Notes to the condensed consolidated annual financial statements

for the year ended 31 March 2017

1 Corporate information

Telkom South Africa SOC Limited (Telkom) is a company incorporated and domiciled in the Republic of South Africa (South Africa) whose shares are publicly traded. The main objective of the Telkom group is to supply telecommunication, multimedia, technology, information and other related information technology services to the group customers, as well as mobile communication services, in Africa.

2 Basis of preparation and accounting policies

2.1 Basis of preparation

The condensed consolidated annual financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting and in compliance with the Listings Requirements of the JSE Limited, the South African Companies Act, 2008, as amended, the SAICA Financial Reporting Guide as issued by the Accounting Practices Committee and the Financial Reporting Standards Council.

The condensed consolidated annual financial statements are disclosed in South African Rand, which is also the group's presentation currency. All financial information presented in Rand has been rounded off to the nearest million.

The condensed consolidated annual financial statements are prepared on the historical cost basis, with the exception of certain financial instruments initially (and sometimes subsequently) measured at fair value. Details of the group's significant accounting policies are consistent with those applied in the previous financial year except for those listed below.

Significant accounting judgements, estimates and assumptions

In preparing these condensed consolidated annual financial statements, the significant judgements made by management in applying the group's accounting policies and the key sources of estimation uncertainty were consistent with those applied to the consolidated financial statements for the year ended 31 March 2016 except for the changes in note 2.2, note 4 and the assumptions used to calculate the deferred tax asset in Telkom company.

Significant accounting policies

The condensed consolidated annual financial statements have been prepared in accordance with the accounting policies adopted in the group's last annual financial statements for the year ended 31 March 2016, except for the adoption of the amendments, new standards and changes in accounting policies as described in note 2.2.

The following new standards and amendments to standards have been early adopted.

Standard(s), Amendment(s)	Salient feature of the changes	Effective date
IFRS 12 Disclosure of Interests in Other Entities	Amendment clarifying the scope of IFRS 12 with respect to interests in entities classified as held for sale in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. This amendment has been adopted and has no impact on the group.	**1 January 2017**
IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses	The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explains in which circumstances taxable profit may include the recovery of some assets for more than their carrying amount. These amendments have been adopted and do not have an impact on the group.	**1 January 2017**

The group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

2 Basis of preparation and accounting policies (continued)

2.2 Correction of prior period errors and change in accounting policy

Correction of prior period errors

The condensed consolidated annual financial statements provide comparative information in respect of the previous period. In addition, the group presents an additional statement of financial position at the beginning of the preceding period when there is a retrospective application of an accounting policy and a retrospective restatement. An additional statement of financial position as at 31 March 2015 is presented in these condensed consolidated annual financial statements due to the retrospective correction of a prior period error.

2.2.1 Telkom Retirement Fund

During the 31 March 2016 reporting period, the group reported the restatement of the balances as a "Reassessment of the Telkom Retirement Fund (TRF) Defined Benefit Plan". For classification purposes, it should be noted that the reassessment of the TRF constituted an error and not a change in accounting policy as previously stated. All relevant IAS 8 disclosures (nature, correction amounts and the amount of correction at the beginning of the year) regarding the error were appropriately disclosed in the FY2016 Financial Statements.

2.2.2 Fair value hierarchy

During the previous reporting periods, the group reported the fair value hierarchy of the TL20 bonds as level 1 instead of level 2 based on the fact that it could access the quoted price of the bonds. According to IFRS 13, bonds can only be level 1 if they are quoted on an active market. The TL20 bonds are quoted on the market, however their transactions are not frequent enough for the market to be regarded as liquid.

The group has corrected this disclosure by changing the TL20 fair value hierarchy from level 1 to level 2. The group has assessed that there has been no impact on the fair value of the TL20 bonds in the prior year as the quoted price is an adjusted market price, for perceived changes in risk as well as the time value of money. The group will continue to assess if the quoted price of the listed TL20 bonds is considered to be a level 1 or level 2 price and if further adjustment might be required.

