Monyetla Project – Accounting Gr 12

Lesson 5: Companies: Analysis and Interpretation, Audit Report and Corporate Governance

ACTIVITY 1: MORE LIMITED

COMPANIES – AUDIT REPORT AND CORPORATE GOVERNANCE

(15 marks; 12 minutes)

1.1 Choose an explanation from column B that matches the term in column A. Write only the letter (A – D) next to the question numbers (1.1.1 to 1.1.4) in the ANSWER BOOK.

COLUMN A		**COLUMN B**	
1.1.1	King Code	A	Impact of business activities on the profit, as well as the effect on the environment and social issues.
1.1.2	Triple-Bottom Line	B	Explains the performance of the company and the major decisions that were taken.
1.1.3	Directors' Report	C	Review and monitor the fee policies to ensure that they are fair.
1.1.4	Remunerations committee	D	This sets out the ethical and effective leadership expected of companies.

(4)

1.2 AUDIT REPORT

An extract of the Audit Report of More Limited is provided.

REQUIRED:

1.2.1 Where, why and when is this audit report expected to be presented? (3)

1.2.2 Provide TWO points why the independent auditors make reference to pages 12 – 30 of the Annual Report. (4)

1.2.3 Explain TWO points on the impact of this report on the company. (4)

INFORMATION:

Extracts from the Audit Report:

To shareholders:
We have audited the financial statements set out on pages 12 – 30….

Opinion:
We have not been able to obtain sufficient audit evidence on significant matters identified and described in the paragraph "basis for opinion"; as such we are unable to express an opinion on the reliability of the financial statements.

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ACTIVITY 2: HADLEY LTD

COMPANIES: ANALYSIS AND INTERPRETATION **(40 marks; 32 minutes)**

The given information relates to Hadley Ltd. The company has an authorised share capital of 900 000 ordinary shares. The financial year ended on 28 February 2019.

REQUIRED:

2.1 **Refer to Information A and B.**

Calculate the missing figures indicated by **(a)** to **(e)** in the Fixed Asset Note below. (17)

2.2 Calculate the Debt-Equity ratio for 2019.
(Round-off to TWO decimal points.) (3)

2.3 The directors decided to increase the loan during the current financial year. Explain TWO financial indicators to indicate why this was a good decision. Quote figures. (8)

2.4 The board of directors is of the opinion that the shareholders should be happy with their percentage return and the market price of their shares. Quote and explain TWO financial indicators with figures to support their opinion. (6)

2.5 The Cash Flow Statement reflects some important decisions taken by the Directors.

Apart from the loans, identify TWO good decisions. Explain the effect of these decisions on the company. Quote figures. (6)

INFORMATION:

A Extract from the Balance Sheet on 28 February

	2019	**2018**
Land and Buildings	5 800 000	6 800 000
Vehicles	2 700 000	?
Equipment	?	850 000
Accumulated depreciation on vehicles	?	960 000
Accumulated depreciation on equipment	?	180 000
Trade and other receivables	405 750	168 300
Shareholders' equity	**11 000 250**	**10 200 000**
Ordinary share capital	10 260 000	9 000 000
Retained income	740 250	1 200 000
Mortgage loan SS Bank	2 100 000	1 380 000
Trade and other payables	**592 200**	**763 950**

B Fixed Asset Note

	Land and Building	**Vehicles**	**Equipment**
Carrying value on 28 Feb 2018	6 800 000	840 000	**(c)**
Cost	6 800 000	**(b)**	850 000
Accumulated depreciation	0	(960 000)	(180 000)
Movements			
Additions at cost		900 000	400 000
Disposals	**(a)**	0	**(d)**
Depreciation		(171 000)	**(e)**
Carrying value on 28 Feb 2019	5 800 000		
Cost	5 800 000	2 700 000	
Accumulated depreciation			

Land and Building

- Part of the Land and Building was sold at carrying value during the financial year.

Vehicles

- A new delivery van was bought on 1 November 2018.
- No vehicles were sold during the financial year.

Equipment

- A printer bought for R150 000 on 1 March 2016, was sold at carrying value on 31 August 2018.
- A new printer was purchased on 31 August 2018.
- Depreciation on equipment is written-off at 10% p.a. on the cost price.

C Cash Flow Statement on 28 February 2019:

Cash flow from operating activities	**(344 715)**
Cash generated from operations	2 656 185
Interest paid	(208 800)
Dividends paid	(2 134 500)
Taxation paid	(657 600)
Cash flow from investing activities	**(187 500)**
Purchase of fixed assets	(1 300 000)
Proceeds from sale of fixed assets	1 112 500
Cash flow from financing activities	**1 944 000**
Proceeds from shares issued	1 800 000
Repurchase of shares	(576 000)
Increase in loan	720 000
Net change in cash and cash equivalents	**1 411 785**
Cash and cash equivalents beginning of year	1 429 465
Cash and cash equivalents end of year	**2 841 250**

D Financial indicators on 28 February:

	2019	**2018**
Earnings per share	252 cents	110 cents
% return on average shareholders' equity (ROSHE)	15,7%	12,3%
% return on average capital employed (ROTCE)	20,9%	21,3%
Net asset value per share	1 608 cents	1 700 cents
Debt-equity ratio	?	0,13:1
The market price of shares on the JSE	1 680 cents	1 560 cents
Interest on alternative investments	7,5%	6,5%
Interest on loans	12,0%	10,5%

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ACTIVITY 3: LOCK LTD & DOWN LTD

COMPANIES – INTERPRETATION OF COMPANY INFORMATION

(35 marks; 25 minutes)

You are presented with financial information of two companies operating in the same industry and of similar size, for the year ended 29 February 2020.

