Assessment of Professional Competence
December 2023
Information on the day
On-Time Airline (Pty) Ltd

December 2023

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B	Sergal Anthony	FW: Accounting calculations	Accounting calculations with notes	06/12/2023
C	Bridget Klaasens	Proposed dividend		06/12/2023
D	Sergal Anthony	Ticket revenue for FY2023		06/12/2023
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G	Sergal Anthony	Hedging		06/12/2023

DOCUMENT A

EMAIL FROM CHIEF FINANCIAL OFFICER TO FINANCIAL ANALYST

From:	Sergal Anthony
Sent:	Wednesday 6 December 2023, 6:59 AM
To:	Financial Analyst
Subject:	Wet leases
Attachment:	Revised salient terms and conditions of proposed agreement.docx 34 KB CFO's draft explanation of accounting treatment.docx 30 KB

Good morning

I hope you rested well last night as today is going to be a busy day.

Regarding the wet leasing opportunity I referred to last week, I have included two attachments:

- Attachment 1: A summary of the revised salient terms and conditions of the proposed agreement. Changes and additions since the previous version (see my email of 1 December) are indicated in underlined text.
- Attachment 2: My draft explanation of the accounting treatment that I intend to submit to the board of directors.

Kindly review both attachments and let me know of any aspects you disagree with in my draft explanation (attachment 2) as well as any other accounting items that should be considered. Please include explanations about any disagreements or suggestions you may have.

In addition, please provide me with a high-level overview of the strategic pros and cons of entering into this proposed wet lease agreement, in comparison to the existing dry leases.

Please note: our intention with leasing this fifth aircraft is to establish a new flight route and not to add capacity to existing routes.

Kind regards
Serg

CFO: On-Time Airline (Pty) Ltd

ATTACHMENT 1 TO EMAIL

REVISED SALIENT TERMS AND CONDITIONS OF PROPOSED AGREEMENT

Commencement date

The effective date of the agreement is 1 January 2024.

Rights and obligations of lessee

The lessee obtains the use of one (1) Airbus 320 aircraft, as well as all related goods and services to operate the envisaged flight route, including –

- pilots
- cabin crew and ground staff
- supporting equipment
- meals
- maintenance of aircraft in accordance with industry and legal standards
- insurance of aircraft.

The lessee only provides fuel and covers airport fees (landing and parking fees, etc.). The aircraft is on the lessor's operators' certificate and the lessor registers the aircraft with the South African Civil Aviation Authority.

Rights of lessor

In exchange for all the above assets, goods and services provided to the lessee, the lessor is entitled to the following:

- Eighteen (18) fixed monthly payments (paid in arrears), starting on 31 January 2024, for the use of the aircraft and all related goods and services; and
- A variable payment calculated as 0,5% of total revenue generated by the lessee from operating the aircraft during the lease term. This calculation is to be completed within two (2) months from 30 June 2025 and is payable by 31 August 2025.

Operational features

The Airbus 320 aircraft is specified in the agreement, and it will be branded similar to On-Time's other leased aircraft. Branding will be for the cost of the lessee and the aircraft should be returned in the same condition (unbranded) at the end of the lease. The lessor, through its personnel, will operate the aircraft. On-Time will be able to direct the use of the aircraft, its scheduled flights, timing and frequency of flights.

Term of agreement

The term of the agreement is exactly eighteen (18) months.

The lessee would have an option to renew the agreement, at a cost of 10% below prevailing market rates upon renewal, for a further eighteen (18) months.

ATTACHMENT 2 TO EMAIL

CFO'S DRAFT EXPLANATION OF ACCOUNTING TREATMENT

Accounting scope

This is a lease agreement and therefore the leasing accounting standard is applicable to the agreement.

Lease classification

The leasing standard defines a finance lease as 'a lease that transfers substantially all the risks and rewards incidental to ownership of an underlying asset'. In contrast, an operating lease is defined as 'a lease that does not transfer substantially all the risks and rewards incidental to ownership of an underlying asset'.

As the lessor insures and maintains the aircraft, and provides all crew, the risks and rewards of ownership are not transferred to On-Time.

A common indicator of a finance lease is if the lease term is for the majority of the useful life of the asset. As aircraft are generally usable for 25 to 30 years, an 18-month lease term is for a small portion of its useful life.

