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EASTERN CAPE
EDUCATION

Suggested answers

COMPANIES

QUESTION 1

1.1.1 Calculate the profit or loss on disposal of the computer on 31 August 2019.

$$\begin{array}{ccccccc}
 30\,000 & - & (13\,680 & + & 1\,632) & - & 8\,000 = 6\,688 \\
 \checkmark & & \checkmark & & \checkmark \boxtimes & & \checkmark \boxtimes \text{one part correct}
 \end{array}$$

one method mark one part correct

OR

Asset disposal

Equipment	30 000	Accumulated depreciation on equipment (13 680 + 1 632)	15 312
		Bank	8 000
		Loss on sale of asset	6 688
	30 000		30 000

6

1.1.2 Calculate the total depreciation for the year.

$$\begin{array}{lcl}
 950\,000 \times 20\% \times 3/12 & = & 47\,500 \checkmark \boxtimes \text{one part correct} \\
 1\,520\,000 - 950\,000 \times 20\% & = & 114\,000 \checkmark \boxtimes \text{one part correct}
 \end{array}$$

161 500 four marks

$$\begin{array}{lcl}
 (660\,000 - 30\,000) \checkmark - (178\,000 - 13\,680) \checkmark \times 20\% & = & 93\,136 \checkmark \\
 \text{Asset disposal (see 3.1.1)} & & = 1\,632 \checkmark
 \end{array}$$

630 000 one mark 164 320 one mark 94 768 four marks

Total: 256 268 ☒

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1.1.3 Suggest ONE internal control measure that the internal auditor can perform to verify the tangible assets figure in the Balance Sheet.

Any one valid points ☒ ☒

- Check the fixed asset register agrees with an actual physical inspection of the tangible assets.

- Check that all controls are adequate and are actually being implemented.
- Check the documentation and financial records to ensure that all purchase and sale of fixed assets have been recorded correctly.

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1.2 Income Statement for the year ended 28 February 2019

Sales $7\,540\,000 \checkmark \times 160/100 \checkmark - 12\,480 \checkmark$ 12 064 000	☒ 12 051 520
Cost of sales $7\,540\,000 \checkmark - 7\,800 \checkmark$	☒ (7 532 200)
Gross profit 8	☒ 4 519 320
Other operating income	☒ 205 680
Commission income	31 580
Rent income $158\,200 + 15\,400 \checkmark \checkmark$	☒ 173 600
Provision for bad debts adjustment	$\checkmark \checkmark 500$
Gross operating profit 7	☒ 4 725 000
Operating expenses	☒ (1 875 000)
Director's fees	932 400
Audit fees	64 000
Salaries and wages	320 000
Insurance	$\checkmark 56\,250$
Bad debts $2\,779 \checkmark + 15\,225 \checkmark \checkmark$	☒ 18 004
Sundry expenses	$\checkmark 187\,640$
Loss on sale of asset see 1.1.1 (could be profit)	☒ 6 688
Loss on theft of stock $37\,500 \checkmark - 26\,250 \checkmark$	☒ 11 250
Trading stock deficit $1\,287\,000 \checkmark + 7\,800 \checkmark - 37\,500 \checkmark - 1\,234\,800 \checkmark$	☒ 22 500
Depreciation see 1.1.2	☒ 256 268
Operating profit 18	☒ 2 850 000
Interest Income balancing figure	☒ 158 200
Profit before interest expense	☒ 3 008 200
Interest expense $2\,398\,200 + 510\,000 - 2\,620\,000$	$\checkmark \checkmark (288\,200)$
Net profit before tax NPAT + Inc tax	☒ 2 720 000

Income tax	2 040 000 x 25/75	✓✓(680 000)	
Net profit for the year	7	2 040 000	40

QUESTION 2

2.1

Net profit before tax	1 449 200	
Directors fees (625 000✓ – 25 000✓)	(600 000)	✓
Packing material (12 000✓ x 80/20✓)	(48 000)	✓
Bad debts (1 200✓ - 480✓)	(720)	✓
Rent income (177 600✓ – 26 400✓)	151 200	✓
Salaries	55 820	✓✓
Operating profit before interest expense	1 007 500	✓
Interest expense	(157 500)	✓
Net profit before tax	850 000	✓
Income tax	(255 000)	✓
Net profit after tax	595 000	✓
Accept brackets instead of – If no sign, assume + Positive/negative effect & figure must be correct Foreign entries -1 (max -2)		

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2.2 KHUMALO FASHIONS LTD.**2.2.1 INCOME STATEMENT FOR THE YEAR ENDED 28 FEBRUARY 2019**

