

# CAA

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ACCOUNTANTS  
ACADEMY



# ICAZ CPD- Indigenisation Accounting

Written and Presented by  
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# Commissioner Anesu Daka CA(SA) CC (T.I)

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- Entrepreneur, Founder & Managing Director of CAA
- Trained Facilitator of Learning
- Passionate Academic & Lecturer for Financial Accounting for ZCTA, QE1 and QEII and ACCA;
- Former IFRS specialist and L&D manager for Ernst & Young Zimbabwe.
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- Technical director for ICAZ
- Commissioner of enquiry in the conversion of pension funds from Z\$ to US\$.



# MENU

Analysis of Indigenisation transactions:

**Other Empowerment transactions:**

- Community ownership trusts
- Compliance Costs- the implications



# MENU

Analysis of Indigenisation transactions:

## **Equity Related Transactions:**

- Direct acquisition of shares/vendor financing by:
  - ✓ sacrificing of dividends for a period, and
  - ✓ loans/ For value
- Employee ownership:
  - ✓ Share based payments
  - ✓ Employee ownership

**NB: Concept of Control – IFRS 10**



# MENU

Analysis of Indigenisation transactions:

## **Accounting by the:**

- Issuing entity (indigenising entity)/foreign owned
- Indigenous/ Empowerment Entity/Receiving Entity



# Purpose of GPFS

OB2 The objective of general purpose financial reporting<sup>1</sup> is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. Those decisions involve buying, selling or holding equity and debt instruments, and providing or settling loans and other forms of credit.



# Choice of accounting policies

- IAS 8 guides on choice of accounting policies:
  - If transaction is covered by a standard- Apply the IFRS
  - If transaction not covered by a standard,
    - Management to apply judgment by considering:
      - i. IFRS dealing with similar issue
      - ii. Applying the Conceptual Framework
      - iii. Applying other GAAPs, e.g. the US GAAP





# MENU

Analysis of Indigenisation transactions:

**Other Empowerment transactions:**

- Community ownership trusts
- Compliance Costs



# Community Ownership Trusts



# Community Ownership Schemes

What is it?

- This involves the foreign entity either:
  - Donating into a fund that will be used to set up facilities
  - donating shares to the surrounding community
  - Or directly providing public facilities (school, vocational centers, etc.) for the benefit of the surrounding communities
  - ?





# Community Ownership Schemes

Is there a standard/IF

**Dr WHAT?**

**Is it an asset or an  
expense?**

**Cr Bank \$,**

**or**

**Cr Share Capital \$,**

**or**

**Cr Non-current assets \$**



# An Asset is

<u>Elements</u>	<u>Definition</u>	<u>Recognition Criteria</u>
<b>Asset</b> <b>4.4(a)</b>	<ol style="list-style-type: none"><li>1. A resource</li><li>2. <b>controlled</b> by an entity</li><li>3. as a result of past events and from which</li><li>4. future economic benefits are expected to flow to the entity</li></ol>	<ol style="list-style-type: none"><li>1. Future economic benefits probable</li><li>2. <b>Reliably measurable</b></li></ol>

Examples:

Cash, inventories, plant, property and equipment, **intangible asset**

**If not paid, you can lose operating licence or huge penalties**



# An Expense is

<u>Elements</u>	<u>Definition</u>	<u>Comment</u>
<b>Expenses</b>	<ol style="list-style-type: none"> <li>1. Decreases in economic benefits</li> <li>2. Not resulting from distributions to equity holders</li> </ol>	<p>Expenses include losses</p> <p>Recognition: Reliably measured</p>

Examples:

Materials and labour costs, depreciation and interest paid on loans



# Community Ownership Schemes

Is there a standard/IF

**Dr EXPENSE?**

**Is it NOT an asset or rather  
it is an EXPENSE?**

**Cr Bank \$,**

**or**

**Cr Share Capital \$,**

**or**

**Cr Non-current assets \$**





# Community Ownership Trust

- RSA Accounting Practices Board AC 503:
  - Also confirms that the DIFFERENCE between fair value given by foreign entity and the amount received for consideration **is an expense**
  - It does not qualify as an intangible asset



