

Part (a) Discuss, with reference to section 1.3 (Reprop: Auditors), the matters JEM Inc. should consider regarding its appointment as the auditors of Reprop for FY2024.		Marks
<b>Client considerations – management integrity</b>		
1.1	<p>Management integrity concerns arise from the <b>non-compliance with laws and regulations</b> that increase the concern of <b>integrity of management</b> and should have been considered by JEM Inc. when deciding whether to accept Reprop as an audit client.</p> <p>The following specific instances of non-compliances with laws and regulations increase the concern about the integrity of management:</p> <ol style="list-style-type: none"> <li>Removal: In terms s91(6) (read with s89(2)) of the Companies Act, auditors can only be removed from office by the board (with a majority vote). <b>The CEO cannot make the decision to remove the auditors alone without the majority vote from the board of directors.</b></li> <li>Appointment: The CEO appears to have appointed the auditors himself (appointment), and – <ol style="list-style-type: none"> <li>it seems as if the <b>audit committee</b> was not involved in the process and/or <b>recommendation</b> of appointing JEM Inc. (s94) and did not review the independence of JEM Inc.; and</li> <li><b>the shareholders</b> should have <b>appointed</b> the audit firm at the <b>AGM</b> in terms of s61(7)(c) of the Companies act. (The board can only appoint if a vacancy arises but then the whole board and not just one director must make this decision.)</li> </ol> </li> </ol>	<p>1</p> <p>1</p> <p>1</p> <p>1</p>
1.2	The fact that management <b>terminated</b> the previous auditor's services based on a <b>disagreement</b> could also be indicative that <b>management's integrity</b> is questionable.	1
<b>Client considerations – vacancy</b>		
2	The change in auditors appears to have taken place without following the necessary processes in terms of the Companies Act and therefore JEM Inc. would have had to consider whether a <b>valid vacancy exists in terms of s90.</b>	1
<b>Auditor's consideration – ethical requirements / independence</b>		
3.1	The audit partner is a CA(SA) and a RA in Public Practice providing assurance services and should therefore comply with the SAICA and IRBA Codes of Professional Conduct, specifically <b>Parts 1, 3 and 4A</b> for an assurance engagement.	1
3.2	<p>In terms of the CoPC, s320, JEM Inc. is required to <b>contact the predecessor</b> auditor and also obtain (written) permission to comply with this professional requirement.</p> <ul style="list-style-type: none"> <li>However, because the change in auditors was due to a <b>dispute</b> with the previous designated auditor, JEM Inc. would need to consider whether it will be able to <b>receive permission</b> from Reprop to contact the previous auditor or <b>should have declined the appointment</b> in accordance with ET320.6a; and</li> <li>Consider whether, since there was a <b>dispute</b> with the CEO, there might <b>be reasons</b> given by the previous auditor that would cause us to not accept the audit.</li> </ul>	<p>1</p> <p>1</p>
3.3	<p>The CEO has stated that he decided to change audit firms based on a <b>dispute with the prior engagement partner.</b></p> <p>This could indicate a possible <b>intimidation threat (½) to independence (½)</b> because –</p> <ul style="list-style-type: none"> <li>in the future if the auditors disagree with management, they <b>will threaten</b> the auditors with dismissal.</li> </ul>	<p>1</p> <p>1</p>

3.4	JEM Inc. being a <b>much smaller audit firm</b> than the previous auditor, could create a <b>self-interest or intimidation threat (½) to independence (½)</b> because Reprop could possibly now compromise a significant portion of JEM Inc's Revenue, and therefore <ul style="list-style-type: none"> <li>they might be worried about losing the client (self-interest) / the client might use this to threaten the auditors in the future if the auditors disagree with management (intimidation).</li> </ul>	1
<b>Auditor's consideration – financial and reputational risk</b>		
4	With no other information available to conclude otherwise, it appears that as it is a <b>large, listed entity</b> with significant operations, it <b>should be able to pay the audit fee.</b>	1
5	<b>Reputational Risk:</b> Reprop's business is the development of new properties in suburban areas across South Africa. This appears to indicate a good reputation in the <b>market and an industry</b> that JEM Inc. would possibly want to be associated with. / Although, the risk of association increases as Reprop is a listed company and therefore a <b>high-profile client</b> with a lot of public interest.	1
<b>Auditor's considerations – resources and competence</b>		
6.	Reprop will be a <b>new client</b> and if the necessary access to work papers cannot be obtained, JEM Inc. will need to assess whether it will have enough <b>additional resources</b> to also perform additional procedures to verify the <b>opening balances</b> of Reprop.	1
7.	JEM Inc. is a small firm with two registered audit partners, two audit managers and ten trainee accountants, while the previous auditor firm was one of the biggest in SA. Due to the size of the firm, JEM Inc. should consider whether it has the necessary <b>resources of staff and time</b> to allocate to the audit of Reprop.	1
8.	JEM Inc. is <b>based in Durban</b> while Reprop's main developments are in the <b>metropolitan areas</b> of Tshwane, Cape Town and Nelson Mandela Bay. This raises a concern on whether JEM Inc. has the resources <b>in the relevant areas</b> to complete the audit effectively.	1
9.	Reprop is listed and JEM Inc. might not have <b>experience of a listed entity</b> or staff that have the necessary knowledge to perform an appropriate audit for a listed entity and within this <b>industry / complex property company. It might need to consult an expert.</b>	1
10.	JEM Inc. has two audit partners and therefore it must ensure that it has internal quality control processes in place and an <b>engagement quality reviewer (EQR)</b> available who are sufficiently competent and independent (eligible to be performing the work) because Reprop is listed.	1
11.	As Reprop's financial statements are prepared <b>in accordance with IFRS®</b> Accounting Standards, JEM Inc. should have the necessary knowledge or consider obtaining the knowledge should it not be familiar with these standards (if it has only knowledge of IFRS for SME).	1
<b>Engagement terms and pre-conditions</b>		
12.	As a <b>listed entity</b> Reprop is required to comply with IFRS® Accounting Standards and it appears that an <b>acceptable financial reporting framework</b> is used by the entity. (ISA210.6(a))	1
13.	Reprop has signed the standard engagement letter without any amendments or restrictions and thus management <b>acknowledged its responsibilities</b> with no limitation of scope. (ISA210.6(b))	1
<b>Available</b>		<b>23</b>
<b>Maximum</b>		<b>12</b>
<i>X1: Communication skill – logical argument</i>		<b>1</b>
<b>Total for part (a)</b>		<b>13</b>

