

UNIVERSITY EXAMINATIONS



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AUE1601

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LEGAL ASPECTS IN ACCOUNTANCY

Duration : 2 Hours

100 Marks

EXAMINERS :

FIRST :

MRS C ROETS

SECOND :

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	21
2	Appointment of directors; Requirement to have annual financial statements audited; Appointment of directors; Pre-incorporation contracts	52
3	Directors conduct; Protection for whistle-blowers	13
4	Financial assistance in order to purchase shares	<u>14</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 are to the Companies Act 71 of 2008, as amended, of the Republic of South Africa.

QUESTION 1

21 marks

You are an expert in the area of company law. One of your friends, Mr Shawn Spencer and his nephew, Mr Burton Guster, are directors of a company entitled Psych Ltd. Psych Ltd has 20 000 unissued authorised ordinary shares. Mr Spencer posed a couple of questions to you regarding the requirements of the Companies Act.

REQUIRED

Marks

- 1.1 If the memorandum of incorporation of the company does not prohibit it, are the directors of Psych Ltd allowed to dispose of the greater part of the company's assets by means of a board resolution? State yes/no and provide a reason for your answer.
- 1.2 May the directors of Psych Ltd resolve to voluntarily liquidate the company? State yes/no and provide a reason for your answer.
- 1.3 To which role in column A in the table below does each of the statements listed in column B relate?

Column A	Column B
(i) Director	(a) Appointing the directors of a company.
(ii) Shareholder	(b) Informing the directors of any relevant law.
(iii) Audit committee	(c) Duties are determined in terms of the Auditing Profession Act.
(iv) Company secretary	(d) Determine the nature and extent of any non-audit services.
(v) Auditor	(e) Must perform duties in good faith and for proper purpose.

- 1.4 What are the Companies Act requirements that should be met if the board of Psych Ltd wishes to issue 50 000 of Psych Ltd's shares to the public? Limit your answer to the following:
 - authority to issue shares
 - authorised shares available for issue
 - consideration for shares

(1½)

Comment [A1]: No. A special resolution of shareholders is needed. Many students incorrectly refer to a special resolution of the board, or simply to a shareholders resolution = this is incorrect. This question relates to topic 7 of the study guide.

(1½)

Comment [A2]: No. Once again a special resolution of shareholders is required. This question was dealt with in topic 8 of the study guide.

(5)

Comment [A3]: E; A; D; B; C

(2)

(6)

(2)

Comment [A4]: Students did not in all cases keep their answer to this specific points. This question is similar to question 6 of tutorial letter 102. A similar question is also included in assignment 3 in tutorial letter 101. Many students also incorrectly stated that the shares had first to be offered to the existing shareholders – but seeing that this is a public company, such a statement would be incorrect.

[TURN OVER]

Marks

- 1.5** Section 45 of the Companies Act, relating to financial assistance to a director of a company, includes certain instances of financial assistance where this section will not apply. List any three (3) such instances.

(3)

Comment [A5]: This was a straight forward theoretical question. The answer can be found in the table on page 102 of the study guide, study unit 7.2. This question is dealt with in Topic 7 of the study guide.

QUESTION 2

52 marks

You are a chartered accountant and an expert on the Companies Act.

MacLarens (Pty) Ltd ("MacLarens") is a newly incorporated company. The company was incorporated on 28 August 2013 and owns a chain of restaurants all over South Africa called "MacLarens Pub & Grill". The shares of the company are held by Mr Marshall Ericson, one of the directors of MacLarens who holds 20% of the shares, whilst the remaining 80% of the shares are held by 20 of the restaurant managers and 70 other shareholders. The year end of MacLarens is 28 February.

On 1 August 2013, prior to the incorporation of the company, Mr Ericson entered into a written agreement on behalf of MacLarens for the supply of meat products to be used in the restaurants.

Shortly after incorporation, the company obtained a loan from GNB bank in the amount of R125 million, to cover the costs of the initial capital layout of the restaurants and to fund an extensive advertisement campaign. MacLarens does not have any other liabilities. The loan is repayable from 1 March 2014, which is also the date from which interest will accrue.