# Community Ownership Schemes

The Accounting dilemma

– Community Ownership

The trust has a Double Entry

**Dr Bank**

**Dr Investment in shares \$, or**

**Dr Non-current assets \$**

**Cr WHAT?**

**Is it income, liability or  
rather it is an Equity?**



# A Liability is

<u>Elements</u>	<u>Definition</u>	<u>Recognition Criteria</u>
<b>Liability</b>	<ol style="list-style-type: none"><li>1. A present obligation</li><li>2. of the entity</li><li>3. arising from past events,</li><li>4. the settlement of which is expected to result in an outflow of an entity's resources.</li></ol>	<ol style="list-style-type: none"><li>1. Future economic outflow probable</li><li>2. Reliably measurable</li></ol>

Examples:

Trade payables, unpaid taxes and outstanding loans



# Equity is

<u>Elements</u>	<u>Definition</u>	<u>Comment</u>
<b>Equity</b>	The residual interest in an entity's assets after deducting all its liabilities	Equity = ownership interest – net assets  Recognition: Reliably measurable

Examples:

Share capital, retained earnings and revaluation reserves



# Income is

<u>Elements</u>	<u>Definition</u>	<u>Comment</u>
<b>Income</b>	<ol style="list-style-type: none"> <li>Increases in economic benefits</li> <li>Not resulting from contributions made by equity holders</li> </ol>	<p>Revenue and gains</p> <p>Recognition: Reliably measurable, revenue must be earned</p>

Examples:

Revenue revaluations, profit on the sale of a non-current asset and interest received on investments, donations

# Community Ownership Schemes

The Accounting dilemma

– Foreign entity

The foreign entity has a Dilemma Country dilemma

**Dr Bank**

**Dr Investment in shares \$, or**

**Dr Non-current assets \$**

**Is it income, liability or  
rather it is an Equity?**

**Cr DONATION Income?**



# Compliance Costs



# Compliance costs

- The cost incurred in achieving compliance with the Indigenisation and Economic Empowerment Act, e.g.:
  - 10% on gross revenue empowerment levy
  - Legal costs
  - Etc.





# Compliance Costs

The Accounting dilemma

– Foreign entity

The foreign entity has a Double Entry dilemma

**Dr WHAT?**

**Cr Bank**

**\$, or**

**Is it an asset or an  
expense?**



# An Asset is

<u>Elements</u>	<u>Definition</u>	<u>Recognition Criteria</u>
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Examples:

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**If not paid, you can lose operating licence or huge penalties**



# Compliance Costs

The Accounting dilemma

– Foreign entity

The foreign entity has a Foreign Entry dilemma

It is an expense if its  
annual pmt

**Dr compliance Expense?**

**Cr Bank**

**\$, or**

**NB: if payable once after compliance + receipt of compliance certificate then it an intangible asset. IAS 38**



# Impact of Compliance Rebates

**Table 3: Rebate earnings**

	Item	Rebate Earnings
1	Indigenisation Legislation Compliance Rebates	4% – IIP Submission
		5% – IIP Approval
		10% – Full Implementation of IIP
2	Good Corporate Citizenship Rebates	Up to 30% – Socially and Economically Desirable Objectives as recommended by sector Line Ministers.
3	Indigenous Shareholding Rebates	Up to 51% in accordance to the extent of indigenous shareholding
	Maximum Possible Empowerment Levy Rebates Score	100%



# Compliance Costs

The Accounting dilemma  
– National Empowerment

The NEF has an obligation  
to pay-back rebate for  
compliance

**Dr Bank?**

<b>Cr Compliance Income</b>	<b>\$, and</b>
<b>Cr Rebate Liability (SFP)</b>	<b>\$</b>