REQUIRED:

NOTE: Provide figures, financial indicators or calculations in EACH case to support your comments and explanations.

3.1 Compare the liquidity position of both companies and comment on the company is managing the short term assets more effectively. (6)

3.2 Compare the dividend pay-out policy of each company. (4)

Provide TWO possible reasons why one company decided to change their policy. (4)

3.3 Lock Ltd decided to increase their loans during the current financial year, whilst Down Ltd decided to maintain their existing loans.

Comment on the decisions of both companies. Make reference to the degree of risk and gearing (8)

3.4 A shareholder of Down Ltd is concerned about the drop in the market price of the shares. Explain why he feel this way. Provide TWO points. (4)

3.5 M. Mtolo owns 576 000 shares in Down Ltd, which represents 48% of the total issued shares. He wants to purchase another 25 000 shares.

Do a calculation to show how this would change his % shareholding in the company. (5)

Provide TWO reasons why you think he is specifically interested in increasing his shareholding in Down Ltd. (4)

INFORMATION:

	LOCK LTD		**DOWN LTD**	
	2020	**2019**	**2020**	**2019**
Current ratio	1,9 : 1	2,1 : 1	3,6 : 1	2,8 : 1
Acid test ratio	1,3 : 1	1,4 : 1	1,5 : 1	1,5 : 1
Dividends per share	45 cents	65 cents	60 cents	62 cents
Earnings per share	86 cents	80 cents	70 cents	72 cents
% return on average equity	13%	11%	11,6%	12%
% return on average capital employed	15%	12%	11,7%	13%
Debt/equity ratio	0,6 : 1	0,3 : 1	0,4 : 1	0,4 : 1
Net asset value per share	642 cents	630 cents	610 cents	618 cents
Market price per share	645 cents	622 cents	582 cents	615 cents
Interest rate on loans	13%		13%	

GRADE 12 ACCOUNTING FINANCIAL INDICATOR FORMULA SHEET	
$\frac{\text{Gross profit}}{\text{Sales}} \times \frac{100}{1}$	$\frac{\text{Gross profit}}{\text{Cost of sales}} \times \frac{100}{1}$
$\frac{\text{Net profit before tax}}{\text{Sales}} \times \frac{100}{1}$	$\frac{\text{Net profit after tax}}{\text{Sales}} \times \frac{100}{1}$
$\frac{\text{Operating expenses}}{\text{Sales}} \times \frac{100}{1}$	$\frac{\text{Operating profit}}{\text{Sales}} \times \frac{100}{1}$
Total assets : Total liabilities	Current assets : Current liabilities
(Current assets – Inventories) : Current liabilities	Non-current liabilities : Shareholders' equity
(Trade & other receivables + Cash & cash equivalents) : Current liabilities	
$\frac{\text{Average trading stock}}{\text{Cost of sales}} \times \frac{365}{1}$	$\frac{\text{Cost of sales}}{\text{Average trading stock}}$
$\frac{\text{Average debtors}}{\text{Credit sales}} \times \frac{365}{1}$	$\frac{\text{Average creditors}}{\text{Credit purchases}} \times \frac{365}{1}$
$\frac{\text{Net income after tax}}{\text{Average shareholders' equity}} \times \frac{100}{1}$	$\frac{\text{Net income after tax}}{\text{Number of issued shares}} \times \frac{100}{1}$
$\frac{\text{Net income before tax + Interest on loans}}{\text{Average shareholders' equity + Average non-current liabilities}} \times \frac{100}{1}$	
$\frac{\text{Shareholders' equity}}{\text{Number of issued shares}} \times \frac{100}{1}$	$\frac{\text{Dividends for the year}}{\text{Number of issued shares}} \times \frac{100}{1}$
$\frac{\text{Interim dividends}}{\text{Number of issued shares}} \times \frac{100}{1}$	$\frac{\text{Final dividends}}{\text{Number of issued shares}} \times \frac{100}{1}$
$\frac{\text{Dividends per share}}{\text{Earnings per share}} \times \frac{100}{1}$	$\frac{\text{Dividends for the year}}{\text{Net income after tax}} \times \frac{100}{1}$
$\frac{\text{Total fixed costs}}{\text{Selling price per unit – Variable costs per unit}}$	