Part (b) With reference to section 1.4 (Reprop: Municipal billings) – (i) discuss the risks of material misstatement at the assertion level for the contingent liability of Reprop in FY2024;		Marks
1.1	Management lacks integrity as they have not reported the error to the municipality and ‘know someone who can make the problem disappear’. This <b>increases the risk of fraudulent financial reporting</b> related to the understatement of the contingent liability. (all assertions)	1
1.2	Due to this overall risk, there is a risk that because this disclosure relates to a present liability, it will be more <b>susceptible to understatement</b> of the amount and disclosure due to the overall integrity of management and having a vague disclosure (completeness, accuracy, valuation and allocation).	1
2.	This is <b>the first time</b> that management have made an estimate of this nature. Their <b>inexperience and unfamiliarity</b> increase the <b>risk of error</b> associated with the appropriate treatment and valuation of the contingent liability.  Management’s estimate of R1 million exactly does not appear to be based on any <b>actual water and electricity readings</b> or municipal tariffs. The ‘round amount’ might be rounded up/off and thus may not be correctly calculated.	1  1
3.	The communal areas consist of the security guardhouse, streetlights, gym, restaurant, swimming pool, clubhouse and park (various areas).	
3.1	There is a risk that <b>not all</b> electricity and <b>water usage have been included</b> in the estimate because the communal property includes meters that Reprop is <b>not aware</b> of (the calculation only includes those they could identify) (completeness) or	1
3.2	The reading of the meters is <b>done incorrectly</b> . (accuracy, valuation and allocation).	1
4.	In performing the calculation, the usage according to the bulk meters was multiplied with the <b>2021 rate and the 2022 rate</b> and there is a risk that the wrong rates might be used as <b>these are not the same</b> .	1
5.	The <b>uncertainty</b> in whether there is a provision, contingent liability or none of the two can be manipulated through interpretation of the definitions due to <b>subjectivity</b> :	
5.1	There is a risk that the contingent liability (present obligation) is not <b>correctly classified</b> but should instead be recorded as a <b>provision / liability</b> in terms of the <b>definitions in IAS37</b> as there is an actual obligation which is certain (classification) with uncertain timing and amount.	1
5.2	Although the event (water and electricity usage) giving rise to the present obligation has occurred, it has not yet been confirmed whether this will result in an <b>outflow of resources</b> embodying economic benefits as the municipality. Therefore, there is a risk that the ‘ <b>possibility of any outflow in settlement is uncertain</b> and might be remote’.	1
6.	It appears that the entity is not charged for water and electricity and therefore there is a risk that <b>property taxes</b> are also not charged and should also be included in the liability. The contingent liability may also be understated as it is calculated using only the meter readings and does not include any <b>penalties</b> for non/late payment or <b>possible interest</b> . (completeness of the amount)	1
7.	There is a risk that the amount due could in fact <b>have been transferred</b> to the Spark-HOA on the transfer of the communal property. Therefore, the correct <b>legal position</b> should be considered; whether the obligation is that of Reprop or rather the Spark-HOA (obligation).	1
8.	Debt due is extinguished after the lapse of time (three years) and therefore the 2021 debt may have prescribed in 2024 (three-year prescription rule applies to	

	water and electricity charges) and may therefore <b>no longer be owed</b> by Reprop and be incorrectly included in the closing balance. (obligation)	1
9.	The <b>vague description</b> increases the risk that the contingent liability may not be properly <b>presented or disclosed</b> in the financial statements (presentation).	1
<b>Available</b>		<b>13</b>
<b>Maximum</b>		<b>6</b>
<b>Total for part (b)(i)</b>		<b>6</b>

<b>Part (b) With reference to section 1.4 (Reprop: Municipal billings) – (ii) formulate substantive test of details procedures to verify the existence, accuracy, valuation and allocation, and presentation, of the contingent liability of Reprop for FY2024.</b>		<b>Marks</b>
<b>Existence</b>		
1.	With the <b>permission</b> of the client,	1
1.1	obtain a <b>legal opinion</b> / confirmation letter (direct external third party) to determine the <b>extent of probability</b> / confirming any other details like fines or penalties for late/non-payment and	1
	a. inspect the expert's CV / affiliation with professional body to confirm his/her <b>competence</b> ; and	1
	b. enquire about any conflict of interest that might exist to assess his/her <b>independence</b> .	1
2.	Inspect minutes of the board of directors' meetings to confirm that the directors accepted the <b>existence of the contingent liability and/or approved</b> the recording of the obligation as a contingent liability.	1
<b>Accuracy, valuation and allocation</b>		
3.	Obtain the schedule of <b>management's calculation</b> of the contingent liability and <b>reperform</b> the client's calculation of the R1 million (usage x tariffs for 24 months) obligation for <b>mathematical accuracy</b> .	1
3.1	Through inspection agree the amount recalculated (R1 million) to the amount <b>disclosed</b> in the note to the <b>financial statements</b> to confirm the accuracy of this amount.	1
4.	Perform the following procedures to evaluate the basis on which the amount was determined to decide whether a reliable estimate could be made:	
4.1	Enquire from management about the <b>process/method followed</b> for the calculation of the contingent liability and the acceptability of the method in terms of the IFRS requirements.	1
4.2	Enquire from management, who performed the calculation and through inspection verify the qualifications, objectivity and based on past calculations whether <b>reliance can be placed</b> on the person's work.	1
4.3	Through inspection ensure that the calculation includes <b>the full period</b> from the commencement date until the communal property was handed over to the Spark-HOA (2021-2022 being 24 months, excluding from 1 January 2023 onwards).	1
4.4	Inspect the purchase agreement / title deeds to verify the <b>transfer dates of ownership</b> in order to verify that they need to include all months of 2021-2022 in the calculation.	1
4.5	Inspect the purchase/sales agreement with Spark-HOA to identify any <b>terms and conditions</b> relating to possible <b>outstanding municipal amounts</b> (would these amounts transfer) / obligation transfers.	1
4.6	Agree through inspection <b>the municipal tariffs</b> to the prescribed / approved rates as published on the Tshwane municipality website.	1
4.7	Inspect management's contingent liability calculation to ensure that <b>different municipal rates</b> were used for the different financial periods of the municipality	1

