## QUESTION 1 50 marks

Ignore VAT implications.

Ilayimi Limited (‘Ilayimi’) crushes limestone at its plant in Mokopane in the Limpopo Province. Ilayimi was incorporated on 2 January 1990. Ilayimi is the largest supplier in South Africa of high-calcium limestone and dolomitic limestone. High-calcium limestone is used in poultry and cattle feedstock, while dolomitic limestone is used in the agricultural industry.

Ilayimi is listed on the JSE Securities Exchange AltX and has a 31 December year end.

The following information relates to Ilayimi for the financial year ended 31 December 2011.

### Securities

At 31 December 2010 Ilayimi had an authorised share capital of 2 300 000 ordinary shares and 1 252 000 ordinary shares in issue.

The following is an extract from the securities register of Ilayimi for 2011. These are the only securities issued during the period 1 January 2011 to 31 December 2011.

<table>
<thead>
<tr>
<th>Name</th>
<th>Title</th>
<th>Address</th>
<th>Shares issued</th>
<th>Date of issue</th>
<th>Certificate number</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>J Stein</td>
<td>Director</td>
<td>6 Lead Ave Johannesburg</td>
<td>20 000</td>
<td>1 April</td>
<td>S124</td>
<td>1</td>
</tr>
<tr>
<td>M Nthuli</td>
<td>Director</td>
<td>77 Park St Kempton Park</td>
<td>30 000</td>
<td>1 April</td>
<td>S125</td>
<td>1</td>
</tr>
<tr>
<td>Ilayimi Tribal Trust</td>
<td>Trust</td>
<td>5 Lourens Dr Mokopane</td>
<td>125 000</td>
<td>1 July</td>
<td>S127</td>
<td>2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name</th>
<th>Title</th>
<th>Address</th>
<th>Share options granted</th>
<th>Vesting start date</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>J Stein</td>
<td>Director</td>
<td>6 Lead Ave Johannesburg</td>
<td>50 000</td>
<td>1 April</td>
<td>1</td>
</tr>
<tr>
<td>M Nthuli</td>
<td>Director</td>
<td>77 Park St Kempton Park</td>
<td>40 000</td>
<td>1 April</td>
<td>1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name</th>
<th>Title</th>
<th>Address</th>
<th>Debentures issued</th>
<th>Date of issue</th>
<th>Type</th>
<th>Conversion date</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>STAR Investments Limited</td>
<td>Company</td>
<td>54 Lion St Cape Town</td>
<td>300 000</td>
<td>1 Dec.</td>
<td>Compulsorily convertible unsecured</td>
<td>30 Nov. 2015</td>
<td>3</td>
</tr>
</tbody>
</table>
Notes

1 On 1 April 2011 Ilayimi appointed two new executive directors. The director remuneration packages were structured as follows:

**J Stein**

- Basic remuneration: R1 020 000 per annum
- Shares as joining bonus: 20 000
- Share options with vesting conditions: 50 000

**M Nthuli**

- Basic remuneration: R1 015 000 per annum
- Shares as joining bonus: 30 000
- Share options with vesting conditions: 40 000

**Vesting conditions**

The share options granted to the directors will vest on 31 March 2015 if the directors are still in the service of the company and the share price of the company exceeds R121 per share.

Mr Stein and Mr Nthuli were still employed by Ilayimi on 31 December 2011, and it is expected that these directors will still be in the employment of Ilayimi on the vesting date.

The fair value per option on 1 April 2011 was R46. This price takes into account the market conditions and the exercise price of R50 per share in terms of the share option agreement.

**Conditions at year end**

On 1 December 2011 the executive directors announced that Ilayimi had entered into a new supply contract with a limestone quarry in the Gope area in Botswana. This report had a positive impact on the share price of Ilayimi.

The share price on 31 December 2011 was R124 per share.

The average share price from 1 April to 31 December 2011 was R112 per share.

