FINANCIAL ACCOUNTING 700 **Seminar RS 4 – Suggested solution** ***PH Ferreira***	**DEPARTMENT OF ACCOUNTING** **UP**

SUGGESTED SOLUTION TO QUESTION A

1. Accounting policy
2. Estimate
3. Estimate
4. Accounting policy
5. Estimate
6. Estimate

SUGGESTED SOLUTION TO QUESTION B

AREND LIMITED
STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 30 JUNE 20X6

	Notes	20X6 R	20X5 R
Revenue (20X5: 344 - 15)		370 000	329 000
Cost of sales (170 + 7,8 - 3) (163 + 3,4 - 7,8)		(174 800)	(158 600)
Gross profit		195 200	170 400
Other income		30 000	-
Administrative expenses		(100 000)	(90 000)
Other expenses (48 000 + 20 000)		(68 000)	(41 000)
Profit before tax	1	57 200	39 400
Income tax expense	2	(10 880)	(15 760)
Profit/total comprehensive income for the year		46 320	23 640

EXTRACT FROM STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 30 JUNE 20X6

	Notes	Retained earnings R
Balance on 1 July 20X4		30 000
Change in accounting policy	4	2 040
Restated balance		32 040
Total comprehensive income/profit for the year (restated)	3	23 640
Dividends paid		(1 000)
Balance on 1 July 20X5		54 680
Total comprehensive income/profit for the year		46 320
Dividends paid		(5 000)
Balance end of year		96 000

NOTES FOR THE YEAR ENDED 30 JUNE 20X6

1. Profit before tax

Profit before tax includes the following:

	20X6 R	20X5 R
Gain on sale of investment	30 000	-
Loss on machinery that was damaged by cloud burst	(20 000)	-

2. Income tax expense

	20X6 R	20X5 R
Major components of tax expense:		
SA Normal		
• Current [C1]	14 000	14 000
• Deferred [C2]	(3 120)	1 760
	10 880	15 760
Tax rate reconciliation		
Accounting profit	57 200	39 400
Tax at 40%	22 880	15 760
Tax effect of non-taxable profit (30 000 x 40%)	(12 000)	-
Tax expense	10 880	15 760

3. Prior period error

The error relates to an underpayment of VAT in 20X5 which was detected in the current year and corrected. The error has been corrected retrospectively and comparative amounts have been restated accordingly. The effect of this error in the results of 20X5 is as follows:

	20X5 R
Decrease in revenue	(15 000)
Decrease in income tax expense	6 000
Decrease in profit for the year	(9 000)
Increase in VAT payable	(15 000)
Decrease in tax payable	6 000
Decrease in equity	(9 000)
Decrease in basic earnings per share	X
Decrease in diluted earnings per share	X

4. Change in Accounting Policy

During the year the company changed its accounting policy relating to inventory valuation. In future the company will value inventory using the average cost method instead of the first-in-first-out formula. (Provide a reason why fairer presentation would be achieved). The change in policy has been accounted for retrospectively and comparative amounts have been restated accordingly. The effect of the change is as follows:

	20X6 R	20X5 R	1/7/20X4 R
Decrease/(increase) in cost of sales	(4 800)	4 400	
(Increase)/decrease in income tax expense	1 920	(1 760)	
(Decrease)/increase in profit for the year	(2 880)	2 640	
Increase in inventory	3 000	7 800	3 400
Increase in current tax payable	(1 200)		
Increase in deferred tax liability		(3 120)	(1 360)
Increase in equity	1 800	4 680	2 040
Adjustment to retained earnings at beginning of 20X5			2 040
Increase/decrease in basic earnings per share	x	x	
Increase/decrease in diluted earnings per share	x	x	

CALCULATIONS

1. Current tax

		20X6 R	20X5 R
Profit before tax		57 200	39 400
Non-taxable profit		(30 000)	-
		27 200	39 400
Temporary differences:		7 800	(4 400)
Opening inventory	- accounting	34 800	22 900
	- tax	(27 000)	(19 500)
Closing inventory	- accounting	(51 000)	(34 800)
	- tax	51 000	27 000
Taxable income		35 000	35 000
Current tax @ 30%		14 000	14 000

2. Deferred tax

	Carrying amount R	Tax base R	Temporary difference R	Deferred tax R
20X4:				
Inventory	22 900	19 500	3 400	1 360
20X5:				
Inventory	34 800	27 000	7 800	3 120
20X6:				
Inventory	51 000	51 000	-	-

Movement in statement of profit or loss and other comprehensive income:

20X5: (3 120 – 1 360)	1 760 dr
20X6: (3 120 – 0)	3 120 cr

SUGGESTED SOLUTION TO QUESTION 1

(a) IAS 17 requires HP-sales to be accounted for by recognising the profit immediately.