Even if the lease is renewed, the maximum period of three years will still be the minority of the estimated useful life.

The proposed lease is therefore an operating lease and should be accounted for as such.

Accounting recognition and measurement

Operating lease payments are expensed as they are incurred.

Thus, the fixed payments are expensed when they are paid at the end of each month over the lease term. Similarly, the variable lease payment will be calculated based on revenue over the lease term and expensed when it is paid at the end of August 2025.

The leasing standard specifies that operating lease payments need to be expensed on a straight-line basis over the lease term.

Disclosure

The full payment (fixed plus variable) will be disclosed in the statement of profit or loss and the notes as a lease payment in exchange for using the aircraft.

DOCUMENT B

EMAIL FROM CHIEF FINANCIAL OFFICER TO FINANCIAL ANALYST

From:	Sergal Anthony
Sent:	Wednesday 6 December 2023, 7:13 AM
To:	Financial Analyst
CC:	Julio Oliveira
Subject:	FW: Accounting calculations
Attachment:	Accounting calculations with notes.docx 29 KB

Hi

I attach the FY2023 accounting calculations that were prepared by Greg & Rashid Consulting – see my email of last week.

Please review and email any comments you may have on these calculations and explanatory notes to me. Include in your comments any additional questions you may have and/or information you may require to conclude on the accounting treatment of the items. We need to make sure we have done everything correctly to be ready for the auditors.

You may ignore tax implications.

Thanks!
Serg

CFO: On-Time Airline (Pty) Ltd

ATTACHMENT TO EMAIL

ACCOUNTING CALCULATIONS WITH NOTES

Greg & Rashid Consulting

Your business, our passion

Calculations with notes

C1 Depreciation on leased aircraft				
	Cost	**Depreciable amount[1]**	**Life**	**Depreciation**
	R'000	**R'000**	**Years**	**R'000**
Four aircraft – components				
• Main aircraft	354 574	283 659	20	14 183
• Engines	270 766	216 613	15	14 441
• Flight and food service equipment	12 894	10 315	7	1 474
• In-flight entertainment system	6 447	5 157	5	1 031
				31 129

1 The depreciable amount was estimated at 80% of the cost, that is, a 20% residual value is assumed.

C2 Maintenance costs	
	R'000
Total maintenance costs summarised from the general ledger	131 822

The above amount relates to routine inspections and maintenance, major aircraft inspections and replacement of significant worn-out or broken parts. The total amount should be recognised as an expense.

C3 Impairment of aircraft #3

Each of On-Time's four aircraft flies a specific configuration of routes and flight times and is essentially a separate operation within the bigger company. Each aircraft is therefore a cash-generating unit (CGU) as defined in IAS 36. We have considered whether there are any indicators of potential impairment on each aircraft and found that the economic performance of the third Airbus 320 ('aircraft #3') is worse than expected.

Calculation of impairment loss on aircraft #3	
	R'000
Right-of-use asset (aircraft)	119 899
Vehicles, furniture and equipment	6 946
Leasehold improvements	3 038
Trade and other receivables	14 580
Cash and cash equivalents	32 916
Total carrying amount of CGU	177 379
Average projected cash profits per annum (inflow)	24 545
Residual value not applicable (leased)	–
South African prime interest rate: 11,25%	
Value in use therefore calculated as	
Annual cash flows (PMT)	24 545
Discount rate (I) [11,25 x 0,73 after tax]: 8,2125%	
Period (N): 10 years	
Present value (PV) is therefore	163 132
Impairment loss is therefore: R177 379 – R163 132	14 247

DOCUMENT C

EMAIL FROM CHIEF EXECUTIVE OFFICER TO FINANCIAL ANALYST

CONFIDENTIAL	
From:	Bridget Klaasens
Sent:	Wednesday 6 December 2023, 7:21 AM
To:	Financial Analyst
Subject:	Proposed dividend

Hi there

In my email last Friday regarding a potential dividend to be paid by On-Time, I forgot to mention a couple of things:

- Upon founding of the company on 1 January 2021, Sergal and I subscribed for R20 million and R31 million respectively of the shares issued by On-Time. To raise these funds, we both borrowed some money from friends, used some of our own hard-earned savings and also obtained loans from First Regional Bank. First Regional Bank lent Sergal and I R10 million each, subject to us pledging our On-Time shares as security for these loans.

