THE INSTITUTE OF CHARTERED ACCOUNTANTS
OF NIGERIA

PATHFINDER

MAY 2012 PROFESSIONAL EXAMINATION II

Question Papers

Suggested Solutions

Plus

Examiners' Reports

FOREWORD

This issue of the PATHFINDER is published principally, in response to a growing demand for an aid to:

(i) Candidates preparing to write future examinations of the Institute of Chartered Accountants of Nigeria (ICAN).

(ii) Unsuccessful candidates in the identification of those areas in which they lost marks and need to improve their knowledge and presentation.

(iii) Lecturers and students interested in acquisition of knowledge in the relevant subjects contained herein, and

(iv) The profession; in improving pre-examinations and screening processes, and so the professional performance of candidates.

The answers provided in this publication do not exhaust all possible alternative approaches to solving these questions. Efforts had been made to use the methods, which will save much of the scarce examination time. Also, in order to facilitate teaching, questions may be altered slightly so that some principles or application of them may be more clearly demonstrated.

It is hoped that the suggested answers will prove to be of tremendous assistance to students and those who assist them in their preparations for the Institute's Examinations.

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THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA
PROFESSIONAL EXAMINATION II – MAY 2012
FINANCIAL REPORTING AND ETHICS

Time Allowed – 3 hours

SECTION A: Attempt All Questions

PART I: MULTIPLE-CHOICE QUESTIONS (20 Marks)

Write only the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions:

Use the information below to answer questions 1 to 3*:*

A company's building under construction in 2000 is being financed with ₦8 million debt, ₦6 million of which is a construction loan on the building. The rest is being financed out of the general debt of the company. The company will occupy the building when it is completed. The debt structure of the firm is as follows:

	₦'000
Construction loan at 11%	6,000
Long-term debentures @ 9%	9,000
Long-term redeemable debentures @ 10%	3,000

All the debentures were issued at the same time.

1. Which of the following is the interest payable during the year 2010?

   A. ₦660,000
   B. ₦810,000
   C. ₦1,110,000
   D. ₦1,470,000
   E. ₦1,770,000

2. The capitalised interest cost to be recorded as an asset in the Statement of Financial Position, according to IAS 23 is

   A. ₦300,000
   B. ₦660,000

C. ₦810,000
D. ₦845,000
E. ₦850,000

3. What amount of interest expense should be reported on the Statement of Comprehensive Income?

A. ₦845,000
B. ₦920,000
C. ₦925,000
D. ₦1,117,000
E. ₦1,140,000

4. The types of shares in increasing order of risk are

A. Warrants, deferred shares, ordinary shares, preference shares
B. Deferred shares, ordinary shares, preference shares, warrants
C. Ordinary shares, preference shares, deferred shares, warrants
D. Preference shares, ordinary shares, deferred shares, warrants
E. Preference shares, deferred shares, ordinary shares, warrants

5. The ethical theory that holds that you ought to make your decisions about what is right or wrong on the basis of valid ethical principles, norms or ground rules is known as

A. Meta ethics
B. Descriptive ethics
C. Normative ethics
D. Rule ethics
E. Organisational ethics

6. Any influence, interest or relationship that could cause a professional accountant's judgement to deviate from applying the profession's standards to client's matter is known as

A. Ethical standard
B. Conflict of interest
C. Professional interest code
D. Accounting-interest dilemma
E. Ethical interest

7. The Managing Director of Inheritance Limited convinced the Board of Directors to buy a building that costs ₦25 million to accommodate all the principal staff at Head office. It was later discovered that the house belongs to the uncle of the Managing Director. This is a case of

   A. Third party transaction
   B. Joint owner transaction
   C. Special interest transaction
   D. Related party transaction
   E. Arms length transaction

8. Waylaid Engineering Limited was awarded a road construction project valued at ₦100 million by the Federal government. A sum of ₦20 million was paid as mobilization fee. Three months later, the company submitted an additional bill of ₦40 million. In certifying the bill for payment, the Accountant-General must ascertain the stage of completion through

   A. Valuation and certification method
   B. Percentage of completion method
   C. Value to value method
   D. Cost to cost valuation method
   E. Completed contract method

9. Which of the following is LEAST important to a professional accountant while initiating an informal conflict resolution process?

   A. Relevant facts
   B. Established internal procedures
   C. Established legal procedures
   D. Alternative courses of action
   E. Ethical issues involved

10. The following are circumstances that threaten the ability of a professional accountant in business relationship to perform his/her duties with a degree of professional competence and due care EXCEPT

A. Insufficient time to properly perform or complete the relevant duties
B. Insufficient experience, training and/or education
C. Inadequate resources for the proper performance of the duties
D. Excessive provision of necessary finance
E. Incomplete, restricted or inadequate information

11. The ethical decision making approach which critically considers a company's ground rules, the benefits it produces and its impacts on stakeholders is

A. Moral standard approach
B. Pastin approach
C. Five questions approach
D. Stakeholders impact analysis
E. Ethical analysis

12. A financial adviser is caught furthering his/her own interest at the expense of the client. What makes the financial adviser's action unethical?

A. Greed
B. Selfishness
C. Furtherance of own interest
D. Own interest is the criterion for action
E. Corruption

13. Which of the following does NOT constitute a change of accounting policies?

A. A change in the rate of depreciation
B. The adoption of an accounting policy for a new transaction
C. Conformity to a new standard
D. Change in accounting policy as a result of change in exchange rate
E. Initial adoption of a new accounting policy in recognition of events occurring for the first time

14. Which of the following transactions would increase the net cash flow from operating activities?

A. Collection of an account receivable from the customer
B. Issuance of capital stock for cash at a price above par
C. Purchase of a delivery truck by issuing a note payable
D. Sale of equipment for cash at a gain
E. Payment for cost of goods purchased

15. A parent company does not need to present a consolidated financial statement EXCEPT

A. It is a wholly-owned subsidiary of another entity
B. It is a partially owned subsidiary of another entity
C. Its securities are not publicly traded
D. Its securities are about to be publicly traded
E. It is not in the process of issuing securities in public securities market

16. According to Carroll Archie, corporate social responsibility implies four responsibilities of business to society. These are legal, ethical, economic and

A. Welfare
B. Environmental
C. Organisational
D. Discretionary/philanthropic
E. Statutory

17. According to IFRS 3 (Business Combination), goodwill acquired in a business combination after initial recognition is measured at cost less any accumulated impairment losses. IFRS 3 requires extensive disclosures. These include reconstitution of the carrying amount of goodwill at the beginning and end of the period showing separately all of the following EXCEPT

A. The gross amount and accumulated impairment losses at the beginning of the period
B. Additional goodwill de-recognised during the period
C. Impairment losses recognised during the period
D. Net exchange differences arising during the period
E. The gross amount and accumulated impairment losses at the end of period

18. For a financial instrument to be held to maturity, it must meet several extremely narrow criteria. The entity must have a positive intent and a demonstrated ability to hold the investment to maturity. These conditions can ONLY be met if

A. The entity intends to hold the financial asset for a defined period
B. The entity stands ready to sell the financial asset in response to changes in interest rates or risks liquidity needs and similar factors
C. It does have the financial resources available to continue to finance the investment until maturity

D. It does not have the financial resources available to continue to finance the investment until maturity

E. It is subject to an existing legal or other constraint that could frustrate its intention to hold the financial asset to maturity

19. On 1 January 2010, an entity issued a debt instrument with a coupon rate of 13.5% at a par value of ₦10 million. The directly attributable costs of issue were ₦550,000. The debt instrument is repayable on 31 December 2011 at a premium of ₦1,500,000. What is the total finance cost associated with the debt instrument at repayment date?

    A. ₦4.20 million
    B. ₦4.57 million
    C. ₦4.75 million
    D. ₦2.05 million
    E. ₦3.25 million

20. Departure from the requirements of an IFRS is allowed only in extremely rare circumstances. In such cases, which of the following should NOT be disclosed by the reporting entity?

    A. That management has concluded that the financial statements present fairly the entity's financial position, financial performance and cash flow
    B. That it has complied with the applicable IFRS
    C. The title of the IFRS from which it has departed
    D. The nature and reasons for the departure
    E. The statistical data relating to the departure, for each period presented

PART II: SHORT-ANSWER QUESTIONS (20 MARKS)

Write the answer that best completes each of the following questions/statements:

1. A method of improving the presentation of a company's financial Statements by borrowing on short term with the aim of improving its liquidity at the statement of Financial Position date is called ……………..

2. According to IFRS 8 (operating segments), two or more operating segments may optimally be aggregated into a single segment provided they have similar …………….characteristics.

3. An increase in Earnings Per Share (EPS) resulting from the inclusion of potentially dilutive securities in EPS calculation is referred to as ……………….

4. The process whereby a corporation can and should be evaluated not only in terms of its financial bottom line, but also in terms of its environmental and social/ethical bottom lines is the ………………………

5. The rules and regulations that govern the behaviour of an organisation and its employee, particularly their shared values, beliefs, customs, concepts, ceremonies and rituals are known as ………….

6. The responsibilities of a business to produce goods and services that society needs and wants at a price that can perpetrate the business and satisfy its obligations to investors are ……………

7. A problem, situation or opportunity requiring an individual or organisation to choose among several actions that must be evaluated as right or wrong, ethical or unethical is known as …………….

8. The behaviour of members of an organisation towards customers, suppliers, subordinates, superiors, peers and others is …………

9. Given the need for responsibility to the public, there is a widespread demand on businesses to act ethically while pursuing …………….

10. In financial reporting, the materiality of an item is determined by having recourse to its ……………… and …………….

11. The foundation of the fiduciary relationship between the financial adviser and the client is ……………………….

12. The general ethical theory relevant for calling an accountant to order on the conduct of his/her duties to the profession and public is ………………………..

13. The funding of an entity's operation in such a way that some or all of the finance may not be shown on the company's Statement of Financial Position is …………………….

14. According to IAS 24 (Related party disclosure), ONE of the grounds for which reporting entities are exempted from the disclosure requirements for government related transaction is …………………..

15. According to IFRS 1, what is the date at which the first-time adopter should recognise all assets and liabilities?

16. According to IAS 20 (Accounting for Government Grants and Disclosure of Government Assistance), the system which recognises government grants on a systematic and rational basis over the periods necessary to match them with related costs or directs that grants should not be credited directly to shareholders' interests is called ……………….

17. According to IAS 20 (Accounting for Government Grants and Disclosure Assistance), non-monetary grants are accounted for at both the grant and the assets fair value or as an alternative accounting for using ………………

18. In allocating an impairment loss, the carrying amount of an asset should not be reduced below the highest of its fair value less cost to sell and its …………………

19. The Sarbanes-Oxley Act of 2002 is also known as the ………………………

20. Alasdair Macintyre's position that we should concentrate on what sort of people we should be rather than the things we should do is an instance of …………

SECTION B (ATTEMPT QUESTION ONE AND ANY OTHER THREE

(60 MARKS)

QUESTION 1

CASE STUDY

Imagine that you are the Chief Financial Officer (CFO) of a Small and Medium Enterprise

(SME).

It is April and the Chief Executive Officer has just returned from a meeting with the company's bankers. She calls you to her office to discuss the results of the negotiations. As things stand, the company requires a fairly significant injection of capital which would be used to modernize plant and equipment. The company has been promised new orders if it can produce goods to an international standard.

Existing machinery is incapable of manufacturing to the required level of quality. Whilst the bank is sympathetic, current lending policies require borrowers to provide an adequate current and projected cash flow, as well as a level of profitability sufficient to indicate a capacity to make repayments from an early date.

Largely because of some industrial problems, the business has not been performing at its optimal level. As such, the figures would not satisfy the bank's requirements.

However, the Chief Executive Officer (CEO) informs you that she has told the bank that the company is in excellent shape; that she believed that its financial results would satisfy the criteria and; that the Chief Financial Officer could deliver the company's financial report to the bank at the beginning of the following week. She adds, "it is up to you to decide on the contents of the report".

As you were getting up to leave her office, she mentioned casually that the company would have no choice but to retrench if the company fails to secure the bank loan required to modernize its plant and equipment. Understandably, you find the possibility of being retrenched very scary as you have just purchased a new house, with a significant mortgage.

Required:

(a) Identify and discuss FIVE ethical issues in this case. (5 Marks)

(b) As the Chief Financial Officer, what decision would you make with regards to the request of the Chief Executive Officer? Use an ethical theory to justify your decision. (5 Marks)

(c) Discuss TWO ethical implications of the Chief Executive Officer's actions. (5 Marks)

(Total 15 Marks)

QUESTION 2

Professional accountants have developed fiduciary services that are all bounded in their primary area of competence, that is, accounting.

Required:

(a) What constitutes a fiduciary duty? (3 Marks)

(b) List EIGHT traditional areas where professional accountants have developed fiduciary services. (4 Marks)

(c) Illustrate briefly the process which an accountant should adopt in writing an effective or adequate code of conduct for his/her firm. (8 Marks)
(Total 15 Marks)

QUESTION 3

There is no gainsaying the fact that effective corporate governance is an enduring factor which enables an establishment to evolve business excellence. It is capable of enhancing Board competence and teamwork which will result in much improved benefits to the shareholders.

Required:

(a) Discuss the different possible interpretations of the concept of a group, and how these may relate to differences in styles of corporate governance and of company financing. (5 Marks)

(b) Are the arguments for "differential reporting" convincing? Should differentiation be made on the basis of company size or some other characteristics?

(5 Marks)

(c) 'Secret reserves make a company stronger, so they should be encouraged'. Discuss. (5 Marks)

(Total 15 Marks)

QUESTION 4

Excel Plc has just commenced business and you have been appointed the Chief Financial Officer.

Management has requested you to give relevant professional advice on accounting policies that would enhance the standard of the company's financial report.

Based on IAS 8, you are required to:

(a) Define Accounting Policies. (1 Mark)

(b) State the main factors that management must consider in selecting and applying Accounting Policies in the absence of any IFRS standard or interpretation. (6 Marks)

(c) Discuss, briefly, alternative Accounting Policies on the following items in financial statements and make appropriate recommendations for Excel Plc:

(i) Property, Plant and Equipment
(ii) Inventories
(iii) Depreciation
(iv) Deferred income taxes (8 Marks)

(Total 15 Marks)

QUESTION 5

Making a good ethical decision requires a trained sensitivity to ethical issues. According to Lawrence Kohlberg, this depends on the stage of an individual's moral development.

You are required to:

(a) Distinguish between an ethical decision and an unethical decision. (3 Marks)

(b) Explain the various stages of Kohlberg's moral development. (9 Marks)

(c) Identify and briefly explain ONE of the principles of professional ethics that enhances ethical decision making. (3 Marks)

(Total 15 Marks)

QUESTION 6

The following are extracts from the financial statements of Dolly Joan Limited:

Statement of Financial Position as at 31 December 2010

	2010	2009
Assets:		
	₦'000	₦'000
Non-current Assets	20,211	21,141
Current Assets	7,214	4,976
Total Assets	27,425	26,117
Equity and liabilities:		
Share capital (16,000,000 shares of ₦0.50 per share)	8,000	8,000
Retained earnings	7,584	7,313
Total equity	15,584	15,313
Non-current liabilities	5,000	5,000
Current liabilities (including dividend payable of ₦1,696,000 (2009) and ₦1,800,000 (2010))	6,841	5,804
Total liability	11,841	10,804
Total equity and liabilities	27,425	26,117

Statement of Comprehensive Income for the year ended 31 December 2010

	2010	2009
	₦'000	₦'000
Net income	3,909	4,572
Income tax	(1,838)	(2,000)
Profit after tax	2,071	2,572
Market price per share	₦5.00	₦7.00

Required:

(a) Calculate the following ratios and discuss their usefulness:

(i) Proprietary ratio (3 Marks)
(ii) Earnings yield ratio (3 Marks)
(iii) Dividend cover ratio (3 Marks)

(b) Ratios are important tools in the analysis and interpretation of Financial Statements. However, they have a number of limitations and shortcomings. Discuss THREE of such limitations. (3 Marks)

(c) A number of factors may render inter-firm comparison invalid. List THREE of these factors. (3 Marks)

(Total 15 Marks)

SOLUTION TO SECTION A

PART I MULTIPLE CHOICE QUESTIONS

1. E
2. D
3. C
4. D
5. D
6. B
7. D
8. B
9. C
10. D
11. D
12. D
13. C
14. A
15. D

16. D

17. B

18. A

19. C

20. E

Tutorials

1. Interest Payable in 2010 = (6,000 X 11%) + (9,000 X 9%) + (3000 + 10%) – (₦'000^{s})
= 660 + 810 + 300 – (₦'000^{s})
= ₦1,770,000

2. ₦660,000 + ($^{2}/_{12}$ X ₦810,000) + ($^{2}/_{12}$ X ₦300,000)
₦660,000 + ₦135,000 + ₦50,000 = ₦845,000

3. ₦1,770,000 - ₦845,000 = ₦925,000

19. (₦10,000,000 X 13.5%) X 2 + ₦550,000 + ₦1,500,000
= ₦2,700,000 + ₦550,000 + ₦1,500,000 = ₦4,750,000

EXAMINERS' REPORT

The questions test the understanding of candidates on most of the topics in the syllabus.

General performance was below average. This suggests that candidates are not conversant with basic concepts, theories and issues in Financial Reporting and Ethics.

They should pay close attention to definitions and meanings in their preparation for future examinations.

PART II SHORT ANSWER QUESTIONS

1. Window Dressing/Creative Accounting

2. Economic

3. Anti-dilusion

4. Tripple Bottom Line

5. Corporate Culture or Code of Ethics
6. Economic responsibilities
7. Ethical dilemma
8. Organizational relationship/public relations
9. Profit/Economic objectives
10. Nature; amount or value or magnitude or size
11. Trust
12. Deontology
13. Off statement of financial position financing
14. i. Government control, joint control or significant influence
    ii. Related party to the reporting entity
    iii. Control over any related entity
15. Date of transition to IFRS
16. Income approach
17. Nominal amount
18. Value in use
19. Corporate and Criminal Fraud Accountability Act
20. Virtue Ethics

EXAMINERS' REPORT

The questions cut across the topics in the syllabus. Most of them require candidates to have an in-depth understanding of specific issues.

Performance was below average. This indicates that candidates did not give sufficient attention to the details of the topics covered in the syllabus.

Candidates are advised to pay more attention to all sections of the syllabus in subsequent examinations.

SOLUTION TO SECTION B

QUESTION 1

(a) The following are some of the ethical issues arising from the case study:

(i) The Question of Honesty/Integrity

The Chief Financial Officer (CFO) is confronted with the question of whether or not to tell the truth with regards to the information to include in the company's financial report. These borders on the principle of integrity which is one of the cardinal principles professional accountants are expected to follow.

