








# Assessment of Professional Competence November 2018 Information on the day Millennial Hotel Group (Pty) Ltd

November 2018						
Sun	Mon	Tue	Wed	Thu	Fri	Sat
				1	2	3
4	5	6	7	8	9	10
11	12	13	14	15	16	17
18	19	20	21	22	23	24
25	26	27	28	29	30	

Inbox <a href="mailto:Junior.Disruptor@millennialhg.co.za">Junior.Disruptor@millennialhg.co.za</a>					
 <b>Mail</b>  <b>Calendar</b>  <b>Contacts</b>  <b>Tasks</b>	 <b>INBOX</b>				
	Doc	From	Subject	Attachment	Received
	1	Travis Jagger	Leasing	–	21/11/2018
	2	Travis Jagger	Leasing (again!)	<i>Attachment: Workings of Travis Jagger: Fair value estimate of Sandton hotel property</i>	21/11/2018
	3	Brian Stewart	Requests related to internal audit secondment	<i>Attachment: Workpaper DIR-01</i>	21/11/2018
	4	Travis Jagger	6CVCF loan restructuring	<i>Attachment: Presentation slides to complete</i>	21/11/2018
	5	Tshepo Umculi	Class B shares	–	21/11/2018
	6	Sarah Naidoo	Guest for life programme	–	21/11/2018
7	Eileen Barkingmad	Mentoring	–	21/11/2018	

Millennial Hotel Group (Pty) Ltd is a fictitious company, and all events as well as the names of all persons associated with this company, as mentioned in this Assessment of Professional Competence, are purely fictitious in nature and any resemblance to real persons, living or dead, or to an actual business entity, is purely coincidental.

## DOCUMENT 1

### EMAIL FROM TRAVIS JAGGER TO JUNIOR DISRUPTOR

**From:** Travis Jagger  
**Sent:** Wednesday 21 November 2018, 5:49 AM  
**To:** Junior Disruptor  
**CC:**  
**Subject:** Leasing

Good morning

Need to get an early start this morning ... there's a lot to do! We have a Board meeting coming up and everyone is waiting for some documents from me in preparation for the meeting.

You might recall my email to you on 9 November about the looming IFRS 16 adoption. The Board is really struggling to understand why our operating leases for the properties must now all of a sudden be capitalised, and have expressed their uncertainty about the impact it would have. I think this could be best illustrated using an example with numbers and conditions similar to our actual existing lease agreements.

I would like you to use the following illustrative lease terms and conditions, which are typical to our business:

- A three-year lease with the option to renew for two years (the maximum term is usually ten years, but that will make your table too cumbersome).
- Assume annual lease payments for the sake of simplicity. The first lease payment at the end of year 1 is R1,1 million, which escalates by 8% every year.
- You can work on an initial property value of R13,5 million and the property will be worth R12,5 million at the end of the lease (not sure if you would need this information).

Kindly draft a memo on my behalf, for circulation to the Board members, which includes the following:

- A table with numbers based on the example above, covering the full lease term, showing the impact on (a) total assets excluding cash, (b) total liabilities and (c) profit for the year, of (1) the old treatment under IAS 17 and (2) the new treatment under IFRS 16.
- Brief notes to explain what you did in this table.
- A conclusion on the impact of IFRS 16 for MHG.

Please don't include the tax implications in your memo for now; the Board will have enough to cope with! One step at a time...

Regards  
Travis

**CFO: Millennial Hotel Group**

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**DOCUMENT 2**  
**EMAIL FROM TRAVIS JAGGER TO JUNIOR DISRUPTOR**

**From:** Travis Jagger  
**Sent:** Wednesday 21 November 2018, 7:02 AM  
**To:** Junior Disruptor  
**CC:**  
**Subject:** Leasing (again!)

Hi again

You know what might persuade the Board that IFRS 16 can be good for us? Answer: if we use it to our advantage!