  In terms of our loan agreements, First Regional Bank now require that Sergal and I repay R5 million of each of our loans within the next three months. Sergal and I were hoping to roll over these payments, but the bank is not willing to do so – it is uncomfortable with its exposure to high-net-worth individuals.

  Simon Bungane, the First Regional Bank representative on the On-Time board of directors, emphasised that the bank's demand that we repay some of our loan balances is not reflective of a negative view of On-Time: it is purely a general risk reduction initiative by the bank. Simon believes that the bank will continue to support On-Time's growth initiatives, but it is scaling back on loans to high-net-worth individuals.

- Basil Oliphant indicated that the Real Equity Impact Fund of South Africa (REIFSA) would greatly appreciate a cash distribution from On-Time. REIFSA is a private equity fund, and its investors require a return of capital wherever possible. REIFSA has struggled with some of its other investments due to the economic conditions in South Africa (low growth, loadshedding, etc.) and a 'dividend' from On-Time would please its investors.

Given the pressure that Sergal and I are under from First Regional Bank, and REIFSA's desire for a cash distribution, I believe a share buyback of R30 million in total would hardly impact the company's bank balances and would be a 'win-win' for all shareholders. Sergal and I could pocket enough to meet First Regional Bank's demands and have some left to enjoy a good holiday with our families.

Please consider the above proposal and advise Sergal and I about the following:

1. The high-level legal requirements of the Companies Act that On-Time would need to comply with in order for On-Time to do the proposed share buyback;
2. The key issues that the board of directors would need to consider in deciding whether to proceed with a share buyback; and
3. Any governance issues and/or challenges facing On-Time that are apparent from the information regarding the proposed cash distribution to shareholders.

We will take these issues to the rest of the board of directors at a later stage. Sergal and I need to have clear thoughts on the concerns before we debate it at a formal On-Time board meeting.

Please keep this confidential at this stage. Thank you in advance for your input – it will be much appreciated.

Thanks!
Bridget

CEO: On-Time Airline (Pty) Ltd

DOCUMENT D

EMAIL FROM CHIEF FINANCIAL OFFICER TO FINANCIAL ANALYST

From:	Sergal Anthony
Sent:	Wednesday 6 December 2023, 7:41 AM
To:	Financial Analyst
Subject:	Ticket revenue for FY2023

Hi!

The unreconciled revenue figure has been giving me sleepless nights. Accordingly, I have asked Julio Oliviera to prepare a reconciliation to account for the difference. He has sent me the following:

	Note	R'000
'Theoretical' flight ticket revenue		**935 327**
Flight ticket cancellations made by RSA Travel but not processed on PASSYS	1	(2 948)
The market value of free tickets issued to customers for inconveniences experienced on On-Time flights (e.g., flight delays, poor service). This amount was debited to marketing expenses		3 251
'Passenger service charges' for April 2023 due to ACSA incorrectly journalised into revenue	2	(572)
Sales of non-refundable tickets recognised as revenue	3	2 000
The nominal amount paid by directors for 40 personal flight tickets purchased during FY2023	4	10
Test transactions recorded on PASSYS not reversed	5	(742)
Immaterial difference that is still unaccounted for		556
Flight ticket revenue according to the trial balance at 30 Nov 2023		**936 882**

Notes

1. Flight ticket cancellations
   - Jim Jackson concluded an agreement with RSA Travel in January 2023 whereby the travel agent –
     - has the right to select and purchase tickets at highly discounted prices for flights for up to 12 months into the future; and
     - has the right to request a refund of such tickets, if unsold within 48 hours of the scheduled flight time.
   - The ticket numbers to be refunded must be communicated in writing to Jim, whereafter a credit note is issued to RSA Travel.
   - This amount reflects the total credit notes issued to RSA Travel thus far during FY2023.

2. 'Passenger service charges' for April 2023 due to the Airports Company South Africa (ACSA) incorrectly journalised into revenue
   - The bookkeeper correctly extracted the passenger service charges amount due to ACSA for April 2023 from PASSYS but, when recording the journal, she incorrectly

credited this amount to the revenue account instead of to accounts payable / ACSA account.

