

QUESTION TWO

SOLUTIONS

SECTION A

1) Fundamental principles:

a) Matters to considered in determining the need to disclose matters in the public interest

i. The potential monetary value involved

The monetary value would determine how significant NewZ values the scandal behind the story. This may also indicate the perceived public profile of the parties involved.

ii. Whether members of the public are likely to be or become involved

The scandals are about people and therefore the public is likely to be involved.

iii. The gravity

As the paper is to be focused on sensation and scandal, these issues can affect all and sundry from the President of the nation to the catholic priest. Certain aspects of these stories can therefore have serious implications.

iv. The likelihood of repetition

As the objective of the paper is to report such matters on a daily basis, it is more likely than not that the issues would be repeated.

v. The reasons for the client's unwillingness to make the disclosures

It is probably unlikely that NewZ would like to publicise that they pay informants for their "news" as this may destroy some level of credibility in the stories.

vi. Relevant legislation, accounting standards and auditing standards

Anything against the law or accounting standards becomes illegal and questions the professional accountant's continuous involvement with the client.

vii. Legal advice obtained

Reporting otherwise confidential matters need to be carefully considered as they can have wide ranging implications, including legal implications. Accordingly, legal advice obtained should be given serious consideration.

b) Analysis of the trainee's actions AND advice

As a registered ZICA licentiate member, Jason is bound by ZICA's Code of Ethics which requires him to show objectivity, professional competence, professional behavior, integrity and confidentiality. Failure to do so could result in him being disciplined by ZICA and, extreme cases, having his membership revoked.

Jason has already demonstrated **professional competence** in identifying this unusual pattern of transactions. He was also correct to investigate them to identify their source.

However, by discussing the matter in the pub after work, Jason has not **behaved professionally**. He should have raised these issues within the workplace to add a degree of formality.

Using his **objectivity**, the trainee should be concerned about these transactions. Although the comments in the pub are not, in themselves, conclusive evidence, it leaves his concerns unanswered and, potentially, increased.

Given the apparent involvement of the Operations Manager (evidenced by his authorization of these expenses), the trainee should find someone else to report it to. However, as there are still other internal avenues to explore, it would be a breach of confidentiality to report this to external bodies such as newspapers at this stage, even though his determination not to accept any money for this story indicates an appropriate level of **integrity**.

Assuming that these payments are not authorized at the highest level, the trainee should report these transactions to a senior, independent manager within the business. Many organizations have a whistle-blowing contact, to whom third parties and employees can report their concerns in confidence. If this doesn't exist, the trainee should consider approaching the internal Audit department (if NewZ Ltd has one) or, if this is not possible, one of the other Directors.

If, having formally reported this issue internally, no action is taken, an assessment should be done as to whether the matter is:

- In the public interest
- Serious
- Public may be adversely affected
- The matter would be repeated

In any case, it would be advisable to seek legal advice before reporting to any external body including the Independent Media Review Board.

c) Continuing professional relationship

In accepting and continuing a professional relationship with client, the professional accountant is required to undertake specific client screening procedures to ensure that the professional accountant is not associated with a client exposed to any adverse publicity.

For NewZ Ltd, the screening procedures would include:

- Consider whether Lisho Associates have the competence to perform the engagement
- Lisho Associates must establish whether the pre-conditions for professional engagement are present and that there is a common understanding between NewZ Ltd and Lisho Associates as to their respective responsibilities.
- Consider whether acceptance would create any threats to compliance with the fundamental ethical principles.

The payments to confidential informants may have far reaching consequences if they are false, as they may lead to litigation for defamation, libel and slander. These are clearly negative consequences that should ethically be avoided. If Lisho Associates consider the threats significant, then the firm must apply appropriate safeguards to manage those threats. However, if the threat is considered so great that no safeguard would effectively reduce the risk, then the engagement should be discontinued.