As you know, the right-of-use asset on leases can be carried in the financial statements in accordance with the revaluation model. I've been playing with this idea to give our balance sheet a bit of a makeover. It's a pity we will have to wait until FY2020, but I want to give the users of our financial statements a bit of a taste of what is to come, by disclosing an estimate of what the increased NAV per IFRS 16 will bring about – all in the spirit of the disclosures of IAS 8 paras 30–31. I've calculated my best estimate of the fair value of the Sandton hotel – see attachment.

Would you mind reviewing my spreadsheet and noting any concerns you have? Thanks, you're a star!

Can't wait for the additional financing we will raise with an improved balance sheet!

Regards  
Travis

**CFO:** Millennial Hotel Group

PS: Time is limited, so please assume that the attached spreadsheet is mathematically accurate, i.e. you don't need to check formulas and casting, etc.

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**ATTACHMENT TO EMAIL**

**Workings of Travis Jagger: Fair value estimate of Sandton hotel property**

Fair Value Sandton Hotel Excel - Excel													
Travis Jagger													
Fair value estimate: Sandton property													
	A	B	C	D	E	F	G	H	I	J	K	L	M
1	<b>Fair value estimate: Sandton property</b>												
3		(1)	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	
4			Rand	Rand	Rand	Rand	Rand	Rand	Rand	Rand	Rand	Rand	
6	Number of rooms		69	69	69	69	69	69	69	69	69	69	
8	Average room rate per night	(2)	1,490	1,565	1,643	1,725	1,811	1,902	1,997	2,097	2,201	2,311	
10	Occupancy	(3)	71%	71%	71%	75%	75%	75%	76%	77%	78%	79%	
11	Days per year		365	365	365	365	365	365	365	365	365	365	
13	Estimated accommodation revenue		R 26,643,212	R 27,975,372	R 29,374,141	R 32,580,473	R 34,209,497	R 35,919,971	R 38,218,850	R 40,657,816	R 43,245,131	R 45,989,534	
15	Food & beverage revenue	(2)	R 11,391,778	R 11,961,367	R 12,559,435	R 13,187,407	R 13,846,777	R 14,539,116	R 15,266,072	R 16,029,375	R 16,830,844	R 17,672,386	
17	Sundry & shop revenue	(2)	R 1,869,556	R 1,963,033	R 2,061,185	R 2,164,244	R 2,272,456	R 2,386,079	R 2,505,383	R 2,630,652	R 2,762,185	R 2,900,294	
19	<b>TOTAL REVENUE</b>		<b>R 39,904,545</b>	<b>R 41,899,772</b>	<b>R 43,994,761</b>	<b>R 47,932,124</b>	<b>R 50,328,730</b>	<b>R 52,845,167</b>	<b>R 55,990,305</b>	<b>R 59,317,843</b>	<b>R 62,838,160</b>	<b>R 66,562,214</b>	
21	Expenses	(4)											
22	Commission expense	(5)	R 1,705,166	R 1,790,424	R 1,879,945	R 2,085,150	R 2,189,408	R 2,298,878	R 2,446,006	R 2,602,100	R 2,767,688	R 2,943,330	
23	Food, liquor & beverages	(6)	R 7,404,656	R 7,774,888	R 8,163,633	R 8,571,814	R 9,000,405	R 9,450,425	R 9,922,947	R 10,419,094	R 10,940,049	R 11,487,051	
24	Cost of goods sold in hotel shops	(7)	R 1,308,689	R 1,374,123	R 1,442,830	R 1,514,971	R 1,590,720	R 1,670,255	R 1,753,768	R 1,841,457	R 1,933,530	R 2,030,206	
25	Bank charges	(2)	R 447,556	R 469,933	R 493,430	R 518,102	R 544,007	R 571,207	R 599,767	R 629,756	R 661,243	R 694,306	
26	Employee costs	(8)	R 10,139,667	R 10,748,047	R 11,392,929	R 10,823,283	R 10,282,119	R 9,768,013	R 9,279,612	R 8,815,632	R 8,374,850	R 7,956,108	
27	Lease payments	(9)	R 9,900,000	R 10,692,000	R 11,547,360	R 12,471,149	R 13,468,841	R 14,546,348	R 15,710,056	R 16,966,860	R 18,324,209	R 19,790,146	
28	Repairs & maintenance	(10)	R 2,163,556	R 2,271,733	R 2,385,320	R 2,504,586	R 2,629,815	R 2,866,499	R 3,124,484	R 3,405,687	R 3,712,199	R 4,046,297	
29	Other operating expenses	(2)	R 2,541,222	R 2,668,283	R 2,801,698	R 2,941,782	R 3,088,871	R 3,243,315	R 3,405,481	R 3,575,755	R 3,754,543	R 3,942,270	
30	Depreciation and amortisation		R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	R 1,619,333	
31	Interest expense: 6CVCF		R 240,000	R 240,000	R 240,000	R 240,000	R 240,000	R 240,000	R 240,000	R 240,000	R 240,000	R 240,000	
33	<b>TOTAL EXPENSES</b>		<b>R 37,469,843</b>	<b>R 39,648,765</b>	<b>R 41,966,478</b>	<b>R 43,290,171</b>	<b>R 44,653,519</b>	<b>R 46,274,274</b>	<b>R 48,101,454</b>	<b>R 50,115,674</b>	<b>R 52,327,644</b>	<b>R 54,749,046</b>	
35	<b>PROFIT</b>		<b>R 2,434,702</b>	<b>R 2,251,007</b>	<b>R 2,028,283</b>	<b>R 4,641,953</b>	<b>R 5,675,211</b>	<b>R 6,570,893</b>	<b>R 7,888,850</b>	<b>R 9,202,170</b>	<b>R 10,510,516</b>	<b>R 11,813,168</b>	