3. Sales of non-refundable tickets recognised as revenue
   - To meet his sales targets, Jim authorised the sale of 2 000 flight tickets at R1 000 each in November 2023, with flight dates from January to June 2024.
   - As the tickets cannot be cancelled, and at the insistence of Jim, the full flight fare amount has been recognised as revenue.

4. The nominal amount paid by directors for 40 personal flight tickets purchased
   - All such tickets are issued by the CEO's personal assistant, Felicity Fouche.
   - Felicity can capture flight bookings onto the PASSYS system – all such bookings are captured as having a nil ticket price.
   - In terms of company policy, each executive director is entitled to book 15 personal flights per year and an amount of R250 is payable for each such booking. These are not transferrable to anyone apart from these directors' immediate family members.

5. Test transactions recorded on PASSYS not reversed
   - In testing an update to the user interface for the capturing of flight bookings, several fictitious flight bookings were captured to determine if the data captured is correctly processed into PASSYS. However, once the testing had been concluded, the development team neglected to remove this data from the system.

We now have a reconciliation of the 'theoretical' revenue to the revenue per the trial balance for the 11-month period ending 30 November 2023, which more or less reconciles these figures. Do you have any concerns regarding the content of this reconciliation? If so, could you please document them? I would like to discuss these concerns with the CEO at our weekly briefing as part of my update to her regarding our preparedness for the 2023 external audit and the effectiveness of our corporate governance arrangements and systems of internal control.

Looking forward to your insights on this important matter!

Kind regards
Serg

CFO: On-Time Airline (Pty) Ltd

DOCUMENT E

EMAIL FROM CHIEF EXECUTIVE OFFICER TO FINANCIAL ANALYST

From:	Bridget Klaasens
Sent:	Wednesday 6 December 2023, 08:45 AM
To:	Financial Analyst
CC:	Sergal Anthony
Subject:	Expansion opportunities

Good morning!

I am aware that Sergal has informed you about On-Time’s discussions regarding entering into a wet lease agreement on an initial 18-month term with the option to renew for a further 18 months. This lessor, JourneyOps, is a well-known wet lease specialist that provides services to airlines. We have discussed the possibility of On-Time opening a new route between the OR Tambo and George airports with JourneyOps and it is most interested in partnering with us in this venture.

As Sergal has communicated to you, JourneyOps will provide us with an Airbus 320 aircraft with similar specifications to On-Time’s existing aircraft fleet in terms of a wet lease arrangement. JourneyOps will, in addition to providing the aircraft, also assume responsibility for the provision of pilots, cabin crews, supporting equipment, in-flight meals, maintenance and insurance. On-Time will cover the cost of jet fuel and airport fees, as well as any additional administrative and marketing costs that would be incurred relative to the operation of the new route.

JourneyOps will provide daily flights between the OR Tambo and George airports. Furthermore, JourneyOps has indicated that the monthly wet lease will cost On-Time R12 million (excluding VAT) per month during the initial 18-month lease term.

I have prepared some high-level financial projections for an initial 12-month period for the new George|OR Tambo flight route, assuming this commences on 1 January 2024. These projections are set out in the table below.

George|OR Tambo flight route 12-months ending December 2024	
Number of wet leased Airbus A320s	1
Annual flights: George|OR Tambo	1 440
Total number of available seats	250 560
Estimated number of passengers	200 448
Load factor	80%
Average price per ticket sold	R1 800
	R'000
Ticket revenue	360 806
Other revenue	18 041
Total revenue	378 847
Wet lease payments	(144 000)
Fuel costs	(73 008)
Landing and parking fees	(21 648)
Commissions paid	(7 216)
Customer reservation charges	(16 236)
Other operating costs	(15 000)
Total operating expenses	(277 108)
EBITDA	101 739

Based on my assessment, the operation of the additional flight route would be quite profitable for On-Time, and I am excited by the opportunity. We will need to provide the On-Time board of directors with these high-level financial projections prior to investigating the opportunity in more detail.

I would therefore appreciate your assistance with the following:

1. Reviewing and commenting on the high-level financial projections that I have prepared. Please indicate any assumptions that in your opinion may be unreasonable or which may require further research; and
2. Providing a summary of the key strategic issues that the board should consider in evaluating the feasibility of the proposed George|OR Tambo route.

I have not yet compiled financial forecasts beyond the end of FY2024 – we can do this once we are happy with the 12-month forecast ending 31 December 2024.