MacLarens employs on average 120 employees at its various restaurants. The restaurants are already very popular with its customers, and the turnover of the company for the month of September alone was approximately seven million rand (R7 million).

The first board meeting of MacLarens was held on 30 September 2013. At this date the company has not yet appointed an auditor or an audit committee. The memorandum of Incorporation of MacLarens clearly states that no auditor may be appointed if such an auditor was not approved by the audit committee. Below is an extract of the minutes of the meeting of the board of directors of MacLarens, held on 30 September 2013.

[TURN OVER]

**MACLARENS (PTY) LTD
MINUTES OF MEETING OF THE BOARD OF DIRECTORS HELD ON
30 SEPTEMBER 2013**

Present:

Mr. Ted Mosby, chairman and independent non-executive director
Mr. Barney Stinson, non-executive director
Mr. Marshall Ericson, sales and marketing director
Ms. Lilly Aldrin, prospective finance director
Ms. Robin Sherbatsky, prospective managing director
Ms. Pamela Fryman, company secretary

Matters for discussion:

1. Appointment of directors

Mr Mosby proposed that the matter regarding the appointment of Ms Aldrin and Ms Sherbatsky as directors of the company be brought to vote.

Mr Mosby held that Ms Aldrin was a qualified chartered accountant and that she therefore met the requirement of the memorandum of incorporation of MacLarens, namely that the finance director should be a person qualified in the field of accounting.

Ms Sherbatsky has obtained several years of experience as the managing director of another large company in the restaurant industry, before she was dismissed after being accused of dishonesty. Ms Sherbatsky ensured the board that these allegations were not true.

The board voted and all three of the existing directors voted in favour of the appointment of the two directors proposed.

2. Appointment of auditors

Mr Mosby suggested that the medium-sized audit firm, Bays & Thomas Inc, be appointed as the auditor of MacLarens Ltd. Mr Mosby was of the opinion that Bays & Thomas Inc was already very familiar with the business operations of MacLarens, as the firm was involved in the drawing up of the initial business plan of MacLarens and was already responsible for the payroll administration and tax affairs of MacLarens.

Mr Ericson was, however, not comfortable with this suggestion, and stated that he believed an audit was overrated, and that he did not see the need for this appointment.

The board voted and Bays & Thomas was appointed as auditors of MacLarens.

[TURN OVER]

3. Contract with meat supplier

The board resolved that the contract entered into between Mr Ericson (on behalf of MacLarens) and the current meat supplier be rejected in full, as the supplier has thus far proven to be rather pricey.

The next board meeting is to be held on 1 December 2013.

REQUIRED

Marks

2.1 Refer to the first point on the agenda: Appointment of directors

Discuss the legality of the appointment of Ms Aldrin and Ms Sherbatsky as directors of MacLarens in terms of the Companies Act, by first stating the requirements of the Companies Act, and then applying it to the scenario. Exclude from your answer any notice or quorum requirements. Structure your answer as follows:

- Procedures followed to appoint the directors.
- Persson disqualified or ineligible for appointment.

(5)
(7)

Comment [A6]: This question was dealt with in topic 5 of the study guide. You firstly had to discuss the procedure to appoint a director (e.g. appointed by the shareholders; voted on separately etc). Then you had to list the theory related to directors who are disqualified/ineligible for appointment, and you had to make this applicable to the specific scenario.

2.2 Taking the background information in the scenario into account, refer to the second point on the agenda: Appointment of auditors

2.2.1 Discuss whether MacLarens will be required to have its annual financial statements audited for the year ended 28 February 2014, in terms of the Companies Act. Structure your answer under the following headings:

- (i) calculation of the public interest score as at the date of the meeting
- (ii) requirement for a private company to be audited.

2.2.2 Assuming that MacLarens is legally required to be audited, discuss the legality in terms of the Companies Act of the appointment of Bays & Thomas as the auditors of MacLarens, by first stating the requirements of the Companies Act, and then applying it to the scenario. Limit your answer to the following:

- (i) role of the audit committee in the appointment of the auditor, and in determining whether or not the auditor is independent

(6)
(6)

Comment [A7]: Although not exactly the same, this question is similar to question 1.1 of assignment 2 in tutorial letter 101. The question differed in that the calculation and discussion was each limited to 6 marks, and also, the company has just started, therefore it should have been stated that the turnover will in all probability still increase.