Fair Value Sandton Hotel Excel - Excel

File Home Insert Page Layout Formulas Data Review View DM Tell me what you want to do... Travis Jagger Share

A1 Fair value estimate: Sandton property

	A	B	C	D	E	F	G	H	I	J	K	L	M
35	<b>PROFIT</b>		<b>R 2,434,702</b>	<b>R 2,251,007</b>	<b>R 2,028,283</b>	<b>R 4,641,953</b>	<b>R 5,675,211</b>	<b>R 6,570,893</b>	<b>R 7,888,850</b>	<b>R 9,202,170</b>	<b>R 10,510,516</b>	<b>R 11,813,168</b>	
37	Discount rate	(11)	4.3%										
39	NPV = Fair value		R 47,211,184										
41	<u>Notes:</u>												
42	(1) Lease renewed for maximum available period of 10 years.												
44	(2) Used a 5% annual price hike in line with general inflation.												
46	(3) We are planning big renovations in 2022 that will increase hotel popularity substantially.												
48	(4) A reasonable allocation of total expenses made to Sandton property based on size.												
50	(5) Assumptions:												
51	• 50% of accommodation booked directly with MHG, attracting no commission.												
52	• 30% of accommodation booked on booking websites with 8% commission on average.												
53	• 20% of accommodation booked through travel agents with 20% commission on average.												
55	(6) 65% of food & beverage revenue.												
57	(7) 70% of sundry & shop revenue.												
59	(8) In our pursuit to become a "leaner" business; fewer employees will be needed (also computers will replace people).												
61	(9) Lease escalation per contract is 8%.												
63	(10) Used 5% growth until 2023; 9% thereafter as building getting older.												
65	(11) Average yield in SA property market: <a href="https://www.privateproperty.co.za/advice/news/articles/the-outlook-for-south-africas-property-market-in-2018/6160">https://www.privateproperty.co.za/advice/news/articles/the-outlook-for-south-africas-property-market-in-2018/6160</a>												
66													
67													
68													
69													
70													

