

Ignore value-added tax (VAT).

1 Background

UbudCargo (Pty) Ltd ('UC') is an innovative start-up technology company aiming to revolutionise the trucking industry with its cutting-edge platform called CargoPlat™. CargoPlat™ serves as a connection hub between truck drivers and the transport industry, similar to an 'Uber for trucks' model. Since its inception, UC has received significant attention from venture capital investors due to its disruptive potential in the trucking industry.



Customers who need cargo transported use the online or mobile CargoPlat™ application ('app') to interact with truck drivers and carrier companies (companies that own trucks), provided they are registered on CargoPlat™. The CargoPlat™ app has over 10 000 registered carriers that are available to transport cargo for UC's customers. In 2024, UC handled shipments via the app for more than 90 000 customers operating in South Africa. UC generates profit from the margin charged between the value of the services provided to customers and what UC pays to the registered carriers.

Although most of the road transport industry in South Africa has benefited from the difficulties experienced by the rail industry, UC experienced low revenue in 2024 due to weak freight demand and excess carrier capacity. Customers and suppliers also faced demand pressure due to higher interest rates and inflation.

UC faces stiff competition from traditional logistics companies, other technology-based service companies and trucking companies. UC is committed to investing in technology to bring solutions to its customers and help solve their complex logistical challenges. The staff of UC mainly comprise data scientists, engineers and developers who are committed to building the next generation of tools and processes that will change how supply chains function.

The company's founder and chief executive officer, Trokkie Smith, has a clear vision for the future of trucking logistics. However, the low-interest rate environment that previously fuelled a funding boom in businesses of this nature has reversed and investors are more cautious with their funding decisions. Despite interest from venture capital firms, UC finds itself facing funding pressures. This has prompted rigorous interrogation from potential investors regarding the company's expansion plans, unit economics¹, valuation, and the potential impairment of intangible assets associated with the platform.

Financial reporting considerations, such as compliance with IAS 38 *Intangible Assets* with regard to platform costs, and financial statement analysis are important in evaluating the company's viability and growth prospects. In addition, compliance with IFRS 16 *Leases* has added another layer of complexity, as UC has concluded various 2–5 year leasing agreements for premises and servers to host CargoPlat™. UC has a 31 December financial year end.

Investors and stakeholders have also expressed concerns over potential risks such as data breaches on the platform, regulatory compliance issues and the possibility of price fixing or collusion among truck drivers.

As UC navigates these challenges and opportunities, the company seeks to maintain its trajectory of growth and innovation while addressing the financial, operational and regulatory complexities inherent in driving the trucking industry's digital transformation.

2 Compliance with IFRS® Accounting Standards (IFRS) and appointment of new auditors

In 2022, UC appointed an accountant, who had boasted about his excellent knowledge of IFRS, to prepare the financial statements. However, he suddenly resigned in March 2024 after the financial statements for the year ended 31 December 2023 (FY2023) were audited. Since then, the chief financial officer (CFO), Bongani Xaba, discovered that IFRS may not have been applied correctly in all instances in the FY2023 financial statements. Bongani started referring to the previous financial accountant as 'That Accountant' ('Mr TAcc') whenever these non-compliant instances came up in discussions. These errors were not identified during the FY2023 audit and the board of directors feels that it would be a 'waste of money' to pay audit fees for FY2024 financial statements that contained errors. UC's Memorandum of Incorporation (MOI) does not contain a voluntary audit clause and an audit is also not required by the shareholders. They are therefore not sure if it is necessary for UC's FY2024 financial statements to be audited or whether an independent review would be sufficient.

Should it be necessary for the financial statements to be audited, the board of directors decided that it would change auditors and appoint Ingxelo Auditors Inc. ('Ingxelo') as UC's auditor for FY2024. Ingxelo's only registered auditor is Maxwell Jones. Bongani has also requested that Maxwell assist with the corrections of the errors made by Mr TAcc, but not to assist with the calculation or processing of the corrections.

¹ Unit economics describes a business' revenues and costs in relation to an individual unit. A unit can refer to any item that is quantifiable and that creates value for a business. Therefore, unit economics indicates how much value each item or unit generates for the business. In the case of UC, this can refer to revenue per customer and profit (or contribution) per customer.

