SUGGESTED SOLUTIONS

SECTION A

1) Application of ethical principles to a fraud investigation

The fundamental principles covered in ZICA code of ethics cover:

- Objectivity
- Professional Behaviour
- Professional Competence
- Integrity
- Confidentiality

(i) Objectivity

As an investigator, ML is required to be independent and should be seen to be independent as they accept and undertake the payroll investigation. It is likely that the report to be issued by ML will be used by the executive committee of the club and may be used as evidence in courts of law. ML is therefore expected to remain professionally objective as any perceived threats to this position may undermine the credibility of the report and ML as a firm.

(ii) Professional behaviour

ML is expected to conduct itself with courteous and consideration. Fraud investigations are often characterized by conflict and sensitive emotions. ML should avoid be seen as acting fairly with both parties to the investigation as any suspicion of obvious bias may undermine their findings. In particular, ML should appreciate that their duty is to obtain evidence and not find the guilty party.

(iii) Professional competence

This requires ML not to accept any assignment unless they are qualified, experienced and competent to carry out such an assignment, including consideration of required resources such as time. Investigations required additions skills such as interviewing, evidence gathering and reporting. Fraud investigations are also governed by specific regulatory framework. ML should consider whether it has competence to be able to provide a professional service with due skill care and caution.

(iv) Integrity

The act of fraud implies cheating and lying and lack of integrity. ML is therefore expected to be in contact with and investigating other people that may not have the same level of integrity. It is important that ML does not get caught in the "lies" and must act with integrity throughout the investigation

(v) Confidentiality

Confidentiality requires that ML does not divulge information obtained in the course of investigation to any third part without the permission of the club. In this case of fraud, it is possible that the police may be involved. ML cannot report or disclose any information to the police unless forced through a court order or with permission from the club.

2) Forensic investigation:

a) Objectives of such an investigation

The objectives of such an investigation should include:

- To confirm whether fraud has taken place or not. It is possible that the suspected fraud may be an error or action without intent.
- To determine how the fraud may have been perpetrated. This will assist in determining what information, records and documents to examine during the investigation
- To determine who is involved in the fraud. As this may involve the police and courts of law, all suspects will need to be interviewed.
- To determine the amount involved in the fraud. This is important as no further action can be taken unless the loss is quantified.

b) Possible procedures

Procedures in investigating suspected fraud:

(i) Understand the operations of the club and the systems relating to payroll

Inquiries need to be made to obtain information relating to:

- Recruitment policies and procedures
- Records maintained about employees
- Policies and procedures relating to including employees on payroll and removing employees on the payroll, including the personnel involved in these process.

(ii) Determine how the fraud could have taken place

From the information given about the fraud, it would appear that the fraud was committed by not removing all those employees declared redundant from the payroll, and payments continued to be made to these employees. The reduction of 6% was not as much as was expected from the total number of employees that had been made redundant.

(iii) Determine the type of fraud

Initial investigations performed by the club treasurer revealed that some of the employees declared redundant had remained on the payroll records and payments to these individuals were still being made. This appears to be a typical fraud associated with starters and leavers resulting in “ghost employees”

(iv) Determine the period covered by the fraud

The fraud was discovered at the time of the review of the management accounts for the quarter end 31st December 2012. This would suggest that the fraud had been going on from the time employees were declared redundant to-date. However, this would need to be verified

(v) Gather evidence

The objective of the gathering evidence is to:

- The occurrence of the fraud
- Identify the perpetrators of the fraud, including the motive and the ability of the fraudster to commit the fraud, as well as any attempt to hide the fraud
- Quantify the monetary value of the fraud

(vi) Make recommendations

It should be expected that the club executive committee should be advised on how to prevent the occurrence fraud in the future, including recommendation that a holistic review of all the policies and procedures to ensure that they are adequate.

