MAY 2015
Q & A

INTERMEDIATE LEVEL

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Contents

EXAMINATION	**:**	**INTERMEDIATE LEVEL**
SUBJECT	**:**	**FINANCIAL MANAGEMENT**
CODE	**:**	**B1**
EXAMINATION DATE	**:**	**TUESDAY, 5TH MAY 2015**
TIME ALLOWED	**:**	**THREE HOURS (2:00 P.M. – 5:00 P.M.)**

GENERAL INSTRUCTIONS

1. There are **TWO** sections in this paper. Section **A** and **B** which comprise **SEVEN** questions.
2. Answer question **ONE** in section **A**.
3. Answer any **FOUR** questions in Section **B**.
4. In total answer **FIVE** questions.
5. Marks are shown at the end of each question.
6. Calculate your answers to the nearest two decimal points.
7. Show clearly all your workings in respective answers where applicable.
8. This question paper comprises **8** printed pages.

SECTION A
Compulsory Question

QUESTION 1

Safari Company wishes to calculate its Weighted Average Cost of Capital (WACC) and the following is the current information relating to the company.

Number of ordinary shares	2 million
Number of 5%, Tshs.100 non-callable preferred stock	1 million
Book value of 10%, Tshs.1,000, irredeemable bonds	Tshs. 20 million
Market price of ordinary shares	Tshs. 50 cum dividend
Market price of 5%, Tshs.100 non-callable preferred stock	Tshs. 43 ex dividend
Total dividend just paid	Tshs. 4 million
Market price of 10% Tshs. 1,000, irredeemable debt	105 percent ex interest
Equity beta of Safari company	1.5
Treasury bill rate	5%
Expected return on the market	12%

Additional information:

1. The corporate tax rate applicable to Safari company is 35%.

2. The dividends of Safari Company are expected to grow at an average rate of 6%.

REQUIRED:

(a) Estimate the Safari Company's equity risk premium and the cost of equity using the Capital Asset Pricing Model (CAPM). **(3 marks)**

(b) Calculate the market value Weighted Average Cost of Capital of Safari Company using:
   (i) The dividend growth model
   (ii) The Capital Asset Pricing Model **(12 marks)**

(c) Discuss whether the dividend growth model or the CAPM offers the better estimate of the cost of equity of a company. **(3 marks)**

(d) Discuss the circumstances under which the weighted average cost of capital can be used in investment appraisal. **(2 marks)**
(Total: 20 marks)

SECTION B

There are **SIX** questions. Answer **ANY FOUR** questions

QUESTION 2

(a) Mabruk Company is considering investing Tshs. 35 million in a new machine with an expected life of five years. The machine will have no scrap value at the end of the five years. It is expected that 20,000 units will be sold each year at a selling price of Tshs. 2,100 per unit. Variable production costs are expected to be Tshs. 1,150 per unit, while incremental fixed costs, mainly the wages of a maintenance engineer, are expected to be Tshs. 7,000,000 per year. Mabruk Company uses a discount rate of 12% for investment appraisal purposes and expects investment projects to recover their initial investment within two years.

REQUIRED:

Calculate the Net Present Value (NPV) of the project and evaluate the sensitivity of the project's NPV to a change in the following project variables:

(i) Sales revenue

(ii) Sales price

(iii) Sales volume

(iv) Variable cost **(12 marks)**

(b) Tangwi plc is considering investing in one of two proposed short-term portfolios of four short-term financial investments. The correlation between the returns of the individual investments is believed to be negligible in both options proposed. The market return is estimated to be 15%, and the risk free rate 5%.

Portfolio 1

Investment	**Amounts invested Tshs. (million)**	**Expected return**	**Total risk**	**Beta**
a	10	20%	8	0.7
b	40	22%	10	1.2
c	30	24%	11	1.3
d	20	26%	9	1.4

Portfolio 2

Investment	**Amounts invested Tshs. (million)**	**Expected return**	**Total risk**	**Beta**
a	20	18%	7	0.8
b	40	20%	9	1.1
c	20	22%	12	1.2
d	20	16%	13	1.4

REQUIRED:

(i) Calculate the risk and return of the two portfolios using the principles of both portfolio theory and the CAPM.

(ii) Which portfolio appears to be more efficient?

(8 marks)
(Total: 20 marks)

QUESTION 3

(a) You have been recently appointed as the Finance Director of Haneti Company, a company specializing in processing milk products. The Managing Director of Haneti Company has approached you for advice. On 31st December 2015 the company will be replacing its three existing company cars with brand new vehicles. The Managing Director wishes to know whether he should replace these new vehicles after every one year, two or three years from now on. He has provided the following background information:

1. Each new car will cost Tshs. 22 million

2. Resale values for each car (assumed to be received in cash on the last day of the year to which they relate) are estimated to be Tshs. 14 million after one year, Tshs. 8.4 million after two years and Tshs. 3.6 after three years.

3. Annual running costs for each car (assumed to be paid on the last day of the year to which they relate) are estimated at Tshs. 13.2 million in the first year of ownership, Tshs. 15.2 million in the second year and Tshs. 18.4 million in the third year.

4. The company uses a discount rate of 10% in appraisal of such investments.

5. For the purpose of advice to be given to the Managing Director, taxation and inflation can be ignored.

REQUIRED:

Using appropriate calculations, advice the Managing Director of the optimal replacement policy for these new company cars. **(10 marks)**

(b) Korongo Mbaka wishes to choose the best of two equally costly cash flow streams: Annuity X and annuity Y. X is an annuity due with a cash inflow of Tshs. 9,000 for each of 6 years. Y is an ordinary annuity with a cash inflow of Tshs. 10,000 for each of 6 years. Assume that Korongo can earn 15 per cent on his investments.

REQUIED:

(i) On a purely subjective basis, which annuity do you think is more attractive? Why? **(3 marks)**

(ii) Find the future value at the end of year 6 for both annuity X and Y. **(3 marks)**

(iii) Use your findings in part b(ii) to indicate which annuity is more attractive. Compare your findings to your subjective response in part b(i). **(4 marks)**

(Total: 20 marks)

QUESTION 4

You have been hired as a Financial Analyst by Hesley Company. The company is considering investing in one of two projects and the Managing Director of the firm has approached you for an immediate advice. Returns on the two projects are very much influenced by the weather.

The details of the two projects as well as the estimated returns of the market are as given below:

State of Nature	Probability	Project I Mwanza Poultry	Project II Arusha Mining	Market
		Possible Return	Possible Return	Estimated Return
Rainy	0.4	10%	15%	30%
Sunny	0.4	20%	20%	20%
Cloudy	0.2	10%	-5%	-10%

Either, project would require an investment of Tshs. 175 million. The company has currently in issue of one million Tshs. 100 ordinary shares with market value of Tshs. 120 ex-div each and 10% unsecured bonds currently quoted at 105.8 percent.

The Tanzania Treasury bill rate is currently 9%.

REQUIRED:

By making necessary computation and analysis, advise the Managing Director whether the company should invest in Project I [Mwanza Poultry] or Project II [Arusha Mining] or neither. **(20 marks)**

QUESTION 5

(a) Benbera Enterprise has carried on business in Zanzibar for a number of years as a retailer of a wide variety of consumer products and it operates from a number of stores throughout Zanzibar. Summary financial information for Benbera Enterprise is given below, covering the last two years.

STATEMENT OF INCOME (EXTRACT)

	Current Year Tshs. '000'	**Previous Year Tshs. '000'**
Revenue	74,500	68,000
Cost of sales	28,300	25,700
Salaries and wages	20,000	19,600
Other costs	11,500	9,200
Profit before interest and tax	14,700	13,500
Interest	1,600	1,900
Tax	4,300	3,700
Profit after interest and tax	8,800	7,900
Dividend payable	4,800	3,100

STATEMENT OF FINANCIAL POSITION (EXTRACT)

	Current Year Tshs. '000'	**Previous Year Tshs. '000'**
Shareholders' fund	39,900	35,100
Long term debt	14,000	17,500
Additional Information		
Number of ordinary shares in issue ('000')	14,000	14,000
P/E Ratio (average for the year)		
Benbera Enterprise	14.0	13.0
Industry	15.2	15.0

REQUIRED:

Evaluate the performance of Benbera Enterprise over the last two years using the following ratios:

(i) Net Profit Margin **(3 marks)**
(ii) Return on Equity **(3 marks)**
(iii) Debt/Equity Ratio **(3 marks)**
(iv) P/E Ratio **(3 marks)**

Assume 365 day year.

(b) Comment on the argument that accounting profits may not be the best measure of a company's performance. **(8 marks)**

(Total : 20 marks)

QUESTION 6

(a) Umoja Company has annual sales of Tshs. 120,000,000 and all sales are on 30 days' credit, although customers on average take ten days more than this to pay. Contribution represents 60% of sales and the company currently has no bad debts. Accounts receivable are financed by an overdraft at an annual interest rate of 7%.

Umoja Company plans to offer an early settlement discount of 2% for payment within 15 days and to extend the maximum credit offered to 60 days. The discount is expected to be taken by 30% of customers, with the remaining customers taking an average of 60 days to pay. The company expects that these changes will increase annual credit sales by 10%, while also leading to additional incremental costs equal to 1% of turnover.

REQUIRED:

Assuming a 360-day year, evaluate whether the proposed changes in credit policy will increase the profitability of Umoja Company. Advice the company on the key factors to be considered when formulating working capital funding policy.

(10 marks)

(b) Shilo Designs Company is a small sized manufacturing entity engaged in the manufacturing of electrical parts. The firm has been following a policy of paying dividend every year. The shares are listed on the stock exchange and currently command a price earnings ratio (P/E) of 11.5.

Other details are as follows:

Earnings of the company	Tshs. 500 million
Dividend	Tshs. 375 million
Number of equity shares	20,000,000 @ Tshs. 250 per share.

The firm is estimated to maintain the current rate of earnings on investment.

REQUIRED:

By applying Walter's dividend model:

(i) Determine the share price **(5 marks)**

(ii) Establish whether the Dividend/Price ratio is optimal. **(5 marks)**

(Total: 20 marks)

QUESTION 7

Rafiq Company, a medium – sized company specializing in the manufacture and distribution of textile products for women, is evaluating a new capital expenditure project. The details of the proposed investment project are set out below:

(i) The project has an immediate cost of Tshs. 42,000,000

(ii) Expected Sales:
- Year 1 through 3: Tshs. 31,000,000 per annum
- Year 4 and 5: Tshs. 13,000,000 per annum

(iii) Variable Costs:
- Cost of sales: 40% of Sales
- Distribution cost 10% of sales

(iv) Fixed cost (rent, utility bills and other fixed expenses) amounted to Tshs. 4,000,000 per annum

(v) Depreciation is not tax allowable

(vi) The corporate tax rate applicable to the firm is 35%

(vii) The company's cost of capital is 6% while the risk adjusted cost of the project is 5%.

The Directors of Rafiq Company require that all investment projects should be evaluated using either payback period or return on capital employed (accounting rate of return). The target payback period of the company is two years and the target return on capital employed is 20%. A project is accepted if it satisfies either of these investment criteria.

REQUIRED:

(a) Evaluate the economic viability of the proposed investment project using the Net Present Value (NPV) Method. **(8 marks)**

(b) Calculate the project's Internal Rate of Return (IRR) and discuss the strengths and weaknesses of the IRR in appraising capital investments. **(4 marks)**

(c) Calculate the return on capital employed (accounting rate of return) and the payback period of the company and assess the economic viability of the project if the project is to be appraised using these methods. **(4 marks)**

(d) Critically discuss the Directors' view on investment appraisal. **(4 marks)**

(Total: 20 marks)

EXAMINATION	**:**	**INTERMEDIATE LEVEL**
SUBJECT	**:**	**FINANCIALACCOUNTING**
CODE	**:**	**B2**
EXAMINATION DATE	**:**	**WEDNESDAY, 6THMAY, 2015**
TIME ALLOWED	**:**	**THREE HOURS (2:00 P.M. – 5:00P.M.)**

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GENERAL INSTRUCTIONS

1. There are **TWO** Sections in this paper. Sections**A** and **B** which comprise **SEVEN** questions.
2. Answer question **ONE** in Section **A.**
3. Answer **ANYFOUR** questions in Section **B**.
4. In total answer**FIVE** questions.
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8. This question paper comprises **9** printed pages.

SECTION A
Compulsory Question

QUESTION 1

KPP Ltd is one of famous soft and hard drink producer in Tanzania, currently the company has been considering how to expand its market share. On 1st October 2014, KPP Ltd acquired 75% of Pluto's equity shares by means of a share exchange of two new shares in KPP for every five acquired shares in Pluto Ltd. In addition, KPP Ltd issued to the shareholders of Pluto Ltd a Tshs.100, 10% loan note for every 1000 shares it acquired in Pluto Ltd. KPP Ltd has not recorded any of the purchase consideration, although it does have other 10% loan notes already in issue. The market value of KPP's shares at 1st October 2014 was Tshs.2 each. The summarized Statements of Financial Position of the two companies as at31st March 2015 are as follows

	KPP Ltd	**Pluto Ltd**
	Tshs. "000"	**Tshs. "000"**
Asset		
Non-Current Asset		
Property, Plant and Equipment	47,400	25,500
Financial Asset: Equity Investments (Notes 1 and 4)	10,500	3,200
Total	**57,900**	**28,700**
Current Assets		
Inventory (Note 2)	17,400	8,400
Trade receivable (Note 3)	14,800	9,000
Bank	2,100	
Total Asset	**92,200**	**46,100**
Equity and Liabilities		
Equity		
Equity shares of Tshs1 each	40,000	20,000
Retained Earnings/losses		
As at 1st April 2014	19,200	(4,000)
As at31st March 2015	7,400	8,000
Total	**66,600**	**24,000**
Non-current Liabilities		
10% Loan notes	8,000	
Current Liabilities		
Trade payables (Note 3)	17,600	13,000
Bank Overdraft		9,100
Total Equity and Liabilities	**92,200**	**46,100**

Notes

The following information is relevant:-

(i) At the date of acquisition, Pluto Ltd produced a draft statement of profit or loss which showed it had made a net loss after tax of Tshs.2 million at that date. KPP Ltd accepted this figure as the basis for calculating the pre-and post-acquisition split of PlutoLtd's profit for the year ended 31st March 2015.

Also at the date of acquisition, KPP Ltd conducted a fair value exercise on PlutoLtd's net asset which were equal to their carrying amounts (includingPluto's financial asset equity investments) with the exception of an item of plant which had a fair value of Tshs.3 million below its carrying amount. The plant has a remaining economic life of three years at 1st October 2014. KPP's policy is to value the non-controlling interest at fair value at the date of acquisition. For this purpose, a share price for Pluto of Tshs.1.2 each is representative of the fair value of the shares held by the non-controlling interest.

(ii) Each month since acquisition, KPP's sales to Pluto Ltd were consistently Tshs. 4.6 million KPP had marked these up by 15% on cost. Pluto Ltd had one month's supply (Tshs.4.6 million) of these goods in inventory at 31st March 2015. KPP's normal mark up (to third party customers) is 40%.

(iii) PlutoLtd's current account balance with KPP Ltd at 31st March 2015 was Tshs.2.8 million, which did not agree with KPP's equivalent receivable due to a payment of Tshs.900,000 made by Pluto Ltd on 28th March 2015, which was not received by KPP Ltd until 3rd April 2015.

(iv) On 1st January 2015, KPP Ltd acquired 35% of the equity shares in RAC Ltd, a holding which enabled it to exercise significant influence. RAC Ltd had retained earnings of Tshs7.5 million at 31st March 2014 and Tshs.13.5 million at 31st March 2015. Its profits accrue evenly over the year. RAC Ltd paid a dividend of Tshs2 million on 1st March 2015 and KPP Ltd credited its dividend received to profit or loss.

(v) The financial asset equity investments of KPP Ltd include Tshs.3 million paid for the shares in RAC Ltd. The other financial asset equity investments of KPP Ltd and Pluto Ltd are carried at their fair values as at 1st April 2014. As at 31st March 2015, these had fair values of Tshs.7.1 million and Tshs.3.9 million respectively.

(vi) There was no impairment losses within the group during the year ended 31st March 2015.

REQUIRED:

Prepare the Consolidated Statement of Financial Position for KPP Ltd as at 31st March 2015. **(20 marks)**

SECTION B

There areSIX questions.Answer **ANY FOUR** questions

QUESTION 2

(a) Discuss the following concepts in the context of IAS 1, Presentation of Financial Statements;

(i) Accruals
(ii) Going Concern
(iii) Materiality and aggregation
(iv) Consistency **(10 marks)**

(b) According to the provisions in International Financial Reporting Standards, there are four major attributes that enhance the qualitative characteristics of useful financial information. These are: "comparability", "verifiability", "timeliness" and "understandability".

REQUIRED:

Briefly elaborate the meaning of each attribute and show how they enhance the qualitative characteristics of useful financial information. **(10 marks)**

(Total: 20 marks)

QUESTION 3

Kalambo Company Ltd. a retailing company, has an authorized share capital of Tshs. 700,000 Ordinary shares of Tshs. 1,000 each. The following trial balance was extracted from the books of account as at 31st December 2014.

Particulars	Dr	Cr
	Tshs. '000,000'	Tshs. '000,000'
Issued share capital		560
Share premium account		140
Profit and loss account		180
10% debentures		100
Furniture and fittings at cost	400	
Depreciation to 1st January 2014		200
Cash balance	118	
Trade debtors	500	
Trade creditors		120
Stock at 1st January 2014	400	
Hire charges (distribution, vehicles, etc)	680	
Purchases	1,000	
Administrative expenses	300	

Deferred taxation		80
Distribution costs	200	
Accrued expenses		50
Auditors' remuneration	40	
Interim dividend (paid on 1st July 2014)	14	
Trade investments at cost (market value Tshs. 170,000,000)	140	
Debenture interest (gross)	10	
Dividends received (on 1st December 2014)		30
Turnover		2,400
Prepaid expenses	58	
	3,860	3,860

You are also given the following information:

(a) Turnover excludes value added tax

(b) Stock at 31st December 2014 was valued at Tshs. 600,000,000

(c) Depreciation of Tshs. 80,000,000 is to be charged on the furniture and fittings for the year to 31st December 2014.

(d) Administration includes Director's emoluments of Tshs. 110,000,000.

(e) The corporation tax payable (based on the profits for the year to 31st December 2014 at a rate of 30%) is estimated to amount to Tshs. 100,000,000.

(f) The company proposes to pay a final ordinary dividend of 10 percent.

REQUIRED:

Prepare Statement of Comprehensive Income and Statement of Financial Position for publication for the year ended 31st December 2014, together with relevant notes. **(20 marks)**

QUESTION 4

Panacea Ltd is a Tanzanian firm famous for production of electronic equipment. The company top management has been concerned about the company's performance especially in comparison to its competitors and the industry in which it operates. Given below are the Statement of Comprehensive Income and Statement of Financial Position for the company for year ended 31stDecember 2014.

Panacea Ltd Statement of Financial Position as at 31st December 2014 and 31st December 2013

PARTICULARS	2013 Tshs. "000,000"	2014 Tshs. "000,000"
Assets		
Current Assets		
Cash	150	125
Account receivable	350	375
Inventory	475	550
Total Current Assets	**975**	**1,050**
Non-Current Assets		

Plant and equipment	2,425	2,750
Less accumulated depreciation	(1,000)	(1,200)
Net plant and equipment	1,425	1,550
Total Assets	**2,400**	**2,600**
Liabilities and Equity		
Liabilities		
Current liabilities		
Account payable	**200**	**150**
Notes payable current 9%	-	150
Total Current liabilities	**200**	**300**
Non-current liabilities		
Long term debt	400	600
Total liabilities	**800**	**900**
Equity		
Common stock	300	300
Paid in capital	600	600
Retained Earnings	700	800
Total equity	**1,600**	**1,700**
Total equity and liabilities	**2,400**	**2,600**

Panacea Ltd Statement of Comprehensive Income for the year ended 31st December 2013 and 31st December 2014

	2013	**2014**
	Tshs. "000,000"	**Tshs. "000,000"**
Sales	1,200	1,450
Cost of goods sold	700	850
Gross profit	**500**	**600**
Operating Expenses	30	40
Depreciation	220	200
Net operating income	**250**	**360**
Interest expense	50	64
Net income before taxes	**200**	**296**
Taxes 40%	80	118
Net income after tax	**120**	**178**

The industrial average performance for 2014 was as follows:

		2014
Current ratio		3.25
Quick ratio		2.75
Inventory turnover		2.2
Average collection period		90
Debt ratio		0.20
Times interest earned		7.00
Total asset turnover		0.75
Non-current Asset turnover		1
Operating profit margin		20%
Return on equity		9%

REQUIRED:

(a) For each of the given industrial average performances, calculate the firm's corresponding ratio and discuss the firm's performance. **(14 marks)**

(b) What are disadvantages of using ratios as the basis of performance measurement?

(6 marks)

(Total: 20 marks)

QUESTION 5

(a) IAS 16: Property, Plant and Equipment, outlines the accounting treatment for most types of property, plant and equipment.

REQUIRED:

Present the recognition criteria under this standard. **(4 marks)**

(b) The IASB's Conceptual Framework specifies manner of determining the value of different elements (i.e. Measurement of elements).

REQUIRED:
Briefly illustrate the measurements bases as spelled out by the Framework.

(6 marks)

(c) Discuss the criteria for classifying an asset as either a current asset or non-current asset. **(2 marks)**

(d) Makao Ltd started a construction of new building to be used as a store on 1st April 2013. The following costs were incurred on the construction:-

	Tshs."000"
Freehold land	4,500
Architect fees	620
Site preparation	1,650
Materials	7,800
Direct labour costs	11,200
Legal fees	2,400
General overheads	940

The store was completed on 1st January 2014 and brought into use following its grand opening on the 1st April 2014. Makao Ltd issued a Tshs.25 million unsecured loan on 1st April 2013 to aid construction of the new store; this meets the definition of qualifying asset as per IAS 23. The loan carried an interest rate of 8% per annum and is repayable on 1st April 2016.

REQUIRED:

(i) Calculate the total amount to be included as property, plant and equipment in respect of the new store

(ii) State what impact the above information would have on the Statement of Comprehensive Income (if any) for the year ended 31st March 2014.

(8 marks)
(Total : 20 marks)

QUESTION 6

(a) In addition to the legal system and tax legislation differences, accounting disclosure practices around the world are influenced by variety of economic, social and political factors. The wide range of factors influencing the development of accounting regulations have resulted in a wide range of different systems which have made it difficult and time consuming to try to standardize accounting practice around the world, hence harmonization seems to be a better way than standardization.

REQUIRED:

(i) What do you understand by the terms "harmonization" and "standardization" as used in conceptual framework? **(3 marks)**

(ii) Why is harmonization of the standard very important? **(2 marks)**

(iii) Briefly describe possible benefits that could accrue from the development of a single set of accounting standard which could be applied in all countries. **(5 marks)**

(b) When companies expand or change its organizational structure by acquiring other companies or through internal division, the new structure must be examined to determine the appropriate financial reporting procedures.