The following information is relevant:

2.1 Development of the CargoPlat™ app

UC completed the development of its CargoPlat™ app by 31 December 2022, when the app was capable of operating in the manner intended by management. The following are relevant extracts from the minutes of the board meetings held during 2022:

| Date | Discussion or action points |
|------------------|---|
| 10 January 2022 | <ul style="list-style-type: none"> Trokkie started the meeting with an opening statement, 'I have a dream!' and with that, the dream of the CargoPlat™ app was born. Trokkie presented a detailed proposal, which emphasised that UC has the technology and resources to develop such an app and use it effectively in its operations. However, UC needed to secure funding for the project. All the directors pledged their commitment to making Trokkie's dream a reality. UC appointed a company to undertake market research on whether a market for such an app exists and how many users were likely to use such an app. The board approved the detailed proposal that Trokkie presented. |
| 5 March 2022 | <ul style="list-style-type: none"> The market research report was tabled, which indicated a significant number of users are likely to use such an app and services. The research found that such apps could be used for six years, after which additional competitors would have entered the market. UC instructed the finance team to prepare a detailed budget of the expected costs to develop such an app and future expected profits from using the app. UC would apply for a bank loan to fund the project. UC instructed the IT team to conceptualise and plan the app. |
| 2 May 2022 | <ul style="list-style-type: none"> The board approved the technical details of the app after considering the IT team's proposal. The board instructed the IT team to design an outline framework for a concept version of the design of the app. |
| 11 June 2022 | <ul style="list-style-type: none"> The board approved the formal budget of future expected profits from using the app as well as a forecast for the development costs of the CargoPlat™ app and the expected profits. The board resolved that the local bank be approached for a loan and that the budget be submitted to it as part of its loan application. |
| 17 June 2022 | <ul style="list-style-type: none"> UC received confirmation that its local bank had approved the company's loan application. The local bank provided a repayment schedule. |
| 28 August 2022 | <ul style="list-style-type: none"> The board – <ul style="list-style-type: none"> approved the concept version of the design of the app; gave the go-ahead to the IT team to commence the development; and resolved that the app be tested by an independent application consultant. |
| 30 November 2022 | <ul style="list-style-type: none"> The test report of the independent application consultant was tabled at the meeting, and it was found that the app was |

| | |
|--|---|
| | <p>technically up to standard, although some minor changes had to be made.</p> <ul style="list-style-type: none"> • The board approved the report and instructed the IT team to make the final changes. • The formal launch was scheduled for 31 December 2022. |
|--|---|

The IT team made the final changes in December 2022, and the app was launched on 31 December 2022 at an extravagant new year eve event during an IT convention held in Mbombela.

Bongani provided the following correct details of the expenditure paid in respect of the CargoPlat™ app:

| | Notes | R'000 |
|--|-------|-------|
| Research phase | 1 | 1 200 |
| Development phase, including the costs of registering the app as a trademark | 1 | 5 010 |
| Launch event during IT convention | | 170 |
| | 2 | 6 380 |
| | | |

Notes

- 1 The research phase and the development phase correspond to the definition set out in IAS 38. All expenses incurred during the development phase occurred after the requirements of para. 57 of IAS 38 had been met.
- 2 Mr TAcc had capitalised the total amount of the expenditure as the initial cost of the app that was recognised as an intangible asset.

During FY2023, Mr TAcc had revalued the application as he believed its value had increased significantly due to the success of the app and the number of users. As no active market for such apps exists, he asked an external valuer to value the app, who valued the app at R6,5 million on 31 December 2023. Mr TAcc then recognised a R120 000 revaluation gain as a revaluation surplus. Mr TAcc did not recognise any amortisation during FY2023, arguing that the revalued carrying amount exceeded the initial cost of the application.

2.2 Lease of server

On 1 January 2023, UC entered into a lease agreement with IT&Tech Supplies (Pty) Ltd ('ITT') to lease a high-performance server from ITT for a non-cancellable lease term of three years. This was to accommodate the additional storage space UC needed for storing information in respect of its CargoPlat™ app. The server being leased consists of several components, including the hardware, motherboards, central processing unit (CPU), random access memory (RAM), chipsets and the basic input / output system. All the internal components of servers need to be connected and working in sync for the server to act as one uniform device.