3) To	:	Executive Committee
From	:	Madison Lengwe -
Subject	:	RE: Visit from the Zambia Revenue Authority (ZRA)

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e purpose of this briefing note is to advise on specific issues raised by the ZRA following their last visit to your club

a) The circumstances under which a company is held to be resident in Zambia for income tax purposes

The terms dealing with the residence for tax purposes apply differently to individuals and companies as follows:

A company is held to be resident in Zambia for Income Tax purposes if:

(i) That company is incorporated of formed in Zambia, or

(ii) The central management and control of the company's business affairs is exercised in Zambia.

A company is centrally managed and controlled in Zambia if the Board of Directors for that company meets in Zambia for the purposes of decision making affecting the company

b) The circumstances under which an individual is held to be resident and ordinarily resident in Zambia for income tax purposes

An individual is held to be resident in Zambia if he or she is physically present in Zambia for a period of not less than 183 days in a charge year:

- Individuals who normally live in Zambia are resident and ordinarily resident in Zambia

· Individuals who come to Zambia with the intention of remaining here for more than 12 months are deemed to be resident and ordinarily resident in Zambia from the date of arrival

· Individuals may be resident in Zambia for only one tax year if they do not show any intentions of remaining here for a relatively long period of time

MLengwe

SECTION B

4) Conditions for revenue recognition

a) IAS 18 *Revenue Recognition* states that the following conditions must be satisfied before revenue from the sale of goods can be recognized:

i) The enterprise has transferred to the buyer the significant risks and reward of ownership of the goods. **In the case of the club, the member becomes entitled to enjoy the benefits associated with being a member, at same time enjoying these benefits at own risk**

ii) The enterprise retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold. **Once the membership fee is paid, the member has full rights of access to facilities provided by the clue**

iii) The amount of revenue can be measured reliably. **For the club the subscription is a fixed amount per annum and therefore can be measured reliably.**

iv) It is probable that the economic benefits associated with the transaction will flow to the enterprise. **For the club, this is virtually certain as the subscriptions is receivable in advance and the member is not allowed entry until membership fees are paid**

v) The costs incurred or to be incurred in respect of the transaction can be measured reliably.**For the club this means that the costs of running the club and providing the amenities including drinks can be measured reliably**

b) Evaluation of the policy

The accounting policy of the club is to account for fees received during the year as income. The fees are not refundable and are not transferrable. Using the conditions discussed above, this policy can be evaluated as follows:

i) **Transfer of significant risks and rewards** – The club has not transferred all the risks and rewards at once as the revenue is paid in advance for the full year. Accordingly, the subscriptions should only be accounted for as revenue to the extent that the club has transferred the risks and rewards – which may be on a monthly basis

ii) **Retention of managerial involvement**. It is implied that since the rewards have not been transferred completely, the club retains a certain amount of involvement and control over the future services, rewards and risks to be transferred

iii) **Reliable measurement.** The portion amount can be reliably measured on a time apportionment basis

iv) **Costs to be incurred.** As some of the costs are to be incurred in the future, this may not be measured reliable

Conclusion

Based on above evaluation, treating the subscriptions received as revenue without regarding the fact the subscriptions are paid in advance is against the conditions prescribed by IAS 18. Revenue should only be recognized to the extent that the member has been given access and has enjoyed the rewards associated with being a member, i.e. on a time apportionment basis. This is consistent with the stage of completion method acceptable and also the accruals and matching concept. The fact that fees are not refundable assumes that the club will provide access and rewards without fail is not relevant for this purpose

5) Conversion and translation

a) Conversion is the process of restating one currency into another. This takes place at the transaction date and at the date of the balance sheet. For example at the date of buying the irrigation equipment, the club would restate the 295,000 Rands into KR 1,947,000 (295,000 * 6.6) in its books

Conversion is the process of exchanging one currency into another. This takes place at the date of payment or receipt. For example on 1st February 2013, the club would need to pay KR476,000 (KR6.8 * 70,000) to remit the SAR 85,000 payable on 1st February 2013.

b) Currency methods

In accordance with IAS 21, *The Effects of Changes in Foreign Currency Rates,* the functional currency is the currency of the primary economic environment where the entity operates. In most cases this will be the local currency. The following are considered when determining the functional currency

- The currency that mainly influences sales prices for goods and services
- The currency of the country who competitive forces and regulations mainly determine the sales price of goods and services

Based on above, the functional currency of the club is Kwacha as almost all the transactions are denominated in Kwacha.