The finance income should be recognised over the period of the agreement by using the effective interest method. The policy followed by A Ltd to recognise profit only once cash in received, is clearly not in line with IAS 17, a standard which has been effective now for a number of years.

The change over from the incorrect policy to the policy required by IAS 17 should be accounted for as a prior period error.

Note that the definition of a prior period error in IAS 8.5 includes mistakes in applying accounting policies.

[A change in accounting policy is applicable only if a standard allows a choice between two or more policies, or if a new standard is issued.]

(b)

	FP 20X1 R	CI 20X2 R	FP 20X2 R	CI 20X3 R	FP 20X3 R
Basis used before	120 000		160 000		195 000
New basis	40 000		50 000		65 000
	80 000	30 000	110 000	20 000	130 000
Taxation					
- @ 40%	(32 000)	(12 000)	(44 000)		
- Tax rate change*				(5 500)	
- @ 45%				(9 000)	(58 500)
Net decrease in provision; but increase in profit	48 000	18 000	66 000	5 500	71 500
	A	B		C	

* 110 000 x 5% = 5 500

A Cumulative effect of change in accounting policy up to 20X1.

B Effect on profit in 20X2.

C Effect on profit in 20X3.

SUGGESTED SOLUTION TO QUESTION 2

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STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 30 JUNE 20X6

	Notes	20X6 R	20X5 R	Calculations
Revenue		1 420 000	1 350 000	
Cost of sales		(652 500)	(683 500)	C4A
Gross profit		767 500	666 500	
Distribution costs		(43 000)	(37 500)	
Administrative costs		(121 000)	(124 500)	
Other expenses		(250 150)	(351 500)	C4
Finance costs		(209 852)	(18 401)	C7
Profit before tax	2	143 498	134 599	
Income tax expense	3	(74 249)	(67 300)	C5
Profit/Total comprehensive income for the year		69 249	67 299	

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 30 JUNE 20X6

	Notes	Retained earnings R
Balance at 1 July 20X4		100 000
Correction of prior period errors	4	(4 182)
Restated balance		95 818
Total comprehensive income/profit for the year (restated)		67 299
Balance at 1 July 20X5		163 117
Total comprehensive income/profit for the year		69 249
Dividends paid		
- Ordinary shares		(15 000)
Balance at end of year		217 366

NOTES

2. **Profit before tax**

The amount was calculated after taking into account the following items:

	R
Income	
Unrealised exchange difference on foreign exchange loan (C2)	140 000
Expenditure	
Operating lease - land and buildings	30 000
Depreciation (1 530 + 13 500)	15 030
Employee benefit expense	333 000

3. **Income tax expense**

Major components of tax expense

SA Normal taxation	
- Current taxation (C5)	67 750
- Deferred taxation (C5)	6 499
Income tax expense	74 249

Tax rate reconciliation

Accounting profit	143 498
Tax at applicable rate of 50%	71 749
Tax effect of non-deductible fine (5 000 x 50%)	2 500
Tax expense	74 249

4. **Prior period errors**

Vat underpayment

The correction of an error in respect of an underpayment in VAT in respect of 20X4. The error has been corrected retrospectively and the comparative amounts have been restated accordingly. The effect of this error on the results is as follows:

	30/6/20X5	1/7/20X4
	R	R
Increase in VAT - payable	(15 000)	(15 000)
Decrease in current tax payable (assessment reopened)	7 500	7 500
Decrease in equity	(7 500)	(7 500)
Adjustment to 20X5 retained earnings opening balance		(7 500)

Capitalisation of finance leases

During the year the company changed its method of accounting for finance leases by capitalising all such agreements. In the past these agreements were accounted for incorrectly by expensing the lease instalments. The error has been corrected retrospectively and the comparative amounts have been appropriately restated. The effect of the correction of the error is as follows:

	30/6/20X5	1/7/20X4
	R	R
Decrease in other expenses	40 000	
Increase in cost of sales	(13 500)	
Increase in finance costs	(16 901)	
Increase in tax expense	(4 800)	
Increase in profit for the year	4 799	
Increase in machinery	108 000[a]	121 500[b]
Increase in finance lease liability	(91 764)	(114 864)
Increase in deferred tax liability	(8 118)	(3 318)
Increase in equity	8 117	3 318
Adjustment to retained earnings at beginning of 20X5		3 318
Increase in basic earnings per share	X	
Increase in diluted earnings per share	X	

a 135 000 – 13 500 – 13 500 = 108 000
b 135 000 – 13 500 = 121 500

NOTE: Although the company changed its accounting policy for finance leases, its previous policy was not in line with existing International Financial Reporting Standards, and therefore the change represents the correction of a prior period error.