	(2021-2022). Inspect <b>water / electricity readings</b> to confirm the water and electricity usage.	1
5..1	<b>Based on all the above verified inputs, calculate your own estimate</b> (auditor's own calculation / estimation range) by using the tariffs and usage and months verified for electricity and water.	1
5.2	<b>Compare this</b> with management's calculation (recalculated) to assess the reasonability of the calculation (and discuss any difference with management). For any differences noted, enquire from management on the reasons and obtain <b>corroborative evidence</b> to support management's explanations.	1
5.2		1
<b>Presentation (and disclosure)</b>		
6.	Inspect that <b>disclosure</b> has only been made in the notes and that there is no recognition within the AFS ( <b>no journal adjustment</b> ).	1
7.	Through <b>inspection of the notes</b> to the annual financial statements at 31 December 2024, verify that the following has been disclosed in terms of IAS37. Specifically inspect for the following:	1
7.1	The <b>description of the nature</b> of the contingent liability (updated and not being vague anymore);	½
7.2	An estimate of the <b>financial effect of R1 million</b> or agree the amount with the amount in the disclosure and ensure they agree;	½
7.3	<b>Uncertainties</b> relating to the amount of timing of outflows;	½
7.4	Material <b>assumptions</b> used by directors; and	½
7.5	Explanations for any possibility of any <b>reimbursements</b> .	½
<b>All assertions</b>		
8.	Obtain a <b>signed management representation letter</b> with regard to the <i>existence, accuracy, valuation and allocation and presentation</i> of the contingent liability for FY2024.	1
9.	<b>Subsequent events testing</b> – enquire from management or inspect minutes of meetings, legal letters, or any municipal invoice that may have been received <b>after year end</b> to verify the amount disclosed / assumptions. (all assertions)	1
10.	Consider engaging the services of an <b>auditor's expert</b> should the auditor not be able to obtain sufficient, appropriate audit evidence to verify the contingent liability.	1
<b>Note:</b> The verification of all these assertions are to evaluate whether there is a legal or constructive present obligation arising out of a past event that actually occurred; evaluate the probability that an outflow of resources will be required to settle the obligation; and evaluate whether the possible obligation will only be confirmed by the occurrence of non-occurrence of an uncertain future event not wholly in the control of the entity in terms of IAS37; or rather a provision which is a 'liability of uncertain timing or amount'  The uncertain future event could be argued to be the fact that the municipality will issue a backdated invoice to Reprop; or the usage could be argued to be the event that has already taken place and thus creates the possibility of recognising a provision instead.		
<b>Available</b>		<b>25½</b>
<b>Maximum</b>		<b>13</b>
<b>Total for part (b)(ii)</b>		<b>13</b>
<b>Total for part (b)</b>		<b>19</b>

Part (c) Discuss, with reference to section 1.4 (Reprop: Municipal billings), the ethical concerns related to Reprop's decision not to report the municipal underbilling.		Marks
<ul style="list-style-type: none"> <li>Do not discuss any aspects related to the SAICA or IRBA Codes of Professional Conduct.</li> </ul>		
<b>1</b>	<b>Good for self and for others</b>	
<b>Self</b>		
1.1	Not paying municipal bills might provide <b>short-term financial relief</b> but damages long-term reputation and credibility. (Short term)	1
1.2	Ethical conduct ensures <b>sustainable success</b> and respect in the community. By not paying its municipal bill, Reprop may hamper the respect it has gained in the community, and furthermore, this may impact Reprop's ability to operate its business because future buyers will be worried that they will inherit unpaid municipal bills. (Long term)	1
1.3	Non-payment of municipal bills is a <b>breach of legal obligations</b> (the management signed a legal contract with the municipality). (Non-compliance with laws and regulations)	1
1.4	It does not appear as if Reprop obtained a <b>clearance certificate</b> when it transferred ownership of the common areas to the Spark-HOA. (Non-compliance with laws and regulations)	1
<b>Others</b>		
1.5	Not paying municipal bills compromises the <b>local government's ability to provide essential services</b> such as water, electricity, sanitation and infrastructure maintenance. (Ubuntu)	1
1.6	This can lead to a decline in the quality of life for the <b>entire community</b> , especially affecting vulnerable groups who rely heavily on these services.	1
<b>2</b>	<b>Ethical frameworks</b>	
2.1	<b>Virtue ethics</b> 'Doing the right thing even when nobody is watching', the CFO should go to the municipality <b>and declare</b> the amount that was not billed during construction as this is the right thing to do.	1
2.2	<b>Deontological theory</b> 'Acting based on duty' required the directors in their role to disclose the material information honestly ( <b>directors' duties</b> ), and the omission of the contingent liability breaches their duty.	1
2.3	<b>Utilitarianism</b> 'Acting based on what maximises well-being of greater majority', which means that the non-disclosure of underbilling may affect <b>public service delivery (majority)</b> and may lead to long-term negative consequences for the <b>well-being of the society</b> .	1
<b>3</b>	<b>Companies Act</b>	
3.1	All of the above matters are <b>not in the best interest of Reprop</b> and the Spark-HOA (not good for the companies), and this can have <b>legal implications</b> as the municipal account may be handed over to attorneys, and the companies may be liable for the underbilling as well as the legal fees. (S76)	1
3.2	In addition, the municipality may <b>impose fines or penalties</b> that would have additional financial <b>implication for Reprop</b> .	1
3.3	The directors may face consequences as a result of their failure to execute their fiduciary duties and the <b>directors will be held liable (S77)</b> .	1
3.4	Management's willingness to work with someone who will <b>'make the problem disappear'</b> are likely to be fraudulent in nature and be <b>unlawful. (Illegal)</b>	1

