



AUE1601

May/June 2013

LEGAL ASPECTS IN ACCOUNTANCY

Duration 2 Hours

100 Marks

EXAMINERS
FIRST
SECOND

MRS C ROETS
MR FN VAN NIEKERK

Use of a non-programmable pocket calculator is permissible

Closed book examination

This examination question paper remains the property of the University of South Africa and may not be removed from the examination venue

THIS PAPER CONSISTS OF **SEVEN (7)** PAGES.

This paper consists of the following questions and main topics:

QUESTION	MAIN TOPIC	MARKS
1	Sundry Companies Act issues	13
2	Issuing of shares, Consideration for shares, Directors personal financial interest, Disposal of the major part of a company's assets, Dividends; Companies secretary	70
3	Rotation of auditors, Audit committee, Public interest score	<u>17</u>
		<u>100</u>

NOTE:

The main objective of the examination is to test a candidate's knowledge and ability to apply the study material, although the examiners will also take into account the candidate's ability to organise and present that knowledge in writing and according to an acceptable standard

[TURN OVER]

In this paper, references to the Companies Act is to the Companies Act 71 of 2008, as amended, of the Republic of South Africa

QUESTION 1

13 marks

Webber Productions Ltd ("Webber Productions") is a company operating in the theatre production industry. Mr Andrew Webber, and his brother Lloyd Webber are both shareholders and directors of the company. The company has an authorised and issued share capital of 100 000 shares.

REQUIRED

Marks

- 1.1 During the financial year under review, a loan was made by Webber Productions to Ms Eva Peron. Ms Peron and Mr Andrew Webber are not married, but they have been living together for several years with their two children.

Are Andrew Webber and Eva Peron related persons in terms of the related persons definition in section 2 of the Companies Act? Motivate your answer **(1½)**

- 1.2 In order to grant a loan to Eva Peron, Webber Productions is required inter alia, in terms of the Companies Act, to meet the solvency and liquidity requirements. The loan should also have been approved during the previous two years, by a special resolution of shareholders. Are the following statements true or false? Motivate your answers.

(i) Webber Productions is liquid if it is able to pay its debts as they become due, in the ordinary course of business, immediately after the date of the test **(1½)**

(ii) Unless the Memorandum of Incorporation (MOI) of Webber Productions provides for a lower percentage to constitute a voter's quorum, the quorum for all shareholders' meetings is the presence at the meeting of the holders of at least 75% of the shares entitled to vote **(1½)**

- 1.3 Webber Productions has updated its Memorandum of Incorporation to comply with the Companies Act. Is the following statement true or false? Motivate your answer.

The Memorandum of Incorporation of Webber Productions will state that the company is a personal liability company **(1½)**

[TURN OVER]

- 1.4** The board of Webber Productions wishes to issue 10 000 shares to Phantom (Pty) Ltd (“Phantom”), a company that supplies décor and costumes for theatre productions. The board is further planning to issue another 10 000 shares to the only subsidiary company of Webber Productions, Cats (Pty) Ltd (“Cats”). Are the following statements true or false? Motivate your answers.
- (i) Shares can **only** be issued to Phantom by the board of Webber Productions, if the authorised share capital has been increased by a special resolution before the company issues the shares **(3)**
 - (ii) The rights and limitations attached to shares which are stated in the company’s Memorandum of Incorporation can be altered by a resolution of the board of directors **(1½)**
 - (iii) Cats may not hold more than 10% of any class of shares of Webber Productions and may exercise any voting rights attached to those shares **(1½)**
- 1.5** Cats (Pty) Ltd is considering converting itself into a close corporation. Is this allowed in terms of the Companies Act? Motivate your answer **(1)**

QUESTION 2

70 marks

You are a Chartered Accountant and an expert on the Companies Act.

Bond Ltd (“Bond”) is the official printer and distributor of the popular “Jane Bond” action novel series, written by Ina Flemming. The majority of the company’s income is derived from the printing and selling of the novels. The company also earns royalties from Fox Pictures Ltd, for rights to produce screenplays and films based on the books. These films are screened in leading cinemas all over the world. Bond experienced a substantial increase in turnover during the year, due to the public’s enthusiasm regarding the new “Jane Bond” film, entitled “Falling-Sky”.

[TURN OVER]

Below is an extract of the minutes of the meeting of the board of directors of Bond

BOND LIMITED
MINUTES OF THE MEETING OF THE BOARD OF DIRECTORS HELD ON
31 JANUARY 2013

Present:

Ms Sienna Connery, chairman and independent non-executive director
Mr Percy Brosnan, non-executive director
Mr Danny Craig, sales and marketing director
Ms Rachel Moore, managing director
Mr Thomas Dalton, financial director
Ms Geraldine Lazenby, company secretary

Apologies:

Ms Money Penny, independent non-executive director

Matters for discussion:

1. Investment in Fox Pictures:

Mr Danny Craig indicated that the success of the "Falling-Sky" film resulted in significant growth for the company. To avoid any decline in growth before the next book is published, he suggested that other areas of operation, such as film production and screenplay writing, should be explored. He also proposed the investment and acquisition of 49% of the issued share capital of Fox Pictures. He indicated to the board that, as he is a holder of 20% of the shares in Fox Pictures, he is aware that Fox Pictures is a very successful company. He is also convinced that this acquisition will increase the share value of Fox Pictures. Mr Thomas Dalton questioned how this transaction will be financed since the purchase price of the shares will amount to R1 million. Ms Rachel Moore proposed that the purchase price of R1 million be settled by issuing an additional 200 000 shares in Bond Ltd at a fair market value of R5 per share. Bond Ltd currently has 50 000 unissued authorised shares.