2 Ilayimi issued 125 000 ordinary shares for a cash consideration of R12 500 to the Ilayimi Tribal Trust, a community trust to be held for the benefit of the Selwane and Majeje tribes. This is part of Ilayimi’s corporate social responsibility programme, and is aimed at helping local communities in the Mokopane area to become self-reliant through sustainable development programmes. An IFRS 2 charge was correctly recognised in the financial records of Ilayimi for this transaction.

3 To fund the construction of a new crushing plant in Gope, Botswana, Ilayimi issued 300 000 6% debentures with a nominal value of R100 each to STAR Investments Limited. Each debenture is compulsorily convertible into one ordinary share, with a conversion price of R100 per share. There is no option for cash settlement. Interest of R150 000 (after tax) was correctly expensed in profit or loss.
Primary crusher machine

As part of its operations, limestone purchased from quarries is crushed by a primary crusher machine before moving on to the next step in the process.

Information relating to the primary crusher machine:

- The machine was purchased on 1 July 2008 at a cost of R1 600 000 (exclusive of VAT) and was capitalised as a single item. Included in the cost was R320 000 for the gearbox.
- The normal capacity of the machine is 30 000 tonnes of limestone per month.
- It was estimated that the machine would crush 1,5 million tonnes of limestone during its useful life and that there would be no residual value for the machine.
- Ilayimi uses the units of production method to calculate depreciation.
- The depreciation is calculated at the end of each financial year.
- The carrying amount of the machine was R953 970 on 1 January 2011.

The gearbox of the primary crusher machine – which is a significant part of the machine – was damaged during September 2011. The necessary parts to repair the gearbox could not be sourced and it was decided to replace the gearbox with a different gearbox model.

The cost of the new gearbox was R320 000. The gearbox was installed and was ready for use on 1 October 2011. It is expected that the new gearbox will be replaced after crushing 600 000 tonnes of limestone. Management expects no scrap value to be attributable to the gearbox at the end of the gearbox’s useful life.

After the installation of the new gearbox, the normal capacity of the primary crusher machine increased to 32 000 tonnes of limestone per month. The overall capacity of 1,5 million tonnes did not change with the installation of the new gearbox.

The following is a schedule of the actual tonnes of limestone crushed by the primary crusher machine during the 2011 financial year:

<table>
<thead>
<tr>
<th>Month</th>
<th>Actual tonnes crushed</th>
<th>Per month</th>
<th>Cumulative total</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>22 890</td>
<td>22 890</td>
<td>22 890</td>
</tr>
<tr>
<td>February</td>
<td>24 400</td>
<td>47 290</td>
<td>47 290</td>
</tr>
<tr>
<td>March</td>
<td>27 000</td>
<td>74 290</td>
<td>74 290</td>
</tr>
<tr>
<td>April</td>
<td>28 000</td>
<td>102 290</td>
<td>102 290</td>
</tr>
<tr>
<td>May</td>
<td>31 000</td>
<td>133 290</td>
<td>133 290</td>
</tr>
<tr>
<td>June</td>
<td>31 500</td>
<td>164 790</td>
<td>164 790</td>
</tr>
<tr>
<td>July</td>
<td>31 800</td>
<td>196 590</td>
<td>196 590</td>
</tr>
<tr>
<td>August</td>
<td>31 500</td>
<td>228 090</td>
<td>228 090</td>
</tr>
<tr>
<td>September</td>
<td>25 000</td>
<td>253 090</td>
<td>253 090</td>
</tr>
<tr>
<td>October</td>
<td>32 000</td>
<td>285 090</td>
<td>285 090</td>
</tr>
<tr>
<td>November</td>
<td>33 500</td>
<td>318 590</td>
<td>318 590</td>
</tr>
<tr>
<td>December</td>
<td>32 200</td>
<td>350 790</td>
<td>350 790</td>
</tr>
</tbody>
</table>
With the replacement of the gearbox, management realised that the machine does have a scrap value, which management can use to determine the residual value as follows:

<table>
<thead>
<tr>
<th>Date</th>
<th>Residual value</th>
<th>Spot rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>31 December 2011</td>
<td>US $4 800</td>
<td>ZAR7.50 = US $1</td>
</tr>
</tbody>
</table>

Ilayimi’s accounting policy is to apply changes in the estimate of the residual values with effect from the beginning of the reporting period in which the change is identified.