Sales	1 225 700	
Cost of sales (1 169 700 x ¹⁰⁰ / ₁₄₀) ☒ + (56 000 x ¹⁰⁰ / ₁₂₅) ☒	☒ (880 300)	
Gross profit (Sales – Cos), operation	☒ 345 400	5
Other operating income operation, one part correct	☒ 112 560	
Commission income (89 200 – 640 ✓✓) operation	☒ 88 560	
Rent income (4 x 6 000)	☒ 24 000	
Gross operating income operation	☒ 457 960	8
Operating expenses Gross operating inc – Operating profit	☒ (151 535)	
Bank charges (3 260 + 340)	☒ 3 600	
Bad debts (5 600 + 800)	☒ 6 400	
Discount allowed (2 940 – 400 ✓) operation	☒ 2 540	
Stationery (3 860 + 100 ✓ – 280 ✓) one part correct	☒ 3 680	
Insurance (14 250 – 2 400 ✓✓) operation	☒ 11 850	
Director's fees (50 000 + 60 000)	☒ 110 000	
Sundry expenses (balancing figure, one part correct, can be negative based on candidate's answers)	☒ 5 345	
Loss of damaged stock (4 800 ✓ – 1 680 ✓) operation	☒ 3 120	
Trading stock deficit	☒ 3 200	
Provision for bad debts adjustment (3 800 – 2 000)	☒ 1 800	22

Operating profit (1 225 700 x 25%)	✓✓ 306 425
Interest income (11 350 + 670)	✓✓ 12 020
Profit before interest expense operation	☑ 318 445
Interest expense Profit before int exp – NPBT, operation	☑ (55 795)
Profit before tax NBPT + Tax, operation, must be greater than NBAT	☑ 262 650
Income tax	✓ (78 795)
Profit after tax (1 225 700 x 15%)	✓✓ 183 855

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3.1

Retained income	
Balance at beginning of year	765 000
Funds used for shares repurchased (125 000 x 0,50)	✓✓ (62 500)
Net profit after tax	✓ 2 040 000
Ordinary Share dividends operation one part correct must be in brackets	☑ (2 182 500)
Interim	✓ 982 500
Final (1 500 000 ✓✓ x 0,80 ✓) operation one part correct	☑ 1 200 000
Balance at the end of year	☑ 560 000 operation one part correct

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3.2

3.2.1

3.2.1.1

Trade and other receivables		
Trade debtors (44 800 ✓ – 1 200 ✓ + 1 000 ✓)	44 600	☑
Provision for bad debts	(1 700)	✓
Net trade debtors Operation one part correct	42 900	☑
Prepaid expense (Directors fees) See 3.2	25 000	☑
SARS Income tax (267 000 ✓ – 255 000 ☑) See 3.2	12 000	☑
Operation one part correct	79 900	☑

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3.2.2.2

Retained income		
Balance at the beginning (130 000 ✓ + 79 000 ✓)	209 000	✓
Buy-back of shares (20 000 ✓ X 3.95 ✓)	(79 000)	☑
Net profit after tax See 3.2	595 000	☑

Dividends correct	Operation one part	(190 820)	☒
Paid / interim		55 820	☒
Final/ recommended (180 000 ✓ X 0.75 ✓)		135 000	☒
Balance at the end of the year Operation		534 180	☒

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4.1 NOTES TO THE BALANCE SHEET ON 28 FEBRUARY 2019

ORDINARY SHARE CAPITAL

AUTHORISED		
800 000 ordinary shares		
ISSUED		
305 000	Ordinary shares in issue at the beginning of the year	1 464 000
(5 000)	shares repurchased during the year (x R4,80 ✓✓)	(24 000) Ignore brackets one part correct do not accept 25 000 as final answer
40 000	shares issued during the year	204 000 See 4.1
✓✓ 340 000	Ordinary shares in issue at the end of the year	Operation - repurch + Issued 1 644 000

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RETAINED INCOME

Balance at the beginning of the year	67 500	✓
Net profit after tax (655 000 – 183 400)	471 600	✓✓
Shares repurchased (25 000 ✓ - 24 000 ☒ see OSC)	Ignore brackets (1 000)	☒
Dividends on ordinary shares	Ignore brackets (263 600)	☒
Interim dividends paid (204 000 ✓ – 90 000 ✓)	one part correct 114 000	☒
Final dividends declared	149 600	✓
Balance at the end of the year Operation: must – repurch and div, one part correct	274 500	☒

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4.2 FREEZA LIMITED**4.2.1 Ordinary Share Capital**

700 000 ✓	Ordinary shares in issue at beginning of year	✓ 3 005 000
200 000 ✓	Additional share purchased during the year	✓ 2 800 000
(60 000) ✓	Repurchase of shares @R6,45 ✓	✓ (387 000)
840 000 ☒ operation	Ordinary shares in issue at end of year	5 418 000

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Retained Income

Balance at beginning		1 221 000
Net profit after tax (2 500 000 ✓ x 0,70 ✓) one part correct		☒ 1 750 000
Shares re-purchased (60 000 ✓ x 6,55 ✓) one part correct		☒ (393 000)
Ordinary share dividends		☒ (856 000)
Interim/paid		✓ 268 000
Final/Recommended one part correct		✓ ☒ 588 000
Balance at end one part correct		✓ ☒ 1 722 000

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4.2.2 Balance Sheet (Statement of Financial Position) as at 28 February 2019:

Assets		
Non-current assets	TA - CA	☒ 6 433 380
Fixed assets (3 600 000✓ + 1 200 000✓ + 1 600 000✓ - 160 000✓ - 630 000✓✓) one part correct		☒ 5 610 000
Financial assets	balancing figure	☒ 823 360
Current assets	CL x 1.5	☒ ☒ 3 343 860
Inventories	balancing figure	☒ 1 703 860
✓ Trade and other receivables (1060 000✓ + 50 000✓✓ + 48 000✓) one part correct		☒ 1 158 000
✓ Cash and cash equivalents (132 000 ✓ + 350 000✓) one part correct		☒ 482 000
Total assets	see E & TL	☒ 9 777 240
Equity and liabilities		
Ordinary shareholders' equity	operation	☒ 7 140 000
✓ Share capital	see 4.2.1	☒ 5 418 000
✓ Retained income	see 4.2.1	☒ 1 722 000
Non-current liabilities		408 000
Mortgage loan (600 000 ✓ + 16 000 ✓ - 112 000 ✓ - 96 000 ✓✓) one part correct		☒ 408 000
Current liabilities	operation	☒ 2 229 240
Trade and other payables (1 440 000✓ + 71 000✓ + 34 240✓✓) one part correct		☒ 1 545 240
✓ Short term loan	see mortgage loan	☒ 96 000
✓ Shareholders for dividends	see note 4.2.1	☒ 588 000
Total equity and liabilities	operation	☒ 9 777 240

4.3 PHAMBILI LIMITED

4.3.1 Prepare the following notes for the financial year ended 28 February 2019.

(a) Ordinary share capital

500 000 ✓	Ordinary shares at beginning of the year	1 220 000 ✓
900 000 ✓	Shares issued at R3,00 ✓	2 700 000 ✓
(150 000) ✓	Shares repurchased at R2,80 ✓✓ ASP (Do not accept R0,75 as ASP)	(420 000) ✓
1 250 000 ✓	Ordinary shares in issue at the end	3 500 000 ✓

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ASP – average share price

(b) Retained income

Balance at the beginning of the year	355 500
Net profit after tax 1 148 000 ✓ × $\frac{72}{28}$ ✓	2 952 000 ✓
Funds used for repurchase of shares (150 000 × R0,75)	(112 500) ✓
Ordinary share dividends operation, one part correct	(975 000) ✓
Interim	350 000 ✓
Final (1 250 000 ✓ × R0,50 ✓) See above operation, one part correct	625 000 ✓
Balance at the end of the year inspect operation Must subtract ordinary share dividends and shares repurchased	2 220 000 ✓

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4.3.2

Complete the Balance Sheet (Statement of Financial Position) on 28 February 2019. Where notes are not required, show ALL workings.

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BALANCE SHEET ON 28 FEBRUARY 2019		
ASSETS		
NON-CURRENT ASSETS	TA-CA	6 519 800 ✓
Fixed Assets		1 499 500 ✓
Financial Assets (Fixed Deposit)	balancing figure	5 020 300 ✓
CURRENT ASSETS		1 400 200
Inventory (480 000 + 16 000)		496 000 ✓✓
Trade and receivables (400 000 ✓ – 5 400 ✓ + 32 000 ✓✓)		426 600 ✓
Cash and cash equivalents (1 010 100 ✓ – 532 500 ✓)		477 600 ✓
TOTAL ASSETS		7 920 000 ✓
EQUITY AND LIABILITIES		
ORDINARY SHAREHOLDERS' EQUITY		5 720 000 ✓
Ordinary share capital	See 4.3.1	3 500 000 ✓
Retained income	See 4.3.1	2 220 000 ✓
NON-CURRENT LIABILITIES		992 000
Loan (1 376 000 ✓ – 384 000 ✓✓) (32 000 × 12) Operation, one part correct		992 000 ✓✓
CURRENT LIABILITIES		1 208 000
Trade and other payables (177 500 ✓ + 10 000 ✓ + 11 500 ✓ + 625 000 ✓)		824 000 ✓ * 199 000 / ** 1 208 000 / *** 583 000
Current portion of loan	See above	384 000 ✓
Shareholders for dividends		625 000
NOTE: CURRENT PORTION OF LOAN + SHAREHOLDERS FOR DIVIDENDS CAN BE ADDED TO TRADE AND OTHER PAYABLES OR SHOWN SEPARATELY * 177 500 + 10 000 + 11 500 = 199 000 ** 177 500 + 10 000 + 11 500 + 625 000 + 384 000 = 1 208 000 *** 177 500 + 10 000 + 11 500 + 384 000 = 583 000		
TOTAL EQUITY AND LIABILITIES		7 920 000 ✓

4.4.1 FIXED ASSETS

(a)	285 000 – 91 200	193 800 ✓
(b)	96 900 2 marks 142 500 ✓ - 45 600 ✓ – (96 900 ✓ x 20% x 9/12 ✓) 14 535 2 marks	one part correct 82 365 ✓
(c)	Remaining: (285 000 – 142 500) – (91 200 – 45 600) 142 500 ✓ – 45 600 ✓ = = 96 900 x 20% = 19 380 ✓ one part correct New: 180 000 x 20% x 1/12 = 3 000 ✓ ✓ one part correct Sold: 14 535 ✓ see (b)	one part correct 36 915 ✓

