THE CHARTERED INSTITUTE OF TAXATION OF NIGERIA

OCTOBER 2023: PROFESSIONAL EXAMINATION

PTE I: GOVERNANCE, RISK & ETHICS

ATTEMPT QUESTION ONE AND ANY OTHER FOUR QUESTIONS.

TIME: 3 HOURS

QUESTION 1

Baba Ahmed had worked in the firm of B. G. & Co. (Tax Practitioners) for several years after qualifying as a CITN Tax Practitioner. Recently, he has not been happy at the direction B. G. & Co. is going due to ineffective and inefficient management. He, therefore, applied for his practice licence from his professional body, Chartered Institute of Taxation of Nigeria, so that he could set up his own practice. After obtaining his practice licence, he registered his firm, Baba Ahmed & Co. (Tax Practitioners), with the Corporate Affairs Commission. However, as he was contemplating resigning from the firm, he was nominated as the Managing Partner of the firm of B. G. & Co. The nomination as the new Managing Partner was due to the declining fortunes of B.G. & Co. and the acknowledgement of the immense contributions of Baba Ahmed to the firm, emanating from his excellent professional skills.

Because of his several years of experience in the firm, he knew that the declining fortune of the firm were due to:

- Some weaknesses he identified in the firm;
- Lack of proactive response to the changing business environment;
- Inability of the partners to improve their professional skills and technical knowledge on the changes in tax laws and new business opportunities;
- Lack of code of professional practice and good governance practices in the firm;
- The firm's non-responsiveness to changes in the external environment; and
- indiscipline among the partners of the firm.

Baba Ahmed was torn between assumption of office as the Managing Partner of B.G. & Co. and setting up Baba Ahmed and Co. After some considerations and critical evaluation of the two options, he decided to accept the challenge of taking the position of the Managing Partner of B. G. & Co. On assumption of office, he decided to critically evaluate the internal and external environments of B. G. & Co. and discuss the key elements to be considered in drawing up a code of professional practice and corporate governance to guide the operations of the firm.

Baba Ahmed has appointed you as a consultant to help him prepare a paper that addresses the following:

(a) Technique to evaluate the alignment of the internal environment of the firm with the opportunities and challenges in its external environment. 6 marks
(b) Advantages and limitations of the technique deployed above. 5 marks
(c) Technique to evaluate the external environment of the firm. 9 marks
(d) Threats to effective corporate governance in an organisation 16 marks
(e) Remedies for structural barriers to effective governance within the firm. 4 marks

Total 40 marks

SOLUTIONS TO QUESTION 1

(a) SWOT is an acronym for "Strengths, Weaknesses, Opportunities, and Threats". It is simply a study undertaken by an organization to identify its internal strengths and weaknesses, as well as its external opportunities and threats. It is a framework which is used to identify and evaluate both the internal factors which confer strengths and weaknesses and the external factors which offer opportunities and threats to a business. A SWOT analysis helps to organize the firm's top strengths, weaknesses, opportunities, and threats into an organized list which is usually presented in a simple two-by-two grid as a strategic planning tool.

SWOT Analysis deals with the four influencing environmental factors, namely:

- **Strength**: an inherent capacity of an organization which helps it gain a strategic advantage over its competitors. Strengths are resources and competences that an organization has, and the capabilities it has developed. Strengths in resources, competences and capabilities can be exploited and developed to create sustainable competitive advantage.

- **Weakness**: an inherent constraint or limitation which creates a strategic disadvantage for a business. Weaknesses are resources, competences and capabilities that are deficient or lacking. These weaknesses are preventing the entity from developing or sustaining competitive advantage.

- **Opportunity**: a favourable condition in the organization's environment enabling it to strengthen its position. Opportunities are presented by the environment within which our organization operates. These arise when an organization can take benefit of conditions in its environment to plan and execute strategies that enable it to become more profitable or dominant. Organizations can gain competitive advantage by making use of opportunities.

- **Threat**: an unfavourable condition in the organization's environment causing damage to the organization. Threats arise when conditions in the external environment jeopardize the sustainability and profitability of the organization's business. They compound the vulnerability when they relate to the organization's weaknesses. Threats are uncontrollable. When a threat comes, the stability and survival of the organization may be at stake. Examples of threats are ever-changing technology, increasing competition leading to excess capacity, price wars and reducing industry profits, etc.

(b) Advantages of SWOT Analysis are:

(i) It is a source of information for strategic planning.
(ii) It enhances the organization's ability to build on its strength.
(iii) It enables an organization to identify and reverse its weaknesses.
(iv) It enables an organization to maximize its response to opportunities.
(v) It enables an organization to overcome its threats.
(vi) It helps in identifying core competencies of the firm.
(vii) It helps in setting of objectives for strategic planning.
(viii) It helps in knowing the past, present and future, so that by using the past and current data, future plans can be formulated.

Limitations of SWOT Analysis are:

(i) SWOT is intended as a starting point for discussion and cannot, in itself, show managers how to achieve a competitive advantage. Because the SWOT analysis is a snapshot of the firm at a particular moment in time, the analysis might obscure the fact that both the internal and external environments are rapidly changing.
(ii) It is argued that SWOT may harm performance since firms or business organizations do not use the outputs within the later stages of the strategy.
(iii) Some scholars in the field of business have critiqued the misuse of the SWOT analysis as a technique that can be quickly designed without critical thought leading to a misrepresentation of strengths, weaknesses, opportunities, and threats within an organization's internal and external environments. If a firm becomes preoccupied with a single strength, such as cost control, they can neglect their weaknesses, such as product quality.
(iv) Another limitation includes the development of a SWOT analysis simply to defend previously decided goals and objectives. This misuse leads to limitations on brainstorming possibilities and "real" identification of barriers. This misuse also places the organization's interest above the well-being of the community.
(v) Furthermore, a SWOT analysis should be developed as a collaborative effort, with a variety of contributions made by participants including community members. The design of a SWOT analysis by one or two workers is limiting to the realities of the forces, specifically external factors, and devalues the possible contributions of community members.

(c) PESTLE Analysis

PESTLE stands for the analysis of the external factors which are beneficial when conducting research before beginning a new project or to help conduct market research. These factors are:

- Political – Laws, global issues, legislation and regulations which may have an effect on your business either immediately or in the future.
- Economic – Taxes, interest rates, inflation, the stock markets and consumer confidence all need to be taken into account.
- Social – The changes in lifestyle and buying trends, media, major events, ethics, advertising and publicity factors.

- Technological – Innovations, access to technology, licensing and patents, manufacturing, research funding, global communications.
- Legal – Legislation which has been proposed and may come into effect and any passed legislations.
- Environmental – Environmental issues either locally or globally and their social and political factors.

(d) Threats to Effective Governance

Some of the threats to effective (corporate) governance are:

(i) ***Conflict of Interest:*** conflict of interest occurs when a member of the management tries to assert his or her personal relations with a certain individual to advance his/her personal agenda. It hinders the effective implementation of Corporate Governance as it only favors a few individuals, thus, creating an impression of "injustice" and "inequality" in the workplace.

(ii) ***Low Employee Morale:*** when a company's employees are not regularly meeting their targets or when they always come late at work, it could be a sign of low employee morale. Employees who are low in morale often disregard the rules set by the business which is counter-productive from a manager's standpoint. Hence, it is advisable to engage in a personal discussion with them to resolve their issues or grievances to the company.

(iii) ***Lack of Transparency*:** lack of Transparency in business dealing affect the corporate governance as it encourages "shady" deals which could lead to wastage of precious resources of a business.

(iv) ***Inadequate information about members of board and management***: In most corporations, shareholders have information about the boards and members of top management, as well as about the general affairs of the company only at Annual General Meetings that are poorly attended. Besides, information distributed is substantially window-dressed.

(v) ***Insincerity on the part of members of board and management***: Directors and management staff who are entrusted with running of the affairs of businesses usually see standards put in place to enhance corporate governance as a set of rules to be circumvented.

(vi) ***Ignorance on the part of stakeholders:*** stakeholders are often ignorant of their statutory corporate rights and responsibilities. This renders them more vulnerable to expropriation and other forms of exploitation. Indeed, the existence of a body of well informed and educated stakeholders would enhance corporate governance.

In most cases, board failures are not due to lack of motivation or competence of the individuals on the boards, but are the result of clear structural barriers ranging from board size to the complexity of a firm, which can lead to the failure of the board to effectively obtain, process and share information as individuals and as a group. Thus, the following structural barriers also constitute threats to effective governance:

Individual Factors (related to the individual board members):

(vii) ***Outside job demands***: As successful and busy professionals, many board members simply do not have the time and availability to discharge their board responsibilities effectively.

(viii) ***Complexity of outside job demands***: With outside responsibilities involving complex issues and situations, the board member is unable to focus on the firm's priorities.

(ix) ***Dissimilarity of outside job demands:*** A board member may not have the experience or knowledge required to make effective decisions for the firm.

Group Factors (related to the dynamics among the directors on the board):

(x) ***Board size:*** Large boards are less effective because of difficulty in coordinating actions, lack of cohesiveness, etc.

(xi) ***Meeting frequency:*** The board meets too infrequently to build trust-based working relationships.

(xii) ***Diversity of the board:*** While diversity can add new perspectives, different backgrounds and experiences can hinder communication and assumptions about how to approach tasks.

(xiii) ***Norms of deference:*** Some board members follow social norms that call for undue deference to the CEO.

(xiv) ***CEO power:*** Powerful CEOs can control the agenda of board meetings and may determine who sits on the board.

Firm Factors (related to the characteristics of the firm):

(xv) ***Firm size*:** Large firm size will lead to increased complexity.

(xvi) ***Firm complexity***: Complexity is due to multiple products, multiple geographic markets, foreign ownership, etc. Part-time boards that meet infrequently do not have the time to fully understand the broad range of information technologies, products and markets of multi-product firms or the variety of cultural and regulatory environments of multi-geographic firms, leaving them unable to effectively monitor the activities and decisions of fully informed, full-time executives and managers.

(e) To address the above structural barriers, the following measures can be taken:

- more frequent meetings — perhaps using information technology alternatives to reduce travel issues;
- longer shared tenure to increase cohesiveness and trust on larger boards;
- norms of openness without fear of retribution to alleviate issues such as social values that encourage deference to CEOs; and
- strategic recruiting to avoid function diversity where board members are unfamiliar with the issues and environment of the firm.

QUESTION 2

The chartered Institute of Taxation of Nigeria (CITN) has introduced nine standards on taxation.

a. State the Nine (9) standards (9marks)

b. Explain any TWO (2) of them. (6marks)

Total 15 marks

SOLUTION TO QUESTION 2

Standards on Taxation introduced by CITN:
1. Know your client;
2. Tax returns position;
3. Procedural aspects of filing returns;
4. Previously agreed tax returns filing position;
5. Form and content of tax advice / procedures;
6. Knowledge of error: Administrative procedures
7. Knowledge of error: return preparation
8. Use of estimates;
9. Tax planning

STS 1: Know your client.
The standard stated that when acting for a client, a member of the Institute places his/her professional expertise at the disposal of the client, and in doing so, the member assumes a duty of care towards the client.

A member must, therefore, exercise reasonable skill and care when acting for a client. Failure to do so may cause a member to be sued for negligence on the discharge of his professional duties. The duty of care will exist whether or not an engagement letter is issued. A member should insist on or instigate a letter of engagement to clearly delineate the scope of his responsibilities.

STS 2: Tax returns position
This standard is for members when recommending tax returns positions and preparing or signing tax returns (including amended returns, claims for refund and information returns) filed with the tax authority.

A member should, therefore, not recommended to a client acceptance of a tax return position with respect to any item unless the member is convinced that the position enjoys the backing of the relevant tax laws and can be effectively defended if challenged by the relevant tax authority.

STS 3: Procedural aspects of filing returns.
It sets our guidance on the applicable standards for members when recommending tax return filing positions and preparing returns.

It deals with preparation and filling of tax returns forms for company income tax and their legal requirements, taking due cognisance of the tax payers' nature of business and other relevant particulars.

The standard states that a member should not recommended that a tax return filing position be taken with respect to any item unless the member is satisfied that the position has a realistic possibility of being sustained on its merit if challenged by the relevant tax authority.

STS 4: Previously agreed tax return filing position.
The standard states that a tax return position with respect to an item as determined in an administrative proceeding or court decision does not restrict a member from recommending a different tax position in a later years return, unless the tax payer is bound to a specific treatment in the later year, such as by a written agreement or dispensation.

STS 5: Form and Content of tax advice/opinion
The standard sets out guidance for members on certain aspects of providing advice to a client. However, the standard does not cover a member's responsibilities when the expectation is that the advice rendered is likely to be relied upon by parties other than the client.

The standard further states that before giving advice to a client, it is important that the member classifies/identifies the following issues. The purpose of the advice, the scope of the advice, who is to rely on it and the risk of reliance. The above issues should be reflected in the engagement letter confirming the client's instructions to the member and the terms on which the advice is to be provided.

STS 6: Knowledge of error: Administrative procedures.
It sets out guidance on the standard for a member who becomes aware of an error in a return that is the subject of an administrative proceeding, such as an examination by any tax authorities. If a member is aware that a tax return contains an error, the tax payer should be informed promptly. The member should recommend the corrective measure

to be taken. The member is not obliged to inform the tax authority, nor should to do so without the tax payer's permission, except when required by law.

The member should request the tax payer's agreement to disclose the error to the relevant tax authority. If the taxpayer refuse, the member should withdraw from representing the taxpayer.

STS 7: Knowledge of error: return preparation.
The standard is to guide members on how to conduct themselves when error is detected in a taxpayer's previously submitted tax returns or taxpayer's failure to submit a required return. A member should inform the taxpayer promptly upon becoming aware of an error in a previously submitted return or upon becoming aware of a taxpayer's failure to submit a required return. The member should recommend the corrective measure to be taken.

The member should not inform the tax authority without the taxpayer's permission except when required by law. If a member is requested to prepare the current years return and the taxpayer has nor taken appropriate action to correct the error in a prior year's return, the member should consider whether to withdraw from preparing the return or whether to continue relationship with the taxpayer.

STS 8: Use of Estimates
The standard set out guidance on the applicable standards for member when using the taxpayer's estimates in preparing a self-assessment returns. A member may advise on estimates used in the preparation of a return, but the taxpayer has the responsibility to provide the estimated data. Valuations are not considered as estimates for the purpose of this statement. The disclosure of the use of estimate should be consistent with the relevant tax authority self-assessment procedures.

STS 9: Tax Planning
It is universally accepted principle that taxpayers are entitled to order their affairs so that the tax payable under the law could be the minimal amount under the law and nothing more.

The following standards are expected of a member when assisting a client in a tax planning arrangement.

i. A member should never be involved in any tax evasion arrangement;
ii. A member should not perform impermissible actions as tax avoidance or be involved in any abusive avoidance scheme.
iii. A member should not recommend tax planning which he does not consider to be appropriate;
iv. A member should not be involved in tax planning arrangement that has potential for tax evasion
v. A member should explain to his client the material risk of the tax planning / tax position and the basis on which the advice is given.

QUESTION 3

The code of best practice for Corporate Governance identifies three key player in the implementation of good corporate governance to be:

(a) The board of directors;
(b) The audit committee; and
(c) The shareholders.

Required:

a. State FIVE (5) functions of each of
   i. Board of Directors 5 marks
   ii. Audit committee 5 marks

b. State FIVE (5) rights of shareholders 5 marks

(Total 15 Marks)

SOLUTION TO QUESTION 3

Functions of board of Directors

(i) Strategic planning for the company;
(ii) Appointment performance evaluation and compensation of services executive officers;
(iii) Ensuring the integrity and accuracy of control systems and annual reports;
(iv) Ensuring adequate disclosure of information on the annual reports;
(v) Ensuring the protection of shareholders rights;
(vi) Ensuring effective communication of financial information to stakeholders;
(vii) Ensuring that ethical standards are developed and complied with; and
(viii) Identifying the company's risk profit and managing them.