(ii) The Issue of Window Dressing

The issue of whether or not to falsify the financial report is a case of window dressing which is one of the key issues that confronts professional accountants. This would have to be carefully considered in connection with the specific situation of the company and the likely effects of window dressing on the company as an entity and also on the employees of the company.

(iii) Limits of Professional Duty

The Chief Executive Officer's request is that the Chief Financial Officer does everything possible to ensure that the bank loan is secured and the jobs of the workers in the organization are preserved. One important question that the Chief Financial Officer would have to consider, however, is whether or not he has a professional duty to do everything possible to achieve the ends stated above. In this regard, the Chief Financial Officer has to determine if there are moral limitations to what he can or should do.

(iv) Self Interest Threat

Given the fact that the Chief Financial Officer has just purchased a house, with a significant mortgage, and confronted with the possibility of being retrenched, he would have to determine the extent to which his self-interest should be considered in determining the course of action that would be morally acceptable.

(v) Conflict of Loyalty

The case presents a conflict of loyalty for the Chief Financial Officer. He would have to determine which of the loyalties he has, as a professional, (to his profession, to society, and to his Chief Executive Officer) should be paramount in deciding on what to do in terms of the request of the Chief Executive that he should falsify the company's financial report.

(vi) The Duty of Objectivity

The Chief Financial Officer would have to sacrifice the duty of objectivity, which he has as a professional accountant, if he would accede to the request of the Chief Executive Officer. The principle of objectivity requires that financial reports should be based on facts and not on prejudice or sentiments.

(vii) Intimidation Threat

By mentioning the possibility of retrenchment, the Chief Executive Officer is intimidating the Chief Financial Officer in a subtle way. Coupled with the Chief Financial Officer's present mortgage burden, he would have to decide on how to respond to the subtle intimidation by the Chief Executive Officer.

(b) The following are some of the alternative courses of action that the Chief Financial Officer might adopt in response to the request of the Chief Executive Officer.

(i) <u>Accede to the Chief Executive Officer's Request</u>

The Chief Financial Officer might decide to accede to the request of the Chief Executive Officer on utilitarian grounds. Going by the theory of utilitarianism which prescribes that people should take decision that would maximize the good for the greatest number of people, it would be reasonable for the Chief Financial Officer to present a window dressed financial report. For one, it would ensure that no one gets retrenched, the organization would be able to secure the much needed loan, and the Chief Financial Officer himself would be in a position to keep the new house and service the mortgage on the house. Besides, this is very likely to enhance the interest of the shareholders of the company.

Also, from the perspective of ethical egoism, window dressing the financial report would be in the personal interest of the Chief Financial Officer. Apart from the personal benefits identified above, it would also put him in the good books of the Chief Executive Officer.

(ii) Refuse to Accede to the Request of the Chief Executive Officer

As the Chief Financial Officer, "cooking the books" constitute a breach of the principles of professional ethics, namely the principles of integrity, objectivity, professional behaviour and professional due care and competence. Besides, on the part of the Chief Financial Officer, it would amount to acting against the interest of the public which he is expected to protect as a professional.Hence, it would be unprofessional and unethical for him as the Chief Financial Officer to succumb to the intimidation of the Chief Executive Officer at the expense of all stakeholders that might be adversely affected by such an action.

The decision to refuse to accede to the request of the Chief Executive Officer could be justified by either ethical deontologism or ethical utilitarianism. By the former if his decision is based on the understanding that "cooking the books", by its nature, violates the fundamental principles of professional ethics. Deontologism maintains that the moral status of actions or decisions should be determined by their nature and not consequences.

Ethical utilitarianism may also be used to justify a refusal to accede to the Chief Executive Officer's request if it is based on an understanding of the likely negative consequences of doing so. For instance, the integrity of the organization and its officials would be at stake, and this might have an adverse effect on the value of its shares.

(iii) Blow the Whistle or Resign

If the Chief Financial Officer explains to the Chief Executive Officer why it would be unethical and unprofessional for him to "cook the books" but she insists that he presents a falsified financial report, the Chief Financial Officer might decide to take a bold step by blowing the whistle, and perhaps resign his appointment. However, before such a drastic step is taken, it would be wise for him to get counsel from other professional colleagues. This alternative is supported by Duty Ethics which specifies that the moral action is one that is based on duty. In the case on hand, the major motivation for blowing the whistle or resigning would be the understanding that the request made by the Chief Executive Officer violates the basic duties he has as a professional.

(c) Though the Chief Executive Officer's actions seem to be the most reasonable thing to do as a survival or turn-around strategy, there are grievous ethical implications. These include:

(i) The action totally violates the principle of integrity that a strategic manager is expected to respect.

(ii) The Chief Executive Officer, at her level, is expected to provide ethical leadership and promote high moral standards that would establish trust within the organization, between the organization and stakeholders, including the bank. The request to falsify the financial report by the Chief Executive Officer might encourage other unethical practices by members of the organization. This would further encourage or create an organizational culture, that over time would become totally insensitive to morality.

(iii) The betrayal of trust which would result from the Chief Executive Officer's action, if discovered would create a serious problem for the image of the company.

EXAMINERS' REPORT

The question tests candidates' capacity to identify some of the ethical issues that could arise for professional accountants. It also examines their ability to arrive at acceptable ethical decisions on the basis of their knowledge of the ethical theories that are relevant to the accountancy profession.

Candidates are expected to discuss ethical issues arising from the case study, provide justification for the ethical decision that is considered to be reasonable within the context of the case, and identify possible ethical implications of the actions of the Chief Executive Officer. Candidates displayed a fair understanding of the question, and performance is average.

A common pitfall in answering the question for many of the candidates is their inability to identify ethical issues arising from the case. This may be a product of their poor understanding of the nature of ethical issues.

There is a need for candidates to pay a close attention to the nature of ethical issues, and how they can arise for professional accountants.

QUESTION 2

(a) Fiduciary duty is the legal or ethical obligation based on trust that one party or a person would act in the best interest of another. For instance, the management of an organization has the legal or ethical obligation to act in the best interest of the stakeholders, especially those that have made financial commitment or investment in that organization. Such commitment is based on trust.

(b) The traditional areas where professional accountants have developed fiduciary services include:

- (i) Auditing of accounting records, systems and financial statements.
- (ii) Financial projections: preparation, analysis and audit.
- (iii) Taxation: preparation of tax returns and advisory services.
- (iv) Insolvency services: executorship and trusteeship, receivership and liquidation.
- (v) Financial planning and advice.
- (vi) Decision making: facilitation through analysis approach.
- (vii) Management control: advice and design of system.
- (viii) Corporate and commercial affairs: general advice.
- (ix) Payroll services.
- (x) Non-current asset management.
- (xi) Debt management.
- (xii) Corporate restructuring and re-engineering.
- (xiii) Treasury management.

(c) The process which an accountant should adopt in writing an effective or adequate code of conduct for his/her firm is as follows:

- (i) Be clear on your objectives and ensure you have the full support of the head of the organization.
- (ii) Set up a realistic time-table for developing and implementing your code
- (iii) Know the cost of running a code program and be sure you have adequate funding to implement the code.
- (iv) The code should be one that could be easily amended to meet new situations and challenges. That is, it should be a living document.
- (v) The code should be designed to address the problems faced by his firm.

(vi) Be aware of the latest developments and trends in the area of self-regulation.
(vii) Ensure that the code is legally defensible.
(viii) Get expert advice on how to promote the code and how to educate relevant stakeholders.
(ix) Write the code as simply as possible. That is, avoid unnecessary jargons.
(x) Be responsive and objective in developing the code of conduct.
(xi) Select an independent administrator of unquestionable competence and integrity.
(xii) Recognise potential ethical and compliance problems.
(xiii) Identify the expectations, as well as the costs, benefits and risks of meeting those expectations.
(xiv) Assess whether proposed code of conduct effectively manages the risks faced by the organization.

EXAMINERS' REPORT

The question examines candidates' knowledge of the fiduciary responsibilities that professional accountants have and the types of fiduciary services they render. It also tests candidates' understanding of what is required to write an adequate code of ethics on behalf of an organization that a professional accountant works for.

Candidates are required to define what a fiduciary duty is, identify some of the traditional fiduciary duties professional accountants have, and the basic process for writing a professional code of ethics. Most candidates attempted the (b) part of the question fairly adequately while many of them performed poorly with regards to the (a) and (c) parts of the question.

A common pitfall for most candidates is their poor understanding of the question and their inadequacy in the use of technical terminologies.

Candidates are advised to make effective use of ICAN's e-library and study pack as all the information they need to pass could be accessed from these sources.

QUESTION 3

(a) (i) The parent concept of a group is based on legal control, which in turn relies on majority voting rights and shareholdings. In some countries, control can also be achieved by contract.

(ii) The entity concept has advantage that it does not treat minority (non-controlling) shareholders differently from majority shareholders, rather, it attempts to look at all enterprises in the group as part of the same economic entity.

(iii) It also appears to have advantages for user groups other than shareholders, such as employees, customers, etc.

(iv) The proprietary concept can more easily accommodate cases where an enterprise member of a group is less clear-cut. Here, ownership and the right to exercise significant influence are decisive factors.

(v) The reason that different concepts of a group have arisen, and appear to fit the patterns which, in some countries, can be linked to historical economic developments and corporate financing.

(b) (i) The arguments for differential financial reporting are convincing because the context of financial statements must be driven by financial statement user's needs.

(ii) The differential reporting principle acknowledges that the information needs of users of non-public companies financial statements differ from those of the users of public entities' financial statements.

(iii) When all owners consider that differential reporting fulfills their needs this signals that owners consider the costs of applying certain accounting requirements exceed the benefits to their enterprise and to themselves.

(iv) The differentiation should not be made on the basis of company size. The Accounting Standard Board deliberated whether size should be a criterion for differential reporting and rejected a size test, as differential reporting is justified by the users' characteristics rather than by the enterprises.

(v) Regardless of their size, all non-publicly accountable enterprises share a common feature that distinguishes them from publicly accountable entities;

they have a narrower range of users of their financial statements.

Most non-public companies, regardless of size, are not required to make their financial statements publicly available and shareholders by unanimous consent may waive an audit of the financial statements.

(vi) Differential reporting is designed to help private companies produce more useful and understandable information for the users of their financial statements, and is optional.

(vii) In certain circumstances, for example, if the enterprise is likely to go public in the future or report to a public investor, differential reporting may not be an appropriate option.

(c) Secret reserves are reserves that do not show up on the statement of financial position. It should be appreciated that one of the main objectives of secret reserves is to strengthen the financial position of a concern, and losses can be made good without disclosing their occurrence to the shareholders and other stakeholders. This helps the concern to remain financially strong in spite of a period of adversity.

They can be achieved in any of the following ways:-

(i) Not writing up the value of an asset, the price of which has permanently gone up.
(ii) Creating excessive reserve for bad and doubtful debts or discount on sundry debtors.
(iii) Providing excessive depreciation on fixed assets.
(iv) Over-valuing the liabilities.
(v) The inclusion of fictitious liabilities.
(vi) Showing contingent liabilities as actual liabilities

However, creation of secret reserves may not be encouraged in order to ensure transparency and achieve true and fair view in the preparation and presentation of financial report. The following are reasons against secret reserves:

- Statement of financial position would not exhibit a true and fair view of the financial affairs of the concern if secret reserves are created and maintained. At the same time, the income statement would also not give the correct results since excessive provision for depreciation or reserve has been made for its creation.

- Secret reserves may be utilized by the management to conceal their weakness or mismanagement. It may conceal losses arising out of bad or careless management or even reckless speculation.

- If non-current assets are undervalued for the purpose of creating secret reserves, and if there is a fire incidence, the company will not be able to claim the full value of the assets because the insurance company will pay according to the book value of the asset destroyed or damaged and hence cause a loss to the company.

- By creating secret reserves, and thus lowering the dividend, the directors may indulge in speculation in the shares of the company.

- The shareholders of the company may suffer a loss due to less dividends on account of the creation of secret reserves.

- Due to creation of secret reserves, the shares may be under-valued.

EXAMINERS' REPORT

The question tests candidates understanding of different conceptions of a group and the different styles of corporate governance, and company financing associated with each conception of a group. It also examines their knowledge of "differential reporting" and secret reserves.

Candidates are expected to discuss different conceptions of a group and arguments in support of "differential reporting". They are also required to discuss the advantages and disadvantages of secret reserves. Few candidates attempted the question and performance was poor as most of them displayed a poor understanding of the requirements of the question.

Candidates' commonest pitfalls were their inability to identify the styles of corporate governance and company financing identifiable with each conception of group. They also lack an adequate understanding of "differential reporting".

Candidates are advised to adequately cover the syllabus, paying special attention to the meaning of basic concepts in financial reporting.

QUESTION 4

(a) Accounting policies are specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements.

(b) In the absence of an IFRS that specifically applies to a transaction, other events or condition, management shall use its judgment in developing and applying an accounting policy that results in information that is:

(i) Relevant to the economic decision-making needs of users; and

(ii) Reliable, in that the financial statements:

- Represent faithfully the financial position, financial performance and cost flows of the entity,
- Reflect the economic substance of transactions, other events and conditions, and not merely the legal form,
- Are neutral, i.e., free from bias,
- Are prudent; and
- Are complete in all material respects.

In making the judgment, management shall refer to, and consider the applicability of, the following sources in descending order:

- The requirements in IFRS dealing with similar and related issues;
- The definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the framework.

Management may also consider the most recent pronouncements of other standard setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices, to the extent that these do not conflict with the sources mentioned above.

(c) (i) IAS 16 provides for two acceptable alternative approaches to accounting for non-current tangible assets such as property, plant and equipment.

- HISTORICAL COST: Under which acquisition or construction cost is used for initial recognition, subject to depreciation over the expected economic life and to possible write-down in the event of a permanent impairment in value.

- REVALUATION: After initial recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably should be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

An entity shall choose either the historical cost model or the revaluation model which assists accounting policy and shall apply the policy to its entire class of property, plant and equipment.

Recommendation

Since the company has just commenced business, its property, plant and equipment should be measured at cost (i.e. initial measurement). In other words, Excel's property, plant and equipment should be carried at cost less accumulated depreciation and subsequent impairment losses.

(ii) Inventories

Under IAS 2, there are two acceptable cost flow assumptions. These are: (1) FIFO (First In, First Out) and (2) the weighted average method. There are variations of each of these cost flow assumptions that are sometimes used in practice, but if an entity presents its financial statements under IFRS, it has to be careful not to apply a variant of these cost flow assumptions that would represent a deviation from the requirements of IAS 2.

The FIFO method of inventory valuation assumes that the first goods purchased will be the first goods to be sold, regardless of the actual physical flow.

This method is said to be closely related to the physical flow of goods for most industries having moderate to rapid turnover.

This yields results similar to those obtained under current cost accounting in the statement of financial position and helps in achieving the goal of

reporting assets at amounts approximate to current values.
However, FIFO method does not necessarily reflect the most accurate or decision-relevant income figure when viewed from the perspective of underlying economic performance, as older historical costs are being matched against current revenue.

Under the weighted-average cost, the cost of goods available for sale (opening inventories plus purchases) is divided by the total units available for sale to obtain a weighted average unit cost.

Closing inventory and units of goods sold are then valued at the computed average cost. When this approach is applied to a perpetual inventory system, the average cost is recomputed after each purchase. This process is referred to as moving average. Sales are costed at the most recent average.

Recommendation

Excel Plc. is urged to adopt FIFO method as this leaves its closing stock at their near current market prices.

(iii) Depreciation

In accordance with the matching principle, the cost of property, plant and equipment are allocated through depreciation to the periods that will have benefitted from the use of the asset.

Whatever method of depreciation is chosen, it must result in the systematic and rational allocation of the depreciable amount of the asset (initial cost less residual value) over the asset's expected useful life. The method of depreciation is based on whether the useful life is determined as a function of time, or as a function of actual physical usage.

IAS 16 states that, although land normally has an unlimited useful life and is not to be depreciated, where the cost of the land includes estimated dismantlement or restoration costs, these are to be depreciated over the period of benefits obtained by incurring those costs. In some cases, land itself may have a limited useful life, in which case it is to be amortised in a manner that reflects the benefits to be derived from it.

Recommendation

Excel Plc. may adopt either of the alternative methods. However, the depreciation method to be adopted should reflect the consumption pattern of the economic benefits associated with its assets.

(iv) Deferred Income Tax

Alternative policies on deferred income taxes are:

- Deferral Method
- Liability Method

However, deferred income taxes are usually calculated using the comprehensive liability method. This method calculates a deferred tax asset or liability on the temporary differences that arise between the recognition of items in the statement of financial position of Group Companies used for tax purposes and one prepared for consolidation purposes.

An exception is that no deferred income tax is calculated for the temporary differences in investments in group companies and associates, provided that the investor (parent company) is able to control the timing of the reversal in the foreseeable future.

Deferred taxes, calculated using applicable local tax rates, are included in non-current assets and non-current liabilities, with any changes during the year recorded in the income statement. Changes in deferred taxes on items that are recognized in equity are recorded in equity.

Deferred income tax is determined using tax rates (and laws) that have been enacted by the statement of financial position date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Recommendation

Liability method of accounting for deferred tax should be adopted by Excel Plc. as this is relatively simple, a statement of financial position oriented and also state as accurately as possible, the obligation for taxes payable.

EXAMINERS' REPORT

The question tests candidates' understanding of IAS 8 as regards factors to consider by management in selecting and applying Accounting Policies in the absence of IFRS standard or interpretation.

Candidates are required to discuss alternative accounting policies that could be adopted for Property, Plant and Equipment, Inventories, Depreciation and Deferred Income Taxes, and make recommendation for the appropriate accounting policies to be adopted.

Candidates' performance was below average, as they displayed lack of understanding of the contents of IAS 8 and its application on the accounting policies of some assets and liabilities items in the financial statements.

Candidates are advised to keep abreast of the contents and application of all Accounting Standards to enhance their performance.

QUESTION 5

(a) An ethical decision is one that is based on a due consideration of relevant ethical principles. It aims at a fair judgment that would enhance the interest of relevant stakeholders while remaining faithful to core ethical principles.

Put differently, whatever is ethical relates to the application of moral principles or the branch of knowledge that deals with morality. An ethical decision, therefore, is one that is socially responsive and aims at having a better impact on all stakeholders.

On the other hand, an unethical decision is one that is insensitive to basic moral principles. It is not socially responsible and does not seek to uphold the interest of the public or relevant stakeholders. Instead, it tends to generate harmful effects for stakeholders or consists of some inherent qualities that are considered to be unfair or unjust.