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4.4.2 BALANCE SHEET ON 30 JUNE 2019

ASSETS	
NON-CURRENT ASSETS TA-CA	✓ 5 777 280
Fixed assets NCA - FA	✓ 5 127 280
Financial assets: Fixed deposit (Shallow Bank)	✓ 650 000
	(3)
CURRENT ASSETS	✓* 1 465 940
Inventories (450 000 ✓ – 5 000 ✓✓ + 15 300 ✓)	✓* 460 300
Trade and other receivables 412 800 3 marks (430 000 ✓✓ - 17 200 ✓ + 79 800 ✓)	✓* 492 600
Cash and cash equivalents (510 640 ✓ + 2 400 ✓)	✓* 513 040
TOTAL ASSETS	✓ 7 243 220 = TE and L
	(15)
EQUITY AND LIABILITIES	
ORDINARY SHAREHOLDERS' EQUITY (800 000 x 6,36)	✓✓ 5 088 000
Ordinary share capital	3 746 500
Retained income OSE - OSC	✓ 1 341 500

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	(3)
NON-CURRENT LIABILITIES	452 000
Loan: Gaga Bank (752 000 ✓ – 300 000 ✓)	☒ * 452 000
	(3)
CURRENT LIABILITIES	☒ * 1 703 220
Trade and other payables *could include SFD/SARS:IT/STL (661 600 ✓ + 103 600 ✓✓ + 14 520 ✓✓)	☒ * 779 720
Current portion of loan	✓ 300 000
Shareholders for dividends (800 000 x 0,75)	✓ ☒ * 600 000
SARS: Income tax	✓ 23 500
TOTAL EQUITY AND LIABILITIES	☒ 7 243 220 = SE + NCL + CL
	(12)
	* one part correct

QUESTION 5**5.1.1 Calculate the following for the Cash Flow Statement:**

Income tax paid $1\,240\,000 - 892\,800$ $12\,000 \checkmark + 347\,200 \checkmark + 8\,500 \checkmark$ OR $- 12\,000 - 347\,200 - 8\,500$ mark the line Accept brackets	367 700 ☒ one part correct
Dividends paid $1\,400\,000 \times 0.15$ $300\,000 \checkmark + 210\,000 \checkmark \checkmark$	510 000 ☒ one part correct
Cost of new delivery vehicles purchased $10\,152\,700 + 425\,000 + 389\,500 - 7\,915\,400 - 2\,250\,000$ $\checkmark \quad \checkmark \quad \checkmark \quad \checkmark \quad \checkmark$	801 800 ☒ one part correct

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5.1.2 Cash effects of financing activities	☒ 1 732 000 one part correct	
Proceeds from shares issued (400 000 x 8.60)	✓✓ 3 440 000	
Funds used to repurchase shares 840 000 ✓✓ + 168 000 ✓	☒ (1 008 000)	
Repayment of loan	✓✓ (700 000)	9

Net change in Cash and Cash equivalents	☒ (77 500) operation	
Cash and cash equivalents in the beginning 45 300 – 2 000	✓ ☒ 43 300 one part correct	
Cash and cash equivalents at the end	✓ (34 200)	4

5.1.3 Calculate the debt/equity ratio		
1 300 000 ✓ : 9 209 000 ✓	☒ 0,1:1 one part correct	3

Calculate the net asset value per share		
$\frac{9\,209\,000}{1\,280\,000} \times 100$	☒ 719 cents one part correct	3

Calculate the return on average shareholders' equity		
$\frac{892\,800}{\frac{1}{2}(6\,458\,200 + 9\,209\,000)} \times 100$ 7 833 600 ✓ ☒ one part correct	☒ 11,4 % one part correct	4

5.1.4 The management decided to change the mark-up % in the current financial year. Was this a good decision? Explain. Quote figures.		
Yes/No ✓ Explanation ✓ figure ✓		
- A decrease in the mark-up% resulted in an increase in sales by 1 650 000 - The gross profit has increased by R262 500 - Gross profit on sales dropped from 43% to 38% - Operating profit on sales did not change, 16%		3

5.1.5 Comment on the management of expenses. Quote TWO relevant financial indicators to support your comment.

Financial indicators and figures ✓ ✓ Comment ✓ ✓

Operating expenses on sales has decreased from 23% in 2018 to 22% in 2019.

The operating profit on sales however, remained unchanged at 16%.

4

5.1.6 Comment on the issue price of the new shares issued on 30 June 2018. Was this fair? Quote figures.

Any three relevant comments ✓ ✓ ✓ ✓ ✓ ✓

- They issued the new shares at 860 cents.
- NAV per share is R7,19 at the end and R6,46 in the beginning.
- Market price per share was R6,30 in the beginning and R7,28 at the end.