In terms of the lease agreement, lease payments of R25 500 are payable monthly in arrears. The interest rate implicit in the lease on 1 January 2023 was 11,75% per annum, compounded monthly. On 1 January 2023, ITT paid R50 000 to UC as an incentive to enter into the lease agreement with ITT rather than a competitor.

Mr TAcc considered this single lease agreement in substance to consist of several individual leases of the underlying components. He therefore elected to apply the recognition exemption

for lessees in terms of IFRS 16 and recognised the lease payments accordingly since 1 January 2023. He based this election on the low value of the individual components of the server, which varied between R30 000 and R75 000 per component.

2.3 Lease of head office building and warehouse

On 1 January 2023, UC entered into a lease agreement, as the lessee, with Embi Properties (Pty) Ltd ('EmbiP'). This lease was for UC's head office building and the adjacent warehouse, consisting of floor areas of 300 m² and 900 m² respectively.

The lease contract between UC and EmbiP contains the following:

- Description and detail of the property;
- A fixed annual rental of R450 per m², payable annually in advance on 1 January.
- A 6% increase in the fixed rental on 1 January of each subsequent year.
- A lease term of five years.
- A refundable deposit of R100 000 payable on 1 January 2023.

3 Relevant accounting policies

- UC accounts for its intangible assets using the cost model and amortises intangible assets on a straight-line basis over their useful lives in terms of IAS 38.
- UC recognises and presents right-of-use assets separately from other assets.
- An underlying lease asset is regarded as having a low value if its value is less than R80 000 (this threshold is acceptable in terms of IFRS 16).
- UC recognises the accumulated depreciation on right-of-use assets in a separate account in the general ledger.

4 Potential takeover

Due to the funding difficulties experienced by UC, some directors felt that the business should be sold. It has attracted the attention of some larger traditional logistics companies who want to leverage off UC's technology.

Emperor Logistics Ltd ('EL'), a company listed on the A2X Markets Stock Exchange (A2X) has approached UC with a purchase offer. EL has offered R120 million for the acquisition of an 80% shareholding and will decide after the offer to purchase has been accepted by the directors of UC whether to settle the purchase price by issuing shares or paying cash.

In view of this offer, Trokkie has asked Bongani to calculate the fair value of UC.

Extract from the management accounts relating to UC, as provided by Bongani:

| UbudCargo (Pty) Ltd Financial information for the year ended / ending 31 December | | | | | |
|--|-------|----------------|----------------|------------------|------------------|
| | Notes | Actual 2023 | Actual 2024 | Forecast 2025 | Forecast 2026 |
| | | R'000 | R'000 | R'000 | R'000 |
| Revenue | 1 | 158 400 | 124 800 | 149 760 | 172 224 |
| Purchased transport and related services | 2 | (122 220) | (102 410) | (107 531) | (112 908) |
| Personnel and related services | | (10 570) | (8 750) | (9 275) | (9 832) |
| Other selling, general and administrative expenses | 3 | (8 499) | (9 620) | (10 005) | (10 505) |
| Operating profit | | 17 111 | 4 020 | 22 949 | 38 979 |
| Finance cost | 4 | (5 172) | (4 767) | (5 053) | (5 356) |
| Income before tax | | 11 939 | (747) | 17 896 | 33 623 |
| Income tax expense | | (3 002) | (25) | (5 200) | (11 210) |
| Net profit / (loss) | | 8 937 | (772) | 12 696 | 22 413 |
| Average employees (including executive directors) | | 45 | 40 | 55 | 60 |
| Number of customers | 5 | 89 000 | 95 000 | 105 000 | 110 000 |
| | | | | | |

The following is an extract of the statement of financial position that was provided by Bongani. This statement of financial position was prepared after all errors in complying with IFRS (see sections 2.1 and 2.2 above) were appropriately corrected.

