



Initial Assessment of Competence

Professional Paper 3

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Part (a) Write a report to Dino and Sipiwe in which you identify the financial and operational risks of Beita Furniture.		Marks
Report To: Dino Biko and Sipiwe Keita From: SAICA IAC Candidate Date: 23 January 20X5 Subject: Risk and strategic priorities of Beita Dear Dino Biko and Sipiwe Keita Please find below relevant financial and operating risks of Beita Furniture. Kind regards SAICA IAC Candidate (<i>'You' is not defined in the question</i>)		
1	Financial risks	
1.1	As a non-profit organization (NPO), Beita was involved in the community development in Coega and received benefits because it focused on upskilling the community. With the dissolution of the NPO, Beita Furniture may not receive the financial incentives as it may no longer meet the requirements.	1.5
1.2	Furthermore, the risk by transferring assets from a PBO to a private company, this could – • jeopardise its tax-exempt status, • which would trigger capital gains tax, donations tax, or transfer duty if not done at fair market value.	1.5 1.5
1.3	As a for-profit company, Beita runs the risk of a reduction in donations to fund the operations. The risk of Beita could face liquidity and solvency problems if the future funding of the company is not appropriately structured.	1.5 1.5
1.3.1	If it does receive donations because its profit company has the same name as the NPO, it runs the risk that it will be expected to pay back the donated funds if it is not able to provide the donors with a s18A certificate.	1.5
1.3.2	A reputational risk may arise from this financial risk if the donors get the impression that Beita is misleading donors into thinking it is still an NPO. Allegations of misrepresentation may lead to legal or regulatory action, which could result in investigations, penalties, fines imposed on Beita.	1.5 1.5
1.3.3	The risk that the donors may also change the terms and conditions relating to donations already made to the for-profit company., which Beita may not be in a position to meet, resulting in liquidity issues should the donations need to be repaid or more onerous conditions being applied.	1.5
1.4	Depending on the value paid by Dino and Sipiwe for the shares taken up (scenario is silent in terms of the value paid), there could be non-compliance with the Companies Act, which could result in potential fines etc.	1.5
1.5	Access funding:	
1.5.1	Access to funding: Beita's failure to secure the debt will hamper Beita's ability to continue its operations.	1.5
1.5.2	The risk of a low equity value may hamper Beita's ability to acquire additional funding.	1.5

1.6	Employee payments:	
1.6.1	Beita is exposed to the risk of insufficient profits being ploughed back into the company given the payment of 50% of its profits to staff in its employee for at least six months, which will hamper future growth prospects of the company.	1.5
1.6.2	There is a risk that insufficient furniture production and sales may render the business model financially unsustainable, while employees continue to be paid below the statutory minimum wage.	1.5
	In addition, there is a risk of exposing Beita to labour law non-compliance, financial penalties, legal claims, and reputational damage.	1.5
1.6.3	The profit payouts are made to employees who have been with the company for more than six months, which will mean that employees who have been with the company for less than six months will still earn below the minimum wage.	1.5
	In addition, there is a risk that this could lead to union action, unhappy and unproductive employees, fines, reputational damage, etc., in other words both financial as well as operational risk.	1.5
1.6.4	Incentives provided to workers may drive the wrong behaviour, especially when the focus is on short-term profit.	1.5
1.7	Dino and Sphiwe decided to pay a dividend during FY2025:	
1.7.1	There is no indication that they considered the liquidity of the company as required by the Companies Act and if no such considerations were made, company may in future be unable to meet its short-term obligations.	1.5
1.8	As Beita is no longer a PBO, it may not be possible for it to continue to purchase the pallets at a reduced price of R10 per pallet.	1.5
1.8.1	This may result in a significant increase in the cost of raw materials if market-related prices are paid, which it may not be able to recover in its selling price.	1.5
1.9	A monthly salary of R15 000 was offered to Joseph and Fulani until the sale of the furniture could cover Beita's monthly costs:	
1.9.1	By merely 'covering the monthly costs' with the sales, breakeven is indicated. If both employees receive an increase when Beita is breaking even, it will lead to the company making a loss once again. The timing of the increase is uncertain.	1.5
1.10.1	Existing operations: No indication is given in the scenario if the rental cost of the factory, (which was not market-related), will increase to a market-related cost, or what the timing of such a change will be. This again will increase the cost base of the business and may not be recoverable in the price of the products.	1.5
		1.5
1.10.2	Future operations: The current floor space could limit Beita's ability to grow in future, having to rent more expensive property will increase the fixed costs of Beita, potentially resulting in losses and impacting negatively on cash flow.	1.5
		1.5
1.11.1	Own assets: Beita not having insured its assets can result in financial losses in the event of theft of, or damage to the assets.	1.5
1.11.2	Absence of third-party insurance would be a risk should Joseph need to borrow a vehicle in future, and he is involved in an accident.	1.5
1.12	Beita's failure to invest in new equipment could result in ever-increasing maintenance costs, which could reduce Beita's profit as well as its future cash flows.	1.5