6

5.1.7 Comment on the pay-out policy of the company by comparing 2018 to 2019 and quote relevant figures

2018	60/62 = 96,8% ✓ ✓
2019	41/69 = 59,4% ✓ ✓

Any relevant comment ✓ ✓

- 96,8% of the earnings was paid out in 2018 but was decreased to 59,4% in 2019 (by 38%).
- The business decided to retain 40,6% of the earnings in 2019 for further growth.

6

5.1.8 Comment on the degree of risk and gearing of the business. Quote TWO financial indicators with figures.

Financial indicators — with figures ✓ ✓ ✓ ✓

Explanation/comment ✓ ✓

- Debt-equity ratio has improved from 0,3 to 0,1:1
- ROTCE has increased from 13,0% to 15,3%

Comment: The risk has decreased/the company is low geared
It was not necessary to pay a large portion of loan as the company is positively geared – the return is greater than interest on loan (13%).

6

5.1.9 How many shares will a shareholder, having 45% of the issued share capital, have to buy to gain control of the company?

Shares owned = 45% x 1280 000 = 576 000✓

He needs to own at least

50% + 1 = 640 001 shares OR

50% + 100 = 640 100 shares OR

51% = 640 000 shares ✓✓✓

Answer – 576 000 shares

4

5.2**5.2.1 Calculate the following for the Cash Flow Statement:**

Income tax paid $1\,240\,000 - 892\,800$ $12\,000 ✓ + 347\,200 ✓ + 8\,500 ✓$ OR $- 12\,000 - 347\,200 - 8\,500$ mark the line Accept brackets	$367\,700 ✓$ one part correct
Dividends paid $1\,400\,000 \times 0.15$ $300\,000 ✓ + 210\,000 ✓✓$	$510\,000 ✓$ one part correct
Cost of new delivery vehicles purchased $10\,152\,700 ✓ + 425\,000 ✓ + 389\,500 ✓ - 7\,915\,400 ✓ - 2\,250\,000 ✓$	$801\,800 ✓$ one part correct

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5.2.2 Cash effects of financing activities

	$✓ (1\,732\,000)$ one part correct
Proceeds from shares issued (400 000 x 8.60)	$✓✓ 3\,440\,000$
Funds used to repurchase shares $840\,000 ✓✓ + 168\,000 ✓$	$✓ (1\,008\,000)$
Repayment of loan	$✓✓ (700\,000)$

9

Net change in Cash and Cash equivalents	$✓ (77\,500)$ operation
Cash and cash equivalents in the beginning $45\,300 - 2\,000$	$✓✓ 43\,300$ one part correct
Cash and cash equivalents at the end	$✓ (34\,200)$

4

5.2.3 Calculate the debt/equity ratio

1 300 000✓ : 9 209 000✓

☒ 0,1:1

one part correct

3

Calculate the net asset value per share
$$\frac{9\,209\,000}{1\,280\,000} \times 100$$
☒ 719 cents

one part correct

3

Calculate the return on average shareholders' equity
$$\frac{892\,800}{\frac{1}{2}(6\,458\,200 + 9\,209\,000)} \times 100$$

7 833 600 ✓ ☒ one part correct☒ 11,4 %

one part correct

4

5.2.4 The management decided to change the mark-up % in the current financial year. Was this a good decision? Explain. Quote figures.

Yes/No ✓ Explanation ✓ figure ✓

- A decrease in the mark-up% resulted in an increase in sales by 1 650 000
- The gross profit has increased by R262 500
- Gross profit on sales dropped from 43% to 38%
- Operating profit on sales did not change, 16%

3

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Financial indicators and figures ✓ ✓ Comment ✓ ✓

Operating expenses on sales has decreased from 23% in 2018 to 22% in 2019.

The operating profit on sales however, remained unchanged at 16%.

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5.2.6 Comment on the issue price of the new shares issued on 30 June

2018. Was this fair? Quote figures.

Any three relevant comments ✓✓ ✓✓ ✓✓

- They issued the new shares at 860 cents.
- NAV per share is R7,19 at the end and R6,46 in the beginning.
- Market price per share was R6,30 in the beginning and R7,28 at the end.

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2018	60/62 = 96,8% ✓✓
2019	41/69 = 59,4% ✓✓

Any relevant comment ✓✓

- 96,8% of the earnings was paid out in 2018 but was decreased to 59,4% in 2019 (by 38%).
- The business decided to retain 40,6% of the earnings in 2019 for further growth.

6

5.2.8 Comment on the degree of risk and gearing of the business. Quote TWO financial indicators with figures.

Financial indicators – with figures ✓✓ ✓✓

Explanation/comment ✓✓

- Debt-equity ratio has improved from 0,3 to 0,1:1
- ROTCE has increased from 13,0% to 15,3%

Comment: The risk has decreased/the company is low geared
It was not necessary to pay a large portion of loan as the company is positively geared – the return is greater than interest on loan (13%).

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5.2.9 How many shares will a shareholder, having 45% of the issued share capital, have to buy to gain control of the company?