(b) Kohlberg's Cognitive Moral Development Theory

Kohlberg's theory explains how individuals make ethical decisions in terms of development through three levels of moral development with two stages within each level.

Level 1 Pre-conventional

The decisions individuals make on ethical matters will have nothing to do with the ethical issues involved, but instead will depend on the personal advantage to the individual.

Stage 1 – Obedience and Punishment

The earliest stage of moral development is especially common in young children, but adults are capable of expressing this type of reasoning. At this stage, children see rules as fixed and absolute. Obeying the rules is important because it is a means of avoiding punishment.

Stage 2 – Individualism and Exchange

Individuals will see ethical decisions in the more complex terms of acting in their own best interest. They will see ethical decision in terms of the deals they can make and whether these deals are fair to them. For example it can mean helping others when others appear over-worked, but in return expecting others to help them when the situation is reversed.

Level 2 Conventional

Stage 3 – Interpersonal Relationships

This stage can be described as the stage in which individuals learn to live up to what is expected of them by their immediate circle (friends, workmates or even close competitors). Often referred to as the "good boy-good girl" orientation, this stage of moral development focuses on living up to social expectations and roles. There is an emphasis on conformity, being "nice", and a consideration of how choices influence relationships.

Stage 4 - Maintaining Social Order

Individuals are seen as operating on a higher stage within this level if they operate in line with social or cultural accord rather than just the opinion of those around them. This certainly means complying with the law as it codifies social accord but it does not just mean that. It is oriented towards monitoring social order.

Level 3 Post-conventional

The most advanced levels relates to individual development for making their own ethical decisions in terms of what they believe to be right, not just acquiescing in what others believe to be right.

State 5 – Social Contract and Individual Rights

At this stage, people begin to account for the differing values, and beliefs of other people. Rule of law is important for maintaining a society, but members of society should agree upon set standards.

There is, an understanding of social mutuality and a genuine interest in the welfare of others with the view of having a good society based on a social contract.

Kohlberg's final level of moral reasoning is based upon universal ethical principles and abstract reasoning. At this stage, people follow these internalized principles of justice, even if they conflict with laws and rules.

(c) Integrity:

A professional accountant should be straightforward and honest in all professional and business relationships. It involves having strong moral principles that one refuses to compromise.

Objectivity

A professional accountant should not allow bias, conflict of interest or undue influence of others to override his professional, or business judgments. Decisions should be based on real facts.

Professional Competence and Due Care

A professional accountant has a continuing duty to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional service based on current developments in practice, legislation and techniques. A professional accountant should act diligently and in accordance with applicable technical and professional standards when providing professional services.

Confidentiality:

A professional accountant should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any of such information to third parties without the right or duty to do so. Confidential information acquired as a result of professional and business relationship should not be used for the personal advantage of the professional accountant or third parties.

EXAMINERS' REPORT

The question tests candidates' understanding of how to make good ethical decisions, especially in terms of Lawrence Kohlberg's theory of cognitive moral development.

Candidates are required to make a distinction between ethical and unethical decisions, and explain how any of the principles of professional ethics can facilitate ethical decision making.

Many candidates' attempted the question and displayed good understanding of the (a) and (c) parts of it but many of them could not answer the (b) part correctly. Overall performance is average.

Candidates' commonest pitfalls were their inability to explain Kohlberg's theory of cognitive moral development and their clumsy grammatical expression.

Candidates are advised to study more closely the ethical theories and principles included in the syllabus.

QUESTION 6

(a)(i) Proprietary Ratio = $\frac{\text{Shareholders Fund/Net Assets}}{\text{Total Assets}}$ X 100%

		2010	2009
Proprietary Ratio	=	$\frac{15,584}{27,425} \times 100$	$\frac{15,313}{26,117} \times 100$
	=	56.8%	58.6%

Proprietary Ratio provides a measure of the adequacy of security to pay all liabilities. It is a test of long-term financial stability and cushion for creditors. The higher the percentage of this ratio, the better the security for creditors especially in case of liquidation.

(ii) Earnings Yield Ratio = $\frac{\text{Earnings Per Share}}{\text{Market price Per Share}}$

$= \frac{\text{EPS}}{\text{MPS}}$

Where EPS = $\frac{\text{PAT – Preference Shares Dividend}}{\text{No. of Equity shares in issue}}$

	2010	2009
EPS =	$\frac{2,071,000}{16,000,000}$	$\frac{2,572,000}{16,000,000}$
	12.94K	16.08K
MPS as given	₦5	₦7
Earnings Yield Ratio =	$\frac{0.13}{5}$	$\frac{0.16}{7}$
EY =	0.026	0.023
	2.6%	2.3%

The Earnings Yield shows the relationship between the market value of company's shares and associated returns. It is the reciprocal of Price Earnings Ratio which shows the market view of the future prospects of the share. This ratio gives capitalization rate at which the stock market capitalizes the value of the current earnings.

The higher the ratio, the faster the growth the market is expecting in the company's future Earnings Per Share.

(iii) Dividend cover = $\frac{\text{Earnings per share}}{\text{Dividend per share}}$ OR $\frac{\text{Profit after tax}}{\text{Total Dividend}}$

	2010	2009

Earnings per share $= \frac{2,071,000}{16,000,000} \times 100 \qquad \frac{2,572,000}{16,000,000} \times 100$

$= 12.94k \qquad 16.08k$

Dividend per share $= \frac{1,800,000}{16,000,000} \times 100 \qquad \frac{1,696,000}{16,000,000} \times 100$

$= 11.25k \qquad 10.60k$

Dividend cover $= \frac{12.94}{11.25} \qquad \frac{16.08}{10.60}$

OR

$\frac{2,071}{1,800} \qquad \frac{2,572}{1,696}$

$= \underline{\underline{1.2 \text{ times}}} \qquad \underline{\underline{1.5 \text{ times}}}$

Dividend cover shows the relationship between available profit or earnings and the dividends paid out of profits. It indicates how many times dividend per share is covered by earnings per share.

A higher dividend cover indicates that only a small portion of earnings has been distributed as dividends, while a substantial portion has been ploughed back into the business. The higher the dividend cover, the more likely it is that the current dividend can be sustained in the future.

(b) Limitations of Ratio Analysis include:

(i) Different accounting policies may render ratio analysis invalid - proper comparison is impossible as a result of unidentical basis of valuation.

(ii) Financial statements prepared on historical basis are the raw material input into ratio analysis. These cannot give a true picture of year to year trends because of the impact of inflation. Trend analysis is impossible.

(iii) Only items measurable in monetary terms are included in financial statements. This is a major defect as we have human assets that could be regarded as strengths of a reporting entity.

(iv) Some of the financial statements especially the statement of financial position are static in nature while the business environment itself is dynamic.

(v) Unrealiable data/financial statements – If the financial statements itself are window dressed, then what is the value of financial analysis based on unreliable data.

(vi) They are not useful for budget preparation where predictions and forecasts are required.

(vii) Unless ratios are calculated on a uniform basis, from a uniform data, comparisons can be misleading.

(viii) A few simple ratios do not provide automatic means of running a company. Business problems usually involve complex patterns which cannot be solved solely by the use of ratios.

(ix) Ratio must not be used as the sole test of efficiency. Concentration on ratios by managers may inhibit the incentive to grow and expand, to the detriment of the long-term interest of the company.

(c) Factors that may render inter-firm comparison invalid include:-

(i) Usage of different accounting dates by entities being compared.
(ii) Application of different accounting policies especially for asset valuation.
(iii) Differences in the size of the entities. Bigger firms may have a number of relative advantages over the smaller ones.
(iv) Different management structures and styles.
(v) Different technical expertise of the entities.
(vi) Differences in product range and product type as well as sales mix among companies within the same industry.
(vii) Ratios may not be calculated according to the same formular (for example, there are several possible definitions of gearing and Return on Capital Employed (ROCE)).

EXAMINER'S REPORT

The question tests candidates' knowledge of accounting ratios, its interpretation and usefulness.

Candidates were expected to discuss the limitations of ratios and mention factors that may render inter-firm comparison invalid. Many candidates attempted the question and performance was below average.

Candidates commonest pitfalls were wrong application of formulae and general mix-up of data between the different years stated in the question.

Candidates are advised to ensure that they cover the syllabus while preparing for the examination.

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA
PROFESSIONAL EXAMINATION II – MAY 2012
STRATEGIC FINANCIAL MANAGEMENT
Time Allowed – 3 hours

SECTION A: Attempt All Questions

PART **I**: MULTIPLE CHOICE QUESTIONS (20 Marks)

Write only the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions:

1. Which of the following is NOT a strategy to be adopted by an organisation for growth opportunities outside the organisation?

   A. Bank circularisation
   B. Audit Committee
   C. Non-executive directors
   D. Due diligence reports
   E. Related party transactions

2. Based on the market growth rates and relative market shares, which of the

following does NOT form part of the grouping of businesses by Boston Consulting Group?

A. Dogs
B. Cats
C. Cash cows
D. Moons
E. Stars

3. In capital budgeting, the post-audit stage is used to

A. Improve cash flow forecasts and eliminate potentially profitable but risky projects.
B. Stimulate management to improve operations, bring results into line with forecasts and eliminate potentially profitable but risky project.
C. Improve cash flow forecasts, stimulate management to improve operations, bring results into line with forecasts and eliminate potentially profitable but risky projects.
D. Improve cash flow forecast, stimulate management to improve operations and bring results into line with forecasts.
E. Discontinue potentially profitable but risky projects.

4. The most appropriate method for the valuation of shares in unquoted companies is the

A. Discounted future profits method
B. Price-earning multiple method
C. Dividend yield basis method
D. Berliner method
E. Dual capitalisation of profits method

5. Which of the following statements about capital structure and leverage is correct?

A. Increasing the company tax rate will not affect capital structure decisions
B. A firm with high business risk is more likely to increase its use of financial leverage than a firm with low business risk
C. Financial leverage is directly related to operating leverage
D. A firm with high business risk is unlikely to increase its use of financial leverage than a firm with low business risk
E. A firm with low operating leverage has a small proportion of its total costs in

fixed assets

6. In deciding the appropriate level of current assets for the firm, management is concerned with a trade-off between

   A. Equity and debt
   B. Cost and revenue
   C. Profitability and risk
   D. Short-term and long-term borrowing
   E. Liquidity and marketability

7. Which of the following statements appropriately describes a 'tender offer'?

   A. A would-be acquirer's friendly takeover attempt
   B. A would-be acquirer's strategy of paying more for acquirer's shares
   C. A business harassment by the acquirer
   D. A would-be acquirer's offer to buy shares directly from shareholders
   E. A goodwill gesture by a 'white knight'

8. Goals of Micro-finance Banks do NOT include

   A. Preventing competitive advantage from companies
   B. Mobilizing savings for financial intermediation
   C. Creating employment opportunities
   D. Involving the poor in the socio-economic development of the country
   E. Providing diversified, dependable and timely financial services to the poor

9. Which of the following is NOT a factor to consider in overseas investment appraisal?

   A. Taxation
   B. Expected Rate of Return
   C. Rate of Immigration and Exchange
   D. Political, Economic and Exchange Risks
   E. Useful Life of Investment

10. Which of the following is NOT emphasised by the concept of Strategic Financial Management?

   A. Allocation of scarce resources

B. Establishment of goals and objectives
C. Identification of possible strategies
D. Implementation and monitoring of the chosen strategy
E. Maximisation of Net Present Value

11. Which of the following is NOT a Qualitative Risk Analysis Technique?

A. Cost benefit
B. Checklist
C. Delphi
D. Brainstorming
E. Storyboarding

12. Good financial planning does NOT include

A. Identification of viable projects and the amount of finance required to finance such projects
B. Identification of surplus/deficit periods and amounts of cash involved in any of the two situations
C. Uses of surplus funds in order to avoid idle cash
D. Raising of funds to take care of deficit and the likely cost of raising such funds
E. Identification of risk and evaluation of its potential impact on the organisation

13. Which of the following is NOT a key element of ethical code?

A. Adhering to the highest standards of honesty, integrity and fairness
B. Seeking or accepting favours which are beneficial to the business
C. Avoiding involvement in any decisions that could bring about conflict of interest
D. Avoiding any financial interest in contracts awarded by the company
E. Avoiding any relationship with contractors or suppliers that might compromise their ability to act impartially

14. What is the maturity period of a Treasury Certificate?

A. 150 days
B. 160 days
C. 170 days
D. 180 days
E. 190 days

15. If a company pays a dividend of 10k per share and its cost of equity is 15%, what is the company's market price per share?

A. 64k
B. 65k
C. 66k
D. 67k
E. 68k

16. Rapola Plc has 20,000,000 ordinary shares of 50k each in issue. These shares are currently valued on the Stock Exchange at ₦1.60 per share. The company requires additional capital and has decided to make a one-for-four rights issue at ₦1.30. Calculate the value of the rights per new share.

A. ₦0.20
B. ₦0.22
C. ₦0.23
D. ₦0.24
E. ₦0.25

17. Portfolio analysis is commonly used in strategy formulation because it offers the following advantages, EXCEPT

A. Its value can lead to self-fulfilling prophecies
B. It encourages top management to evaluate each of the company's businesses, set objectives and allocate resources
C. It stimulates the use of externally oriented data to supplement management's judgement
D. It raises the issue of cash flow availability for use in expansion and growth
E. Its graphic depiction facilitates communication

18. Ade sells 2,000 drums of Water Purifying chemical each year. It has been estimated that the cost of holding one drum of chemical for a year is ₦4.00. The cost of placing an order for new inventories is estimated at ₦250. What is the number of orders Ade has to make?

A. 2
B. 3

C. 4
D. 5
E. 6

19. Which government agency is established to take care of the interests of small firms?

A. Small and Medium Enterprises Development Agency (SMEDAN)
B. Nigerian Stock Exchange (NSE)
C. Securities and Exchange Commission (SEC)
D. Small and Medium Industries Equity Investment Scheme (SMIEIS)
E. Nigerian Deposit Insurance Corporation (NDIC)

20. According to Net Income Approach to Capital Structure, the impact of increasing debt equity ratio is for the market value to

A. Increase and later decrease
B. Remain the same
C. Decrease and later increase
D. Decrease and later remain constant
E. Remain constant up to a point and later reduce

PART II: SHORT-ANSWER QUESTIONS (20 MARKS)

Write the answer that best completes each of the following questions/statements:

1. In a firm, conflict in relation to the goals of management and shareholders causes ………………………… problem

2. The Finance Manager must be conversant with the financial, political, business and ……………………… environmental factors

3. Installation of systems and processes to ensure that management acts in the best interest of the stakeholders is known as………………………………

4. Dogo Plc. has earnings after interest but before tax of ₦300,000. Assuming the company's interest cover is 7, the company's interest charge is…………….

5. A company has just paid a dividend of ₦2.50 per share. Dividend is expected to grow at 5% per annum. If the required return on equity is 15%, what is the intrinsic

value of the share?

6. Use the data below to compute the beta of security K:

Market Return (%)	Security K-Return (%)
5	-2
25	38

7. The level of stock kept to cover uncertainty in the lead time or the demand during lead time is referred to as.......................................

8. State the number of years a bank shall be free to divest its shares in anyway it deems fit, in a small scale industry under the Small and Medium Enterprises Equity Investment Scheme (SMEEIS)

9. State the reason why SMEs, in determining their discount rates to be used for project appraisal, need to add a margin to that of quoted companies.

10. If the exchange between US dollar and Nigerian Naira is $1 = ₦140 and inflation rate presently runs at 5% in USA while it runs at 15% in Nigeria, what will be the exchange rate after one year given that the US dollar strengthens its value against naira?

11. What is the effective rate of interest on a ₦20,000,000 loan at 30% discounted for a year?

12. An approach to corporate finance strategy in which management views its product lines and business units as a series of investments from which it expects a profitable return is called..............

13. Conceptualising and running a business whose primary goals are profitability and growth characterised by innovative strategic practice are known as...........

14. What is the term used for a diversification strategy that involves a move into another industry to produce products unrelated to its current products?

15. The diagrammatical and practical way of showing a sequence of interrelated decisions and outcomes is called..................

16. What is the present value of ₦40,000,000 at an interest rate of 10% to perpetuity?

17. The informal group of official creditors whose role is to find co-ordinated and sustainable solutions to the payment difficulties experienced by debtor nations is called……………………

18. State the name given to an intervention in the foreign exchange market without adjusting for the change in money supply.

19. The degree to which a firm's present value of future cashflows can be influenced by exchange rate fluctuations is termed……………

20. The quantity of inventory that should be purchased in order to minimise total inventory cost is known as………………………

SECTION B: ATTEMPT QUESTION ONE AND ANY OTHER THREE QUESTIONS
(60 Marks)

QUESTION 1

CASE STUDY

Nagode Limited is a private company established about a decade ago in the Northern part of Nigeria to produce plastic bottles. The first six years of the company witnessed tremendous growth, generally facilitated by successful business operations and reduced competition.

As a result of the global economic melt-down and losses sustained in recent years, the directors and the entire management of the company became worried and were contemplating closing down the company for six months in the first instance. The concomitant effect of the proposed closure would be further loss of sales and profits. For how long will this continue? This was the question being asked by the Chairman and Chief

Executive of the company.

In an attempt to avert the problem, the management held an emergency meeting where various suggestions were put forward but none of them seems to proffer solutions to the problem. The Chairman and Chief Executive thought of outright sale of the company to a willing competitor, Adawa Limited, but this idea was not acceptable to the Board of Directors as this could lead to the extinction of the company
Following deliberations and resolutions as to ways of taking the company out of the current predicament, negotiations between the two Boards of Directors began. The most recent information relating to each of the two businesses is set out below:

	Nagode Ltd	Adawa Ltd
Current earnings	₦ 20,000,000	₦ 9,000,000
Number of shares in issue	4,000,000	3,000,000
Earnings per share	₦ 5	₦ 3
Price per share	₦80	₦30
Price earnings ratio	16 Times	10 Times

If negotiations are successful, Adawa Limited would be willing to accept an offer of ₦40.00 per share in exchange for a share of Nagode Limited.

Required:

(a) From the Strategic Financial Management perspective, what options would you advise management of Nagode Limited to explore in order to prevent a shut-down or outright discontinuation of business?