2) Tax implication of the Despatch:

a) Value Added Tax (VAT) issues facing Despatch Ltd, including the tax point, the tax period and computation of the VAT position for the first year

The Value Added Tax (VAT) issues facing Despatch Ltd are as follows:

i. VAT registration

VAT registration is compulsory once taxable supplies exceed K50 million in any period of three months or K200 million in any period of twelve months. Monthly taxable supplies are K48 million ($K60 \text{ million} \times 80\%$), so quarterly registration threshold will be exceeded at the end of May 2011 ($K48 \text{ million} \times 2 = K96 \text{ million}$). The Commissioner General should be notified immediately the company intends to trade and registration would normally be granted from 1 April 2011 as it is clear from the outset that the turnover will exceed the registration threshold.

Despatch would benefit from registering for VAT as soon as trading commences, rather than when the VAT registration is exceeded. If significant amount of sales are to VAT registered customers, charging VAT will not be an additional cost to them. Despatch Ltd's input VAT

will be recoverable, subject to the partial exemption rules, and pre-registration VAT may not be cut off from recovery.

ii. Partial Exemption

Despatch is making exempt supplies in addition to standard rated supplies. It is necessary to determine the amount of input VAT recoverable:

	K'000
Recoverable K 28 million * 16% * 80%	3,584
Irrecoverable K 28 million * 16% * 20%	896

iii. Tax point

The correct tax point will have to be identified. The basic tax point is when the services are performed, unless an invoice is issued, or payment is received before this date, in which case this becomes the basic tax point. The basic tax point is generally replaced with an actual tax point which is the invoice date when an invoice is issued within 14 days of the basic tax point, as in Despatch case.

iv. Pre-registration input VAT

Assets and inventories have been purchased in the previous two months. As the inventory was acquired for the purpose of the business within six months prior to registration, any input VAT may be recovered if at the time of registration for VAT, they will not have been consumed. Input VAT may also be recovered on non-current assets to be used for business purposes and bought within six months of registration. Input VAT incurred on the equipment will be recovered as a result. Input VAT incurred on the two motor cars will not be recovered.

Total recoverable pre-registration input VAT will be:

	K'000
Inventory K32,480,000 * 4/29	4,480
Equipment K 72,500,000 * 4/29	10,000

Total recoverable pre-registration VAT	14,480
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v. Bad Debts relief

Output VAT must be accounted for when a sale is invoiced and can only be recovered when the debt has been written off as bad in the supplier's books of account and is at least eighteen months overdue. Despatch will therefore be able to claim bad debt relief in respect of any bad debts written off provided the above conditions are met.

b) Tax payable by Despatch, including withholding tax and taxes payable by the directors.

Tax computations for 2011/12

(i) Income Tax payable for Despatch

	K'000	K'000
Total turnover (K60 million * 12)		720,000
Less allowable expenses:		
Cost of sales (K28 million * 12)	336,000	
Motoring expenses	12,000	
Fuel allowance (K24 million * 2)	48,000	
Directors' emoluments (K60 million * 2)	120,000	
	-----	(516,000)

		204,000
Add adjustment for personal to holder cars: (15 million * 2)		30,000

		234,000
Less capital allowances:		
Motor cars (20% * 2 * K30 million)	12,000	
Equipment (25% * 72.5 million * 25/29)	15,625	
	-----	(27,625)
Taxable profit		-----
		206,375
		=====
Company tax @ 35%		72,231
Withholding tax on dividends (20 million * 2 * 15%)		6,000

		78,231
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(ii) Taxes payable by the managing editor and her deputy

	MANAGING EDITOR	DEPUTY
	K'000	K'000
Emoluments	60,000	60,000
Fuel Allowance	24,000	24,000
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Taxable income	84,000	84,000

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Income Tax:		
K9,600,000 * 0%	0	0
K6,420,000 * 25%	1,605	1,605
K33,180,00 * 30%	9,954	9,954
K34,800,00 * 35%	12,180	12,180
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	23,739	23,739
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SECTION B

The Zambia Institute of Chartered Accountants launched the three tier Financial Reporting Framework in Zambia on 15th December 2010.