1.13	There is a risk that Beita's products are purchased on an infrequent basis because of the nature of the tables/benches, limiting opportunities for repeat business from the Swallows Group: negatively affecting future sales and cash flow	1.5 1.5
1.14	The company does not have proper financial governance structures in place, such proper vetting of suppliers could lead to the purchasing of inferior quality materials, or overpaying for materials purchased, or not receiving the pallets purchased, resulting in financial losses.	1.5 1.5
1.15	Should Beita contravene the development criteria of the Coega Development Corporation (CDC) then Beita will lose out on the Customs Duty and employment tax incentives, negatively impacting the financial sustainability of Beita.	1.5
2	Operational risks	
2.1	Should the quality of Beita's output not improve going forward, there is a risk that Beita's sales would be negatively impacted, as they are no longer a PBO.	1.5
2.2	Should the new wood treatment process not be tested before being implemented, there is a risk of inferior quality output being produced, impacting Beita's sales negatively.	1.5
2.3	Inferior quality output would likely expose Beita to reputational risk, which too would negatively impact Beita's profitability and value.	1.5
2.4	The company may incur warranty or damage claims if poor quality furniture fails or is returned by customers	1.5
2.5	There is a risk that the company procures stolen goods or becomes involved in corrupt activities, resulting in legal, financial, regulatory, and reputational risks.	1.5
2.6	The company may be in breach of laws and regulations such as the Companies Act if their auditors perform management functions.	1.5
2.7	It is likely that as Beita's competitors are well-established, there is a risk that they will not gain a big enough share of the market.	1.5
2.8	Should market research around customer preferences not be carried out, there is a risk that Beita will not meet customer expectations resulting in low demand, lost revenue, and inefficient use of resources.	1.5 1.5
2.9	Beita is exposed to the risk of trained staff not being retained resulting in a loss of skills and institutional knowledge, and workforce instability resulting in a disruption in its operations.	1.5
2.10	There is a risk that the transition to a for-profit model (change in strategic intent) has diminished Beita's contribution to community development, resulting in reduced social impact.	1.5 1.5
2.11	No evidence of insurance being in place: From an operational perspective, there is a risk that inadequate insurance coverage for factory-related accidents could expose Beita to substantial financial, legal, and operational consequences arising from employee injuries, property damage, or other incidents impacting business continuity	1.5 1.5
2.12	Joseph had to borrow a vehicle to pick up pallets. The fact that there is no delivery vehicle, creates a distribution risk for the company.	1.5
2.13	Dino and Siphiwe studied interior design and do not have any managerial or financial management experience. This could lead to poor management of the company.	1.5
2.14	The equipment purchased was purchased second hand, which could lead to breakdowns that could in turn result in down-time that will disrupt production.	1.5

2,15	Beita's reliance on factory space that it does not own, combined with its limited trainee workforce, may constrain its production capacity and ability to scale operations, resulting in an inability to meet increased demand from new boutique hotel contracts, potential loss of revenue, customer dissatisfaction, and reputational damage.	1.5 1.5
2.16	Zolani lacks experience:	
2.16.1	There appears to be limited review of Zolani's work, resulting in her potentially issuing erroneous reports, which could lead to poor decision-making.	1.5
2.16.2	The lack of a dedicated financial management function, coupled with Zolani's split focus between Finance and HR, increases the risk of weak financial governance, inadequate controls, and ineffective oversight of the organisation's financial resources.	1.5
2.17	The lack of segregation of duties at director level increases the risk of management override of controls, resulting in unauthorised transactions, fraud, financial misstatements, and ineffective governance going undetected.	1.5
2.18	Beita has a dependency risk on Joseph and Fulani; should they resign, it is likely that it will be difficult to replace them, which will result in Beita's operations being disrupted.	1.5
Available		85.5
Maximum		31
<i>X1: Communication skills – clarity of expression</i>		1
<i>Candidate's risks are clear and understandable</i>		
<i>Y1: Critical thinking skills</i>		
<i>Evidence of linking identified risks to the scenario</i>		1
Total for part (a)		33

Part (b) Based on the financial information in appendix 1, calculate the breakeven sales in units per month for Beita Furniture, a commercial entity, if – - Beita Furniture produces the product(s) that will provide the most profitable result; and - Beita Furniture pays Fulani and Joseph a market-related salary, pays a market-related rent and buys used pallets at market-related prices.				Marks
1	Contribution per product			
	Description	Table	Bench	
		R	R	
	Sales price	3 950	1 895	1
	Variable costs			
	Pallets – wood (at R80 per pallet)			
	4,5 pallets	(360)		1
	2 pallets		(160)	1
	Indirect materials (per plank)			
	[4,5x20xR10,10]	(909)		1
	[2x20xR10,10]		(404)	1
	Based on October 2024(could use any month) [Alt: work in terms of pallets instead of planks – 119 pallets @ R202 per pallet]			
	$[(10 \times 4,5 \times 20) + (37 \times 2 \times 20)] = 2\,380$ planks			1
	$[R24\,038 / 2\,380] = R10,10$ per plank			1