CALCULATIONS

1. Interest paid on foreign exchange loan

31/12/20X5	(630 000 x 15% x 6/12)/0,4725	100 000
30/6/20X6	(630 000 x 15% x 6/12)/0,50	94 500
		194 500

2. Unrealised foreign exchange difference

630 000/0,50 - 1 400 000	140 000

(Note that 194 500 - 140 000 = 54 500 as supplied in question).

3. Finance lease schedule

		Capital	Interest	Balance
1/7/20X3	Cash price			135 000
30/6/20X4	Instalment	20 136	19 864	114 864
30/6/20X5	Instalment	23 099	16 901	91 765
30/6/20X6	Instalment	26 498	13 502	65 267
30/6/20X7	Instalment	30 397	9 603	34 870
30/6/20X8	Instalment	34 870	5 130	-

4. Other expenses

	20X6 R	20X5 R
Operating costs given	641 000	555 000
Finance lease capitalised *	(40 000)	(40 000)
Legal costs	4 500	-
Interest on bank overdraft disclosed separately	(1 850)	(1 500)
Interest on foreign borrowing disclosed separately (calc. 1)	(194 500)	-
Fine due to contravention of Companies Act (erroneously classified as extraordinary item)	5 000	-
Expenses disclosed separately		
• 20X6 (43 + 121)	(164 000)	
• 20X5 (37,5 + 124,5)		(162 000)
	250 150	351 500

Note that the exchange gain is included in (deducted from) other expenses. Alternatively it may be included as part of other income.

4A Cost of sales

Cost of sales (given)	639 000	670 000
Add: Depreciation on leased assets * (135 000/10)	13 500	13 500
Cost of sales after new policy	652 500	683 500

* *The lease charge was erroneously included in operating costs, but should actually be split into a depreciation charge and a finance cost charge and then be allocated elsewhere. Once the split has been made, the depreciation should be included in cost of sales as it relates to a manufacturing machine. The finance costs should form part of the line item for finance costs on the face of the statement of profit or loss and other comprehensive income.*

5. Taxation calculations

20X5 Normal taxation (current and deferred) 134 599 @ 50% — 67 300

20X6 Current taxation

Profit before tax		143 498
Add back: - Fine		5 000
		148 498
Taxable temp. differences		(12 998)
Depreciation		13 500
Lease finance charges		13 502
Lease instalment		(40 000)
Taxable income		135 500
Current taxation		67 750
Deferred taxation	- taxable (12 998 @50%)	6 499
		74 249

Deferred tax – alternative calculation

	Carrying amount R	Tax base R	Temporary difference R	Deferred tax R
20X4:				
Lease liability (C3)	114 864	-	(114 864)	(57 432)
Machinery	121 500	-	121 500	60 750
				3 318
20X5:				
Lease liability (C3)	91 765	-	(91 765)	(45 882)
Machinery	108 000	-	108 000	54 000
				8 118
20X6:				
Lease liability (C3)	65 267	-	(65 267)	(32 633)
Machinery	94 500	-	94 500	47 250
				14 617

Movement in profit or loss:

20X5 (8 118 – 3 318)	4 800 dr
20X6 (14 617 – 8 118)	6 499 dr

6. **Prior year adjustment**

	20X6	20X5	Before 20X5
Finance lease instalments	40 000	40 000	40 000
New policy	(27 002)	(30 401)	(33 364)
Depreciation	13 500	13 500	13 500
Lease finance charges	13 502	16 901	19 864
Increase in profit (taxable temp. differences)	12 998	9 599	6 636
Increase in deferred taxation	6 499	4 800	3 318
	6 499	4 799	3 318

7. **Interest and finance charges**

A detail analysis is not required, but only the total amount:

