Candidate #	Marker #	Afrikaans (tick)	Total mark out of 40

Part (a)(i) With reference to the Alpha share appreciation rights scheme granted to the executives of APM, discuss, with supporting calculations, the amounts that should be recognised in profit before taxation for the financial year ended 31 December 2013 of APM		**Marks**
APM is an entity within the Alpha group of companies and **is receiving services from their executive employees in exchange for cash amounts that are based on the price of equity instruments of Alpha, another group entity.** Therefore this constitutes a share-based payment arrangement and IFRS 2 is applicable.		1
As APM is receiving the services provided by the executive committee members, APM has to account for the share-based payment expense within their separate financial statements (IFRS 2:43A).		1
As APM has **no obligation** to settle the share-based payment transaction, APM accounts for the share-based payment arrangement as **an equity settled share-based payment transaction** with their separate financial statements (IFRS2:43B(b)).		1 1
Equity-settled share-based payments are measured at the fair value of goods and services received. When granted to employees, however, **the fair value of services received is measured indirectly with reference to the fair value of the equity instruments granted** (IFRS 2:11).		1
Consequently, APM measures the services received at **the fair value of the share appreciation rights (SARs) on 1 July 2010 (the grant date)** (IFRS2:10, 12).		1
The share-based payment expense should be recognised over the **vesting period of three years** (IFRS2:15), taking into account **estimates of the number expected to vest** (IFRS2:20).		1 1
For the current financial year, **the expense shall be recognised over the 6 month period to 30 June 2013** and given the vesting date of 30 June 2013, shall take into account the **actual number of employees on vesting date**.		1 1
No adjustments are made subsequent to the vesting date (30 June 2013) for SARs forfeited or lapsed should employees resign (IFRS2:23).		1
Cumulative (balance)		
30/06/2013: 50 000 x 12 employed**(1)** x 3/3 x R9,80**(1)**	5 880 000	See left
31/12/2012: 50 000 x 11 expected**(1)** x 2,5/3**(1)** x R9,80	(4 491 667)	See left
Net impact on profit or loss (expense)	**1 388 333**	1C
	Total	16
	Maximum	10
	Total for part (a)(i)	**10**
	Awarded for part (a)(i)	

Part (a)(ii) With reference to the Alpha share appreciation rights scheme granted to the executives of APM, discuss, with supporting calculations, the amounts that should be recognised in profit before taxation for the financial year ended 31 December 2013 of the Alpha group.				**Marks**
Because the group has **an obligation to settle the transaction in cash**, the group accounts for the share-based transaction as **cash settled** (IFRS2:B58).				1 1
Consequently, the group measures the transaction **at the fair value of the liability** as the employees render the service (over the three-year service period), **re-measured until settlement date**, at the fair value of the share appreciation rights (IFRS2:30-33).				1 1
Relating to the **re-measurement of the 250 000 rights on the settlement date, these rights are re-measured to their intrinsic value on 31 December 2013**, this being the fair value of the rights on the settlement date.				1
The consolidation journals/process will involve the following: The **APM expense will flow through to the group records and needs to be reversed at group level.** Aplha may record as cash-settled in their separate records and this expense flows through to the group records but is not reversed.				1
Calculation				
Bank (250 000 x (R39,80 – R27,8))**(1)**	3 000 000	Opening balance: 31/12/2012 50 000 x 11**(½)** x 2,5/3**(½)** x R10,12**(1)**	4 638 333	See left
Closing balance: 31/12/2013 50 000 x 11 = 550 000 – 250 000 exercised = 300 000**(1)** x 13**(1)**	3 900 000	Staff costs (P/L) (derived)**(1C)**	2 261 667	See left
	6 900 000		6 900 000	
Available				12
Maximum				9
Total for part (a)(ii)				**9**
Communication skills – clarity of expression				*1*
Awarded for part (a)(ii) including communication				