REQUIRED:

Identify and explain several approaches used for expansion or change of organizational structure. **5 marks)**

(c) On 30th September 2014, J.J. Ltd purchased 100% of the ordinary share capital of Kamata Ltd for Tshs.1,800,000. The book value of Kamata Ltd's net assets at the date of acquisition was Tshs.1,350,000. A valuation exercise showed that the fair value of Kamata Ltd's property, plant and equipment at that date was Tshs.100,000 greater than its book value. Kamata Ltd immediately incorporated this revaluation into its own books of account. Kamata Ltd's financial statements at 30th September 2014 contained notes referring to a contingent liability with a fair value of Tshs.200,000.

REQUIRED:

Calculate goodwill on acquisition. **(5 marks)**
(Total :20 marks)

QUESTION 7

In December 2014, Mkinga Company paid Tshs. 54 million cash for a new building acquired to accommodate an expansion of operations. The company financed this purchase partly by a new issue of long-term debt for Tshs. 40 million cash. During 2014, the company also sold fixed assets for Tshs. 5 million cash. The assets were listed on Mkinga Company's books at Tshs. 5 million. All sales and purchases of merchandise were on credit.

The 2014 net income of Tshs. 4 million was the highest in the company's history. However, MakusaroMkinga, the Chairman of the Board, was puzzled by the company's extremely low cash balance.

The following information was obtained from the company;

Statement of Comprehensive Income for the year ended December31, 2014

	Tshs.	Tshs.
Sales		100,000,000
Less: Cost of goods sold		
Inventory, December 31, 2013	15,000,000	
Purchases	105,000,000	
Cost of goods available for sale	120,000,000	
Inventory, December 31, 2014	(47,000,000)	73,000,000
Gross profit		27,000,000
Less: other expenses		
General expenses	8,000,000	
Depreciation	8,000,000	
Property taxes	4,000,000	
Interest expense	3,000,000	
		23,000,000
Net income		4,000,000
Retained earnings, December 31, 2013		7,000,000
Total		11,000,000
Dividends declared and paid		1,000,000
Retained earnings, December 31, 2014		10,000,000

Statement of Financial Position as at December 31Assets Liabilities and Stockholders Equity

	2014 Tshs.	2013 Tshs.		2014 Tshs.	2013 Tshs.
			Accounts payable	39,000,000	14,000,000
Cash	1,000,000	20,000,000	Accrued property tax payable	3,000,000	1,000,000
Accounts receivable	20,000,000	5,000,000	Long-term debt	40,000,000	0
Inventory	47,000,000	15,000,000	Common stock	70,000,000	70,000,000
Prepaid expenses	3,000,000	2,000,000	Retained earnings	10,000,000	7,000,000
Net Non-current assets	91,000,000	50,000,000			
Total assets	162,000,000	92,000,000	Total liabilities and stockholders' equity	162,000,000	92,000,000

REQUIRED:

(a) Prepare a Statement of Cashflows from the Mkinga Company financial statements. Ignore income taxes. Use the direct method for reporting cash flows from operating activities. **(15 marks)**

(b) (i) Analyse the Statement of Cashflow prepared in (a) above and advise on Mkinga Company financial (cash) performance.

(ii) Does it help you reduce MakusaroMkingas' puzzle? why? **(5 marks)**

(Total: 20 marks)

EXAMINATION	**:**	**INTERMEDIATE LEVEL**
SUBJECT	**:**	**AUDITING PRINCIPLES AND PRACTICE**
CODE	**:**	**B3**
EXAMINATION DATE	**:**	**THURSDAY, 7TH MAY, 2015**
TIME ALLOWED	**:**	**THREE HOURS (9:00 A.M. – 12:00 NOON)**

GENERAL INSTRUCTIONS

1. There are **TWO** sections in this paper. Section **A** and **B** which comprise **SEVEN** questions.
2. Answer question **ONE** in sections **A**.
3. Answer **ANY FOUR** questions in sections **B**.
4. In total answer **FIVE** questions.
5. Marks are shown at the end of the each questions.
6. In marking candidates' scripts, examiners will take into account clarity of exposition, logic of arguments, proper arrangement and presentation of answers together with the use of relevant examples.
7. This question paper comprises **6** printed pages.

SECTION A
Compulsory Question

QUESTION 1

(a) As society becomes more complex, decision makers are more likely to receive unreliable information.

REQUIRED:

Discuss the major factors in today's society that have made the need for independent audits much greater than it was 50 years ago. **(4 marks)**

(c) Materiality consideration are important in both planning and performing the audit.

REQUIRED:

(i) Explain the meaning of the term 'materiality' as used in auditing. **(2 marks)**

(ii) Identify the three materiality criteria **(6 marks)**

(iii) State the generally accepted rules about materiality. Include in your answer ways that rules are important than rules of thumb. **(4 marks)**

(c) International Standard on Auditing (505) addresses the issue of External Confirmations.

REQUIRED:

With reference to this standard distinguish between 'Positive' and 'Negative' confirmation requests. **(4 marks)**
(Total : 20 marks)

SECTION B

There are **SIX** questions. Answer **ANY FOUR** questions

QUESTION 2

(a) According to ISA 200, *Objectives and General Principles Governing an Audit of Financial statements*, the objectives of an audit is "to enable the auditor to express an opinion whether the Financial Statements are prepared, in all material respect, in accordance with an identified Financial Reporting Framework". The phrases used to express the auditor's opinion are that the "Financial Statements give a true and fair view" or "Financial Statements present fairly in all material respects".

REQUIRED:

Explain the concepts of 'true and fair view'. **(4 marks)**

(b) You are the Audit Manager in A & A audit firm. The audit work of one of your clients has been completed, but there is one outstanding matter you are currently investigating about the client who is constructing a building using the company's workers and the following two problems have arisen concerning the research costs and cost of labour:

- The calculation of cost of direct labour incurred on construction of building by the company's employees have been posted as part of the cost of sales (expensed during the year). The direct costs of labour expenses is Tshs.15,000,000 while net profit before tax of the company is Tshs.150,000,000.

- The company has capitalized research costs amounting to Tshs.30,000,000. This research costs does not meet the requirement of IAS 38 *Intangible Assets.*

REQUIRED:

Explain with reasons whether a qualified audit report would be necessary for each of the two circumstances outlined in the two scenarios above. **(8 marks)**

(c) Describe the different types of audit opinion and state the circumstance in which each is appropriate. **(8 marks)**

(Total : 20 marks)

QUESTION 3

(a) The overall audit objective is to give an opinion on the truth and fairness a concept that is very wide and could lead to vastly different audits being performed. To avoid this problem detailed audit assertions are required.

REQUIRED:

Explain why are 'detailed audit assertions' necessary **(4 marks)**

(b) Auditors rely on created evidence more than any other type of evidence.

REQUIRED:

Describe and compare the reliability of the following types of documentary evidence as far as the auditor is concerned, giving one example for each.

(i) Confirmations received directly by the auditors from third parties. **(3 marks)**

(ii) Documents produced by the client for the auditor which have been prepared by outsiders. **(3 marks)**

(iii) Documents produced by the client for the auditor which have been prepared by personnel within the client company. **(3 marks)**

(iv) Documentary evidence calculated by the auditor from company records. **(3 marks)**

(c) Identify the factors governing the following principles as used in the context of audit evidence:

(i) Sufficiency **(2 marks)**

(ii) Reliability **(2 marks)**

(Total : 20 marks)

QUESTION 4

(a) Fundamental principles require that a member of a professional accountancy body should behave with integrity in all professional, business and financial relationships and should strive for objectivity in all professional and business judgements. Objectivity can only be assured if the member is and is seen to be independent. Conflicts of interest have an important bearing on independence and hence also on the public's perception of the integrity, objectivity and independence of the Accountancy profession.

A partner in the firm was told by the regulatory body that he must resign because he was in breach of the regulatory body's independence rules, as his brother-in-law was a Financial Controller of an audit client. He was told that the only alternative was to move his home and place of work at least 400 kms from the offices of the client, even though he was not the reporting partner. This made his job untenable. The regulatory body was seen as 'taking its rules to absurd lengths' by the accounting firm. Shortly after this comment, the audit firm announced proposals to split the firm into three areas between audit, tax and business advisory services; Management consultancy; and investment advisory services'

REQUIRED:

Discuss the impact that the above events may have on the public perception of the integrity, objectivity and independence of the audit firm.

(10 marks)

(b) ISA 530 explains about the audit sampling and other selected test procedures. The standards apply to statistical and non-statistical sampling methods and provide practical guidance on such matters as sampling risks, stratification and selection methods.

REQUIRED:

What are the main advantages that can be derived by the auditor from the successful employment of the statistical sampling techniques, as opposed to non-statistical sampling? **(10 marks)**

(Total : 20 marks)

QUESTION 5

Maraha hotels is a parastatal organization established by an Act of Parliament in 2012. The objective of its establishment was to use its chain of stores as model hotels towards boosting tourism in the country. It has prime hotel facilities across major cities, towns and within all major national parks in Tanzania with 1,500 staffs. Of recent, the management has experienced an abnormal increase of expenditure in its Housekeeping Department in two hotels located in Serengeti and Mikumi national parks. One of the Board members who had an accountancy background initiated an agenda that required a conduct of a value for money audit in the area. The Board meeting then resolved that an expert should be invited to enlighten the Board and Management on the concept of a value for money audit.

REQUIRED:

(a) Explain briefly to the Management the nature and purpose of a value for money audit in relation to the Maraha hotels. Provide specific examples to the scenario. **(12 marks)**

(b) Briefly explain the deficiencies of value for money audit. **(4 marks)**

(c) By citing relevant laws and regulations, advise the Board members on who can be appointed as an appropriate auditor to the entity to carry out the statutory audit of the Financial Statements for the year ending 30th September 2015.

(4 marks)

(Total : 20 marks)

QUESTION 6

(a) The Public Finance Act (as amended in 2010) states that:

"There shall be an Internal Auditor General under the Ministry responsible for finance who shall be appointed by the President from amongst qualified persons in accountancy, auditing or financial matters on such terms and conditions to be specified in the letter of appointment."

REQUIRED:

Describe the roles and functions of the Internal Auditor General. **(12 marks)**

(b) In order to maintain and enhance internal auditing's credibility there must be a system of monitoring its effectiveness and efficiency. The International Professional Practices Framework (IPPF) provides guidance to internal audit activities on measuring their effectiveness and efficiency and the level of customer service they provide to stakeholders. These measurements can be both quantitative and qualitative.

REQUIRED:

Provide any four examples of audit activity performance measures that can be used to measure the effectiveness and efficiency of internal audit activities.

(8 marks)
Total : 20 marks)

QUESTION 7

(a) You have been auditing Kishavu & Co, an upcoming vehicle manufacturer in Tanzania famous for its new product in the market called Kirikuu. You have noticed that the company purchased four major machines to be employed in its production processes.

REQUIRED:

Describe five tests of control that you will employ regarding the purchase of the machinery. **(5 marks)**

(b) As you were performing the tests in part (a) above, one of the audit trainee observed that your team leader was busy going through some documents that he had collected from the Director of Finance of Kishavu & Co. These documents were:

(i) Payments made after financial year end
(ii) Lease of a premise occupied by the company
(iii) Memorandum and Articles of Association (MEMARTS) of the company
(iv) Minutes of the Board of Directors' meetings
(v) Minutes of the shareholders meetings (AGM)

REQUIRED:

Briefly explain the reasons that would lead you into scrutinizing each of the above documents. **(15 marks)**
(Total : 20 marks)

EXAMINATION	**:**	**INTERMEDIATE LEVEL**
SUBJECT	**:**	**PUBLIC FINANCE AND TAXATION I**
CODE	**:**	**B4**
EXAMINATION DATE	**:**	**THURSDAY, 7TH MAY, 2015**
TIME ALLOWED	**:**	**THREE HOURS (2:00 P.M. – 5:00 P.M.)**

GENERAL INSTRUCTIONS

2. There are **TWO** Sections in this paper. Sections **A** and **B** which comprise **SEVEN** questions.

2. Answer question **ONE** in Section **A**

3. Answer **ANY FOUR** questions in Section **B**.

4. In total attempt **FIVE** questions.

5. Marks are shown at the end of each question.

6. Calculate your answers to the nearest two decimal points where necessary.

7. Show clearly all your workings in respective answers where applicable.

8. This question paper comprises **6** printed pages.

SECTION A
Compulsory Question

QUESTION 1

(a) Outline ten (10) sources of investment income as per section 9(1) of the Income Tax Act, 2004 (as revised in 2006). **(5 marks)**

(b) Magil Ltd is a Company located at Kibaha town dealing with agricultural business. The company was formed in the United Republic of Tanzania in 2007 and became listed in the Dar es Salaam Stock Exchange (DSE) in 2009. The following transactions took place during the year of income ended on 31st December, 2014.

(i) Invested Tshs.1,800,000 in acquiring computers and data handling equipment, which were used in the internet café.

(ii) Dividends amounting to Tshs.2,500,000 received from Harpel Limited, which is a resident corporation listed on the DSE, and is owned 25% by Magil Ltd.

(iii) It acquired two (2) bulldozers each costing Tshs.10,000,000 to be used in clearing land situated at Kilwa. Prior to 2011, this land was used for agricultural purposes for four (4) years. In addition, the company also purchased two lawn mowers, which were used in keeping the surroundings clean at Tshs.450,000 each.

(iv) Paid employer's contributions amounting to Tshs.75,000,000 to an approved retirement fund.

(v) During the year, the company sold a grain storage warehouse at Tshs.120,000,000 and rice milling building at Tshs.55,000,000. These buildings were constructed and completed at a cost of Tshs.85,000,000 and Tshs.60,000,000 respectively and were put into use on 15th May 2014.

(vi) Bought shares of WAJAMENI Ltd at Tshs.25,000,000. Sold shares at Tshs.18,000,000 of WAJAMENI Ltd which were acquired in 2013 at Tshs.12,000,000. Magil Ltd owns 30% WAJAMENI Ltd.

(vii) Received dividend from Tata Limited, a non-resident corporation, amounting to Tshs.70,000,000. Magil Limited owns 45% of the shares of Tata Limited.

(viii) Magil Ltd paid interest of Tshs.5,600,000 to Tanzania Revenue Authority during the year for failure to pay taxes on due dates.

(ix) Sold a residential house for a gain of Tshs.12,000,000 to Mr. Abayo. Prior to the sale, Mr. Abayo had lived in the house for three (3) years continuously.

(x) Paid interest of Tshs.12,000,000 to CBC Bank Ltd as a result of an overdraft.

(xi) Shares worth Tshs.155,000,000 were bought from Chukua Company Limited, a resident corporation.

(xii) Received rental income of Tshs.8,000,000 from ABBY Ltd, a resident corporation. This was in respect to another residential house owned by the company.

(xiii) During the year, Magil Ltd sold five (5) hectares of land which had been used for agricultural purposes from 1983 to 2000. The land had a market value of Tshs.9,000,000. This land was purchased for Tshs.3,000,000.

(xiv) The company had bought shares from Semeni Ltd worth Tshs.28,000,000. Magil Ltd earned a profit of Tshs.4,000,000 on the sale of the shares. Semeni Ltd is cross listed in the Nairobi Stock Exchange.

(xv) Magil Ltd received Tshs.15,000,000 as interest from ABC Ltd for debentures it had acquired from the company.

(xvi) Magil Ltd paid Tshs.87,000,000 for scholarship expenses for full time studies for six (6) of its employees.

REQUIRED:

Calculate total income from investment for Magil Ltd and the total taxes due to the company for the year of income ended 31st December 2014. **(15 marks)**

(Total : 20 marks)

SECTION B

There are **SIX** questions. Answer **ANY FOUR** questions

QUESTION 2

(a) Examine the nature and types of non-tax government revenue. **(5 marks)**

(b) Analyze the nature and the objectives of taxation. **(5 marks)**

(c) Explain the principles of taxation. **(5 marks)**

(d) Explain the incidence of taxation. **(5 marks)**

(Total : 20 marks)

QUESTION 3

(a) Assume you are given the following information below:

Sales/Purchases	**Tshs. VAT exclusive**
Sales of water	680,000
Importation of standard rated services	12,000,000
Transportation of cows by a VAT registered person	150,000
Sale of maps to a secondary school	400,000
Sales of mosquito coils	800,000
Purchase of postage stamps	30,000
Purchase of taxable goods	25,000,000
Sales to Uganda (exports)	15,000,000
Purchase of water	300,000
Retail taxable sales	56,000,000
Purchase of eggs	200,000
Electricity bill	350,000
Payment of salaries	25,000,000
Purchase of alcohol for employees	3,000,000

REQUIRED:

Compute the input tax using the standard rate method. **(5 marks)**

(b) As part of improvement of tax administration and tax revenue through proper accounting records, the Value Added Tax (Electronic Fiscal Device) Regulation, 2010 requires taxable person to issue electronic fiscal receipts through Electronic Fiscal Devices (EFDs)

REQUIRED:

(i) Explain the advantages of introducing Electronic Fiscal Devices (EFDs) to different stakeholders in Tanzania. **(5 marks)**

(ii) Describe the challenges being faced in relation to Electronic Fiscal Devices (EFDs) adoption in Tanzania. **(5 marks)**

(iii) Advise the government on how it can improve the administration of Electronic Fiscal Devices (EFDs) in Tanzania. **(5 marks)**

(Total : 20 marks)

QUESTION 4

(a) Distinguish between 'tax evasion' and 'tax avoidance'. **(4 marks)**

(b) Enumerate at least five ways through which tax evasion and tax avoidance are committed. **(10 marks)**

(c) Summarise at least six consequences of tax evasion. **(6 marks)**

(Total : 20 marks)

QUESTION 5

On 28th March, 2014, Mr. Enny imported 8,000 pieces of used automobile batteries from Red Rose & Partners in Europe where Mr. Enny is also an active partner. Goods were immediately stored in a custom warehouse. The following costs relate to the goods imported:

Direct material (per unit)	Euro (€)6
Direct labour (per unit)	€4
Variable overheads (per unit)	€2
Selling unit price	€20
Insurance	€1000

The following rates were applicable at the time of importation:

Imported duty	20%
Excise duty	5%
Exchange rate: €/TZS	TZS.1,920 - TZS.2,035

Other values relating to the goods imported are as follows:

Computed value	TZS.400,000,000
Fall back value	TZS.386,000,000
Deductive value	TZS.402,000,000

Due to unavoidable circumstances, Mr. Enny failed to settle all the custom duties within the required time. The Commissioner for Customs gave several notices and decided to sell the goods through public auction on 12th February, 2015. The goods were sold for TZS.320,000,000.

REQUIRED:

(i) Compute the transaction value of the goods imported. **(5 marks)**

(ii) Compute the custom duties payable thereof. **(8 marks)**

(iii) Determine how the proceeds of sale might have been distributed assuming Mr. Enny had the following obligations to settle:

Freight charges	TZS. 3,000,000
Clearance agency fees – Dar es Salaam port	TZS. 450,000
Duties due to customs	TZS.102,000,000
Rent and charges due to customs	TZS. 8,800,000
Port charges	TZS. 4,500,000
Expenses of removal and sale of goods	TZS. 2,600,000

(5 marks)

(iv) To whom the balance, if any, is supposed to be paid to, assuming the terms of importation of the goods imported were breached? **(2 marks)**

(Total : 20 marks)

QUESTION 6

(a) Explain four possible reasons why the Tanzania government set deadlines for filling return and or paying taxes. **(12 marks)**

(b) A person with a year of income starting 1st July 2014 ending 30th June 2015, his estimated income tax for the year of income is Tshs.13,000,000. During the first two months of the year of income, he paid Tshs.1,000,000 income taxes under non-final withholding payments.

REQUIRED:

Compute the amount for each installment. **(8 marks)**

(Total : 20 marks)

QUESTION 7

(a) Describe at least four roles of public finance in a country's economy. **(10 marks)**

(b) Explain at least four primary functions of a government relating to the public finance. **(10 marks)**

(Total : 20 marks)

EXAMINATION	**:**	**INTERMEDIATE LEVEL**
SUBJECT	**:**	**PERFORMANCE MANAGEMENT**
CODE	**:**	**B5**
EXAMINATION DATE	**:**	**FRIDAY, 8TH MAY, 2015**
TIME ALLOWED	**:**	**THREE HOURS (9.00 A.M. – 12.00 NOON)**

GENERAL INSTRUCTIONS

3. There are **TWO** sections in this paper. Section **A** and **B** which comprise **SEVEN** questions.

4. Answer question **ONE** in Section **A**

5. Answer **ANY FOUR** questions in Section **B**.

4. In total answer **FIVE** questions.

5. Marks are shown at the end of each question.

6. Show clearly all your workings in respective answers where applicable.

7. State clearly any assumptions made in your answers.

8. This question paper comprises **9** printed pages.

SECTION A
Compulsory Question

QUESTION 1

ABC Ltd. manufactures three prototype toy furniture products – chairs, benches and tables. The budgeted unit cost and resource requirements for each items are detailed below:

	Chair	**Bench**	**Table**
	Tshs.	**Tshs.**	**Tshs.**
Timber cost	5,000	15,000	10,000
Direct labour cost	4,000	10,000	8,000
Variable overhead cost	3,000	7,500	6,000
Fixed overhead cost	4,500	11,250	9,000
	16,500	**43,750**	**33,000**
Budgeted Volume per annum	4,000	2,000	1,500

The volumes are believed to equal the market demand for these products. The fixed overhead costs are attributed to the three products on the basis of direct labour hours. The labour rate is Tshs.4,000 per hour. The cost of the timber is Tshs.2,000 per square metre. The products are made from a special timber. A memo from the Purchasing Manager advises you that because of a problem with a supplier, it is to be assumed that this special timber is limited in supply to 20,000 square metres per annum. The Sales Manager has already accepted an order for 500 chairs, 100 benches and 150 tables which if not supplied would incur a financial penalty of Tshs.2,000,000. These quantities are included in the market demand estimates above. The selling prices of the three products are:

Products	**Tshs.**
Chair	20,000
Bench	50,000
Table	40,000

REQUIRED:

(a) Determine the optimum production plan and state the net profit that should be yield per annum. **(16 marks)**

(b) Calculate and explain the maximum prices which should be paid per square metre in order to obtain extra supplies of the timber. **(4 marks)**

(Total : 20 marks)

SECTION B

There are **SIX** questions. Answer **ANY FOUR** questions

QUESTION 2

The Management Accountant was making presentation about implementation of the Theory of constraints. The following is part of the presentation:

> "Implementation of the Theory of Constraints is a continuous process of improvement in order to clear the throughput constraints. Our company needs to do this in relation to the three products that we produce and sell because these go through the same process centres. I have extracted some information about the market demand for each product, the processing time that each product demands from a process and the capacity of each process from records for this presentation and these are indicated in **Table 1** below:

Table 1: Market demand and hours demanded by a batch

PRODUCT BRAND	MARKET DEMAND (BATCH = 1,000 UNITS)	TIME DEMANDED BY A BATCH		
		PROCESS 1	PROCESS 2	PROCESS 3
ATUPE	300 batches	2 hours	2 hours	1 hour
BIBI	200 batches	1 hour	2 hours	3 hours
CHEMA	400 batches	½ hour	1 hour	2 hours
Total capacity available in a process		1,250 hours	1,120 hours	2,000 hours

Information about the throughput margin is that ATUPE will generate Tshs.6,600,000, BIBI will generate Tshs.2,200,000 and CHEMA will generate Tshs.2,300,000.

