INSTRUCTIONS TO CANDIDATES:
1. Your attention is drawn to the necessity to provide suitable substantiating reasons and/or workings in support of your answers.

2. Where workings are presented separately from your answer, these must be clearly referenced thereto.

3. Each of the TWO questions must be answered in a separate answer booklet. Therefore, a minimum of TWO answer booklets must be handed in. Answers written in the incorrect booklet may not be marked. Ensure that answer booklets are labeled with the correct question number.

4. Fill in all necessary information on the front cover of each answer booklet.

5. Answers must be written in ink only. Pencil workings will not be marked.

6. All questions must be answered.

7. The use of a non-programmable calculator is permitted.

8. No abbreviations are to be used. Abbreviations will not be marked.

9. A recommended time allocation has been provided for each question. Manage your time effectively.

10. Please note that this question paper does not contain the ‘required’ section. You have 10 minutes to familiarize yourself with the information contained in this question paper and thereafter you will be provided with a separate sheet with the ‘required’ section. You may only start writing after you have received the ‘required’ section.
Vortex Sports Limited (Vortex) is a company that focuses their core strength on the athletic footwear and apparel market.

**EXECUTIVE OFFICES:**

Vortex purchased an office building at a cost R10 000 000 on 1 January 2013. The cost of the land was considered negligible. This was the latest in a series of expansions of the company’s operations. The company’s sports scientists commenced operations from this building.

The building is depreciated over 25 years on a straight line basis to Rnil residual value.

At 29 December 2013, the recoverable amount of the building was considered to be R9 000 000.

On 31 December 2014, the company moved its team to alternative and more suitable premises, at which date the company began searching for a tenant to rent the now vacant building. A suitable tenant immediately moved into the building on 31 December 2014.

Valuations by an independent valuer and member of the SA Institute of Valuers were performed on the following dates:

<table>
<thead>
<tr>
<th>Date</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>31 December 2013</td>
<td>8 600 000</td>
</tr>
<tr>
<td>31 December 2014</td>
<td>9 500 000</td>
</tr>
<tr>
<td>31 December 2015</td>
<td>10 200 000</td>
</tr>
</tbody>
</table>

Vortex uses:

- the cost model to measure property, plant and equipment and
- the fair value model to measure its investment properties.

**FINANCE LEASE:**

On 1 April 2014, Vortex entered into a finance lease agreement for an item of plant with Banking Limited (Both the lessor and the lessee are vendors for VAT purposes). The lease allowed Vortex the opportunity to acquire a plant which was important to the operations of the business with the benefit of upgrading equipment in three years (as technology changes rapidly).
Details relating to the lease are:

<table>
<thead>
<tr>
<th>Cash cost of asset /fair value of plant</th>
<th>R1 539 000 (incl. VAT). This equals to the present value of the future minimum lease payments.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commencement of the lease</td>
<td>1 April 2014</td>
</tr>
<tr>
<td>Lease term</td>
<td>3 years</td>
</tr>
</tbody>
</table>

- The lease agreement requires that instalments (calculated using an effective interest rate of 10% per annum), be payable annually in arrears as follows:
  31 March 2015: R600 000
  31 March 2016: R600 000
  31 March 2017: R662 409
  Interest is compounded on 31 March each year.

- Plant is depreciated over its estimated useful life of 3 years to a nil residual value using the straight-line method.

- The plant was available for use immediately.

**TAX INFORMATION:**

1. Profit before tax was correctly determined to be R2 900 000;

2. Vortex raises deferred tax assets;

3. Vortex measures deferred tax relating to Investment Property in accordance with the rebuttable presumption in terms of IAS 12 *Income Taxes*;

4. The tax authorities grant an allowance of 10% per annum on the building on the straight line basis, not apportioned for part of a year; and

5. The corporate income tax rate is 20.15: 29% (20.14: 28%) Taxable capital gains are calculated using an inclusion rate of 50% of the capital gain. The base cost of the building equals its cost.
Cadberry Limited (Cadberry) is an entity operating in the KwaZulu-Natal region and operates a chocolate dipped strawberry business. Juicy strawberries are handpicked at the peak of ripeness, and coated with a generous layer of chocolate and then packaged in gift boxes.

However, the company has suffered a double blow, with two droughts in 20.10/20.11 and 20.15/20.16 respectively. The drought which has been described to be the worst to hit South Africa, has adversely affected Cadberry and it is estimated that Cadberry will make a loss of R3 million in 20.15 and will be profitable from relief efforts expected from the government thereafter. Due to the previous drought, Cadberry has an assessed loss of R8 million at 31 December 20.14, all of which is available for set-off against future taxable income.