	20X6	20X5
Overdrawn bank	1 850	1 500
Foreign loan (calc 1)	194 500	-
Lease finance charges (calc 3)	13 502	16 901
	209 852	18 401

SUGGESTED SOLUTION TO QUESTION 3

ASPATAT LIMITED

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 30 JUNE 20X8

	Note	20X8 R'000	20X7 R'000
Revenue (700 + 24)		800	724
Cost of sales (**C2**)		(410)	(340)
Gross profit		390	384
Other income (9 + 14)		23	9
Other expenses (250 + 100)		(350)	(220)
Profit before tax	2	63	173
Income tax expense	3	(1)	(65,6)
Profit/total comprehensive income for the year		62	107,4

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 30 JUNE 20X8

	Notes	Retained earnings R'000
Balance at 1 July 20X6		66,0
Change in acc. policy	6	30,0
Restated balance		96,0
Total comprehensive income/profit for the year (restated)	5	107,4
Dividends paid		(41,0)
Balance at 1 July 20X7		162,4
Total comprehensive income/profit for the year		62
Dividends paid		(48,0)
Balance at end of the year		176,4

NOTES FOR THE YEAR ENDING 30 JUNE 20X8

2. **Profit before tax**

The amount is shown after taking into account:

	20X8 R'000	20X7 R'000
Gain on sale of land	14	-
Carrying amount of vehicle destroyed in flood	(100)	-

3. **Income tax expense**

Main components of tax expense

SA Normal	20X8	20X7
Current (**C3, C4**)	45	53,6
Deferred taxation (**C5**)	(33)	12
Tax rate adjustment (**C5**)	(11)	-
Taxation per statement of profit or loss and other comprehensive income	1	65,6

Taxation rate reconciliation

Accounting profit	63	173
Tax at 30% (20X7 – 40%)	18,9	69,2
Non-taxable income ((9 + 14) x 30%) (9 x 40%))	(6,9)	(3,6)
Effect of rate change	(11)	-
Income tax expense	1	65,6

The standard tax rate decreased from 40% to 30% during the current year.

5. **Prior period error**

The error relates to not accounting for certain sales in 20X7, which was detected during the current year and corrected. The error has been corrected retrospectively and the comparative amounts have been adjusted accordingly. The effect on 20X7 is as follows:

	20X7 R
Increase in revenue	24 000
Increase in tax expense	(9 600)
Increase in profit for the year	14 400
Increase in trade receivables	24 000
Increase in tax due	(9 600)
Increase in equity	14 400
Increase in basic earnings per share	x
Increase in diluted earnings per share	x

6. **Change in accounting policy**

During the year the company changed its accounting policy in respect of inventory valuation. (Provide reason why fairer presentation would be achieved). The company will in future value inventory at the average cost method instead of the FIFO method. The change in policy has been accounted for retrospectively and the comparative amounts were appropriately restated. The effect of the change is as follows:

	20X8 R	20X7 R	1/7/20X6 R
Decrease in cost of sales	20 000	30 000	
(Increase)/decrease in tax expense	2 000	(12 000)	
Increase in profit for the year	22 000	18 000	
Increase in inventory	100 000	80 000	50 000
Increase in deferred tax liability		(32 000)	(20 000)
Increase in current tax due	(30 000)		
Increase in equity	70 000	48 000	30 000
Adjustment to retained earnings at the beginning of 20X7			30 000
Increase in basic earnings per share	x	x	
Increase in diluted earnings per share	x	x	

CALCULATIONS

1. Effect of change in accounting policy

	20X6		20X7		20X8
Old method	500		600		700
New method	550		680		800
Statement of profit or loss and other comprehensive income	50	30	80	20	100
Deferred taxation	(20)	(12)	(32)	24[a]	
Rate adjustment				8[b]	
Current tax				(30)[c]	
	30	18	48	22	

a 80 x 30% OR 32 balance – 8 rate change (b)
b 32 x 10%/40%
c 100 x 30%

2. Cost of sales

20X7: 370 + 50 - 80 = 340
20X8: 430 + 80 - 100 = 410

3. Current taxation for 20X8

Accounting profit	63
Non-taxable income (9 + 14)	(23)
	40
Accounting loss – flood damage	100
Tax loss – flood damage	(70)
Difference in opening inventory ito Receiver's policy	80
	150
Taxation @ 30%	45

4. Current taxation for 20X7

Amount shown in question	44
Additional tax on sales invoices (24 x 40%)	9,6
	53,6