Functions of audit committee.

(i) To ascertain whether the accounting and reporting policies of the company are in agreement with the laws and standards;
(ii) To keep under review, the effectiveness and compliance of internal control systems;
(iii) To authorise the internal audit to carry out investigations into any activity of interest to them;
(iv) To give recommendations to the board with regard to the appointment, removal and renumeration of the external auditors;
(v) To review the findings of the external and internal auditors of the company and follow up management responses; and
(vi) To review the scope and planning of audit requirements thereon.

Rights of shareholders

(i) Right to attend Annual General Meeting (AGM): The venue of any Annual general meeting (AGM) should be communicated to shareholders;

(ii) Right to receive notices: Before the Annual general meeting (AGM), notices should be sent at least 21 working days to enable shareholders vote wisely on important issues;

(iii) Right to have decisions implemented: The board should ensure that decisions reached at the Annual General meeting (AGM) are implemented;

(iv) Right to the represented: There should be at leased one director on the board to represent non-controlling interest member;

(v) Right to receive dividends: The board should ensure that annul dividends are paid as approved at the Annual General Meeting (AGM); and

(vi) Right to receive information: The board should ensure that all information and annual reports are communicated to shareholders.

QUESTION 4

(a)	Identify and discuss four major components of business risk.	6 Marks
(b)	Briefly explain four different ways of dealing with risks in organisations.	4 Marks
(c)	Highlight five (5) principles of risk management.	5 Marks

(Total 15 Marks)

SOLUTION TO QUESTION 4

(a) Identify and discuss four major components of business risk.

Business risk usually occurs in one of four ways, namely, strategic risk, compliance risk, operational risk, and reputational risk.

(i) **Strategic risk** is understood as a possible loss that might arise from the pursuit of an unsuccessful business plan. It might arise, therefore, from making poor business decisions or poor execution of decisions or from inadequate resource allocation, etc. It is often a major factor in determining a company's worth, particularly observable if the company experiences a sharp decline in a short period of time.

(ii) **Compliance risk** is exposure to legal penalties, financial forfeiture and material loss an organization faces when it fails to act in accordance with industry laws and regulations, internal policies or prescribed best practices.

(iii) **Operational risk**, in line with the definition adopted by the European Solvency II Directive for insurers, is the risk of a change in value caused by the fact that actual losses, incurred for inadequate or failed internal processes, people and systems, or from external events (including legal risk), differ from the expected losses. It summarizes the uncertainties and hazards a company faces when it attempts to do its day-to-day business activities within a given field or industry.

(iv) Reputational risk is the potential loss to financial capital, social capital and/or market share resulting from damages to a firm's reputation. It is a threat or danger to the good name or standing of a business or entity and can occur in the following ways:

(i) directly, as a result of the actions of the company itself;

(i) indirectly, due to the actions of an employee or employees; and

(ii) tangentially, through other peripheral parties, such as joint venture partners or suppliers. Reputational risk is consequential of an adverse or potentially criminal event even if the company is not found guilty. Adverse events typically associated with reputation risk include ethic violations, safety or security issues, lack of sustainability, etc. (6 Marks)

(b) Briefly explain four different ways of dealing with risks in organizations.

There are basically four effective risk mitigation strategies and they are:

(i) Risk Avoidance: If a risk presents an unwanted negative consequence, one can avoid those consequences by staying away from the business activities in question. In other words, the best way to avoid risk is to exit the business, cancel the project, close the factory, etc. This, of course, has other consequences, yet it is an option. Another approach is to establish policies and procedures that assist the organization to foresee and avoid high-risk situations.

(ii) Risk Acceptance: This is also known as risk retention. This strategy is implemented when we accept the identified risk and do not take any other action in order to reduce the risk because we can accept its impact or the possible consequences. When the decision to accept the risk is in part based on an estimate or prediction, there is the risk the information incorrectly forecasts the future. Therefore, for high consequence field related failures, closely monitoring field performance or establishing early warning systems may be prudent.

(iii) Risk reduction or control: this strategy occurs when we take some measures to reduce the risk to an acceptable level. Reducing the probability or the severity of the consequences of an unwanted risk – say, a product failure – is a natural outcome of risk prioritization tools. If it is not possible to reduce the occurrence or severity, then implementing controls is an option, that is, controls that either detect causes of unwanted events prior to the consequence occurring during use of the product, or the detection of root causes of unwanted failures that the team can then avoid. Controls may focus on management or decision-making processes. Improving the ability to find design flaws or to improve the accuracy of field failure rate prediction both improve the ability to make the appropriate decisions concerning risk. Another method to reduce risk is to diversify. For example, reflecting on the mix of products, technologies, markets, operations, and supply chains permit the team the ability to limit the high-risk opportunities to a manageable or acceptable level.

(iv) **Risk transfer**: this occurs when we transfer the risk to another person or entity. In practice, companies can, for instance, get insurance (transfer of risk to an insurance company) or can transfer the risk to another company by means of outsourcing. This strategy is to shift the burden of the risk consequence to another party. This may include the conventional means of transferring risk to another organization with the purchase of insurance. This may require a careful analysis of the risks. Also, contract terms with suppliers, vendors, contractors, etc. may provide a means to shift risk away from one's organization. For example, if power supply fails causing damage to an expensive server, resulting in loss of revenue for a customer, one might ask for and receive a replacement power supply. Or one could require the power supply vendor to cover the cost of the entire server (which the power supply caused to fail) and the loss incurred by the customer.

(c) Highlight five (5) principles of risk management.

- The process should create value.
- It should be an integral part of the organizational process.
- It should be factored into the overall decision-making process.
- It must explicitly address uncertainty.
- It should be systematic, structured and timely.
- It should be based on the best available information.
- It should be tailored to the organization's internal and external environments.
- It should take into account an organization's human and cultural factors.
- It should be transparent and inclusive.
- It should be responsive to changes.

QUESTION 5

(a) Explain three (3) benefits that socially responsible organisations can derive from the act of being socially responsible. (3 Marks)

(b) Briefly discuss the view of Archie Carroll on Corporate Social Responsibility in his Four-part Model of Corporate Social Responsibilities. (6 Marks)

(c) Highlight and briefly explain important stakeholder groups in the middle area of responsibility of a company according to Stefanie Hiss (6 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 5

(a) Explain Three (3) benefits that socially responsible organizations can derive from the act.

(i) Businesses that are socially responsible are likely to attract more customers while those that are socially irresponsible may experience undesirable consumer actions. For example, they may have their goods and services boycotted by customers.

(ii) Corporate social responsibility is a way of making a positive and long-term investment that would facilitate the evolution of a more educated, more equitable and safer society. Such a society would provide a better social environment within which corporate entities would be better positioned to pursue their corporate interests.

(iii) Skilled employees are likely to be attracted to corporations that are considered to be socially responsible. Employees are also more likely to be more committed to corporations that are socially responsible than they would be to those that are not.

(iv) Being socially responsible would facilitate corporate independence as there would be the reduced need for governments to legislate in corporate matters.

(v) Corporations, through their activities, generate social problems and as such have a social responsibility to resolve such problems and also prevent other social problems arising from them. One of such problems is the problem of environmental pollution caused by many manufacturing industries.

(vi) In contemporary society, corporate entities wield tremendous socio-economic and socio-political influence and also have great resources at their disposal. They should use all these responsibly in ways that would enhance social welfare.

(vii) Corporate activities have social impacts on all stakeholders through the provision and distribution of goods and services, employment of workers, payment of taxes, publication of financial statements, and other corporate actions. As such, corporations cannot escape responsibilities for the social effects of their actions, be it positive, negative or neutral.

(viii) Corporate entities benefit from society in the sense that the latter provides the platform as well as all the resources required by the former to function. This imposes a duty on corporate entities to take into account the interest of the larger society as they embark upon their profit-making activities.

(b) Briefly discuss the view of Archie Carroll on Corporate Social Responsibility in his Four-part Model of Corporate Social Responsibilities.

Archie Carroll sees corporate social responsibility as a complex concept that has four essential components, levels or aspects that are interrelated, namely, economic, legal, ethical, and philanthropic responsibilities. These levels of responsibilities are usually presented in such a way that corporations are expected to satisfy all of them in order to be truly socially responsible. They are:

(i) **Economic responsibility**: the main reason for setting up a business is to generate profit for their owners, provide good quality products for their customers or clients and well-paying jobs for employees. Achieving these objectives constitutes the basic economic responsibility of businesses, and it is the extent to which this economic responsibility is fulfilled that a business could be said to be a properly functioning and viable economic unit. This economic responsibility is mostly considered as the basis for all other forms of responsibilities.

(ii) **Legal responsibility**: The legal responsibility of corporations places an obligation on them to carry out all their activities in accordance with the law or all the legal requirements of the society in which they operate. It is in this regard that they are expected to play the game of business according to the rules of the game of business. Law, in this regard, may be rightly construed as the codification of the moral values of society. Hence, abiding by them is requisite for further reasoning about social responsibilities.

(iii) **Ethical responsibility**: Ethical responsibilities are the obligations that corporate entities have to do what is right, just, and fair even when there are no legal requirements that they should do so. They consist of those general expectations that society have towards corporate entities. These include, for example, maintaining a safe environment.

(iv) **Philanthropic responsibility**: Philanthropic responsibilities require that a corporation does all it can to improve the quality of life of its employees, local community and society in general. Philanthropic responsibilities include charitable donations, support for local schools, sponsoring social events such as sports and arts, and building recreational facilities for employees and their families or even the local community. Generally, philanthropic responsibilities include all those things that are desired of corporations but which they are not required to do. As such, this category of responsibilities appears to be the least important of the four categories of corporate social responsibilities.

(c) Highlight and briefly explain important stakeholder in the middle area of responsibility of a company according to Stefanie Hiss.

Stefanie Hiss suggests that the middle area of responsibility mainly refers to stakeholders. Generally speaking, stakeholders are people who have an increased interest in processes, working conditions and, in most cases, the success of the company. According to Hiss, the following groups of people form important stakeholders:

- **Employees**: Companies have a duty to their employees to ensure a pleasant working environment and, in addition, to make information sufficiently transparent in terms of career opportunities and hierarchies. This also includes the issue of fair remuneration and profit sharing as well as the limitation of the term of contracts. Another fundamental element for healthy corporate social responsibility in this area is the constructive interaction with trade unions when they operate within the company. In extreme cases, there can be strikes if companies do not take their social responsibility towards their employees seriously. Unacceptable working conditions sometimes invite human rights organizations' or state institutions' attention to the issue. Frequently, employees will make these grievances public, meaning that the news can spread like wildfire across social media and cause considerable image damage.

- **Equity and debt capital providers**: Investors have a clear interest not only in the success of the company, but also in fair cooperation. Above all, listed companies are threatened with considerable damage if their dealings with business partners and investors are morally questionable or dishonest.

- **Clients**: Companies that supply products should not deceive their customers. Especially in the case of consumer goods such as food, a company has the responsibility to correctly inform the customer about the preparation and composition of the product. Knowing the origin of the product and the raw materials used is also important to many customers. If a company presents itself to the outside world as environmentally friendly, but, uses eggs from caged production or components from environmentally harmful production plants in the manufacturing of a product, this can lead to a considerable loss of customer base. For many companies, the customer is by far the most important stakeholder. If a company does not take its social responsibility towards its customers seriously, this is often due to poor corporate social responsibility management (if any).

- **Local residents**: Companies located in cities or at least in the immediate vicinity of settlements also have a responsibility towards local residents. The operation should not have a negative impact on the quality of life of the residents. This applies, for example, to noise and environmental pollution. In many countries, people still suffer from harsh living conditions as large factories ignore their social responsibility. In the worst case, companies cause drinking water pollution, unacceptable noise, air pollution, and damage to the surrounding flora and fauna. If such injustices are made public, the company is threatened not only with damage to its image, but also problems with the law and environmental protection organizations.

- **Governmental agencies**: Companies must comply with the laws of the countries they operate within. This also includes smooth and honest cooperation with government organizations such as, for example, health and safety departments and health offices. In production facilities, the quality standards and regulations specified by the law must be observed through regular checks and surveys.

- **Media**: The responsibility of the "fourth estate" includes the most complete possible reporting of grievances in companies. The relationship between journalists and business is therefore often two-sided: on the one hand, a company wants to present itself as well as possible, so that the media can help cultivate a positive image of them through their reporting. On the other hand, companies that do not live up to their corporate responsibilities can quickly suffer damage to their image if journalists speak out about it. Media representatives are, therefore, not welcome on some company premises. Since corporate social responsibility is not subject to state control, the media often feels obliged to inform the public about corporate misconduct. In principle, good corporate social responsibility management in principle involves an open and honest dialogue with the media. However, journalists will rarely report on the positive performance of companies, but instead focus on incidents of misconduct simply because negative press sells better.

QUESTION 6

(a) What is tax risk control framework? (2 Marks)
(b) What are the three major steps that are essential to tax audit risk assessment? (3 Marks)
(c) Discuss Five ways by which tax justice system can address the problem of inequality in an economy. (5 Marks)
(d) State any five features of morality. (5 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 6

(a) What is tax risk control framework?

Tax risk control framework sets out the activities, tools, techniques and organizational arrangements to ensure all tax risks are identified, assessed, understood and that appropriate responses are in place to mitigate the impact of all risks.

(b) What are the three major steps that are essential to tax audit risk assessment?

The following points are crucial in tax audit risk assessment.

(i) Tax audit staff must be properly trained to be able to educate individual taxpayer on how to undertake effective tax planning.

With tax laws and the global environment becoming more complex, greater commercial awareness and training for employees is necessary. Staff must have the training and the expertise to administer tax law based on the rule of law. Meanwhile, individuals, trusts and companies need to undertake effective tax planning so they can stay competitive. They should be aware of the increased uncertainty of tax filing positions, which requires taxpayers to be prepared and think through next steps.

(ii) Taxpayers should fully document their positions upfront to prevent complications down the road. To the extent possible, organizations should consider maximizing the scope of privilege when identifying their tax risks. For instance, they may consider obtaining a litigation risk review, a process in which the legal advice is privileged. This not only helps identify risks in a protected way, but it means that if a dispute occurs many years later, all of the required information will readily be organized and available to substantiate their tax position.

(iii) Consultation with tax experts; it is important to consult with tax experts from the start of an audit and not wait until problems arise. Managing the audit process will enable one to anticipate, prevent and resolve issues as much as possible.

(c) Discuss Five ways by which tax justice system can address the problem of inequality in an economy.

The following points show how tax justice system can address the problem of inequality:

(i) Tax Justice systems should focus on financial secrecy and tax abuse as key problems that deprive developing countries of the revenues to which they are entitled.
(ii) Tax systems should reflect the balance of powers in the society.
(iii) Tax justice system should formulate effective tax and fiscal policies.
(iv) The concept of tax justice is particularly relevant to a region where many people have long felt deprived of economic opportunity and excluded from the benefits of the high growth achieved in the early years of the third millennium. Tax justice should be relevant to region where many people have felt deprived of economic opportunity.
(v) Tax reforms should not place disproportionate burden on the poor without delivering on social and economic rights.
(vi) Radically different economic and social policies are needed, with social justice at the forefront, and based on equitable and progressive policies to raise sufficient revenues for public expenditures prioritizing marginalized groups and regions, alongside investment and incentives to create decent work opportunities and more productive economies.
(vii) Trust in tax and fiscal policies must also be built. Tax systems need to be progressive and differential in their application, so that individuals and

companies are happy to contribute to financing the development of the country according to their means and capacity.