To begin with, our Company needs to identify a process whose capacity will limit production to a least level. I have prepared **Table 2** below for this purpose".

Table 2: Establishing the bottleneck

PRODUCT	OUTPUT BATCHES	HOURS REQUIRED BY OUTPUT		
		PROCESS 1	PROCESS 2	PROCESS 3
ATUPE	300	2 x 300 = 600	2 x 300 = 600	1 x 300 = 300
BIBI	200	1 x 200 = 200	2 x 200 = 400	3 x 200 = 600
CHEMA	400	½ x 400 = 200	1 x 400 = 400	2 x 400 = 800
TOTAL		1,000	1,400	1,700
The process load factor ➡		$\frac{1,000}{1,250} = 0.8$	$\frac{1,400}{1,120} = 1.25$	$\frac{1,700}{2,000} = 0.85$

At this stage, the Management Accountant collapsed and he was rushed to hospital. Immediately after this event, the General Manager appointed you to take over from him and continue to do the illustrations:

REQUIRED:

In the course of fulfilling General Manager's directives, present a production plan that will exploit the bottlenecks identified by the Management Accountant. Support your answers with brief explanations. **(20 marks)**

QUESTION 3

The Information Technology division (IT) of the JR Business Consulting Group provides consulting services to its clients as well as to other divisions within the group. Consultants always work in teams of two on every consulting day. Each consulting day is charged to external clients at Tshs.750,000 which represents cost plus 150% profit mark up. The total cost per consulting day has been estimated as being 80% variable and 20% fixed.

The Director of the Human Resources (HR) division of JR Business Consulting Group has requested the services of two teams of consultants from the IT division on five days per week for a period of 48 weeks, and has suggested that she meets with the Director of the IT division in order to negotiate a transfer price. The Director of the IT division has responded by stating that he is aware of the limitations of using negotiated transfer prices and intends to charge the HR division Tshs.750,000 per consulting day. The IT division always uses 'state of the art' video-conferencing equipment on all internal consultations which would reduce the variable costs by Tshs.50,000 per consulting day. This equipment can only be used when providing internal consultations.

REQUIRED:

(a) Calculate and discuss the transfer prices per consulting day at which the IT division should provide consulting services to the HR division in order to ensure that the profit of the JR Business Consulting Group is maximized in each of the following situations:

(i) Every pair of consultants in the IT division is 100% utilized during the required 48 week period in providing consulting services to external clients, i.e. there is no spare capacity. **(4 marks)**

(ii) There is one team of consultants who, being free from other commitments, would be available to undertake the provision of services to the HR division during the required 48 week period. All other teams of consultants would be 100% utilized in providing consulting services to external clients. **(4 marks)**

(iii) A major client has offered to pay the IT division Tshs.264,000,000 for the services of two teams of consultants during the required 48 week period. **(4 marks)**

(b) Briefly discuss **FOUR** limitations of negotiated transfer prices. **(8 marks)**

(Total : 20 marks)

QUESTION 4

Mohamed Ltd manufactures special meat pies, which it sells in bulk to delicatessen shops. The only variable cost is raw materials, which consists of three types of raw meat. The standard cost of the raw materials used in the manufacture of each 100 kilograms of special meat pie is as follows:

Raw Material	**Kilograms**	**Standard Price per Kilogram in Tshs.**
Type A	25	2
Type B	60	3
Type C	40	4
Total Input	**125**	
Normal Loss (20% of Input)	(25)	
Output	**100**	

In preparing its budget for 2014, the company assumed that there would be a market in Tanzania for 125,000 kilograms of special meat pie and that Mohamed's product would have a 40% share of this market. The budget also assumed a selling price of Tshs.6 per kilogram for Company's product. However, during 2014 both Mohamed and its competitors were adversely affected by diminishing consumer confidence in meat products. The actual total market size was only 110,000 kilograms of special meat pie (instead of the anticipated 125,000 kilograms), and Mohamed sold only 33,000 kilograms of its product.

The Managing Director of the company recently explained how his company attempted to respond to the difficulties which it faced in 2014: "First, we reduced our selling price from Tshs.6 to Tshs.5.90. This was a modest price reduction in comparison with those of our smaller competitors. Second, we took advantage of falling market prices for some of the types of meat which we use as raw material for our product. With benefit of hindsight, we should perhaps have done more to increase consumers 'confidence in the safety and quality of meat products in general and our own product in particular".

The actual raw materials used by Mohamed Ltd in 2014 were as follows:

Raw Material	**Kilograms**	**Actual Price per Kilogram Tshs.**
Type A	8,800	Tshs.1.7
Type B	19,200	Tshs.3
Type C	12,000	Tshs.4
Total Input	40,000	

The company had no opening or closing stocks of raw materials or finished product.

REQUIRED:

Calculate:

(a) Raw materials price; raw materials mix and raw materials yield variances. **(12 marks)**

(b) Sales Price and Sales Volume Variances. **(8 marks)**
(Total : 20 marks)

QUESTION 5

(a) DW, a transport company, operates three depots. Each depot has a manager who reports directly to the Operations Director. For many years the depot managers have been asked by the Operations Director to prepare a budget for their depot as part of the company's annual budgets process. A new depot manager has been appointed to the Southern region and he has concerns about the validity of these annual budgets. He argues that the annual budgets will soon become out of date as operational circumstances change. At a recent manager's meeting he said, "The annual budgets are restrictive. They do not permit the depot managers to make decisions in response to operational changes, or change in working practices for next year until that year's budget has been approved".

REQUIRED:

(i) Explain the differences between the above annual budgeting system and a rolling budget system. **(4 marks)**

(ii) Discuss how the Southern region depot Manager could use a rolling budget system to address his concerns. **(6 marks)**

(b) XY provides accountancy services and has three different categories of client: limited companies, self employed individuals and employed individuals requiring taxation advice.

XY currently charges its clients fees by adding a 20% mark-up to total costs. Currently the costs are attributed to each client based on the hours spent on preparing accounts and providing advice.

XY is considering changing to an activity based costing system.

The annual costs and the causes of these costs have been analysed as follows:

	Tshs.'000'
Accounting preparation and advice	580,000
Requesting missing information	30,000
Issuing fee payment reminders	15,000
Holding client meetings	60,000
Travelling to meet clients	40,000

The following details relate to three of XY's clients and to XY as a whole:

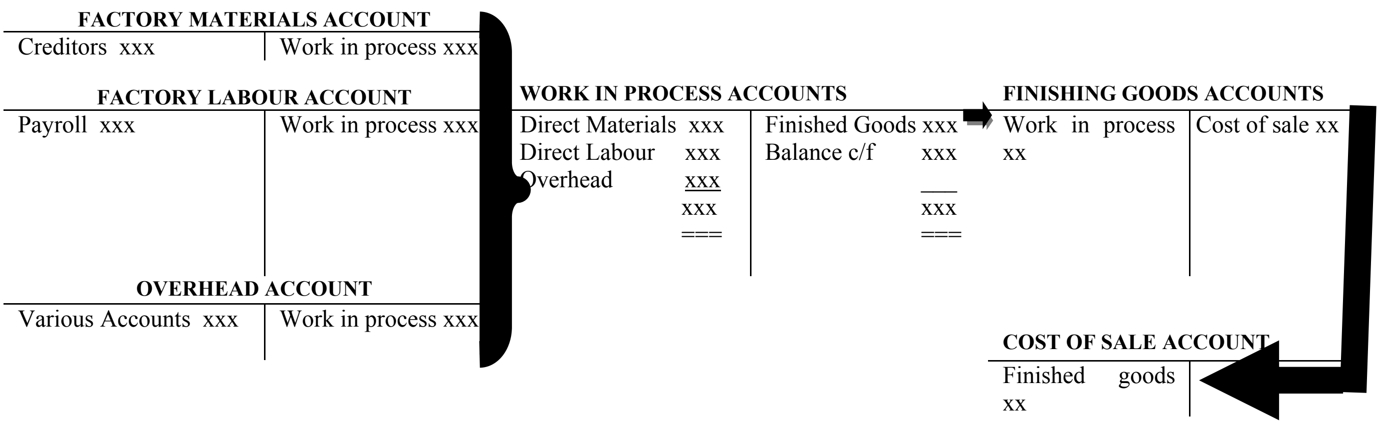
	Client			XY
	A	B	C	
Hours spent on preparing accounts and providing advice	1,000	250	340	18,000
Requests for missing information	4	10	6	250
Payment reminders sent	2	8	10	400
Client meetings held	4	1	2	250
Kilometres travelled to meet clients	150	600	0	10,000

REQUIRED:
Make calculations to show the effect of changing to the new costing system on fees charged to each of these three clients. **(10 marks)**

(Total : 20 marks)

QUESTION 6

(a) The traditional inventory costing tracks factory costs to cost of sale is as indicated below:



In order to scale down the accounting routines that are associated with stocks costing in a traditional way indicated by the diagram, a manufacturing business may use a simplified product costing method called "back-flush costing".

REQUIRED:

(a) What do you think justifies the business to use a traditional procedure to track inventory costs to finished goods and cost of sale? **(4 marks)**

(b) In which circumstances will the business use back flush costing? Discuss this with reference to Just-in-Time manufacturing and batch costing that it entails. **(6 marks)**

(b) Evaluations of profit centres based on Return on Investment and Residual Income are intended to establish if the segments were able to earn sufficient return to investors.

REQUIRED:

Indicate how and why Economic Value Added (EVA) deviates from the two performance evaluations mentioned above. **(10 marks)**

(Total : 20 marks)

QUESTION 7

ABC Ltd is in the business of publishing, printing and distributing a range of catalogues and other manuals. The management have now decided to discontinue printing and distributing the products and concentrate solely on publishing. Instead of ABC Ltd, XYZ Ltd shall now print and distribute the range of catalogues and other manuals. This shall be done on behalf of ABC Ltd under a contract that will commence either on 30th June 2015 or 30th November 2015 in which XYZ Ltd will receive Tshs.65,000,000 per month.

The results of ABC Ltd for a typical month are as follows:

	Publishing	**Printing**	**Distribution**
	Tshs.'000'	**Tshs.'000'**	**Tshs.'000'**
Salaries and wages	28,000	18,000	4,000
Materials and supplies	5,500	31,000	1,100
Occupancy costs	7,000	8,500	1,200
Depreciation	800	4,200	700

Information related to the possible closure proposals is as follows:

(i) Two specialist staff from printing will be retained at their present salary of Tshs.1,500,000 each per month in order to fulfil a link function with XYZ Ltd. One further staff member will be transferred to publishing to fill a staff vacancy through staff turnover, anticipated in July. This staff member will be paid at his present salary of Tshs.1,400,000 per month which is Tshs.100,000 more than that of the staff member who is expected to leave. On closure all other printing and distribution staff will be made redundant and paid an average of two months redundancy pay.

(ii) The printing department has a supply of materials (already paid for) which cost Tshs.18,000,000 and which will be sold to XYZ Ltd. for Tshs.10,000,000 if closure takes place on 30th June, 2015. Otherwise the material will be used as part of the July 2015 printing requirements. The distribution department has a contract to purchase pallets at a cost of Tshs.5,000,000 per month for July and August, 2015. A cancellation clause allows for non-delivery of the pallets for July and August for a one-off payment of Tshs.300,000. Non-delivery of the pallets for August only will require a payment of Tshs.100,000. If the pallets are taken from the supplier, XYZ Ltd has agreed to purchase them at a price of Tshs.380,000 for each month's supply which is available. Pallet costs are included in the distribution material and supplies cost stated for a typical month.

(iii) Company expenditure on apportioned occupancy costs to printing and distribution will be reduced by 15% per month if printing and distribution departments are closed. At present, 30% of printing and 25% of distribution occupancy costs are directly attributable costs which are avoidable on closure, whilst the remainder are apportioned costs.

(iv) Closure of the printing and distribution departments will make it possible to sub-let part of the building for a monthly fee of Tshs.2,500,000 when space is available

(v) Printing plant and machinery has an estimated Net Book Value of Tshs.48,000,000 at 30th June 2015. It is anticipated that it will be sold at a loss of Tshs.21,000,000 on 30th June 2015. If sold on 30th November 2015, the prospective buyer will pay Tshs.25,000,000.

(vi) The Net Book Value of distribution vehicles at 30th June, 2015 is estimated at Tshs.80,000,000. They could be sold to the original supplier at Tshs.48,000,000 on 30th June, 2015. The original supplier would purchase the vehicles on 30th November 2015 for a price of Tshs.44,000,000.

REQUIRED:

Using the above information, prepare a summary to show whether ABC Ltd. should close the printing and distribution departments on financial grounds on 30th June, 2015 or 30th November 2015. Explanatory notes and calculations should be shown. Ignore taxation. **(20 marks)**

EXAMINATION	**:**	**INTERMEDIATE LEVEL**
SUBJECT	**:**	**MANAGEMENT, GOVERNANCE AND ETHICS**
CODE	**:**	**B6**
EXAMINATION DATE	**:**	**FRIDAY, 8TH MAY, 2015**
TIME ALLOWED	**:**	**THREE HOURS (2:00 P.M. – 5:00 P.M.)**

GENERAL INSTRUCTIONS

6. There are **TWO** Sections in this paper. Section **A** and **B** which comprise **SEVEN** questions.

2. Answer question **ONE** in Section **A.**

3. Answer **ANY FOUR** questions in Section **B**.

4. In total answer **FIVE** questions.

5. Marks are shown at the end of each question.

6. This question paper comprises **5** printed pages.

SECTION A
Compulsory Question

QUESTION 1

(c) Assume you are a consultant specialized on strategic management field. You have been invited by TAMECO Ltd which is a newly established company expecting to deal with training on strategic management issues. You have been asked to prepare a presentation to the management about the issue of vision and mission of the organization.

REQUIRED:

(i) Explain how you would define the terms "Vision and Mission" in your presentation. **(4 marks)**

(ii) Assist TAMECO Ltd to formulate a vision statement of the organisation. **(3 marks)**

(d) Analysing business's external environment is one of the major challenges facing managers in organisations.

REQUIRED:

Explain the impact of the following external environment factors to an organisation's business strategy: (Choose any four)

(i) Economic

(ii) Market competition

(iii) Technology

(iv) Climate change

(v) Legal

(vi) Media

(vii) Political

(viii) Demographic

(8 marks)

(e) One of the major challenges facing business organisations is the power to compete. Inability to face market competitions results into organisation's failure to perform hence business closedown.

REQUIRED:

By referring to Michael Porter Strategic Management Model, known as the five forces of competition, explain the five competitive forces which must be analysed when evaluating a business's profitability in the future. **(5 marks)**

(Total : 20 marks)

SECTION B

There are **SIX** questions in this section. Answer **ANY FOUR** questions

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QUESTION 2

(a) Budgeting is one of the main functions of management, without it both long and short term operations of an organisation may be paralysed.

REQUIRED:

(i) Account for the advantages of budgeting process. **(5 marks)**

(ii) Elucidate the limitations of budgeting. **(5 marks)**

(b) One of the challenges facing managers in many organisations is how to allocate an appropriate number of subordinates under a supervisor.

REQUIRED:

Explain at least five factors to consider when deciding how many number of employees should be allocated under a supervisor's span of control. **(10 marks)**

(Total : 20 marks)

QUESTION 3

(a) Mr. Keto Bill and Mr. Clinton Sebbo were two businessmen. They decided to borrow money from the bank in order to increase their capital. They borrowed the same amount for that purpose. After acquiring the loans Mr. Bill decided to re-think about his decision of increasing capital for the existing business. Instead of increasing capital for the existing business he decided to open a new business. As a result he had two business companies running simultaneously and both were doing well. On the other side Mr. Sebbo's business did not expand as he was expecting and as a result he failed to pay back the loan hence declared bankrupt.

REQUIRED:

Identify and analyse at least five benefits for diversification of businesses.

(10 marks)

(b) Although the concept of Corporate Social Responsibility (CSR) is widely accepted by businessmen and other stakeholders, there are those who oppose it by giving various excuses and reasons.

REQUIRED:

(a) Explain at least five reasons to support CSR. **(5 marks)**

(b) Explain at least five reasons that oppose CSR. **(5 marks)**
(Total : 20 marks)

QUESTION 4

(a) Trading through electronic method is rapidly increasing. Research has shown that the world is now changing from face to face trading to e-business.

REQUIRED:

(d) Explain any five advantages of e-commerce. **(5 marks)**

(e) Explain any five limitations of e-business. **(5 marks)**

(b) In order to perform effectively, a manager of a business company must make a good use of information which is obtained from various sources.

REQUIRED:

Enumerate any five sources of internal information. **(10 marks)**
(Total : 20 marks)

QUESTION 5

(a) Suppose you have been employed in a newly established business company as a Risk Manager. You would like to demonstrate to senior management that you know well your responsibilities as a Risk Manager.

REQUIRED:

Enumerate eight functions of a Risk Manager. **(12 marks)**

(b) Experience shows that most managers do not put emphasize on the importance of having a succession plan in their organisations. They look at succession plan as something that is voluntary.

REQUIRED:

Discuss the advantages and disadvantages of a succession plan in an organization.

(8 marks)
(Total : 20 marks)

QUESTION 6

(c) One of the major functions of a manager in an organization is to promote ethical conduct among employees.

REQUIRED:

Amplify various strategies that can be used by a manager to promote ethical conducts at a workplace. **(10 marks)**

(d) Accountants like any other professionals are required to possess certain competencies in order to carry out their responsibilities efficiently.

REQUIRED:

Narrate various competencies required for an accountant to work effectively.

(10 marks)
(Total : 20 marks)

QUESTION 7

(c) Suppose you attend one of the professional debate forums and hear one of the presenters who was a manager in a public corporation saying "Formulation of policies is a wastage of time and resources, an organization can go without policies. What matters is an integrity of the staff in a particular organization". As a professional accountant you have decided to oppose by arguing against what he said.

REQUIRED:

Analyse five importances of policies in an organization. **(5 marks)**

(d) Major corruption scandals have now been the order of the day in many developing countries including Tanzania. Funny enough major corruption scandals involve those who are called "untouchables" thus they seem to be above the laws. There are many complaints against the organs that are responsible to combat corruption that they deal only with petty corruptions and sideline the major ones.

REQUIRED:

Enumerate five measures to combat grand corruption in Tanzania. **(5 marks)**

(e) Write brief notes on the following terms as used in corporate governance and ethics.

(i) Reputational risk

(ii) Due deligency.

(c) Ethical theory of absolutism

(d) Deontologist ethics

(10 marks)
(Total : 20 marks)

SUGGESTED SOLUTIONS
BI – FINANCIAL MANAGEMENT
MAY 2015

ANSWER 1

(a) Safari Company's Equity risk Premium and the Cost of Equity using the CAPM.

- Equity risk Premium
  Equity Risk Premium = $\left(\overline{R}_m - R_f\right)\beta_e$
  $= \left(12\% - 5\%\right)1.5 = 10.5\%$
- Cost of Equity

  $k_e \quad = R_f + \left(\overline{R}_m - R_f\right)\beta_e$
  = 5% + (12% - 5%)1.5 = 15.5%

(b) The market value weighted average cost of capital of Safari Company.

(i) Market Value WACC using the dividend growth model

Cost of Equity (k_e)

$$k_e = \frac{D_o\left(1+g\right)}{P_o} + g$$

D_o = Total Dividend Paid/Number of Ordinary Shares in Issue
+TZS4,000,000/2,000,000 = TZS2 per share

P_o = Market Price per Share cum dividend – Dividend per Share
= TZS50 – TZS2 = TZS48

g = 6%

Thus $k_e = \frac{D_o\left(1+g\right)}{P_o} + g$ = k_e = $\frac{TZS\,2(1.06)}{TZS\,48} + 0.06 = 10.4\%$

Cost of Irredeemable Debt (k_i)

$K_d = I/P_o$ = [10% x TZS1,000]/(1.05 X tzs1,000) = TZS100/TZS1050 = 9.52%

Thus the after tax cost of debt, k_i = kd(1 – T)
=9.52% (1 – 0.35) = 6.2%

Cost of Non-Callable Preferred Stock (k_p)

$K_p = D_p/P_o$ = (5% x TZS100)/TZS43 = 5/43 = 11.6%

The WACC

Market Value of Equity = TZS48 x 2,000,000 shares = TZS96 million
Market Value of =TZS1,050 x 20,000 bonds = TZS21 million
Market Value of Preferred Stock =TZS43 x 1,000,000 shares = TZS43 million

Equity proportion = 96/160 = 0.6
Debt proportion = 21/160 = 0.13
Preferred stock proportion = 43/160 = 0.27

WACC = (0.6)(10.4%) + (0.13)(6.2%) + (0.27)(11.6%) = 10.18%

(ii) **Market Value WAC using the Capital Asset Pricing Model**

Cost of Equity

$$k_e = R_f + \left(\overline{R}_m - R_f\right)\beta_e$$
$$= 5\% + (12\% - 5\%)1.5 = 15.5\%$$

After Tax of Debt
K_i = 11.6%

Thus the WACC = (0.6)(15.5%) + (0.13)(6.2%) + (0.27)(11.6%) = 13.23%

(c) The Dividend Growth Model vs. CAPM

Dividend growth model
There are a number of problems with the dividend growth model. It uses a set of figures which assumes that dividends grow smoothly. In reality, dividends change according to decisions made by managers who do not necessarily repeat historical trends. It is therefore very difficult to accurately predict the future dividend growth rate. The other main problem is how to incorporate risk. The dividend growth model does not explicitly consider risk, particularly business risk. The company may change its area of business operations and the economic environment is notoriously uncertain. The share price will however fall as risk increases, leading to an increased cost of equity. The model also ignores the effects of taxation and assumes there are no issue costs for new shares.

Capital asset pricing model
The main advantage that the CAPM has over the dividend valuation model is that it does explicit consider risk. The CAPM is based on a comparison of the systematic risks of individual investments with the risks of all shares in the market. Systematic risk is risk that cannot be diversified away and an investor will require a higher return to compensate for higher risk. This higher return is

the higher cost of equity that is calculated using the CAPM formula. The formula does however require estimates to be made of excess return, the risk-free rate and beta values. All of these can be difficult to estimate, but are more reliable than the dividend growth rate used in the dividend valuation model.

Conclusion

The CAPM does explicitly consider risk and uses estimated values that are more reliable than those used in the dividend valuation model. It can therefore be said that CAPM offers the better estimate of the cost of equity of a company.

(d) Circumstances under which WACC can be used in Investment Appraisal

The Weighted average cost of capital is the average cost of the company's finance and represents the average return required as compensation for the risks of the investment.