2.3 Taking the background information in the scenario into account, refer to the third point on the agenda: Contract with meat supplier

Discuss the legality and consequences of the decision to reject the contract entered into between Mr Ericson (on behalf of MacLarens) and the meat supplier by first stating the requirements of the Companies Act and then applying it to the scenario. Omit any notice or quorum requirements from your answer.

(15)

Comment [A8]: This question is dealt with in Topic 6 of the Study guide. The theory in the question was taken from the table on pg 87 of the study guide. Many students incorrectly listed the composition requirements of the audit committee or listed all duties of the audit committee.

(13)

Comment [A9]: This question is dealt with in topic 2 of the study guide. The solution is exactly the same as that for Activity 1 on pg 22 and 23 of the Study guide

[TURN OVER]

QUESTION 3

13 marks

Big Bang (Pty) Ltd (“Big Bang”) is a company that manufactures children’s toys. During the year under review it was discovered that one of the directors of the company, Mr Sheldon Cooper, submitted fraudulent tax returns to the South African Revenue Service (SARS) on behalf of the company.

His neighbour, Mr Leonard Hofstadter, came to know of this incident while having Mr Cooper over for a “braai” at his house. Even though Mr Hofstadter is not related to Big Bang, he nevertheless reported the matter to the head of the audit committee of Big Bang, Mr Howard Wolowitz. Mr Hofstadter believes that he will be protected in terms of section 159 of the Companies Act, “protection for whistle-blowers”, as he acted in good faith.

Mr Wolowitz in turn contacted you for advice on the matters below:

REQUIRED

Marks

- 3.1 Discuss the submission of the fraudulent tax returns to SARS by Mr Cooper (list the requirements of the Companies Act and apply it to the scenario) with regards to the directors conduct.
- 3.2 List the persons who will be protected in terms of section 159 of the Companies Act “protection for whistle-blowers” and conclude whether or not Mr Hofstadter will enjoy protection in terms of this section.

(5)

Comment [A10]: This question is dealt with in topic 5 of the study guide.

(8)

Comment [A11]: The question is dealt with in topic 8 of the study guide. Full marks could have been obtained by simply listing all the persons protected by this section.

QUESTION 4

14 marks

You are a chartered accountant and the auditor in charge of the audit of CBI Ltd (CBI), a company that is involved in the import and retail of motor vehicles. CBI does not lend money in the ordinary course of its business. Below is an extract of the financial statements of CBI for the year ended 30 September 2013 (year under review).

Assets	R'000
Current assets	2 500
Non-current assets	<u>3 000</u>
	5 500
Liabilities	
Current liabilities	3 500
Non-current liabilities	<u>1 000</u>
	4 500

During your inspection of the minutes of the directors’ meetings of CBI held during the year, the following two related matters came to your attention:

[TURN OVER]

1. A loan in the amount of R750 000 has been granted to an unrelated third party, Mr Patrick Jane. The decision to grant the loan to Mr Jane was approved by the CEO (Chief Executive Officer) of CBI, Ms Theresa Lisbon. The loan is to be repaid in fixed monthly instalments, over a period of one year, at an interest rate of 15%. The prime interest rate is currently 8.5%.
2. 100 000 CBI shares were issued at its market value of R7,50 per share, to Mr Patrick Jane. All the Companies Act requirements were met regarding the share issue.

REQUIRED

Marks

Discuss the legality of the granting of the loan to Mr Patrick Jane in order to purchase shares in CBI, by first listing the requirements of the Companies Act, and then applying it to the scenario. Exclude from your answer any notice and quorum requirements.

(14)

Comment [A12]: This question is dealt with in topic 7 of the study guide. It has similarities to question 2.2 of the written assignment. The question however deals with a loan for the specific purpose of purchasing shares (section 44).