**NB: NEF has a legal obligation to rebate those who comply based on statute-IEEA**



# MENU

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**NB: Concept of Control – IFRS 10**



# Employee Ownership

## Share-based payment- IFRS 2

Dr **Expense**

Cr Equity (if equity-settled),or

Cr SBP Liability (if cash-settled)

## Employee Ownership Trust

Treasury shares

Same as IFRS 2



# Direct Equity Transactions- 51%

## Foreign Owned Entity/shareholder

Dr Bank/Amount Receivable \$  
 Dr Expense (difference)  
 Cr Share Capital \$

Foreign owned entity

Dr Bank/Amount Receivable \$  
 Cr Investment \$  
 Foreign shareholder

## Receiving Entity

Dr investment -51% \$  
 Cr Bank/Liability \$

Are these deferred shares- not fully paid for, either guaranteed by the foreign shareholder or bought on vendor financing?- **CONTROL?**





# Does 51% shareholding control an entity?

A head-ache of the receiving entity!!!



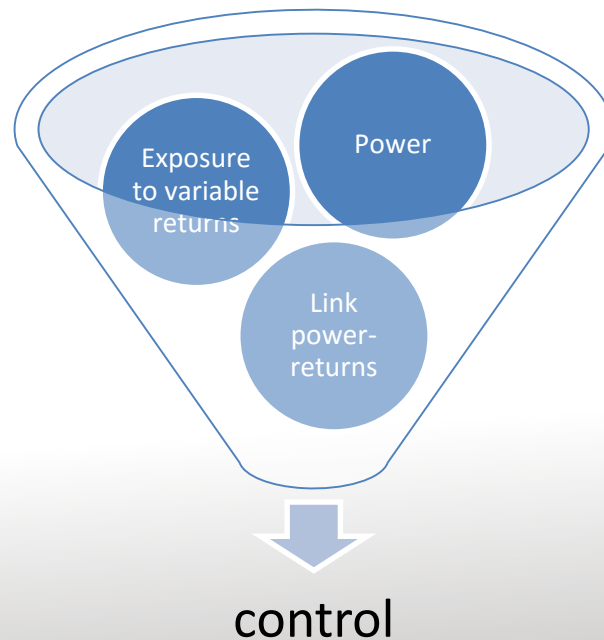
# Media Extract: “Whose line is it anyway?”

By now it is abundantly clear that the 10:10:31 indigenisation formulation does not give control to indigenous entities, rather it leaves control with the very party that must work hard to generate the revenues that can legitimately convert inert to real control.