Shares owned = 45% x 1280 000 = 576 000✓

He needs to own at least

50% + 1 = 640 001 shares OR

50% + 100 = 640 100 shares OR

51% = 640 000 shares ✓✓✓

Answer – 576 000 shares

4

5.3

5.3.1 Cash generated from operations note to the Cash Flow Statement.

Net profit before tax	✓✓ 668 000
Adjustment for:	
Depreciation	356 000
Interest expense	104 000
Operating profits before changes in working capital	1 128 000
Changes in working capital	operation ☒ 22 000
Decrease in inventory	*✓ ☒ 134 800
Increase in debtors	*✓ ☒ (32 000)
Decrease in creditors	*✓ ☒ (80 800)
Cash generated from operations	☒ 1 150 000 operation

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* one mark for correct amount and one mark for correct use of brackets

5.3.2 Cash Flow Statement

Cash flow from operating activities operation	☒ 579 780
Cash generated from operations one part correct	☒ 1 150 000
Interest paid	✓ (104 000)
Dividends paid (120 000 ✓ + 176 000 ✓) one part correct	☒ (170 220)
Taxation paid (4 220 ✓ – 187 040 ✓ + 12 600 ✓)	☒ (296 000)
Cash flow from investing activities operation	☒ (984 680)
Fixed assets purchased (5 137 460 ✓ + 356 000 ✓ – 4 348 780 ✓) one part correct	☒ 1 144 680
Change in fixed deposit	✓✓ 160 000
Cash flow from financing activities	320 000
Sale of shares	2 000 000
Shares re-purchased	(1 080 000)
Change in loan	(600 000)
Net change in cash and cash equivalents operation	☒ (84 900)
Cash and cash equivalents at beginning	✓ 69 400
Cash and cash equivalents at end operation	✓ ☒ (15 500)

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5.3.3 Calculate: Current ratio

827 200 ✓ : 479 700 ✓
1,7 : 1 ☒ one part correct must be x:1

3

Calculate: Debt-equity ratio

1 000 000 ✓ : 4 784 960 ✓
0,2 : 1 ☒ one part correct must be x:1

3

Calculate: Net asset value per share

$$\frac{4\,784\,960}{760\,000} \times \frac{100}{1}$$

629,6 cents ☒ one part correct

3

5.3.4

On 1 July 2018 additional shares were issued at R10 each. Will the existing shareholders be satisfied with this price? Explain. Quote relevant financial indicators with figures in your explanation.

Yes/No ✓

Explanation ✓✓ valid financial indicator with figures ✓✓

Compare R10 to the NAV 629,6 cents

Compare R10 to market price 512 cents

5

5.3.5

The directors decided to pay back a large portion of the loan. Do you think that this was a wise decision? Quote TWO relevant financial indicators and figures to support your answer.

Yes ✓

Quoting valid indicators and figures

Debt – equity ratio ✓ improved from 0,4 : 1 to 0,2 : 1 ✓ (low geared)

ROTCe ✓ increased from 13,2% to 14% ✓ positively geared

Explanation

The business return is higher than the current interest rate on loans (12%) and is therefore positively geared. ✓✓

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5.3.6

Besides paying back the loan, the directors have taken other major decisions that have affected the cash balances. State **TWO** other major decisions (exceeding R400 000) and quote the figures from the Cash Flow Statement. In **EACH** case, state how the decision will affect the future of the company.

DECISION Decision ✓ ✓ and amount ✓ ✓	FUTURE EFFECT ON COMPANY Valid explanation ✓ ✓
Purchase of fixed assets – R1 144 680	• Capital growth – investment in fixed assets will lead to expanded business activities. • Creation of employment • Cater for more customers to increase profits
Issue of shares – R2 000 000	• Financing expansions/ extensions • Expanded shareholder base will affect dividends • Improve cash flow
Repurchase of shares – R1 080 000	• Large cash outlay led to overdraft. • Could result in cash flow problems

5.4.1 Notes to the Financial Statements

	Calculations	Answer
2	A. 1 900 000 – 1 100 000	800 000 ✓✓ no part marks
7	B. Vehicle 1 One mark 500 000 x 20/100 = 100 000 but only 49 999 ✓✓	
	Vehicle 2 437 500 x 20/100 x 9/12 65 625 ✓✓	185 624 ✓ One part correct
4	Vehicle 3 350 000 x 20/100 70 000 ✓✓	
	C. See B 437 500 ✓ – (87 500 ✓ + 65 625 ✓) 153 125 two marks	284 375 ✓ One part correct
3	D. 300 000 – 120 000 = 180 000 ✓ – 81 000 ✓	99 000 ✓ One part correct

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5.4.2 Ordinary share capital

Authorised 2 000 000 shares
Issue

800 000	Shares issued at the beginning @ R7	5 600 000
200 000	shares issued during the year @ R9.80	1 960 000 ✓
(120 000) ✓	Buy-back of shares at R7.56 ✓	(907 200) ✓
880 000 ✓	Shares issued at the end Operation	6 652 800 ✓