(e) State any five features of morality.

Features of Morality

(1) Morality involves making normative statements or judgments about specific human actions to the effect that they are either good or bad, right or wrong, just or unjust. Examples of normative statements made in the realm of morality are:
  (a) Danladi did something wrong by lying.
  (b) It is morally bad for Steven to have stolen the money.

(2) It is always meaningful to demand for the reasons or justifications for the normative statements made in the domain of morality.

(3) There is usually a reliance on some normative principles, rules or ideals in the effort to provide justification for the moral judgments made in the arena of morality. Such normative principles include Lying is wrong; Honesty is a virtue; Stealing is bad.

(4) Morality involves some emotional states of approval or disapproval attached to the moral judgments made and the moral rules and principles relevant to them. There would also be the desire to communicate such emotional states to others.

(5) There are sanctions or incentives, usually verbal, in the form of either blame or praise attached to moral judgments.

QUESTION 7

(a) Is Emotional Intelligence the same as Intelligence Quotient? Justify. (4 Marks)

(b) Explain comprehensively the importance of Emotional Intelligence to business success. (5 Marks)

(c) Explain the three main models of Emotional Intelligence. (6 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 7

(a) Is Emotional Intelligence the same as Intelligence Quotient. Justify

Comparison between Emotional Intelligence and Intelligent Quotient.

- High IQ is no guarantee of success; how successful we are in life is determined by both emotional intelligence and by IQ, though intellect works best when it is accompanied by high emotional intelligence.

- Both IQ and EI have considerable value. Where IQ tells us the level of cognitive complexity a person can achieve and may to some degree predetermine levels of academic achievement, EI indicates which individuals will likely make the best leaders within top management positions.

- IQ has limited connections to both work and life successes. IQ is actually less of a determinant of how well one will do in life than our ability to handle frustration, control emotions, and get along with other people – characteristics not only accounted for but also learnable under current EI theory.

- That IQ alone is the predictor of success is a misconception; it has been argued that life success is influenced more by an individual's ability to engage the five categories of EI, namely, self-awareness, self-regulation, motivation, empathy and social skills.
- While there is much discussion regarding the capability of individuals to improve IQ scores, EI can be developed and refined over time just like any skill – that is given the necessary focus and effort to do so. Many would argue that the ability to connect with and understand others is a more powerful skill to possess than cognitive intellect alone.

- EI, unlike IQ which is relatively fixed, is a dynamic aspect of one's psyche and includes behavioral traits that, when worked upon, can yield significant benefits, from personal happiness and well-being to elevated success in a professional context.

(b) Explain Comprehensively the importance of Emotional Intelligence to business success.

Importance of Emotional Intelligence to business Success.

- **Staff motivation**: Emotional intelligence matters for motivation, and motivation matters for success. In relation to work, personal goals or health, the emotionally intelligent individual understands the deeper meaning of their aspirations and the self-motivation skills required to achieve them. An emotionally intelligent individual not only possesses the skills for self-motivation but also the skills required to motivate others, a useful talent to have especially in management positions.

- **Better working environment**: As the workplace evolves, so do individuals (from interns to managers) with higher EI are better equipped to work cohesively within teams, deal with change more effectively, and manage stress, thus, enabling them to efficiently pursue business objectives. Increasingly, organizations are recognizing the value of employees who exhibit the skills to cope with change and respond accordingly.

- **Enhanced business success:** The ability to understand and manage emotions is crucial to realizing one's true potential in business. Developing EI can greatly influence one's success by contributing to increased morale, motivation and greater co-operation. In the workplace, for instance, managers who consistently outperform their peers not only have technical knowledge and experience, but more importantly, they utilize the strategies associated with EI to manage conflict, reduce stress and as a result, improve their success.

- **Team spirit and bonding**: Emotional intelligence is an integral part of forming and developing meaningful human relationships. It is established that EI engenders significant links between high EI and more successful interpersonal relations.

- **Elimination of communication barrier**: The process of successful communication, and in times of conflict, successful negotiation is closely linked to high levels of EI. While those with low levels of EI may react defensively in stressful situations and escalate conflict, individuals with higher emotional intelligence have the skills available at their disposal to communicate effectively without resorting to confrontation or escalating tension.

(c) Explain the three main models of Emotional Intelligence.

Three main models of Emotional Intelligence are:

- **Ability Model**: The ability-based model views emotions as useful sources of information that help one to make sense of and navigate the social environment. The model proposes that individuals vary in their ability to process information of an emotional nature and in their ability to relate emotional processing to a wider cognition. This ability is seen to manifest itself in certain adaptive behaviors. The model claims that EI includes four types of abilities:

  (i) Perceiving emotions: the ability to detect and decipher emotions in faces, pictures, voices, and cultural artifacts—including the ability to identify one's own emotions.

  (ii) Using emotions: the ability to harness emotions to facilitate various cognitive activities, such as thinking and problem-solving. The emotionally intelligent person can capitalize fully upon his or her changing moods in order to best fit the task at hand.

  (iii) Understanding emotions: the ability to comprehend emotion language and to appreciate complicated relationships among emotions. For example, understanding emotions encompasses the ability to be sensitive to slight variations between emotions, and the ability to recognize and describe how emotions evolve over time.

  (iv) Managing emotions: the ability to regulate emotions in both ourselves and in others. Therefore, the emotionally intelligent person can harness emotions, even negative ones, and manage them to achieve intended goals.

- **Mixed model:** The model introduced by Daniel Goleman focuses on EI as a wide array of competencies and skills that drive leadership performance. Goleman's model outlines five main EI constructs:
  - (i) Self-awareness – the ability to know one's emotions, strengths, weaknesses, drives, values and goals and recognize their impact on others while using gut feelings to guide decisions.
  - (ii) Self-regulation – involves controlling or redirecting one's disruptive emotions and impulses and adapting to changing circumstances.
  - (iii) Social skill – managing relationships to get along with others
  - (iv) Empathy – considering other people's feelings especially when making decisions
  - (v) Motivation – being aware of what motivates them. Goleman includes a set of emotional competencies within each construct of EI. Emotional competencies are not innate talents, but rather learned capabilities that must be worked on and can be developed to achieve outstanding performance.

This model posits that individuals are born with a general emotional intelligence that determines their potential for learning emotional competencies.

- **Trait Model:** Trait EI is "a constellation of emotional self-perceptions located at the lower levels of personality." In lay terms, trait EI refers to an individual's self-perceptions of their emotional abilities. This definition of EI encompasses behavioral dispositions and self-perceived abilities and is measured by self-report, as opposed to the ability-based model which refers to actual abilities, which have proven highly resistant to scientific measurement.

THE CHARTERED INSTITUTE OF TAXATION OF NIGERIA

OCTOBER 2023: PROFESSIONAL EXAMINATION

PTE I: INDIRECT TAXATION

ATTEMPT QUESTION ONE AND ANY OTHER FOUR QUESTIONS.
TIME: 3 HOURS

QUESTION 1

Jakod Nigeria Limited is a manufacturer and importer of Wines and Spirits. The company is based in Ota Industrial Estate, Ogun State.
During the year, the company manufactured the following products in its factory in Ota:

Nigel Non-alcoholic Red wine	200,000 centilitres
Nigel Sparkling Red Wine	150,000 centilitres
Nigel Exotic Wine	100,000 centilitres
Natural-H Exotic Red Wine	125,000 centilitres
Nigel Cognac Spirits	250,000 centilitres

Excise tax/duties were paid on the manufactured products in accordance with the following rates:

Nigel Non-alcoholic Red wine	₦2/centilitre
Nigel Sparkling Red Wine	₦2/centilitre
Nigel Exotic Wine	₦2/centilitre
Natural-H Exotic Red Wine	₦2/centilitre
Nigel Cognac Spirits	₦3/centilitre

During the year the company paid for raw materials to the tune of ₦1,881,250, vat inclusive, to manufacture its various products as follows:

Nigel Non-alcoholic Red wine	₦456,061
Nigel Sparkling Red Wine	₦342,045
Nigel Exotic Wine	₦228,030
Natural-H Exotic Red Wine	₦285,038
Nigel Cognac Spirits	₦570,076

Also, during the year, the company imported the following products from France and Spain:

French Champagne 50,000 centilitres @ $1.25 per bottle of 25 centilitre.
French Cognac Spirit 150,000 centilitres @ $1.00 per bottle of 25 centilitre.
French Red Wine 100,000 centilitres @ $0.60 per bottle of 25 centilitre.
Spanish Sparkling Red Wine 150,000 centilitres @ $0.60 per bottle of 25 centilitre.
Spanish Sparkling White Wine 100,000 centilitres @ $0.60 per bottle of 25 centilitre.
Spanish Red Non-alcoholic Wine 200,000 centilitres @ $0.50 per bottle of 25 centilitre.
Spanish White Non-alcoholic Wine 100,000 centilitres @ $0.50 per bottle of 25 centilitre.

Custom duties were paid on the imported goods as follows:
Duty:

Wines	200%
Spirits	250%
Surcharge:	7.5%

Also, the closing inventories for the products on December 31, 2022 were as follows:

Nigel Non-alcoholic Red wine	20,000 centilitres
Nigel Exotic Wine	25,000 centilitres
Natural-H Exotic Red Wine	40,000 centilitres
French Cognac Spirit	25,000 centilitres
French Red wine	10,000 centilitres
Spanish Sparkling Red Wine	25,000 centilitres
Spanish Red Non-alcoholic Wine	50,000 centilitres

However, there were no opening inventory for any of the products on January 1, 2022.

The selling prices for the company's products during the year are as follows:

Nigel Non-alcoholic Red wine	₦1,000 per bottle of 25 centilitres
Nigel Sparkling Red Wine	₦750 per bottle of 25 centilitres
Nigel Exotic Wine	₦1,000 per bottle of 25 centilitres
Natural-H Exotic Red Wine	₦1,200 per bottle of 25 centilitres
Nigel Cognac Spirits	₦1,500 per bottle of 25 centilitres
French Champagne	₦2,500 per bottle of 25 centilitres
French Cognac Spirit	₦2,000 per bottle of 25 centilitres
French red wine	₦1,500 per bottle of 25 centilitres
Spanish Sparkling Red Wine	₦1,500 per bottle of 25 centilitres
Spanish Sparkling White Wine	₦1,500 per bottle of 25 centilitres
Spanish Red Non-alcoholic Wine	₦1,200 per bottle of 25 centilitres

Spanish White Non-alcoholic Wine ₦1,200 per bottle of 25 centilitres

The excise duty paid to the Nigerian Customs and Excise during the year was ₦1,250,000. While total Vat remitted to the FIRS was ₦5,000,000.
Exchange rate of $1 to Naira has been pegged at ₦500.

Required:

a. Distinguish between customs and Excise duties. (5marks)

b. Calculate the total custom duty paid by the company during the year 2022. (9marks)

c. Determine the total excise duty payable by the company in 2022. (6marks)

d. Determine the total input Vat paid by the company during the year. (10 marks)

e. Calculate the Vat due to the FIRS during the year and the balance payable on December 31, 2022. (7 marks)

f. What is the balance on the company's VAT ledger on December 31, 2022? (1½ marks)

g. What is the balance on the company's Excise duty ledger on December 31, 2022? (1½ marks)

(Total 40 Marks)

SOLUTION TO QUESTION 1

(a) Excise duty and custom duty are two types of indirect taxes. Excise duty is collected on the goods produced by a manufacturer that are to be sold in the country. Custom duty is levied on the goods that are imported from other country and are meant to be sold in the country. Both taxes are indirect taxes as they are passed on to the consumer by adding them to the cost of products.

Excise duty is levied along with another tax which can be sales tax or VAT. Excise duty constitutes the largest proportion of taxes in the price of a good. Unlike sales tax, excise duty is charged ad valorem, that is it is generally calculated on the number of goods or in volume of liquid.

Custom duty also known as consumption duty, is collected by the authorities on the goods imported by an importer and are meant to be sold in the country. The custom duty is levied on the goods whose value is determined by its assessable value, usually cost, insurance and freight. This assessable value has been developed by World Customs Organisation and has given codes to every product known as H. S. Codes that can be of four to ten digits. The rate of custom duty is decided by the government of the country in which the goods are being imported.

Both excise and custom duty are taxes levied by the government, but the major difference between the two is that excise is the tax levied by the government on the goods manufactured in the country while customs duty is a tax levied upon goods imported in to the country from other countries.

There are many provisions that are common to both excise and customs duty. The procedures of administration, settlement and tribunal are same for both taxes. The principles of valuation, refund search, confiscation and appeal are almost same in the case of the two taxes.

(b) **Custom Duty Paid**

Product	Quantity Centilitres	Quantity Bottles	Unit price in USD	Exch. Rate	Unit Price in Naira	Value ₦	Duty Rate	Custom Duty ₦
French Champagne	50,000	2,000	1.25	500.00	625.00	1,250,000.00	200%	2,500,000.00
French Cognac Spirit	150,000	6,000	1.00	500.00	500.00	3,000,000.00	250%	7,500,000.00
French red wine	100,000	4,000	0.60	500.00	300.00	1,200,000.00	200%	2,400,000.00
Spanish Sparkling red Wine	150,000	6,000	0.60	500.00	300.00	1,800,000.00	200%	3,600,000.00
Spanish Sparkling White Wine	100,000	4,000	0.60	500.00	300.00	1,200,000.00	200%	2,400,000.00
Spanish Red Non-alcoholic Wine	200,000	8,000	0.50	500.00	250.00	2,000,000.00	200%	4,000,000.00
Spanish White Non-alcoholic Wine	100,000	4,000	0.50	500.00	250.00	1,000,000.00	200%	2,000,000.00
Duty payable						-		24,400,000.00
Surcharge							7.50%	1,830,000.00
Total custom duty paid								**26,230,000.00**

(c) **Excise Duty Payable**

Product	**Quantity**	**Rate**	**Total**
		₦	₦
Nigel Non-alcoholic Red wine	200,000	2.00	400,000.00
Nigel Sparkling Red Wine	150,000	2.00	300,000.00
Nigel Exotic Wine	100,000	2.00	200,000.00
Natural-H Exotic Red Wine	125,000	2.00	250,000.00
Nigel Cognac Spirits	250,000	3.00	750,000.00
Excise Duty Payable			1,900,000.00

(d) **Input Vat Paid during the Year**

Imported Products

Product	Quantity Centilitres	Quantity Bottles	Value ₦	Duty ₦	Surcharge ₦	Total Value of Import ₦
French Champagne	50,000	2,000	1,250,000.00	2,500,000.00	187,500.00	3,937,500.00
French Cognac Spirit	150,000	6,000	3,000,000.00	7,500,000.00	562,500.00	11,062,500.00
French red wine	100,000	4,000	1,200,000.00	2,400,000.00	180,000.00	3,780,000.00
Spanish Sparkling red Wine	150,000	6,000	1,800,000.00	3,600,000.00	270,000.00	5,670,000.00
Spanish Sparkling White Wine	100,000	4,000	1,200,000.00	2,400,000.00	180,000.00	3,780,000.00
Spanish Red Non-alcoholic Wine	200,000	8,000	2,000,000.00	4,000,000.00	300,000.00	6,300,000.00
Spanish White Non-alcoholic Wine	100,000	4,000	1,000,000.00	2,000,000.00	150,000.00	3,150,000.00
						37,680,000
Input Vat on imported products						7.50%
Input Vat on rate of input Vat imported products						2,826,000.00
Input Vat on local purchases (7.5/107.5 x 1,881,250)						131,250.00
Total input vat paid during the year						2,957,250.00