Business risk

The WACC can only be used if the business risk of the proposed investment is similar to the business risk of existing operations. This would involve the expansion of existing business. If the proposed investment is in a different type of business, a project-specific cost of capital should be used which reflects the changing risk. The technique to use involves changing the beta in the capital asset pricing model.

Financial risk

The WACC can only be used where the existing capital structure will be maintained. This means that the finance for the project will be raised in the same proportions as the existing finance.

Size of the project

The WACC can only be used if the project being appraised is small relative to the company. If the project is large in scale, it is more likely to cause in risk and make the WACC inappropriate.

ANSWER 2

(a) MABRUK COMPANY

Project NPV and Sensitivity Analysis (TZS Millions)

Project NPV

End of Year	0	1	2	3	4	5
Initial Cash Inv.	(35)	-	-	-	-	-
Sales Revenue	-	42	42	42	42	42
Variable Costs	-	(23)	(23)	(23)	(23)	(23)
Fixed Costs	-	(7)	(7)	(7)	(7)	(7)
Net Cash Flow	(35)	12	12	12	12	12
Discount Factor (at 12%)	1	0.893	0.797	0.712	0.636	0.567
Present Value	(35)	10.7	9.6	8.5	7.6	6.8

NPV = TZS [10.7 + 9.6 + 8.5 + 7.6 + 6.8] – 35
=TZS8.2 million

Sensitivity of Project NPV

(i) Sensitivity of Sales Revenue
For the NPV to equal zero sales revenue must fall by 5.4%, namely by:
NPV/PV of Sales Revenue = TZS8.2 million/TZS42(3.605). The project will cease to be economically viable if sales revenue fall by more than 5.4%.

(ii) Sensitivity to Sales Price
If sales revenue must fall by 5.4%, selling price must fall by TZS2,100 x 5.4% = TZS113.40. Should the selling price fall by more than TZS113.40 the project will stop to be economically viable.

(iii) Sensitivity to Sales Volume
Since sales volume affects the level of contribution, the change in the contribution must be calculated first.

Required Decrease in Contribution =NPV/PV of Contribution
=TZS8.2m/(TZS19)(3.605) = 11.97%
Thus the required decrease in sales volume will be 11.97% x 20,000 = 2,394 units

(iv) Sensitivity to Variable cost
For the NPV to equal zero variable cost must increase by 9.9%, namely by:
NPV/PV of Variable Cost = TZS8.2 million/TZS23(3.605) = 9.9%

(b) TWIGA PLC

Portfolio 1 Solution

Investment	Investment weightings	Expected return (%)	Portfolio expected return (%)	Beta	Weighted beta
a	0.1	20	2.00	0.7	.07
b	0.4	22	8.80	1.2	.48
c	0.3	24	7.20	1.3	.39
d	0.2	26	5.20	1.4	.28
			23.20		1.22

The required return: 5 + (15 – 5) 1.22 = 17.20%

Portfolio 2 Solution

Investment	Investment weightings	Expected return (%)	Portfolio expected return (%)	Beta	weighted beta
a	0.2	18	3.60	0.8	.16
b	0.4	20	8.00	1.1	.44
c	0.2	22	4.40	1.2	.24
d	0.2	16	3.20	1.4	.28
			19.20		1.12

The required return: 5 + (15 – 5) 1.12 = 16.20%

Alpha table

	Expected returns	Required returns	Alpha values
Portfolio 1	23.20%	17.20%	6.00%
Portfolio 2	19.20%	16.20%	3.00%

Portfolio 1 is chosen because it has the largest positive alpha.

Portfolio theory calculations

The formula for a multi-asset portfolio with no correlation between the returns is:

$$\sigma \text{port(A,B)} = \sqrt{\sigma_a = x_a = + \sigma_b = x_b = \sigma_c = x_c = + \sigma_d = x_d =}$$

$$\sqrt{w_1^2\sigma_a^2 + w_2^2\sigma_b^2 + w_3^2\sigma_c^2 + w_4^2\sigma_d^2}$$

Portfolio 1

σ port 1 = $\sqrt{8 = .1 = +10 = .4 = +11 = .3 = +9 = 2}$ –

= 5.55%

Portfolio 2

σ port 2 = $\sqrt{7 = .2 = +9 + .4 = +12 = .2 = +13 = .2}$

= 5.24%

Summary table

	Expected returns	portfolio risk
Portfolio 1	23.20%	5.55%
Portfolio 2	19.20%	5.24%

The portfolio with the highest return also has the highest level of risk. Therefore, neither portfolio can be said to be more efficient than the other. An objective answer cannot be reached. As the company is making decisions on behalf of its shareholders the correct way to evaluate the investments is by looking at the effect they have on a shareholders existing/enlarged portfolios.

ANSWER 3

(a) Approach: Calculate the Equivalent Annual Costs for each possible replacement cycle and select the replacement cycle with the least EAC

EAC = PV of Cost for One Replacement Cycle/Cumulative PV Factor for the No. of Years in the cycle

One Year Replacement Cycle

Year	Cash Flow	TZS ‘000’	Discount Factor (at 10%)	PV TZS ‘000’
0	Car Cost	(22,000)	1	(22,000)
1	Resale Value	14,000	0.909	12,726
				(9,274)

EAC = TZS(9,274)/0.909 = TZS(10,202.42)

Two Year Replacement Cycle

Year	Cash Flow	TZS '000'	Discount Factor (at 10%)	PV TZS '000'
0	Car Cost	(22,000)	1	(22,000)
1	Running Costs	13,200	0.909	(11,998.8)
2	Resale Value	8,400	0.826	6,938.40
				(27,060.4)

EAC = TZS(27,060.4)/1.735 = TZS(15,596.77)

Three Year Replacement Cycle

Year	Cash Flow	TZS '000'	Discount Factor (at 10%)	PV TZS '000'
0	Car Cost	(22,000)	1	(22,000)
1	Running Costs	13,200	0.909	(11,998.8)
2	Running Costs	15,200	0.826	(12,555.20)
3	Resale Value	3,600	0.751	2,703.60
				(43,850.40)

EAC = TZS(43,850.40)/2.486 = TZS(17,638.94)

Advice
The One Year Replacement cycle produces the lowest EAC and should therefore be chosen as optimal replacement cycle.

(b) KORONGO MBAKA

(i) On a purely subjective basis, annuity Y looks more attractive than annuity X because it provides Tshs. 1,000 more each year than annuity X. of course, the fact that X is an annuity due means that the Tshs. 9,000 would be received at the beginning of the first year, unlike the Tshs. 10,000 at the end of the year, and this makes annuity X awfully tempting.

(ii) Annuity X:
FVA_6 = Tshs. 9,000 * $FVIFA_{15\%,\ 6\ YEARS}$ *(1 + 0.15)
= Tshs. 9,000*8.754*1.15
= Tshs. 90,603.90

Annuity Y:
FVA_6 = Tshs. 10,000 * $FVIFA_{15\%\ 6\ years}$
= Tshs. 10,000 * 8.754
= Tshs. 87,540.00

(iii) Annuity X is more attractive because its future value at the end of year 6, FVA6, of Tshs. 90,603.90 is greater than annuity Y's end of the year 6 future value, FVA6, of Tshs. 87,540.00. The subjective assessment in part (a) was incorrect. The benefit of receiving annuity X's cash flows at the beginning of each year appears to have outweighed the fact that annuity Y's annual cash inflow, which occurs at the end of each year, is Tshs. 10,000 larger (Tshs. 10,000 vs. Tshs. 9,000) than annuity X's.

ANSWER 4

Project Evaluation and Selection: The CAPM
Approach: Compare the project expected return with the Required Return on the project calculated using the CAPM

Project 1: MWANZA POUTRY
Project 1: Analysis

State	Pi	R_{MZ}	$R_{MZ}Pi$	$R_{MZ} - E[R_{MZ}]$	$[[R_{MZ} - E[R_{MZ}]]]^2 Pi$
Rainy	0.4	10	4	-4	6.4
Sunny	0.4	20	8	6	14.4
Cloudy	0.2	10	2	-4	3.2
		E(R_{MZ})=	14		Var (MZ)=24

Market: Analysis

State	Pi	R_M	$R_M Pi$	$(R_M - E[R_M]Pi)^2$	$([R_{MZ} - E[R_M)(R_{MZ} - E[R_M]Pi)$
Rainy	0.4	30	12	57.6	-19.2
Sunny	0.4	20	8	1.6	4.8
Cloudy	0.2	-10	-2	156.8	22.4
			E(R_M)=18	216	Cov (MZ,M)=8

Thus: β_{MZ} =8/216 = 0.037

Required Return

R_{MZ} $= R_f + \left(\overline{R}_m - R_f\right)\beta_e$

=9% + (18% - 9%)0.037 = 9.33%

Expected Return 14%

Thus Net Return = 14% - 9.33% = 4.67%

PROJECT II: ARUSHA MINING

Project I: Analysis

State	Pi	R_{AR}	$R_{AR}Pi$	$R_{AR} - E[R_{AR}]$	$[[R_{AR} - E[R_{AR}]]^2 Pi$
Rainy	0.4	15	6	2	1.6
Sunny	0.4	20	8	7	19.6
Cloudy	0.2	-5	-1	-18	64.8
		E(R_{AR})=	13		Var (AR)=86

Market: Analysis

State	Pi	R_M	$R_M Pi$	$(R_M - E[R_M]Pi)^2$	$([R_{AR} - E[R_{AR})(R_M - E[R_M]Pi)$
Rainy	0.4	30	12	57.6	-19.2
Sunny	0.4	20	8	1.6	4.8
Cloudy	0.2	-10	-2	156.8	22.4
			E(R_M)=18	216	Cov (AR,M)=-85.6

Thus: $\beta_{AR} = -85.6/216 = -0.4$

Required Return

$R_{MZ} = R_f + \left(\overline{R}_m - R_f\right)\beta_e$

$=9\% + (18\% - 9\%)(-0.4) = 5.4\%$

Expected Return = 13%

Thus Net Return = 13% - 5.4% = 7.6%

Arusha Mining has the higher net return. Invest in Project II: Arusha Mining

ANSWER 5

BENBERA ENTERPRISE

(a) Evaluation of the Performance of Benbera Enterprise

(i) Net Profit Margin

The Net Profit Margin is one of the indicators of profitability. The Net Profit Margin is given by: Net Profit Margin = Net Profit/Revenue

Current Year: Net Profit Margin = TZS8,800/TZS74,500 = 11.8%

Previous Year: Net Profit Margin = TZS7,900/tzs68,000 = 11.6%

The company has slightly grown in terms of profit with an increase by 0.2 in Net Profit Margin (from 11.6% in the previous year to 11.8% in the current year. The slight increase in profitability may be attributable to the increase in net revenue by about 9%)

(ii) Return on Equity

Return on Equity (ROE) is another measure of profitability. It is given by: Net Profit/Equity.

Current Year: ROE = TZS8,800/39,900 = 22.1%

Previous Year: ROE = TZS7,900/35,100 = 22.5%

The return on equity has slightly declined, indicating a deterioration in return on investment of the common shareholders of the firm.

(iii) Debt/Equity Ratio

This ratio is a good indicator of the financial risk level of the firm. It is given by:

Gearing Ratio = Debt/Equity

Current Year: Debt/Equity Ratio = TZS14,000/TZS39,900 = 35.1%

Previous Year: Debt/Equity Ratio = TZS17,500/TZS35,100 = 49.9%

The gearing ratio has declined from 49.9% to 35.1% indicating that the financial risk that the shareholders are exposed to does not appear to be a problem area. The company may want to consider increasing gearing to invest in suitable projects and generate further growth.

(iv) P/E Ratio

The P/E Ratio reflects the market's appraisal of the share's future prospects and this has improved. It is still lower than the industry average which suggests that more growth could be achieved.

(b) Comment on the argument that accounting profits may not be the best measure of a company's performance.

Accounting profits may not be the best measure of a company's performance due to the following reasons:

Manipulation
Accounting profits can be manipulated to some extent by choices of accounting policies. For example, the depreciation amount will depend on the basis of calculation of depreciation and development costs can be capitalized instead of being written off to the income statement.

Risk
Profit does not take account of risk. Shareholders will be very interested in the level of risk, and maximizing profits may be achieved by increasing risk to unacceptable levels.

Volume of investment
Profits on their own take no account of the volume of investment that it has taken to earn the profit. Profits must be related to the volume of investment to have any real meaning.

Short-term performance
Profits are reported every year (with half-year interim results for quoted companies). They are measures of short-term historic performance, whereas a company's performance should ideally be judged over a longer term and future prospects considered as well as past profits.

ANSWER 6

(a) **Evaluate of Change in Credit Policy: UMOJA COMPANY**

Current average collection period: 30 + 10 = 40 days

Current Accounts Receivable: TZS 120m x 40/365 = TZS13,150,685
Av. Collection period under new policy = [30% x 15 days + (70% x 60 days)] = 46.5 days

New level of credit sales = TZS120m (1.1) = TZS132 million
Account receivable after policy change = TZS132m x 46.5/365 = TZS16,816,438.4

Increase in financing cost = (TZS16,816,438.4 – tzs13,150,685) x 7% = TZS256,602.7

Increase in financing costs	TZS256,602.7
Incremental Costs (1% x TZS132m)	TZS1,320,000
Cost of Discount (30% x TZS132m x 2%	TZS792,000
Increase in Cost	TZS2,368,602.7
Contribution from increased sales (TZS120m x 10% x 60%)	TZS7,200,000
NET BENEFIT FROM POLICY CHANGE	TSHS4,481,397.3

Thus the proposed policy will increase the profitability of Umoja Co.

Advice on the key factors to be considered when formulating a working capital funding policy

In order to understand working capital financing decisions, assets can be divided into three different types:

Non-current (fixed) assets: are long term assets from which an organization expects to derive benefit over a number of periods. For example, buildings or machinery.

Permanent current assets: are the amount required to meet long term minimum needs and sustain normal trading activity, for example inventory and average level of accounts receivable.

Fluctuating current assets: are the current assets which vary according to normal business activity. For instance due to seasonal variations.

Funding Alternatives:

Short term sources of funding are usually cheaper and more flexible than long term ones. There are three principle approaches to financing working capital:

- *Matching principle:* This is a policy of maturity matching in which long term funds finance permanent assets while short term funds finance non-permanent assets.

- *Conservative approach:* This involves all noncurrent assets and permanent current assets, as well as part of the fluctuating current assets being financed by long term financing.

- *Aggressive approach:* In this policy not only are fluctuating current assets all financed out of short term sources but so are some of the permanent current assets.

(b) **SHILO DESIGNS COMPANY**

(i) Calculating the Price for share

The relationship between dividend and market value of a share according to Walter is given as:

$$P = \frac{D + \frac{r}{k_e}(E - D)}{k_e}$$

(1 mark)

Where,

P = market price of share
D = dividend per share
E = earnings per share
r = rate of return on firm's investment
k_e = cost equity

- Dividend per share = Dividend pay-out/number of shares
  = Tshs375 million / 20 million shares
  = 18.75 per share

- Earnings per share = Earnings / number of shares
  = Tshs500 m / 20 m
  = Tshs25 per share

- Return on investment = Earnings/capital employed
  = Tshs500m / Tshs5000 m
  = 10%

- Cost of equity = EPS/MPS
  = 1/(MPS/EPS)
  = 1/(P/E ratio)
  = 1/11.5
  = 8.69%

Applying Walter's model

$$P = \frac{18.75 + \frac{0.1}{0.0869}(25 - 18.75)}{0.0869}$$

$$P = \frac{18.75 + \frac{0.1}{0.0869}(6.25)}{0.0869}$$

$$= P = \frac{18.75 + 7.19}{0.0869}$$

$$= P = \frac{25.94}{0.0869}$$

= Tshs298.5

(ii) Since $r > k_e$, at 75% dividend pay-out, it is not optimal. A zero D/P ratio would be optimal considering current parameters:

$$\frac{D + \frac{r}{k_e}(E - D)}{k_e}$$

$$\frac{0 + \frac{0.1}{0.0869}(25 - 0)}{0.0869} = 28.77/0.0869 = \text{Tshs. } 331.05$$

ANSWER 7

(a) **Evaluation of the economic viability of the proposed investment project using the Net Present Value (NPV) Method.**

Project Evaluation (Millions of TZS)

	0	1	2	3	4	5
Initial Cash Inv.	(42)	-	-	-	-	
Sales Revenue	-	31	31	31	13	31
Less: Cost of Sales Distribution Costs Fixed Costs	- - -	(12.4) (3.1) (4.0)	(12.4) (3.1) (4.0)	(12.4) (3.1) (4.0)	(5.2) (1.3) (4.0)	(5.2) (1.3) (4.0)
Income before Tax Tax (at 35%)	- -	11.5 (4.025)	11.5 (4.025)	11.5 (4.025)	2.5 (0.875)	2.5 (0.875)
After Tax Net Cash Flow Discount Factor (at 5%)	(42) 1	7.475 0.95	7.475 0.91	7.475 0.86	1.625 0.82	1.625 0.78
Present Value	(42)	7.1	6.8	6.4	1.3	1.3

NPV = TZS million [7.1 + 6.8 + 6.4 + 1.3 + 1.3] – 42
= Tsh 19.1 million

Comment: Project has a negative NPV. It is therefore not economic viable and should be rejected.

(b) Project's Internal Rate of Return (IRR)

Trial and Error Method
At 5% discount rate: NPV = TSHS19.1 million
At 1%: NPV = (7.475)(2.283) + (1.625)(0.572) + (1.625)(0.497) – 42
= -TZS 1.3 million
No rate that can yield positive NPV to allow the trial and error method.

Approx. IRR = 5% + 2.9/[2.9 + 1.3](15%-5%) = 11.9%

Strengths and Weaknesses of the IRR in Appraising Capital Investments

Strengths of the IRR

1. It is a percentage which is more easily understood.
2. It considers the time value of money
3. It uses a cash flow not profit
4. Considers all cash flows over the life of a project
5. It is directly related to the objective of maximizing shareholders' wealth.

Weakness of IRR

1. It is not a measure of absolute probability
2. Interpolation only provide estimate accurate rate require use of spread sheet
3. Fairly complicated to calculate.
4. It cannot be used to appraise projects with non convention cash flows.

(c) **Return on Capital Employed (ARR) and the Payback Method.**

The ARR Method

= Average Net Income/Average Investment

Average Net Income = TZSm [7.475 + 7.475 + 7.475 + 1.625 + 1.625]/5 = TZS5.1m

ARR = TZS5.1m/TZS20m = 25.5%

$$\frac{5.135}{42} = 12.23\%$$

Comment: As the target return on capital employed (20%) is greater than the project average expected return (12.25%) the project is not economically viable using the ARR Method.

The Payback Period Method [TZS millions]

Year	Cash Flows	Cumulative Cash Flow
1	7.475	7.475
2	7.475	14.95
3	7.475	22.425
4	1.625	24.050
5	1.625	25.675

If the Io is 42 million, the cfs from year 1 to 5 cannot retain this amount.
Therefore, no PBP became the Io of 42 million cannot be recovered.
PBP = 2 + 5.05/7.475 = 2.67 Years
Comment: As the maximum acceptable Pay Back Period is 2 Years and the expected PBP (2.67 Years), the project is economically viable using the PBP Method.

(d) Discussion on the directors' View on Investment Appraisal (Evaluation using either payback or return on capital employed)

Payback and ROCE are inferior to discounted cash flow methods of investment appraisal. Payback ignores the timing of cash flows within the payback period, the cash flows after the end of payback period and therefore the total project return, and the time value of money. ROCE is based on accounting profit, which can be manipulated, instead of cash flows. ROCE should clarify why either method can be used to justify a project when then asses different characteristics and neither should be used solely to judge an investment opportunity.

The target values are both very subjective, for example why is a maximum payback period of two years important?

Discounted cash flow methods remove some of these problems by using either a weighted average cost of capital or a project-specific cost of capital to discount cash flows. Both of these approaches have an academic justification.

SUGGESTED SOLUTIONS
B2 - FINANCIAL ACCOUNTING
MAY 2015

ANSWER 1

Consolidated Statement of Financial Position as at 31 March 3015

	Tshs "000"	Tshs. "000"
Assets		
Non-current Assets		
Property, plant and equipment (47,400+25,500-2,500)(w6)		70400
Goodwill (W1)		8500
Investment in associate (W7)		3700
Financial asset: equity investments (7,100+3,900)		11000
Total		93600
Current Assets		
Inventory (17400+8400-600(W2)	25200	
Receivables (14,800+9000-900(W3)-2,800 inter company	20100	
Cash (2100+900 (W3)	3000	48300
Total Assets		**141900**
Equity and Liabilities		
Equity attributable for owners of KPP Ltd.		
Share capital (40000+6000(W1)		46000
Share premium (W1)		6000
Retained Earnings (W4)		34700
Total		86790
Non-Controlling Interest (W5)		8800
Non-current liabilities		
10% loan notes (8000+1500(W1)		9500
Current Liabilities		
Trade payables (17600+13000-2800 intercompany)	27800	
Overdraft	9100	36900
Total Equity and Liabilities		**141900**

Workings

W1: Goodwill		
	"000"Tshs	"000"Tshs
Consideration transferred		
Shares (20mil x 2/5 x 75% x 2 Tshs)		12,000
Loan notes (15 mil x 100/1000)		1,500
		13,500
Non-controlling interest (5mil x 1.2 Tshs)		6,000
		19,500

Net assets at acquisition		
Share capital	20,000	
Retained earnings (4000+2000)	(6,000)	
Fair Value adjustment(W6)	(3,000)	
		(11,000)
Goodwill		8,500

W2: Provision for Unrealized Profit

Intercompany sales in inventory 4.6 mil Tshs.

Inventory = 4.6 mil Tshs. 15/115 = **600,000 Tshs.**

W3: Intercompany cash in transit

Dr. Cash 900,000

Cr. Receivables 900,000

W4: Retained Earnings		
	KPP Ltd.	Pluto Ltd.
	“000”Tshs.	“000”Tshs.
Per draft	26,600	4,000
Add back pre acquisition loss		6,000
		10,000
Provision for Unrealized Profit	(600)	
Gain/loss on equity investment*	(400)	700
Movement on fair value adjustment (W6)		500
		11,200
Group share of Pluto Ltd. (75% x 11,200)	8,400	
Group share of RAC	700	
Group retained earnings	**34,700**	
*Loss on equity investments in KPP.(10,500 – 3,000 – 7100)= 400		

W5: Non-Controlling Interest		
	“000”Tshs.	“000”Tshs.
Fair value at acquisition (W1)		6,000
Share of post-acquisition retained earnings (11200(W4) x 25%		2,800
		8,800

W6: Movement on fair value adjustment			
	At acquisition	Movement	At year end
	"000"Tshs.	"000"Ths	
FVA on Plant (W1)	-3000	500	-2500

W7: Investment in RAC Ltd.		
	"000"Tshs.	"000"Tshs.
Cost of investment		3,000
Post-acquisition earnings (13.5 mil Tshs.-7.5 mil Tshs.)	6,000	
Add: dividend paid	2,000	
	8,000	
x 3/12	2,000	
x 35%		700
		3700

ANSWER 2

(a) IAS 1 set down a number of principle that govern the preparation and presentation of Financial Statements. These principles include Accruals, Going Concern, Materiality and Aggregation and consistency.