<b>4.</b>	<b>King IV</b>	
4.1	Through being aware of the underbilling and doing nothing about it / not accounting for it properly in the financial statements, the governing body will be in breach of <b>King IV Principle 1 'Ethical and effective leadership'</b> (ethical culture) - due to their actions of not being honest and transparent. (P1-3)	1
4.2	This will have a severe impact on the credibility of Reprop because the company will not be viewed as a <b>responsible corporate citizen</b> . (P16)	1
<b>Available</b>		<b>15</b>
<b>Maximum</b>		<b>6</b>
<b>Total for part (c)</b>		<b>6</b>

Part (d) Discuss any concerns you may have with regard to the Spark-HOA's compliance with the Companies Act.		Marks
<ul style="list-style-type: none"> <li>Do not discuss any concerns related to section 45 of the Companies Act.</li> <li>Do not discuss any concerns related to the composition of the audit committee.</li> </ul>		
<b>Removal of a director – Mr Archie Fernando (s71)</b>		
1	A director may be removed by an ordinary resolution, but before the members may consider such a resolution the director must be given notice of the meeting and the resolution:	
1.1	However, it appears that the <b>removal was spontaneous</b> and was because of the complaints from the members about the finance portfolio.	1
1.2	The resolution was not communicated to Archie as <b>no such resolution</b> was noted in the agenda of the meeting. The removal of Archie was initiated during <b>the AGM</b> .	1
2	The director must be afforded a reasonable <b>opportunity to make a presentation</b> , in person or through a representative, to the meeting before the resolution is put to a vote – the <b>minutes of meetings do not indicate</b> that Archie was given an opportunity to make a presentation or to respond to the concerns of members regarding the finance portfolio.	1
<b>Contract services approval (s73)</b>		
3.	The chairman of the board dismissed and approved a new garden service and appointed a new security company as of 1 January 2024, but s73(5)(b) and (d) require <b>a majority of directors</b> to be present at any vote and there needs to be a majority of the votes cast on a resolution to approve that resolution. <b>It appears that the chairman is making decisions alone without a majority vote being cast.</b>	1
4.	Carol noted that contractors had been approved via a message in the board of directors' WhatsApp chat group and it is unlikely <b>that proper records were kept</b> about these discussions and resolutions. This is a concern, as resolutions adopted by the board must <b>be dated and sequentially numbered</b> (and kept for seven years) and it would <b>not have been signed</b> by the chair if it was only on a <b>WhatsApp chat group</b> .	1
<b>Appointment of L&amp;P Registered Auditors (s90)</b>		
5.	Joe assured the members that the audit company, L&P Registered Auditors Inc., is separate from L&P Prop that assists the Spark-HOA with the preparation of the annual financial statements:	
5.1	Appointment: Therefore, it appears that the <b>audit committee</b> (required by the MOI) <b>was not involved in evaluating</b> the non-assurance services and the approval for the appointment (s94(a)) after evaluating the firm's independence.	1
5.2	Independence: It is questionable whether L&P Registered Auditors Inc. is <b>independent given</b> that its subsidiary company (L&P Prop) has been appointed as the preparers of Spark-HOA's AFS. This should have been evaluated first.	1
6.	<b>Joe (chairman)</b> feels that the Spark-HOA audit is not mandatory because the company is a non-profit company and this indicates that as a director, he might not have the <b>necessary skills and competence</b> to be party to a decision that he does not understand.	1
<b>Directors' personal financial interests – garden services contract (s75)</b>		
7.	Joe, the chairperson of the board, is a <b>related party</b> to Joey Budden within the <b>second degree of affinity</b> , because Joey is his first-born son.	1
8.	The garden services contract therefore qualifies as a contract in which the chairperson of the board knows of a related person who holds <b>a personal</b>	



