



AUE1601

October/November 2013

LEGAL ASPECTS IN ACCOUNTANCY

Duration 2 Hours

100 Marks

EXAMINATION PANEL AS APPOINTED BY THE DEPARTMENT.

Use of a non-programmable pocket calculator is permissible.

Closed book examination

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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	32
2	Reckless trading, Financial assistance, Auditors, Audit committees, Dismissal of directors	55
3	Shareholders meetings and resolutions	<u>13</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

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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

32 marks

You are an expert in the area of company law. Elementary Ltd (“Elementary”) is a new company, specialising in home décor and renovations, founded by Mr. Sherlock Holmes.

The company plans to appoint new directors at the upcoming annual general meeting. Mr. Holmes is unsure about all the legal requirements regarding directors, as well as the way meetings should be conducted. He is also quite nervous about the company being audited, as he is not quite sure what an audit entails. Furthermore, Mr. Holmes is worried about the course of action should the company not succeed, and has directed questions to his accountant, Ms. Watson, regarding the process of liquidation and the selling of the company's assets, should the need ever arise.

Ms. Watson has in turn contacted you, as her Companies Act knowledge is not up to date. Your task is to respond to the queries below.

REQUIRED

Marks

1.1 Give **four (4)** examples of when a special resolution is required **(4)**

1.2 Complete the following table by indicating the minimum number of directors required for each of the following categories of company

Category of company	Minimum number of directors
Private company (Pty) Ltd	(i)
Personal liability company (Inc)	(ii)
Public company (Ltd)	(iii)
Non-profit company (NPC)	(iv)

(2)

1.3 The Companies Act provides that certain persons are either not eligible to be appointed as directors, or are disqualified from being appointed as directors. Name any **four (4)** of these persons **(4)**

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REQUIRED	Marks
<p>1.4 When the directors of a public company are conducting a meeting, certain individuals may not be included in determining the quorum for that meeting. Indicate whether the following individuals can be included, by writing “yes” or “no”, and providing a reason for your answer</p> <ul style="list-style-type: none">(i) The company secretary, who is not a director of the company(ii) The auditor of the company(iii) The financial director of the company	(6)
<p>1.5 The Companies Act provides that a director must at the earliest possible opportunity communicate any information concerning the company that came to his attention, to the board of directors. However, there are certain instances where this is not necessary. Name any one such instance</p>	(1)
<p>1.6 In terms of the Companies Act, the auditor has certain rights to records and information of a company that is being audited. Indicate whether each of the following statements are true or false, and provide reasons for your answers in each case</p> <ul style="list-style-type: none">(i) At all times the auditor has the right of access to the accounting records, documents and storage warehouses of the company(ii) The auditor may attend any directors meeting held during the year(iii) The auditor has the right to receive all notices of any shareholder meetings and any other communication concerning transactions conducted by the company	(6)
<p>1.7 Discuss the Companies Act requirements, should Mr Holmes decide to sell all of the assets of the company</p>	(5)
<p>1.8 Will Elementary Ltd need to have its public interest score calculated to determine whether or not it needs to be audited in terms of the Companies Act? State “yes” or “no”, and provide a reason for your answer</p>	(2)
<p>1.9 The Companies Act provides that a solvent company may be liquidated in two instances. Name these two instances</p>	(2)

QUESTION 2

55 marks

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

Rocknroll Ltd ("Rocknroll") is a company conducting business in the music industry. The company imports and sells new musical instruments, purchase and restore second hand instruments, and provides tuning and moving services for pianos and organs

The chief executive officer (CEO) of the company, Mr Elvis Presley contacted you and explained that he was very concerned about the attitude and performance of one of the directors, Ms. Marilyn Monroe. He is also aware that she is not willing to resign as director of

Rocknroll. He further expressed his concern regarding the current financial performance of the company. Mr Presley also brought to your attention the fact that there were several unresolved issues resulting from the previous directors meeting, and asked for your advice regarding these issues

The following extract is from Rocknroll's annual financial statements for the year ended 30 June 2013

	2013 R
ASSETS	
Total Non-Current Assets	6 000 000
Total Current Assets	<u>2 000 000</u>
	<u>8 000 000</u>
LIABILITIES	
Total Non-Current Liabilities	5 000 000
Total Current Liabilities	<u>5 000 000</u>
	<u>10 000 000</u>

Below is an extract of the minutes of a meeting of the board of directors of Rocknroll, pointing out these unresolved issues

ROCKNROLL LIMITED
MINUTES OF MEETING OF THE BOARD OF DIRECTORS HELD ON
28 AUGUST 2013

Present:

Ms Nancy Sinatra, chairman and independent non-executive director
Mr Steven Tyler, non-executive director
Mr Michael Jackson, sales and marketing director
Ms Marilyn Monroe, finance director
Mr Elvis Presley, managing director
Ms Laura Brannigan, company secretary

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Apologies:

Mr Elton John, non-executive director

Matters for discussion:

1. Loan granted to Mr. Elton John

Ms Monroe indicated that she has approved and issued a loan to Mr Elton John. Mr John will use the cash to start a piano rental and training company. He will repay the loan as soon as his company starts making a profit. As Mr John is expecting a significant profit, seeing that his overheads will be quite low, Ms Monroe is of the opinion that it was a reasonable decision to grant this loan.