(b) If merger option is adopted, what are the likely financial effects on the shareholders of the two companies? (Total 15 Marks)

QUESTION 2

The Board of Directors of Falcum Plc. is concerned about the optimal replacement cycle of one of its equipment. The initial outlay required to purchase a new equipment is ₦1.5million. The longer the asset is held, the higher the operating and maintenance costs and the lower the residual value. Relevant data on the various cost items relating to the equipment are given below:

Year	0	1	2	3
Initial outlay (₦'000)	1500			
Operating and Maintenance Cost (₦'000)		300	600	750
Residual value (₦'000)		1,050	750	600

Cost of Capital is 10%

You are required to

(a) Determine the optimal period of replacing the equipment using the Annual Equivalent Cost Method (8½ Marks)

(b) State FOUR areas of relevance of Information Technology to investment decisions (4 Marks)

(c) In determining the present value of a ₦400,000 investment for 5 years at 10 percent per annum using the screen shot of a present value formular in a spreadsheet application shown below, indicate the correct information to be entered in the spaces provided in order to generate the correct present value (PV) amount. Do not generate the 'PV'.

PV
Rate =?
Nper =?
Pmt =?
FV =?
Type =? (2½ Marks)

(Total 15 Marks)

QUESTION 3

Minimax Plc is planning an investment project in South Africa where the currency is Rand. The expected cashflows from the project are as follows:

Year	Rand (Million)
0	160
1	80
2	96
3	64

The Rand/Naira spot rate is 0.0455 and the Rand is expected to appreciate by 2% per annum. A similar Nigerian-based project would be expected to earn a minimum required rate of return of 10 percent.

You are required to

(a) Appraise the viability of the project, discounting the foreign cash flows at the foreign cost of capital
(10 Marks)

(b) State FIVE reasons why business organisations engage in cross-border investments
(5 Marks)

(Total 15 Marks)

QUESTION 4

The Managing Director of Soulex Limited, a small scale business enterprise, is worried about the short-term solvency/liquidity of his company. The Management Accountant, based on the instruction of the Managing Director, came up with the following estimated figures for the coming trading year:

Sales/Turnover	₦8,400,000
Average Accounts Receivable	₦759,000
Gross Profit Margin	25%
Average Inventories	₦
Finished Goods	525,000
Work in Progress (80% complete)	825,000
Raw Materials	330,000
Average Accounts payable	315,000

Materials' costs represent 50% of the total cost of sales.

Required:

(a) Calculate the cash operating cycle of the company to the nearest day.

(6 Marks)

(b) One of the measures taken by the Government of Nigeria to enhance the status of Small and Medium Scale Enterprises is the establishment of Small and Medium Scale Equity Investment Scheme. List FOUR objectives of the Scheme.
(4 Marks)

(c) State FIVE benefits of strategic planning to an organisation. (5 Marks)
(Total 15 Marks)

QUESTION 5

Karaole Technology Limited is a software business owned and managed by two computer software specialists. Although, sales have remained stable at ₦40,000,000 per annum in recent years, the level of trade receivable has increased significantly. A recent financial report submitted to the owners indicates an average settlement period of 60 days for trade receivable compared with an industry average of 40 days. The level of bad debts has also increased in recent years and the company now writes off approximately ₦40,000 bad debts each year.

The recent problems experienced in controlling credit have led to a liquidity crisis for the company. At present, the company finances its trade receivables by a bank overdraft on an interest rate of 14% a year. However, the overdraft limit has been exceeded on several occasions in recent months and the bank is now demanding a significant decrease in the size of the overdraft.

To meet this demand, the owners of the company have approached a factor who has offered to make an advance payment equivalent to 85% of trade receivables based on the assumption that the level of receivables will be in line with the industry average.

The factor will charge a rate of interest of 12% a year for this advance. The factor will take over the sales records of the Company and, for this service, will charge a fee based on 2% of sales. The company believes that the services offered by the factor should eliminate bad debts and lead to administrative cost savings of ₦52,000 per year.

Required:

(a) Calculate the effect of employing a debt factor on the profit of Karaole Technology Limited. Comment on your findings. (8 Marks)

Note: You may assume 360 days in a year.

(b) State FIVE potential advantages and TWO disadvantages of using the services of a debt factor by a business organisation. (7 Marks)

(Total 15 Marks)

QUESTION 6

The management of Ballserve Plc. disagreed with the financial controller of the company for using Walter's Model in estimating its share value. One director was of the opinion that Gordon's model would have presented a better position because of the company's dividend policy of 40% payout ratio. The cost of capital is 7.5% and the earnings per share is 285 kobo.

Required:

(a) Explain the importance of Walter's dividend model and state THREE assumptions of the model. (8 Marks)

(b) Discuss THREE limitations of Walter's model. (3 Marks)

(c) (i) Calculate the share values at the payout ratios of 40% and 60% respectively and an internal rate of return of 7.5% on each occasion. (2 Marks)

(ii) Calculate the share values at the payout ratios of 40% and 60% respectively and an internal rate of return of 12% on each occasion. (2 Marks)

(Total 15 Marks)

SOLUTIONS TO SECTION A

PART I - MULTIPLE-CHOICE QUESTIONS

1. C
2. D
3. D
4. C
5. E
6. C
7. D
8. A
9. C
10. B
11. A
12. E
13. B
14. D
15. D
16. D
17. A
18. C
19. A
20. A

WORKINGS

15. $\frac{d}{ke} = \frac{10k}{0.15} = 66.67\ k$

= 67k

16.

No of shares	Share Price	
4	₦1.60	= ₦6.40
1	₦1.30	= ₦1.30

$\underline{5}$ $\qquad\qquad\qquad$ $\underline{\underline{₦7.70}}$

Ex-rights price = $\frac{₦7.70}{5}$

= ₦1.54

Value of the rights = ₦1.54 −₦1.30

= 24k

18. EOQ = $\sqrt{\frac{2cd}{hc}}$

$= \sqrt{\frac{2 \times ₦250 \times 2{,}000}{₦4}}$

$= \sqrt{250{,}000}$ = 500 drums

No of orders = $\frac{2{,}000}{500}$

= $\underline{\underline{4}}$

EXAMINERS' REPORT

The questions cover a reasonable part of the syllabus.
Candidates' performance was average.

Candidates are advised to cover the syllabus adequately before attempting the examinations of the Institute.

PART II – SHORT-ANSWER QUESTIONS

1. Agency
2. Economic
3. Corporate governance
4. ₦50,000
5. ₦26.25
6. 1.2
7. Safety stock /Buffer stock /Minimum level

8. 3 years (Minimum)

9. To take care of the associated risk

10. ₦153.33

11. 42.86%

12. Portfolio analysis

13. Entrepreneurship

14. Conglomerate diversification

15. Decision tree

16. ₦400 million

17. Paris club

18. Non-sterilised intervention

19. Economic exposure

20. Economic Order Quantity (EOQ)

WORKINGS

4. Let i represent the interest charge.

Therefore:

$\frac{₦(300{,}000+i)}{i} = 7$

₦300,000 $+ i = 7i$

$6i$ = ₦300,000

$i = \frac{300{,}000}{6}$

= ₦50,000

5. MV = $\frac{d(1+g)}{r-g}$ where

MV = Market Value

d = Dividend

r = rate of return or interest

g = growth rate

MV = $\frac{d(1+g)}{r-g} = \frac{₦2.50(1.05)}{0.15-0.05} = \frac{₦2.625}{0.10}$ = ₦26.25

6. Market Return % Security K-Return (%)

Market Return %	Security K-Return (%)
5	-2
25	38
30	36

Beta $= \frac{36}{30}$ = 1.2

10. $\frac{a\,(1+b)n}{1+c}$

Where a is exchange in naira, b = inflation rate in Nigeria, c = inflation rate in the US and n = number of years

i.e $\frac{₦\,140\ (1.15)}{1.05} = \frac{₦161}{1.05}$ = ₦153.33

11. Effective rate of interest = $\frac{p-[p \times (I-r)]}{p\,(I-r)}$

where P = Principal sum, r = rate of interest

$\frac{₦20m-(₦20m \times 0.70)}{₦20m \times 0.70}$

$\frac{₦20m-₦14m}{₦14m} = \frac{₦6m}{₦14\,m}$

= 0.4286 OR 42.86%

16. PV = $\frac{V}{i}$ where

PV = Present Value

i = interest

V =Value

i.e $\frac{₦40m}{0.10}$

= ₦400 million

EXAMINERS' REPORT

The questions cover a reasonable part of the syllabus.
Almost all the candidates attempted the question but performance was below average.

Candidates are advised to cover the syllabus adequately and read relevant text books and reputable local and international journals and also visit the websites to facilitate better performance in future.

SECTION B

SOLUTION TO QUESTION 1

(a) The following are the various options available to Nagode Limited:

(i) Merger: The term merger is normally used to describe a situation where two businesses come together by agreement to form a single entity. Here, the two companies go into liquidation and an entirely new one is formed to acquire their shares. Alternatively, the life of one company is, in law, terminated (still in physical existence as a division or branch) and the other one remains.

(ii) Take over: This describes a situation where one business acquires control of another business. This usually occurs when one company buys shares in another company substantial enough to acquire a controlling interest in the other company. The former is called the bidding company while the latter is called the target company.

(iii) Consolidation: This is a combination of two or more companies into a new company.

(b)

- Exchange ratio = 40/80 = 1:2 (one share of Nagode Limited exchanges for every two shares of Adawa Limited.)

- Number of shares to be issued to shareholders of Adawa Limited = 3,000,000/2 = 1,500,000

- Combined post merger number of shares = 5,500,000 (i.e 4,000,000 +1,500,000)

- Combined post acquisition earnings = ₦29,000,000 (i.e ₦20,000,000 + ₦9,000,000)

- Post merger earnings per share of enlarged company –Nagode Limited = ₦29,000,000/5,500,000 = ₦5.27

Comment:

The merger improves the Earnings Per Share (EPS) of Nagode Limited from ₦5.00 to ₦5.27. However, the shareholders of Adawa Limited suffer a drop in their EPS from ₦3.00 to ₦2.64 (i.e ₦5.27/2)

EXAMINERS' REPORT

The question tests candidates' knowledge of corporate restructuring, mergers and acquisitions and its financial effects on the shareholders of merged companies.

Candidates performed poorly because most of them did not understand the requirements of the question.

Candidates are advised to read, understand and interprete questions appropriately and note their specific requirements before attempting them.

SOLUTION TO QUESTION 2

Year	DF (10%)	1	2	3
		₦'000	₦'000	₦'000
0	1.0000	(1,500.00)	(1,500.00)	(1,500.00)
1	0.9091	(272.73)	(272.73)	(272.73)
2	0.8264		(495.84)	(495.84)
3	0.7513	_______	_______	(563.48)
		(1,772.73)	(2,268.57)	(2,832.05)
PV of scrap		954.56	619.80	450.78
NPV		(818.17)	(1,648.77)	(2,381.27)
Annuity factor		0.9091	1.7355	2.4868
Annual Equivalent Cost:		(899.98)	(950.02)	(957.56)

The optimal replacement cycle is one-year because it has the lowest cost.

ALTERNATIVE SOLUTION

Decision: Replace every 1 year.

Year	Cash Flow	DF@ 10%	PV
	₦		₦
0	(1,500,000)	1.0000	(1,500,000)
1	(300,000)	0.9091	(272,730)
1	1,050,000	0.9091	954,555
			(818,175)

Replace every 2 years

Year	Cash Flow	DF@ 10%	PV
	₦		₦
0	(1,500,000)	1.0000	(1,500,000)
1	(300,000)	0.9091	(272,730)
2	(600,000)	0.8264	(495,840)
2	750,000	0.8264	619,800
			(1,648,770)

Replace every 3 years

Year	Cash Flow	DF@ 10%	PV
	₦		₦
0	(1,500,000)	1.000	(1,500,000)
1	(300,000)	0.9091	(272,730)
2	600,000	0.8264	(495,840)
3	750,000	0.7513	(563,475)
3	600,000	0.7513	450,780
			(2,381,265)

Calculation of Annual Equivalent Value (AEV)

Every 1 year	(818,175)/0.9091	=	(899,984)
Every 2 years	(1,648,770)/1.7355	=	(950,026)
Every 3 years	(2,381,265)/2.4868	=	(957,562)

(b) Areas of relevance of Information Technology to investment decision include:

- Spread sheet models that incorporate present value analysis of expected cashflows.
- Probability analysis of risk to determine optimal mix of capital projects.
- Generation of random numbers for solving models that simulate real life situations.
- Investment decisions when there is capital rationing using linear programming.

(c) Rate = 0.10
Nper = 5
Pmt = nil
FV = ₦400,000
Type = nil

EXAMINERS' REPORT

Part 'a' of the question tests candidates' understanding of replacement decision while parts 'b' and 'c' test candidates' knowledge of the application of Information Technology in Financial Management process.

About 85% of the candidates attempted the question and performance was average.
Candidates' commonest pitfall in parts 'b' and 'c' of the question was their inability to understand the requirements of the parts, hence they failed to proffer correct solutions to them. Instead of addressing the areas of usefulness of Information Technology (IT) to investment decisions, candidates were writing on the benefits of Information Technology as a tool in Financial Management process.

Candidates are advised to cover the syllabus adequately, work on past questions in the Institute's PATHFINDER and improve their knowledge in Information Technology, particularly the application of spreadsheet in solving Financial Management problems.

SOLUTION 3

(a) Determination of the expected future exchange rates based on the information that Rand is expected to appreciate by 2% per annum. Value of Rand today in terms of naira is ₦22 per Rand. This is expected to appreciate by 2% per annum. Therefore:

Yr			₦
0	Spot	=	22.00
1	22(1.02)	=	22.44
2	$22\,(1.02)^2$	=	22.89
3	$22(1.02)^3$	=	23.35

In order to determine the cost of capital in Rand using Interest Rate Parity, the following formula is adopted.

$$\frac{1+RF}{1+RD} = \frac{S}{F}$$

where RF= Foreign Rate, RD = Domestic Rate, S = Spot Rate and F = Future Rate

$$\frac{1+RF}{1+0.10} = \frac{22}{22.44}$$

22.44 (1+RF) = 22(1.1)

22.44RF = 22(1.1) – 22.44

$:.\ RF = \frac{22(1.1) - 22.44}{22.44} = \frac{24.2 - 22.44}{22.44}$

RF = 7.8% ≅ 8%

Computation of the Rand NPV.

Year	Cash Flow (Rand'm)	Discount Factor (8%)	Present Value (Rand'm)
0	(160)	1.0000	(160.000)
1	80	0.9259	74.072
2	96	0.8573	82.301
3	64	0.7938	50.803
		Net Present Value(NPV)	47.176

Since the NPV at the required rate of return gives a positive value, the project is viable.

ALTERNATIVE SOLUTION

Year	Cash Flow (Million Rand)	Discount Factor (7.8%)	Present Value (Million Rand)
0	(160)	1.0000	(160.00)

1	80	0.9276	74.21
2	96	0.8605	82.61
3	64	0.7983	51.09
		Net Present Value	47.91

(b) Reasons why business organisations engage in cross-border investment include the following:

(i) To take advantage of new markets e.g coca-cola, electronics etc

(ii) To seek raw material e.g Us Oil companies establishing business in nations where there are oil deposits.

(iii) In search of new technology.

(iv) Avoidance of political and regulatory hurdles.

(v) Diversification.

(vi) Tax avoidance.

(vii) Possible benefits from variations in exchange rates.

(viii) Protection of profit margin.

(ix) Depriving another firm of any abnormal profit

EXAMINERS' REPORT

The question tests candidates' knowledge of capital budgeting and International Financing under International Financial Management Section of the syllabus.
About 80% of the candidates attempted the question but most of them did not have clear and accurate understanding of part 'a' of the question.

In addition, candidates' commonest pitfall in the part 'a' of the question was their inability to compute the expected future exchange rate which would have enabled them determine the discount factor using the interest rate parity formula. The resulting rate is expected to be used in discounting the expected cash flows from the project in order to determine its viability.

Candidates are advised to read, understand and interprete questions appropriately before attempting them. They should also acquaint themselves with key formulae.

SOLUTION 4

(a) Calculation of cash operating cycle:

Cost of sales is 75% of sales i.e 75% x ₦8,400,000 = ₦6,300,000 since gross profit
margin is 25%.

Purchases = 50% of ₦6,300,000 = ₦3,150,000.

Thus,

Days

Raw materials holding period = $\frac{Av.Inventory\ of\ RM}{Annual\ Purchases}$ × 365 i.e $\frac{₦330,000}{₦3,150,000}$ x $\frac{365}{1}$ =38

Average Payables period = $\frac{Av.Account\ Payable}{Annual\ purchases}$ x 365 $i.e$ $\frac{₦315,000}{₦3,150,000}$ x $\frac{365}{1}$ =37

Average Production period = $\frac{Av.Inventory\ of\ Work\ in\ progress}{Annual\ Cost\ of\ Sales}$ x degree of completion x 365 i.e $\frac{₦825,000}{₦6,300,000}$ x 0.8 x $\frac{365}{1}$ = 38

Average Finished stock holding period = $\frac{Av.Stock\ of\ FG}{Annual\ COS}$ x 365 i.e $\frac{525,000}{6,300,000}$ x $\frac{365}{1}$ = 30

Average Receivables' collection period = $\frac{Av.Account\ Receivable}{Annual\ sales}$ x 365 i.e $\frac{759,000}{8,400,000}$ x $\frac{365}{1}$ = <u>33</u>

Length of cash operating cycle <u>102</u>

where: COS = Cost of Sales
FG = Finished Goods

(b) The objectives of Small and Medium Scale Equity Investment Scheme include the following:

(i) Facilitation of the flow of funds for the establishment of new Small and Medium Scale Enterprises and reactivation, expansion or restructuring of on-going projects.

(ii) Stimulation of economic growth, development of local technology and generation of employment for suitable and capable Nigerians.

(iii) Management and stimulation of corporate governance in the Small and Medium Scale Enterprises.

(iv) Elimination of interest and other financial charges burden on the entrepreneurs.

(v) Provision of financial advisory, technical and material support to the entrepreneurs through consultancy.

(c) The benefits accruing to a business organisation from strategic planning include the following:

(i) The purpose of organisation is clearly defined for the establishment of realistic goals and objectives consistent with that mission in a defined time frame given the organisation's capacity for implementation.

(ii) Communication of goals and objectives to the organisation's departments and units.

(iii) Development of a sense of ownership of the plan.

(iv) Making the most effective use of the organisation's resources based on key priorities.

(v) Provision of basis for performance measurement and establishment of mechanism for informed change as required.

(vi) Integrating everyone's best and most reasoned efforts to achieve important value in building a consensus about where an organisation is going.

(vii) Provision of clearer focus of the organization to produce greater efficiency and effectiveness.

(viii) Bridging the gap between staff and Board of Directors.

(ix) Building strong teams within the organisation.

(x) Achievement of great satisfaction among planners based on a common vision.

(xi) Ensuring increased productivity through increased efficiency and effectiveness.