	<b>financial interest</b> in terms of s75 of the Companies Act.	1
9.	As the chairman of the board, Joe should have –	
9.1	<b>disclosed the interest and general nature</b> to the rest of the board – it does not appear as if <b>Joe disclosed</b> that the garden services company belongs to his son;	1
9.2	<b>disclosed any material information</b> relating to the matter. Joe should have disclosed that he has a vested interest in the company as both himself and his son are involved in the operations of the garden services company; and	1
9.3	<b>left the meeting</b> after making any disclosure and not have taken part in consideration of the matter except in terms of making above-mentioned disclosures. Joe should <b>not have participated</b> in the decision to grant the supply contract to the garden services company.	1
10	However, this decision, although made without complying with s75(5), can still be valid if an <b>ordinary resolution</b> of the members of the Spark-HOA <b>ratified</b> it.	1
<b>Standards of directors' conduct (s76)</b>		
11	A director of a company must –	
11.1	not use the <b>position of director</b> or any information obtained while acting in the capacity of a director to gain <b>an advantage</b> for the director – it appears that Joe used his position as the chairperson of the board to obtain a garden services contract that he runs together with his son;	1
11.2	not <b>knowingly cause harm to the company</b> – he may have caused financial harm to the company by approving a contract that may be above the mandate of R250 000 without the approval of the members, or he approved contracts that other directors deemed unnecessary and wasteful (financial impact).	1
11.3	when <b>acting in that capacity</b> , exercise the powers and perform the functions of a director in <b>the best interests of the company</b> – he approved a contract that was not B-BBEE compliant, and insisted on the approval of contracts without providing other directors with sufficient reasons; and	1
11.4	act with the <b>degree of care, skill and diligence</b> that may reasonably be expected – Joe also did not follow the correct procedures as the contract was approved via a WhatsApp communication with no proper board resolutions being passed.	1
<b>Other concerns</b>		
12	Due to the non-adherence to s75 and 76, the director of a company can be held <b>liable in terms of s77</b> .	1
13	The MOI is a binding agreement, and certain provisions of <b>the MOI were breached</b> (e.g. improvements to the clubhouse and common areas were seemingly not approved of at the AGM, given that the directors felt that some of the improvements were unnecessary), thereby breaching s15(6) of the Companies Act.	1
<b>Available</b>		<b>20</b>
<b>Maximum</b>		<b>13</b>
<b>X1: Communication skill – clarity of expression</b>		<b>1</b>
<b>Total for part (d)</b>		<b>14</b>

Part (e) Discuss Carol's professional responsibility relating to the information that she discovered at and after the AGM of the Spark-HOA.		Marks
<b>SAICA Code of Professional Conduct (CoPC)</b>		
1.	Carol is a <b>CA(SA) in business</b> and has been appointed <b>as a director</b> of the Spark-HOA. She is therefore required to adhere <b>to parts 1 and 2</b> of the SAICA Code of Professional Conduct (CoPC).	1
2.	Based on the information discovered during and after the AGM, Carol fears that the role of the board chairperson has not been executed as it should, and the board <b>has been making decisions without informing</b> the Spark-HOA members. This is <b>contrary to the MOI which states</b> that – <ul style="list-style-type: none"> <li>directors cannot approve contracts exceeding R250 000 without the approval of the majority of all Spark-HOA members;</li> <li>all improvements to the clubhouse and common areas can only be made following approval at an AGM;</li> <li>a stringent process to appoint new contractors with consultation of the board and the members of Spark-HOA should be followed, but new garden and security companies were appointed with 13% higher fees; and</li> <li>emergency expenditure must be circulated to the members for approval by means of a resolution.</li> </ul>	2
3.	3.1 Carol has also identified that Joe <b>has a conflict of interest</b> with the gardening services contract, which does not appear to have been declared <b>in terms of s75</b> of the Companies Act. 3.2 All these actions contravene <b>s76 of the Companies Act</b> on the conduct of the directors.	1 1
4.	The non-compliance with the Companies Act by Joe represents non-compliance with laws and regulations in terms of <b>s260 of the CoPC</b> and requires Carol to respond appropriately. A <b>self-interest</b> (½) or <b>intimidation threat</b> (½) to the principles of <b>integrity</b> (½) and <b>professional behaviour</b> (½) is created when a professional accountant becomes aware of non-compliance or suspected non-compliance with laws and regulations. 4.1 Integrity: If Carol does nothing, she would not be acting with integrity as required by the CoPC. She has a responsibility to act and <b>respond honestly</b> after identifying the non-compliance. 4.2 Professional behaviour: The non-compliance would <b>discredit the profession</b> if the public became aware that Carol did not act appropriately in response to her discovery / Carol will not be <b>complying with the Companies Act</b> if she does <b>not take action</b> as a director in the best interest of the company.	2 1 1
5.	Carol must <b>evaluate the impact</b> of these threats: 5.1 The additional expenses incurred by the Spark-HOA by appointing contractors that are more expensive, e.g. a security company which <b>charges 13% more</b> than the previous company, <b>appear significant</b> . 5.2 Non-compliance with the <b>MOI and Companies Act</b> may result in the directors being held <b>personally liable</b> (s77).	1 1
6.	Therefore, the threat is <b>not at an acceptable level and she should respond in terms of the CoPC to address the threat</b> .	1
<b>NOCLAR response</b>		
7.	Carol is the newly qualified CA(SA) and the finance member of the board and therefore as the <b>senior professional accountant</b> , Carol must address the above threats by taking appropriate action in terms of s260 of the CoPC. <u>Obtain an understanding (260.12)</u> 7.1. Carol must ensure she has <b>obtained a full understanding</b> of the circumstances surrounding the appointment of the contractors.	1