(e) **Vat Due to FIRS in 2022**

Product	Quantity Available	Closing Inventory	Quantity sold Centilitres	Quantity sold - Bottles	Selling Price ₦	Revenue from Sales ₦
French Champagne	50,000	--	50,000	2,000	2500	5,000,000
French Cognac Spirit	150,000	25,000	125,000	5,000	2000	10,000,000
French Red wine	100,000	10,000	90,000	3,600	1500	5,400,000
Spanish Sparkling Red Wine	150,000	25,000	125,000	5,000	1500	7,500,000
Spanish Sparkling White Wine	100,000	--	100,000	4,000	1500	6,000,000
Spanish Red Non-alcoholic Wine	200,000	50,000	150,000	6,000	1200	7,200,000
Spanish White Non-alcoholic Wine	100,000	--	100,000	4,000	1200	4,800,000
Nigel Non-alcoholic Red wine	200,000	20000	180,000	7,200	1000	7,200,000
Nigel Sparkling Red Wine	150,000	--	150,000	6,000	750	4,500,000
Nigel Exotic Wine	100,000	25,000	75,000	3,000	1000	3,000,000
Natural-H Exotic Red Wine	125,000	40000	85,000	3,400	1200	4,080,000
Nigel Cognac Spirits	250,000	--	250,000	10,000	1500	15,000,000
		195,000	1,480,000			79,680,000
Vat						7.50%
Vat Due						5,976,000.00
Less Input vat*						369,153.98
Vat due to FIRS						5,606,846.02
Vat paid during the year						5,000,000.00
Balance vat payable as at 31 December 2022						**606,846.02**

- **Calculation of input Vat on Closing Inventories**

Product	**Quantity Available**	**Closing Inventory**	**Cost of Available Inventory** ₦	**Input Vat on Available Quantity** ₦	**Input Vat on Closing Inventory** ₦
French Cognac Spirit	150,000	25,000	11,062,500.00	829,687.50	138,281.25
French Red wine	100,000	10,000	3,780,000.00	283,500.00	28,350.00
Spanish Sparkling Red Wine	150,000	25,000	5,670,000.00	425,250.00	70,875.00
Spanish Red Non-alcoholic Wine	200,000	50,000	6,300,000.00	472,500.00	118,125.00
Nigel Non-alcoholic Red wine	200,000	20000	456,061.00	31,818.21	3,181.82
Nigel Exotic Wine	100,000	25,000	228,030.00	15,909.07	3,977.27
Natural-H Exotic Red Wine	125,000	40000	285,038.00	19,886.37	6,363.64
					369,153.98

(f) **Balance on the company's Vat Ledger on December 31, 2022**

	₦	
Balance on input vat	369,153.98	Dr
Balance on Vat payable at 31 Dec	606,846.02	Cr
Balance on the ledger	237,692.05	Cr

(g) **Balance on the company's Excise Duty Ledger on 31 December 2022**

	₦	
Excise Duty Payable	1,900,000.00	
Excise Duty Paid	1,250,000.00	
Balance on the ledger on 31 Dec	**650,000.00**	Cr

QUESTION 2

Like any other tax law, the Value Added Tax Act Cap V1 LFN 2004 (as amended) provides for
penalties for non-compliance with the provisions of the VAT law.

Required:

(a) Discuss the following penalties as provided in the VAT law:

(i) Failure to issue tax invoice (2 marks)

(ii) Failure to notify change of address (2 marks)

(iii) Resisting, etc., an authorised officer (2 marks)

(iv) Failure to register (2 marks)

(v) Aiding and abetting commission of offence (2 Marks)

(b) Apart from the ones mentioned above, itemise five (5) penalties provided for in the VAT law. (5 Marks)

(Total 15 marks)

SOLUTION TO QUESTION 2

(a)

(i) Failure to Issue Tax Invoice: Section 29 of the Value Added Tax Act Cap V1 LFN 2004 (as amended) provides stiff penalty for failure to issue tax invoice. A person who fails to issue tax invoice for goods sold or services rendered is guilty of an offence and liable on conviction to a fine of 50% of the cost of the goods or services for which the invoice was not issued;

(ii) Failure to notify change of address; *"Failure to notify of change of address or permanent cessation of trade or business"* .A taxable person who fails to notify the Service of any change of address within 30 days of such change, or who fails to comply with the requirement for notification of permanent cessation of trade of business under Section 8 of this Act, is liable to pay -N50,000 for the first month in which the failure occurs; andN25,000 for each subsequent month in which the failure continues

(iii) Resisting, etc., an authorised officer: A person who:
resists, hinders or obstructs or attempts to resist or hinder an authorised officer acting under section 39 of this Act; or
fails to comply fully with any requirement made under section 39 of this Act; or
makes any statement in response to a requirement made under section 5 of this Act which is false or incomplete; or
procures or attempts to procure by any means any other person to act as afore- said, is guilty of an offence and liable on conviction to a fine of ₦10,000 or imprisonment for a term of six months or to both such fine and imprisonment;

(iv) Failure to register: a taxable person who fails or refuses to register with the Service within the time specified in subsection (1) of this section shall be liable to pay as penalty an amount of -

- ₦50,000 for the first month in which the failure occurs; and
- ₦25,000 for each subsequent month in which the failure continues

Where a taxable person permanently ceases to carry on a trade or business in Nigeria, the taxable person shall notify the Service of its intention to deregister for tax purposes within 90 days of such cessation of the trade or business;

(v) Aiding and Abetting Commission of Offence:
An officer of the Service or any other person who aids or abets the commission of any of the offences under this Act, is guilty of an offence and is liable on conviction to a fine of N50,000 or to imprisonment for a term of five years.
Where a person's conduct during any specified period has involved the commission or omission by him of anyone or more of the foregoing offences under this Act, then whether or not the particulars of the offences are known, he shall, by virtue of this section, be guilty of an offence and liable to pay a fine of N 10,000 or four times the amount of any tax that was, or was intended to be evaded by his conduct, whichever is greater, or to imprisonment for a term not exceeding six months or to both such fine and imprisonment.

(b) Other things that attract penalties under the VAT law are:
(i) Unauthorized Issue of Tax Invoice;
(ii) Failure to render returns;
(iii) Effect of non-remittance of tax;
(iv) Furnishing of false document;
(v) Evasion of tax;
(vi) Failure to make attribution;
(vii) Failure to keep proper records and accounts; and
(viii) Failure to remit tax.

QUESTION 3

HUGAD Nigeria Limited is a manufacturing company that is located along Lagos/Ibadan expressway. The company needs a property (equipment) for the use of its business activities. The property was acquired for ₦40,000,000 in 2022. Immediately the property was purchased, the company's tax consultant advised the manager to send the purchase agreement of the transaction to the stamp duties office. The Managing Director disagreed with this instruction by arguing that the transaction agreement does not need to be sent to the stamp duties office.

Required:
You as a tax expert is consulted to:

a. Explain THREE (3) implications of non-stamping of instruments to the director. (3 marks)
b. With TWO (2) examples for each, list the TWO types of stamp duties. (4 marks)
c. Discuss the administration of Stamp Duties in Nigeria. (4 marks)
d. List any EIGHT (8) instruments that are chargeable to stamp duties. (4marks)

(Total 15 Marks)

SOLUTION TO QUESTION 3

(a) Three implications of non-stamping of Instruments are:

i. Such an instrument shall not be admissible in court as documentary evidence;

ii. Such an instrument is not admissible whether directly or for collateral purpose. The secondary evidence of the instrument is not admissible either; and

iii. Cross examination upon an unstamped instrument is not allowed.

(b) Two forms of Stamp Duties are:

i. **Fixed duties:** These are duties which do not vary with the consideration for the document. Examples of fixed duties are:

- Admission as a Barrister or Solicitor;
- Admission as a Notary public;
- Affidavit, affirmation and statutory declaration;
- Instrument of apprenticeship;
- Letter of power of attorney;
- Policy of insurance against accident;
- Receipt; and
- Bills of Exchange payable on demand or at sight or on presentation or within three days after date or sight.

ii. **Ad Valorem duties:** These are duties which vary with the amount or value of the consideration for the document, in accordance with scale of rates provided in the schedule to the Act.

Examples of Ad Valorem duties include:

- Valuation of any property;
- Bills of Exchange of any other kind and promissory note;
- Share Capital;
- Loan Capital;
- Contract notes for or relating to the sale or purchase of any stock or Marketable Security;
- Conveyance of transfer on sale or purchase of any stock or marketable security;
- Debenture;
- Mortgage; and
- Policy of life insurance.

(c) Stamp Duties are managed by the Commissioner of Stamp Duties who may be appointed from within the Service. The duty of a Commissioner may be performed by any one of the Commissioners where there is more than one. An instrument must be sent to the Commissioner of Stamp Duties for adjudication.

The Federal Government is the only competent authority to impose, charge and collect duties on instruments specified in the schedule to the Act, if such instruments relate to the matters executed between a company and an individual group or body of individuals. State Governments impose, charge, collect Stamp Duties on instruments executed by individuals.

(d) Instruments subject to stamp duties are:

- Lease;
- Contract notes;
- Bills of lading;
- Agreements;
- Duplicate and counterparts;
- Marketable securities;
- Mortgages;
- Notarial acts;
- Insurance policies;
- Receipts;
- Settlements;
- Share warrants;
- Warrants of goods;
- Appraisement;
- Instrument of apprenticeship;
- Capital of companies;
- Other conveyances;
- Letter of powers of attorney and voting papers;
- Bank notes, bills of exchange and promissory notes; and
- Exchange partition or division;

QUESTION 4

ADEU Nigeria Limited is into trading that collects industrial products from one or more manufacturers as well as importing raw material inputs, including packaging materials used for the production of goods exported. Towards the end of last month, the manager of the company resigned given a short notice and the company employed a new manager to oversee the activities of the company but unfortunately the new manager does not know anything about Temporary Importation Permits (TIP) which the company has been using for years.

The company has sought your assistance to explain the following to the newly employed manager:

a. Temporary Importation Permit (TIP) (3 marks)
b. The process of obtaining Temporary Importations permit(TIP) (5 marks)

c. Extension of Temporary Importation Permit (3 marks)

d. Documentary requirements for extension of Temporary Importation Permit TIP approval (4 marks)

(Total 15 marks)

SOLUTION TO QUESTION 4

(a) ADEU NIGERIA LIMITED

Temporary Importation Permit (TIP) is a permit issued for the importation of equipment and not imported for resale or rent but for the use of a specific project in Nigeria. They are usually marked for re-exporting at the completion of the project. The Nigerian Customs Service is usually the agency responsible for issuing the permit for the importation of such items needed for oil rigs, ships barges, aircrafts and other special equipment with a minimum value of USD 100,000.

(b) The process obtaining Temporary Importation Permit (TIP)

1. The temporary importation approval from Nigeria Custom Service (NCS) are obtained prior to shipment, the item are usually exempted from both the "Form M" and "pre-shipment inspection" procedures.
2. Before application is made, the following documents are required:
   (a) Pro-formal invoice from owner to the Nigerian importer stating the cost of freight of the item(s).
   (b) Lease agreement between the owner of the equipment and the Nigerian importer, specifying the equipment, lease period, lease cost, and other lease conditions.
   (c) Brochures and/or technical manual describing the items to be imported.
   (d) Copy of registration certificates (vessels and rigs only).
   (e) Copy of measurement certificate (vessels and rigs only).
   (f) Permit to operate in Nigerian waters from the Federal Ministry of Transport.
   (g) Copy of importer's certificate of incorporation.
   (h) Letter from importer addressed to Concessionary Logistic Limited authorizing the application for temporary importation on their behalf and stating the reasons for temporary importation.
   (i) Copy of importer's Tax Clearance Certificate (TCC) for 3 years.
   (j) Copy of the complete contract(s) between the importer and main contractor with duration and purpose of the equipment.
3. Upon receipt of the document above, the freight provider issues an application to the Comptroller General of the NCS in Abuja. A bond amount is fixed by NCS Head Quarters and is indicated in the formal temporary importation approval letter.

4. The temporary importation approval is then submitted to the Custom Area Comptroller at the point of entry, the cargo will be physically examined and the bond amount will be fixed as surety.
5. The process of applying for and getting the approval takes a minimum of four weeks.

(c) Extension of Temporary Importation Permit

A Temporary Importation is approved for an initial period of one year and can be extended by Customs Headquarters Abuja twice for six months. The maximum total period of a temporary importation is two years and extensions beyond that period are granted by Customs exceptionally on a case by case basis only for further period of three or six months.

(d) Documentary requirements for extension of TI approval

Photocopy of agreement (addendum) jointly signed by contractor and sub-contractor specifying that contract is still under execution and stating the duration of the contract. Note that variation of contract/service agreement is not acceptable. Also, it should be noted that the agreement/contract (addendum) should not be considered as in past similar cases.

- Photocopy Form Sale 33
- Photocopy of initial TI approval or last execution (if any)
- Photocopy of registration certificate (vessels and rigs only)
- Covering letter to Customs applying for extension of TI
- Letter from insurance/bank confirming validity of bond, copy of bond to be attached

QUESTION 5

Describe briefly the meaning of the following, in relation to tax professionals:

a. Conduct (3marks)
b. Integrity (3marks)
c. Courtesy (3marks)
d. Competence (3marks)
e. Confidentiality (3marks)

(Total 15 marks)

SOLUTION TO QUESTION 5

(a) Conduct

A member must:

(a) Take due care in his conduct;
(b) Take due care in all his professional dealings; and
(c) Uphold the professional standards of the CITN as set out in the Laws of the CITN.

A member must not:

(a) Perform his professional work, or conduct his practice or business relationships, or perform the duties of his employment improperly, inefficiently, negligently or incompletely to such an extent or on such number of occasions as to be likely to bring discredit to himself, to the CITN or to the members or any part of the membership or to the taxation profession.

(b) Breach the Laws of the CITN.

(b) Integrity

In addition to the above, a member:

(a) Must be honest in all his professional work. In particular, a Chartered Tax Practitioner (CTP) must not knowingly or recklessly supply information or make any statement which is false or misleading, or knowingly fail to provide relevant information.

(b) Must not be party to bribery or other illegal activities.

(c) Should not act if he considers that the fulfilment of his client's instructions involves a risk of assisting in a criminal activity.

(c) Courtesy

A member must be courteous and considerate towards all with whom he comes into contact in the course of his professional work.

(d) Competence

A member must carry out his professional work with a proper regard for the technical and professional standards expected. In particular, a member must not undertake professional work which the member is not competent to perform, whether because of lack of experience or the necessary technical or other skills; unless appropriate advice or assistance is obtained to ensure that the work is properly completed.

(e) Confidentiality

It is a criminal offence for tax officials or practitioners to disclose information, relating to a taxpayer that was obtained in the course of the performance of their duties. No universal definition of what constitutes tax information, however, in general, it covers all information obtained in the course of a person's duties as a tax official.

The obligation to maintain confidentiality applies even after the official has ceased to work for the tax administration or practitioner.

In addition to a tax requirement, an obligation of confidentiality may arise from boarder laws or regulations that applies to all civil servants.

QUESTION 6

Destination Inspection is offered as a support service to the Nigeria Customs Service. It is an outsourced service which involves the inspection of foreign sourced goods at the port of destination. The underlying demand for inspection services arose from the huge loss of revenue by Government on imported goods and the need to secure life by ensuring that dangerous and prohibited goods are not imported into the country.

You are required to:

(a) State any FOUR (4) benefits of destination inspection. (2 marks)

(b) List any SEVEN (7) responsibilities of importers as required by the Nigerian Customs Service. (7 marks)

(c) Discuss any three (3) types of Warehouses available in Nigeria. (6 marks)

(Total marks 15)

SOLUTION TO QUESTION 6

(a) Some of the benefits of destination inspection are listed below:

(i) Improvement of trade facilitation to cope with increased demand by traders for faster clearance of goods.
(ii) Securing revenue collection.
(iii) Combating fraud and smuggling.
(iv) Guaranteeing national security and fighting terrorism.
(v) Complying with the prevailing international regulations and guidelines in the domain of Customs valuation, trade facilitation, conformity and security.
(vi) Addressing congestion at ports and in-land border posts.