(xii) Solving major problems.

(xiii) Ensuring a strong tie among the Board members.

EXAMINERS' REPORT

Part 'a' of the question tests candidates' knowledge of cash operating cycle under working capital management section of the syllabus. Part 'b' tests candidates' understanding of the objectives of Small and Medium Scale Equity Investment Scheme (SMEEIS) under Small and Medium Scale Enterprise (SMEs) while part 'c' focuses on strategic planning.

About 90% of the candidates attempted the question but most of them showed lack of understanding of the question, particularly parts 'b' and 'c' hence the performance was poor.

Candidates' commonest pitfalls were their inability to distinguish between SME and SMEEIS in part 'b' of the question and the importance of strategic planning in an organisation in part 'c'. For part 'a', some candidates were unable to compute the cash operating cycle due to their inability to determine the correct formula to use for each item in the operating cycle.

Candidates are advised to read wide and cover the syllabus adequately for better result in future.

SOLUTION 5

Karaole Technology Limited

(i) Cost of current policy – Credit sales

Credit sales	₦40 million per annum
Average credit period	60 days

The annual cost is as follows: ₦

Cost of financing receivables: $\frac{60}{360} \times \frac{₦40million \times 0.14}{1}$ = 933,333

Bad Debts: 0.5% x ₦1,500,000	40,000	
Total Cost		973,333

(ii) Cost of using a factor

80 percent of credit sales financed by the factor would be 85 percent of ₦40,000,000 = ₦34,000,000.

For a consistent comparison, we must assume that 15% of credit sales would be financed by a bank overdraft.

The average period would be only 60 days (but 40 days – industry average-is to be adopted)

In view of the above, the annual cost of using a factor would be as follows:

	₦
Factor's finance charges: $\frac{40}{360}$ x $\frac{(0.85 \ x \ ₦40m) \ x \ 0.12}{1}$	453,333
Bank overdraft (interest) $\frac{40}{360}$ x $\frac{(0.15 \ x \ ₦40m) \ x \ 0.14}{1}$	93,333
	546,666
Factor's service charge: 0.02 x ₦40m	800,000
	1,346,666
Less: Savings in Company's administration cost	52,000
Cost of using a factor	1,294,666

Comment:

Factoring is more expensive in this case because of the 2 percent charge on sales that is ₦800,000. This appears too high . However, since the service charge cannot be eliminated or reduced (in this case), the resulting difference of ₦321,333 (₦1,294,666- ₦973,333) makes factoring of the company's debt unattractive hence it is not advisable for Karaole Technology Limited to engage the services of a factor.

(b) Potential advantages of using the services of a debt factor include the following:

- Savings in the cost of credit administration
- Releasing key staff engaged in debt recovery exercise for other tasks

- Greater certainty in cash inflow.

- Receiving advice on the credit worthiness of customers.

- In the case of full service non-recourse factoring, the company will be provided with full or partial protection against bad debts.

- The fear customers have for factors may prompt the debtors to pay up.

- Receiving information on market trends, competitors and customers.

ii Potential disadvantages of using the services of a debt factor include the following:

- It is an indication that the business is experiencing financial difficulties which may have an adverse effect on the confidence of customers, suppliers and staff.

- It may increase the operating cost of the company.

- In the case of full service recourse factoring, the company is not protected against the risk of bad debts.

EXAMINERS' REPORT

The question tests candidates' knowledge of debt collection techniques with particular emphasis on debt factoring and its effects on a firms profit.
About 95% of the candidates attempted the question and performance was average. 70% of the candidates that attempted the question did not understand the requirements of part 'a' of the question but many of them performed well in part 'b'

Candidates' commonest pitfall in part 'a' of the question was their failure to compute the cost of employing a factor for comparison with the cost of collecting debts internally.

Candidates are advised to adequately cover the syllabus and work on past questions making use of the Institute's PATHFINDER when preparing for the Institute's examinations.

SOLUTION 6

(a) Professor James E. Walter argues that the choice of dividend policies almost always affects the value of the firm. The model shows the importance of the relationship between the firm's rate of return and its cost of capital in determining the dividend policy that will maximize the wealth of shareholders.

The model is based on the following assumptions:

(i) Internal Financing - It assumes that the firm finances all investments through retained earnings, that is, debt or new equity is not issued.

(ii) Constant return and cost of capital – The firm's rate of returns, r, and its cost of capital, k, are constant.

(iii) 100 percent payment or retention– All earnings are either distributed as dividends or wholly re-invested internally immediately.

(iv) Constant Earnings Per Share and Dividend–Beginning Earnings and Dividends never change.

(v) Infinite time - The firm has a very long or infinite life.

(b) Limitations of Walter's Model:

The following are the critical evaluation of some of the assumptions underlying the model.

(i) No external financing - It assumes that there is no external financing and that investment opportunities of the firm are financed by retained earnings only. When such a situation exists, it is either the firm's investment or its dividend policy or both will be sub-optimal.

(ii) Constant rate of return (r)– This is based on the assumption that 'r' is constant. In fact, "r" decreases as more and more investment is made. This reflects the assumption that the most profitable investments are made first before the poorer investments. It assumes that the firm's earnings should be distributed when "r" is less than "k". This is clearly an erroneous assumption as it will fail to optimise the wealth of the owners.

(iii) Constant opportunity cost of capital (k)– A firm's cost of capital or discount rate, k, does not remain constant, it changes directly with the firm's risk. Thus, the present value of the firms' income moves inversely with the cost of capital. By assuming that the discount rate, k, is constant, Walter's model distracts from the effect of risk on the value of the firm.

c. Using Gordon's model, the calculation is as follows:

Gordon's Model

$$P = \frac{EPS\,(1-b)}{k-br}$$

where

EPS = Earnings per share

P = market price per share

1-b = payout ratio

k = the cost of of capital

r = internal rate of return (IRR) or ROE

b = retained earnings

(i) Ballserve Plc's share value at an Internal Rate of Return of 7.5 percent.

- Share value at 40 percent payout ratio is as follows:

$$MV = \frac{₦2.85\ (1-0.60)}{0.075-(0.60\ x\ 0.075)}$$

$$= \frac{₦1.14}{0.075-0.045} = \frac{₦1.14}{0.03}$$

=₦38

Share Value at 60% payout ratio:

$$MV = \frac{₦2.85\ (1-0.40)}{0.075-(0.40-0.075)}$$

$$= \frac{₦2.85\ x\ 0.60}{0.075-0.03} = \frac{₦1.71}{0.045}$$

= ₦38.00

(ii) Ballserve Plc's share value @ an Internal Rate of Return (IRR) of 12 percent

- At 40 per cent pay out ratio

$$MV = \frac{₦2.85\ (1-0.60)}{0.075-(0.60\ x\ 0.12)}$$

$$= \frac{₦2.85\ x\ 0.40}{0.075-0.072} = \frac{₦1.14}{0.003}$$

= ₦380.00

At 60 percent payout ratio

$$MV = \frac{₦2.85\ (1-0.40)}{0.075-(0.40\ x\ 0.12)}$$

$$= \frac{₦2.85\ x\ 0.60}{0.075-0.048} = \frac{₦1.71}{0.027} = ₦63.33$$

ALTERNATIVE SOLUTION USING WALTER'S MODEL

$$P = \frac{DIV}{k} + \frac{(EPS - DIV)r/k}{K}$$

OR

$$P = \frac{DIV + (EPS - DIV)r/k}{k}$$

Where P is market price per share
DIV is dividend per share
EPS is earnings per share
r is firm's rate of return (average)
k is the firm's cost of capital or capitalization rate

(i) Ballserve Plc's share value @ an Internal Rate of Return (IRR) of 7.5%

At 40 percent payout ratio

$$Mv = \frac{₦2.85\ (1-0.60) + \{(₦2.85 - ₦2.85\,(1-0.60)\}0.075/0.075}{0.075}$$

$$= \frac{(₦2.85\ x\ 0.40) + \{₦2.85 - (₦2.85\ x\ 0.40)\}}{0.075}$$

$$= \frac{₦1.14 + (₦2.85 - ₦1.14)}{0.075} = \frac{₦1.14 + ₦1.71}{0.075}$$

$$= \frac{₦2.85}{0.075} = ₦38.00$$

At 60 per cent payout ratio

$$MV = \frac{₦2.85\ (1-0.40) +\ ₦2.85 - ₦2.85\ (1-0.40)0.075/0.075}{0.075}$$

$$= \frac{(₦2.85\ x\ 0.60) + \{₦2.85 - (₦2.85\ x\ 0.60)\}}{0.075} =$$

$$= \frac{₦1.71 + (₦2.85 - ₦1.71)}{0.075} = \frac{₦1.71 + ₦1.14}{0.075}$$

$$= \frac{₦2.85}{0.075} = ₦38.00$$

(ii) Ballserve Plc's share value at an Internal Rate of Return (IRR) of 12 percent
At 40 percent payout ratio.

$$MV. = \frac{₦2.85\ (1-0.60) + \{₦2.85 - ₦2.85(1-0.60)\}0.12/0.075}{0.075}$$

$$= \frac{(₦2.85\ x\ 0.40) + \{₦2.85\ -(2.85\ x\ 0.40)\}\ 1.60}{0.075}$$

$$= \frac{₦1.14 + (₦2.85 - ₦1.14)1.6}{0.075} = \frac{₦1.14 + ₦2.736}{0.075}$$

$$= \frac{₦3.876}{0.075} = ₦51.68$$

At 60 percent payout ratio

$$MV = \frac{₦2.85\ (1-0.40) + \{₦2.85 - ₦2.85\ (1-0.40)\}0.12/0.075}{0.075}$$

$$= \frac{(₦2.85\ x\ 0.60) + \{₦2.85 - (₦2.85\ x\ 0.60)\}1.60}{0.075}$$

$$= \frac{₦1.71 + (₦2.85 - ₦1.71)1.60}{0.075} = \frac{₦1.71 + ₦1.824}{0.075}$$

$$= \frac{₦3.534}{0.075} = ₦47.12$$

EXAMINERS' REPORT

The question tests candidates' appreciation of the theoretical arguments put forward by Professor James E. Walter and Myron Gordon on the choice of dividend policy.
Candidates did not understand the question, hence about 20% of them attempted it and they performed poorly.

The commonest pitfalls of the few candidates that attempted the question were their inability to differentiate between Walter's theory and Gordon's theory and their assumptions. In addition, they did not have knowledge of the models (formulae) hence they could not compute the share value as required by the question.

Candidates are advised to always cover the syllabus adequately and give consideration to all sections of the syllabus in their preparation for the Institute's examinations. They should also endeavour to remember key formulae (models).

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA
PROFESSIONAL EXAMINATION II
ADVANCED TAXATION – MAY 2012

Time Allowed – 3 hours

SECTION A: Attempt All Questions

PART I: MULTIPLE-CHOICE QUESTIONS (20 Marks)

Write only the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions:

1. Which ONE of the following is NOT an allowable deduction for tax purposes?

   A. Any sum payable by way of interest on any money borrowed and employed as Capital in acquiring the profits
   B. Any expense incurred for repair of premises, plant, machinery or fixtures employed in acquiring the profits or for the renewals, repair or alteration of any implement, utensil or articles so employed
   C. Other deductions as may be prescribed
   D. Capital repaid or withdrawn and any expenditure of a Capital nature
   E. Any contribution to a Pension, Provident or other Benefits Fund, Society or Scheme approved by the Joint Tax Board

2. Which ONE of these is NOT a limitation to efficient tax administration?

   A. Inadequate funding of Tax authorities
   B. Tax Evasion
   C. Poor governance
   D. Loopholes in the Law
   E. Voluntary Compliance

3. Which ONE of the following taxes has been expunged from the Nigerian Tax Laws?

   A. Personal Income Tax
   B. Value Added Tax
   C. Capital Transfer Tax
   D. Education Tax
   E. Capital Gains Tax

4. Under the Personal Income Tax Act, CAP P8 LFN 2004, which ONE of the following is central in determining a tax payer's relevant tax authority?

   A. Revenue profile
   B. Expenditure pattern
   C. Residence
   D. Arbitration
   E. Employment

5. Under Personal Income Tax Act CAP P8, LFN 2004, which ONE of the following determines incomes that cannot be taxed in Nigeria

   A. Accruing in Nigeria
   B. Derived in Nigeria

C. Brought into Nigeria
D. Distributed in Nigeria
E. Received in Nigeria

6. Under the Companies Income Tax Act, CAP C21 LFN 2004, which ONE of the following is an allowable expenditure for tax purposes?

A. Any sum recoverable under an insurance or contract of indemnity
B. Depreciation of any asset
C. Interest on money borrowed and employed as capital
D. All appropriations of profit
E. Capital repaid or withdrawn and any expenditure of a capital nature

7. Where turnover is ₦500,000 or below and the company has been in business for at least four calendar years, which ONE of the following is NOT applicable for computing Minimum Tax?

A. 0.5% of Gross Profit
B. 0.5% of Net Assets
C. 0.25% of Paid-up Capital
D. 0.01% of Working Capital
E. 0.25% of the Turnover

8. Under the Petroleum Profits Tax Act CAP P13 LFN 2004, which ONE of the following is an Allowable Expenditure?

A. Rent of or cost of repairs to any premises or part of premises not incurred for petroleum operations
B. Any disbursements or expenses not wholly and exclusively paid out or expended or not wholly or exclusively incurred for petroleum operations purposes
C. All sums by way of duty, customs and excise duties, stamp duties, education tax, tax other than PPT or any other rate, fee or other like charges
D. Any Capital employed in improvements as distinct from repairs
E. Payment to unapproved Provident, Savings, Widows and Orphans or other Society, Scheme or Fund

9. Under the Stamp Duties Act CAP S8 LFN 2004, which ONE of the following does NOT fall under Fixed Duties?

A. Mortgages
B. Insurance Policy (Non Life)

C. Cheque Leaves
D. Memorandum and Articles of Association of Companies
E. Debentures Trust Deeds

10. Under the Companies Income Tax Act CAP C21 LFN 2004, which ONE of these penalties is payable by a company that fails to file tax returns as and when due?

A. ₦25,000 in the first month of default and ₦1,000 for each subsequent month in which default continues
B. ₦5,000 in the first month of default and ₦500 for each of the subsequent months of default
C. ₦25,000 in the first month of default and ₦5,000 for each subsequent month in which default continues
D. ₦500 in first month of default and ₦400 per month in subsequent months of default
E. ₦20,000 in the first month of default and ₦5,000 in each subsequent month of default

11. The Nigerian National Gas Marketing Plc, partly owned by Government, has just been privatised. The tax implication of this exercise is that the

A. Company will not be subject to tax under CITA or other relevant Acts
B. Company continues to fulfil its tax obligations under CITA and other relevant Acts
C. Company is exempted from taxes under Nigerian Tax Acts
D. Company's profits or incomes are exempted from tax in so far as they are not derived from trade or business carried on
E. Company will be subject to commencement rules in taxation

12. What is the tenure of members of the Tax Appeal Tribunal?

A. Two years, renewable for a term of two years from the date on which he/she assumes office or attains the age of 70 years, whichever is earlier
B. Two years, renewable for another term of three years from the date on which he/she assumes office or attains the age of 70 years, whichever is earlier
C. Three years, renewable for a term of one year from the date on which he/she assumes office or attains the age of 70 years, whichever is earlier
D. Three years, renewable for another term of two years from the date on which he/she assumes office or attains the age of 70 years, whichever is earlier

E. Three years, renewable for another term of three years from the date on which he/she assumes office or attains the age of 70 years, whichever is earlier

13. A Company engaged in the production of one of the following products cannot be regarded as a Pioneer Company

A. Vegetable oil
B. Aluminium roofing sheet
C. Fan milk/yoghurt
D. Cocoa products
E. Plastic and Petroleum products

14. The composition of the Technical Committee of the Federal Inland Revenue Service Board is made up of the following EXCEPT

A. Secretary to the Board
B. Legal Adviser of the Service
C. The Executive Chairman
D. Directors and Heads of Departments of the Service
E. Executive Secretary, Corporate Affairs Commission

15. The following are the incentives granted to Companies engaged in the utilisation of "associated gas" under PPTA CAP P13 LFN 2004, EXCEPT

A. Gas transferred from the Natural gas to Liquid facility to the gas-to-liquid facilities shall be 0% tax and 0% royalty
B. An Investment Tax Allowance of 15% which shall not reduce the value of the asset
C. Interest on loans for gas project is to be deductible provided that prior approval is obtained from the Federal Ministry of Finance before taking the loan.
D. Investment required to separate crude oil and gas from the reservoir into usable products shall be considered as part of the oil field development
E. The Company shall pay the minimum amount charged by the Minister of Petroleum Resources for any gas flared by the company

16. Where in the course of adjudication, the Tax Appeal Tribunal discovers evidence of possible criminality on the part of a tax payer, the tribunal shall be obliged to pass such information to all of the following, EXCEPT…………

(i) Office of the Attorney-General of the Federation
(ii) Office of the Attorney-General of any State
(iii) Office of the Solicitor-General of the Federation
(iv) Any relevant Law Enforcement Agency

A. (i) only
B. (ii) only
C. (iii) only
D. (ii) and (iii)
E. (i), (iii) and (iv)

17. The Government Agency responsible for the administration of the Value Added Tax (VAT) in Nigeria is

A. States' Inland Revenue Service
B. Value Added Tax Technical Committee
C. Federal Ministry of Finance
D. The VAT Directorate within Federal Inland Revenue Service
E. Federal Internal Revenue Service

18. Oil Mining Lease in Nigeria is a ……………………..

A. Lease for mining in Nigeria
B. Lease for mining in Nigerian offshore areas
C. Lease granted for operations in upstream activities
D. License granted under the PPTA CAP P13 LFN 2004 for the purpose of winning petroleum
E. Lease which entitles the owner to engage in drilling operations in Nigeria

19. What disclosure is NOT made on the face of the Tax Clearance Certificate in respect of the last three years of assessment?

A. Total profits or Chargeable income
B. Nature of Assessment
C. Tax payer's Identification Number (TIN)
D. Tax paid
E. Tax outstanding

20. Where two or more Banks merge to form a completely new Bank, ONE of the following represents the tax implication. Which one?

A. Only the individual merging Banks will be affected by possible implication
B. Cessation rule will be applicable to the individual merging and the new Bank
C. Cessation rule will be applicable to the individual merging Banks and commencement rules will apply to the new Bank
D. Change in accounting date rule will apply to the individual merging Banks
E. Roll-over relief provision will apply to the individual merging Banks

PART II: SHORT-ANSWER QUESTIONS (20 MARKS)

Write the answer that best completes each of the following questions/statements.