	7.2. She must consider whether she needs to <b>report the matter</b> to any appropriate authority, such as the <b>Community Schemes (CSOS) ombudsman</b> , while maintaining her responsibility of confidentiality.	1
	7.3. She should also consider if she needs <b>external legal advice</b> or should consult with a <b>professional body</b> if she is unsure on the action to follow.	1
	7.4. Carol should assess the <b>potential consequences</b> to the company and its members.	1
8.	<u>Address the NOCLAR (260.14)</u>	
	8.1. Carol should bring the non-compliance to the <b>attention of the board of directors</b> (those charged with governance of the Spark-HOA).	1
	8.2. Carol should have the consequences of the non-compliance <b>rectified, remediated or mitigated by the Board</b> .	1
	8.3. Carol should consider <b>withdrawing from her directorship</b> of the HOA.	1
9.	Carol should consider <b>informing the auditor</b> , as this would most probably also constitute a <i>reportable irregularity</i> . Carol needs to ensure that Reprop will discuss this with L&P Registered Auditors Inc. and ensure that this matter (Joe's conflict of interest) is reported to all the members of the Spark-HOA. (CoPC 260.18 A2).	1
10.	<u>Determining whether further action is needed</u> Carol should assess the <b>appropriateness of the board's response</b> to the NOCLAR and determine whether further action is required. (CoPC 260.16-17)	1
11.	Determining whether <b>further action</b> is needed (CoPC 260.16) and further disclosures:	
	11.1 Carol should <b>obtain proof</b> that the matter of all contractors in excess of R250 000 has been <b>communicated to all the Spark-HOA members</b> .	1
	11.2 The board should <b>reassess the appointment of all contractors and ratify</b> the current contracts if deemed suitable for the Spark-HOA or be <b>cancelled</b> if a more suitable contractor is identified.	1
12.	<u>Documentation (260.23)</u> Carol <b>should document</b> the substance of the issue, the details of any discussions, the decisions made and the rationale for those decisions.	1
<b>Other</b>		
13.	As a member of the board (director), <b>Carol</b> also has a <b>fiduciary duty to act</b> in the best interest of the company in terms of <b>s76 of the Companies Act</b> and to thus act to <b>rectify and prevent future re-occurrence</b> of such events (contract approvals).	1
<b>Available</b>		<b>25</b>
<b>Maximum</b>		<b>11</b>
<b>Y6: Ethical reasoning</b>		<b>1</b>
<b>Total for part (e)</b>		<b>12</b>
<b>Total for part I</b>		<b>64</b>

Part (f) Critically evaluate whether the decisions of the board of directors of Spark-HOA align with its strategic objectives.		Marks
<ul style="list-style-type: none"><li>Do not discuss sustainability and environmental strategic goals.</li><li>Do not discuss regulatory compliance and governance issues.</li></ul>		
<i>Maintaining and enhancing property values</i>		
1	The board of directors have a new contract for gardening services to ensure the upkeep of the property and landscaping. As a result of family relationship relating to the garden services, the upkeep standard may not be what it ought to be.	1 1
2	To ensure the uniform appearance of homes and common areas, the same solar and water backup solutions are proposed for all the homes, and this will ensure that the uniform appearance is maintained.	1
3	Although Carol has questioned the necessity of some expenses, it appears that improvements have been made to the estate and this will enhance the value of the properties in the estate.	1
<i>Financial stability and transparency</i>		
4	At the recent AGM, the members of Spark-HOA appointed a new person to fill the finance portfolio to ensure that the review of annual budgets and financial statements is done timeously.	1
5	In addition, L&P Prop has been appointed to prepare annual financial statements on behalf of Spark-HOA and this will help ensure that members receive accurate financial statements, as the annual financial statements will be prepared on time and reviewed by a qualified CA(SA) for approval in good time by the board of directors.	1
6	L&P RPA has been reappointed to audit the annual financial statements, although the validity of this reappointment is questionable given that a subsidiary of L&P RPA has been appointed to prepare the financial statements	1
7	The chairman of the board has raised concerns about the late payment of levies by homeowners and financial statements not being approved on time. This can hamper the Spark-HOA's ability to maintain sufficient reserves.	1
8	Entering into a contract that is more costly than the current contract (e.g., the garden service), could result in a wasteful expenditure should the new contract not result in a benefit for the Spark-HOA.	1
9	In addition, the financial ability to maintain the common properties could be negatively impacted by aspects such as Joe approving two new contracts of over R1,5 million, which will result in more cash reserves being required to cover these contracts.	1
10	It is worth noting, however, that despite the late collection of levies, it appears that the Spark-HOA has enough cash reserves as the board has proposed that the cash reserves be used to finance a project that requires over R17,4 million.	1
<i>Community engagement and communication</i>		
11	It appears there is communication with members, although there are complaints that the communications are late.	1
12	There is no indication of any social media or website for the Spark-HOA.	1
13	However, there seems to be a regular AGM where all members are kept up to date with all the necessary information relating to the HOA.	1
14	The communication relating to the appointment of contractors is not in accordance with the rules of the Spark-HOA and this may indicate that the directors are not maintaining open lines of communication with the members.	1

<i>Safety and security</i>		
15	A 24-hour guard ensures that the residents of the Spark-HOA live in a safe environment, and this includes state-of-the-art security gates that limit unauthorised entry into the estate.	1
16	A new security company has also been appointed, which charges 13% more than the previous security firm. This may indicate that this is an experienced firm that will ensure the safety of the residents. OR it may indicate that the new security firm is in collusion with the chairperson of the board and this decision may not be to the benefit of the homeowners.	1
17	On the other hand, since there was no indication that sufficient due diligence on the security company was carried out, and this may compromise the security of the estate as a whole, if the security company is not up to standard with the current security demands of the estate.	1
<b>Available</b>		<b>18</b>
<b>Maximum</b>		<b>9</b>
<b>Total for part (f)</b>		<b>9</b>