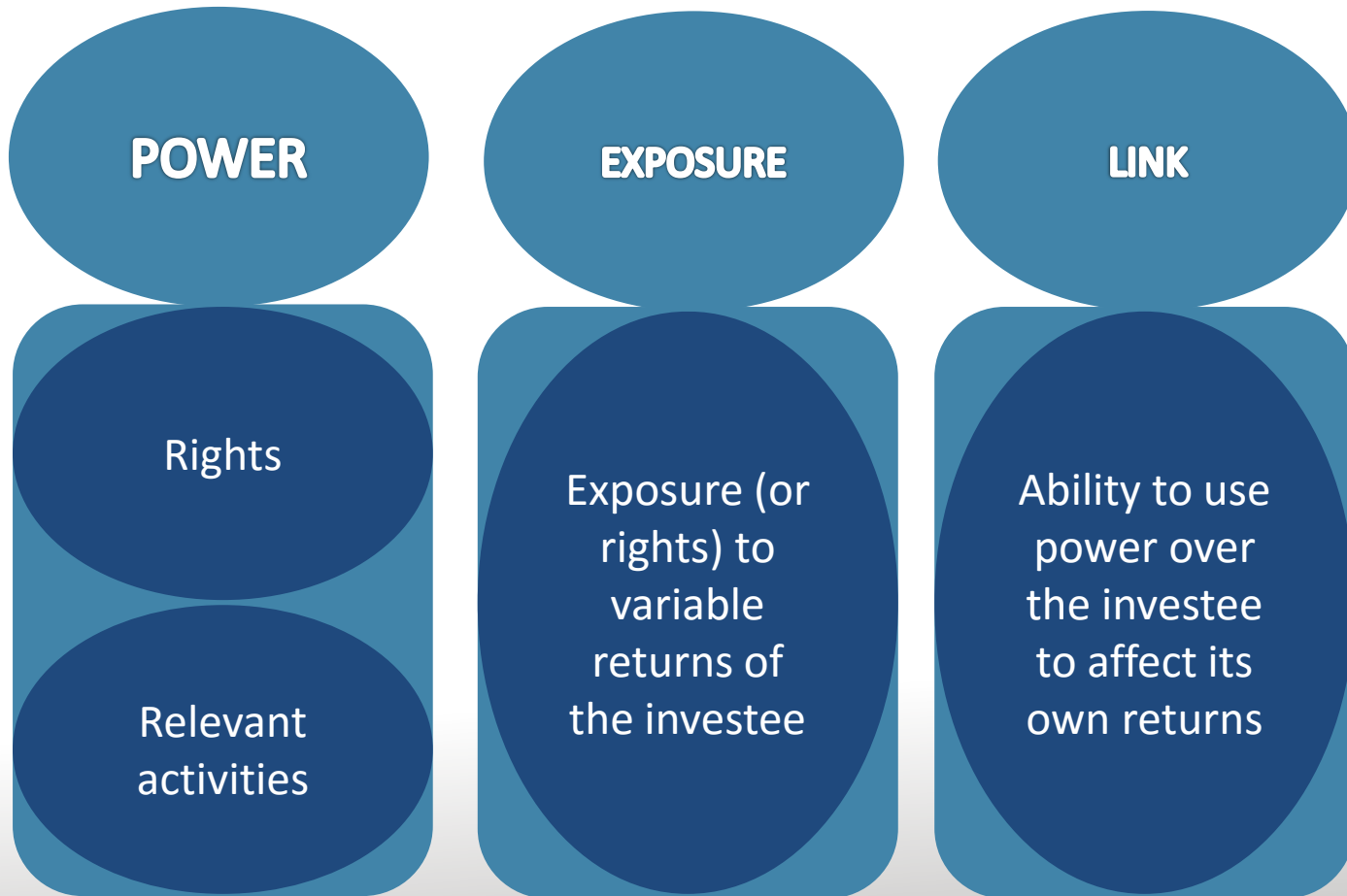


# The control model—an overview

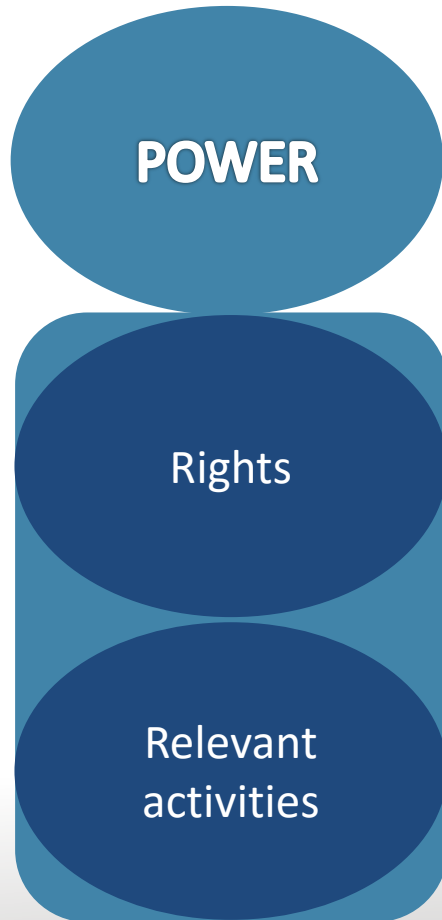
An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.