6

5.4.3 Calculations of figures to appear in the Cash Flow Statement

Calculations	Answers
Dividends paid + 230 000 ✓ + 514 000 ✓ – 290 000 ✓ 224 000 two marks Operation one part correct – 230 000 – 514 000 + 290 000 choose the line	454 000 ✓
Tax paid + 243 000 ✓ – 28 000 ✓ – 45 000 ✓ Operation one part correct – 243 000 + 28 000 + 45 000 choose the line	170 000 ✓

4

4

5.4.4	Cash flow from financing activities		
	Proceeds on shares issued	1 960 000	✓
	Buy back of shares (120 000 X 10)	(1 200 000)	✓✓
	Changes in loan	340 000	✓
	Operation one part correct	1 100 000	☑

5

5.4.5 The directors have taken significant decisions which will be reflected in the Cash Flow Statement. Identify TWO of these major decisions and quote figures. In each case give one consequence of the decision to the business.

Any two valid decisions and consequences		Consequence marked with a decision
Decision ✓	Figure ✓	Consequences ✓
Proceed on shares issued by R1 960 000		To finance the purchases of fixed assets and to finance the repurchased shares.
Purchases of fixed assets by R 1 270 000		Productivity will increased and the business will have more fixed assets
Buy-back of shares by R 1 200 000		To reduce the dividends and shareholders' equity. Improve NAV/EPS.

6

5.4.6 Percentage Operating Profit on Sales

$$\frac{952\,000 \checkmark}{3\,400\,000 \checkmark} \times \frac{100}{1}$$

= 28% ☑ operation one part correct

3

5.4.7 Briefly explain ONE consequence that might be faced by directors and ONE consequence for majority shareholder.

Any valid point ✓✓ ✓✓

Directors

- Directors might lose their job.
- Lose customer or investors because of the fraud/tarnished image.
- Directors might lose trust from minority shareholders.

Majority shareholder

- Shares will lose value in JSE.
- Business can be liquidated.

4

5.5.1

Your friend is of the opinion that the liquidity position of Westland Ltd. is better than that of Northwood Ltd. Quote TWO financial indicators (with figures) to support her opinion.

Quote TWO financial indicators.

Candidate must compare both companies

Any two financial indicators ✓✓ Figures for both companies ✓✓ Explanation ✓✓

- Current ratio of Northwood Ltd is 3,6 : 1 and Westland Ltd. is 2,4 : 1
- Acid-test ratio of Northwood Ltd is 0,6 : 1 and Westland Ltd. is 1,2 : 1
- The stock turnover rate of Northwood Ltd. is 4 times and Westland Ltd. is 8 times

Explanation

- Westlands Ltd. has a better current ratio and is able to cover current liabilities whereas Northwood Ltd's. ratio is too high – funds tied up in stock (current assets)/not used profitably
- Westlands Ltd. has a better Acid-Test Ratio than Northwood Ltd. Northwood Ltd. has too much stock on hand which resulted in the poor Acid-Test Ratio
- Westlands Ltd. is selling its stock faster (8 times) during the year as compared to Northwood Ltd. (4 times).

6

5.5.2

Northwood Ltd. paid off a large portion of its loan during the financial year. Quote TWO financial indicators with relevant figures to show why this was not a good decision taken by the directors.

Financial indicators and figures ✓✓ ✓✓

Valid comment ✓✓

Relevant financial indicators:

Debt: equity is 0,2 : 1

ROTCE: is 18,4%

Comment

The company is at low risk. Therefore there was no need to pay a large portion of the loan.

It is also positively geared. The ROTCE (18,4%) is higher than the interest rate of 10,5%.

6

5.5.3

Will the shareholders be satisfied with the price at which the new shares were issued for both companies? Explain. Quote relevant financial indicators and figures for each company.

	Northwood Ltd.	Westland Ltd.
Yes/No	NO	YES
Relevant indicator and comment Explanation ✓ ✓ Figures ✓ ✓ Must indicate MP & NAV	They sold the shares at 260 cents under the market price (450 cents compared to 710 cents). Selling price is also 85 cents less than the NAV of 535 cents. Existing shareholders are being disadvantaged (260 x 189 000= R491 000). Could have raised more money if they increased the price	They sold the shares at 290 cents above the market price (1200 cents compared to 910 cents). Selling price is also 80 cents more than the NAV of 1 120 cents. Existing shareholders and directors should be happy to raise additional income (280 x 189 000= R529 200).

4

5.5.4 Your friend owns 30 000 shares in each of the companies.

	Northwood Ltd.	Westland Ltd.
Calculate the dividends that he earned from each company.	30 000 x R2,30 = R69 000 ✓	30 000 x R2,45 =R73 500 ✓
Compare and comment on the dividend pay-out policies of the two companies. Provide calculations in your explanation.	DPS 230 cents EPS 350 cents Distributes 66% ✓ (230/350) of earnings. OR Northwood Ltd. decided to retain 34% of its EPS.	DPS 245 cents EPS 285 cents Distributes 86% ✓ (245/285) of earnings. OR Westland Ltd. decide to retain only 14% of its EPS.
Explain ONE reason for the dividend pay-out of each company.	Northwood Ltd. appears to have plans for growth (better long-term benefits) / equalisation of dividends over time. ✓✓	Westland Ltd. appears to keep shareholders satisfied by giving them good dividends. ✓✓

8

6.1**6.1.1 Briefly explain the role of an independent auditor.**

Valid explanation ✓✓

- Protects the interest of the shareholders.
- To express an independent opinion on the fair presentation of the financial statements.