(b) Responsibilities of Importers as required by the Nigerian Customs Service

(i) Persons intending to import physical goods into Nigeria must firstly process Form M through any bank irrespective of the value and whether payment is involved or not.

(ii) Consignments shall bear the name of products, country of origin, specifications, date of manufacture, batch or lot number, standard(s) to which they were produced (e.g. BS, DIN, ISO/IEC, NIS etc.) Foodstuff (including drinks), pharmaceuticals and chemicals should carry expiry dates and/or shelf life and specify active ingredients where applicable on their packaging. The expiry date should be at least half the shelf life as at the time of inspection.

(iii) All electronics equipment/items and instruments MUST carry INSTRUCTIONAL MANUAL and not diagrams and notation on the containers. All electronic equipment/items and instruments MUST carry SAFETY information and/or safety signs. All electronic equipment/items and other instruments where applicable MUST carry a GUARANTY/WARRANTY of at least of six months.
(iv) Computer hardware and software must be year 2000 compliant.
(v) Plant materials, whether for planting, consumption of industry shall be covered with phytosanitary certificate of the country of export, certifying that the plant materials was inspected and found free from pests and that some treatment has been made where applicable in line with the International Plant Protection Convention of FAO.
(vi) Every manufactured item including components and spare parts shall be branded and bear manufacturers' names. Electrical appliances (fluorescent lamps, electric bulbs electric irons, kettles etc.) are required carry information about their life performance whilst cables must carry information on their rating.
(vii) Misrepresentation of products specifications will result in delays and/or seizure. Supply of wrong information with an intention to cheat will also result in delays and/or impoundment/seizure with attendant consequences. Blank products will be automatically seized and destroyed.
(viii) All goods imported into the country shall be labelled in English in addition to any other language or render themselves liable to confiscation.
(ix) Manufactured goods and materials are subject to Standard Organisation of Nigeria's (SON) certification in accordance with the provision of its enabling law.
(x) The importer shall advise his supplier on the need to submit after the completion of inspection, the Commercial Invoice within 72 hours to the Inspection Agent. This is to facilitate the issuance of Clean Report of Inspection by the Inspection Agent.
(xi) The importer shall ensure that he pays the appropriate customs duty as established on the Clean Report of Inspection to any of the designated banks.

(c) Types of Warehouses available in Nigeria

(i) Ordinary Warehouse:- This warehouse also known as goods warehouse may belong to the wholesaler or the producer or rented by them. They store their goods there as they are required by the wholesaler or retailer or their agents.

(ii) Customs Warehouse:- Owned by the Nigeria Custom Services (NCS), is a place where imports or exports are kept until they are required by the owners or until necessary duties are paid on the goods. Also kept in the customs warehouse are goods that restrictions have been placed on their importation know as contraband, which are seized by the NCS until they are disposed, sold or destroyed.

(iii) Bonded Warehouse:- It is a place where the Nigerian Custom Services (NCS) keep good whose owners have not paid their required duties. As the name suggests, it is hired from individuals or corporate bodies who sign bond with the NCS not to release the goods until government gives them an indication that the duties on them have been paid. The NCS pays certain fees for using these bonded warehouses.

(iv) Public Warehouse:- This is a privately owned warehouse that is meant for renting purposes such warehouse are found near docks, railway stations, airports etc. Some warehouses were built by the government but have been privatized and managed by individual and corporate bodies for profit. Public warehouses are used by occupiers for a short period of time to store goods that is in transit from one location to another.

QUESTION 7

The objective of ECOWAS Trade Liberalisation Scheme (ETLS) is to establish a custom union among all members' states aimed at the total elimination of customs duties and taxes of equivalent effect, removal of non-tariff barriers and the establishment of a common customs external tariff to protect goods produced in member states.

(a) What is ECOWAS Trade Liberalisation Scheme? (2marks)

(b) State and explain briefly any two (2) groups of goods covered under the scheme and the kind of concessions granted to each of them. (4 marks)

(c) State any SIX conditions to be fulfilled by the importer from any of the ECOWAS States. (6 marks)

(d) List any SIX justifications for the imposition of tariffs (3marks)

(Total 15 marks)

SOLUTION TO QUESTION SEVEN

(a) (i) ECOWAS Trade Liberation is a mechanism put in place by ECOWAS to promote economic integration among member countries. It is used to facilitate the free trade area by ensuring that goods can be circulated freely without payment of customs duties and taxes on imports.

(b) Three groups of goods covered under the scheme and the kind of concessions granted to each of them are:

1. Unprocessed goods- such as livestock, fish plant or mineral products that have not undergone any industrial transformation. This is given total exemption from import duties and taxes.

2. Traditional handicraft products- these articles are made with or without the help of tools, instruments or devices that are activated by the craftsman. Such products include wooden cooking utensils, fancy goods, small cabinet work, mats, carpets, bed lines footwear, headgear, prepared feathers. This is given no quantitative restriction.

3. Industrial products of community origin. This is given non-payment of compensation for loss of revenue for items (1) and (2) as a result of their importation.

(c) Five conditions to be fulfilled by the importer from any of the ECOWAS States are:

1. Goods must originate from members states of the community.
2. Goods must appear on the list of products annexed to decisions liberalizing trade in these products.
3. Goods must be accompanied by a certificate of origin and on ECOWAS Export Declaration Form.
4. Such goods must be subjected to the import clearance procedure spelt out under Nigeria and Export guidelines.
5. Exemption of goods whose value is not above $500 from documentation.
6. The beneficiary of the scheme must be resident within ECOWAS Sub-region.
7. The inter-state road transit declaration shall either be typewritten or hand-written but in the latter case, it shall be in ink, legible and in printed characters.
8. The inter-state transit declaration shall be signed by the principal oblige or by his authorized representative as well as the approved National Guarantor.
9. The goods must be transported under the cover of the ECOWAS ISRT Log Book and without being transferred to another means of transport between a member state and the office of final destination.

(d) Justifications for Tariffs

(i) Tariffs are one form of protective device to restrict trade.
(ii) To protect infant industries
(iii) To prevent dumping
(iv) As a means of raising revenue
(v) As a retaliatory measure
(vi) To encourage production of goods of strategic importance (i.e for strategic reasons)
(vii) To promote employment at home
(viii) To restrict importation of demerit or harmful goods thereby regulating the consumption.
(ix) To correct an adverse balance of payment or to ensure favourable balance of payment.
(x) To prosecute political objectives or decisions through imposition of sanction.

THE CHARTERED INSTITUTE OF TAXATION OF NIGERIA

OCTOBER 2023: PROFESSIONAL EXAMINATION

PTE I: INCOME TAXATION

ATTEMPT QUESTION ONE AND ANY OTHER FOUR QUESTIONS.

TIME: 3 HOURS

QUESTION 1

YOTO Agro Limited is a duly registered agricultural company with the Corporate Affairs Commission (CAC) in June 2020. It is situated in a remote village near Yotoyoto local government and has been prominent in the agricultural value chain in the area buying almost all the cassava roots harvested in the neighbourhood and processing into starch cassava flakes, cassava flour, cassava pellet and chips etc.

The company initially planned to be a primary agricultural producing company hence, it acquired 100 acres of land which was divided into four portions meant for: Portion A - Agric processing 10 acres; Portion B – Cattle: Sheep and Goat 20 acres; Portion C - Arable crops 30 acres; and Portion D - Permanent crops 40 acres.

The company however, changed its planned corporate objective and ventured into mainly agro-processing (i.e. Cassava processing) because it had financial difficulty and could only raise capital internally through disposal of land purchased except portion A (10 acres) which was earmarked for Agro-processing.

Surprisingly, for the past few months that the company commenced business, it has not registered with any tax agencies and therefore has not been tax compliant. However, the Federal Inland Revenue Service (FIRS) search beam light discovered its existence in the remote location and the business was served letter of non-compliance accordingly. This necessitated the appointment of Cleanslate Associates–a firm of Chartered Tax Practitioners as the company's tax consultants.

The firm, while gathering information and going through the business records established that:

(a) the company had taken loan from a bank; and

(b) other major capital-intensive transactions relate to capital expenditure and capital receipts as detailed below:

(i) The 100 acres of land was purchased at a cost of ₦86,250,000 excluding 10% agency commission/legal processing fees and additional ₦5,125,000 spent on landscaping/sand filling.

The total cost of 100 acres of land purchased is to be shared into 4 portions pro-rata based on acreage of land covered by each portion: A; B; C; and D;

(ii) Portion B (20 Acres) was disposed off at an arm's length transaction for ₦42, 222,250 excluding 10% attributable expenses (i.e. agency fees etc) to sales;

(iii) Portion C (30 Acres) with a market value of ₦65 million was not earmarked to be sold but was compulsorily acquired by the government for its "School-to–land" agricultural programme for the unemployed graduates. The government however, paid ₦34.8million as compensation for this compulsory acquisition; and

(iv) Portion D (40 acres) with a market value of ₦76 million was also disposed to a connected person at ₦80million, excluding allowable incidental expenses of 10%.

The first meeting of the Partners of the firm with the Directors and other important stakeholders showed the absolute need to enlighten them on the relevant tax issues and the business responsibilities as a taxpayer, to the relevant tax office.

You have been saddled with the responsibility to anchor the enlightenment programme as directed.

Required:

(a) Explain the expectation of a company as a taxpayer in the areas of registration with relevant tax agency for Tax Identification Number (TIN) and how to get this done with relevant supporting documents. (6 Marks)

(b) With respect to assessment, filing and payment, you are to briefly explain;

(i) what is meant by Self-assessment and what purpose it intend to achieve. (5 Marks)

(ii) taxpayer obligation under self-assessment. (3 Marks)

(iii) Administrative assessment and relate this to a company that failed to file returns and pay taxes (4 Marks)

(c) With reference to the Finance Act, 2020 concerning changes in the existing tax laws and regulation as it affects agricultural business, you are to briefly explain the amendments to section 11(2) of CITA on replacement of Agric. Trade or Business and how it will affect this business. (4 Marks)

With respect to the land purchased and subsequently disposed off or compulsorily acquired by the government.

(d) Determine the total cost of 100 acres of land acquired by the business and allocate the cost pro rata based on land acreage to the 4 portions (A, B, C, & D). (9 marks)

(e) For the portions of land disposed (i.e. portions B and D) or compulsorily acquired by government (i.e. portion C), determine with reason(s) where necessary;

(i) Capital gains and

(ii) Capital gains tax (9 Marks)

(Total 40 Marks)

SOLUTION TO QUESTION 1

(a) Registration with relevant tax agency for Tax Identification Number (TIN) and how to get this done with relevant supportive documents.

Tax registration is the starting point in the tax compliance cycle. Therefore, for a newly incorporated company, it would need to register as a taxable person with the relevant tax authority i.e. FIRS for authentication of Tax Identification Number (TIN) (now issued at the point of incorporation along with other incorporation documents).

Based on the business address stated at the point of incorporation, the company TIN issued would have been attached to the nearest FIRS office and the newly incorporated company is expected to register at such FIRS office so attached. However, there may be the need to redirect the TIN to the nearest FIRS office when it becomes necessary to do so.

Necessary documents required for TIN registration with FIRS include:

- A copy of Memorandum and Articles of Association;
- A copy of Certificate of incorporation;
- Form CAC1.1- Status Report (formerly form CAC 7) contains Particulars of Directors;
- CAC 2 Company’s Statement of Share Capital and Return of Allotment of Shares;
- Collect VAT Registration form 001 and CIT form from nearest FIRS Office and FIRS Questionnaire;
- Submit duly completed and stamped Registration form and Questionnaire;
- Other forms to fill include; Application for e-filling, e-TP access and New Tax Payer’s update;
- Utility bill to corroborate Business address; and
- Brief description of Taxpayer business office or site or farm siting landmarks etc.

Having successfully completed the registration process, the business should be ready to prepare and file monthly returns.

(b) (i) What is meant by Self-assessment?

It is a modern system of Tax administration introduced by government on mutual trust and commitment of parties involved, whereby a taxpayer (individual or corporate organisation) in accordance with the relevant tax laws is required to fulfil their duties and responsibilities by;

- correctly computing tax liability for a defined period or transaction
- properly file tax returns (now online).
- voluntarily generate Payment Reference Number (PRN) on FIRS Tax ProMAX online or Payment Code for IRS.
- voluntarily pay the self-assessed tax through the bank, bank transfer, or Remita or Interswitch.

(ii) Taxpayer obligation under self-assessment Regime

- Registration of Business with the relevant tax authorities (i.e. obtain requisite form, complete, and submit).
- Completion and filling of Returns.
- Maintenance of Business records (Sales Income, Purchases, Capital & Revenue Receipt & Payments, Drawings, loans, bank statements, Receipts and invoices).
- Voluntary disclosure of transactions, events, and declaration of relevant information.

(iii) Administrative assessment and relate this to a company that failed to file returns and pay taxes

This is where the relevant tax authority assesses the tax liability of a taxable person or entity using different sources of information (current information available plus additional information, third party sources, comparison of records, trends/ratio analysis etc).

It could arise where;

- a taxpayer has failed to file a return and pay tax due.
- the tax authority has additional information that necessitate raising additional assessment.
- the tax authority has established an understatement of tax in the returns filed or hidden income.

(c) Amendments to section 11(2) of CITA on replacement of Agric. Trade or Business and how it will affect this business

Section 11(2) of CITA was amended by replacing "agricultural trade or business" with "primary agricultural production" i.e. (production of crops, livestock, forestry, fishing, etc) and excludes production at the intermediate/by-products or derivatives level.

In view of the above, YOTO Agro Limited is not into "core or primary agricultural production" but, rather it is into trading by buying from "core" or "primary agricultural producer" i.e. cassava and adding value to it by processing into various products. Therefore, YOTO Agro Limited will not be excluded from payment of CIT or Minimum tax. It will not enjoy exemptions granted core or primary agricultural farm.

(d) **Cost of Land Acquired 100 acres**

	₦	₦
Acquisition cost		86'250'000
Add: Other incidental expenses.		
-Commission and legal processing fees (10%)	8,625,000	
-Land Scapping/sand filling	5,125,000	13,750,000
Total Cost of Land		100,000,000

(ii) **Cost Allocation to Portions based on acres occupied;**

Total cost of 100 acres = N100,000,000; N'000

Shared:	A	10 acres	10%	10,000 – in use
	B	20 acres	20%	20,000 - Disposed

C	30 acres	30%	30,000 - Acquisition
D	40 acres	40%	40,000 - Disposed

(e) Disposals -Determination of Capital Gain and Capital Gain Tax.
PORTION B

	₦
Sale of land (B) at arms-length	42,222,250
Less: Agency fee (10% x N 42,222,250)	(4,222,225)
Net sales (90%)	38,000,025
Less: Cost of acquisition (1 above)	(20,000,000)
(i) Capital Gain	18,000,025
(ii) Capital Gain Tax @ 10%	1,800,002.50

PORTION C - Compulsory Acquisition by Government.

	₦	₦
Market value of land (Not relevant)		76.000,000
Compensation received		34,800,000
Less: Cost of acquisition		(30,000,000)
Capital Gain		4,800,000
Capital Gain Tax @ 10% (Exempted WN1)		NIL

Working Note 1
Exempted is any capital gain on disposal of landed property by a forced/compulsory acquisition by any government in Nigeria provided that;

1. The taxpayer has not shown any previous intention to dispose off the asset e.g. by way of advertisement.
2. The taxpayer has not taken any previous step to dispose the asset by way of entering negotiation to sell.