Part (b)(i) Discuss the tax implications of the share appreciation rights and share options granted to Mr Music in the hands of Mr Music.	**Marks**
The share appreciation rights and shares are **not** section 8B **Broad-based employee share plan** shares, as these rights and shares were only available to a select few employees.	1
Shares (5 000)	
The tax implications of the shares in the hands of Mr Music must be determined in terms of **section 8C**, because he acquired equity instruments as defined and by reason of employment.	1
The shares are a **restricted equity instrument. Vesting took place on 27 February 2013** when he was free to dispose of the shares.	1
The shares vested on 27 February 2013 and the gain on vesting is the market value of the shares at this date (R37,00 per share) less the amount paid of R27,80 (x 5 000 shares = **R46 000)**. This gain was included in his **income** and was subject to employees' tax.	1 1
On disposal (31 December 2013) **a capital gain arises** (proceeds of R39,80 less base cost of R37,00 x 5 000) = R14 000.	1
Appreciation rights (10 000)	
The share appreciation rights are **equity instruments** in terms of paragraph (c) of that definition in section 8C(7). It was also a **restricted instrument.** These **rights vested on 30 June 2013.** *(<u>Alternative 31 December 2013:</u> The rights remain a restricted instrument until 31 December 2013 as the cash bonus payable in terms of the SAR is not deliverable to the taxpayer until the happing of an event (namely the exercise of the employee's right)).*	1 1
The gain on vesting is (10 000 x (R38,20 minus R27,80) or 10 000 x (R10,40 minus R0,00) = **R104 000** *(<u>Alternative 31 December 2013:</u> 10 000 x (R39,80 minus R27,80) = 120 000)* This constitutes "remuneration" as defined in par. 1, Schedule 4 and employees' tax must be withheld. The amount is included in his **income** (s8C(2)).	1 1
On exercise of his share appreciation rights (31 December 2013) **a capital gain arises** (proceeds of R120 000 less base cost of R104 000) = R16 000.	1
No capital gain amount will be included in his taxable income as the combined capital gain equals R30 000 which equals the **annual exclusion**.	1
In the year when the equity instruments were *granted* to Mr Music (the 10 000 share appreciation rights and the 5 000 shares), it would constitute a receipt otherwise than in cash – gross income para (*c*) **but is exempt under s10(1)(*n*D)**.	1
Available	**13**
Maximum	**10**
Total for part (b)(i)	**10**
Awarded for part (b)(i)	

Part (b)(ii) Discuss the tax implications of the share appreciation rights and share options granted to Mr Music in the hands of Alpha.	**Marks**
Deduction of the payment of the share appreciation rights	
There is no specific section in the Income Tax Act that provides for the deduction **(section 11(lA) does not apply)** and the deduction must therefore qualify in terms of **section 11(a)** and not be prohibited by section 23(g).	1
The expense is **not capital in nature** and it is in the **production of income** (employees). It is also for purposes of trade. The issue relating to "in the production of income" relates to retaining and motivating Mr Music as an executive (employee) of Alpha. The ***P.E. Electric Tramway*** case and the closeness of connection of the payment of the R120 000 on 31 December 2013 is relevant.	1 1
At issue then is when the expense was **actually incurred**. **In *Edgars Stores Ltd v CIR*** the Judge stated that the words 'expenditure ... actually incurred' refer to only expenditure (otherwise qualifying for deduction) in respect of which the taxpayer has incurred an **unconditional legal obligation** during the year of assessment in question that may be deducted in terms of section 11(a) from income returned for that year.	1 1 1
Conclusion: The expense was actually incurred when paid in December 2013 and can be deducted in terms of section 11(a) read with section 23(g).	1C
Shares	
CSARS v Labat (669/10) [*2011*] ZASCA 157: 'Expenditure … requires a diminution (even if only temporary) or at the very least movement of assets of the person who expends.'	1
The **issue of shares does not constitute expenditure** and no deduction can therefore be made.	1
Available	**9**
Maximum	**8**
Total for part (b)(ii)	**8**
Communication skills – clarity of expression *logical argument*	*1* *1*
Awarded for part (b)(ii) including communication	