(i) Accruals

The accruals concept provides that income and expenditure should be recognized in the financial statements of the financial year to which they relate, rather than in the year in which they are paid. On this basis, for example, rent and other expenses owing at the year-end date should be included as expenses in the Income Statement for the year in question and as accruals/liabilities in the Statement of Financial Position, notwithstanding that the amounts involved may not be paid until the subsequent year. Likewise, amounts paid in the current year that relate to future financial periods should not be included as expenses in the current years Income statement but instead carried forward as prepayments in the Statement of Financial Position and expensed in future years as appropriate.

OR

- Means the effects of transactions and other events are recognized when they occur (and not as cash received or paid), and are recorded in the accounting records and reported in the financial statements of the period to which they relate.

- Financial Statements prepared under the accruals basis show user past transactions involving cash and also obligations pay to cash in the future and resources which represent cash to be received in future.

(ii) Going Concern

The "Going Concern" concept provides that readers of financial statements are entitled to assume unless it is explicitly stated otherwise, that the reporting entity will continue in business for the foreseeable future (i.e. at least the next twelve months) and that the financial statements in question have been prepared on this basis. If management intend to liquidate the entity or if there is no realistic alternative but to do so, then the financial statements should be prepared on a "break-up "basis. Where material uncertainties exist or cast doubt over the going concern assumption, then under IAS 1, these should be disclose in the financial statements.

(iii) Materiality

Information is material to the financial statements if its omission or misstatement could influence the economic decisions of users. Information can be material in terms of its size in relation to the financial statements as a whole or an item could be material by its nature. IAS 1 provides that each material class or similar items must be presented separately in the financial statements. Dissimilar items can only be aggregated if they are individually immaterial. For example, sales invoices are aggregated in the Income Statement and included as a line item. "Revenue". However revenue is not aggregated with expenditure.

(iv) Consistency

IAS 1 requires that the presentation and classification of items in the financial statements should be the same from one period of the next, unless a change is justified by a change circumstance or by a new IFRS. This is to ensure comparability of financial statements from one period to the next. If the presentation of financial state4mensts were allowed to change on a regular basis or if the classification of elements were allowed to change then, the comparability statements would be significantly reduced.

(b) Brief explanations on

(i) Comparability

Comparability of financial information is important for its users. Examining an entity's financial statements for one accounting year gives only a certain amount of insight into the financial performance and position of the entity. By comparing financial information of an entity over time, one can assess trends and by comparing financial information against industry standards, one can benchmark performance against competitors.

Comparability both in presentation and calculation can be achieved by being consistent in the use of accounting policies over time. Where new policies are introduced by for example, the introduction of a new accounting standard, consistency and comparability can be achieved by properly disclosing the change in the accounting policy and outlining the effect of the change.

(ii) Verifiability

Verifiability can be achieved when two or more independent and knowledgeable observers can reach a consensus on the treatment and measurement of an economic transaction. In these circumstances the economic transaction is regarded as being faithfully represented. For example, if financial information is independently verified by external auditors, this increases the degree to which it is regarded as faithfully represented and hence increased the usefulness of the reported information.

OR

Verifiability

Means that different knowledgeable and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation verification can be direct or indirect. Direct verification means verifying an amount or other representation through observation, for example by counting cash. Indirect verification means checking the inputs to a model, formula or other technique and recalculating the outputs using the same methodology.

(iii) Timeliness

If information is to be useful, it must be provided in a timely manner. If information is out of date, it is less likely to be useful to a user's decision making. This may not always be the case however as historical data can be used to identify trends which provide useful information for predicting future outcomes and accordingly aid decision-making.

(iv) Understandability

When information is classified, characterized, and presented clearly and concisely it is likely to be understandable to users with a reasonable knowledge of business, economic activity and accounting and who are prepared to study the information. The "Conceptual Framework" accepts that prepares of financial statements can assume that users have this reasonable information.

ANSWER 3

Kalambo Company Ltd.
Statement of Comprehensive Income for the year ending 31 December 2014

	Tshs. '000,000'	Notes
Turnover	2,400	(1)
Cost of sales (Workings 1)	(800)	
Gross profit	1,600	
Distribution costs (200 + 680)	(880)	
Administrative expenses (300 + 80 + 40)	(420)	
Operating profit	300	(2)
Other income	30	(3)
Interest payable and similar charges	(10)	(4)
Profit on ordinary activities before taxation	320	
Tax on profit on ordinary activities	(100)	(5)
Profit for the financial year	220	
Dividends paid and proposed	(70)	(6)
	150	
Earnings per share	0.00039	(7)

Magambo Company Ltd.
Statement of Financial Position as at 31 December 2014

	Tshs. "000,000	Notes
Non Current Assets		
Tangible assets	120	(8)
Investments	140	(9)
	260	
Current assets		
Stock	600	
Debtors	558	(10)
Cash	118	
	1,210	
Creditors		
Amounts falling due within one year	(326)	(11)
Net current assets	950	
Total assets less current liabilities	1,210	
Creditors		
Amounts falling due after more than one year	(180)	(12)
	1,030	

Capital and reserves

Called – up share capital	560
Share premium account	140
Profit and loss account (180 + 150)	330
	1,030

Notes			**Tshs. "000,000**
(1)	Turnover		
	Turnover represents the amount received, net of VAT, for goods sold during the year.		
(2)	Operating profit		
	Operating profit is stated after charging:		
	Depreciation		80
	Director's emoluments		110
	Hire charges for distribution activities		680
	Auditors' remuneration		40
(3)	Other income		
	Other income arising from trade investments		30
(4)	Interest		10
	Interest payable on debenture stock		
(5)	Taxation		
	Taxation on the profit for the year:		100
	corporation tax at 30%		
(6)	Dividend		
	Ordinary – interim Tshs. 25 per share		14
	- Proposed final 100 per share		56
			70
(7)	Earnings per share		
	The calculation is based on 560,000 ordinary shares of Tshs. 1,000 each in issue during the year.		
(8)	Tangible Non Current Assets		
	Furniture and fittings at cost		400
	Less: Accumulated depreciation to 1 Jan. 2014 Tshs	200	
	Depreciation for the year	+80	280
			120
(9)	Investments		
	Shares at cost in respect of investments listed on a recognized stock exchange (market value Tshs 170,000,000)		
(10)	Debtors		140
	Trade		360
	Prepaid expenses		500
	Amount falling due within one year		58
			558
(11)	Creditors: Amounts falling due within one year		
	Trade creditors		120
	Taxation		100

	Accruals	50
	Proposed divided	56
		326
(12)	Creditors: Amounts falling due after more than one year	
	Debenture loans	100
	Deferred taxation	80
		180
	Workings	
	1 Cost of sales	
	Opening Stock	400
	Purchases	1,000
		1,400
	Less: Closing stock	600
	Cost of sales	800

OR

	Tshs. "000,000
Turnover	
Turnover represents the amount received, net of VAT, for goods sold during the year.	2400
Cost of sales (Note 1)	(800)
Gross Profit	1600
Other Income (Dividend Received)	30
Gain on fair value Adjustment of trade investments (170 – 140)	30
Distribution costs	(880)
Administrative Expenses (300 + 40 + 80)	420
Finance costs (Decenttrine Interest	(10)
Profit before tax	350
Taxation	(100)
Profit for the year	250

Workings:

Retained earnings at 31st December 2014

Balance at start	180
Profit for the year	250
Dividends (14 + 10% x 560)	(70)
	360

ANSWER 4

(a) Firm performance: Candidates should calculate the following ratio and discuss the performance of firm in comparison to the industrial average's given.

Current ratio $= \dfrac{Current\ assets}{Curreent\ liabilities} = 1{,}050{,}000{,}000 / 300{,}000{,}000$

$= 3.5{:}1$

Quick ratio $= \dfrac{Current\ assets - Invetories}{Curreent\ liabilities} = 500{,}000{,}000 / 300{,}000{,}000$

$= 1.67{:}1$

Inventories Turnover $= \dfrac{Cost\ of\ goods\ sold}{Inventory} = 850{,}000{,}000 / 550{,}000{,}000 = 1.55$ times

Average collection period $= \dfrac{Accounts\ receivable}{Daily\ credit\ slaes} = 362{,}500{,}000 / (1{,}450{,}000{,}000 / 365)$

$= 91.25$ days

Debt ratio $= \dfrac{Total\ debt}{Total\ assets} = 900{,}000{,}000 / 2{,}600{,}000{,}000 = 0.3462$

Time interest earned $= \dfrac{Operating\ profit}{\text{int}erest\ \text{exp}enses} = 360{,}000{,}000 / 64{,}000{,}000$

$= 5.625$ times

Total asset turnover $= \dfrac{Sales}{Non - Current} = 1{,}450{,}000{,}000 / 2{,}600{,}000{,}000$

$= 0.5577$ times

Fixed assets turnover $= \dfrac{Sales}{Non - Current\ \ Asset} = 1{,}450{,}000{,}000 / 1.550{,}000{,}000$

$= 0.9355$ times

Operating profit margin $= \dfrac{Operating\ profits}{Sales} = 360{,}000{,}000 / 1.450{,}000{,}000 = 0.2483$

$= 24.83\%$

Return on Equity = Operating profit/Equity = 360,000, 000/1,700,000,000 = 21.17%

= Profit After/Equity = 178,1,700,000,000 = 10.47%

(b) **Disadvantages of using ratio analysis**

Despite usefulness, financial ratio analysis has some disadvantages. Some key demerits of financial ratio analysis are:

- Different companies operate different industries each having different environmental conditions such as regulation, market structure, etc. Such factors are so significant that a comparison of two companies from different industries might be misleading.

- Financial accounting information is affected by estimates and assumptions. Accounting standards allow different accounting policies, which impairs comparability and hence ration analysis is less useful in such situations.

- Ratio analysis explains relationships between past information while users are more concerned about current and future information.

- **Problem of getting comparable information-** It is a known fact that ratios are useless if they are not compared with ratios from similar entity. You must compare likes to have realistic information. In practice, it is impossible to consciously find two companies that are identical in every sense.

- **Use of outdated information-** Historical accounting information is the primary source of data used for investment ratio analysis. This alone is enough to render every other factor useless. It is hard to make any meaningful judgment from information that is already out of date.

- **Ratio are subjective**- No two humans will give two exact judgments even while presented with the same information. Personal sense of judgment must be introduced and this makes it prone to having personal investment bias.

- **Analysis cannot be used in isolation**- An investment ratio analysis cannot be used in isolation. It must be combined with some other information from other sources. This make it possible for element of wrong judgment to be introduced into the decision making variables through the introduction of information from unreliable and unverifiable source.

- **Ratios are not definite**- Ratio analyses are just guide and never a definite or concrete assertion. This makes it possible for wrong investment decision to be taken. Investment ratio analysis is not like mathematics and is therefore susceptible to inflows of noise.

- **Ratios are subject to manipulation (Creative accounting, inappropriate accounting policies)** – Creative accounting and other form of manipulations like window dressing of accounts in a serious facto that affects financial statements ratio analysis. An investment analyst working on ratio analysis should bear this at the back of his or her mind.

- **Ratio have no standard form** – There are no generally acceptable formats for presenting and interpreting ratios. This is in addition to the fact that ratio analyses are subjective in nature.

ANSWER 5

(a) Recognition criteria under IAS 16 PPE

Property, plant, and equipment should be recognized as assets when it is probable that: (IAS 16.7)

- It is probable that the future economic benefits associated with the asset will flow to the entity, and

- The cost of the asset can be measured reliably.

(b) Measurement bases

(i) Historical cost

Under historical cost, assets are recorded at the amount of cash or cash equivalent paid or the fair value of consideration given to acquire them at the time of acquisition.

(ii) Current cost (fair value)

Under this, assets are carried at the amount of cash or cash equivalent that would have to be paid if the same or equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalent that would be required to settle the obligation currently.

(iii) Realizable (settlement) Value

Under this, assets are recorded at the amount of cash or cash equivalent that could currently be obtained by selling the asset in an orderly disposal Liabilities are carried in their settlement values; that is undiscounted amount of cash or cash equivalents expected to be paid to satisfy the liabilities in the normal course of business.

(iv) Present value

Assets are carried at the present discounted value of future net cash inflows that the item is expected to generate in the normal course of doing business. Liabilities are carried at the present discounted value of future net cash outflows that expected to be required to settle the liabilities in the normal course of doing business.

(c) An entity shall classify an asset as current when

(i) It expects to realize the asset, or intends to sell or consume it, it its normal operating cycle.

(ii) It holds the asset primarily for the purpose of trading

(iii) It expects to realize the asset within twelve months after the reporting period

(iv) The asset is cash or a cash equivalent (as defined in AIS 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

An entity shall classify all other assets as non-current.

(d) Cost of Property, Plant and equipment

This is self-constructed asset, all cost to get the new store to its present location and condition for its intend use should be capitalize. All of the expenditure listed in the question, with exception of general overheads would qualify for capitalization.

The interest on the loan should also be capitalized from 1 April 2009 as it meets the definition of IAS 23. The capitalization of the interest will cease when the asset is ready for use. The cost of PPE will then be.

	"000"Tshs
Freehold land	4,500
Architect fees	620
Site preparation	1,650
Materials	7,800
Direct labor costs	11,200
Legal fees	2,400
Borrowing costs (25000 x 8%) x 9/12	1,500
Total Capitalization	29,670

Impact to income statement

Income statement should be charged with

(i) General overheads of 940,000 as expenses

(ii) Remaining interest for January – March which is now an expense 500,000 Tshs. (25,000,000 x 8% x 3/12)

(iii) Depreciation of the store – Although we cannot calculate by now since due to absence of the information surrounding useful economic life of the store but IAS 16 states that depreciation of an asset begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by the management.

ANSWER 6

(a)(i) Harmonization Versus Standardization

Harmonization tends to mean the process of increasing the compatibility of accounting practices by setting bounds to their degree of variation. This takes into account some of countries variation caused by differences in economic, social and political factors.

Standardization tends to imply the imposition of a rigid and narrower set of rules. Standardization also implies that one technically correct method can be identified for every aspect of accounting and then this can be imposed on all preparers of accounts.

Due to the variations between countries full standardization of accounting practices is unlikely. Harmonization is more likely, as the agreement of a common conceptual framework of accounting may enable a closer harmonization of accounting practices.

(ii) Importance of Harmonization

Each country has its own accounting regulation, financial statements and reports prepared for shareholders and other uses are based on principles and rules that can vary widely from country to country. Multinational entities may have to prepare reports on activities on several bases for use in different countries, and this can cause unnecessary financial costs. Furthermore, preparation of accounts based on different principles makes it difficult for investors and analysts to interpret financial information.

This lack of comparability in financial reporting can affect the credibility of the entity's reporting and the analysts' reports and can have a detrimental effect on financial investment.

The increasing levels of cross-border financing transactions, securities trading and direct foreign investment has resulted in the need for a single set of rules by which assets, liabilities and income are recognized and measured.

The number of foreign listings on major exchanges around the world is continually increasing and many worldwide entities may find that they are preparing accounts using a number of different rules and regulations in order to be listed on various markets.

(iii) Benefits for using single set of accounting standards

- **Comparability**

  The biggest advantage of a single set of global accounting standards is the enhancement in comparability between companies in different countries. Currently, accounting standards can fifer greatly between countries. Before an investor can compare two potential investments, she must reconcile the two companies to the same basis of accounting. The problem is similar for creditors: When evaluating a company's creditworthiness, differences in accounting standards can make two companies that are in similar economic shape appear very different. Enacting a set of global accounting standards would put comparisons on equal footing, making it easier for small-business owners to evaluate international options for investment and cash management. Right now, many small-business owners do not have the resources to effectively compare international and domestic investment options. If financial statements were more comparable, owners would be able to complete more of these comparisons in house.

- **International Expansion**
  Moving to a single set of global financial standards would also ease barriers to expansion for companies. If companies wish to expand overseas today, they need to consider international costs of compliance, which could mean adopting a completely new set of accounting records to meet statutory requirements in the new country. In some cases, this would nearly double the company's accounting costs. For many small business, even large rewards of moving overseas are dwarfed by these expansion costs.

- Access to a wider range of international finance opportunities. If international standards were widely accepted, the international financial markets would be accessible by a wider range of entities. This could have the effect of reducing financing costs;

- It helps multinational companies with subsidiaries to improve management control as all parts of the entity would be reporting using one consistent basis;

- Greater efficiency in accounting departments as they would not have to spend time converting data from one accounting basis to another;

- Easier consolidation of subsidiaries, preparation of group accounts would be simplified.

- Investors should benefit by being able to compare the results of different entities more easily and make more informed investment decisions.

(b) (i) Approaches

- **Merger:-** A merger is a business combination in which the acquired company's assets and liabilities are combined with those of the acquiring company. Thus, two companies are merged into a single entity. In essence, the acquiring company "swallows" the acquired company.

- **Controlling ownership:-** A business combination in which the acquired company remains ass a separate legal entity with a majority of its common stock owned by the purchasing company leads to a parent-subsidiary relationship. Accounting standards normally require that the financial statements of the parent and subsidiary be consolidated for general-purpose reporting so the companies appear as a single company. The treatment is the same if the subsidiary is created rather than purchased. The treatment is also the same when the other entity is unincorporated and the investor company has control and majority ownership

- **Non-controlling ownership:-** The purchase of a less-than-majority interest in another corporation does not usually result in a business combination or controlling situation. A similar situation arises when a company creates another entity and holds less than a controlling position in it or purchases a less-than-controlling interest in an existing partnership. In its financial statements, the investor company reports its interest in the investee as an investment with the specific method of accounting for the investment dictated by the circumstances.

- **Other beneficial interest:-** One company may have a beneficial interest in another entity even without a direct ownership interest. The beneficial interest may be defined by the agreement establishing the entity or by an operating or financing agreement.

  When the beneficial interest is based on contractual arrangements instead of majority stock ownership, the reporting rules may be complex and depend on the circumstances.

In general, a company that has the ability to make decisions significantly affecting the results of another entity's activities or is expected to receive a majority of the other entity's profits and losses is considered to be that entity's primary beneficiary. Normally, that entity's financial statements would be consolidated with those of the primary beneficiary.

(c) Goodwill on acquisition

	Tshs.	Tshs
Investment in Kamata Ltd.		1,800,000
Acquired		
Net asset at book value	1,350,000	
Revaluation	100,000	
Contingent Liability	(200,000)	
		1,250,00
Goodwill in acquisition		**550,000**

ANSWER 7

(a) Computer cash flows from operating activities as follows:

	Sales	(Tshs. In millions)
		100,000,000
	Less increase in accounts receivable	(15,000,000)
(i)	Cash collection from customers	85,000,000
	Cost of goods sold	73,000,000
	Plus increase in inventory	32,000,000
	Purchases	105,000,000
	Less: increase in accounts payable	(25,000,000)
	Cash paid to suppliers	80,000,000
(ii)	General expenses	8,000,000
	Plus increase in prepaid general expenses	1,000,000
(iii)	Cash payment for general expenses	9,000,000
(iv)	Cash paid for interest	3,000,000
	Property taxes	4,000,000
	Less: Increase in accrued property tax payable	(2,000,000)
(v)	Cash paid for property taxes	2,000,000

Cash flows from operating activities		
Cash collections from customers (i)		85,000,000
Cash payments		
Cash paid to suppliers (ii)	(80,000,000)	
General expenses (iii)	(9,000,000)	
Interest paid (iv)	(3,000,000)	
Property taxes (v)	(2,000,000)	(94,000,000)
Net cash used by operating activities		(9,000,000)
Cash flows from investing activities		
Purchase of fixed assets (building)	(54,000,000)	
Proceeds from sale of fixed assets	5,000,000	
Net cash used by investing activities		(49,000,000)
Cash flows from financing activities		
Long-term debt issued	40,000,000	
Dividends paid	(1,000,000)	
Net cash provided by financing activities		39,000,000
Net decrease in cash		(19,000,000)
Cash balance, December 31, 2013		20,000,000
Cash balance, December, 31, 2014		1,000,000

(b) The statement of cash flows shoes where cash has come from and where it has gone. Operations used Tshs.9 million of cash. The statement of cash flows above, which uses the direct method, shows the result clearly: Tshs.94 million in cash paid for operating activities exceeded Tshs.85 million in cash received from customers. The three largest items differentiating net income from cash flow are changes in inventory, accounts receivable, and accounts payable. Sales during the period were not collected in full because accounts receivable rose sharply, by Tshs.15 million, 30% increase. Similarly, Mkinga spend cash on inventory growth, although it financed much of that growth by increased accounts payable. In summary, the large increases in accounts receivable (Tshs.15 million) and inventory (Tshs.32 million), plus an increase in prepaid expenses (Tshs.1 million), show that Mkinga used Tshs.48 million of cash. In contrast, the sum of the items not in addition show that Mkinga generated only Tshs.39 million in cash, that is, Tshs.4 million + Tshs.8 million +Tshs.25 million + Tshs.2 millin. Thus, the company used a net amount of Tshs.9 million in operations (Tshs.39 million – Tshs.48 million).

SUGGESTED SOLUTIONS
B3 – AUDITING PRINCIPLES AND PRACTICE
MAY 2015

ANSWER 1

(a) The major factors in to day society that have made the need for independent audits much greater than it was 50 years ago include:

- **Remoteness of Information.** In a global economy, it is nearly impossible
  for a decision maker to have much firsthand knowledge about the organization with which they do business. Information provided by others must be relied upon. Hen information is obtained from others, the likelihood of it being intentionally or unintentionally misstated increases.

- **Biases and Motives of the Provider.** In information is provided by someone whose goals are inconsistent with those of the decision maker, the information may be biased in favour of the provider. The reason can be honest optimism about future events or an intentional emphasis designed to influence users. In either case, the result is a misstatement of information.
- **Voluminous Data.** As organisations become larger, so does the volume of their exchange transactions. This increases the likelihood that improperly recorded information is included in the records – perhaps buried in a large amount of other information. For example, if a large government agency overpays a vendor's invoice by TZS: 2 million, it is unlikely to be uncovered unless the agency has instituted reasonably complex procedures to find this type of misstatements remain undiscovered, the combined total can be significant.

- **Complex Exchange Transactions.** In the past few decades, exchange transactions between organisations have become increasingly complex and therefore more difficult to record properly. For example, the correct accounting treatment of the acquisition of one entity by another poses relatively difficult accounting problems.

- **Fraud** (misappropriation of Assets, manipulation of financial reporting)
  Occurrence of Fraud, in many organizations lead to higher need of Independent audit in those organizations.

- **Bankruptcies**
  Many organizations have received clean report and after few days declared to be bankruptcy i.e. WorldCom, Union, Parmalat

- Development of Capital market

- Increase in number of transactions in many organizations
- Mismanagement in many organization.