Mr Presley stated that Ms Monroe neither followed the appropriate channels to get this loan approved nor did she consult the Memorandum of Incorporation of the company, and that he was uncertain about the course of action to be taken, as the company has never before granted a loan of this nature.

2. Resignation and appointment of auditors

Rocknroll's auditor, Jazz Incorporated, was asked to resign following a disagreement with the management of Rocknroll concerning the accounting treatment of certain transactions.

Mr Presley recommended Blues Incorporated to the audit committee of Rocknroll, to be considered for appointment as the new external auditors. Mr Presley feels that this will be of great benefit to Rocknroll, as his wife, Priscilla Presley, is one of the partners of Blues Incorporated. She will thus have a very good understanding of Rocknroll's operations.

The board was undecided on this matter.

3. Duties of the audit committee

Ms Nancy Sinatra raised the issue that the audit committee of the company currently only has one other member, besides herself. Mr Presley disagreed with her, and explained to her that he believed it not to be an issue, as the only necessary duties of the audit committee are

- to ensure that the appointment of the auditor complies with the provisions of the Companies Act 71 of 2008, as amended, and any other legislation relating to the appointment of auditors,
- to perform other functions determined by the board of directors, including the development and implementation of a policy and plan for a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes within the company,
- to pre-approve any proposed agreement with the auditor for the provision of non-audit services to the company.

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4. Dismissal of director

Mr Presley suggested that another point be added to the board agenda – the dismissal of Ms Monroe as a director, due to her continuous reckless and negligent actions Ms Monroe expressed her surprise, as she did not expect Mr Presley to make such a suggestion She strongly recommended the matter to be discussed at the next board meeting

The next board meeting is to be held on 1 April 2014

REQUIRED

Marks

- 2.1 Refer only to the extract from the financial statements in the scenario:**
- Discuss whether Rocknroll Limited is trading recklessly in terms of the requirements of the Companies Act 71 of 2008, as amended (6)
- 2.2 Taking the financial information of the company into consideration as per the extract from the financial statements, refer to the first point on the agenda: Loan to Mr. Elton John**
- Discuss the legality in terms of the Companies Act, 2008, with regards to the loan to Mr Elton John by
- (i) stating the requirements of the Companies Act that should be met (6)
 - (ii) applying the requirements listed in (i) to the scenario (8)
 - (iii) concluding on whether or not the granting of the loan was in fact legal (1)
- 2.3 Refer to the second point on the agenda: Resignation and appointment of auditors**
- Discuss the requirements of the Companies Act 71 of 2008, as amended, for the appointment of Blues Incorporated as the new external auditor of Rocknroll Limited, **only** in terms of the following
- (i) Requirements to be met in order to be appointed as the auditor of a company and whether or not Ms Presley may be appointed (7)
 - (ii) Requirements to be met where a vacancy arises in the office of an auditor (3)
 - (iii) Considerations to be taken into account in order to determine whether or not Blues Incorporated is independent (5)
- 2.4 Refer to the third point on the agenda: Duties of the audit committee**
- List the remaining duties of the audit committee which Mr Presley is not aware of in terms of the Companies Act 71 of 2008, as amended (11)

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2.5 Refer to the fourth point on the agenda: Dismissal of director

Advise Mr Presley regarding the issue of dismissing Ms Monroe from her position as director of Rocknroll Limited, by explaining the requirements of the Companies Act in this regard, to him

(8)

QUESTION 3

13 marks

Designers Ltd is a large clothing manufacturing company. The company's board is chaired by Mr Jimmy Choo, and the company has 20 ordinary shareholders.

The financial director of the company, Mr Roberto Cavalli, has informed Mr Choo of his plan to obtain additional finance for the company, to the amount of R15 million, by issuing additional ordinary shares to the directors of the company. The company however has no authorised shares left in issue, and the number of authorised shares will therefore have to be increased.

These matters will be decided on at the upcoming annual general meeting of shareholders.

REQUIRED

Marks

- 3.1** Discuss whether the decision to issue shares to the directors will require an ordinary or a special resolution in terms of the Companies Act **(2)**
- 3.2** Discuss the requirements of the Companies Act that will have to be met with regards to conducting the upcoming shareholders meeting **only** with regards to the meeting itself. Include in your answer the requirements for notices, quorums, and voting on the resolutions. (Do not refer to the requirements where a quorum is not present, or to the involvement of proxies.) **(11)**