Definitions
P Botswana Pula
USD United States Dollar
ZAR South African Rand

Present value tables are presented on p. 12 at the end of the paper.

Enjoy-SA (Pty) Ltd (“Enjoy-SA”) operates in the leisure and tourism industry. Enjoy-SA is a South African company with a 28 February year end. It has two significant assets, namely the Stimela luxury train and a shareholding in the Botswana Swamp Hotel company. Its other assets comprise inventories, which are measured at the lower of cost or fair value less costs to sell, and trade receivables.

A The Stimela luxury train

Stimela is a luxury train operated by Enjoy-SA, running on routes between Cape Town, Johannesburg and Victoria Falls.

Historically, approximately 60% of Stimela’s passengers have been non-South African residents. However, because of the strengthening of the ZAR in the past few years, the number of non-resident passengers has steadily declined. This decline has not been compensated for by an increase in the number of South African resident passengers.

Enjoy-SA acquired the newly manufactured train on 1 March 1998 from the manufacturer at a cost of R62 million. The train had an estimated useful life of ten years, after which Enjoy-SA expects to purchase a new train. At initial recognition, Enjoy-SA estimated the residual value of the train to be R12 million. This estimate was not revised by 28 February 2005 and the company still intends to sell the train on 28 February 2008.

The manufacturer of the Stimela train maintains records of resale values of various trains. At 28 February 2005, the resale prices of trains of the same make and model as Stimela were as follows:
• Ten-year-old trains were selling for R7 050 000; and
• Seven-year-old trains were selling for R16 million.

The costs of selling the second-hand trains are negligible.

The carrying value of the train has not been reduced for any amounts other than the annual depreciation charge, which is calculated at the end of each financial year. The South African Revenue Service agreed to a straight line write-off of the train over 12 years in terms of section 11(e) of the Income Tax Act.

Prior to finalising the financial statements of the company for the year ended 28 February 2005, executive management had to present budgets for the next three financial years to the board of directors of Enjoy-SA.

The following budgets were approved by the Board for the Stimela operation:

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</thead>
<tbody>
<tr>
<td>Cash revenue</td>
<td>Actual</td>
<td>Budgeted</td>
<td>Budgeted</td>
<td>Budgeted</td>
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<tr>
<td></td>
<td>R'000</td>
<td>R'000</td>
<td>R'000</td>
<td>R'000</td>
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<tr>
<td>Cash revenue</td>
<td>15 000</td>
<td>15 800</td>
<td>16 600</td>
<td>17 400</td>
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<tr>
<td>Cash operating</td>
<td>11 000</td>
<td>11 277</td>
<td>11 400</td>
<td>11 700</td>
</tr>
<tr>
<td>Depreciation</td>
<td>5 000</td>
<td>5 000</td>
<td>5 000</td>
<td>5 000</td>
</tr>
<tr>
<td>Total expenses</td>
<td>16 000</td>
<td>16 277</td>
<td>16 400</td>
<td>16 700</td>
</tr>
<tr>
<td>Pre-tax (loss)</td>
<td>(1 000)</td>
<td>(477)</td>
<td>200</td>
<td>700</td>
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</table>
Additional information

1. The above estimates include the effects of inflation.
2. All operating costs are incurred in ZAR.
3. Revenue is earned and received evenly throughout the years.

The following discount rates are applicable to investments equivalent in risk to the Stimela operation:

- Pre-tax ZAR nominal (i.e. including the effect of inflation) 15%
- Pre-tax ZAR real (i.e. excluding the effect of inflation) 10%

B Botswana Swamp Hotel (Pty) Ltd

Enjoy-SA acquired 10% of the Botswana Swamp Hotel (Pty) Ltd (“Botswana Swamp Hotel”) on 1 September 2002 for P1 million. The company is incorporated in Botswana. On the same day, Enjoy-SA acquired an option to purchase an additional 30% of the company at any time between 1 September 2004 and 1 September 2010 at a strike price of P3 million. The cost of the option was P500 000.

On 1 September 2002, Enjoy-SA classified its 10% interest in Botswana Swamp Hotel as an available-for-sale financial asset and elected to recognise changes in the fair value of the investment directly in equity.

Dividends paid from Botswana companies to investors outside Botswana are subject to a withholding tax of 15%. No dividends have been paid by Botswana Swamp Hotel since 1 September 2002.

REQUIRED

(a) Prepare journal entries, with workings and narrations, to record the changes to the carrying value of the Stimela train and the related tax in the financial statements of Enjoy-SA for the year ended 28 February 2005.

(b) Calculate the revised budgeted depreciation charge for Stimela for the year ending 28 February 2006.

(c) List the audit procedures that the auditor of Enjoy-SA should carry out to audit the recognition and measurement of the Stimela train at 28 February 2005.

(d) Prepare a report to the financial director of Enjoy-SA, describing, with reasons, the appropriate recognition and measurement of the investment in Botswana Swamp Hotel and the option to purchase an additional interest in Botswana Swamp Hotel in the consolidated (group) financial statements of Enjoy-SA for the year ended 28 February 2005. Your report must consider the effect of the Botswana withholding tax on the 2005 financial statements, but should not consider any other tax effects.