2

6.1.2 Explain why the independent auditor mentioned IFRS and the Companies Act in the audit report.

Valid explanation ✓✓

- The financial statements must be comparable to those prepared by companies internationally.
- To comply with the Companies Act which controls companies.

2

6.1.3 Provide TWO possible consequences of this audit report on the market price of the shares.

Any two valid explanations ✓✓ ✓✓

- Negative image of the company (bad publicity).
- Potential investors and shareholders would lose confidence in the company and directors and would not want to invest in the company.
- Share price of the company will drop (supply and demand).
- Current shareholders will lose confidence in the company and directors and will try to sell their shares.

4

6.2 AUDITING

6.2.1 **Explain why the shareholders would be satisfied with this audit report.**

Any ONE relevant answer ✓✓

- This is a positive report / clean report / in accordance with IFRS or Companies Act.
- This is an unqualified report / the report was fairly presented as per the auditor's opinion.
- The auditors did not mention any irregularities / shortcomings in the financial statements.

2

6.2.2 **Tello Motloun, the managing director, has informed the auditors that he intends to buy the unissued shares for himself without informing the other shareholders. What advice should the auditors give to Tello? Explain.**

Valid explanation ✓✓

- Advice – This is unethical and the issue of new shares should be advertised to all according to the Memorandum of Incorporation / Companies Act.
- It is unethical as it constitutes insider trading.

2

6.2.3 **Explain why the auditors found it necessary to stipulate the page numbers in the report.**

Any ONE valid explanation ✓✓

- They are only responsible for the pages that they have stipulated in the report / only financial statements on Pages 23 – 89 were subjected to audit / examination.
- They are not accountable for the other information in the annual report.

2

6.2.4 **Explain TWO major consequences for Mxo and Frank should they be negligent in performing their duties.**

Any TWO explanations ✓✓ ✓✓

- Not to be re-appointed as auditors
- Face disciplinary procedures by the professional body
- Lose clients / fired by shareholders (because their integrity would be questioned)
- Can be sued

4

6.3 AUDIT REPORT**6.3.1 Explain why the auditors did specifically address the report to shareholders?**

They are the owners of the business. ✓✓

2

6.3.2 Explain why the independent auditors referred to pages 25-51 in the report.

Any valid explanation ✓✓

Part-marks for unclear / incomplete answers

- Auditors are responsible for only parts / certain pages of the annual report.
- They are not accountable for the other information in the annual reports.
- Financial statements on pages 25–51 were subjected to audit / examination.
- Additional information, such as corporate social investment matters, is not audited.

Do not accept statistical sampling as a reason.

2

6.3.3 The directors claimed that the value of the buildings increased over the years and that the value must be increased and shown as additions in the fixed asset note.

As the independent auditor, what advice would you give? Provide ONE point.

ONE valid point ✓✓

Part-marks for unclear / incomplete answers

- It is fraudulent to indicate revaluation as an addition
- No audit evidence exists, so there is no proof of the actual value of the buildings
- GAAP prescribes the historical (original) cost principle when recording assets
- Only physical acquisitions/expansions can be shown as additions

2

6.3.4 The company received a/an (unqualified/qualified/disclaimer) audit report.

Qualified ✓

Give a reason for your answer.

The auditors queried the increase of the assets in the Balance sheet. ✓

2

6.4

6.4.1 Choose the correct word from those in brackets and explain your choice.

Graafwater Ltd received a/an (qualified/unqualified/disclaimer of opinion) audit report.

Choice :

Disclaimer of opinion ✓

Explanation:

Auditors could not find sufficient audit evidence to express opinion ✓✓

3

6.4.2 Briefly indicate how this audit report would possibly affect the shares of Graafwater Ltd on the Johannesburg Securities Exchange (JSE). Mention TWO points.

Any TWO valid points ✓✓ ✓✓

- Potential investors and shareholders would lose confidence in the company and directors and would not want to invest in the company
- Current shareholders will lose confidence in the company and directors and will try to sell their shares
- Share price of the company will drop (supply and demand)
- Negative image of the company (bad publicity)

4

6.4.3 You have been appointed as the external auditor of Graafwater Ltd. The managing director, Laetitia Witbooi, has asked you to reflect her directors' fees of R5 million under 'Salaries and wages' in the Income Statement. Would you agree to her request? Give a reason for your answer.

Would you agree?

No ✓

Reason: Explanation of reason ✓✓

This is a material amount which is of interest to the shareholders who have appointed the directors. (GAAP materiality concept).

The Companies Act No. 71 of 2008 and King Code requires for the director's fees to be disclosed separately

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