Fair value

Ready 95%

## DOCUMENT 3

### EMAIL FROM BRIAN STEWART TO JUNIOR DISRUPTOR

**From:** Brian Stewart  
**Sent:** Wednesday 21 November 2018, 8:05 AM  
**To:** Junior Disruptor  
**CC:**  
**Subject:** Requests related to internal audit secondment

Dear Junior Disruptor

I must admit that I am burning the midnight oil trying to get through all my work – and hence I will greatly appreciate your assistance with the following urgent matters:

- 1 Please review the attached audit workpaper DIR-01 – prepared by Jane Wyman, a junior member of my team – and provide her with coaching/review notes regarding the adequacy and appropriateness of the audit work she has performed. While she is in her final year of BCom (Accounting) studies (part time), it is clear that Jane needs a lot of development and hence detailed feedback is required. Please do not formulate a list of audit procedures for Jane – while I want her to clearly understand your concerns and to learn the specific areas that require further audit work, I want her to formulate the audit procedures. Otherwise, how will she ever develop as an auditor?
- 2 From my superficial review of Jane's work, I am also concerned that she has interpreted the scope of her assignment too narrowly. Her audit work seems to be confined to detecting material misstatements in the loan balance of Tshepo Umculi, while ignoring possible material misstatements that may exist in other areas of the 2018 annual financial statements (AFS) as a result of the loan transactions. Please also deal with these potential misstatements in your coaching/review notes.
- 3 I attended a meeting with Tshepo early this morning where he reported that he had received an anonymous email late last night alleging that some of the staff in our hotels were –
  - allowing guests who have not made a reservation (i.e. walk-ins) to use otherwise empty hotel rooms, asking them to pay in cash, and then pocketing all or part of the amount due; and
  - allocating an excessive number of complementary room nights to travel agents and other third parties in exchange for kick-backs.

Tshepo has instructed the internal audit unit to undertake an initial investigation into these allegations as our utmost priority to determine whether there is reason to regard these as credible. Should the evidence gathered point to the likelihood of such irregularities taking place, we will appoint a forensic auditor to take the matter further. Can you therefore formulate the procedures that my audit team members should carry out to ascertain whether there is substance to the whistleblower's allegations? Please email these to me by 17:00 for my review. To facilitate easy execution, I need you to keep these procedures clear, specific and understandable.

I look forward to your submissions relating to the above. My motto: When the going gets tough, the tough gets going!

Kind regards

Brian Stewart BCom (Hospitality Management) PGD in Risk Management

**Chief Audit Executive: Millennial Hotel Group**

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## ATTACHMENT TO EMAIL

<b>Millennial Hotel Group</b>	<b>Financial Year: 2017/2018</b>	<b>DIR-01</b>
<b>Prepared by: Jane Wyman</b>	<b>Date: 15/11/2018</b>	
<b>Reviewed by:</b>	<b>Date:</b>	
<b>Subject: Loan: Tshepo Umculi</b>		

### Objective

To detect material misstatements in the 2018 AFS resulting from the transactions on Tshepo Umculi's loan account, and from the loan balance at 30 September 2018.

### Audit procedures

1. Obtain a printout of the general ledger account for 'Loan: T. Umculi' for FY2018.
2. Reperform the clerical accuracy of the calculations to determine the accuracy of the closing balance.
3. For all entries in the general ledger account, inspect supporting documentation to verify that the entry is recorded at the correct amount, at the correct date, and is appropriately described (in the 'Description' column).
4. Request Tshepo Umculi to sign a written confirmation letter confirming that he is in agreement with the loan balance at 30 September 2018.