| UbudCargo (Pty) Ltd Statement of financial position as at 31 December 2024 | | | |
|---|-------|---------------|---------------|
| | Notes | 2024 R'000 | 2023 R'000 |
| Assets | | | |
| Non-current assets | | | |
| Property, plant and equipment | | 7 375 | 7 474 |
| Intangible assets | 8 | 30 938 | 30 951 |
| Right-of-use assets | 7 | 10 617 | 11 164 |
| Investment in associate | | 1 200 | 800 |
| | | 50 130 | 50 389 |
| Current assets | | | |
| Cash and cash equivalents | | 1 018 | 1 522 |
| Trade receivables | | 22 225 | 26 038 |
| Prepaid expenses | | 352 | 257 |
| | | 23 595 | 27 817 |
| Total assets | | 73 725 | 78 206 |
| Equity and liabilities | | | |
| Equity | | | |
| Share capital | 6 | 3 500 | 3 500 |
| Retained earnings | | 3 491 | 7 200 |
| | | 6 991 | 10 700 |
| Non-current liabilities | | | |
| Interest-bearing loans | 2 | 21 595 | 25 371 |
| Deferred tax liabilities | | 65 | 58 |
| Lease liabilities | 7 | 6 249 | 6 589 |
| | | 27 909 | 32 018 |
| Current liabilities | | | |
| Trade and other payables | | 22 958 | 23 439 |
| Accrued expenses | | 5 740 | 3 516 |
| Income tax payable | | 2 102 | 1 065 |
| Short-term portion of interest-bearing loans | | 3 205 | 2 305 |
| Short-term portion of lease liabilities | 7 | 4 820 | 5 163 |
| | | 38 825 | 35 488 |
| Total equity and liabilities | | 73 725 | 78 206 |

Notes

- Customers are charged on a transactional basis or pre-arranged contract rates with most of the contracts being for a three-year term to allow for renegotiation. The terms and conditions in respect of transactions concluded on UC's CargoPlat™ stipulate that UC remains solely responsible and liable for ensuring delivery services are rendered to customers. The directors of UC believe they will be able to increase UC's market share in 2025 and 2026 by 20% and 15% respectively. The increase in revenue will stabilise

at 7% from 2027 onwards. UC's largest customer accounted for about 10% of total revenue in 2024.

- 2 Purchased transport costs represent amounts paid to the owners of trucks for services rendered. Most of the purchased transport from UC carriers are priced on the spot basis (or transactional basis) with very few being based on pre-arranged contract rates. Spot basis means rates are negotiated on a shipment-by-shipment basis and fluctuate dynamically in accordance with changes in supply and demand. The contract is between UC and the carrier (not the customer) and UC is able to stipulate and / or substitute multiple carriers to meet UC's delivery obligation to customers using the CargoPlat™ app. UC is responsible for prompt payment to suppliers selected to render services to customers. The nature of this business is such that transportation of cargo often takes time and customers pay when delivery is made.

- 3 The following amounts are amongst others included in other selling, general and administrative expenses:

| | 2023 | 2024 | 2025 | 2026 |
|---|--------------|--------------|--------------|--------------|
| | R'000 | R'000 | R'000 | R'000 |
| Amortisation of intangible assets | 1 820 | 1 850 | 1 920 | 1 960 |
| Depreciation on right-of-use assets | 2 520 | 2 580 | 2 230 | 2 140 |
| Share of profit of associate | 120 | 135 | 140 | 143 |
| Depreciation on property, plant and equipment | 710 | 705 | 695 | 680 |
| Bad debts | 82 | 90 | 110 | 130 |

- 4 Finance costs relate to interest on loans and lease liabilities. All loans and lease liabilities have been correctly reflected in terms of IFRS in the forecast by Bongani and are accounted for at amortised cost.
- 5 The CFO believes UC will be able to increase the number of customers through an extensive marketing campaign that will be launched in 2025.
- 6 UC's five shareholders had each invested R700 000 when they initially founded the company.
- 7 In addition to the leases noted in sections 2.2 and 2.3, UC also leases a number of warehouses and office buildings across South Africa, as well as various server components.
- 8 The intangible assets include the self-developed CargoPlat™ app, and other applications and trademarks acquired.

Bongani performed the following valuation as at 31 December 2024 using the free cash flow to firm valuation method:

| Free cash flow to firm valuation as at 31 December 2024 | | | | |
|---|-------|-------------------|---------------|---------------|
| | Notes | 2024 R'000 | 2025 R'000 | 2026 R'000 |
| Income before tax | | | 17 896 | 33 623 |
| Revenue adjustment | a | | 619 507 | 712 433 |
| Depreciation on property, plant and equipment | | | 695 | 680 |
| Bad debts | | | 110 | 130 |
| Amortisation of intangible assets | | | 1 920 | 1 960 |
| Synergy benefits (reduced costs) | b | | 1 620 | 1 620 |
| Lease instalments | c | | (1 250) | (1 250) |
| Taxation paid | | | (5 200) | (11 210) |
| Dividends received from associate | | | (80) | (80) |
| Tax saving on dividends received | | | 22 | 22 |
| Finance costs | | | 5 053 | 5 356 |
| Property, plant and equipment | d | | (7 488) | (8 611) |
| Investment in associate | d | | (20) | (20) |
| Intangible assets | d | | (14) | (14) |
| Movement in working capital | e | | 15 992 | 16 791 |
| Free cash flow | | | 648 763 | 751 430 |
| Terminal value [(751 430*1,07)/(0,1264-0,07)] | | | | 14 255 854 |
| | | | 648 763 | 15 007 285 |
| PV of FCF and TV @ WACC ² | | 12 404 112 | | |
| Lease liability at market value | | (11 069) | | |
| Intangible assets at market value | f | 32 000 | | |
| Value of 100% equity | | 12 425 043 | | |
| Minority discount | g | (1 242 504) | | |
| Equity value | | 11 182 539 | | |
| WACC calculation | | | | |
| Beta of MH Roberts Transport | h | 0,81 | | |
| Risk-free rate | | 8,80% | | |
| Expected return on SA market | | 13,45% | | |
| Ke = 8,8%+0,81*(13,45%-8,8%) | | 12,57% | | |
| Kd | i | 12% | | |
| WACC (12,68%*60%)+(12,57%*40%) | j | 12,64% | | |

Notes

- (a) Bongani believes that EL will be able to get 100% of the revenue from the platform when it takes over UC. The revenue in the statement of profit and loss amounts to 15% of the amount charged by UC, with the rest being paid over to carriers. An adjustment for the 85% of the revenue which was not included in the statement of profit or loss has been added net of tax in the valuation.

² PV = present value; FCF = free cash flow; TV = terminal value; WACC = weighted average cost of capital.

- (b) Bongani also believes there will be savings in costs due to economies of scale that will be achieved after acquisition. The cost savings will result from EL being able to reduce IT services and personnel costs once the takeover is completed.
- (c) This amount represents the future lease instalment payments for all leases UC has entered into.
- (d) Bongani estimates that UC will only need to acquire property, plant and equipment equal to 5% of revenue in the forecast years. Intangible assets represent the movement in intangible assets from FY2023 to FY2024 and increased by 5% per annum. Bongani forecasts that UC will add to its investment in the associate in 2025 and 2026.
- (e) Current assets less current liabilities for FY2024 increased by 5% in 2025 and again in 2026.
- (f) This represents the market value of intangible assets held by UC as at 31 December 2024.
- (g) EL will only be acquiring 80% of the shares in UC. This represents a 10% minority discount applied to the valuation.
- (h) There is no listed company on the A2X which is very similar to UC, so the beta of MH Roberts Transport ('Roberts'), a company incorporated in the United States of America and listed on the New York Stock Exchange, was used. Roberts' revenues amount to more than USD10 billion³ and its app also brings together customers who want their cargo transported using trucks as well as air and sea transport. Roberts has a debt-equity ratio of 1,5. The largest customer of Roberts accounted for less than 2% of its revenue in 2024.
- (i) This represents the market-related rate on interest-bearing debt, being 12,68% per annum.
- (j) UC's target debt-to-equity ratio of 0,6 was used in the WACC calculation. This is because the current weights do not reflect what the directors believe is possible for UC.

5 Additional information

- 1 Inflation in South Africa is expected to stabilise at 5% per annum for the next ten years. South African ten-year government bonds have a yield of 12,23% per annum while the yield on bonds maturing in 2026 is 8,80% per annum.
- 2 The expected market return on the South African equity market is currently 13,45%.
- 3 The transport industry is expected to have an annual growth rate of 5% for the next three years, then stabilise at 5,9% thereafter.
- 4 The corporate tax rate in South Africa is 27% and is expected to remain the same during the investment period.
- 5 The formula to lever and un-lever beta coefficients is as follows:
Hamada formula: $\text{Beta (levered)} = \text{Beta (unlevered)} \times [1 + [(1 - \text{tax rate}) \times (\text{debt} / \text{equity})]]$
- 6 All amounts are material.

³ USD = United States dollar.