1. In the case of any property holding company, allowable deduction for tax purposes with regards to Directors' remuneration, shall not exceed .... per annum in respect of each Director.

2. The tax which impacts on the final consumer if he/she pays for certain classes of goods or services is called ....

3. Whenever a relevant Tax Board is of the opinion that tax assessed on profits or incomes of a taxable entity has been fully paid or that no tax is due on such profits or incomes, it shall issue a Tax Clearance Certificate, to the taxable entity within ....of the demand for such.

4. A newly Incorporated Company is expected to file its Returns............................ after the accounting year-end or .... from the date of Incorporation, whichever is earlier?

5. Education Tax and Value Added Tax are examples of ....and

……………………… tax respectively.

6. With regards to foreign employment, the gain or profit shall NOT be deemed to be derived from Nigeria, if the employee is not in Nigeria for a minimum period of ……………………….or more in any twelve months period commencing in a calendar year and ending either within that same year or the following year.

7. When a Company uses the proceeds of sale of one asset to buy another asset of the same category and used for the same purpose as the one sold, the Company will be entitled to enjoy……………………………… relief

8. A Company which has incurred Capital Expenditure in an approved manufacturing activity in an Export Processing Zone, shall be granted …………… per cent Capital Allowance in any year of assessment

9. State ONE procedure to be adopted in seeking extension of the period for making Statutory Tax Returns

10. Under the Petroleum Profits Tax Act, CAP P13 LFN 2004, Casing Head …………….. means any Liquid Hydrocarbons obtained in Nigeria from Natural Casing Head Gas by separation or by any chemical or physical process but before the same has been refined or otherwise treated.

11. The amount of any rent as to which there is provision for its deduction from the amount of any royalty under an Oil Prospecting License or Oil Mining Lease, to the extent that such rent is not so deducted, is known as……………………

12. A relevant tax authority's power to assess and charge tax on Turnover or Trade or Business is known as ……….……… basis of Assessment?

13. When is the tax holiday period for a Pioneer company expected to commence?

14. The process of confirming the accuracy of information for tax purposes which often calls for visits to clients' premises, is known as……………………………

15. Under Capital Gains Tax, what is claimable when the sales proceeds on an asset disposed of is fully re-invested in the replacement of the asset for the purpose of the Company's business?

16. All appeals with regards to Petroleum Profit tax assessment is usually made to the………………………………………

17. What is 'G' factor under Petroleum Profits Tax?

18. The gas that is obtained from boreholes and wells and consisting primarily of hydrocarbons is called ……………………..

19. What is "Depreciation Ratio" for the purpose of computing the Adjusted Profit of a company engaged in shipping operations?

20. If an appeal is discontinued at the instance of the tax authority, the Revenue will revise the assessment as agreed and serve notice of the …………………… on the Tax Appeal Tribunal.

SECTION B: ATTEMPT QUESTION ONE AND ANY OTHER THREE QUESTIONS (60 Marks)

QUESTION 1 - CASE STUDY

Megida Nigeria Limited commenced business on 1 July 2009. It is engaged in the importation and sale of Building materials.

The Managing Director, Chief Dandan Ogeba, had been keeping the records of the company from inception until when the Accountant, Mr. Babajide James was appointed on 1 May 2010.

The following details were provided by the Managing Director for the period 1 July 2009 to 30 April 2010.

	₦
Cost of incorporating the Company	250,000
Purchases (1July 2009 to 31 December 2009)	82,000,000
Purchases (1 January 2010 to 30 April 2010)	50,000,000
Sales (1 January 2009 to 31 December 2009)	106,600,000
Sales (1 January 2010 to 30 April 2010)	67,500,000
Depreciation (1 July 2009 to 31 December 2009)	850,000
Advertisement (1 July 2009 to 31 December 2009)	150,000
Medical (1 July 2009 to 31 December 2009)	250,000
Construction of New office block completed on 20 October 2009	10,000,000

The Managing Director has computed the Company's Tax liability as ₦9,180,000 as shown below:

Managing Director's Computation of Net Profit and Tax Liability

	₦'000	₦'000
Sales (₦106,600 + ₦67,500,000)		174,100
Purchases (₦82,000,000 + ₦50,000,000)		132,000
		42,100
Less:		
Cost of Floating the company	250	
Advertisement	150	
Medical	250	
Construction of New office block	10,000	
Depreciation	850	
		(11,500)
Net Profit		30,600
Tax on ₦30,600,000 at 30%		9,180,00

Assume that the Company makes up accounts to 31 December each year.

Ignore Capital allowance

Required:

(a) As an External Consultant appointed by the Company, compute the correct Tax Liability of the Company. (5 Marks)

(b) Compute the Education Tax Liability for the relevant year of assessment permitted by the information given above. (1 Mark)

(c) What is the Total Tax liability? (1 Mark)

(d) Give FOUR reasons why your computation is different from that of the Managing Director. (8 Marks)

(Total 15 Marks)

QUESTION 2

Some of the objectives of Taxation in a Nation are to generate revenue to meet the financing requirements of government activities and the redistribution of Income or Wealth.

Required:

(a) Highlight the functions of the Joint State Revenue Committee. (5 Marks)

(b) State the TWO possible forms of Anti-Avoidance legislation. (3 Marks)

(c) Explain the TWO broad categories of Incomes subject to tax under the Personal Income Tax Act CAP P8 LFN 2004. (4 Marks)

(d) Define Agricultural Trade or Business for the purposes of Nigerian Tax Acts. (3 Marks)

(Total 15 Marks)

QUESTION 3

Regional Commercial Bank Limited, fully owned by Nigerians, has been in banking business for the past 8 years.

You are provided with the following information extracted from the Books of the Bank:

Regional Commercial Bank Limited

	₦
Adjusted profit for year ended 31 December 2010	5,500,000
Capital allowances for the year	1,500,000
Issued Share Capital	11,200,000
Statutory Reserves	1,800,000
General Reserves	1,600,000
Long-term Loan	1,900,000

You are also informed that the following relate to the accounts for year ended 31 December 2010:

	₦
The turnover	250,000,000

The gross profit	25,000,000
The Net Assets	16,500,000
Unutilised Capital allowances brought Forward from 2010 assessment year	3,725,000

Required:

(a) Compute the Bank's Tax liabilities for 2011 year of assessment. (8 Marks)

(b) The International Financial Reporting Standards (IFRS) contains some provisions that have Income Tax implications. State THREE issues in IFRS that have some Tax implications? (3 Marks)

(c) Capital expenditures qualify for grant of Capital Allowances based on certain criteria.

(i) List FOUR categories of Capital expenditure that qualify for grant of Capital Allowances under the Companies Income Tax Act CAP C21 LFN 2004. (2 Marks)

(ii) List the conditions for granting Capital Allowances (2 Marks)

(Total 15 Marks)

QUESTION 4

Abilewa Nigeria Limited is a Pharmaceutical Company involved in the production and distribution of drugs. In an effort to have a fair share of the market, the Company has lately been involved in the research of a new drug to be used in the treatment of pancreas called Haemoxylin. To date, so much money has been committed to the project.

It has just been revealed that a competitor is developing an identical product that will threaten its anticipated market dominance. The Research and Development Director is worried by this development and is requesting, amongst other things, the release of the sum of eight million naira (₦8,000,000) to champion the cause of stopping the product from entering the market. In realisation of this, he has paid so much to an employee of the other Company to provide information on the drug. It was revealed that the sum of four million naira (₦4,000,000) was expended in the purchase of equipment for the research. Meanwhile, the food and drugs unit in the Federal Ministry of Health has been invited on the mix of the drug and has considered the need for the Company to stop further research until they are cleared.

The Managing Director, while appreciating this cheering news, unilaterally approved an additional three million naira (₦3,000,000) which was not included in the total amount for Research and Development initially approved by the Board in the Budget of the current

year. He opined that the money was genuinely spent. These commitments have been reflected in the Profit and Loss account with a total profit of ₦32,000,000 (thirty-two million naira). While this was unfolding, the Board of the Company relieved the Managing Director of his appointment. His compensation of ₦10,500,000 was paid from the Research and Development Budget.
Required:

As the Tax Consultant to the Company, you have been invited to examine the Books of Abilewa Nigeria Limited and write your report on:

(a) The determination of non-allowable Research and Development cost and the treatment of each of the amounts spent. (12 Marks)

(b) Ethical considerations arising from the case. (3 Marks)
(Total 15 Marks)

QUESTION 5

In the University of Naibawa, Professor Joda Yobo is the Dean of the Faculty of Management Sciences. He is married with three children and a dependent relative. He earns a basic salary of ₦7,200,000 per annum, an allowance of ₦1,800,000 per annum, transport and other benefits in kind are worth ₦3,000,000.

In 2010, Professor Joda Yobo was appointed by the University of South Africa in London as a visiting Professor to lecture on Integrated Accounting Technology. The University of South Africa in London has agreed to pay his fares to and fro twice per week when visiting South Africa to give lecture. The gross remuneration as agreed is £720,000 before deducting Income Tax in England. During the year, he was paid Net Income of £540,000.

The exchange rate for both currencies is ₦250 = £1.

You are required to:

(a) Compute the tax liability of Professor Joda Yobo in Nigeria after granting him Double Taxation Relief for the relevant tax year. (12 Marks)

Ignore the provisions of the Personal Income Tax (Amendment) Act 2011.

(b) State SIX main features you would expect to deal with in a Double Taxation

Agreement between two Countries. (3 Marks)

(Total 15 Marks)

QUESTION 6

Havensis Shipping company Limited was incorporated in 2006 with ₦50,000,000 as its share capital. The company commenced business on 1 January 2007 and makes up its financial statements to 31 December

	₦	₦
Income from passenger freight earned on transit terms	200,000	
Income from passenger freight into Nigeria	600,000	
Income from passenger freight out of Nigeria	200,000	
Income from passenger freight on other routes	5,200,000	
		6,200,000
Less: Administrative expenses	1,000,500	
Depreciation	1,910,000	
Other disallowable expenses	120,000	3,030,500
Net Profit		3,169,500

Required:

(a) Compute the Total Profit of Havensis Shipping Company as a foreign company, for Nigerian tax purposes. (10 Marks)

(b) How would the company be assessed to Nigerian taxation where the Federal Inland Revenue Service is not satisfied that there is a reciprocal tax exemption granted to Nigerian companies in the Shipping company's home country. (2 Marks)

(c) State the reasons why Havensis Shipping company is NOT qualified for Pioneer status. (3 Marks)

(Total 15 Marks)

SOLUTION TO SECTION A

PART 1 MULTIPLE-CHOICE QUESTIONS

1. D
2. E
3. C
4. C
5. D
6. C
7. D
8. C
9. D
10. C
11. B
12. E
13. E
14. E
15. E
16. C
17. D
18. D

19. E

20. C

EXAMINERS' REPORT

The questions covered the entire syllabus and the candidates' performance was generally above average.

PART II: SHORT ANSWER QUESTIONS

1. ₦10,000

2. Value Added Tax (VAT)

3. Two (2) weeks

4. 6 months, 18 months

5. Direct, Indirect

6. 183 days

7. Roll-over

8. 100

9. The tax payer applies in writing before the due date, stating reasons for seeking extension

10. Petroleum spirit

11. Non-productive rent

12. Best of Judgment

13. Production Day

14. Field Tax Audit

15. Roll-over Relief

16. Tax Appeal Tribunal

17. Gas Production Cost Adjustment Factor

18 Natural Gas

19. Depreciation Ratio = $\frac{\text{Global Depreciation}}{\text{Global Income}}$ x 100%

20. Discontinuance

EXAMINERS' REPORT

The questions adequately covered the syllabus. The candidates' performance was good.

SOLUTION TO SECTION B

QUESTION 1

MEGIDA NIGERIA LIMITED
COMPUTATIONS OF TAX LIABILITY FOR ASSESSMENT YEAR 2009
(1 July 2009 – 31 December 2009)

	₦'000
Net Profit (Wk 1)	23,350
Add back:	
Depreciation	850
Adjusted/Assessable Profit	24,200
Deduct:	
Capital Allowances	–
Total Profit	24,200

(a) Tax Liability – 30% of ₦24,200,000 = ₦7,260,000

(b) Education Tax – 2% of ₦24,200,000 = ₦484,000

(c) Total Tax Liability = ₦7,260,000 + ₦484,000 = ₦7,744,000

(Wk 1) Calculation of Net Profit	₦'000	₦'000
Sales		106,600
Less:		
Purchases		82,000
Gross Profit		24,600
Less:		
Advertisement	150	
Medical	250	
Depreciation	850	
		1,250
Net Profit		23,350

(d) Reasons for differences in both figures for Tax liability as derived by the Managing Director.

(i) Since the Company commenced business on 1 July 2009, the commencement rules or provisions will apply.

(ii) The Managing Director's treatment of Depreciation is wrong. Depreciation is not an allowable deduction for tax purposes, and the Consultant correctly treated it by adding it back.

(iii) Since accounts are made up to 31 December each year, the first set of accounts will cover the period 1 July 2009 to 31 December 2009 based on commencement rule.

(iv) The cost of incorporating the Company of ₦250,000, is a disallowable expense. Since it was not taken into account in arriving at Net Profit, it was not therefore added back.

(v) Only sales figure relating to the period July 1, 2009 to 31 December 2009 should be used in ascertaining the Net Profit.

(vi) Only purchase figure relating to the period 1 July 2009 to 31 December 2009 should be used in ascertaining the Net Profit.

(vii) The cost of the construction of new office block of ₦10,000,000 is of a Capital nature. It should not have been included in the ascertainment of Net Profit as done by the Managing Director. Also Capital Allowances computations were ignored as instructed.

EXAMINERS'REPORT

The question tests candidates' knowledge of Companies Income Tax Computations and treatment of capital expenditure in tax computations.

Majority of the candidates attempted the question. Performance was average.

Students had problems in computing the Net Profit correctly.

Candidates are advised to prepare adequately for future examinations.

QUESTION 2

(a) The Functions of Joint State Revenue Committee:

(i) Implement decisions of the Joint Tax Revenue Service
(ii) Advise the Joint Tax Revenue Service, the State and Local Governments on revenue matters.
(iii) Harmonise Tax Administration in the State
(iv) Enlighten the public generally on State and Local government revenue matters and
(v) Execute such other functions as may from time to time be assigned by the Joint Tax Revenue Service.

(b) The two (2) possible forms of anti-avoidance legislation are:

(i) Specific legislation to block known tax avoidance devices.
(ii) General anti-avoidance legislation which vests the Revenue with power to disregard all transactions entered into that could be proved to have been entered into solely for tax avoidance purposes.

(c) The two (2) broad categories of incomes subject to tax under the Personal Income

Tax Act are:

(i) Earned Incomes:

In relation to an individual, earned incomes mean incomes derived from a trade, business, profession, vocation or employment, carried on or exercised by him, i.e. incomes that were earned through physical, intellectual or artistic exertion as opposed to those earned passively through investment. These include profits, salaries, wages, commissions, bonuses etc.

(ii) Unearned Incomes

These are incomes derived from sources other than employment, business or reward for services rendered. Unearned incomes are investment incomes such as rental incomes, dividends, royalties, earnings from trade-marks, patents etc.

(d) Agricultural trade or business is defined in the Tax Act as any trade or business connected with:

(i) The establishment or management of plantations for the production of rubber, oil, coffee, tea and similar crops.

(ii) The cultivation or production of cereal crops, tubers, fruits of all kinds, cotton, beans, groundnuts, shea nuts, beniseed, vegetables, pineapples, bananas and plantains.

(iii) Animal husbandry, that is Poultry, Piggery, Cattle rearing, Fish farming and deep sea-fish trawling.

EXAMINERS'REPORT

The question is designed to test candidates' knowledge and understanding of some topical issues under the Nigerian Tax Laws. It covers the functions of the Joint State Revenue Committee, Anti-avoidance legislation, Incomes subject to tax under the Personal Income Tax Act, as well as the understanding of Agricultural Trade or Business for the purposes of Nigerian Tax.

Almost all the candidates attempted the question, and performance was average.

Many candidates mistook the Joint State Revenue Committee for either the Joint Tax Board or the Federal Inland Revenue Service. Some candidates could not explain the two broad categories of Income subject to Personal Income Tax or examples of Anti-avoidance legislation under the Nigerian Tax Laws.

Candidates are advised to understand the distribution between terms, concepts and organs of administration under the Nigerian Tax system.

QUESTION 3

(a) REGIONAL COMMERCIAL BANK LIMITED
INCOME TAX COMPUTATION
FOR 2011 ASSESSMENT YEAR

	₦	₦
Adjusted profit for year ended 31 October 2010		5,500,000
Deduct: Capital allowances		
Unutilized b/f from 2010	3,725,000	
For the year	1,500,000	
	5,225,000	
Maximum claimable is		
$66^2/_3$% of Assessable Profit		
i.e. $66^2/_3$% of ₦5,500,000	(3,666,667)	
		(3,666,667)
Unutilised Capital Allowance c/f	1,558,333	

Chargeable profits	1,833,333
Income tax at 30% of ₦1,833,333	550,000
Education tax @2% of Assessable profits	110,000.00

MINIMUM TAX PAYABLE

		₦
(a)	0.5% of ₦25,000,000 (Gross Profit)	125,000
(b)	0.5% of ₦16,500,000 (Net Assets)	82,500
(c)	0.25% of ₦11,200,000 (issued Capital)	28,000
(d)	0.25% of ₦500,000 (Turnover)	1,250
	Highest (a) to (d)	125,000

	₦
Turnover	250,000,000
Less	500,000
	249,500,000

-	0.125% of ₦249,500,000 (Excess Turnover)		311,875
	Add Highest (a) to (d)	125,000	
	Minimum Tax	436,875	

Summary

Since the Minimum tax is lower than the computed tax of ₦550,000, the tax payable is ₦550,000.

(b) Three issues in International Financial Reporting Standards (IFRS) that have tax implications –

(i) Employees' benefits in all forms are to be recognized as part of staff cost
(ii) Provision for impairment on property, plant and equipment.
(iii) Goodwill that should be recognized on business combination and takeover, will have Capital Gains Tax impact.
(iv) Fair value gains and losses on Investment Properties and Financial Instruments.
(v) IFRS transition adjustments.

(c)(i) Five categories of Capital Expenditure that qualify for the grant of Capital Allowances are as follows:

- Qualifying Building Expenditure
- Qualifying Industrial Building Expenditure
- Qualifying Mining Expenditure
- Qualifying Plant Expenditure
- Qualifying Furniture and Fittings expenditure
- Qualifying Motor Vehicles
- Qualifying Plantation Equipment
- Qualifying Housing Estate
- Qualifying Ranching and Plantation
- Qualifying Research & Development

(ii) Conditions for granting Capital Allowances

- The Company claiming the allowance must be the owner of the assets at the end of its basis period for a year of assessment.