No deferred tax as wear and tear equals depreciation (calc 5)

OR

Profit before tax	173
Non-taxable income	(9)
	164
Difference in inventory i.t.o. Receiver's policy	(30)
	134
Taxation @ 40%	53,6

5. Deferred tax

	Carrying amount R	Tax base R	Temporary difference R	Deferred tax R
20X6:				
Inventory	550	500	50	20
Vehicle	140	110	30	12
Deferred tax liability				32
20X7:				
Inventory	680	600	80	32
Vehicle	120	90	30	12
Deferred tax liability				44
Rate change (44 x 10/40)				(11)
				33
20X8:				
Inventory	800	800	-	-

Movement in statement of profit or loss and other comprehensive income (excluding rate adjustment):

20X7 (44 – 32)	12 dr
20X8 (33 – 0)	33 cr

SUGGESTED SOLUTION TO QUESTION 4

NOTES FOR THE YEAR ENDED 31 DECEMBER 20X2

		20X2 R	20X1 R
2.	**Profit before tax**		
	Included in profit before tax is the following:		
	Gain on sale of machine	-	52 833
	Depreciation	(851 000)	(925 833)
	Impairment (machine destroyed in flood)	(660 000)	-
	Income from insurance (machine destroyed in flood)	630 000	-
3.	**Income tax expense**		
	Major components of tax expense:		
	SA Normal tax		
	Current [**C5**]	-	-
	Deferred [**C6**]		
	- current year	150 300	(155 100)
	- rate adjustment	-	(25 850)
		150 300	(180 950)
	Tax rate reconciliation		
	Accounting profit/(loss) [**C7**]	1 677 000	(1 442 000)
	Tax at 30%	503 100	(432 600)
	Tax effect of:		
	Dividends received (150 000 x 30%); (101 000 x 30%)	(45 000)	(30 300)
	Rate adjustment	-	(25 850)
	Unprovided, unutilised tax loss [(2 397 500 [**C6**] – 1 500 000 [**C6**]) – 1 923 500 [**C5**]] x 30% (Utilised in 20X2)	(307 800)	307 800
	or [(3 423 500 [**C5**] – 2 397 500 [**C6**]) x 30%]	150 300	(180 950)

On 1 January 20X1 the tax rate changed from 35% to 30%. No current tax was paid during any of the two years, as the company had assessed losses. An amount of R307 800 which was previously unprovided was used to reduce the current tax 20X2.

4. **Change in accounting policy**

During the year the company changed its policy regarding the valuation of inventory from the first-in-first-out method to the weighted average method, in order to achieve fairer presentation (provide reason why fairer presentation would be achieved). Comparative amounts have been restated accordingly.

	20X2	20X1	1/1/20X1
(Increase)/decrease in cost of sales	(32 000)	48 000	
(Increase)/decrease in income tax expense	(5 700)(B)	1 050(A)	
Increase/(decrease) in profit for the year	(37 700)	49 050	
Increase in inventory	19 000	51 000	3 000
Increase in deferred tax liability	(5 700)(B)	-	(1 050)
Increase in equity	13 300	51 000	1 950
Adjustment against retained earnings at the beginning of 20X1			1 950
Increase/decrease in basic earnings per share	X cent	X cent	

(A) The change in the accounting policy had no impact on the current tax for 20X1. If the accounting policy did not change, the deferred tax balance for 20X0 would have been R179 900 and for 20X1 R0 – therefore a movement of R179 900cr through profit or loss. After the change in accounting policy, there is a movement of R180 950cr through profit or loss – therefore an increase of R1 050cr in the movement through profit or loss.

(B) Although the R19 000 increase in closing inventory has been taken into account in the calculation of the current tax expense, the company is still not in a tax paying position as a result of the unused assessed loss. Therefore the change in policy does not affect the current tax expense or taxation payable account, as would normally be the case. The R19 000 however reduces the balance of the unused assessed loss at the end of 20X2. As the full assessed loss is recognised for deferred tax purposes at the end of 20X2, the change in accounting policy results in a higher deferred tax liability. Before the change in policy, the cumulative unused assessed loss at the end of 20X2 amounted to R1 964 000 (3 423 500 [cumulative loss end 20X1] – 1 459 500 [taxable income 20X2]), resulting in a deferred tax balance of R144 600 [(2 446 000 – 1 964 000) x 30%]. After the change in policy, the deferred tax balance amounted to R150 300 [C6]. The effect of the change in policy is therefore an increase in the liability of R5 700 (150 300 – 144 600). Similarly, before the change in policy the movement in the statement of profit or loss and other comprehensive income was from a zero balance in 20X1 to a liability of R144 600. After the change in policy the movement in the statement of profit or loss and other comprehensive income is R150 300 [C6]. The income tax expense thus also increased with R5 700.