<b>Part (g) Perform a net present value analysis and conclude on whether the Spark-HOA should undertake to procure solar and water solutions under the Spark-HOA based on the information in the scenario.</b>						<b>Marks</b>
<ul style="list-style-type: none"><li>Assume for calculation purposes that all cash flows occur at the end of the year.</li><li>Do not consider the impact on the homeowners of savings in electricity and water costs.</li><li>Do not include the effect of the financing of the project.</li></ul>						
<b>Year</b>	<b>Calc.</b>	<b>0</b>	<b>1</b>	<b>2</b>	<b>3</b>	
		<b>R'000</b>	<b>R'000</b>	<b>R'000</b>	<b>R'000</b>	
<b>Procure under the Spark-HOA</b>						
Solar special levies	1		5 940,0	5 940,0	5 940,0	0.5
Water special levies	1		1 508,4	1 508,4	1 508,4	0.5
Solar solutions purchased	2	(13 500,6)				0.5
Water solutions purchased	2	(3 952,8)				0.5
Insurance premiums	3		(1 302,0)	(1 406,2)	(1 518,7)	0.5
Annual service fees (fixed)	4		(250,0)	(260,0)	(270,4)	0.5
Annual service fees (variable)	4		(12,5)	(28,6)	(42,5)	0.5
		(17 453,4)	5 883,9	5 753,6	5 616,8	0.5
Discount rate		15%				
Net present value		(4 293,18)				1P
<b>Calculation 1:</b>						
$((20 \times 7200)+(60 \times 4800)+(18 \times 3500)) \times 12 = 5\,940\,000$						2
$\{[(60 \times 1500)+(40 \times 960)] \times 0,8\} + \{[(35 \times 1500)+(65 \times 960)] \times 0,2\} \times 12 = 1\,508\,400$						2
<b>Calculation 2:</b>						
$((20 \times 245000)+(60 \times 155000)+(18 \times 93500)) \times 85\% = 13\,500\,550$						1
$\{[(60 \times 56800)+(40 \times 33920)] \times 0,8\} + \{[(35 \times 56800)+(65 \times 33920)] \times 0,2\} \times 0,85 = 3\,952\,840$						2
<b>Calculation 3:</b>						
$(750 \times 98 \times 12) + (350 \times 100 \times 12) = 1\,302\,000$ (adjusted by 1,08)						1,5
<b>Calculation 4:</b>						
$(290\,000 - 275\,000) / (80 - 50) = R500$ variable tariff						1
$(290\,000 - [80 \times R500])$ OR $(275\,000 - [50 \times R500]) = R250\,000$ fixed fee (adjusted by 1,04)						1
First year (variable): $25 \times R500 = R12\,500$						0.5
Second year (variable): $55 \times R500 \times 1.04 = R28\,600$						1
<b>Third year (variable):</b>						
$\{[367\,500 - (100 \times R500)] - [322\,500 - (100 \times R500)]\} / (250 - 150) = R450$ variable tariff above 100 maintenance hours						2
Alt: $(367\,500 - 322\,500) / (250 - 150) = R450$ variable tariff where hours > 100 hours						
100 – 25 – 55 = 20 hours at original tariff of R500, rest at R450						1
$(20 \times R500 \times 1.04 \times 1.04) + (65 \times R450 \times 1.04 \times 1.04) = R42\,453$						1
<b>Conclusion:</b>						
The net present value of the project is negative, which indicates that the special levy is not sufficient to cover the cash flows of the project and as such, unless the special levy were to increase sufficiently, the project is not financially viable.						1
<b>Available</b>						<b>22</b>
<b>Maximum</b>						<b>20</b>
<b>Y4: Decision making</b>						<b>1</b>
<b>Total for part (g)</b>						<b>21</b>

Part (h) Evaluate the performance forecast of the Spark-HOA in line with its sustainability, environmental stewardship and strategic goals.				Marks
<ul style="list-style-type: none"><li>Assume that the water and solar solutions are procured under the Spark-HOA.</li><li>Base your evaluation on relevant non-financial performance indicators.</li></ul>				
	FY2026	FY2027	FY2028	
	%	%	%	
Decrease in average electricity consumption per home per month – more energy efficient Alt: CAGR = -14,50%	(4,17%)	(26,09)	(11,76)	1
Increase in the average electricity production (self-generating) per home per month since solar installation – more self-sustainable <i>FY2026: (1 150 – 935) = 215 kWh self-generated per month from 1 July 2025 (only producing own power for 6 months in FY2026, thus on average 430 per month since solar panels were installed)</i> <i>FY2027: 850 – 400 = 450 kWh</i> <i>FY2028: 750 – 290 = 460 kWh</i> Alt: % electricity consumed self-generated	NC	4,65	2,22	0.5   0.5 0.5
Decrease in water consumption Alt: CAGR = -10,37%	-	(20)	(10)	1
Increase/(decrease) in self-storage of water [(25 – 10) – (20 – 8)] / (25 – 10) = 20% [(18 – 6) – (20 – 8)] / (18 – 6) = 0% <i>CAGR cannot be measured for this indicator</i> Alt: % of water consumed provided from storage tanks	NC	(20)	0	1
Increase in utilisation of recycling programmes. Alt: CAGR = 10,06%	60% 8,33%	60% 15,38	66,67% 6,67	
				1
1	The installation of solar solutions is expected to create awareness of electricity consumption in general by homeowners over the longer term, as evidenced by the expected decrease in the average consumption per home per month of 26,09% in FY2027 and 11,76% in FY2028, leading to more energy-efficient behaviour and improved environmental performance for the estate.			1
2	An increase in the expected electricity self-generated per home per month of 4,65% in FY2027 and 2,22% in FY2028 shows a clear improvement in the utilisation of environmentally friendly energy (solar) in FY2027 and in FY2028, with the further improvement in self-generating electricity. There is an expectation that homeowners may gradually install more solar panels at their own cost, increasing the self-sustainability of the homes in the estate.			1
3	The gradual expected decrease in the average water consumption per home per month of 20% and 10% in FY2027 and FY2028 respectively, also shows that the water solutions are creating awareness for using water more sparingly.			1
4	The average expected self-storage of water per home decreases by 20% in FY2027 and remains constant in FY2028, which shows that there is in fact an expectation that homeowners will initially be very aware of using water more sparingly, but that a lack of commitment in the self-storage of water is expected, which indicates an area in which awareness needs to be a constant focus.			1