	Treatment			
	Tables [4,5x20x0,2x15/60xR15]	(67,50)		1
	Tables [4,5x20x0,8x5/60xR15]	(90)		1
	Bench [2x20x0,6x15/60xR15]		(90)	1
	Bench [2x20x0,4x5/60xR15]		(20)	1
	Lubricants			
	R5 227 [(10x4,5)+(37x2)]=119pallet			1
	R4 915 [(8x4,5)+(22x2)]= 80pallet			1
	R312 39pallets			1
	Therefore: Variable R8,00 per pallet			1
	[4,5xR8] [2xR8]	(36)	(16)	1C / 1C
	Alternative if based on time:			
	Weighted average pallet processing time:			
	Trained 10hrs = 20 pallets processed			
	Trainees: 5hrs = 5 pallets processed			
	15 hs = 25 pallets processed			
	Therefore 0,6hrs per pallet			
	R5 227 [(10x4,5)+(37x2)]=119pallets x 0,6hrs = 71,4hrs			1
	R4 915 [(8x4,5)+(22x2) = 80pallets x 0,6hrs = 48,0hrs			1
	R312 23,4hrs			1
	Cost per pallet hour = R13,33			1
	Table [4,5x0,6hrsxR13,33] = R36			1C
	Bench [2x0,6hrsxR13,33] = R16			1C
	Contribution per unit	2487,50	1 205	1C
2	Fixed costs			
			R	
	Salary			
	Fulani	25 000		0.5
	Joseph	27 000		0.5
	Treatment operator	12 000		0.5
	Carpenters [10xR4 000]	40 000		0.5
	Trainees [5xR3 200]	16 000		0.5
	Rent [200xR150]	30 000		1
	Carpentry machines:			
	Depreciation [R250 000/6/12]	3 472		1
	Lubricants and cleaning [R5 227-(119xR8)] (could use any month)	4 275		1C
	Repairs (average) [(R5 990-R3 790)+R2 740+R2 560+R2 845+R2 315+R3 060]/6	2 620		1C 1
	Treatment machine			
	Rental [R72 000 / 12 months = R6 000]	6 000		0.5
	Total	166 367		1
3	Constraints			
	Labour: Carpenters [10x8x20=1 600hx2pallets]= 3 200pallets p/m			2
	Labour: Trainees [5x4x20=400hx1pallets]= 400pallets p/m			2
	Total: 3 600pallets p/m			

	Used carpentry machines:		
	Given 1000 pallets p/m		0.5
	Treatment machines:		
	3 machines x 200 hours per month = 600 hours		0.5
	If extensive sunlight treatment $[600 \times 60 / 15] = 2\,400$ planks/20 = 120 pallets		1
	If normal treatment = $[600 \times 60 / 5] = 7\,200$ planks/20 = 360 pallets		1
	There may be a constraint on the treatment machines to produce all the tables and benches needed for customers if Beita was to grow Alt: there is no constraint at this stage which will be limit production of the product mix based on recent production volumes		1C
4	If a candidate concludes that the treatment hours are limiting then:		
	Table/treatment machine hour $[(4,5 \times 20 \times 0,2 \times 15 / 60) + (4,5 \times 20 \times 0,8 \times 5 / 60)] = 10,5$ h machine hour		1
	Bench/treatment machine hour $[(2 \times 20 \times 6 \times 15 / 60) + (2 \times 20 \times 5 / 60)] = 7,33$ h machine hour		1
	Contribution per treatment machine hour: Table R2 487,50/10,50 hours = R236,00/h Bench R1205/7,33 = R164,10/h Therefore, it is better for Beita to manufacture and sell tables rather than benches given the constraint in treatment machine hours		1C 1C 1C
	Contribution per table	2 487,50	1C
	Breakeven – number of tables (R166 367 / R2 487,50)	66.88	0.5C
	Therefore, rounded up to	67	0.5C
	If the candidate concluded that NO constraints apply		
	Mix based on Oct 2024 sales (be tolerant of a different month):		
	Tables sold (R51 350 / R3 950)	13	1
	Benches sold (R56 850 / R1 895)	30	1
	Sales mix for Oct 2024	13:30	0.5C
	Weighted contribution based on Oct 2024's sales mix $[(R2\,487,50 \times 13 / 43) + (R1\,205 \times 30 / 43)]$	R1 592,73	1C
	Breakeven 'batches'	104,45	0.5C
	In the breakeven 'batches':		
	Tables (104,45x13/43)	32	1C
	Benches (104,45x30/43)	73	1C
Available			46.5
Maximum			41
Y3: Problem-solving skills Identify that the product mix is determined by a constraint, properly identify and split fixed and variable costs			1
Y1: Critical thinking skills Properly calculate the various elements in a logical manner			1
Total for part (b)			43
TOTAL FOR PART I			76