The voting commenced and the proposed transactions to invest in Fox Pictures and to fund the investment with a share issue were approved by **all** of the directors.

2. Disposal of printing machines:

Ms Rachel Moore indicated that Bond currently does not utilise all of the specialised printing machinery that it owns. She subsequently proposed to dispose of seven of the ten machines that the company owns, with a book value of R3 million each.

The voting commenced and the proposal was unanimously accepted. It was deemed unnecessary to inform the shareholders of this decision.

[TURN OVER]

3. Declaration of Dividend

Mr Thomas Dalton presented the financial results for the financial year ended 31 December 2012 which indicated the following

Profit for the year	R12 million
Total assets	R35 million
Total liabilities	R20 million

As at 31 December 2012 the current assets of the company exceeded its current liabilities by R7 million

The directors applied the solvency and liquidity test and resolved to declare a dividend of R5 million due to the company's favourable financial results flowing from the "Falling-Sky" film

4. Resignation of company secretary

Ms Geraldine Lazenby presented her written notice of resignation as company secretary. She indicated her intention to resign from the position with effect from 21 February 2013, as her husband has been offered a job opportunity in the United States

The board approved her resignation, and suggestions were made for one of the following nominees to be appointed at the next board meeting

- Casino Royale Incorporated, the auditors of Bond Ltd
- Quantum of Solace (Pty) Ltd ("Quantum") which is incorporated in Russia. The brother of Mr Dalton, is the managing director of Quantum. He lives in South Africa with his family and previously acted as the company secretary for a few well-known listed companies

The next board meeting is to be held on 1 April 2013

Ms Sienna Connery approached you for advice regarding the resolutions passed at the meeting of the board of directors held on 31 January 2013

REQUIRED

Marks

Refer only to the first agenda point: Investment in Fox Pictures

- 2.1 Discuss whether the purchase price of R1 million can be settled by issuing 200 000 shares at a fair market value of R5 per share in terms of the requirements of the Companies Act by first stating the requirements of the Companies Act and then applying these to the scenario. Use the following headings in your solution

- (i) Issuing of shares (12)
- (ii) Consideration for the shares (3)

[TURN OVER]

REQUIRED (CONTINUED)

Marks

- 2.2 With regard to Mr Craig's personal financial interest in the acquisition of the Fox Pictures shares by Bond Ltd, discuss the legality of Mr Craig's actions, by first stating the requirements of the Companies Act, and then applying these to the scenario (14)

Refer to the second point on the agenda: Disposal of printing machines

- 2.3 List the requirements of the Companies Act for the disposal of the greater part of a company's assets. Do not include any requirements on quorums or voting (5)

- 2.4 Discuss the legality of the disposal of the printing machines in terms of the Companies Act. Do not discuss any requirements regarding quorums or voting. (You should also take into account the financial information supplied in the minutes) (5)

Refer only to the third point on the agenda: Declaration of dividend

- 2.5 Determine whether Bond Ltd satisfies the solvency and liquidity test as defined in the Companies Act, by first stating the requirements of the Companies Act, and then applying these to the scenario (6)

- 2.6 (i) List the requirements of the Companies Act in respect of the declaration of the dividend of R5 million (4)

- (ii) Apply the requirements listed in (i) above to the scenario in order to determine where the Companies Act has been complied with regarding the dividend declaration (4)

Refer only to the fourth point on the agenda: Resignation of company secretary

- 2.7 Discuss the resignation of Ms Lazenby, the company secretary, in terms of the Companies Act (6)

- 2.8 Explain to the board of Bond Ltd which of the candidates nominated for the position of company secretary at Bond Ltd will be permitted to act as such in terms of the requirements of the Companies Act (6)

- 2.9 List any five duties of the company secretary (5)

[TURN OVER]

QUESTION 3

17 marks

You are a director at the audit firm Windsor Incorporated (“Windsor”), together with two (previously three) other auditors, Mr William Windsor and Mr Harry Mountbatten. The following matters require your attention.

Matter 1

Ms Kate Middleton, the auditor in charge of one of Windsor’s audit clients, Buckingham Ltd, resigned from the position of director in the audit firm during the year.

Matter 2

Mr Earl Spencer, the managing director of one of your audit clients, Kensington Ltd, contacted you for advice regarding the composition of the audit committee of Kensington Ltd. He wanted to know if the following persons are allowed to form part of the audit committee, in terms of the Companies Act

- Mr Spencer himself;
- The son of Mr Spencer, since he has chaired audit committees in the past, and
- Ms Sarah Ferguson, an expert on the Companies Act. She is also one of the major customers of Kensington Ltd.

REQUIRED

Marks

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| 3.1 | With reference to matter 1, determine whether a vacancy arose in the position of auditor due to the fact that Ms Middleton, the current auditor of Buckingham Ltd, resigned from Windsor Incorporated, in terms of the requirements of the Companies Act | (3) |
| 3.2 | With reference to matter 2, discuss if Kensington Ltd is required to have an audit committee in terms of the Companies Act | (1) |
| 3.3 | List all the requirements regarding the composition of the audit committee in terms of the Companies Act and discuss the legality of the composition of the audit committee as suggested by Mr Spencer in terms of these requirements | (10) |
| 3.4 | List the four factors that contribute to the calculation of the public interest score of a company | (3) |