(b) (i) **Materiality.** Refers to misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

(ii) Materially **criteria**

The three materiality criteria are:
An item might be material due to its;

Nature	Given the definition of materiality as an item that would affect the readers of the financial statements, some items might **by their nature affect readers.** Examples include **transactions related to directors,** such as remuneration or contracts with the company.
Value	Some items will be significant in the financial statements by virtue of their size, for example, if the company had bought a piece of land with a value which comprised three quarters of the assets value of the company that would be material. That is why materiality often expresses in terms of **percentages** (of assets, of profits).
Impact	**Some items may be chance have a significant impact** on financial statements, for example, a proposed journal entry which is not material in itself could convert a profit into a loss. The difference between a small profit and a small loss could be material to some readers.

(iii) **Rules on materiality**

The generally accepted rules about materiality that exist include:

- Items relating to directors are generally material
- Percentage guidelines are often given for materiality

While materiality is **always a matter of judgement** for the auditor, it is helpful to have some rules to bear in mind. Reasons for this are: (Importance of rules)

- The rules give the auditor a **framework** within which to assess the quality of auditing, for example, in the event of litigation or disciplinary action.
- The rules provide a **benchmark** against which to assess the quality of auditing, for example, in the event of litigation or disciplinary action.

(c) A **positive** external confirmation request asks the respondent to reply to the auditor in all cases either by indicating the respondent's agreement with the given information, or by asking the respondent to fill n information. Response to a positive confirmation request is ordinarily expected to provide reliable audit evidence. There is a risk, however, that a respondent may reply to the confirmation request without verifying that the information is correct.

A **negative** external confirmation request asks the respondent to reply only in the event of disagreement with the information provided in the request. However, when no response has been received to a negative confirmation request, the auditor remains aware that there will be no explicit audit evidence that intended third parties have received the confirmation requests and verified that the information contained therein is correct. Accordingly, the use of negative confirmation requests ordinarily provides less reliable audit evidence than the use of positive confirmation requests.

ANSWER 2

(a) **Definition**

True and fair view in auditing means that the financial statements are free from material misstatements and faithfully represent the financial performance and position of the entity.

Explanation

Although the expression of true and fair view is not strictly defined in the accounting literature, we may derive the following general conclusions as to its meaning:

True suggests that the financial statements are factually correct and have been prepared according to applicable reporting framework such as the IFRS and they do not contain any material misstatements that may mislead the users. Misstatements may result from material errors or omissions of transactions & balances in the financial statements.

Fair implies that the financial statements present the information faithfully without any element of bias and they reflect the economic substance of transactions rather than just their legal form.

(b) **Need for modifications**

- Expensed direct labour: The amount of direct labour represent 10% of the net profit, and hence the question of the materiality of TZS 15,000,000 then arise. The standard require all costs associated with construction of assets be capitalize, and the treatment of written of direct costs during the year is likely to be considered material, in such circumstances, a modification may be necessary.

- Capitalization of Research costs: IAS 38 does not permit research costs to be capitalized under any circumstances. The amount involved does appear to be material based on the annual profits and hence audit modification would therefore be necessary.

(c) There are four common types of auditor's reports, each one presenting a different situation encountered during the auditor's work. The four reports are as follows:

- **Unmodified audit report**

  When auditor on the basis of examination and the evidence obtained expresses his opinion that financial statements of the entity are prepared in all material respects in accordance with applicable financial reporting framework or financial statements give true and fair view than such audit report or auditor's report is called **unmodified or unqualified report. Isa 700** describes the contents and format of the unmodified report in detail.

- **Emphasis of Matter**

  Auditor includes an emphasis of matter paragraph (EMP) when auditor considers that it is necessary to draw the attention of users of financial statements to the matter that is **already disclosed or reported in the financial statements** and understanding of the specified matter is important in **understanding of the financial statements**. EMP is included after the opinion paragraph in the audit report. However students must be clear that inclusion of EMP DOES NOT mean that auditor's opinion is modified.

- **Modified report with modified opinion**

Auditor modify his opinion when he concludes that it will not be appropriate to express an unmodified/unqualified opinion. Auditor reaches such conclusion when:

- The auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or
- The auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

The modification to the audit opinion is determined by the audit opinion is determined by the auditor by applying his professional judgement on the circumstances at hand. He may modify his opinion to express a qualified opinion, an adverse opinion or a disclaimer.

- **Other Matter Paragraph**

  Auditor includes other matter paragraph (OMP) when auditor considers that it is necessary to communicate a matter **other than those that are presented or disclosed in the financial statements** and in auditor's judgement understanding that matter is vital for users' **understanding of the audit, the auditor's responsibilities or the auditor's report** and this is not prohibited by law or regulation. OMP is included after opinion paragraph and any EMP in the auditor's report or somewhere else in the auditor's report if the content of the Other Matter paragraph is relevant to the Other Reporting Responsibilities section.

ANSWER 3

(a) Detailed assertions are necessary because they give the auditor:

- **A clear definition of audit aims**
  The overall audit objective is extremely wide. There is therefore a danger that unless we break the overall objective down into smaller chunks the auditor might or might fail to perform sufficient work to achieve the overall objective. The detailed audit assertions also help the auditor focus on key areas.

- **A clear demonstration of work done**
  An audit is like justice – it must not only be done, it must be seen to be done;
  An auditor must be able to reconstruct the thought processes, if necessary, and show that the work done was adequate and conclusions drawn were soundly based. By constructing the programme of work by reference to audit assertions that auditor can demonstrate that this is the case.

(b)(i) Confirmations received directly by the auditor from third parties have a very high degree of reliability as far as the auditor is concerned, and are to be preferred to either (ii) or (iii). The reason for this high degree of reliability is that the client cannot interfere with the communication between the auditor and the third party. This means the client cannot alter the documentary evidence obtained from the third party, or Change Company records to agree with the documentary evidence. It is vital, however, that the third party is independent of the client's company and is competent to supply the information required. An example of such evidence is a bank letter received from the client's bank confirming balance held and supply other additional information.

(ii) Documents produced for the auditor by the client and prepared by outsiders, although not as strong as (i) above, is still regarded as valuable audit evidence, and in fact such evidence is far more common than confirmations sent directly to the auditor. It would be quite impracticable for the auditor to receive all the evidence direct from third parties and therefore most of the information is produced by the client. An example of evidence prepared by outsiders is an invoice received by the client from a supplier in respect of goods delivered. It is important to the auditor that such evidence appears authentic and any alterations need careful investigation.

(iii) Documents produced for the auditor by the client and prepared by personnel within the client company are likely to be less reliable than the types of evidence described in (i) and (ii). The reason for this is that if an employee has been responsible for defrauding the company in any way then the documents prepared by the employee may be falsified to conceal the fraud. In addition, the employees preparing the documentation are under the direct control of management and therefore the evidence may not be fully acceptable in attempting to corroborate management representations.

Internal evidence may circulate outside the business and because of this the reliability is increased because of its acceptance by outsiders. An example of such evidence is a paid cheque issued by the client which if unendorsed is regarded as acceptable evidence that the payee named on the cheque has received the amount stated on the cheque. It does not, however, offer evidence of consideration.

(iv) An example of evidence calculated by the auditor from company records is a schedule of accounting ratios (or percentages) prepared by the auditor. An auditor may find it very useful to prepare such a schedule showing key ratios in order that these can be compared with those of previous years and similar companies (if this is possible). Changes in gross profit percentages, expenses to sales, etc require very careful investigation, as the auditor expects a certain relationship to exist and there should be some comparability from year to year. This evidence calculated by the auditor is circumstantial as opposed to the direct evidence described in (i) to (iii). This circumstantial evidence is, however, very useful in that it supports an inference as to the reasonableness of a given figure in the client's financial statements or of the statements as a whole.

(c)(i) The principle of sufficiency is the measure of the quantity of audit evidence. The amount of evidence required in a given situation is a matter of judgement and will depend inter alia on the following matters:

- The importance of the figure being checked in terms of its impact on the view given by the financial statements, in terms of size or importance.
- The level of risk attaching to the figure: more assurance, and so evidence, is required in a case where there is greater risk of error or fraud.
- The source of evidence available
- The quality of evidence available in terms of reliability
- The cost of obtaining the different types of evidence that are available.

(ii) A number of factors govern the reliability of evidence. These include:

- The category of evidence (in decreasing order of reliability): natural evidence (the asset or event itself), created evidence (documentation) and rational augmentation (application of logic to determine the accuracy of a figure) however, the source of the evidence, whether created by the auditor, the client or third parties have arguably a greater impact on reliability.
- Evidence generated by the auditor is the most reliable but the problem is that it is also the most costly.
- Evidence from within the company should be fairly reliable and easy to obtain, but it may be susceptible to director manipulation

- Evidence obtained by the auditor directly from a third party is least likely to be manipulated by the client, but the auditor has no way of checking the quality of the processes that produce the evidence.

- Documentary evidence is more reliable than oral evidence. An auditor will thus seek out documentary evidence, or if none is available, obtain confirmation of oral evidence in writing from the directors in a letter of representation.

ANSWER 4

(a) (i) Independence required to be demonstrated in relation to facts and appearance.

(ii) Movements (distance away from the office) could not justify the resolution, still there is a room of communication through computer networking.

(iii) Based on the family relationship it creates familiarity threat which can only be avoided by not be involved in engagement (particular client).

(iv) Splinting the firm into three (3) areas would not resolve the existing objective threat, since self review threat will still persist if a firm involved in provision of business advisory services, management consultancy and investment advisory services. Otherwise a firm concentrates in providing auditing services only to the client.

Independence of mind is very vital as compared t independence in appearance.

(v) Integrity as one of the professional ethics need to be considered by a partner since was supposed to declare existed conflict of interest (familiarity relationship) with the financial controller of an audit client before acceptance of the engagement.

(v) Objectivity in auditing engagement once observed could provide a room for an auditor to provide more than one service to the client.

(b) Advantages of using statistical sampling
The main advantages gained by successfully using statistical sampling are listed below:

- It is possible to state, with a stipulated degree of confidence, that the sample result is not further away from the true condition of the population than some specific amount.

- The result obtained by the sample is not subject to the complaint of bias, i.e. that the auditor has looked at the worst items.

- The method provides a means of knowing in advance the size of the maximum sample needed. If auditors have decided on the degree of risk they are prepared to accept, then they are relieved of the obligation of determining sample sizes arbitrarily. Justification is provided for the size of the sample used and thus for the time spent on the audit work.

- Statistical sampling can be more accurate than an examination of every time in a large population. Examining a high volume of data involves tedious detailed work, causing carelessness and different interpretations, and errors may arise.

- The evaluation of results is simplified, but great care is necessary, first to ensure that each characteristic being tested is evaluated separately and, second that in fixing an acceptable error rate". For example, a low error rate may be serious evasions of internal control but, on the other hand, a relatively high error rate may not give concern if the errors are of a random nature, showing no particular trend and indicating no specific control weakness.

ANSWER 5

(a) A value for money audit is conducted to determine the economy, efficiency and effectiveness of an entity. For the hotel this review will be beneficial as it will help management to identify the activities where it is spending more without getting the adequate returns. In order to identify the reasons for the increase in the housekeeping department's expenses, the auditor should verify the economy, efficiency and effectiveness of the housekeeping department.

The three main aspects of value for money are as follows:

(i) Economy

In this review, the auditor will determine the following:

- The total carpet space or rooms to be cleaned
- The number of employees actually required to clean them and the number actually employed, the pay rates of employees and whether these seem to be reasonable.
- The rates of organisations providing housekeeping services and whether the work can be outsourced.

(ii) Efficiency

A review of efficiency determines whether or not Eagle Hotels is utilizing its resources optimally. In the case of the housekeeping department, this depends on whether or not the available manpower is utilized fully and whether or not there is any idle time. The following questions need to be answered:

- How much time is spent in cleaning in a day and what work is allotted to the employees in other times? Are they kept occupied during their working hours or is a lot of time left idle?
- Are consumables such as linen, bed sheets, pillow covers, towels, etc. replaced only after the set in use has reached the end of its life? Are the purchases authorized?
- Is a reasonable inventory maintained of all the consumables?

(iii) Effectiveness

A review of effectiveness determines whether the hotel is receiving adequate returns against the services rendered. Here, the auditor will have to judge whether or not, as a result of the increase in housekeeping expenses, the satisfaction level of the guests has improved. If the hotel is clean, meets all the health and safety norms and has a good reputation in the market, it may indirectly result in increase in business. The value for money audit aims to ensure a good quality and quantity at the lowest price. The organization also has to ensure that, for example, for the standard of hotel it runs that bed linen is not changed more often than would be normal.

(b) **Deficiencies of value for money audit**

- **There exist no universal measures for outputs.** For example, the output of a customer care executive in a call centre can be measured by the number of calls attended by him or her. However, each call can be of different difficulty and take different amounts of time. However, the output of a machine is likely to be uniform and will be in terms of the units manufactured.

- **Objectives of audit and measure of efficiency vary with the type of work being audited.** For example, the objective of a customer care executive is to satisfy the queries of a customer in the minimum time. Hence, their efficiency would be determined on that basis. However, the objective of a machine is to produce the maximum output with minimum resources.

- **Quality might be sacrificed to achieve economy and efficiency.** The objective of VFM audits is to achieve economy, efficiency and effectiveness. Sometimes efficiency is sacrificed to achieve economy. For example, the customer care executive may end the call without giving adequate answers to the queries posed by the customer. The servicing of the machine may be delayed to avoid the machine's downtime.

It is not easy to measure effectiveness. For example, the effectiveness of a customer care executive will improve if they give detailed replies to the queries of the customers. However, it would result in low call turnover and other customers would have to wait for a long time before their phone call is attended. Therefore the measurement of effectiveness of this function is subjective, and not easy.

(c) Being a parastatal organization Maraha must be audited by the CAG. This is because the mandate to audit the public authorities solely lies with the CAG and not private audit firm.

This is in accordance with Article 143 (2) (c) of the Constitution of the United Republic of Tanzania, which preserves the statutory requirement for the audit of the Public Sector (as amplified under Section 34 (1) of the Public Audit Act No. 11 of 2008), the Controller and Auditor General shall express a professional opinion, in respect of each account within a period of **nine months after the end of the year** to which the accounts relate.

The law further requires that each public authority or body shall prepare and submit for audit its financial statements to the Controller and auditor General each financial year.

ANSWER 6

(a) The roles and functions of the Internal auditor General are:-

(i) Scrutinize and compile audit reports from Ministries, Department, Government institutions, Regions, Local Government Authorities, Executive Agencies and Donor funded projects and shall prepare a summary of major audit observations and recommendations and submit the same to the Paymaster General for further action;

(ii) Undertake continuous Audit risk Management;

(iii) Develop and supervise the implementation of Internal Audit Strategy;

(iv) Develop, implement and review annual audit Programme;

(v) Liaise with the Controller and Auditor General, Accountant General, Accounting Officers and Professional Standards Setting Authorities on audit matters;

(vi) Manage and control the quality of operations of the audit cadre and enhance Capacity of Audit Committees;

(vii) Evaluate the effectiveness of Audit Committees in Ministries, Departments, government Institutions, Regions, Local Government Authorities and executive agencies;

(viii) Facilitate the development of internal audit cadre;

(ix) Review and appraise budget planning and implementation with a view to promoting compliance with national goals and objectives; technical reports on development initiatives; works, goods offered and services supplied to the government from development and recurrent budgets and determine their value for money;

(x) Prepare audit reports and advise the government on intervention measures towards ensuring values for money on public expenditure;

(xi) Make follow up on the agreed audit recommendations and required corrective actions;

(xii) Undertake special and investigative audits;

(xiii) Review, monitor, evaluate and recommend on systems of Government revenue collections for proper accountability;

(xiv) Participate in the hearings and render advice to the relevant Parliamentary Oversight Committees.

(b) Examples of audit activities performance measures

The International Professional Practices Framework (IPPF) is the conceptual framework that organizes authoritative guidance promulgated by the Institute of Internal Auditor (IIA). The guidelines are divided into two major groups namely mandatory guidance (Definition of Internal Auditing, Code of Ethics and International Standards) and Strongly Recommended Guidance (Position Papers, Practice Advisories and Practice Guides).

One of the IPPF practice guide (**measuring internal audit effectiveness and efficiency)** provides guidance to internal audit activities on measuring their effectiveness and efficiency and the level of customer service they provide to stakeholders.

Effectiveness and efficiency measurements can be quantitative and qualitative and examples of audit activity performance measures may include:

- Achievement of key goals and objectives
- Evaluation of progress against audit activity plan
- Improvement in staff productivity
- Increase in efficiency of the audit process
- Increase in number of action plans for process improvements
- Adequacy of engagement planning and supervision
- Effectiveness in meeting stakeholders' needs.

ANSWER 7

(a) The auditor should employ the following tests of control for verifying the purchase of the new machinery:

(i) On a sample basis verify the ownership documents for non-current assets purchased during the year and confirm that the entity owns them.

(ii) Check if the useful life of the machinery is estimated rationally. For this the report of an expert can be used after the auditor has evaluated the work of the expert.

(iii) Verify that the depreciation charged is appropriate i.e. in accordance with the life of the machinery. Verify also the rates to see if they are consistent with the existing company policy.

(iv) On a sample basis verify the purchase voucher and confirm that the purchases are approved by an authorized official of the company (in addition to board approvals).

(b) Usefulness of documents requested;

(i) Payment made after year end:

- To ensure that all expenses related to the year under audit had been accrued properly. Management may deliberately choose to defer such expenses to a future period in order to show a higher profit this year.

- To establish whether dividend on shares sold ex-div or cum div respectively had been received in the subsequent year.

- To establish the accuracy of cash in hand at year especially where the auditor did not attend the year-end cash count exercise.

(ii) Lease of premises

- Value of the lease
- Terms of the lease because if there is any breach the lease would terminate
- Period of the lease so that appropriate provision could be made for their renewals.

(iii) Articles of Association

- Whether shares have been issued according to rules laid down in the articles
- To know the date on which a call could be made and at what rate
- Whether interest should be charged on calls in arears
- Circumstances under which shares could be forfeited
- Borrowing powers, appointment, remunerations, powers and duties of directors, managing agents etc
- To know about accounts and audit of the company.

(iv) Minutes of Board of Directors

- Allotment of shares and debentures
- Adoption of contracts
- Appointment of bankers and officers authorized signatories
- Call of shares
- Forfeiture of shares
- Appointment of managing director and his/her remunerations
- Appointment of auditors and their remunerations
- Adoption of annual financial statements
- Dividends declarations
- Any matter to which a resolution of the directors is specifically required by the articles.

(v) Minutes of the shareholders

- Adoption of Annual financial statements
- Any resolution affecting the accounts
- Remunerations voted for directors
- Auditors remunerations
- Appropriation of profits by way of dividends, reserves etc.

SUGGESTED SOLUTIONS
B4 – PUBLIC FINANCE AND TAXATION I
MAY 2015

ANSWER 1

(a) According to Section 9 (1) of the Income Tax Act 2014, the following items are sources of investment income.

1. Dividend
2. Distribution of a trust
3. Gains of an insured from life insurance
4. Gains from an interest in an unapproved retirement fund
5. Interest
6. Natural resource payment
7. Rent
8. Royalty
9. Net gains from the realization of investment assets of the investment
10. Amounts derived as consideration for accepting a restriction on the capacity to conduct the investment

(b) **Working I: Depreciation Allowable**

S/N	PARTICULARS	CLASS I (37.5%)	CLASS II (25%	CLASS III (12.5%)	CLASS V (20%)
1	Computers & Data	1.8 mil	-	-	-
2	Mowers (2 mowers)	-	-	0.90 mil	-
3	Bulldozers	20 mil	-	-	-
4	Milling building	-	-	-	85 mil
5	Building	-	-	-	60 mil
	Total Depreciation basis	21.8 mil	-	0.90 mil	145 mil
	Less: Disposal of Assets	-	-	-	(175 mil)
	Depreciation Allowed	8.175 mil	-	0.90 mil	-
	Realization Gain	-	-	-	(30)
	Total Depreciation All	9.075 mil			

Note: Under class III: The depreciable Asset less than 1 mil is fully allowable for Depreciation.

Working II: Business Income

Gain of Realization of Business Asset (Building)	30,000,000
Gain from Realization of Business Asset (Land)	6,000,000
	36,000,000
Deductions	
• Depreciation Allowance	9,075,000
• Contribution to Approved Retirement Fund	75,000,000
• Interest paid to CBC	12,000,000
• Scholarship	87,000,000
Business Loss	147,075,000

Investment Income

(1)	Gain from Realization of shares (18,000,000 – 12,000,000)	6,000,000
(2)	Dividend from Tata Coy Ltd.	70,000,000
(3)	Gain from Realization of Residential House	12,000,000
(4)	Received Rental Income from Abby	8,000,000
(5)	Gain from Realization of shares	4,000,000
(6)	Interest from ABC Ltd.	15,000,000
	Total	115,000,000

Total Tax Computation

(1)	Chargeable to Income from Investment 115 x 30% =	34,500,000
(2)	Interest	5,600,000
		40,100,000

ANSWER 2

(a) **Non-tax government revenue**

1. Grants or aids

   Types

   (i) Grants provided by the central government to state government for specific objectives

   (ii) Grants provided by foreign countries to the Central/State Governments

2. Debts from other governments or banks/funds

   Sources

   (i) Foreign countries

   (ii) International borrowings from the private sector in the form of debentures or bonds etc

   (iii) Internal borrowings from central bank of the country

3. Income from investments made by the Government

4. Revenue from public enterprises

5. Royalties

6. Fees and penalties

7. User fees
8. Subsidies received from other countries/bank
9. rent

(b) **Nature of taxation**

Revenue from taxation may be in several forms

1. Revenue Tax
    (i) Income tax

    Sources
    - Income from earnings (e.g. employment income/trade profit)
    - Income from pensions
    - Income from other benefits (e.g. rental income)
    - Income from savings (e.g. interest income)
    - Income from investments (e.g. dividends income)

    (ii) Corporation tax

    (iii) National Insurance Contributions (NIC

    (iv) VAT
2. Capital taxes
    (i) Capital Gain Tax

    (ii) Inheritance Tax

Objectives of taxation

(i) To make provision for funds to meet public expenditure for achieving economic and social objectives.

(ii) To encourage saving by individuals

(iii) To encourage taking risks in investments by entrepreneurs

(iv) To encourage donations to charities

(v) To encourage investment in industrial buildings (e.g. factories, warehouses etc)

(vi) To discourage motoring e.g. to minimize pollution, smoking and alcohol

(vii) Encouragement domestic industry and discouraging imports

(viii) Income redistribution

(ix) Economic stability

(x) Protection of particular sectors/industries

(c) **Principles of a good tax system**

(i) Equity

(ii) Economy

(iii) Certainty

(iv) Efficiency

(v) Benefit principle

(vi) Convenience

(vii) Fairness/equity

(viii) Demand management

(ix) Elasticity

(x) Flexibility

(xi) Broad basing

(xii) Earmarking

(d) **Incidence of taxation**

Tax incidence is said to be on the person who ultimately bears the burden of tax whereas impact of tax is on the person from whom government collects money in the first instance. It is important for the government to know who ultimately bears the tax in order to achieve equality in taxation.