- The assets must be used for the purpose of a trade or business of the Company.

- The grant is for a year of assessment and is usually against the Assessable Profits of the basis period for that year of assessment.

- A claim should be made by the Company before any Capital Allowance can be granted.
- Where the basis period for any year of assessment is less than one year, when commencement provisions are being applied, the annual allowance for that year of assessment shall be proportionately reduced.

- The relief is granted by deduction from the remainder of Assessable Profits in the computation of the Company's Total Profits. The remainder of the Assessable Profit is the Assessable Profits plus any balancing charge and any Loss Relief due, that is, Capital Allowance relief is granted after giving effect to Loss Relief.

- Unutilised allowances in the year of permanent cessation of a trade or business carried on by a Company shall be available for relief against the remainder of its Assessable Profits for the preceding years of assessment up to the fifth year-before the year of permanent cessation.

- Where a relief is to be granted to a Company after the assessment has become final and conclusive in respect of any assessment year, the Revenue Service may make such repayment or set-off of the tax in lieu of making the deduction for the amount of the relief.

- The amount of Capital Allowances calculated is generally restricted to a percentage (at present 66 $^2/_3$%) of the Assessable Profit. For any company in the Agro Allied Industry or that which is engaged in the trade or business of manufacturing is not affected by the restriction.

- The residue of expenditure is the total qualifying expenditure incurred less the total of any initial and annual allowances granted to date. Investment Allowance should not be deducted from qualifying expenditure to arrive at the residue.

EXAMINERS'REPORT

This question tests candidates' knowledge and understanding of the computation of tax liability of a commercial bank, tax implications of matters relating to IFRS as well as conditions for granting Capital Allowances.

Majority of the candidates attempted the question. Performance was average. Over 90% of the candidates who attempted the question had no clue to requirement "b" of the question whilst requirements "a" and "c" were fairly well attempted.

Candidates are advised to keep abreast of current developments in the Financial Sector of the world economy, such as the provisions of the IFRS, as they prepare themselves for this level of the Professional Examinations.

QUESTION 4

The Board of Directors
Abilewa Nigeria Limited
Pharmacy Road
Abah

Dear Sir,

<u>RE: EXPENDITURE ON RESEARCH AND DEVELOPMENT</u>

We refer to your instruction on the above subject matter and are pleased to present hereunder our report.

Research and Development Expenditure (R&D)

Qualifying R & D expenditure include those incurred on equipment and facilities, patents, licences, secret formulae or process or for information, concerning industrial, commercial or scientific processes, technical feasibility of products or processes and purchases, searching for and discovering and testing products or processes for future market use, and such similar costs which have not brought into existence, any assets. The amount deductible from profit in respect of provision for R &D is restricted to 10% of Total Profits before deduction of donation and before deduction of the R&D expenditure provision.

(a) Tax Implication of the R&D Costs.

(i) The release of ₦8,000,000 is inclusive of ₦4,000,000 expended on purchase of equipment for the research on Haemoxylin

The₦4,000,000 used to purchase equipment for research would be capitalized and 20% of the amount will be allowed as Investment Tax Credit on Qualifying expenditure

(ii) The additional ₦3,000,000 approved by the Managing Director is also disallowed for tax purpose.

(iii) The compensation of ₦10,500,000 paid to the Managing Director for loss of Office also does not qualify as R & D expenditure.

(iv) From the foregoing, the total amount released was ₦21,500,000 (wk.1) out of which ₦17,500,000 is disallowed. (wk.2)

(v) From the balance of ₦4,000,000, only ₦3,200,000 actually qualifies as R & D expenditure. (wk3)

(vi) The balance of ₦800,000 is also disallowed.

The above submission explains the final position on the determination of non-allowable Research and Development cost of Abilewa Nigeria Limited.

(b) <u>Ethical Issues</u>

(i) The Managing Director did not seek the approval of the Board before committing the additional ₦3,000,000, though the commitment passes the test of the amount being wholly, exclusively, necessarily and reasonably spent, there ought to be authorization. It is also disallowed.

(ii) It is unethical to involve a paid staff of the other Company to obtain information of their business secrets.

(iii) The Competitor and Abilewa Nigeria Limited did not seek necessary approval from the relevant regulatory bodies

Yours faithfully,

XYZ Consultants

APPENDIX

Workings

Calculation of composition of Total Research and Development Costs.

		₦	
Initial Release	8,000,000		
Additional Release		3,000,000	
Compensation to MD		10,500,000	
		₦21,500,000	(wk 1)

Less: Non Allowable Costs

Purchase of equipment	4,000,000		
Compensation to MD	10,500,000		
Additional Release	3,000,000	(17,500,000)	(wk 2)
		4,000,000	

Determination of Non-Allowable Research & Development

	₦	
Actual Research and Development	4,000,000	
10% of Total Profit (10% of ₦32,000,000)	3,200,000	
	800,000	(Wk 3)

EXAMINERS' REPORT

The question tests candidates' knowledge and understanding of what constitutes Research and Development expenditure or costs as well as the distinction between such costs and other costs when considering whether or not the costs are allowable for tax purposes. The question also examines candidates' understanding of ethical considerations arising from the actions or inactions of organs of management of the company.

Candidates' performance reflected a very poor understanding of the question. Less than half of the candidates attempted the question, and performance was poor. The main pitfall was that majority of the candidates that attempted the question, did not display knowledge of the distinction in the treatment of Research and Development costs vis-a-vis-other costs. They also displayed a complete lack of understanding of the requirements of part (b) of the question.

Candidates are advised to ensure they study distinct classifications/treatment of costs for tax purposes.

QUESTION 5

Professor Joda Yobo

Computation of Tax Liability in Nigeria for Assessment Year 2010

	₦	
Salary in Nigeria	7,200,000	
Transport Allowance	1,800,000	
Benefit-in-kind	3,000,000	
Gross Remuneration from England (£720,000 @ 250)	180,000,000	
	192,000,000	(x)
Less Relief:		
Personal (₦5,000 + 20% of ₦192,000,000)	38,405,000	
Children Allowance (2,500 x 3)	7,500	
Transport Allowance	20,000	
Rent Allowance	150,000	
Dependent Relative Allowance	2,000	
	38,584,500	(y)
Chargeable Income (x – y)	₦153,415,500	
Tax payable:		
₦30,000 at 5%	₦1,500	
₦30,000 at 10%	₦3,000	
₦50,000 at 15%	₦7,500	

₦50,000 at 20%		₦10,000
Next ₦153,255,500 at 25%		₦38,313,875
		₦38,335,875

Nigerian Rate of Tax ₦38,335,875 x 100 / ₦192,000,000 = 20%

½ of Nigerian rate of tax = 10%

Commonwealth rate of tax = ₦180,000 x 100 / ₦720,000 = 25%

Relief will be based on ½ of Nigerian rate of tax = 10%
Tax payable on Income brought into Nigeria = 20% x ₦180,000,000
= ₦36,000,000

Relief claimable thereon = 10% of ₦36,000,000 = ₦3,600,000

Net Tax liability of Prof. JodaYobo after Deduction of Double Tax Relief.

	₦
Tax liability on Total Income as computed above	38,335,875
Relief claimable thereon	(3,600,000)
Net tax Due	34,735,875

(b) Features to be dealt with in a Double Taxation Agreement

- Taxes to be covered by the Agreement e.g. Personal Income tax, Company Income tax Petroleum Profits Tax, Capital Gains Tax
- Industrial and Commercial Profits: enterprises engaged in business partly in Nigeria and partly in the other Country and vice versa.
- Profits exempted from Tax: Profits from specified trades and businesses.
- Connected person: enterprises in the two Countries under common control or where one has control over the other and profits are affected.
- Dividends, Interests and Royalties to persons resident in the other Country who are not engaged in business in the paying Company's Country.

- Director's fees and other personal or earned income.
- Methods by which the effect of double taxation is eliminated e.g. Tax Credits
- Appeal procedures
- Exchange of information by the Tax Authorities for the prevention of fraud
- Diplomatic privileges
- Date of coming into force and termination date
- Parties and scope: the two Countries concerned, the meaning of residence, persons affected, industrial and commercial enterprises, etc.

EXAMINERS' REPORT

The question tests candidates' knowledge of Double Taxation Treaty requirements. About 30% of the candidates attempted the question.

Performance was below average.

Majority of the candidates did not understand what Double Taxation Treaty is all about.

Candidates are advised to study this aspect of the syllabus.

QUESTION 6

(a) HAVENSIS SHIPPING COMPANY

Statement Showing the Total Profit for
Nigerian Tax Purposes

	₦	₦
Net Profit as per accounts		3,169,500
Less: Income from passenger freight on transit terms		200,000
		2,969,500
Add:		
Depreciation	1,910,000	
Other Disallowable Expenses	120,000	
		2,030,000
Adjusted profit		4,999,500

Havensis adjusted
Profit ratio: $\frac{₦4,999,500}{₦6,200,000} \times 100\% = 81\%$

Depreciation Relief
Ratio $\frac{₦1,910,000}{₦6,200,000} \times 100\% = 31\%$

Gross Adjusted Profit 81% x ₦200,000 = ₦162,000

Less: Depreciation relief 31% x ₦200,000 = 62,000
Total Profit ₦100,000

(b) Where the Federal Inland Revenue service is not satisfied that there is a reciprocal tax exemption granted to Nigeria Companies in the foreign country, the Federal Inland Revenue Service can apply a "fair percentage" to compute the deemed chargeable profit.

(c) Havensis Shipping Company might not be granted Pioneer status because the company is not registered in Nigeria with the Corporate Affairs Commission.
In addition, the nature of the business does not qualify it for a pioneer status.

EXAMINERS' REPORT

The question tests candidates' knowledge of taxation of Shipping or Air Transport Companies, Double Taxation and Pioneer Legislation.

Majority of the candidates attempted the question. Performance was below average. The candidates did not understand what constitutes the profit or loss of these specialised areas, especially with respect to income from transit.

Candidates are advised to have a better understanding of this area of the syllabus.

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA
PROFESSIONAL EXAMINATION II - MAY 2012
PUBLIC SECTOR ACCOUNTING AND FINANCE

Time allowed – 3 hours

SECTION A: Attempt All Questions

PART I: MULTIPLE-CHOICE QUESTIONS (20 Marks)

Write only the alphabet (A, B, C, D or E) that corresponds with the correct option in each of the following questions:

1. Which ONE of the following is dealt with by International Public Sector Accounting Standard No 2?

   A. Presentation of Financial Statements
   B. Cash Flow Statements
   C. Construction Contracts
   D. Leases
   E. Procurement

2. A Local Government Council Chairman shall

   i. Ensure compliance with the existing financial guidelines on receipt and payment procedures
   ii. Issue instructions relating to the spending of public funds by the Accounting Officer
   iii. Render monthly statements of income and expenditure to the legislative arm

   A. i
   B. ii
   C. iii
   D. i and ii
   E. i, ii and iii

3. The following are the objectives of Bureau of Public Procurement EXCEPT

   A. Harmonization of existing government policies on public procurement
   B. Ensuring probity, accountability and transparency in the procurement process
   C. Establishment of pricing standards and benchmarks
   D. Ensuring competitive, transparent and value-for-money standards and practices
   E. Awarding procurement contracts to selected contractors

4. For which ONE of the following functions will government corporations NOT obtain the approval from the supervising ministry?

   A. The budget
   B. Signing of Foreign Agreement
   C. The Bye-Law
   D. Payment of staff monthly salaries
   E. Increasing the price of its goods and services

5. The functions of the National Council on Public Procurement as established under the Public Procurement Act, 2007, include the following EXCEPT

   A. Consider, approve and amend the procurement, monetary and prior review threshold
   B. Consider and approve public procurement policies
   C. Approve the appointment of the Directors of the Bureau of Public Procurement
   D. Establish pricing, standards and benchmarks
   E. Approve changes in the procurement process

6. The power of the Revenue Mobilisation Allocation and Fiscal Commission, as specified in the Third Schedule, Part1 (N) of the constitution, provides for all the following EXCEPT

   A. Monitoring the accruals to and disbursement of revenue from the federation Account
   B. Advising the Federal and State governments on fiscal efficiency and methods

by which their revenue can be increased

C. Determine the remuneration appropriate for political office holders and the holders of the offices mentioned in Sections 84 and 124 of the 1999 Constitution

D. Review, from time to time, the revenue allocation formulae and principles in operation to ensure conformity with changing realities, provided that the formula has been accepted by an Act of the National Assembly for a period of not less than three years

E. Discharge such other functions as delegated by the 1999 Constitution or any Act of the National Assembly

7. Under Section 31(7) of the Public Procurement Act, 2007, which ONE of the following is NOT regarded as a major deviation during the examination of bids?

A. Sub-contracting not provided for in the contract
B. The fact that the bidder is not invited
C. The fact that the bidder is not pre-qualified
D. The bid documents are not signed
E. The bid is not submitted promptly

8. Which ONE of the following is NOT true about the operating surplus of and general reserve fund of the Central Bank of Nigeria, as specified under Section 5 of its 2007 Act?

A. Determining the operating surplus which is the residual sum from its income and other receipts less all expenditure approved by the Board
B. Establishing a general reserve fund
C. Allocating, at the end of each financial year, one-third of the operating surplus for the year to itself.
D. Making provision for the contribution to staff pension funds, in accordance with the Pension Reform Act, 2004 and for any other purpose approved by the Board for the year
E. Paying the balance of the operating surplus to the Federal Government half-yearly

9. In order to enhance efficiency in the preparation of the accounts of Ministries and Extra-Ministerial Agencies, expenditures are expected to be classified in accordance with

A. Treasury Circulars

B. Civil Service Rules
C. Financial Regulations
D. Estimates
E. Accounting Codes

10. The National Assembly approved the sum of ₦0.84 billion for the maintenance of three buildings in 2010. The National Assembly also confirmed that additional two would be ready for use on 1 January 2011. The inflation factor was set at 30%. Calculate the budgetary proposal for the maintenance of all the five buildings in 2011.

A. ₦1.89 billion
B. ₦1.82 billion
C. ₦1.40 billion
D. ₦1.092 billion
E. ₦0.86 billion

11. Which ONE of the following is an advantage of public debt?

A. It crowds out private investments
B. It leads to capital formation
C. Debt servicing distorts income
D. Debt servicing may require taxation
E. Public debt may tend to be inflationary

12. In order not to stifle growth and economic stability, government should

A. Reduce the country's debt service ratio to a manageable size
B. Finance fiscal deficits with bank loans
C. Increase recurrent expenditure relative to capital expenditure
D. Withdraw tax incentives granted to local industries
E. Increase import duties imposed on imported raw materials

13. The sources of domestic public debt in Nigeria include all but ONE of the following

A. Statutory corporations and individuals
B. Central Bank of Nigeria
C. Deposit Money Banks
D. Bilateral Creditors

E. Insurance Companies

14. The use of government expenditure and taxation to influence economic activities is classified as

    A. Physical policy
    B. Commercial policy
    C. Monetary policy
    D. Prices and incomes policy
    E. Fiscal policy

15. The principle of revenue allocation which suggests that each level of government has a minimum responsibility to shoulder is that of

    A. Even development
    B. Equality of States
    C. Continuity of Government
    D. Fiscal efficiency
    E. Derivation

16. A medium-term development plan in which new plans are made and acted upon yearly in keeping with the requirements of the economy is known as

    A. Rolling plan
    B. Perspective plan
    C. Supplementary budget
    D. Deficit budget
    E. Balanced plan

17. Reasons to justify the desirability of government intervention in a private sector economy include all the following EXCEPT

    A. Provide public goods
    B. Redress negative externalities
    C. Redistribute income and wealth

D. Enforce the legal structure required by the market system
E. Provide competitive edge over the private sector

18. The tax on the supply of goods and services which is borne by the final consumer but collected at each stage of the production and distribution chain is

A. Personal Income Tax
B. Company Income Tax
C. Capital Gains Tax
D. Value Added Tax
E. Excise Tax

19. A project appraisal method in which comparisons are made between the costs of achieving desired outcomes is called

A. Cost Benefit Analysis
B. Cost Outcome Analysis
C. Present Value Analysis
D. Cost Effectiveness Analysis
E. Internal Rate of Return

20. Government expenditure in the forms of unemployment benefits, pension payments and aid to other countries are grouped under

A. Capital expenditures
B. Transfers
C. Economic services
D. Social and community services
E. General Administration

PART II: SHORT ANSWER QUESTIONS (20 MARKS)

Write the answer that best completes each of the following questions/statements:

1. Pension Fund Administrators and custodians are to provide customer service support to employees including access to employee………………………… on demand.

2. The Federal Inland Revenue Service Act 2007 S. (17) shall prepare not later than the 30 September in each year an ……………………… in the succeeding year for the purpose of appropriation by the National Assembly

3. The Financial Warrant used to re-vote capital expenditure which had lapsed over the years is known as……………………………. Warrant

4. An independent appraisal activity within an organization for the review of operations as a service to Management and managerial control which functions by measuring and evaluating the effectiveness of other controls is known as…………………………………

5. The document that sets out series of questions to determine the adequacy, effectiveness and efficiency of internal control system is known as ………………..

6. The entity of Government is established by the Constitution, the Finance (Control and Management) Act, 1958 and Audit Ordinance Act, 1956 whereas that of commercial enterprise is established under the……………………Act.

7. According to Section 3 and 4 of Finance (Control and Management) Act Cap 144 Laws of the Federation, 1990, the…………………shall have full authority to direct on all matters relating to finance and accounting affairs of the Federation which are not by law assigned to any other officer.

8. In accordance with Section 70 of the Constitution of the Federal Republic of Nigeria, 1999, the salary and other allowances of members of the National Assembly shall be as determined by the…………………Commission.

9. According to International Public Sector Accounting Standards No 11, a construction contract in which the contractor is reimbursed for allowables is called a……………………contract.

10. The process by which government will meet its financial obligations to contractors, suppliers, government employees and pensioners without issuing cheques is called...................................

11. The institution that is entrusted with the issue and management of Federal Government loans publicly issued in Nigeria is called ....

12. Revenue generated by the Federal Government from the use of land for exploration of the mineral resources under oil mining lease is called ....

13. Discretionary financial assistance given by the Federal Government to the State and Local Government to supplement statutory allocation is classified as ....

14. The rate at which society is willing to trade off present consumption for future consumption is known as ....

15. A practice whereby a government makes interest and principal payments on debts which fall due is referred to as ....

16. A debt management strategy which involves changing of the maturity structure of a loan is called ....

17. Bringing under government ownership and control, resources and activities formerly operated by private businesses is referred to as ....