3) Intended purposes of the Framework

The intended purposes of the Framework

a) To provide guidance on the accounting treatments suitable for MSEs in Zambia

For some time now, the criteria used for defining an MSE has been unclear and the related accounting, taxation and auditing requirements somewhat conflicting. The Framework provided a welcome clarification on these issues

b) To reduce the reporting burden on such entities

Before the introduction of the Framework, all Limited companies in Zambia were required to have their financial statements comply with the full International Financial Reporting Standards as adopted by ZICA. For many SMEs the cost of the audit and compliance was prohibitive.

c) To ensure that transactions are recognised with integrity to enable the primary users to place reliance on the financial statements

There are many negative perceptions typically associated with SMEs. These include incomplete and inaccurate records and high levels of non-compliance with applicable laws and regulations. Compliance with the new Framework is expected to significantly reduce on these perceptions.

d) To enable entities to prepare financial statements that enable the primary users to evaluate or assess the reporting entity's profitability, liquidity, solvency, resources and cash flows , as well as other risks

The primary users are deemed to be the owners, tax authorities, lenders and other external parties. These require useful financial information for them to make economic decisions

4) Requirements of the Framework:

a) **Description of the three categories**

b) **Stated Financial Reporting Framework and the Audit Assurance requirements**

Under the three tier financial reporting framework, entities have been categorised are as follows:

No.	Type of Entity	Financial Reporting Framework	Audit Assurance Requirement
1.	Listed Companies, Public Interest Entities and Government Owned Enterprises	Full IFRS	Full Audit Assurance Engagement
2.	Economically Significant Companies – companies that are not public companies or quoted on the stock exchange with turnover of K20 billion and above	IFRS for SMEs or Full IFRS if the Company opts to use it	Full Audit Assurance Engagement
3.	Micro and Small Entities – entities with Turnover of less than K20 billion	Zambian Financial Reporting Standard for Micro and Small Entities	No full audit required. If needed full audit can be done, otherwise Accountants report will suffice subject to Companies Act amendment

c) **Enterprises prohibited from applying this Standard**

Entities prohibited from applying this Standard.

Regardless of whether or not the entity is an incorporated entity or not, the following entities are prohibited from applying this Standard:

- a) Entities which actively trade in financial instruments including shares, derivatives and bonds.
- b) Entities which are property investment entities [i.e. entities whose primary business is to hold a portfolio of properties (land and /or building, or part thereof) to earn rentals or for capital appreciation, or both]

5) Transition rules:

a) Restatement of previous periods

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NewZ Ltd's first financial statements that conform to this Standard are the first annual financial statements in which the entity makes an explicit and reserved statement in those financial statements of compliance with the standard

NewZ Ltd is not required to restate its comparative financial information to comply with this Standard. The entity may however, if it wishes to, restate its comparative financial information as if it has always complied with this standard, or from the earliest dated practicable. NewZ Ltd may restate any item previously accounted for on a basis other than the adjusted historical cost, for example fair value, as if the requirements of this Standard have always applied

In this case the previous period carrying amounts (s) shall be deemed to be the cost of the item at the beginning of the current reporting period. These items may, however, not be re-valued again and shall only be accounted for on the adjusted historical cost basis from the beginning of the current period.

b) Disclosure requirements

Disclosure requirements

When NewZ adopts this Standard for the first time, it is required to disclose the applicable framework, standards or details of its entity-specific accounting policies that it applied in the comparative period.

If any of the items in the previous accounting framework was recognised on a basis other than adjusted historical cost, for example fair value, NewZ Ltd is required to disclose these items. In addition, NewZ Ltd will be required to disclose the basis and date of the last valuation or measurement that formed the basis of the recorded carrying amount, and the fact that no later valuation has been recorded (except in the case of impairment adjustments based on a valuation).

NewZ Ltd will be required to disclose an analysis of the extent to which comparative amounts were restated in the first reporting period that an entity adopts this Standard.