### Findings (for each of the above audit procedures)

1. Done – see general ledger account on the next page. (Note: Credit entries are denoted by negative amounts in the 'Amount' column.)
2. Done – no exceptions found.
3. Done – refer to the right-most (shaded) column in the the general ledger account for the identification of the specific documents and records inspected. All amounts, dates and descriptions reflected in the general ledger account correspond to the amounts on the supporting documentation. The following is specifically noted:
  - o Note A: The amount recorded in the loan account is exclusive of VAT.
  - o Note B: The amount debited is the carrying amount of the furniture and fittings transferred from the company's hotels to Tshepo's holiday home.
  - o Note C: The amount recorded represents the total charges on Tshepo's company credit card, including VAT and tips, for the period 1/10/2017 to 30/9/2018.
4. Done – Tshepo agrees with the NIL balance on his loan account as at 30 September 2018, and his written submission has been filed.

### Conclusion

No misstatements were detected. As a result it can be concluded that there are no material misstatements in the 2018 AFS resulting from the transactions on Tshepo Umculi's loan account, and from the loan balance at 30 September 2018.



**Printout of general ledger account 723: 'Loan: T Umculi'**

<b>Date</b>	<b>Account</b>	<b>Reference</b>	<b>Description</b>	<b>Amount</b>	<b>Document(s) Inspected</b>
1/10/2017			Opening balance	0.00	
25/10/2017	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
10/11/2017	Accounts payable	Purchases journal	Purchase of BMW 530i vehicle for Tshepo Umculi's personal use	875 000.00	Supplier's invoice (note A)
11/11/2017	Bank	Cash book	Deposit	-275 000.00	EFT log
25/11/2017	Salaries and wages	Payroll	Mrs Umculi's salary	-50 000.00	Monthly payroll report
28/12/2017	Revenue	General journal	The value of hotel accommodation used by the Umculi family	-125 000.00	Memo from Tshepo Umculi instructing transfer
25/1/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
25/2/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
25/3/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
25/4/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
25/5/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-50 000.00	Monthly payroll report
25/7/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
25/8/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
25/9/2018	Salaries and wages	Payroll	Mrs Umculi's salary	-25 000.00	Monthly payroll report
15/9/2018	Furniture and fittings	General journal	Furniture for Tshepo Umculi's holiday home	127 875.00	Fixed asset register (note B)
30/9/2018	Entertainment	General journal	Expenditures incurred on behalf of company	-175 895.00	Credit card statements (note C)
30/9/2018	Bank	Cash book	Deposit	-126 980.00	EFT log
30/9/2018			Closing balance	0.00	

## DOCUMENT 4

### EMAIL FROM TRAVIS JAGGER TO JUNIOR DISRUPTOR

**From:** Travis Jagger  
**Sent:** Wednesday 21 November 2018, 8:11 AM  
**To:** Junior Disruptor  
**CC:**  
**Subject:** 6CVCF loan restructuring

Hi there

I know that you are having a busy day, but I need your assistance please.

As mentioned to you a while ago, 6CVCF wants to get their hands on Class B shares. They have now submitted a proposal to restructure their loan so that 50% of the current loan is convertible at their discretion into 3 000 Class B shares in three years' time. If not converted, the previous repayment terms apply. In return, they will now lend a further R10 million to MHG immediately. It will cost MHG approximately R80 000 in attorney's fees to get the legal paperwork for such a restructuring.

I would like you to draft a presentation to be made to the Board at our next meeting, indicating the likely impacts this will have on MHG and its shareholders. I've started working on presentation slides in the typical MHG style (see attached) that you must populate further. Please stick to the six attached slides as we have a lot to cover at that meeting. Also, include speaker/presenter notes for each slide so that I remember what is meant by those bullet points that are not self-explanatory.

Thanks in advance, looking forward to your input.

Regards  
Travis

**CFO:** Millennial Hotel Group

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## ATTACHMENT TO EMAIL

*Presentation slides to complete*

### **6CVCF proposal**

- Lend additional R10m to MHG now
- R15m of existing loan stays the same
- Other R15m of existing loan becomes convertible
  - into 3 000 Class B shares
  - three years from now

1

### **Pros**

- R10m immediate cash injection
- ???
- ???
- Etc.