The presentation currency is the currency in which the entity presents its financial statements. This can be different from the functional currency, particularly if the entity in question is foreign-owned subsidiary. For the club the presentation currency is still Kwacha.

c) Pax pty

i) Amount payable as at 31 March 2013 KR 469,000 – **see working below**

ii) The exchange loss of KR42,000 will be debited to the income statement

iii) The analysis of the loss is as follows:

Description	**(KR'000)**	**(KR'000) Amount at original rate of KR6.60**	**(KR'000) Difference Gain/(Loss)**
1st January – Bank (85,000 * 6.60	561	561	0
1st February – Bank (70,000 * 6.80)	476	462	(14)
1st March – Bank (70,000 * 6.90)	483	462	(21)
31 March – Balance c/d (70,000 * 6.70)	469	462	(7)
Exchange loss – income statement		Total	(42)

WORKING – PAYABLE ACCOUNT

Description	DEBIT (KR'000)	CREDIT (KR'000)
1st Jan 2013 – Equipment (295,000 * 6.60)		1,947
1st January – Bank (85,000 * 6.60	561	
1st February – Bank (70,000 * 6.80)	476	
1st March – Bank (70,000 * 6.90)	483	
31 March – Balance c/d (70,000 * 6.70)	469	
Exchange loss – income statement		42
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	1,989	1,989

6) Leasing option

a) Classification of the lease

The classification of a lease as either a finance lease or an operating lease is critical as significantly different accounting treatments are required for the different types of lease. The classification is based on the extent to which risks and rewards of ownership of the leased asset are transferred to the lessee or remain with the lessor. Risks include technological obsolescence, loss from idle capacity, and variations in return. Rewards include rights to sell the asset and gain from its capital value.

A lease is classified as a finance lease if it transfers substantially all the risks and rewards of ownership to the lessee. If it does not, then it is an operating lease. When classifying a lease, it is important to recognize the substance of the agreement and not just its legal form. The commercial reality is important. Conditions in the lease may indicate that an entity has only a limited exposure to the risks and benefits of the leased asset. However, the substance of the agreement may indicate otherwise.

The lease with the bank should be classified as a finance lease because:

· The Bank has no further interest in the lease and will transfer ownership to the club after four years – The substance of the transaction appear to be that the Bank is only interested in financing the asset and not owning it.

· The club will be required to pay all repair, maintenance and insurance costs as they arise –the risks and rewards of the asset have been transferred to the club

b) Accounting for the finance lease- Financial statement extracts – see workings below

Statement of Income

Year ended 31st March	**(KR'000) 2014**	**(KR'000) 2015**	**(KR'000) 2016**	**(KR'000) 2017**
Finance cost	389	307	209	90

Statement of financial position

As at 31st March	**(KR'000) 2014**	**(KR'000) 2015**	**(KR'000) 2016**	**(KR'000) 2017**
Non-current Liabilities				
Lease obligations	1,043	452	0	0
Current liabilities				
Lease obligations	493	591	452	0

Workings

Fair value of the asset			1,947
Less instalments:			
31st March 2014		800	
31st March 2015	800		
31st March 2016	800		
31st March 2017	542		

			2,942
Interest			995

Year End	Opening Balance	Interest @ 20%	Sub Total	Instalment	Closing balance
March 2014	1,947	389	2,336	(800)	1,536
March 2015	1.536	307	1,843	(800)	1,043
March 2016	1,043	209	1,252	(800)	452
March 2017	452	90	542	(542)	0

		995			

		2014	`2015	2016	2017

Amount outstanding	1536	1043	452	0
Less principal repayment in next 12 months *-current	(493	(591)	(452)	
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Payable after more than 1 year – non-current	1,043	452	0	

· Amount payable in next twelve months less interest for that year – e.g. for 2014 (800-307 =) -