# Assessing control of an investee



# Assessing power over an investee



- Power = existing **rights** that give it the current ability to direct the **relevant activities**
- **Power** arises from **rights** (e.g voting rights, rights to appoint key personnel, among others)
- **Relevant activities:** significantly affect the investee's returns

An investor **need not have absolute power** to control an investee



# Power—the ‘ability approach’

- Power over an investee = existing rights that give it the current ability to direct the relevant activities, i.e. the activities that significantly affect the investee’s returns.
- Current ability to direct the relevant activities = investor is able to make decisions at the time that those decisions need to be taken.
  - Can have current ability even if it does not actively direct
  - An investor is not assumed to have current ability to direct simply because is actively directing activities
- Having the current ability is not limited to being able to act today.



# Power—rights

- Only substantive rights must be considered in assessing power.
- For a right to be substantive, the holder must have the practical ability to exercise that right.
- To be substantive, rights also need to be exercisable when decisions about the direction of the relevant activities need to be made.



# Power—rights

- Voting rights
- Potential voting rights
- Contractual rights
- Removal or ‘kick out’ rights
- An investor that holds **only protective** rights does not have power



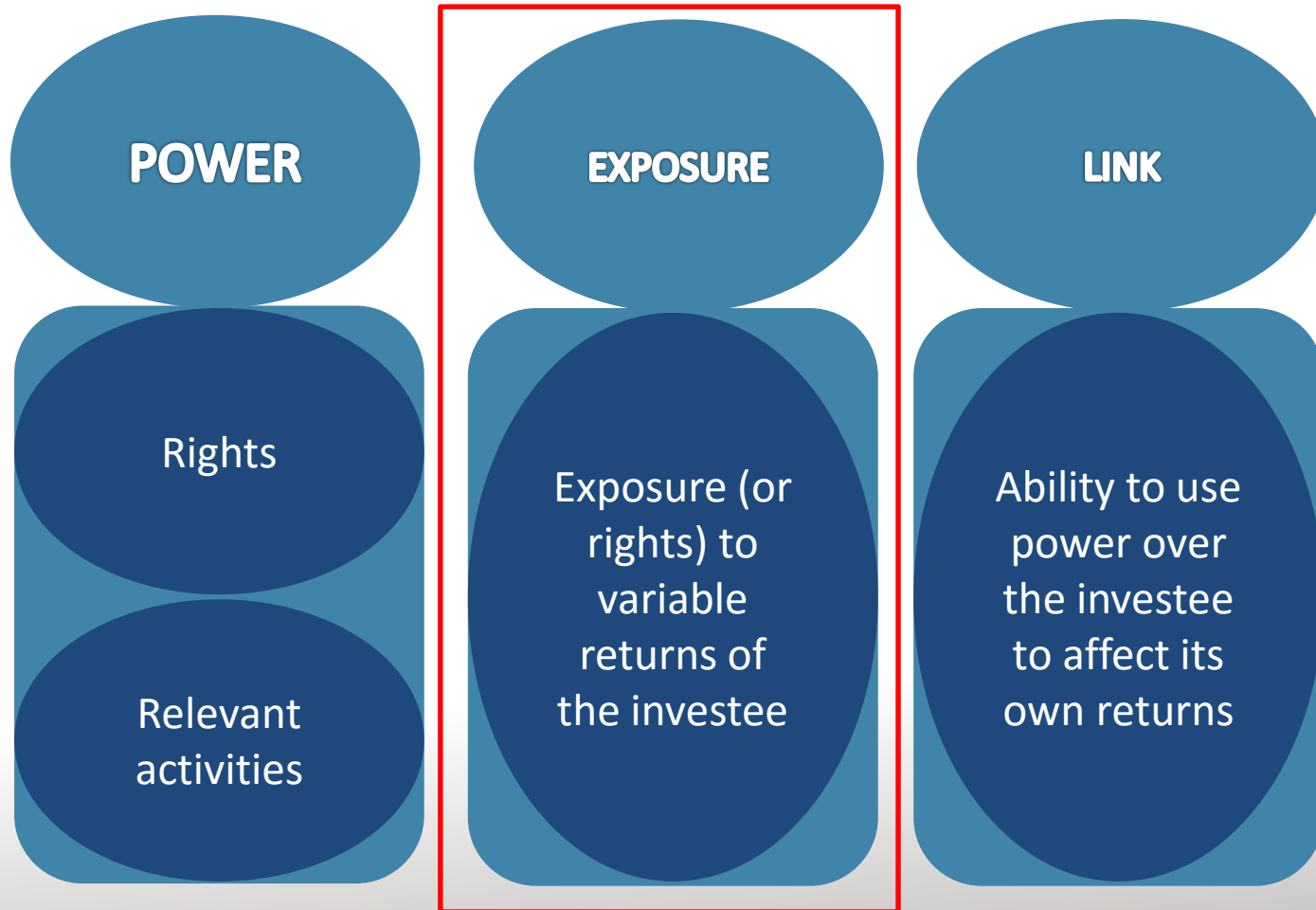


# Power—relevant activities

- Relevant activities → significantly affect the investee's returns
- For many investees, a range of operating and financing activities significantly affect their returns. Examples:
  - selling and purchasing of goods or services
  - making capital expenditures or obtaining finance
- A higher degree of judgment is particularly required when assessing control of investees that are not directed through voting or similar rights and for which there may be multiple parties with decision-making rights over different activities.