18. The process whereby the economic agent that bears the initial impact of tax is able to pass the whole or part of the tax to another economic agent is called ....

19. Domestic debt instruments which are issued by the State and Local Government Councils and are backed up by the pledge of revenue to be generated from the project being financed are called ....

20. In the main heads of government expenditure, expenditures on defence, police, and the cost of running the entire civil service are grouped under ....

SECTION B: ATTEMPT QUESTION ONE AND ANY OTHER THREE QUESTIONS (60 MARKS)

QUESTION 1

CASE STUDY

THE QUEST FOR DEVELOPMENT AGENDA

Klepto is a developing nation endowed with abundant natural and human resources. For instance, besides a large expanse of arable land and large deposits of both solid and non-solid minerals, the country has a population of about 180 million.
With a population growth rate average of about 3% over the past fifteen years, the country presents a good example of a labour-surplus economy. However, Klepto contends with a number of developmental challenges that are sources of serious concern to its government and people.

In Klepto, it is a common occurrence to see able-bodied young men and women appearing in their thousands at every job interview opportunity. The jobs are not really there and there is no hope that one will be available tomorrow. The existing labour-intensive industries are even closing shop for reasons of poor supply of electricity, water, transportation services and insecurity of lives and properties. Despite this, the nation's tertiary institutions continue to turn out hundreds of thousands of graduates every year.

The Kleptonian economy is also in deep recession, with majority of the people lacking necessary purchasing power to access the basic necessities of life let alone luxuries. There is the argument as to the more appropriate budget type to adopt between surplus and deficit budgets to solve these problems. There exists simultaneously a pocket of Kleptonians whose lifestyle is conspicuously at variance with that of the masses of the people. These few Kleptonians are said to be mostly products of corruption which is pervasive in the land.

Worse still, Klepto is highly indebted to the Paris Club. Debt service burden constitutes an obstacle to developmental efforts because the scarce foreign exchange resources are not available for the finance of planned developmental projects.
There is ample evidence, however, that the newly installed government is highly desirous of a change for the better.

Required:

(a) Identify and explain FOUR main developmental problems facing Klepto. (12 Marks)

(b) Explain briefly the type of budget the new government should adopt out of the options given, to stimulate the Kleptonian economy. (3 Marks)

(Total 15 Marks)

QUESTION 2

"Public debt as of a given point in time is the sum of past deficits and surpluses".
You are required to:

(a) Elaborate on the statement: (6 Marks)
(b) Explain any THREE disadvantages of public debt. (6 Marks)
(c) Comment on "the inevitability of public debt". (3 Marks)
(Total 15 Marks)

QUESTION 3

The need for development planning cannot be overemphasized, especially in developing countries. And for economic transformation, a paradigm shift in favour of a Rolling Plan appears inevitable, but such methodology of planning in design and implementation is only meaningful in the context of a Perspective Plan.

You are required to:

(a) Explain the linkage between the Rolling Plan and the Perspective Plan. (6 Marks)
(b) Provide any THREE reasons why development planning has been considered inevitable, especially in developing countries. (6 Marks)

(c) How far have development plans fared in transforming your country? (3 Marks)
(Total 15 Marks)

QUESTION 4

In Nigeria, a preponderant part of government revenue comes from oil while only a paltry sum comes from the non-oil sector.

You are required to:

(a) Provide TWO reasons why governments need revenue. (2 Marks)
(b) Explain any TWO components each of oil and non-oil sources of government revenue receipts in Nigeria. (4 Marks)
(c) Discuss the relative importance of oil and non-oil revenue in the Nigerian economy. (9 Marks)
(Total 15 Marks)

QUESTION 5

Ministry of Transport of Tolotolo State is instructed to get buses for the State as one of the palliative measures to cushion the effect of removal of subsidy on petrol. The ministry is of the opinion of leasing the buses instead of direct purchase.
In accordance with the International Public Sector Accounting Standard (IPSAS) 13 on Leases, you are required to:

(a) Explain any FIVE criteria which would lead to a lease being classified as finance lease. (10 Marks)

(b) State any FIVE disclosures required of the Lessor for finance lease. (5 Marks)
(Total 15marks)

QUESTION 6

"Stores include all moveable property purchased from public funds or otherwise acquired by government. They may be in the form of Consumable, Expenditure, Non-Expendable, Allocated and Unallocated stores".

You are required to:

(a) Distinguish between "allocated" and "unallocated" stores. (4 Marks)
(b) State any FOUR qualities each, of "allocated" and "unallocated" stores. (4 Marks)
(c) State any SEVEN responsibilities of the Storekeeper as specified under Section 2231 of the Financial Regulations (2009). (7 Marks)
(Total 15 Marks)

SOLUTIONS TO SECTION A

PART I - MULTIPLE CHOICE QUESTIONS

1. B
2. D
3. E
4. D
5. D
6. D
7. A
8. C
9. C
10. B
11. B
12. A
13. D
14. E
15. D
16. A
17. E
18. D
19. D
20. B

<u>Tutorial to Question 10</u>

Maintenance cost for 3buildings in 2010 = ₦0.84b
Maintenance cost per building = 0.84 ÷ 3
= ₦0.28b
Incorporation of inflation = 1. (0.28)
For 5 buildings in 2011 = 1.3 (0.28) x 5
= ₦1.82b

EXAMINERS' REPORT

The questions cover most of the topics in the syllabus and the performance was average.

Some of the candidates could not identify:

(i) The statement that is dealt with by International Public Sector Accounting Standard No.2
(ii) The functions of Local Government Council Chairman
(iii) The difference between the objective and functions of Revenue Mobilisation Allocation and Fiscal Commission

Candidates are advised to read widely in order to cover the syllabus and improve performance.

PART II SHORT-ANSWER QUESTIONS

1. Account Balance and Statement
2. Estimate of income and expenditure
3. Development fund supplementary expenditure
4. Internal Audit
5. Internal Control Questionnaire
6. Company and Allied Matters
7. Minister of finance
8. Revenue Mobilisation Allocation and fiscal
9. Cost plus or cost based
10. E-payment/money transfer/fund transfer
11. Debt Management Office (DMO)
12. Royalties
13. Grants
14. Social Rate of Discount
15. Debt servicing
16. Debt Rescheduling
17. Nationalisation
18. Tax shifting
19. Revenue Bond
20. General Administration

EXAMINERS' REPORT

The questions cover most of the topics in the syllabus and the performance was below average.
The commonest pitfalls identified include:

(i) Inability to identify the financial warrant issued to re-vote capital expenditure.
(ii) Inability to identify the authority cover on the Minister of Finance by Finance

(Control and Management) Act Cap 144 Laws of the Federation, 1990.

(iii) Inability to understand the contents of International Public Sector Accounting Standard No.11

Candidates should study contemporary issues both in Public Sector Accounts and Public Finance.

SOLUTIONS TO SECTION B

QUESTION 1

(a) Development problems identified are:

- (i) Unemployment: Many able-bodied men and women of working age bracket are not engaged in productive activities.
- (ii) Poverty: The masses of the people are not able to access the basic necessities of life.
- (iii) Inequality: Existence of a few rich people who are swimming in affluence.
- (iv) Unsustainable external debt owed to the Paris Club: Using the limited foreign exchange earnings to service external debt.
- (v) Deep economic recession: People lack necessary purchasing power to access basic necessities of life.
- (vi) Insecurity of lives and properties.
- (vii) Pervasive corruption.
- (viii) Poor infrastructure such as electricity, water, transportation etc.

(b) The country should adopt a deficit budget, that is, spend more than the revenue generated to finance capital projects. This will help to create employment opportunities in the process of executing capital projects e.g fixing electricity, constructing roads, schools and hospitals.

EXAMINERS' REPORT

This is a case-study question where candidates are expected to reflect on some issues of concern in the context of the case provided. Candidates are to identify and explain the main problems of Klepto and proceed to indicate the appropriate budgetary policy to stimulate the economy.

As a compulsory question, all the candidates attempted it. The overall performance in the question was impressive. Majority of the candidates identified well the main developmental problems in the case study and provided relevant and copious explanation of the budgetary measure to stimulate the so-called Kleptorian economy.

In few cases, candidates were too general in their presentation of the developmental problems with little or no reference to the case study. Candidates are therefore advised to pay particular attention to the content of the case study in answering a question of this type.

QUESTION 2

(a) A public debt is the total outstanding borrowings of the government during a given period. Alternatively, public debt is defined as the accumulated total of past deficits less past surpluses.

A budget surplus is the excess of government's total income over its expenditure, while budget deficit is the excess of government's total expenditure over its income. At any point in time, budget deficit has to be met by borrowing, which gives rise to or increases government debt.

(b) The disadvantages of public debt include the following:

i) Debt servicing may require increased taxation which may bring hardship to people and when government defaults in the payment of external debt, it many undermine economic development.

ii) Financing public debt by selling bonds to the public may cause loss of income and employment, especially when it crowed out private investment.

iii) Public debt may tend to be inflationary, especially as the holders of debt instruments may go into a spending spree.

iv) Public debt servicing distorts income distribution. A few rich people who buy debt instruments become richer by debt repayment while the poor groan under higher tax burden to repay loans.

v) Vulnerability to external shocks

vi) Intergenerational tax burden transfer

(c) Public debt is inevitable because of:
   (i) Differences in timing between expenditure and receipt of income by the government.
   (ii) Limited resources relative to the immediate developmental aspirations of the government .
   (iii) Deficit budget financing to reflate the economy.

EXAMINERS' REPORT

The focus in the question is on "public debt", what it means, its rationale and the disadvantages.

Virtually all the candidates attempted the question, with just a few of them showing good understanding of the requirements of the question, especially (a) aspect. Many of them lost marks in this aspect of the question as they failed to elaborate on how public debt constitutes the sum of past deficits and surpluses.

However, the candidates' responses to (b) and (c) were much better. In all, the performance in the question was a little below average.

Candidates are advised to be painstaking and specific in answering questions and also be reflective on the requirements of a question.

QUESTION 3

a) Rolling Plan: The rolling plan is a medium-term (3-year) development plan in which new plans are made and acted upon yearly in keeping with the requirements of the economy. Under a rolling plan, it is relatively less difficult to make projections over a 3-year period than a longer term period.

   Perspective Plan. This is a long-term development plan i.e a projection for 15, 20 or more years. It provides direction of planned changes of the socio-economic structure of the economy over a long term period, thereby determining the path of future improvement in all key sectors of the economy. It also identifies policy measures necessary to achieve set targets.

Since the same perspective plan is presented every year it follows that the rolling plan usually serves as an input into the perspective plan. This is actually the linkage between the two plans.

b) Arguments often advanced in favour of the desirability of development planning in developing counties include the following:

(i) Economic development. The argument is that the rather slow development process pace in developing countries can only be hastened through a conscious setting of objectives and targets.

(ii) Resource mobilization and allocation argument. The market system aggravates inequalities of income and wealth because goods and services are produced in response to demand. Development planning is desirable to redistribute resources, especially to ensure resources are not concentrated on unproductive activities at the expense of productive activities.

(iii) Foreign aid argument. Planning creates an impression of seriousness on the part of the potential recipient of assistance and gives the donors confidence that such an assistance will be judiciously utilized on productive projects. Thus development plan is a potent means of attracting bilateral and multilateral aid.

(iv) Attitudinal argument. It is argued that the formulation of development plan will create awareness on the part of the public and a positive attitude in support of government efforts to mobilize resources for economic development.

(v) The Market Failure argument. The free market system, if left alone, cannot ensure efficient functioning of the society. Therefore, government must intervene in the form of development planning to improve the living conditions of the generality of the people.

(c) Some developmental strides have been taken in building physical structures and social infrastructures (Kainji Hydro electric power, airports, seaports, educational institutions etc). However, because of the country's poor maintenance culture, bad leadership, planning indiscipline, corruption etc, the impact of development plans has been limited.

EXAMINERS' REPORT

The question tests candidates' understanding and familiarity with the nature, bases and performance of development planning in developing countries.

Majority of the candidates attempted the question and the performance was average. Most of them explained Rolling Plan and Perspective Plan without specifying the time horizon while virtually all of them could not provide reasons for development planning.

Candidates are advised to consult relevant text books on development planning in order to have familiarity with this aspect of the syllabus.

QUESTION 4

(a) Reasons why governments need revenue

(i) To meet the cost of administration e.g. salaries of government officials.
(ii) To meet the cost of developmental projects e.g. building of educational institutions.
(iii) To provide social infrastructures like roads.
(iv) To service public debts both internal and external

(b) Sources of Oil revenue

(i) Petroleum Profit Tax: This is the tax paid for the mining or obtaining and transportation of petroleum oil in Nigeria, by or on behalf of a company for drilling, mining, extracting or other similar operations.

(ii) Royalty: This is the revenue generated from the use of land for exploration and exploitation of the mineral resources under oil prospecting licence or oil drilling lease.
(iii) Crude oil: Sale of crude oil by the government.

(iv) Liquified natural gas: Sale of liquified natural gas

(v) Penalties: Penalty for flaring gas

(c) Sources of non-oil revenue

(i) Taxation: This is the most important source of non-oil revenue in Nigeria. It is a compulsory levy on all taxable persons and corporate bodies. It includes both direct tax such as personal income tax, corporate profit tax, capital gains tax; and indirect tax like value-added tax customs duties etc.
(ii) Loans: Government may also source for loans from external sources like international financial institutions and internal sources like banks and the public using debt instruments like treasury bills, treasury certificate, development loan stocks.
(iii) Grants and aids: Government may get financial assistance from international institutions and friendly countries.
(iv) Government investment: Returns on investment made by the government also serve as a source of revenue to the government.
(v) Licences: These include revenue from vehicle, bicycle, gun and drivers' licences.
(vi) Rent of government properties: These include rent of government quarters, land and buildings, fees for temporary occupation etc.
(vii) Interest and repayment: These include interest on, and repayment of loans granted individuals and State Governments by the Federal Government.

Prior to the early 70s, the non-oil sources contributed the lion share of the total Federal Government revenue of Nigeria. However, since the oil boom of the early 70s, the oil sources have been contributing above 70% of the total government revenue and relegating the non-oil sources to the background. The reasons for greater contribution of oil sources include the following:

(i) Oil sector is a ready source of foreign exchange earnings.
(ii) There are structural rigidities and constraints in the non-oil sector
(iii) Government policies to promote the non-oil sector are not effective

EXAMINERS' REPORT

It tests candidates understanding of the bases, components and relative importance of oil and non-oil revenue in the Nigerian economy.

Virtually all the candidates attempted the question and the performance was average. Most candidates showed good understanding of the reasons for, and components of oil and non-oil revenue. They, however, had problem discussing the relative importance of oil and non-oil revenue in the Nigerian economy.

Instead of explaining and accounting for the relative contribution to government revenue, majority of them discussed the usefulness of the revenue sources to the government.

Candidates are advised to spend more time on gaining understanding of the requirements of questions generally in order to maximize performance.

QUESTION 5

(a) The following are situations which would lead a lease to be classified as a finance lease:

(i) The lease transfers ownership of the asset to the lessee by the end of the lease term.
(ii) The lease term is for the major part of the economic life of the asset even if title is not transferred.
(iii) The lessee has the option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable, so that at the inception of the lease it is reasonably certain that the option will be exercised.
(iv) At the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased assets.
(v) The leased asset cannot easily be replaced by another asset.
(vi) If the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee.
(vii) The leased assets are of a specialized nature such that only the lessee can use them without major modifications being made.
(viii) The lessee has the ability to continue the lease for a secondary period at a rent which is substantially lower than market rent; and
(ix) Gains or losses from the fluctuation in the fair value of the residual fall to the lessee.

(b) Lessors should make the following disclosures in their financial statements

(i) Unearned finance revenue

(ii) The unguaranteed residual values according to the benefit of the lessor.

(iii) A reconciliation between the total gross investment in the lease at the reporting date and the present value of minimum lease payments receivable at the reporting date.

(iv) The total gross investment in the lease and the present value of minimum lease payments receivable at the reporting date.

(v) The accumulated allowance for uncollectable minimum lease payments receivable.

(vi) Contingent rents recognized in the statement on financial performance; and

(vii) A general description of the lessor's significant leasing arrangements.

EXAMINERS' REPORT

The question tests the candidates' understanding of provisions of International Public Sector Accounting Standard (IPSAS) 13 on Leases.

The question was one of the least attempted by the candidates and the performance was below average.

Most candidates who attempted the question were not able to distinguish between Operating Lease and Finance Lease. Candidates are advised to consult relevant text books and digest the requirements of all the International Public Sector Accounting Standards (IPSAS) for improved performance in future examinations.

QUESTION 6

(a) Allocated stores are items, the cost of which are chargeable direct to and remain a charge to the sub-head of expenditure in which funds for their purchase are provided in the estimate.

Unallocated stores are those purchased for general stock rather for a particular work or service, for which the final vote of charge cannot be started at the time of purchase.

(b) Qualities of allocated and unallocated stores.

	Allocated	Unallocated
i.	Purchased directly or obtained from the unallocated stores.	Purchased for general stock.
ii.	They are taken on numerical charge.	They are held on charge by both value and unit.
iii.	It is put into immediate use.	When issued for use, they are charged to the appropriate sub-head of expenditure.
iv.	The cost is chargeable to and remains a charge to the sub-head of expenditure.	The cost of unallocated store is debited to an unallocated stores sub-head expenditure.
v.	The accounting officer does not determine the stock level.	It is the responsibility of accounting officer to determine the stock level e.g re-orders level.

(c) Responsibilities of the Store keeper as specified under Section 2231 of Financial Regulations (2009) are

(i) Maintenance of proper books of accounting records to timely reflect the transactions.
(ii) Proper cleanliness of the store.
(iii) Diligent arrangement of the store.
(iv) Issue of items out of the store, based on a properly authenticated store requisition.
(v) Invitation of purchase requisition from the needy department.
(vi) Updating the bin or tally cards and ledger balances and reporting any discrepancies revealed.
(vii) Preparation of store receipt and issue vouchers.
(viii) Collection of store items from the suppliers to ensure that the items delivered agree with the specification and the agreed price stated on the Local Purchase Order (L.P.O)
(ix) Ensuring that there is adequate security over the custody of the store.

EXAMINERS' REPORT

The question tests candidates' ability to distinguish and state the qualities between allocated and unallocated stores.

Majority of the candidates attempted the question and the pass rate was average. Most of the candidates who attempted the question could not differentiate between the definitions and qualities of allocated and unallocated stores. In most cases, points were duplicated.

Candidates are advised to prepare adequately for this paper and understand all the provisions of Financial Regulations (2009) for future examination.