

QUESTION 2

50 marks

Ignore value-added tax

1 Background

The FutureWyze Group is a group of companies whose ethos is 'science for social good'. The group was founded in 2015 by scientific researcher and social entrepreneur, Dr Tumelo Makgange, to support grassroots innovation and digitisation in townships and rural areas across South Africa. Her vision was to find local innovations that could be commercialised and sold across the African continent, while providing the youth with access to opportunities created by the Fourth Industrial Revolution (4IR). The group prides itself on its ethical decision making, responsible social footprint, and various donations to social upliftment programmes.

The group's head office is in Johannesburg. All companies in the group have a 31 March year end.

2 Overview of group companies

2.1 FutureWyze (Pty) Ltd ('FutureWyze')

FutureWyze manufactures, services and sells scientific labs known as 'innovation stations'. Innovation stations are solar-powered digital labs made from shipping containers. The labs are designed to promote scientific research and technological innovation. The containers are fitted with solar panels, are wi-fi enabled and contain high-value equipment. The fitted equipment includes 3D printers and digital animation equipment.

FutureWyze manufactures and services the innovation stations. It buys and refurbishes redundant shipping containers, uses recyclable materials and supports the use of renewable energy as evidenced by fitted solar panels on its innovation stations. FutureWyze's average lead time varies from 2–10 weeks, depending on the size of the order.

2.2 TransportWyze (Pty) Ltd ('TransportWyze')

TransportWyze, a wholly-owned subsidiary of FutureWyze, is a transport and logistics company that specialises in transporting shipping containers, portable accommodation and portable cabins. TransportWyze transports all of FutureWyze's shipping containers and distributes the innovation stations across the country.

2.3 EnerWyze (Pty) Ltd ('EnerWyze')

FutureWyze owns an 80% interest in EnerWyze, a solar-panel manufacturing company, which gives FutureWyze control over the relevant activities of EnerWyze. This shareholding was acquired in a single transaction on 1 April 2020 for R265 million when the net asset value of EnerWyze amounted to R320 million. On acquisition, all the assets and liabilities of EnerWyze were considered fairly valued. This subsidiary is viewed as a single cash-generating unit.

Since acquisition, FutureWyze has purchased all its solar panels from EnerWyze at its retail selling price, less a 12,5% discount. EnerWyze applies a standard mark-up of 20% on its cost price.

2.4 FutureWyze's inventory balance

A summary of the solar panels inventory account of FutureWyze is provided below. This provides the value of the solar panels transferred (inventory materials) into manufacturing (work-in-progress and finished goods innovation stations) during the financial year ended 31 March 2024 (FY2024). FutureWyze accounts for all its inventory, including parts and materials, using the weighted average valuation method, and the periodic inventory counting method.

	R
Opening inventory – 1 April 2023	6 864 000
Purchases from EnerWyze during the year	132 000 000
Closing inventory – 31 March 2024	(10 560 000)
Transfers into manufacturing of innovation stations	128 304 000

3 Contract with Vuka Mzansi

During FY2024, Vuka Mzansi, a newly established and registered non-profit organisation based in the Eastern Cape, approached FutureWyze to supply them with 250 customised innovation stations with Vuka Mzansi branding. The chief executive officer of Vuka Mzansi, Mr Sisa Ntlabo, is a longstanding friend of Tumelo. They share a passion for social upliftment and have worked together on many successful projects in the past. Vuka Mzansi is sponsored by a large multinational corporation in the United States of America (USA) and focuses on youth development and empowerment.

Just before supplying Vuka Mzansi with a quote for the 250 customised innovation stations, FutureWyze was approached by an unrelated company, The Container Company (Pty) Ltd ('TCC'), which sells redundant shipping containers. TCC offered 300 shipping containers to FutureWyze at a price that is almost 60% lower than what FutureWyze would normally pay for shipping containers from its usual, approved suppliers.

The deal seemed too good to be true, so Ms Louisa Melroux, FutureWyze's inventory manager (not a director), investigated the deal to avoid being scammed. TCC claimed that it was being liquidated and was selling all its assets for less than carrying values to pay back creditors. Louisa was unable to find any evidence of previous trading activities or a registered address of the company or any notice that the company was being liquidated. The company explained that it had sold all its trading premises and would supply a temporary address, where the shipping containers were kept, once FutureWyze agreed to view them. It further asked FutureWyze to pay in cash upon collection of the shipping containers and to remove them immediately.

However, Louisa remembered reading an article about a syndicate operating in Johannesburg that had pulled off the theft of shipping containers, causing shipping container companies to lose millions. In the article, the police warned the public to be cautious of companies selling containers at low prices as anyone that purchases goods that were later found to be stolen could be arrested for possession of stolen goods. The police further requested that all suspicious transactions should be reported.

Louisa was conflicted about whether she should make the purchase, as this was a very good deal and would help FutureWyze to increase profits on these innovation stations. It would also enable FutureWyze to help Vuka Mzansi by offering them a lower price on their order.

After careful consideration she decided that, since the majority would benefit (FutureWyze, Vuka Mzansi and the youth) with very little negative impact on anyone, she could not, in good conscience, turn down the deal. She further reasoned that she had done her part in

investigating the matter to make sure that the supplier existed and felt that its reason for offering liquidation prices seemed valid. Therefore, there was no reason to suspect them of wrongdoing. Louisa met with the suppliers, purchased the shipping containers and TransportWyze collected the shipping containers immediately.