# Assessing control of an investee



# Assessing exposure (or rights) to variable returns

## EXPOSURE

Exposure (or  
rights) to  
variable  
returns of  
the investee

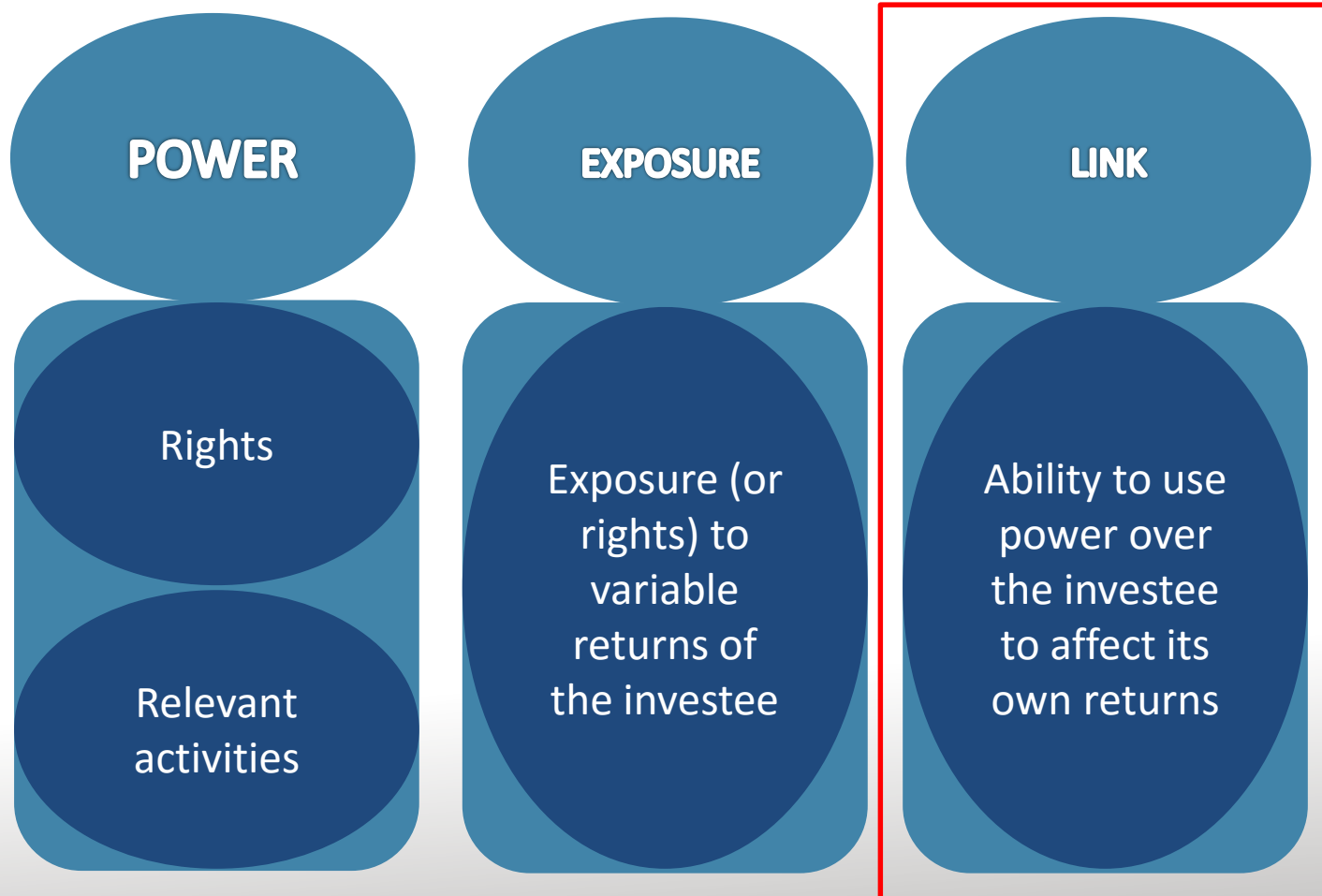
- Definition of control: concept of returns is used in two ways
  - power → ability to direct relevant activities (i.e. directing inconsequential activities is not relevant to assessment of power)
  - rights, or exposure, to variable returns
- Broad definition of **returns**:  
dividends; remuneration from services, fees and exposure to losses; residual interests on liquidation; tax benefits; access to future liquidity; returns not available to other investors (e.g. synergies)

# Exposure or rights to variable returns

- An investor is exposed, or has rights, to variable returns from its involvement with the investee when the investor's returns from its involvement have the potential to vary as a result of the investee's performance.
- The investor's returns can be only positive, only negative or both positive and negative.
- Although only one investor can control an investee, more than one party can share in the returns of an investee. For example, holders of non-controlling interests can share in the profits or distributions of an investee.



# Assessing control of an investee



# Assessing the link between power and returns

LINK

Ability to use  
power over  
the investee  
to affect its  
own returns

- Power + rights = necessary conditions for control (but still not enough)
- To control an investee, an investor must also have the ability to use its power to affect investor's returns from its involvement with the investee
- Control = power that can be used to benefit the investor
- Returns and power: need not be perfectly correlated
- Only one party can control an investee

# Link between power and returns

- A case of power without control is the agency relationship.
- An agent is a party contracted by a principal to perform some service on behalf of the principal that involves delegating some authority to the agent.
- Agent
  - acts in the best interests of the principal (fiduciary responsibility)
  - principal and agent seek to maximise their own benefits
  - additional measures to ensure the agent does not act against the interests of the principal
- Delegated power does not mean control.



# Link between power and returns

- Consider all of the following factors in assessing whether an investor is acting as a principal or as an agent:
  - rights held by other parties (ie kick-out rights)
  - scope of the decision-making authority
  - remuneration of the decision-maker
  - other interests that the decision maker holds in the investee





# Final Remarks:

- As the accountants profession we shall discharge our duty of safe-guarding PUBLIC INTEREST in national empowerment entities- a test of supreme custodianship
- Let's achieve articulate disclosures that shows the “substance over the form”
- Let's achieve true and complete empowerment



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I am honoured to serve you!