PORTION D

Sales to Connected persons.

	₦	₦
Sales proceed-land D (to Connected persons)	80,000,000	
Less: incidental expenses (10%)	(8,000,000)	
Net sales (90%)	72,000,000	
Market value of land	76.000,000	
Use: Higher of; Mkt value or Net sales (WN2)	76,000,000	
Less: Cost of acquisition	(40,000,000)	
Capital Gain	36,000,000	
Capital Gain Tax @ 10%	3,600,000	

Working Note 2
For disposal of land to third party (i.e. not at arm's length), the Disposal value to use will be the higher of market value of land or net sales received

QUESTION 2

Wuse Textile Company Limited has been in existence for over six years and makes account to 31st December. The following information was extracted from the audited accounts in respect of accounting year ended 31/12/2021.

Turnover	₦115,437,329
Net profit per account (PBT)	₦859,891
Depreciation	₦1,234,525
Capital Allowance:	
- brought forward 1/1/2021	₦4,760,469
- for the year	₦985,443

Required:

(a) Briefly discuss the reduction in minimum tax provision rate introduced by the Nigerian government to cushion the impact of Covid 19 on businesses in Nigeria as it applies to Wuse Textile company. (3 Marks)

(b) Compute the relevant tax liabilities of the company for tax year 2022 in line with Companies Income Tax Act 2004 (as amended). (12 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 2

(a) Reduction in Minimum Tax rate introduced by the government was as a palliative to taxpayer to cushion the impact of Covid 19 pandemic on businesses in Nigeria. Thus, Minimum Tax rate was reduced by 50% i.e. from 0.50 % of Gross turnover less franked investment income to 0.25%. The rate is, however, applicable for the Year of Assessment due from 1/1/2020 to 31/12/ 2021 i.e. for only two years of assessment.

The accounting year given in the question falls into this period therefore, Minimum Tax provision of Wuse Textile company limited will be 0.25% of turnover that is;
0.25% of N115,437,329 = <u>₦288,885</u>

PTF: A levy of 0.005% of the net profit of companies operating businesses in Nigeria

(b) **WUSE TEXTILE COMPANY LIMITED**
COMPUTATION OF TAX LIABILITY
2022 TAX YEAR (ACCOUNTING YEAR: 1/1/2021 – 31/12/2021)

	₦	₦
Net profit per account		859,891
Add back depreciation		<u>1,234,525</u>
Adjusted profit		2,094,416
Less: capital allowances (schedule 1)		
Initial for 2022 YOA	--	

Annual for 2022 YOA	(985,443)	
B/f from 2021YOA	(4,760,460)	
Total capital allowances	(5,745,903)	
Restricted to 662/3 x N2,094,416 (WN1)	1,396,277	(1,396,277)
Unabsorbed capital allowance c/f	(4,349,626)	
Chargeable profit		698,139
EDT @ 2.5% x N2,094,416 (WN2)		52,361
Higher of CIT computed OR Minimum Tax Provision:		
CIT @ 30% x N698,139 (WN3)	209,442	
Minimum Tax provision	288,885	288,885

MINIMUM TAX PROVISION	₦
0.25% of Gross Turnover: (0.25% x N115,553,956)	288,885
POLICE TRUST FUND	
0.005% of profit before tax: (0.005% x N859,891)	43
NASENI	
0.25% of profit before tax: (ie N859,891)	2,150

SUMMARY	₦
CIT (Minimum Tax Provision)	288,885
Education tax	52,361
PTF	43
NASENI	2,150
Tax Liability	343,439

Working note;

1. Capital allowance is restricted to 662/3 of adjusted profit.
2. CIT rate is 30% being a large company whose turnover is above N100m.
3. Tertiary Education Tax is reduced by 50% from 5% to 2.5% as a palliative to cushion effect of covid19 on businesses during the accounting period

QUESTION 3

The management of a medium-sized trading conglomerate with branches in over twelve major cities in Nigeria has engaged your firm of Tax Consultants to organise a workshop on Pay-As-You-Earn, for staff in the Payroll and Tax Units of the organisation. The objective of the workshop is to update the staff on operations of PAYE. It is hoped that at the end of the workshop, the perennial conflicts between the company and the tax authority on issues relating to operations and administration of PAYE scheme will be significantly mitigated.

As the resource person, you are to draft a paper (in form of a report), which you intend to present at the workshop.

Required to:

Specifically address the following areas of PAYE administration:

(a) Responsibility for PAYE (employer and managers)- agency workers and managed services scenarios. (7 Marks)

(b) Earnings and benefits treated as income and exclusion for employment related expenses. (4 Marks)

(c) Deductions allowed from employment income. (4 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 3

WORKSHOP ON PAY-AS-YOU-EARN

(a) Responsibility for PAYE (employer and managers)- agency workers and managed services scenarios.

(i) Section 81 of Personal Income Tax Act 2004 (as amended) provides that for employees under a contract of service, it is the responsibility of their employers to deduct and remit taxes from the emoluments paid to such employees.

(ii) Section 82 of PITA 2004 (as amended) provides further that the employer is answerable to the tax authorities for taxes deducted from the employees.

(iii) The employer is required to file annual returns in respect of emoluments paid to their employees and account for the taxes withheld and remitted to the relevant tax authorities.

(iv) Section 81(2) of PITA 2004 (as amended) requires the employer to file annual returns not later than 31st January of every year in respect of all emoluments paid to its employees in the preceding year. Failure to comply attracts a penalty upon conviction.

(v) For individuals working under an outsourcing arrangement, the responsibility to account for their PAYE tax and all matter connected therewith lies with their employer (the outsourcing company).

(vi) Self-employed individuals are personally responsible for their own taxes.

(vii) Self-employed individuals are expected to file personal income tax returns under the self-assessment regime. However, the company to whom the services are rendered has the responsibility for deducting and remitting withholding tax on fees payable under the contract at applicable rate.

(viii) Self-employed individual has an obligation to register for Value Added Tax and charge VAT on invoices issued for services rendered, unless such services are specifically exempted.

(ix) The New Pension Reform Act 2014 mandates employers with 5 or more employees to make contributions on behalf of their employees into an approved pension fund. This is not compulsory for individuals with a contract for service. They can however make voluntary pension contribution into their retirement savings account.

(x) While the employer responsibility to account for PAYE is limited to employees engaged by the company, it is important for every organisation to ensure that appropriate records are in place to support its tax position.

(xi) The onus is on the organisation to ensure that it discharges its civic obligation as an unpaid agent of the government to deduct and remit PAYE taxes of its employees to the relevant tax authorities

(b) Earnings and benefits treated as income and exclusion for employment related expenses.

(i) Under the PITA 2004 (as amended), any salary, wages, fees, allowances or other gains or profits from employment including bonuses, premiums, or perquisites allowed, given or granted to any employee are chargeable to tax.

(ii) The following income streams are tax exempt:

* Reimbursement of expenses incurred by the employees in the performance of their duties, and from which the employee is not expected to make any profit.
* Retirement gratuities
* Compensation for loss of office
* Interest on loans for developing an owner-occupied residential house.

(iii) The following are tax deductible contributions:

* National Housing Fund contribution
* National Health Insurance Scheme
* Life assurance premium
* National Pension scheme

(iv) Along with the above listed tax exempts, the Consolidated Relief Allowance (CRA) will be granted as a relief. It is the higher of 1% of gross income or N200,000 plus 20% of gross income.

(c) Deductions allowed from employment income.

For the purpose of ascertaining the income or loss of an individual for any period from any source chargeable with tax under this Act, there shall be deducted all outgoing and expenses, or any part thereof, wholly, exclusively, necessarily and reasonably incurred during that period and ultimately borne by that individual in the production of the income.

These allowable deductions include:

(i) A sum payable by way of interest on money borrowed and employed as capital in acquiring the income;

(ii) Interest on loans for developing an owner-occupied residential house;

(iii) Rent for that period, and premiums the liability for which was incurred during that period, payable in respect of land or buildings occupied for the purpose of acquiring the income;

(iv) Any expense incurred for repair of premises, plant, machinery or fixtures employed in acquiring the income, or for the renewal, repair or alteration of any implement, utensil or article so employed;

(v) Bad debts incurred in any trade, business, profession or vocation, proved to have become bad during the period for which the income is being ascertained.

(vi) A contribution or an abatement deducted from the salary or pension of a public officer under the Pension Act or under any approved scheme any contribution, other than a penalty, made under the provisions of any Act establishing the Nigeria Social Insurance Trust Fund or other retirement benefits scheme for employees throughout Nigeria.

(vii) A contribution to a pension, provident or other retirement benefits, fund, society or scheme, recognised under the Pension Reform Act (Section 26 of Finance Act 2020)

QUESTION 4

Withholding Tax (WHT) is a tax deducted at source from income before the taxpayer receive the income to which the tax applies. Its provisions have become part of the income tax legislations that cut across relevant sections of Companies Income Tax Act 2004 (as amended), Personal Income Tax Act 2004 (as amended), Value Added Tax Act 2004 (as amended) and Petroleum Industry Act 2021.

Required:

(a) State **EIGHT** items that are contained in the WHT payment schedule, which will accompany the WHT cheque to be paid to the relevant tax authority. (4 Marks)

(b) Explain FIVE problems of administration of WHT in Nigeria. (5 Marks)

(c) Identify SIX dividends that are exempted from WHT. (3 Marks)

(d) Discuss the treatment of active income and passive income for WHT purposes. (3 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 4

(a) Items that are contained in the WHT payment schedule, which will accompany the WHT cheque to be paid to the relevant tax authority include:

(i) Names of the taxpayers who suffered the deduction;
(ii) Taxpayers addresses;
(iii) The nature of their activities/services;
(iv) The tax file numbers;
(v) The total amount payable;
(vi) The rate of tax applied;
(vii) The rate of tax withheld;
(viii) The balance paid to the taxpayer;
(ix) The tax period of the contract for which returns were being made;
(x) The date of payment; and
(xi) The cheque number and date.

(b) Problems of administration of WHT in Nigeria include:

(i) Non-deduction by some organisations;
(ii) Non-remittance after deduction;

(iii) Deductions at wrong rates;
(iv) Lumping together of deductions;
(v) Incomplete/incorrect information provided on the schedule;
(vi) Credit Notes not given to taxpayers by the Revenue Authorities (deducting agents);
(vii) Payment to wrong tax authority. For example, WHT meant for the State being paid to FIRS and vice-versa;
(viii) Dishonoured cheques; and
(ix) Failure to cooperate with tax inspectors by ministry, department and agencies (MDAs) when they come for inspections.

(c) Dividends that are exempted from WHT include:

(i) Dividends paid out of pioneer profit;
(ii) Dividends paid by issue of bonus shares;
(iii) Dividends from small companies in the manufacturing sector in the first five years of operations;
(iv) Dividends paid out of taxed petroleum profits;
(v) Dividends from companies engaged in petrochemical and liquefied natural gas;
(vi) Dividends received from investments in wholly export-oriented businesses;
(vii) Dividends received by a company from a country outside Nigeria and brought into Nigeria through government approved channels; and
(viii) Dividends distributed by unit trust.

(d) The treatment of active income and passive income for WHT purposes

Active income: This is an income for which the taxpayer performs services. Examples are wages, salaries, bonuses, business and partnership income in which the taxpayers materially participate in the business or partnership.

Passive income: This is an income from business activities in which the recipients do not materially participate in the business giving rise to the income. Examples are rental income, dividends, interests, royalties, etc.

While active income is subject to PAYE, passive income is subject to withholding tax deductions using the appropriate withholding tax rates.

QUESTION 5

The Federal Inland Revenue Service (Establishment) Act 2007 was enacted to provide for the establishment, collection of, and accounting for revenues accruable to the Government of the Federation and other related matters. Part 1 of the enabling Act specifically provides for the establishment of the Federal Inland Revenue Service and its management board.

Required:

(a) State the composition and functions of the Federal Inland Revenue Service Board. (8 Marks)

(b) Discuss any FIVE of the functions of the Federal Inland Revenue Service. (5 Marks)

(c) Identify any FOUR taxes that are collectible by the Federal Inland Revenue Service. (2 Marks)

(Total 15 Marks)

SOLUTION TO QUESTION 5

(a) Composition of the Federal Inland Revenue Service Board (FIRSB)

The Federal Inland Revenue Service Board comprises:

(i) Executive Chairman – who shall be a person within the service, to be appointed by the President;

(ii) Six members with relevant qualifications and expertise, to be appointed by the President to represent each of the six geo-political zones;

(iii) A representative of the Attorney-General of the Federation;

(iv) The Governor of the Central Bank of Nigeria or his representative;

(v) A representative of the Minister of Finance not below the rank of a Director;

(vi) The Chairman of the Revenue Mobilisation Allocation and Fiscal Commission or his representative who shall be any of the commissioners representing the 36 states of the Federation;

(vii) The Group Managing Director of the N.N.P.C. Ltd or his representative who shall not be below the rank of a Group Executive Director of the Corporation or its equivalent;

(viii) The Comptroller-General of the Nigerian Customs Service or his representative, not below the rank of Deputy Comptroller-General;

(ix) Registrar-General of the Corporate Affairs Commission or his representative not below the rank of a Director; and

(ix) The Chief Executive Officer of the National Planning Commission or his representative not below the rank of a Director.

(xi) Board Secretary Federal Inland Revenue Service.

Functions of the FIRSB

The FIRSB shall:

(i) Provide the general policy guidelines relating to the functions of the Service;

(ii) Manage and superintend the policies of the Service, on matters relating to the administration of the revenue assessment, collection and accounting system under this Act or any enactment or law;

(iii) Review and approve the strategic plans of the Service;

(iv) Employ and determine, the terms and conditions of service including, disciplinary measures of the employees of the Service;

(v) Stipulate remuneration, allowances, benefits and pensions of staff and employees in consultation with the National Salaries, Income and Wages Commission; and

(vi) Do such other things, which in its opinion, are necessary to ensure the efficient performance of the functions of the Service under the Act.

(b) Functions of the Federal Inland Revenue Service

Section 8 (1) of the FIRS (Establishment) Act 2007 provides that the FIRS shall:

(i) Assess persons including companies, enterprises chargeable with tax;

(ii) Assess, collect, account and enforce payment of taxes as may be due to the Government or any of its agencies;

(iii) Collect, recover and pay to the designated account any tax under provision of the Act;

(iv) In collaboration with the relevant ministries and agencies, review regimes and promote the application of tax revenues to stimulate economic and development;

(v) In collaboration with the relevant tax enforcement agencies, carry examination and investigation with a view to enforcing compliance with provisions of this Act;

(vi) Make, from time to time, a determination of the extent of financial and such other losses by government arising from tax fraud or evasion and losses (or revenue forgone) arising from tax waivers and other related matters;

(vii) Adopt measures to identify, trace, freeze, confiscate or seize proceeds derived from tax fraud or evasion;

(viii) Adopt measures which include compliance and regulatory actions, introduction and maintenance of investigative and control techniques on detection and prevention of non-compliance;

(ix) Collaborate and facilitate rapid exchange of information with relevant national or international agencies or bodies on tax matters;

(x) Undertake exchange of personnel or other experts with complimentary agencies for purposes of comparative experience and capacity building;

(xi) Establish and maintain a system for monitoring international dynamics of taxation in order to identify suspicious transactions and the perpetrators and other persons involved;

(xii) Provide and maintain access up to date and adequate data and information on all taxable persons, individuals, corporate bodies or all agencies of government involved in the collection of revenue for the purpose of efficient, effective and correct tax administration and to prevent tax evasion and fraud;

(xiii) Maintain database, statistics, records and reports on persons, organisations, proceeds, properties, documents or other items or assets relating to tax administration including matters relating to waivers, fraud or evasion;

(xiv) Undertake and support research on similar measures with a view to stimulating economic development and determine the manifestation, extent, magnitude and effects of tax fraud, evasion and other matters that affect effective tax administration and make recommendations to the government on appropriate intervention and preventive measures;

(xv) Collate and continually review all policies of the Federal Government relating to taxation and revenue generation and undertake a systematic and progressive implementation of such policies;

(xvi) Liaise with the office of the Attorney-General of the Federation, all government security and law enforcement agencies and such other financial supervisory institutions in the enforcement and eradication of tax related offences;

(xvii) Issue taxpayer identification number to every taxable person in Nigeria in collaboration with State Internal Revenue Service and Local Government Councils;

(xviii) Carry out and sustain rigorous public awareness and enlightenment campaign on the benefits of tax compliance within and outside Nigeria;

(xix) Carry out oversight functions over all taxes and levies accruable to the Government of the Federation and as it may be required, query, subpoena, sanction and reward any activities pertaining to the assessment, collection of and accounting for revenues accruable to the Federation; and

(xx) Carry out such other activities as are necessary or expedient for the full discharge of all or any of the functions under this Act.