2.2.3 Fraud – Trudon

During the current financial year, the group uncovered fraud at one of its subsidiaries, Trudon, resulting in the termination of the services of the general manager, IT.

An internal investigation into the fraud was launched, which identified invoicing and accounting irregularities which led to the incorrect recognition and subsequent measurement of intangible assets over a period of several years. The investigation also identified the past practice of irregularly capitalising operating expenditure as intangible assets. The nature of the errors identified included:

> Intangible assets capitalised for which there was no evidence of a valid asset or expense as a result of the above fraud
> Expenses capitalised to intangible assets which on re-evaluation of the nature of expense, based on the invoice detail, was deemed to not meet the recognition criteria of IAS 38 at date of capitalisation
> Identification of intangible assets which were no longer in use and which had been decommissioned in earlier periods but not de-recognised at time of decommissioning
> Income tax implications in relation to expenses and wear and tear allowances deducted in prior periods relating to invoices associated with financial irregularities which based on senior counsel opinion should not have been deducted for tax purposes.

These issues identified constituted material prior period errors and have been corrected by restating each of the affected line items for the prior period as shown in the table 2.3 and 2.4 below.

2.2.4 Change in accounting policies

Cost of sales

The group has previously included all the expenses that can be directly linked to revenue received for services provided and goods sold to customers in the definition of cost of sales.

Following the sale of the Enterprise business to BCX in November 2016, the group elected to change its accounting policy for cost of sales to only include expenses directly tied to revenue from the sale of goods. This decision to change the accounting policy in the view of management will provide more reliable and relevant information to ensure consistent presentation across the group following the sale of Enterprise to BCX.

The new group accounting policy now applies that cost of sales determined as:
> Cost of goods sold relating to the sale of goods net of supplier rebates and discounts including:
  • Commission costs paid to external parties for the sale of goods sold
  • Logistics and delivery expenses relating to the goods sold

All other costs are disclosed by nature with the following being the key categories:
> Employee expenses
> Selling, general and administrative expenses
> Service fees
> Operating leases
> Depreciation and amortisation

This change in policy has resulted in the re-classification of these line items in the comparative statement of profit or loss and other comprehensive income. Refer to note 2.3.

Notes to the condensed consolidated annual financial statements – continued

for the year ended 31 March 2017

2 Basis of preparation and accounting policies - continued

2.3 Adjustments to the condensed consolidated provisional statement of profit or loss and other comprehensive income for the year ended 31 March 2016

	Group				
	As previously reported Rm	Telkom restatement * Rm	BCX restatement * Rm	Trudon IAS 8 disclosure** Rm	Restated Rm
Operating revenue	37 325	–	–	–	**37 325**
Payments to other operators	2 793	–	–	–	**2 793**
Cost of sales	6 969	100	(2 047)	(11)	**5 011**
Net operating revenue	27 563	(100)	2 047	11	**29 521**
Other income	1 281	–	–	–	**1 281**
Operating expenses	20 083	(100)	1 968	75	**22 026**
Employee expenses	10 901	–	1 264	–	**12 165**
Selling, general and administrative expenses	4 978	–	743	75	**5 796**
Service fees	3 106	(100)	(41)	–	**2 965**
Operating leases	1 098	–	2	–	**1 100**
EBITDA	8 761	–	79	(64)	**8 776**
Depreciation of property, plant and equipment	4 370	–	79	(1)	**4 448**
Amortisation of intangible assets	902	–	–	(22)	**880**
Write-offs, impairment and losses of property, plant and equipment and intangible assets	170	–	–	–	**170**
Operating profit	3 319	–	–	(41)	**3 278**
Investment income	203	–	–	–	**203**
Finance charges and fair value movements	622	–	–	–	**622**
Interest	521	–	–	–	**521**
Foreign exchange and fair value movements	101	–	–	–	**101**
Profit before taxation	2 900	–	–	(41)	**2 859**
Taxation expense	524	–	–	14	**538**
Profit for the year	2 376	–	–	(55)	**2 321**
Other comprehensive income					
Items that will be reclassified subsequently to profit or loss					
Exchange losses on translating foreign operations	(9)	–	–	–	**(9)**
Items that will not be reclassified to profit or loss					
Defined benefit plan actuarial losses	191	–	–	–	**191**
Defined benefit plan asset ceiling limitation	86	–	–	–	**86**
Other comprehensive income for the year, net of taxation	268	–	–	–	**268**
Total comprehensive income for the year	2 644	–	–	(55)	**2 589**
Total operations					
Basic earnings per share (cents)	439.4				**432.4**
Diluted earnings per share (cents)	432.8				**425.8**