5. **Deferred tax**

	20X2 R	20X1 R
Machinery (2 536 000 [**C6**] x 30%); (2 380 500 [**C6**] x 30%)	760 800	714 150
Inventory (51 000 [**C6**] x 30%)	-	15 300
Prepaid expenses (50 000 x 30%)	-	15 000
Accrued leave [(84 000 + 6 000) x 30%]; (84 000 x 30%)	(27 000)	(25 200)
Assessed loss (1 945 000 [**C6**] x 30%); (2 397 500 [**C6**] x 30%)	(583 500)	(719 250)
	150 300	-

Tax benefit i.r.o. unprovided unutilised tax loss amounting to R1 026 000 in 20X1.

CALCULATIONS

C1. Machine sold

	Acc R	Tax R
Carrying amount/tax base 1 March 20X1	697 167	600 750
Proceeds	750 000	750 000
Profit/recoupment	52 833	149 250

C2. Machine destroyed in flood

	Acc R	Tax R
Carrying amount/tax base 1 July 20X2	660 000	390 000
Proceeds	630 000	630 000
(Loss)/Recoupment	(30 000)	240 000

C3. Depreciation/wear and tear/carrying amount/tax base

	Acc R	Tax R
Carrying amount/tax base 1 Jan 20X1 [5 972 000 – (704 900/35%)]	5 972 000	3 958 000
Depreciation/wear and tear 20X1	(925 833)	(1 388 750)
Machine sold	(697 167)	(600 750)
Carrying amount/tax base 1 Jan 20X2	4 349 000	1 968 500
Depreciation/wear and tear 20X2	(851 000)	(1 276 500)
Machine destroyed	(660 000)	(390 000)
Carrying amount/tax base 31 Dec 20X2	2 838 000	302 000

C4. Change in accounting policy

	F/P 20X2 R	C/I 20X2 R	F/P 20X1 R	C/I 20X1 R	F/P 20X0 R
Old method	433 000		321 000		568 000
New method	452 000		372 000		571 000
Effect on financial position	19 000		51 000		3 000
Effect on profit (down)/up		(32 000)		48 000	

C5. Current tax

	20X2 R	20X1 R
Taxable income/(assessed loss) – given at end of year	1 459 500	(1 923 500)
Increase in closing inventory	19 000	-
Taxable income/(assessed loss)	1 478 500	(1 923 500)
Loss carried over/used	(3 423 500)	(1 500 000)
Unused loss	(1 945 000)	(3 423 500)

C6. Deferred tax

	Carrying amount R	Tax base R	Temporary difference R
20X0			
Machinery [**C3**]	5 972 000	3 958 000	2 014 000
Inventory	571 000	568 000	3 000
			2 017 000
Assessed loss [**C5**]			(1 500 000)
			517 000
Deferred tax balance @ 35% - credit			180 950
20X1			
Machinery [**C3**]	4 349 000	1 968 500	2 380 500
Inventory	372 000	321 000	51 000
Prepaid expenses	50 000	-	50 000
Accrued leave	(84 000)	-	(84 000)
			2 397 500
Assessed loss [**C5**] (Limited to taxable differences)			(2 397 500)
			-
Deferred tax balance @ 30%			-
Opening balance – credit			(180 950)
Decrease in liability			(180 950)
Rate adjustment (180 950 x 5%/35%)			25 850
Normal deferred tax through profit or loss			(155 100)

20X2			
Machinery [**C3**]	2 838 000	302 000	2 536 000
Inventory*	452 000	452 000	-
Accrued leave	(90 000)	-	(90 000)
			2 446 000
Assessed loss [**C5**]			(1 945 000)
			501 000
Deferred tax balance @ 30% (as well as increase in liability)			150 300

*Accounting and tax are the same because SARS allows new policy from 20X2.

C7. Accounting profit/(loss*)*

	20X2 R	20X1 R
Given	1 709 000	(1 490 000)
Change in policy **[C4]**	(32 000)	48 000
	1 677 000	(1 442 000)