FutureWyze then entered into a contract with Vuka Mzansi to supply them with the 250 customised innovation stations and a three-year service contract for each innovation station, at a total contract price of R25 million. The service contracts are sold separately for R36 000 per three-year service contract and the branded innovation stations typically retail for R110 000 each. Vuka Mzansi paid a 50% deposit on 10 December 2023, following the signing of the contract by the designated representatives from both parties. The balance was payable on delivery of the innovation stations to Vuka Mzansi.

During February 2023, FutureWyze was informed that some of the sites, mostly in remote rural areas, were not ready to receive the innovation stations. Accordingly, Vuka Mzansi requested that FutureWyze keep 40 innovation stations at no charge until the sites were ready. Ordinarily, FutureWyze would have charged a total of R320 000 for this storage arrangement, but it agreed to do so at no cost. The site-readiness process was expected to take two months (March and April 2024). Vuka Mzansi had all 250 customised and branded innovation stations inspected for quality compliance and confirmed that they were all in good working condition and ready for physical transfer to the customer on 29 February 2024. 210 innovation stations were delivered to Vuka Mzansi on this date while the remaining 40 innovation stations were placed in FutureWyze's storage area and clearly marked as belonging to Vuka Mzansi.

FutureWyze did not service any innovation stations during FY2024.

4 Vuka Mzansi sustainability and financing model

In a conversation with Tumelo over lunch, Sisa raised some concerns regarding the sponsorship that his organisation received from the USA corporation. Sisa asked whether Tumelo could reach out to her networks and organise a think-tank with him to come up with alternative models to ensure that Vuka Mzansi remained a financially viable and sustainable entity if Vuka Mzansi lost its USA sponsorship. He was considering aspects such as how to obtain financing or generate income from the solar-powered innovation stations in the Eastern Cape.

He hoped that the brainstorming session would also highlight significant challenges that Vuka Mzansi would face while operating in the innovation station industry in the Eastern Cape and that Tumelo would come up with ideas to improve Vuka Mzansi's environmental impact, particularly in rural areas.

5 Civil unrest

In January 2024, there was a series of unprecedented riots across South Africa. In one incident of vandalism, rioters set fire to EnerWyze's manufacturing plant and some of the assets in the plant, excluding inventory, were damaged. The company continued to operate, despite the significant losses and disruptions.

The following is a summary of the net assets owned by EnerWyze on 31 January 2024:

	Carrying amount on 31 January 2024¹
	R'000
Inventories	66 500
Trade receivables	6 000
Cash and cash equivalents	8 000
Building leased out under an operating lease	185 000
Solar-panel manufacturing plant	110 000
Delivery trucks and motor vehicles	97 500
Trade payables and other liabilities	(107 000)
Total	366 000

1 These amounts have not yet been adjusted for the impact of the riots.

On 31 January 2024 the recoverable amount of EnerWyze was R350 million. The inventory carrying amount on 31 January 2024 is measured at the lower of cost or net realisable value.

6 Additional information

- TransportWyze's related-party disclosure note reflected transport income of R11,2 million (2023: R9,8 million).
- FutureWyze measures all its investment property at fair value in terms of IAS 40 *Investment Property* and all its property, plant and equipment using the cost model in terms of IAS 16 *Property, Plant and Equipment*.
- FutureWyze measures non-controlling interests initially at a proportionate share of the net identifiable assets.
- FutureWyze measures progress towards complete satisfaction of performance obligations as follows:
 - Service contracts: Costs incurred over the total expected costs.
 - Storage services: Time elapsed over the total expected time.
- A 27% corporate income tax rate and 80% capital gains inclusion rate applied to all the periods under review.

INITIAL TEST OF COMPETENCE, JUNE 2024

PROFESSIONAL PAPER 4

**This paper consists of two questions.
Answer each question in a separate answer book.**

PAPER 4 QUESTION 2 – REQUIRED		Marks	
		Sub-total	Total
(a)	Prepare the pro forma consolidation journal entries to account for all intragroup transactions in the consolidated financial statements of the FutureWyze Group for FY2024. <i>Communication skills – presentation</i>	9 1	 10
(b)	Discuss whether you agree with Louisa’s decision to buy the shipping containers from TCC, with reference to the good for self and good for others approach and the utilitarian ethical theory. <i>Communication skills – logical argument</i>	13 1	 14
(c)	Calculate the revenue that FutureWyze should recognise in accordance with IFRS 15 <i>Revenue from Contracts with Customers</i> , from the contract with Vuka Mzansi for FY2024.	7	7
(d)	Briefly discuss matters that should be considered during the brainstorming session that Sisa asked Tumelo to organise regarding – <ul style="list-style-type: none"> • the fact that Vuka Mzansi can obtain financing or generate income from the solar-powered innovation stations in the Eastern Cape; • the significant challenges that Vuka Mzansi will face while operating innovation stations in the Eastern Cape; and • the environmental impact of the innovation stations, particularly in rural areas. <i>Communication skills – clarity of expression</i>	9 1	 10
(e)	Prepare the pro forma consolidation journal entries to account for the effects of the civil unrest in the consolidated financial statements of the FutureWyze Group for FY2024. <ul style="list-style-type: none"> • Ignore taxation. • Pro forma journal entries to account for non-controlling interest are not required. 	9	9
Total for the question			50