(c) Taxes that are collectible by the Federal Inland Revenue Service (FIRS)

(i) Companies Income Tax;

(ii) Withholding Tax on Companies and non-resident individuals;

(iii) Petroleum Profits Tax (now Hydrocarbon tax);

(iv) Value Added Tax;

(v) Education Tax;

(vi) Capital Gains Tax on Companies and non-resident individuals;

(x) Stamp Duties on Corporate bodies; and

(xi) Personal Income Tax on:
- * Members of the Armed Forces of the Federation of Nigeria;
- * Members of the Nigeria Police Force; and
- * Staff of the Ministry of External Affairs (or Foreign Affairs) and non-resident individuals.

QUESTION 6

Mr. Orubulolo is an employee of a Ceramic company based in Are township of Ekiti State. He was on a gross salary of ₦2.4m per annum in 2019. Other income received net of Withholding Tax of ₦1,500,412 is ₦18,498,708.

The total contributory pension in the year credited to Mr. Orubulolo's account is ₦360,000 of which he contributed 8% as employee while his employer contributed 10%.

Required:

Compute Orubulolo's income tax payable for the 2019 year of assessment, under the following scenarios:

(i) Without pension; and (7½ Marks)

(ii) With pension (7½ Marks)

(Total 15 marks)

SOLUTION TO QUESTION 6

MR ORUBULOLO

TAX LIABILITY:

1	**WITHOUT PENSION**		₦
	PAYE payable	See below	4,038,873.15
	Less; WHT credit		(1,500,412)
	Net tax liability		**2,538,461.15**
2	**WITH PENSION**		
	PAYE payable	See below	4,008,537.15
	Less; WHT credit		(1,500,412)
	Net tax liability		**2,508,125.15**

S/N		1 **WITHOUT PENSION**		**2 WITH PENSION**	
		₦	₦	₦	₦
Total earning in the year (WN2)			**22,399,120**		**22,399,120**
Less: Employee Pension Contribution			(-)		(160,000) WN1
Total Earning less Employee Contribution	(a)		22,399,120		22,239,120
CFR:					
20% of gross income (i.e. 0.2 x a) plus			4,479,824		4,447,824
Higher of 1% or N200,000			1% of N22,399,120		1% of N22,239,120
			--		--
					222,391.20
			223,991.20		4,670,215.20
			4,703,815.20		
Pension WN1			0		160,000

Total relief	**b**	4,703,815.20	4,830,215.20
Taxable income	**c = (a-b)**	**17,695,304.80**	**17,568,904.80**
Tax Liability;			
7% on N300,000		21,000	21,000
11% on N300,000		33,000	33,000
15% on N500,000		75,000	75,000
19% on N500,000		95,000	95,000
21% on above N1.6m		336,000	336,000
24% on above N3.2m		3,478,873	3,448,537
Tax liability per year		**4,038,873.15**	**4,008,537.15**

Workings;
(1)

PENSION:	N360,000	₦
Employee 8%	8/18 x 360,000	**160,000**
Employer 10 %	10/18 x 360,000	200,000

(2) Total income in the year

	₦	₦	
1. Gross salary received			2,400,000
2. Gross income from other sources:			
(a) Net income from other sources	18,498,708		
Add back: (b) Withholding Tax charged	1,500,412		
Gross income from all sources		19,999,120	
		22,399,120	

QUESTION 7

(a) What do you understand by a "statute of limitation" in the Nigerian Tax System? (5 marks)

(b) One main guiding principle regarding "treatment of the gains" from disposal of asset(s) is the "purpose for which such asset is bought and/or sold" (that is, either for business use or as an investment for gains or profit).

In line with the above, how would you treat a motor vehicle bought for ₦9million and disposed for ₦12.32million by MPOPSON ventures under two independent situations as stated below:

a. Where the motor vehicle was purchased and used purposely for the business. (5 marks)

b. Where the motor vehicle is a stock-in-trade of the business (that is, motor vehicles are bought and sold regularly for gains or profit). (5 marks)

(Total 15 Marks)

SOLUTION TO QUESTION 7

(a) "Statutes of limitations in the Nigerian Tax System are provisions which set the maximum time after an event within which legal proceeding may be initiated.
In the Nigerian system, the statute of limitations refers to the maximum period after which the Relevant Tax Authority (RTA) can assess a taxable person to tax in respect of a certain year of assessment. Nigerian tax legislation provides that RTA'S only have six (6) years after the relevant accounting period to assess a taxable person to additional tax.

However, the above tax laws further provide that; where any form of fraud, wilful default or neglect has been committed in connection with any tax imposed by the Acts, the six-year limitation would not apply and an investigation may be instituted by the RTA. This creates ambiguity implying that the RTA can go as far back as they want to review, assess, and collect tax from taxpayer.

Recently however, Tax Appeal Tribunal (20/8/2015) sitting in Enugu, held that a taxpayer may not be liable to (including interest and penalties) based on assessments **arising after the expiration of six years statutory period** for tax audits. Non-compliance with this time limit could render the assessment and accompanying interest and penalty unenforceable. (5 marks)

MPOPSON Ventures under two independent situations

(b) (1) the tax treatment of capital or amount received on disposal and the Gains M/V purchased for Biz use

	₦
Proceed (Capt. Receipt)	12,320,000
Less:	
Cost of M/V	(9,000,000)
Gain (Capital Receipt)	3,320,000
WN1	
CGT @10%	332,000

(i) M/V purchased as a stock-in-trade

	₦	
Proceed (Rev Receipt)	12,320,000	
Less:		
Cost of M/V		(9,000,000)
Gain (Rev Receipt)		3,320,000
WN2 (i.e. Profit on Disposal)		
CGT @10%:	not applicable	

Working note

(1) Where the motor vehicle was purchased and "used purposely for the business",

- The proceeds /amount received from sale of asset would be regarded as a Capital Receipt i.e. a one off or not a regular income and therefore;
- Capital Gain of N3,232,000 shall be taxed @ 10% under CGT Act Cap CI LFN 2004 as amended.

(2) Where the motor vehicle is a "stock-in-trade of the business" that is, Motor vehicles are bought and sold regularly for gains or profit then,
  (a) the proceeds/amount received on sale would be regarded as a Revenue receipt (normal income received from the business).

The gains ₦3,232,000 would be regarded as a profit or on disposal and treated under PITA P8 (as amended) or CITA CAP 12 LFN 2004 (as amended) for corporate business.

THE CHARTERED INSTITUTE OF TAXATION OF NIGERIA

OCTOBER 2023: PROFESSIONAL EXAMINATION

PTE I: FINANCIAL REPORTING

ATTEMPT QUESTION ONE AND ANY OTHER FOUR QUESTIONS.

TIME: 3 HOURS

QUESTION 1

The following information relates to the financial statements of Wole-Wole Ltd, a manufacturing company, which were submitted to the MSTO as part of the annual tax returns:

Statement of financial position as at 31 December

	2022	**2021**
Assets	**₦'000**	**₦'000**
Non-Current Assets:		
Property, plant & equipment	22,325	14,095
Current assets:		
Inventories	5,860	5,010
Trade & other receivables	11,305	8,285
Cash & cash equivalents	1,930	15
	19,095	13,310
Total Assets	41,420	27,405
Equity and Liabilities:		
Ordinary share capital	2,610	1,770
Preference share capital (Irredemable 8%)	750	750
Revaluation surplus	9,285	--
Retained earnings	10,420	10,470
Equity:	23,065	12,990
Non-Current Liabilities:		
Borrowings	525	--
Current liabilities:		
Trade and other payables	9,705	8,190
Taxation	915	310
Bank overdraft	7,210	5,915
	17,830	14,415
Total equity and liabilities	41,420	27,405

Wole-Wole Ltd
Statement of profit or loss and other comprehensive income for year ended 31 December

	2022	2021
	₦'000	₦'000
Revenue	121,335	109,790
Cost of sales	(104,675)	(96,310)
Gross profit	16,660	13,480
Net operating expenses	(13,020)	(10,135)
Profit from operations	3,640	3,345
Net finance cost	(335)	(280)
Profit before taxation	3,305	3,065
Taxation	(1,015)	(815)
Profit for the year	2,290	2,250
Other comprehensive income:		
Revaluation of property, plant & equipt	9,285	--
Total comprehensive income	11,575	2,250

Additional information:
The following additional information were obtained from the notes to the financial statements of the company and information from the taxpayers file.

(i) Reconciliation of profit before tax to cash generated from operations

	2022
	₦'000
Profit before taxation	3,305
Depreciation charged for the year	4,825
Profit on disposal of PPE	(70)
Finance cost	335
Increase in inventories	(850)
Increase in trade and other receivables	(3,020)
Increase in trade and other payable	1,515
Net cash flow generated from operations	6,040

(ii) During the year the company disposed off part of its PPE with sales proceed of ₦3,350,000 and made a profit of ₦70,000.

(iii) Key ratios computed from the financial statements of the company are as follows:

	2022	2021
Gross profit margin	13.7%	12.3%
Net margin	1.9%	2.0%
Net assets turnover	5.3 times	8.5 times
Trade receivable collection period	34 days	28 days
Interest cover	10.9 times	11.9 times
Current ratios	1.1	0.9
Quick ratios	0.7	0.6

(iv) During the year Wole-Wole Ltd paid dividend of ₦2,280,000 to its ordinary shareholders.

You are required to prepare:

(a) Statement of changes in equity of Wole-Wole Ltd for the year ended December 31, 2022. (10 marks)

(b) Statement of cashflows for the year ended December 31, 2022. (18 marks)

(c) Draft a report on the profitability, efficiency and liquidity position of the company, and conclude on the tax relevance of your report. (12 marks)

(Total 40 marks)

SOLUTION TO QUESTION 1

(a) **Wole-Wole Ltd**

Statement of changes in equity for year ended 31 December 2022

	Ord. Share Capital	**Irredemable Preference Share**	**Revaluation Reserve**	**Retained Earnings**	**Total**
	N'000	**N'000**	**N'000**	**N'000**	**N'000**
Bal. F/Fwd	1,770	750	--	10,470	12,990
Total Comprehensive Income:					
Profit for the year	--	--	--	2,290	2,290
Revaluation surplus	--	--	9,285	--	9,285
Transaction with owners in capacity as owners:					
Issue of ord. shares	840	--	--	--	840
Dividend paid (Ord. shares)				(2,280)	(2,280)
Dividend paid (irredeem. per shares):					
(750 x 0.8)	--	--	--	(60)	(60)
Bal. as at 31 Dec. 2022	2,610	750	9,285	10,420	23,065

(b) **Statement of cashflows for the year ended December 31, 2022**

Operating activities:	**N'000**
Net cash flow generated from operations	6,040
Interest paid	(335)
Tax paid (w1)	(410)
Net cash from operating activities	5,295
Cash flow from investing activities:	
Purchase of non-current asset (w2)	(7,050)
Proceed on sale of PPE	3,350
	(3,700)
Cash flows from financing activities:	
Proceed from borrowings (525 – 0)	525

Dividend paid	(2,280)
Irredeemable dividend on pref. shares	(60)
Issue of ordinary shares	840
	(975)
Net change in cash and cash equivalent	620
Cash and cash equivalent @ beginning (15 – 5,915)	(5,900)
Cash and cash equivalent @ year end (1,930 – 7,210)	(5,280)

Workings:

(w1)	**Tax paid**	
		N'000
	Bal. B/d	310
	Add: Charged to P or L	1,015
		1,325
	Less: Bal. C/fwd	(915)
		410
(w2)	**Purchases of non-curent assets**	**N'000**
	Bal. C/Fwd	22,325
	Carry amount of PPE disposed (3,350 – 70)	3,280
	Depreciation charged in the year	4,825
		30,430
	Less: Revaluation reserve	(9,285)
	Balance B/Fwd	(14,095)
	Non-current asset purchased in the year	7,050

(c) Report on Wole-Wole Ltd is profitability, efficiency and liquidity position and their tax relevance

Profitability

The company experienced marginal increase in its gross margin which shows certain level of stability in its primary business involvement. It however did not lead to direct impact on its net margin which reduced, albeit, marginally too. The slight reduction was occassioned by increase in the company's operating expenses in the 2022 accounting year which also translated into similar impact on the interest cover for the current year.

Efficiency

There was a decline in trade receivables collection period. It implies the company has failed to improve on its efficiency in managing this asset. The reduced asset turnover from the previous year to the current year is also a demonstration of the likely challenged efficiency to which assets are put to use.

The above pictures show reduced profitability of Wole-Wole Ltd in its latest year from the previous year. An improvement on its asset management efficiency in the future will contribute to improved profitability.

Liquidity
Both the current ratio and the acid-test ratio revealed an improved position on the ability of the company to meet its liquidity obligations as they fall due irrespective of whether it needs to realise its inventories or not before such settlement. There are current and liquid assets enough to cover current liabilities that exist.
This shows a comfortable liquidity position of the company in meeting maturing short term obligations.

Conclusion on Tax Relevance
The company is profitble and would likely continue to remain profitable and thus, a going concern to remain in business.

Improvement on its asset management will translate to improved profit for tax purposes.

The company has current or liquid resources to service its current obligations and thus, its tax obligations.

QUESTION 2

(a) EPS is regarded as a very important measure of a company's performance; such that IAS 33 was issued by IASB on its measurement and presentation whereas there are no regulations about the calculations of the other accounting ratios.

Required:
Explain why EPS is regarded as important in the measurement of a company's performance. (2 marks)

b. (i) Osakuni Plc has EPS of ₦0.26 in the year ended March 31, 2022. The company has in issue 400,000,000 ordinary shares of ₦0.50 per share during the year ended March 31, 2022. In the year ended March 31, 2023 Osakuni issued 250,000,000 bonus shares. The profit after tax for the year ended March 31, 2023 was ₦130,000,000.

Required:
Calculate the EPS for the year ended March 31, 2023 and the restated EPS for 2022 that will be included in 2023 financial statements. (5 marks)

(ii) Sasu PLC has 125,000,000 ordinary shares of ₦0.50 per share in issue throughout the year ended March 31, 2023. The profit after tax for the period was ₦800,000,000. The entity has two convertible instruments in issue:

- ₦125,000,000 10% loan notes, each ₦1,000 of the loan notes is having the right to convert into 1,000 ordinary shares
- 100,000,000 convertible preference shares of ₦1 each. Dividend payable on each preference share is ₦0.10. Two preference shares are to be converted to one ordinary share. The income tax rate is 30%

Required:
Calculate the basic and the diluted EPS for Sasu Plc. (8 marks)

(Total 15 marks)

SOLUTION TO QUESTION 2

(a) Importance of EPS

- Earnings per share is one of the component parts of price earnings ratio which is used by investors to evaluate the relative riskiness of investment, hence it may help them to choose the most suitable investment option.