2

## Cons

- Dilute decision-making power of existing Class B shareholders
- ???
- ???
- Etc.

3

## Accounting (IFRS) implications

- Not a clue!
- 
- 

4

## Accounting (IFRS) implications (continued)

- Still clueless
- 
- 

5

## Tax considerations

- MHG?
  -
- 6CVCF?
  -

6

## DOCUMENT 5

### EMAIL FROM TSHEPO UMCULI TO JUNIOR DISRUPTOR

**From:** Tshepo Umculi  
**Sent:** Wednesday 21 November 2018, 8:18 AM  
**To:** Junior Disruptor  
**CC:** Travis Jagger  
**Subject:** Class B shares

Hi there

I was just wondering about the 6CVCF request to convert a portion of their loan into Class B ordinary shares. Hypothetically, if we all decided to sell 100% of all our shares to a listed or international hotel group for the fair value of the business of say R250 million, how would we allocate the total purchase price between the Class A and B shares? The Class A shareholders have the right to dividends and to vote. The Class B shareholders have no rights to dividends yet have a powerful veto right on any major corporate decision MHG faces.

Please don't waste time doing valuation calculations. Rather apply your mind to the key factors and/or issues that we would need to consider in evaluating how to equitably allocate the total purchase price for MHG between the Class A and Class B shareholders. Your thoughts on this would be most enlightening. Thanks.

Regards  
Tshepo

**CEO:** Millennial Hotel Group

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## DOCUMENT 6

### EMAIL FROM SARAH NAIDOO TO JUNIOR DISRUPTOR

**From:** Sarah Naidoo  
**Sent:** Wednesday 21 November 2018, 8:42 AM  
**To:** Junior Disruptor  
**CC:**  
**Subject:** Guest for life programme

Hi there

Travis mentioned that he sent you an email about his idea to introduce a 'guest for life' programme. There could be benefits and unintended consequences to such a programme but it is interesting thinking. I was wondering whether it would not be better for us to focus on the corporate market – instead of selling lifetime packages to individuals, we could sell, say, ten-year packages to corporate customers. For example, sell ten-year access to any of our hotels to companies but subject to a maximum of 60 nights per customer in any year. Corporate customers may think R500 000 (my gut feeling of a suggested price) for each such package is a bargain? The companies could also potentially get a big income tax bonus – they could claim the deduction upfront on paying for ten-year access.

What are the five most important things MHG should consider in evaluating whether to pursue the above corporate guest package strategy?

Regards  
Sarah

**Marketing & Business Development Director:** Millennial Hotel Group

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## DOCUMENT 7

### EMAIL FROM EILEEN BARKINGMAD TO JUNIOR DISRUPTOR

**From:** Eileen Barkingmad  
**Sent:** Wednesday 21 November 2018, 8:58 AM  
**To:** Junior Disruptor  
**CC:**  
**Subject:** Mentoring

Hi there

It has been so good getting to know you over the past three weeks and developing a mentoring relationship. I think it is amazing that MHG invests so much in its key staff and uses outside consultants like myself to mentor young talent like yourself. Remember that I am here to assist you in developing and learning within the workplace in whatever way I can. Our discussions and interactions are strictly confidential and I may not share this with anyone at MHG except with your express permission. It's a safe space for us to interact! In addition, you are free to share whatever confidential information you wish about MHG and its operations since MHG has given express approval for you to do so.

Ok, a question for you ahead of our next mentoring session: MHG prides itself on its Code of Conduct. Is there anything that you have observed or encountered regarding the behaviour and actions of the executive directors and other key employees during your brief employment at MHG that may conflict with the second key principle listed in the Code ('MHG employees should use good judgement at all times and do the right thing')?

I look forward to your email response. Please list any such issues that you may have encountered or become aware of, together with brief explanations of each. This will enable us to discuss these issues meaningfully when we next meet.

Regards  
Eileen

PhD (Industrial Psychology)  
*Your personal mentor in business and executive sparring partner*

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