I look forward to your feedback.

Regards
Bridget

CEO: On-Time Airline (Pty) Ltd

DOCUMENT F

EMAIL FROM CHIEF FINANCIAL OFFICER TO FINANCIAL ANALYST

From:	Sergal Anthony
Sent:	Wednesday 6 December 2023, 8.58 AM
To:	Financial Analyst
CC:	Julio Oliveira
Subject:	Company income tax return FY2022
Attachments:	FY2022 income tax calculation workings.docx 29 KB Selected financial information used for the income tax calculation.docx 29 KB

Hi

Julio has forwarded his workings to me for the purposes of preparing the 2022 year of assessment's income tax return. I have attached them to this email. As previously mentioned, I would like you to assist me with this. Because this is the first time that Julio is performing the calculation without Tania's oversight, please undertake a critical review. Consider each reconciliation item and, if it is incorrect, partially correct or needs further clarification, please provide him with the correct treatment or state what additional information is needed.

Please also highlight which, if any, of the reconciling items would have impacted the FY2022 tax rate reconciliation.

Send Julio an email with your feedback and copy me in it.

Thanks again, really appreciate your help!

Kind regards
Serg

CFO: On-Time Airline (Pty) Ltd

ATTACHMENT 1 TO EMAIL

FY2022 INCOME TAX CALCULATION WORKINGS

	Amount R'000	Reasons/comments
(Loss) before tax	(54 994)	
Ticket revenue	0	No adjustment – meets gross income definition, taxed on earlier of receipt or accrual. ACSA passenger service charges amount should be taxed as it was received by On-Time even though it did not accrue to the company.
Other revenue	0	No adjustment – meets gross income definition, taxed on earlier of receipt or accrual.
Fuel costs	0	No adjustment – incurred in the production of income, thus tax deductible. Forward agreements have no income tax impact.
Employee costs	0	No adjustment – in the production of income, thus tax deductible. Unconditional obligation to pay bonuses, thus tax deductible.
Landing and parking fees	0	No adjustment – in the production of income, thus tax deductible.
Maintenance costs	125 118	Added back as One-Time is not the owner of the aircraft, thus no tax deduction. Also, no adjustment for maintenance costs related to the replacement of significant broken parts.
Commissions paid	0	No adjustment – in the production of income, thus tax deductible.
Customer reservation charges	0	No adjustment – in the production of income, thus tax deductible.
Unrealised loss on foreign exchange contract (FEC)	1 500	Added back the R1 500 000 unrealised loss on the FEC included in other operating costs as this is not deductible in the 2022 year because it has not yet been incurred.
Other operating costs	0	Included in other operating costs is an annual insurance premium of R567 000 that was paid to an insurance company on 1 October 2022. This annual insurance premium relates to the short-term insurance cover for vehicles, furniture and equipment. The annual premium covers the period 1 October 2022 to 30 September 2023. No adjustment, in the production of income, thus tax deductible.
Office cleaning cost	(137)	Office cleaning costs for August 2021 to December 2021. We forgot to claim this in the 2021 tax return. In the production of income, thus tax deductible.
Depreciation: Right-of-use assets	64 468	Accounting entry – needs to be reversed for tax purposes.

	Amount R'000	Reasons/comments
Other depreciation (vehicles, furniture, leasehold improvements and equipment)	6 561	Accounting entry – needs to be reversed for tax purposes.
Wear and tear on vehicles, furniture and equipment	(5 800)	Wear and tear allowance calculated based on write-off periods in Binding General Ruling No.7. No tax allowance on right-of-use assets, as this is an accounting entry.
Interest expense – lease liabilities	0	No adjustment – in the production of income, thus tax deductible.
Annual learnership allowance	(500)	Tax deduction for learnership agreements.
Taxable income before taking into account assessed loss	136 216	
Less: Prior-year assessed loss	(92 000)	Higher of R1 million and 80% of assessed loss Prior-year loss = R115 000 000 80% x R115 000 000 = R92 000 000
Taxable income for the year	44 216	
Tax liability	11 938	R44 216 000 x 27%