- EPS can be used to compare the financial standing of a company over the years. A steady increase in EPS may signify a reliable investment option.

(b) Calculation of EPS

i. Osakuni PLC basic earnings per share

Profit after tax	₦130,000,000
Number of shares in issue:	
At April 1, 2022	400,000,000
Bonus issue	250,000,000
Number of shares ranking for dividends in 2023	650,000,000
Basic EPS ₦130,000,000/650,000,000	₦0.20
Restated EPS for 2022 ₦0.26 x 400/650	₦0.16

ii. Sasu PLC

Calculation of basic EPS

Profit after tax		₦800,000,000
Number of shares ranking for dividends		125,000,000
Basic EPS ₦800/125		₦6.40
Calculation of diluted EPS:		
Profit (working 1)		818,750,000
Number of shares for diluted EPS (working 2)		575,000,000
Diluted EPS = ₦818.75m/ 300m shares		₦2.73
Calculation of profits for diluted EPS:		
	₦	₦
Profit for basic EPS		800,000,000
Savings on 10% loan notes= 10% x ₦125m	12,500,000	
Tax on savings =30% x ₦12.5m	(3,750,000)	8,750,000
Savings on preference dividends ₦0.10 x 100m		10,000,000
		818,750,000
Number of shares for calculating diluted EPS		
Shares for basic EPS		125,000,000

Conversion of loan notes = ₦125m x 1000/1000	125,000,000
Conversion of preference shares 100m x1/2	50,000,000
	300,000,000

QUESTION 3

Babe Ltd began trading 1 January 2019, preparing financial statements to December 31 each year. During 2022, the company decided to change its accounting policy with regards to the depreciation of property, plant and equipment (PPE). Depreciation charges calculated using the previous accounting policy as shown in the company's financial statements for the first three years are as follows:

	₦'000
Year to 31 December 2019	1,380
Year to 31 December 2020	1,620
Year to 31 December 2021	1,740

If the new policy had been applied in previous years, depreciation charges would have been:

	₦'000
Year to 31 December 2019	2,340
Year to 31 December 2020	1,860
Year to 31 December 2021	1,380

An extract from the company's statement of comprehensive income for the year to December 31, 2022 (before adjusting comparative figures to reflect the change in accounting policy) shows the following:

	2022	**2021**
	₦'000	**₦'000**
Profit before depreciation	15,060	14,700
Depreciation of property, plant & equipment	(1,140)	(1,740)
Profit before taxation	13,920	12,960
Taxation	(4,176)	(3,888)
Profit after taxation	9,744	9,072

Retained earnings were reported as ₦17,658,000 on December 31, 2020. No dividend has been paid in any year. It may be assumed that the company's tax is always equal to 30% of the profit before taxation.

Required:

(a) Rewrite the extract from the statement of comprehensive income so as to reflect the change in accounting policy, in accordance with the requirements of IAS 8. (7½ marks)

(b) Compute the company's retained earnings at December 31, 2022 and the restated retained earnings at December 31, 2020 and 2021. (7½ marks)

(Total 15 Marks)

SOLUTION TO QUESTION THREE

(a) Babe Ltd

Rewrite of extract from the Statement of Comprehensive Income:

2022 2021

	₦'000	₦'000
Profit before depreciation	15,060	14,700
Depreciation on PPE	(1,140)	(1,380)
Profit before taxation	13,920	13,320
Taxation	(4,176)	(3,996)
Profit after taxation	9,744	9,324

(b) Computation of the company's earnings for 2022

	₦'000
Balance at 31 December 2022 as previously reported	17,658
Change in accounting policy relating to depreciation	(840)
Restated balance at 31 December 2020	16,818
Restated profit for the year to 31 December 2021	9,324
Restated balance at 31 December 2021	26,142
Profit for the year to 31 December 2022	9,744
Balance at 31 December 2022	35,886

Note:

(i) This is a case of change in accounting policy and it will be accounted for retrospectively.

(ii) The change in accounting policy results in depreciation of ₦960,000 in 2019 and ₦240,000 in 2020. The total is ₦1,200,000. Tax saved at 30% is ₦360,000. Therefore, profit after tax for the two years falls by ₦840,000.

(iii) Comparing the new accounting policy and old accounting policy, it can be observed that in 2019 and 2020, there is an increase in depreciation charge (2019 - ₦960,000, 2020 - ₦240,000) while in 2021 is a decrease in depreciation (2021- ₦360,000).

QUESTION 4

The statements of financial position of Krapeh and Joko both public companies, as at December 31, 2022 are presented below.

	Krapeh	Joko
	₦'m	₦'m
Assets		
Non-current assets:		
Property, plant and equipment	7,900	3334
Investment in Joko	3,740	--
	11,640	3,334

Current assets	3,550	1,327
	15,190	4,661
Equity and liabilities		
Equity:		
Ordinary share capital of ₦1 each	5,700	2,100
Retained earnings	5,490	2,000
	11,190	4,100
Non-current liabilities:		
Loan notes	1700	--
Current liabilities:		
Trade payables	1,300	561
Other payables	1,000	--
	2,300	561
	15,190	4,661

Additional information

(i) Krapeh acquired 80% of the share capital of Joko on January 1, 2020 for ₦3.74 billion when the retained earnings of Joko were ₦1.2billion. There had been no issue of shares since the date of acquisition of Joko.

(ii) At the date of acquisition, the fair value of the net assets of Joko was the same as their book value with the exception of property that has a fair value of ₦480 million higher than their book value. The property had an estimated useful life of 10 years from the date of acquisition.

(iii) Non-controlling interest was measured at its fair value of ₦540million at the acquisition date. The group policy is to measure the non-controlling interests at fair value at the date of acquisition.

(iv) Krapeh purchased goods from Joko for ₦350m, at a margin of 20%, during the year ended December 31, 2022, 25% of these items remains in Krapeh's inventories at the reporting date.

(v) There had been no impairment of goodwill since acquisition of Joko.

Required

Prepare the consolidated statement of financial position of Krapeh Group as at December 31, 2022. **(15 marks)**

SOLUTION TO QUESTION 4

Krapeh Group

Consolidated statement of financial position for the year ended December 31,2022

	₦'m
Assets	
Non-current assets:	
Goodwill(w2)	500
Property, plant and equipment 7,900 +3,334 +336(w1)	11,570

	12,070
Current assets 3,550 +1,372 -14 (w5)	4,863
Total assets	16,933
Equity and liabilities	
Equity:	
Ordinary shares	5,700
Retained earnings (w4)	6,004
	11,704
Non-controlling interests	668
	12,582

Non-current liabilities	
Loan notes	1700
Current liabilities:	
Trade payables	1,861
Other payables	1,000
	2,861
Total equity and liabilities	16,933

Workings

1 Net assets of Joko at:

	Reporting date	Acquisition date	Post-acquisition
	₦m	₦m	₦m
Ordinary share capital	2,100	2,100	--
Retained earnings	2,000	1,200	800
Fair value increase on PPE	336	480	(144)
Unrealised profits	(14)	--	(14)
Total	4,422	3,780	642

1. Goodwill

	₦m
Purchase consideration	3,740
Fair value of non-controlling interests	540
	4,280
Fair value of net assets at acquisition date	(3,780)
Goodwill consolidated	500

2. Non-controlling interests

	₦m
Fair value at acquisition date	540
Share of post-acquisition retained earnings of Joko 20% x 642	128
	668

3. Group retained earnings

	₦m
Parent	5,490
Share of post-acquisition retained earnings of Joko 80% x 642	514
	6,004

4. Unrealised profit = 25% x 20% x ₦350m = ₦14m

QUESTION 5

(a) Explain the five (5) main elements of financial statements in accordance with IASB's Conceptual Framework. **(5 marks)**

(b) Identify any five (5) user groups of financial statements and explain what information they are likely to be interested in. **(10 marks)**

(Total 15 marks)

SOLUTION TO QUESTION 5

(a) The main elements of financial statements include the following:
(i) Assets
(ii) Liabilities
(iii) Equity
(iv) Income (Revenue/Gains)
(v) Expenses (Losses)

Assets
An asset is a present economic resources controlled by the entity as a result of past events. An economic resources is a right that has the potential to produce economic benefits. Examples include current and non-current assets.

Liabilities
A liability is a present obligation of the entity to transfer an economic resources as a result of past event.

For liabilities to exists three criteria must all be satisfied, these are:
- The entity has obligation;
- The obligation is to transfer an economic resources; and
- The obligation is a present obligation that exists as a result of past events.

Equity
Equity is the residual interest in an entity after the value of all its liability has been deducted from the value of all its assets.

Income
Income is increase in assets or decrease in liabilities that results in increase in equity, other than those relating to contribution from holders of equity claims e.g. revenue and gains.

Expenses
Expenses arising in the normal course of activities, such as cost of sales, other operating costs, including depreciation of non-current assets. Expenses results in outflow of assets or depletion of assets.

(b) The people who might be interested in financial information about a company may be classified as follows:

(i) **Shareholders in the company:** They will be interested in the company's profitability and its ability to pay dividends. They will also be interested in the company's long term prospects.

(ii) **Management of the company:** Those are people appointed by the company's owners to supervise the day-to-day activities of the company. They need information about the company's financial situation as it is currently and as it is expected to be in future. This is to enable them manage the efficiently and to take effective control.

(iii) **Debtors, creditors & suppliers:** Suppliers provide goods to the company on credit and customers who purchase the goods and services provided by the company. Suppliers will want to know about the compay's ability to pay its debts; customer needs to know that the company is a secure sources of supply and is in no danger of having to close down.

(iv) **Government/Tax Authorities**
Government will want to know about a business profits in order to assess the tax payable by the company on its profits and any sales taxes.

(v) **Providers of finance to the company**
These might include a bank which permits the company to operates an overdraft or provides longer-term finance by granting a loan. The bank will want to ensure that company is able to keep up with principal and interest payments.

(vi) **Employees of the company**
These should have a right to information about the company's financial position because their future careers and the size of their wages and salaries depends on it.

QUESTION 6

Your company, Steady Plc, is in the process of drafting the annual report for the year ended December 31, 2022. The company is in the process of preparing a note on taxation to be incorporated to the financial statements. Your boss has asked you to prepare the note and the following information is available to you.

(i) The deferred taxation account had a credit balance of ₦6.2m at December 31, 2021. This amount arose in respect of the difference between depreciation and capital allowances. During the year ended December 31, 2022, the company charged ₦74.4m in depreciation and claimed ₦86m capital allowances.

(ii) At December 31, 2021 the company had a liability for tax of ₦64m. The tax charged for the year ended December 31, 2021 was underestimated by ₦7m. The profit before tax for the year ended December 31, 2022 is ₦987m.

(iii) Other than depreciation and capital allowances, the other inadmissible deduction that is included in the profit figure is a fine of ₦63m paid.

The tax rate is at 30%.

Required

(a) Explain the accounting requirements of deferred tax in IAS 12 -Income Taxes **(5 marks)**

(b) Determine the income tax expense for the year ended December 31, 2022. **(6 marks)**

(c) Prepare a note to the financial statement in respect of deferred tax, in accordance with the requirement of IAS 12. **(4 marks)**

(Approximate your figures to the nearest ₦'000)

(Total 15 marks)

SOLUTION TO QUESTION 6

(a)

- IAS 12 Income Taxes requires that a deferred tax liability should be made for all taxable temporary differences. A deferred tax asset must be recognised to the extent that it is probable that taxable profits would be available in future against which it will be recovered.

- The tax rate that should be used to calculate the deferred tax balance should be the tax rate that is expected to apply to the period when the asset is realised, or the liability is settled; this is often the current tax rate.

- Deferred that provisions are required to be shown as non-current liability while deferred tax assets are shown as non-current asset in the statement of financial position.

- IAS 12 does not permit the discounting of deferred tax neither does it permit offsetting deferred tax assets against deferred tax liability.

- An increase in deferred tax liability is added to the current tax while a reduction is deducted to arrive at the income tax expense in the statement of profit or loss.

b. Statement of profit or loss for the year December 31, 2022

Calculation of income tax expense

	₦'000
Income tax charge for the current year (Wk1)	311,520
Increase in deferred tax w2	3,480
Under estimate of tax in prior year	7,000
Income tax expense	322,000

Wk 1: Calculation of tax charged on profit for the year

	₦'000
Profit before tax	987,000
Add back depreciation	74,400
Fine paid	63,000
	1,124.400
Deduct capital allowances	(86,000)
Assessable profit	1,038,400
Income tax charged is at 30%	311,520

c. Note on deferred tax

	₦'000
Balance at January 1,2022	6,200
Increase in the year	3,480
Balance at December 31,2022	9,680

Working on increase in provision for deferred tax

	₦'000
Capital allowances	86,000
Depreciation	(74,400)
	11,600
Tax rate at 30%	3,480

QUESTION 7

(a) Financial Instruments should be properly classified by ensuring appropriate and consistent reporting. This classification is made at the time the financial instrument is issued and not changed subsequently.

Required:

Explain the following classes of financial instruments, giving example of each:

(i) Financial assets
(ii) Financial liabilities
(iii) Equity

(6 marks)

(b) (i) Explain how entities classify convertible instrument and why it is important to distinguish between debt and equity in their financial statements. **(4 marks)**

(ii) Karimistic Ltd issues a convertible bond for of ₦10,000,000. The bond is convertible into equity shares of the issuer at the discretion of the holder at any time in the next 10 years. The bond can be converted into a variable number of shares equal to the value of the liability.

Karimistic Ltd also issues ₦7,000,000 of 8% convertible redeemable preference shares. In 5 years time the preference shares will either be redeemed or converted into 5,000,000 equity share of the issuer, at the option of either the holder or issuer.

Required:
How should Karimistic Ltd account for the instrument according to IAS 32. **(5 marks)**
(Total 15 marks)

SOLUTION TO QUESTION 7

(a) (i) A financial asset is any asset that is:
- Cash
- An equity instrument of another entity.
- A contractual right to receive cash or another financial assets from another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity.
- A contract that will or may be settled in the entity's own equity instrument, subject to some conditions.

Examples are: Trade receivables, investment in ordinary shares of another entity loans and advances granted to customers.

(ii) A financial liability is any liability that is;
- A contractual obligation to deliver cash or another financial assets of another entity.
- A contractual obligation to exchange financial instrument with another entity under conditions that are potentially unfavourable.
- A contract that will or may be settled in the entity's own equity instruments subject to certain conditions.

Example are: Trade payables, debentures, loan notes, bank loan received.

(iii) An equity instrument is any contractual that evidences as residual interest in the assets of an entity after deducting all of its liabilities.

Examples: A company own shares, share options, irredemable preference shares.

(b) (i) The issuer of a financial instrument shall classify the instrument as liability or equity in accordance with the substance (not necessary its legal form) of the contractual arrangement and the definitions of a financial liability and an equity instrument.

The critical features in differentiating liability from equity is the existence of contractual obligation on the issuer either:

- To deliver cash or another financial assets to the holder or
- To exchange another financial instrument with the holder under conditions which are potentially unfavourable the issuer.

The distinction between the two elements is important to ensure that an entity correctly reflects the current level of gearing in the financial statements as reflected by the level of the debts relative to the level of equity (capital and reserves). This is important for lenders and other investors in making future lending and/or investment decisions.

(ii) Convertible bonds of N10,000,000:

- The convertible bond is not a compound financial instrument as it is not settled in a fixed amount of shares. Therefore it should be classified as a liability.

- **Convertible redeemable preference shares** are compound instruments. They have financial liability component as there is an obligation to deliver cash through dividends and on redemption in five years time to deliver either cash or equity instrument (through the holders right to convert into equity).