* *Refer to note 2.2.4*
** *Refer to note 2.2.3.*

2.4 Adjustments to the condensed consolidated provisional statement of financial position	Group - March 2016			Group - March 2015		
	As previously reported Rm	Trudon IAS 8 disclosure* Rm	Restated March 2016 Rm	As previously reported Rm	Trudon IAS 8 disclosure* Rm	Restated March 2015 Rm
Assets						
Non-current assets	33 875	(186)	33 689	30 855	(160)	30 695
Property, plant and equipment	25 357	(7)	25 350	24 479	(8)	24 471
Intangible assets	4 584	(179)	4 405	2 982	(152)	2 830
Other investments	2 318	–	2 318	2 231	–	2 231
Employee benefits	846	–	846	452	–	452
Other financial assets	55	–	55	28	–	28
Finance lease receivables	281	–	281	413	–	413
Deferred taxation	434	–	434	270	–	270
Current assets	12 912	(48)	12 864	11 127	(27)	11 100
Inventories	971	–	971	638	–	638
Income tax receivable	57	(14)	43	11	(8)	3
Current portion of finance lease receivables	207	–	207	200	–	200
Trade and other receivables	7 375	(34)	7 341	5 388	(19)	5 369
Current portion of other financial assets	1 754	–	1 754	1 247	–	1 247
Cash and cash equivalents	2 548	–	2 548	3 643	–	3 643
Total assets	46 787	(234)	46 553	41 982	(187)	41 795
Equity and liabilities						
Equity attributable to owners of the parent	26 134	(159)	25 975	24 864	(123)	24 741
Share capital	5 208	–	5 208	5 208	–	5 208
Share-based compensation reserve	241	–	241	126	–	126
Non-distributable reserves	1 507	–	1 507	1 507	–	1 507
Retained earnings	19 178	(159)	19 019	18 023	(123)	17 900
Non-controlling interest	473	(83)	390	363	(64)	299
Total equity	26 607	(242)	26 365	25 227	(187)	25 040
Non-current liabilities	7 104	–	7 104	5 272	–	5 272
Interest-bearing debt	4 566	–	4 566	3 244	–	3 244
Employee related provisions	1 665	–	1 665	1 264	–	1 264
Non-employee related provisions	66	–	66	61	–	61
Deferred revenue	656	–	656	687	–	687
Deferred taxation	151	–	151	16	–	16
Current liabilities	13 076	8	13 084	11 483	–	11 483
Trade and other payables	7 134	–	7 134	5 635	–	5 635
Shareholders for dividend	22	–	22	19	–	19
Current portion of interest-bearing debt	703	–	703	1 612	–	1 612
Current portion of employee related provisions	2 231	–	2 231	1 882	–	1 882
Current portion of non-employee related provisions	142	–	142	303	–	303
Current portion of deferred revenue	1 708	–	1 708	1 502	–	1 502
Income tax payable	675	8	683	344	–	344
Current portion of other financial liabilities	455	–	455	185	–	185
Credit facilities utilised	6	–	6	1	–	1
Total liabilities	20 180	8	20 188	16 755	–	16 755
Total equity and liabilities	46 787	(234)	46 553	41 982	(187)	41 795

** Refer to note 2.2.3.*