ATTACHMENT 2 TO EMAIL

SELECTED FINANCIAL INFORMATION USED FOR THE INCOME TAX CALCULATION

On-Time Airline **Selected financial information**	**Notes**	**FY2022** **Actual** **R'000**
Ticket revenue		848 684
Other revenue	1	50 346
Total revenue		899 030
Fuel costs		(411 840)
Employee costs	3	(107 757)
Landing and parking fees		(57 711)
Maintenance costs	4	(125 118)
Commissions paid		(16 125)
Customer reservation charges		(39 124)
Other operating costs	2	(68 726)
Total operating expenses		(826 401)
EBITDA		72 629
Depreciation: Right-of-use assets		(64 468)
Other depreciation	5	(6 561)
EBIT		1 600
Interest income		1 091
Interest expense: Lease liabilities		(57 685)
(Loss) before taxation		(54 994)

Explanatory notes

1. Other revenue represents mainly food and beverages sold on flights to passengers. Also included in this amount is a profit on the sale of furniture and equipment. On-Time realised a handsome profit on the sale of certain imported equipment, with the rand-denominated sales price exceeding the initial rand-denominated cost. The furniture sold as second-hand items yielded an accounting profit, but the sales price did not exceed the initial cost thereof.
2. Other operating costs include an unrealised foreign exchange loss in respect of an FEC entered into just before year end to hedge foreign currency exposures.
3. Included in employee costs is the current year movement in respect of a provision for bonuses. The bonuses are determined based on the year-end results, but employees are only entitled to these bonuses if they are still employed on the date of payment, which is typically three months after the year end.
4. The amount relates to routine maintenance and day-to-day servicing of aircraft. Included in the amount are costs associated with replacement parts and consumables.
5. Other depreciation relates to depreciation on vehicles, leasehold improvements on aircraft, furniture and equipment.

DOCUMENT G

EMAIL FROM CHIEF FINANCIAL OFFICER TO FINANCIAL ANALYST

From:	Sergal Anthony
Sent:	Wednesday 6 December 2023, 9.00 AM
To:	Financial Analyst
Subject:	Hedging

Hi

I sent you an email last Friday about hedging jet fuel prices, but I have had some subsequent thoughts and questions for you.

As I mentioned, jet fuel is priced in USD. Hedging the jet fuel price alone would not fully cover our exposure. Perhaps we need to hedge our foreign currency exposure as well? On-Time has in the past occasionally hedged our foreign currency exposures using FECs.

I reached out again to my investment banker friend, and he provided the following information regarding forward rates during the period 1 July 2022 to 20 June 2023:

FEC contract establishment date	FEC rate USD:ZAR	FEC maturity date
1 July 2022	16,50	30 September 2022
1 October 2022	18,40	31 December 2022
1 January 2023	17,20	31 March 2023
1 April 2023	18,00	30 June 2023

The above FEC contracts had fixed maturity dates, that is, delivery took place on maturity dates with no option to take delivery of foreign currency at any time before the maturity dates.

As a matter of interest, the spot rates at these selected dates were as follows:

	Spot rates USD:ZAR
1 July 2022	16,27
30 September 2022	18,15
31 December 2022	17,00
31 March 2023	17,75
30 June 2023	18,83

I think it may be worth exploring a position where On-Time hedges 50% of its total exposure to jet fuel prices and foreign currency exposures instead of fully hedging. That may give the company the benefit of both worlds, namely hedging adverse movements and benefitting from lower jet fuel prices / ZAR strengthening against the USD.

Some questions for you:

1. Briefly explain if my suggested hedging strategy (using call options to hedge 50% of our exposure to jet fuel prices and using FECs to hedge 50% of On-Time's estimated foreign currency exposure) would have been cost effective, using the following assumptions:

   On-Time pre-ordered and purchased 1,8 million gallons of jet fuel at the beginning of every quarter during the 12-month period ended 30 June 2023 (namely on 1 July 2022, 1 October 2022, 1 January 2023 and 1 April 2023) for delivery and settlement at the spot jet fuel prices at the end of each quarter (namely on 30 September 2022, 31 December 2022, 31 March 2023 and 30 June 2023).

2. What are two key benefits and two potential downsides of hedging against jet fuel price increases?

3. Is it advisable to use a partial hedging strategy, that is, hedge 50% of On-Time's exposure to rising jet fuel prices and USD exposures rather than fully hedging our exposures? Please give me your opinion in a brief paragraph, I do not require too much detail.

Kind regards
Serg

CFO: On-Time Airline (Pty) Ltd