INITIAL ASSESSMENT OF COMPETENCE, JUNE 2025

PROFESSIONAL PAPER 1

**This paper consists of one scenario and THREE required parts.
Answer each required part in a separate answer book.**

| PAPER 1 PART I – REQUIRED | | Marks | |
|---------------------------|---|-----------|-----------|
| | | Sub-total | Total |
| (a) | With reference to the development of the CargoPlat™ app – | | |
| | (i) explain, with reasons, from which date an intangible asset should have been recognised given that the CargoPlat™ app meets the definition of an intangible asset in terms of IAS 38; and | 7 | |
| | (ii) prepare an extract of the prior period error note in the financial statements of UC for FY2024. | 8 | |
| | <ul style="list-style-type: none"> Only present any correction for each individual financial statement line affected and do not present any subtotal or total of any statement. Do not present the totals of the closing balance of equity items at the end of the year. Narrative information is not required. Ignore all forms of taxation. | | |
| | <i>X1: Communication skill for part (a)(i) – logical argument</i> | 1 | 16 |
| (b) | With reference to the lease agreement with ITT – | | |
| | (i) discuss whether you agree that UC may have elected the recognition exemption at the commencement of the lease; and | 4 | |
| | (ii) prepare the journal entries to correct all aspects of the lease on 1 January 2024. | 12 | |
| | <ul style="list-style-type: none"> Irrespective of your answer in part (b)(i), assume that UC has not elected the recognition exemption. Assume that journal entries that relate to any previous financial year cannot be posted to the previous year, and that any correction should be made to the opening balance of the items as at the beginning of the current year. Assume the corrections are material. Ignore all forms of taxation. | | |
| Total for part I | | | 32 |

INITIAL ASSESSMENT OF COMPETENCE, JUNE 2025

PROFESSIONAL PAPER 1

This paper consists of one scenario and **THREE** required parts.
Answer each required part in a separate answer book.

| PAPER 1 PART II – REQUIRED | | Marks | |
|----------------------------|--|-------------|------------|
| | | Sub-total | Total |
| (c) | Discuss whether or not UC's financial statements for FY2024 are required to be audited or if an independent review would be sufficient. <i>X1: Communication skill – logical argument</i> | 10 1 | 11 |
| (d) | Discuss the ethical requirements that Ingxelo will have to consider as part of the pre-engagement activities of the audit of UC's financial statements for FY2024. <ul style="list-style-type: none"> Do not discuss the significance considerations of the SAICA or IRBA Codes of Professional Conduct. Do not provide safeguards. <i>Y6: Ethical reasoning</i> | 11 1 | 12 |
| (e) | Describe the substantive tests of detail procedures you would perform to obtain sufficient appropriate audit evidence regarding the initial recognition and measurement as well as the subsequent measurement of the individual lease liability relating to the office building and the warehouse for FY2023 and FY2024. <ul style="list-style-type: none"> Assume that the present auditors are not relying on the work of the previous auditor. <i>X1: Communication skill – clarity of expression</i> | 14 1 | 15 |
| Total for part II | | | 38 |

INITIAL ASSESSMENT OF COMPETENCE, JUNE 2025

PROFESSIONAL PAPER 1

This paper consists of one scenario and **THREE** required parts.
Answer each required part in a separate answer book.

| PAPER 1 PART III – REQUIRED | | Marks | |
|-----------------------------|--|-----------|------------|
| | | Sub-total | Total |
| (f) | Perform an analysis of the financial information, based on the extracts from the management accounts prepared by Bongani by – | 19 | |
| | (i) calculating profitability and liquidity ratios; and | 10 | |
| | (ii) commenting on the outcome of the calculations you performed in part (f)(i). | | |
| | <ul style="list-style-type: none"> Your calculations should include unit economic ratios. Do not perform an analysis on the free cash flow valuation performed by Bongani. | | |
| | <i>Y1: Critical thinking for part (f)(ii)</i> | 1 | 30 |
| (g) | Criticise the free cash flow valuation performed by Bongani. | 19 | |
| | <ul style="list-style-type: none"> Do not re-perform the valuation. Assume that calculations are arithmetically correct. | | |
| | <i>Y2: Integrative thinking</i> | 1 | 20 |
| Total for part III | | | 50 |
| TOTAL FOR THE PAPER | | | 120 |