 24,450       |                |
| Expenditure on prevention of soil erosion | 27,750       |                |
| Good for personal use (K22,500 x 20%)     | <u>4,500</u> |                |
|                                           |              | <u>263,250</u> |
|                                           |              | 1,283,250      |

|                              |                  |
|------------------------------|------------------|
| Less: capital allowances (b) | (279,150)        |
| Final actual taxable profit  | <u>1,004,100</u> |

**d) Compute the final taxation payable by Mr. Nsapato for the tax year 2024  
(4 marks)**

|                              |                  |
|------------------------------|------------------|
| Final taxable profit (above) | <u>1,004,000</u> |
| <u>Income Tax</u>            |                  |
| K61,200 x 0%                 | 0                |
| K942,900 x 10%               | <u>94,290</u>    |
|                              | 94,290           |
| Less provisional income tax  | <u>(122,880)</u> |
| Final income tax refund      | <u>(28,590)</u>  |