ANSWER 3

(a) Input Tax

Important of standard rated services	12,000,000	
Transportation of cows by VAT person		150,000
Purchase of taxable goods	25,000,000	
Purchase of water (assumed processed)		300,000
Electricity bills		350,000
	37,800,000	
VAT 18%	0.18	
Input tax	6,804,000	

Note: The tax payer is doing importation and therefore partial exemption will not apply.

(b) (i) **Advantages of EFDs**

- Provides business security for traders as all information entered in to the machine stored in to a fiscal memory
- Cannot be erased or altered. Hence the trader can keep track of all business transactions.
- Enhance fairness in tax assessment as all tax information is transmitted to TRA system automatically and hence reduces objection or disputes.
- Minimize pilferages commonly practiced by unfaithful shop attendants.
- Easy to retrieve sales and stock reports (weekly, monthly).

To the User of EFD/Taxpayer

- Easy to operate by users as user can opt to use either Kiswahili or English language.
- Security of the business information as once stored in fiscal memory cannot be erased.
- Simplify refunds applications as information's are contained in fiscal documents.
- Modern way of keeping records as compared to manual records.
- Assurance that the tax on the receipt issued has been remitted to the Government.
- Access to genuine receipts every time a purchase is made.
- Enjoys the social services provided by the Government as a result of the collected taxes.

To the Government

- Fair bases for verification of self-assessments due to timely availability of accurate/reliable tax information.
- Minimizes tax disputes and tax arrears.
- Collection of more revenue due to timely availability of tax information of the taxpayers/EFD users.
- Assist other parties like EWURA to capture accurate data relating to fuel consumption.
- Custody for useful tax information that may enable easy access for statistical analysis and forecasting.

(ii) **Challenges of EFDs**

- Little or no culture, among Tanzanians of demanding fiscal receipts for every purchase made from their resellers.
- Resistances by Phase II traders to acquire and use EFDs.
- Reluctance by some traders to issue correct fiscal receipts and sometimes not issuing receipts for some sales, creating a potential for revenue losses to the government.
- Claiming of underserved VAT input tax by few dishonest traders using ghost fiscal receipts contrary to the law.
- Some EFD users delay in reporting the EFD problems to EFD suppliers contrary to EFD Regulations.
- Durability of EFD Machine.
- Some EFD suppliers delay in servicing of non-working EFDs on time contrary to EFD Regulations.
- Mode of operations/Network
- Telecommunication infrastructure constraints especially in remote areas.
- Lack of education
- Price of the device is high.

(iii) **Government intervention**

- Carrying out continuous surveillance and surprise visits in all high risk areas of non-issuance of receipts.
- Applying sanctions against all identified defaulters.
- Introduction of lottery (raffle) as one of the strategies to stimulate compliance.
- Conducting continuous training to all EFD operational staff on analysis of Z reports, information, audit and enforcement.
- Carrying out continuous tax educational programs to the general public, on the importance of demanding fiscal receipts and invoices upon purchase of goods and services from the eligible EFD users.
- Carrying out continuous sensitization programs to identified EFD phase II traders to acquire and use the EFDs.
- Carrying out continuous and rigorous EFD seminars to EFD users on proper usage and safe keeping of the device.
- Taking punitive measures against EFD users and suppliers who delay reporting and servicing malfunctioned EFDs.

ANSWER 4

(a) Tax Avoidance

Is the practice and technique whereby one so arrange his business affairs such that he pays little or no tax at all but without contravention of tax laws. Tax avoidance takes advantage of any loophole and weaknesses, deficiencies and loose or vague clause in tax legislation to minimize tax liability. Therefore it is sometimes considered as legally allowed.

Tax evasion

Tax evasion on the other hand involves a tax payer's deliberate contravention of the tax laws in order to eliminate or minimize tax liability. It is the application of fraudlent practices in order to minimize or eliminate tax liability. For example:

- Making a false return of income
- Making a false statement in a return affecting tax liability
- Preparation and maintenance of false books of account or records

Tax evasion constitutes fraud which is heavily punishable by law.

(b) **There are several ways of committing tax fraud that include**

1. *Keeping two sets of books to record business transactions.* One records the actual business transactions while the other is **falsified** intentionally understating the taxable amount which is shown to the tax authorities. Some evaders use two cash registers.

2. *Moonlight for cash*. Working an extra job is perfectly legal. However, the income received on such jobs is often paid in cash rather than by cheque. Hence, no legal record exists, and the income is not reported to the tax authorities.
3. *Barter*. When you receive payment in kind instead of money, it is legally a taxable transaction. However, such income is seldom reported.

4. *Deal in cash*. Paying for goods and services with cash and cheques made out to "cash" makes it very difficult for the tax authorities to trace transactions.

5. Under-invoicing of imports.

6. Under-reporting of income especially where income is earned and paid in cash to hide transactions or exchanged in a barter way – receiving payment in kind instead of money.

7. Smuggling. Refers to business transactions which are done illegally and therefore not subjected to the requirements of paying taxes.

8. Money Laundering. Deals with dirty money which is normally covertly cleansed through legal business transactions.

9. Loopholes and weaknesses in the Law

10. Tax planning /Tax Arrangements

11. Transfer pricing

12. Changing Form of business eg from Sole Trader to Limited Company

13. Capitalization – Debt to Equity Ratio.

(c) **Consequences of Tax Evasion**

1. Less Government revenue: for provision of public goods, deficits and its consequences.
   - Non realization of other non-revenue goals of taxation e.g. inequality.
2. Heavy burden on those who comply leading to unequal income distribution.
3. Unfair competition.
   - Bring inequality in the tar system
4. More cost to tax authority.
   - Fine and Penalties and imprisonment.
5. Renders redistribution plan ineffective.
   - Punishment to tax payer.
6. Understating taxable capacities for countries.
   - Cost of goodwill/reputation of business.
7. Promote inefficiency allocation of resources.
   - Non Realization of government objective and plan
   - Non Realization of cannon of principles of tax

ANSWER 5

(a) **The transaction value of the goods imported (CIF)**

Item	€	TZS
Price €20 x 8,000	2035 x 160,000	325,600,000
Add: Insurance	1,000 x 2,035	2,035,000
Add: Freight	Assumption from part (c)	3,000,000
Transaction value		**330,635,000**

(b) **The custom duties payable**

Item	TZS
Deductive value	402,000,000
Import duty (20% x 402,000,000)	80,400,000
Excise duty (402,000,000 + 80,400,000) x 5%	24,120,000
VAT (18% [402,000,000 + 80,400,000 + 24,120,000])	91,173,600
TOTAL DUTIES (80,400,000 + 24,120,000 + 91,173,600)	**195,693,600**

Note:

- The actual transaction value of goods cannot be used because the importer has interests in the company of the exporter. There is no proof that the transaction took place at arm length. Since we are not provided with transaction value of identical or similar goods, a deductive valuation method has been used for tax calculation.

- The value Added Tax (VAT) is implied at the statutory rate of 18%.

(c) **Distribution of the proceeds**

Item	TZS
Proceeds	320,000,000
Order of payment	
Duties	102,000,000
Balance	**218,000,000**
Removal and sales expenses	2,600,000
Balance	**215,400,000**
Rent and Charges	8,800,000
Balance	**206,600,000**
Port charges	4,500,000
Balance	**202,100,000**
Freight charges	3,000,000
Balance	**199,100,000**

(d) **To whom the balance, if any, is supposed to be paid to, assuming the terms of importation of the goods imported were breached**

- According to Section 42 (5) of the East Africa Custom Management Act, 2004, when there is a balance after the above payments, the balance should go to the custom revenues if the goods were prohibited or restricted goods which their terms were breached.
- For this case, used automobile batteries are categorized as restricted goods therefore the balance of the proceeds will go to the custom revenue.

ANSWER 6

(a) **Reasons**

(i) Enables entities to plan when to undertake the work on their tax assessment and to accommodate the cash flow impact.

(ii) Enables the tax authorities to plan their work and for governments to prepare their budgets more easily.

(iii) Provides reference points for the tax authorities to enforce disclosure and payment of tax and to determine the amounts of any penalties that may arise.

(iv) Prevent entities from being tempted to spend personal income tax and social security contributions deducted at source from employees pay. The longer monies remain uncollected, the greater the risk that employers will use the funds for other purposes.

(b) **To compute the amount for each installment**

(i) The amount of first installment is

$$\frac{13{,}000{,}000 - 1{,}000{,}000}{4} = \frac{Shs.12{,}000{,}000}{4} = Tshs.3{,}000{,}000$$

(ii) The amount of 2nd installment is

$$\frac{13{,}000{,}000 - (3{,}000{,}000 + 1{,}000{,}000)}{3} = Tshs.3{,}000{,}000$$

(iii) The amount of 3rd installment is

$$\frac{13{,}000{,}000 - (3{,}000{,}000 + 3{,}000{,}000 + 1{,}000{,}000)}{2} = Tshs.3{,}000{,}000$$

(iv) The amount of 4th installment is

$$\frac{13{,}000{,}000 - (3{,}000{,}000 + 3{,}000{,}000 + 3{,}000{,}000 + 1{,}000{,}000)}{1} = Tshs.3{,}000{,}000$$

ANSWER 7

(a) Roles of Public Finance in a country's economy.

(i) Ensuring economic and financial stability
Public Finance is used to ensure economic and financial stability in an economy. Economic stability is the absence of excessive fluctuations in the economy, whereas financial stability can be achieved by efficient allocation of resources by appropriate policy making for example any increase in direct taxes will reduce the money available with the people to purchase goods and services and will, in turn, help to reduce inflation. Public finance helps to reduce the economic imbalance on account of unequal distribution of income and wealth among the public.

(ii) Optimum utilization of resources:
Public finance ensures optimum utilization of scarce resources by adopting suitable monetary policies.

(iii) Effective tool to tackle unemployment:
Public finance is an effective tool to tackle unemployment for example the government sets up fiscal policies which increase employment opportunities.

(iv) Capital formation public finance involves:

Providing infrastructure like railways, roadways improved transportation etc. this kind of capital expenditure in turn ensures increase in capital formation which brings about long term benefits to the public in general.

(v) Improved income and service of economy:
Public finance involves raising funds from the public. Furthermore, investments in such funds is sometimes linked to a reduction in the amount of tax paid by the general public. This helps in increasing the income and savings of an economy thereby helping in its development.

(b) Primary functions of a government relating to the public finance

(i) Providing basic utility services and promoting social and economic development
The government is mainly engaged in providing public utility services like electricity, telephone, roads and high ways, transportation facilities etc. to the public such services are provided at economical rates so that these can be veiled by common man. The government generally establishes its own monopoly over the supply of such services, with a view to avoid consumer exploitation. In providing of such services the government invests in social and economic capital.

(ii) Encouraging capital formation
Industrialization is the key to development of an economy. This is brought about by investing in heavy infrastructure such as machinery and tools, chemicals, iron and steel. Such investments carry high risks and the return can be gained only in the long run. Therefore the private sector rarely makes investments. Thus it becomes the responsibility of

the government to make such investments in these sectors which ultimately enables the economy to improve its capital formation.

(iii) Complementing private investment
The private sector also invests in industrial goods. However, whenever there is insufficient investment by the private sector, the government steps in and makes good the shortage. This ensures a balanced development of the economy with the government investing in less profitable sectors or back ward areas where private investment is not forthcoming.

(iv) Providing an environment conducive to development
The government encourages private investment in areas of economic development by setting up basic industries and providing financial assistance by promoting the development of banks.

(v) Conserving and efficiency utilizing natural resources
Economic development depends on the efficient and effective utilisation of its natural resources like oil, minerals acquatic life and forestry. Many economies especially the developed and developing economies are often faced with under utilization as well as inefficient utilization of its natural resources. The government therefore intervenes as well as conserve the natural resources.

SUGGESTED SOLUTIONS
B5 – PERFORMANCE MANAGEMENT
MAY 2015

ANSWER 1
(a)
Require capacity = (4,000 x 2.5) = (2000 x 7.5) + (1500 x 5)
= 32,500 sq meters

Available capacity = 20,000
Shortage = 12,500 sq. meters

Square meters: Chair = 5,000/2,000 = 2.5
Bench = 15,000/2,000 = 7.5
Table = 10,000/2,000 = 5

	Chair	Bench	Table
SP/U	20,000	50,000	40,000
VC/U	12,000	32,500	24,000
CM/U	8,000	17,500	16,000
Sq meter/unit	2.5	7.5	5
Cm/sq. meter	3,200	2,333.33	3,200
Rank	1	3	2

Order of Product Plan		**Sq. meters**	**Contribution**
Chair – 4,000 units x 2.5	=	10,000 x 3,200 =	32m
Tables – 1,500 units x 5	=	7,500 x 3,200=	24m
Benches – 333 units x 7.5	=	2,500 x 333.33 =	5,833,328
	Available	20,000 Cm	61,833,328
		Less fixed costs	54,000,000
		Net profit	7,833,328

(b) Note: Demand for chairs and tables is satisfied but any additional timber would be utilized to manufactures benches.

∴ Maximum price = 2333 + 2,000 = 4,333/=

i.e. Each sq. meter used on a bench contributes Tshs 2,333 after charging the present cost
of timber (Tshs2,000 per sq.)

ANSWER 2

Process 2 creates a bottleneck production because available hours are less than the required hours.

PRODUCT	ATUPE	BIBI	CHEMA
Contribution per batch	$\frac{6,600,000}{2 \text{ hours}}$ = Tsh3,300,000	$\frac{2,200,000}{2 \text{ hours}}$ =Tsh1,100,000	$\frac{2,300,000}{1 \text{ hour}}$ =Tsh2,300,000
Allocation priority/Ranking	1	3	2

PRODUCTION PLAN

ALLOCATION	HOURS	PRODUCTION PLAN		
		ATUPE	BIBI	CHEMA
Hours available in Process 2	1,120			
Less hours allocated to ATUPE	600	300 batches		
Balance of hours available	520			
Less: hours allocated to CHEMA	400			400 bathes
Balance for BIBI @ unit 2 hours	120		60 batches	

Therefore, the business will be able to fulfil demand for ATUPE and CHEMA. Because process 2 constraints, the business will produce only 60 batches for BIBI instead of 200 batches demanded by the market.

ANSWER 3

(a)

(i) The transfer price of TZS 750,000 proposed by the IT division is based on cost plus 150% from which it can be deduced that the total cost of a consulting day is (100/250) x TZS750,000 = TZS300,000. This comprises TZS240,000 (80%) variable cost and TZS 60,000 (20%) fixed cost.

In this instance the transfer price should be set at marginal costs plus opportunity cost. It is assumed in this situation that transferring internally would result in the IT division having a lost contribution of TZS 750,000 – TZS 240,000 = TZS510,000 per consulting day. The marginal cost of the transfer of services to the HR division is **TZS190,000** (TZS240,000 external variable costs leas **TZS50,000** saving due to use of internal video-conferencing equipment). Adding the opportunity cost of TZS510,000 gives a **transfer price of TZS700,000 per consulting day.**

This is equivalent to using market price as a basis for transfer pricing where the transfer price is set at the external market price (**TZS750,000)** less any costs avoided **(TZS50,000)** by transferring internally.

(ii) There is in effect no external market available for one of the required pairs of consultants within the IT division and therefore opportunity cost will not apply and **transfers should be made at the variable** cost per consulting day of **TZS190,000.**

The other pair of consultants, who would otherwise be 100% utilised in providing consulting services to external clients, should be charged at a rate of **TZS700,000** per day which represents marginal cost plus opportunity cost.

(iii) The lost contribution from the major client amounts to TZS264,000,000/(2 x 240) = TZS550,000 less variable costs of TZS240,000 = TZS310,000 per consulting day. Thus, in this instance the transfer price should be the contribution foregone of TZS310,000 plus internal variable costs of **TZS190,000** making a total of TZS500,000 per consulting day.

(b) Negotiated transfer prices suffer from the following limitations:

- The transfer price which is the final outcome of negotiations may not be close to the transfer price that would be optimal for the organisation as a whole since it can be dependent on the negotiating skills and bargaining powers of individual managers.
- They can lead to conflict between divisions which may necessitate the intervention of top management to mediate.
- The measure of divisional profitability can be dependent on the negotiating skills of managers who may have unequal bargaining power.
- They can be time-consuming for the managers involved, particularly where large numbers of transactions are involved.
- It is a subjective way of determining transfer pricing.
- The outcome may not be optimal thus necessitating intervention by top management.

ANSWER 4

(a) Variances

Raw Material Price Variance

Raw Material Price Variance			
Type	Actual Price	Standard Price	[Actual Price-Standard price] x Actual Quanty
Type A	Tshs 1.7	Tshs 2	[1.7-2] x 8800 = 2,640F
Type B	Tsh 3	Tsh 3	NIL
Type C	Tshs 4	Tshs 4	NIL
Total Material Price Variance			Tshs 2,640F

Material Mix Variance

	Standard input	Weight	Actual Quantity In Actual Mix	Actual Quantity in Standard Mix		Standard Price per Kg	[AQ in actual mix-AQ in standard mix] x standard price per Kg
Type A	25	20%	8800	20%x40000= 8000		2	[8800-8000]x2=1,600U
Type B	60	48%	19200	48% x40000= 19200		3	NIL
Type C	40	32%	12000	32%x40000= 12800		4	[12,000-12,800]x4= 3,200F
Total	**125**	**100%**	**40000**	**40000**			**1,600F**

Material Yield Variance

Actual material used = 40,000 Kgs

Workings for material yield variance.

	Actual Input at Standard Mix at Standard costl 40,000 kg	Standard Impact based on output at Standard Mix at Standard Cost		
Mix	(1)	$\frac{33000}{0.8} = 41{,}250kg$		Variance
			(3)	(2 – 1)
A	20% x 40,000 = 8,000 kg	41,250 x 20% = 825 kg	250F@2 =	500F
B	40% x 40,000 = 19,200 kg	41,250 x 48% = 19,800 kg	600F@3 =	1,800F
C	32% x 40,000 = 12,800 kg	41,250 x 32% = 13,200kg	400F @4 =	1,600F
		Total Variance		3,900F

Sales Variances

Quantity A 33,000 kg A 33,300 kg S 50,000

Margin

A = Z	S = 2.1	S = 2.1
66,000	69,300	105,000

3300F	35,700F
Sales Price Variance	Sales Volume Variance

(b) **Sales Price and Volume Variances**

Sales volume variance (SVV)

Sales Volume Variance			
Actual Quantity AQ	Budgeted Quantity BQ	Standard contribution per Kg (SCMU)	[AQ-BQ]x SCMU
3300Kg	50000kgs	2.1 Tshs	SVV=[3300-50000]x2.1=35,700U

Sales price variance (SPV)

Sales Volume Variance			
Actual Price (AP)	Budgeted Price (BP)	Actual Quantity (AQ)	[AP-BP]x AQ
5.9 Tshs	6 Tshs	33000 Kgs	SPV=[5.9-6]x33000=**3,300U**

ANSWER 5

(a)

(i) An annual budgeting system is a system of preparing a set of budgets for a 12 month period, usually coinciding with the financial year of the company. A rolling budget system is a system of budgeting that is continuous. Once the budget has been prepared it is added to each month, or perhaps quarterly, thus ensuring that a budget always exists for the next 12 months and possibly for longer depending on the company's budgeting policy.

One of the key differences between these two systems is that, when a rolling budget system is being used, managers see budgeting as part of their ongoing planning and decision making processes, rather than as a separate exercise which is used to measure their performance.

In some organisations, where rolling budgets are used, the unexpired portion of the budget is also updated monthly or quarterly to reflect any changes in operational circumstances since the budget was originally prepared.

(ii) The manager of the Southern depot has raised two specific issues with the current annual budgeting system.

One of these is his argument that the budgets become out of date due to changing operational circumstances. Whether or not rolling budgets provide a solution to this issue depends on the organisation's philosophy of the use of rolling budgets. If the view is that they should be used to plan for future budget years so as to ensure that managers can make better decisions for those years, but not change the current year's budget, then a rolling budget will not be the solution to this problem. However, the manager can now effect changes to future budget periods, as yet unapproved, in the light of those circumstances.

If the rolling budget system allows revision of the remaining part of the plan for the current budget year then their use will solve the argument that the original budget has become out of date.

It is important to consider the use of the budget. There two main uses: operational control and strategic decision making. From an operational control perspective care must be taken to ensure that a rolling budget does not become a vehicle for eliminating variances caused by actual performance. Once a budget has been set and approved, then any unexpected changes to circumstances should be reported via the budgetary control system using variance analysis including planning variances as appropriate.
From a strategic decision making perspective, it is important to use the rolling budget process to determine whether strategies need to be revised in the light of the current operational circumstances.

The second of the manager's arguments relates to the lack of authority for actions in respect of future periods. The rolling budget method does have a role here because as it is continuously being updated then if each update is approved by the Board of Directors, managers will always have authority to carry out decisions in line with the approved budget for the next 12 months or more. This is a weakness of the annual budgeting system, especially towards the end of the current year when next year's budget is still to be approved.

Managers can often find that they do not have authority for decisions which will impact on the early part of the next budget year until that year has almost started.

If DW were to introduce a system of rolling budgets then this would enable the depot manager to plan and improve their decisions, for example with regard to recruiting and training employees, and to evaluate alternative operating methods and possible capital investments based on the budgets that have been agreed for the next 12 months or more.

(b) Cost driver rates:
Accounts preparation and advice 580,000,000/18,000 hours = TZS 32,220 per hour
Requesting missing information 30,000,000/250 times = TZS 120,000 per request
Issuing fee payment reminders 15,000,000/400 times = TZS 37,500 per reminder
Holding client meetings 60,000,000/250 meetings = TZS 240,000 per meeting
Travelling to client 40,000,000/10,000 km = TZS 4,000 per km

Client costs:

	Client A	B	C
	TZS '000'	TZS '000'	TZS '000'
Accounts preparation and advice	32,222	8,050	10,955
Requesting missing information	480	1,200	720
Issuing fee payment reminders	75	300	375
Holding client meetings	960	240	480
Travelling to clients	600	2400	0
Total costs	34337	12,195	12,530
Total costs on original basis*	40,280	10,070	13,695

The company adds 20% mark-up cost to get the charges to customers. When you add mark-up you get:

Client fees – new basis	41,204	14,634	15,036
Client – original basis	48,336	12,084	16,434
Increase/(Decrease)	(7,132)	2,550	(1,398)

*TZS725,000,000/18,000 hours = TZS40,280 per hour

ANSWER 6

(a)

(i) Tracing stock costs in a traditional way is justified when levels of raw materials, work in process and finished goods are significant. This occurs mainly when a business produces products in anticipation of unknown demand. In such circumstances, stocks for stocks for raw materials, work in process and finished goods become significant. Because of this, management desires detailed information about the levels of raw materials work in process, finished goods.

(ii) When a business uses Just in Time manufacturing, it reduces stock levels, defective output spoilage and stock movement. This justifies the scaling down the accounting routines that are associated with them. In these circumstances, management has no need for stock information that justifies the cost of generating it. Instead, stock recording is done only when finished goods are transferred to the warehouse or when they are sold.