INVESTMENT IN THE CUMULATIVE PREFERENCE SHARES OF CHOCO LIMITED

Cadberry viewed the current environment as an opportunity to consider new opportunities. Since the company seeks income optimisation, tax efficiency and low risk to capital, the preference share market was considered to be an attractive option. On 1 January 20.14, Cadberry purchased 250 000 cumulative 10% R1 preference shares in CHOCO Limited, a local listed company, for R1.40 each. The preference shares are compulsorily redeemable at R1.25 each on 31 December 20.18. Preference dividends on these shares are payable annually on 31 December each year.

The preference share investment is held within a business model whose objective is to hold the assets in order to collect contractual cash flows. Cadberry is also satisfied that the contractual terms of the preference shares give rise to cash flows on specific dates that are solely payments of principal and interest on the principal outstanding. Cadberry classified the investment accordingly (having not elected to designate the shares as a ‘fair value through profit and loss’ financial asset).

The fair values of the listed preference shares of CHOCO Limited at the relevant dates were:

- 31 December 20.14 - R1.52 per share
- 31 December 20.15 - R1.68 per share

Where required, assume an effective interest rate of 5.2% on the preference shares.
INVESTMENT IN BUILDING:

Cadberry owns one building that was purchased for R4 800 000 (in cash) on 1 January 20.14. This building was available for use from this date.

- Depreciation on this building in 20.14 was calculated on the straight-line basis at 10% per annum to a nil residual value. During 20.15, the remaining useful life of the building was re-assessed to be 12 years, calculated from 1 January 20.15. The straight-line method and the residual value of nil were still considered to be appropriate.

- The building was revalued to its fair value of R7 200 000 on 31 December 20.14. Cadberry computes depreciation prior to carrying out the revaluation.

- The company applies the gross replacement value method when revaluing its assets (i.e. any accumulated depreciation at the date of the revaluation is restated proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount \[\text{IAS 16.35}\]).

- The company transfers the revaluation surplus to retained earnings over the life of the asset.

- Management's intention has always been to sell this building. (the criteria for classifying this asset as a non-current asset held for sale were not met and therefore the building is still considered to be property, plant and equipment).

- The tax authorities do not allow tax deductions relating to the cost of the building.

- The corporate income tax rate is 29% (20.14: 28%) Taxable capital gains are calculated using an inclusion rate of 50% of the capital gain. The base cost of the building is R5 400 000.

- There are no temporary differences other than those evident from the information provided.
**REQUIRED : PART A**

1. Explain how the building should be *recognised* and *measured* in the financial statements of Vortex for the years ended 31 December 2013, 2014 and 2015 in order to be compliant with International Financial Reporting Standards.

   *The definition of property, plant and equipment and the definition of an asset are *not* required.*

   *You must include all calculations to support your answer.*

   *A discussion of the tax effect of the land and buildings is *not* required.*

2. Prepare all journal entries relating to the plant for the year ended 31 December 2014. *Journals relating to tax are *not* required.*

   *Dates and narrations are required.*

3. Using the balance-sheet approach, calculate the deferred tax balance caused by the *finance lease* over plant as at 31 December 2015. Assume that the closing deferred tax balance recognised at 31 December 2014 caused by this *finance lease* was R126 819 (asset).

4. Using the balance-sheet approach, calculate the deferred tax balance caused by the *building* as at 31 December 2015. Assume that the closing deferred tax balance recognised at 31 December 2014 caused by this building was R420 000 (liability).

5. Prepare, in accordance with International Financial Reporting Standards, the tax expense note for inclusion in the annual financial statements for the year ended 31 December 2015. There is insufficient evidence to recognise deferred tax assets at reporting date. Comparatives are *not* required.

**REQUIRED : PART B**

1. Briefly discuss how the investment in the cumulative preference shares of CHOCO Limited will be *accounted for* (including classification and *measurement* but excluding disclosures) by Cadberry in its financial statements (*quantification* is not required). *Ignore tax consequences.*

2. Determine the carrying amount of the Investment in Preference Shares at 31 December 2015. *Ignore tax consequences.*

3. Provide the journal entries relating to the building (including all related deferred tax entries) for the years ended 31 December 2014 and 31 December 2015.

   *You *MUST* show narrations and *ALL* workings. *IGNORE VAT.*

4. Discuss, with reason, how the assessed loss should be accounted for in the financial statements of Cadberry at 31 December 2015. You must show calculations.

   *The credit balance on the Deferred Tax account account from temporary differences was correctly calculated to be R990 000 at 31 December 2015.*