5	Although there is an increase in homeowners making use of the recycling programmes (15,38% in FY2027 and 6,67% in FY2028), there are still about 20 homes that are expected to not use this service, which indicates an area on which the Spark-HOA should try to improve.	1
<b>General</b>		
6	This shows that Spark-HOA could be expected to perform better on reducing their community's environmental footprint when the Spark-HOA procures the solutions as more homeowners will likely install environmentally friendly solutions than had there not been a collective effort.	1
7	Further to this, individual homeowners will procure solar and water solutions at a much slower rate than when Spark-HOA does the procurement, indicating that the Spark-HOA will perform better by reducing the community's environmental footprint at a faster rate if procurement is done collectively under the Spark-HOA.	1
8	The Spark-HOA's non-financial performance on sustainability and environmental strategic goals is estimated to be better when the Spark-HOA procures the solutions. <i>This highlights an important financial trade-off that Spark-HOA might need to consider when deciding on which option to choose for the procurement of water and solar solutions.</i>	1
<b>Conclusion</b>		
9	Overall, the expected performance of Spark-HOA in line with its sustainability and environmental strategic goals to promote water conservation and to be more energy efficient is positive, although it could perform better on promoting recycling programmes.	1
	No mention is made of using sustainable materials in community projects, which signals an area for improvement.	1
	<b>Available</b>	<b>16</b>
	<b>Maximum</b>	<b>9</b>
	<i>X1: Communication skill – logical argument</i>	<b>1</b>
	<b>Total for part (h)</b>	<b>10</b>



<b>Part (i) Write a report to the board of directors of the Spark-HOA in which you advise it on the best option for financing the solar and water backup solutions.</b>					<b>Marks</b>
<ul style="list-style-type: none"><li>Assume that the sustainability-linked loan conditions in option 2 of section 2.5 (The Spark-HOA: Financing), are met.</li><li>Assume that the water and solar solutions are procured under the Spark-HOA.</li></ul>					
<b>Report to the directors of Spark-HOA</b>					
Date: June 2025					
To: Directors of Spark-HOA					
Subject: Financing of solar and water backup solutions					
The financing options that you have considered are different, depending on the terms, and will also result in differing IRRs. Please see below the IRR based on the conditions of the loans and the recommendation that follows.					
<b>Secured loan</b>					
A					
Calculation of repayment:					
PV: R17 400,0					0.5
N: 3					0.5
I/YR: 11,75% - 1% = 10,75%					1
PMT = R7 089,4					0.5
	<b>1 Jul 25</b>	<b>30 Jun 26</b>	<b>30 Jun 27</b>	<b>30 Jun 28</b>	
	<b>R'000</b>	<b>R'000</b>	<b>R'000</b>	<b>R'000</b>	
Loan received	17 400,0				0.5
Attorney and upfront loan fees [17,4 million * 4%]	(696,0)				1
Repayment		(7 089,4)	(7 089,4)	(7 089,4)	1P
	16 704,0	(7 089,4)	(7 089,4)	(7 089,4)	
<i>Alt for marking purposes:</i>					
Capital repayment		5 218,9	5 779,9	6 401,3	
Interest paid		1 870,5	1 309,5	688,1	
IRR = 13.12 %					1P
<b>Sustainability linked loan principle</b>					
Effective interest year 1	9,5%				1
Effective interest year 2	9,5% *85% = 8,075%				1P
Effective interest year 3	9,5% *85% = 8,075%				1P
	<b>1 Jul 25</b>	<b>30 Jun 26</b>	<b>30 Jun 27</b>	<b>30 Jun 28</b>	
	<b>R'000</b>	<b>R'000</b>	<b>R'000</b>	<b>R'000</b>	
Loan received	17 400				0.5
Attorney and upfront loan fees [17,4 million * 2%]	(348)				1
Interest paid 2026 [17,4 million * 9,5%]		(1 653,0)			0.5P
Interest paid 2027 [17,4 million * 8.075%]			(1 405,05)		0.5P

Interest paid 2028 [17,4 million * [8,075%]				(1 405,05)	0.5P
Capital repayment (at 10% premium)				(19 140)	1
	17 052,0	(1 653,0)	(1 405,05)	(20 545,05)	
IRR	12,39%				1P
<b>Cash reserves</b>					
Using this financing option may result in insufficient cash reserves for Spark-HOA to pay future repairs, maintenance and improvements on common areas property. In addition to this there is an opportunity cost on interest earned of 6% per annum that will be lost if the cash reserves are spent.					1
Although this option may be the cheapest option from a financing cost point of view, it is not a viable option as the Spark-HOA will not have sufficient cash resources for the day-to-day operations.					1
<b>Conclusion</b>					
The sustainability linked loan is the cheaper option because it has a lower IRR when compared to the secured loan. Two additional benefits apply to this facility, which need to be considered:					1
No collateral is required, whereas in the case of option 1, the clubhouse will be used as collateral for the loan, reducing the Spark-HOA's ability to raise funding in future; and					1
With a bullet repayment applying, Spark-HOA will be able to manage its liquidity better					1
However, since the coupon is based on the prime rate, should the prime rate change, this will have an impact on the IRR; as such, the board will have to monitor changes in the prime rate. OR In addition, if there is a significant change in the South African economy with favourable interest rate changes and projections, the secured loan may be more cost effective.					1
<i>Report end.</i>					
<b>Available</b>					<b>20</b>
<b>Maximum</b>					<b>15</b>
<i>X1: Communication skill – layout and structure</i>					<b>1</b>
<b>Total for part (i)</b>					<b>16</b>
<b>TOTAL FOR PART II</b>					<b>56</b>