When Just in Time is used, production runs are initiated by customer orders. In this way, production batches are small and these do not cause stock piling for raw materials, work in process and finished goods. The following are aspects of batch costing that go along with back flush costing:

1. Each batch processed is small and it may desire only the differentiation of standard products in order to suit the specifications of customers' orders. In these circumstances, batch costing is used because the costs of each batch processed are separately accounted for.

2. Each batch processed consists of many similar units that pass through a series of standardized operations where common manufacturing costs are added. Because of this, most costs are traced to a batch as direct costs.

3. Labour cost charged to a batch is not nalysed into direct and indirect labour since a batch may not influence meaningful labor cost. In this way, labour forms part of conversion costs that are allocated to a batch using a pre-determined rate.

(b) Businesses operating activities create value, which is reported as its revenue. The process of creating this value provides advantage to other individuals besides those who invest capital in the business. Individuals who benefit from the value created by the business are the employees who receive compensation in exchange for labour service they provide, the suppliers of goods and services that the business uses as expense, the public that benefits from the taxes that are levied on the business, and the investors who receive interest and dividends that the business pays. A surplus that a business retain for growth if referred to as **Economic Value Added**. This benefits to shareholders because it is available for business growth increases shareholders' value.

Because debtors are stakeholders as well in the business operating results, the profit that is use for performance evaluation is net of interest expense. In addition, weighted average cost of capital after tax is determined by including the cost of debt calculated after tax as follows:

(i) Cost of debentures after tax $\frac{1(1-T)}{P_0}$

Where T = Tax rate and I is interest expense, and P_0 is the market Value of the debenture.

This is unlike in the case of Residual Income based evaluation where profit before tax is used and cost of capital before tax is determined by including the cost of debt calculated before tax as follows:

Cost of debentures before tax $\frac{\mathrm{I}}{P_0}$

While what has been said is true, the business-sustained growth is of interest to every individual who has a stake in the value that the business creates especially the investors. This growth is possible only if the business retains a surplus after it has rewarded appropriately all interest parties mentioned. This is why management becomes interested in the Economic Value Added component for evaluation of profit centre performance.

ANSWER 7

The costs/benefits of closing on 30 November 2015 instead of closing on 30 June, 2015 are:

	TSHS.'000'	TZS.'000'
payment to XYZ Ltd avoided (5 months @ TZS. 65,000,000)		325,000.00
Salaries and wages cost (notes 1)		(101,500.00)
Printing materials (Notes 2)		(147,000.00)
Distribution materials (Notes 3)		
Occupancy costs:		
Printing (Notes 4)	17,212.50	
Distribution (notes 5)	2,175.00	(19,387.50)
Loss of sub-letting income (5 months @ TZS.2,500,000)		(12,500.00)
Additional loss on sale of plant (note 6)		(2,000.00)
Additional loss on sale of vehicles (TZS. 48,000,000-TZS 44,000,000)		(4,000.00)
Net benefit of closing on 30 November		

Notes:

1. The total salaries equal TZS. 22,000,000 (TZS. 18,000,000 + TZS. 4,000,000) but two staff will be retained so the net saving of closing on 30 June is reduced by their salaries (TZS. 3,000,000 per month). If closure does not occur until November, the vacancy in the publishing department will need to be filled (at TZS. 1,300,000 per month) until closure in November when the transfer occurs. The redundancy pay will arise whenever closure occurs and is therefore irrelevant.

   Therefore, net Salary and wages cost = (5 months @ (TZS. 18,000,000 +TZS. 4,000,000 – TZS. 3,000,000 + 1,300,000) = TZS. 101,500,000.

2. The future cash outflow on printing materials is TZS. 31,000,000 per month for five months less the TZS. 18,000,000 held in stock. However, the opportunity to sell the stock is lost, therefore, there is an additional cost of TZS. 10,000,000. Printing material costs = (5 months @ TZS. 31,000,000) – TZS. 18,000,000 + TZS. 10,000,000) = TZS 147,000,000.

3. If the department is closed then the options are (from note (ii) in the question):
   (i) Accept both deliveries, pay for them and sell the goods to XYZ Ltd: (2 x TZS.
   5,000,000) – (2 x TZS. 380,000) = TZS. 9,240,000 net cost.

   (ii) Accept the July delivery, pay for it, sell it to XYZ Ltd. and pay the cancellation cost for August: (TZS. 5,000,000 – TZS. 380,000) + TZS. 100,000 = TZS. 4,720,000 net cost.

(iii) Cancel both deliveries at a net cost of TZS. 300,000.
The lowest cost option would be selected if closure occurred; therefore this is a benefit of continuing to November. The distribution material costs to November are (5 months @ TZS. 1,100,000) – TZS. 300,000 = TZS. 5,200,000.

4. Attributable costs are [(TZS. 8,500,000 X 30%) + (TZS. 8,500,000 X 70% X 15%)] x 5 months = TZS. 17,212,500.

5. Attributable costs are [(TZS. 1,200,000 x 25%) + (TZS. 1,200 x 75% x 15%)] x 5 months = TZS. 2,175,000.

SUGGESTED SOLUTIONS
B6 – MANAGEMENT, GOVERNANCE AND ETHICS
MAY 2015

ANSWER 1
(a)

(i) Mission statement is written declaration of an organization's core purpose and focus that normally remains unchanged over time. Properly crafted mission statements (1) serve as filters to separate what is important from what is not, (2) clearly state which markets will be served and how, and (3) communicate a sense of intended direction to the entire organization.

A mission is different from a vision in that the former is the cause and the latter is the effect; a mission is something to be accomplished whereas a vision is something to be pursued for that accomplishment.

(ii) Candidate has to write one example of a mission statement by being guided with the following questions:

- What the company does?
- For whom does the industry work for?
- Does it serve its clients in the required way?
- What is the purpose of the company?
- Why the business has been started?
- What image does the business want to convey?

(b) The influence of external environment factors into business organization

(i) Economic conditions
Prevailing economic conditions of the nation will have an effect on the spending patterns of citizens. Increases in interest rates and/or a high level of unemployment will depress consumption of non-essential goods and services. For example, when people experience financial hardship, they will spend much less on sport and recreation, holidays, new cars and luxury goods. Economic conditions are global as well as national, and when there is a global financial crisis as in 2007, changes in the external environment can be dramatic.

(ii) Market (competition)
The strength of business competition is a constantly changing factor in the external business environment. Not only will competitors come and go, but they will also change marketing strategies, product lines and prices. Often such changes are not heralded and business managers must be alert as to what competitors are doing.

(iii) Technology

Technological change has been rapid in the last 50 years and is a factor in the external environment that constantly exerts pressure on the business or organization. If businesses do not adapt sufficiently quickly to technological change, they risk losing market share. It's not just that technological change affects the design of products, but even the delivery of services can change.

(iv) Climate Change

Climate change is an insidious threat because the pace of change may be recognizable only if considered on a decade-by-decade basis. The effect of climate change will not fall equally on all nations and all businesses. Businesses that depend directly on a good supply of water e.g. agriculture, field sports will be adversely effected if climate change results in reduced rainfall. However the flow on affects of drought will eventually work their way through to all businesses in the effected community.

(v) Legal

Taxation is one of most obvious changes in law through legislation. Sometimes taxation changes occur overnight with little warning and sometimes there is plenty of time for the business to prepare. Other law changes that commonly affect business include Workplace Health and Safety, Industrial Relations, Consumer Protection and Environmental Law.

(vi) Media

The media is undergoing rapid and significant change. The main driver of this change is technology and the rise of the internet. Newspapers once carried many pages of job adverts but now this business is conducted by online recruitment companies such as Seek.

(vii) Political

Like law, changes in government policy can be well notified and discussed, or without warning. As an example of how government policy has an effect, is that many organisations depend on government financial assistance. When there is a change of government, such funding assistance can disappear in a short space of time.

(viii) Demographic

There is constant change in the make-up of the population. Some of these changes include an increasing proportion of elderly citizens, increasing number of two-income families, the age at which people marry is increasing, increasing ethnic diversity, suburbs which were once dominated by young families now have few. These demographic changes can have a significant effect locally. For example, a sport club which once prospered can begin to decline as the local area has less and less children.

(c) Five forces as narrated by Michael Porter:

(i) Threat of potential entrants
Profitable markets that yield high returns will attract new firms. This results in many new entrants, which eventually will decrease profitability for all firms in the industry.

(ii) Threat of substituted products or services
The existence of products outside of the realm of the common product boundaries increases the propensity of customers to switch to alternatives.

(iii) Bargaining power of customers (buyers).
The bargaining power of customer is also described as the market of outputs: the ability of customers to put the firm under pressure, which also affects the customers' sensitivity to price changes.

(iv) Bargaining power of suppliers
The bargaining power of suppliers is also described as the market of inputs. Suppliers of raw materials, components, labour and service to the firm can be a source of power over the firm where there are few substitutes.

(v) Intensity of competitive rivalry: for most industries the intensity of competitive rivalry is the major determinant of the competitive of the industry.

ANSWER 2

(a)

(i) **Advantages of Budgeting:**

- Budgeting compels and motivates management to make an early and timely study of its problems. If generates a sense of caution and care, and adequate study among managers before decisions are made by them.

- Budgeting provides a valuable means of controlling income and expenditure of a business as it is a plan for spending

- Budgeting provides a tool through which managerial policies and goals are periodically evaluated, tested and established as guidelines for the entire organization.

- Budgeting helps in directing capital and other resources into the most profitable channels.

- Budgeting coordinates and correlates all business activities. It enables management to decentralize responsibility without losing control of the business.

- It provides a norm, basis or yardstick for measuring performance of departments and individuals working in organizations.

- Budgeting encourages productive competition, provides incentive to perform efficiently and gives a sense of purpose to each individual in the organization).

- Budgeting, if executed in nearly every enterprise, helps the total national economy by providing stability of employment, economic use of resources and effective prevention of waste.

(ii) **Limitations of Budgeting**

- Planning, budgeting or forecasting is not an exact science; it uses approximations and judgment which may not be hundred percent accurate. At best a budget is an estimate no one knows precisely what will happen in future.

- The success and utility of budgeting depends on the cooperation and participation of all members of management. Many time budgeting has failed because executive management has paid only lip service to its execution.

- The establishment of a budgeting process takes time. Also, sometimes too much is expected from a budget and in case expectations are not fulfilled, the blame is put on the budget.

- A budget is only a toll and does not eliminate nor take over the place of management. Executives generally feel circled in by a budget and its related figures. They fail to understand that budget is meant to provide detailed information, goals and targets which may help in achieving the company objectives.

- Excessive emphasis on budgeting may result in attempts by lower level management and employees to buck the system by providing inaccurate estimates of future costs and revenues.

(b) Factors to consider when deciding on the span of control

(i) Job complexity: Subordinate jobs that are complex, ambiguous, dynamic or otherwise complicated will likely require more management involvement and a narrower span of management.

(ii) Similarity of subordinate jobs: The more similar and routine the tasks that subordinates are performing, the easier it is for a manager to supervise employees and the wider the span of management that will likely be effective.

(iii) Physical proximity of subordinates: The more geographically dispersed a group of subordinates the more difficult it is for a manager to be in regular contact with them and the fewer employees a manager could reasonably oversee, resulting in a narrower span of management.

(iv) Abilities of employees: Managers who supervise employees that lack ability, motivation, or confidence will have to spend more time with each employee. The result will be that the manager cannot supervise many employees and would be most effective with a narrower span of management.

(v) Ability of the manager: Some managers are better organized, better at explaining things to subordinates, and more efficient in performing their jobs. Such managers can function effectively with a wider span of management than a less skilled manager.

(vi) Technology: Cell phones, email, and other forms of technology that facilitate communication and the exchange of information make it possible for managers to increase their spans of management over managers who do not have access to or who are unable to use the technology.

ANSWER 3

(a) Reasons for Diversification

(i) Economies of scope
- Sharing activities
- Transferring core competencies

(ii) Market Power
- Blocking competitors through multi-point competition
- Vertical integration

(iii) Financial economies (unrelated diversification)
- Efficient internal capital allocation
- Business restructuring

(iv) Tax laws

(v) Uncertain future cash flows

(vi) Risk reduction for firm

(vii) Tangible resources

(viii) Intangible resources

(ix) Diversifying managerial employment risk

(x) Increasing managerial compensation

(b)

(i) Reasons for Corporate Social Responsibility

- Win new business
- Increase customer retention
- Develop and enhance relationships with customers, suppliers and networks
- Attract, retain and maintain a happy workforce and be an employer of choice
- Save money on energy and operating costs and manage risk
- Differentiate yourself from your competitors
- Generate innovation and learning and enhance your influence
- Improve your business reputation and standing
- Provide access to investment and funding opportunities
- Generate positive publicity and media opportunities due to media interest in ethical business activities.

(ii) The major arguments against the assumption of social responsibilities by business are:

- Violation of profit maximization: This is the essence of the classical viewpoint
  Business is most socially responsible when it attends strictly to its economic interests and leaves other activities to other institutions.
- Dilution of purpose: The pursuit of social goals dilutes business's primary purpose: economic productivity. Society may suffer as both economic and social goals are poorly accomplished.
- Costs: Many socially responsible activities do not pay their own way. Someone has to pay these costs. Business is already one of the most powerful institutions in our society. If it pursued social goals, it would have even more power. Society has given business enough power.
- Lack of skills: The outlook and abilities of business leaders are oriented primarily toward economies. Business people are poorly qualified to cope with social issues.
- Lack of accountability: Political representatives pursue social goals and are held accountable for their actions. Such is not the case with business leaders. There are no direct lines of social accountability from the business sector to the public.
- Lack of broad public support: There is no broad mandate from society for business to become involved in social issues.

ANSWER 4

(a)

(i) **Advantages of e-business**

- Quicker and easier communications.
- Strengthened marketing capabilities and reach.
- Increased hours of operation (a web-site provides 24-hour seven day information to existing and potential customers).
- Access to broader information through research.
- Reducing the cost of doing business by lowering transaction costs and increasing efficient methods for payment, such as using online banking and reducing stationery and postage costs.
- The opportunities to adopt new business models and develop tailored customer support.

(ii) **Limitations of e-business**

- The companies or the businesses who are selling the products are not able to communicate with the customer face to face. Due to this they are not able to get the feedbacks about the products so that they may improvise on the products.
- Another limitation with E-commerce is that you are not able to touch and check quality of a product before buying it.
- Credit Card security is a serious issue. People who are carrying out a transaction over the Internet are worried about their credit card security. Customers are still worried and fear about their online Credit Card orders
- The next one is a technological limitation that the cost involved with bandwidth and server is too high.
- Another limitation is that the people are becoming more and more isolated without having a contact with other people. Due to this people are facing difficulty interacting with people.

(b) **Sources of internal information**

(i) Financial information is information related to the performance and profit and loss of the company.

(ii) Personnel information: information held by the company on their employees.

(iii) Marketing information: Is used by the marketing team to identify what products or services offered by the business are most successful.

(iv) Purchasing information: is collected by the purchasing department who are involved with buying of all the products needed to run the business

(v) Sales information: Just like the purchasing information sales information needs to be monitored based on the product or services offered by the company.

(vi) Manufacturing information: information about the cost of manufacturing goods within the company.

(vii) Administrating information: this links very much with personnel information but also involves communicating with external sources and storing information on customers.

ANSWER 5

(a) The Risk Manager is responsible to Senior Management for the following functions:

(i) To identify and quantify the organization's exposures to accidental loss.

(ii) To adopt proper financial protection measures through risk transfer (to outside parties), risk avoidance, and risk retention programs.

(iii) To develop and update a complete system for recording, monitoring, and communicating the organization's Risk Management program components and costs to the executive staff and others as necessary.

(iv) To design master insurance programs and self-insurance programs including the preparation of underwriting specifications.

(v) Securing and maintaining adequate insurance coverage at the most reasonable cost.

(vi) To determine the most cost-effective way to construct, refurbish, or improve the loss protection system of any facility leased, rented, purchased, or constructed by company.

(vii) To develop and implement loss prevention/loss retention programs.

(viii) To actively participate on all contract negotiations involving insurance, indemnity, or other pure risk assumptions or provision *prior* to the execution of the contracts. To establish indemnity and insurance standards for standard contract forms.

(ix) To create and publish guidelines on the handling of all property and liability claims involving the organization.

(x) To manage claims for insured and uninsured losses.

(xi) To comply with local insurance laws.

(xii) To select and manage insurance brokerage representatives, insurance carriers and other necessary risk management services providers.

(xiii) To establish deductible levels

(xiv) To locate insurance premiums.

(xv) To issue bonds and certificates as necessary.

(xvi) To establish Risk Management policies and procedures.

(b) (i) Benefits of succession planning

1. It serves as contingency planning and keeps the organization well prepared for any sudden attrition that may happen and reduces the impact of losing key employees to a great extent.
2. By insisting on succession planning, managers get to identify various skill-sets among the team members and their strengths come to light.
3. Also, employees who are identified as successors based on the skill-sets they possess can be groomed well to handle the relevant positions, and any skill-set that is lacking in the employee can be developed by prodding appropriate training and opportunities
4. Employees get to have a well-defined road map of their career and it serves as a motivation factor for them to perform even better.
5. Employees who get understand that their organization has future plans for them, will tend to stay with the organization for longer time.
6. Internal employees already have a good understanding of the organization and its goals. Thus, it saves a considerable amount of time and cost for the organization in hiring and inducting new candidates for these positions.
7. Overall, it creates a very positive atmosphere within the organization and leaves employees feeling extremely satisfied in terms of career progress and highly motivated.

(ii) Disadvantages of Succession Plan

1. Hinder Recruitment of new talents entrant in the organization.
2. It can create enemity among the organization top management.
3. Inappropriate appointment especially when done quickly.
4. It can result to employees turnover especially when the successor is not acceptable by other employees.
5. It can demotivate some of the top managers as they might be expected to lead the organization.
6. Result to company rigidity in the sense that if the former CEO was prioritizing some issues even the successor will follow the system hence not allow new issues to interfere the organization.
7. It can result to family conflict incase the organization is family owned.

ANSWER 6

(a) How to promote ethical codes in a work place

(i) **Train Employees** You can't expect your staff to act ethically in accordance with your company's code of ethics if they don't know what that code is or why it's important. Hold regular sessions on ethics and how to approach ethical dilemmas among staff. The more training and resources you provide, and the greater emphasis you place on being ethical and acting accordingly, the more your staff understands exactly what you expect in the office.

(ii) **Reward Ethical Behavior**
Far too often, companies simply expect ethical behavior; however, if you want to promote this as a prominent behavior among staff, then you need to show and prove, so to speak. Provide rewards for good ethical behavior; for example, if you have an employee that goes above and beyond to put her personal interests aside to always do what is best for her clients, that is considered ethical behavior and she should be rewarded and held up as an example for others to strive to do the same. The more you reward employees for sound ethical decisions, the more likely the masses will follow suit.

(iii) **Lead by Example**
Expect more of your management team; employees generally follow company examples set forth for them by management employees. Hold your managers to a higher ethical standard so that they are credible when they communicate expectations to their staffers to do the same. Challenge management staff to hold regular discussions with employees to work through potential ethical issues that may come up and find ways to brainstorm through them as a team. If everyone is on the same page, it is more likely that the team as a whole will adopt the same types of ethical behaviors.

(iv) **Consider Work-Life Balance**
Employees are most likely to make good ethical decisions at work when they have a better sense of work-life balance. Pay attention to signs of burnout or discontent among staff, and take steps to address these types of issues when they present themselves.

(v) **Expectations**
Ensure that your company states its values in the employee handbook and that values are talked about and implemented in everyday business matters by all employees in a supervisory capacity. These values are self-control, wisdom, justice, transcendence, kindness and integrity. For example, the value of self-control can result in the behavior or doing what it right regardless of personal motivations.

(vi) **Policies**
Sometimes implementing a policy to prevent unethical behavior is the best option. For example, if workers regularly use the copy machine to make personal copies or steal supplies from the storeroom, you can require a code for the copier and ask the secretary to distribute office supplies as requested.

(b) Key competencies required by an accountant

(i) Technical skills. Collecting, storing and processing information to be shared with other stakeholders. Tasks include financial accounting and reporting; cost accounting; treasure management; and tax strategy, planning and compliance

(ii) Business skills. Using knowledge of the organization and the organization's business environment to turn data into insight. Tasks include strategy, process and project management, and macroeconomic analysis.

(iii) People skills. Used to influence decisions, actions and behaviors of decision-makers and other stakeholders. Tasks include negotiating, decision-making, and collaborating or partnering.

(iv) Leadership skills. These skills come in three types – peer, functional and strategic. Tasks include team building, managing change and driving performance.

Other competencies

(i) Integrity
(ii) Objectivity
(iii) Independence
(iv) Confidence

ANSWER 7

(a) Importance of policies in an organization

(i) Employees are provided with information that allows them freedom to carry out their job and make decisions with defined boundaries.

(ii) Employee understand the constraints of their job without using "trial and error" approach as key points are visible in well written policies.

(iii) Policies enable the workforce to clearly understand individual and team responsibilities thus saving time and resources.

(iv) Clearly written policies allow managers to exercise control over the staff.

(v) Policies provide legal protection for both employees and employers.

(b) Measurement to combat corruption

(i) Give better salary in government jobs: Many employees in government positions receive low salary hence they expect to make money by bribery.

(ii) Increase the number of workers: In many offices of the government sector, the work load has gone up drastically but the recruitment of vacancies has declined. This gives an option for delaying the work by officials and expect monetory or other benefits for faster completion.

(iii) Enact laws to dismiss from public service if found to be involved in corruption

(iv) Keep transactions transparent to the citizens/stakeholders.

(v) Put security camera in government offices

(vi) Speed up the work process in government institutions.

(vii) Make media responsible to disclose corrupt practices.

(viii) Verify the selection procedures: Many people compete for government jobs and in the process there are corruption happens in the selection of candidates for the posts.

(ix) Keep inflation low: This is another factor for keeping corruption high and also persistent. Due to rise in prices, any amount of income seems to be insufficient.

(x) Speed up the process of judgment and increase the courts: Many cases of corruption take years to be given verdict hence make people not fear for being corrupt.

(c) Short notes on:

(i) Reputational risk: is the possible loss of the organization’s reputational capital. It is a hidden danger that can pose a threat to the survival of an organization.

(ii) Due deligency: Is the process of systematically researching and verifying the accuracy of a statement. The term originated in the business world, where due deligency is required to validate financial statement. The goal of the process is to ensure that all stakeholders associated with financial endeavor have the information they need to assess risk accordingly.

(iii) Ethical theory of absolutism: Is the view that there will be internally and universally applicable moral principles and that, as a result right and wrong are objective qualities that can rationally determined. Therefore a moral principle could be bribes are unacceptable in all forms.

(iv) Deontologist ethics: under this theory, the means are more important than the ends. Deontologists believe that actions which are right bring about a good state of affairs. It is the normatical ethical position that judges morality of an action based on the action’s adherence to a rule or rules. For this theory action is more important than the quencequences.