**Bonus scheme**

Ilayimi has a bonus plan in terms of which employees receive a fixed rate for each actual tonnage of limestone crushed above normal capacity each year. The rate per tonne is negotiated with the employees at the beginning of each financial year. These bonuses are paid out two years after they are awarded, provided the employee is still employed by the company.

In terms of this bonus plan, management awarded a bonus of R4 000 per employee to the 64 employees that qualified under the scheme, based on the performance of the 2011 financial year on 10 January 2012. Management estimates that 18 of the employees will resign and consequently forfeit their rights to the bonus during the two-year period until payment. Management is planning to finalise the financial statements of Ilayimi for the year ended 31 December 2011 before 15 March 2012.

**Transport subsidiary**

As part of its operations Ilayimi operated a transport subsidiary. The transport subsidiary represented a separate major line of business for Ilayimi.

A detailed formal plan for discontinuing the transport subsidiary was finalised on 30 September 2011, and the main features of the plan were announced on 30 November 2011. The discontinuation and actual sale on tender of the assets and related liabilities of the transport subsidiary is expected to be completed on 29 February 2012. (Note that the plan is to sell the assets and related liabilities of the transport subsidiary and not the subsidiary itself.)

On 30 November 2011 the fair value less costs to sell of the disposal group amounted to R5 350 000. The value increased to R5 365 000 on 31 December 2011.

Negotiations with the affected employees were in an advanced stage and almost completed by 31 December 2011.

1 Relevant information regarding the assets and liabilities of the transport subsidiary prepared correctly in accordance with International Financial Reporting Standards (IFRS):
Carrying amount at 30/11/2011 | Impairment loss allocation | Carrying amount with re-measurement at 30/11/2011 | Impairment reversal | Carrying amount at year end
---|---|---|---|---
Land | 1.1 | 2 000 000 | (12 347) | 1 987 653 | 6 467 | 1 994 120
Tanker trucks | 1.2 | 6 166 667 | (38 070) | 6 128 597 | 19 938 | 6 148 535
Debtors | 1.3 | 150 000 | – | 150 000 | – | 50 000
Creditors | 1.4 | (50 000) | – | (50 000) | – | –
Secured loan | 1.5 | (2 866 250) | – | (2 866 250) | – | (2 827 655)
| | 5 400 417 | (50 417) | 5 350 000 | 26 405 | 5 365 000

Notes

1.1 There are no other potential capital gains in the future against which a loss on sale of the land could be applied.

1.2 The tax base of the tanker trucks at 31 December 2010 was R8 000 000 and at 31 December 2011 it was R6 000 000. The original cost of the tanker trucks was R10 000 000.

1.3 The debtors are fully recoverable. During December R100 000 was received in payments from debtors.

1.4 The creditors were all settled in December.

1.5 The secured loan is settled in monthly instalments of R62 500. The interest component of the instalment for December was R23 905. The loan is secured over the tanker trucks.

1.6 The opening deferred tax balance for the transport subsidiary as at 1 January 2011 was R0.

2 Information relating to the discontinued transport subsidiary:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual</td>
<td>Actual</td>
<td>Actual</td>
<td>Estimate</td>
</tr>
<tr>
<td>R</td>
<td>R</td>
<td>R</td>
<td>R</td>
</tr>
</tbody>
</table>

Revenue | 5 856 189 | 528 445 | 6 384 634 | 939 412
Operating expenses (excluding impairment / re-measurement of the disposal group and items listed below) – all of the items included are tax deductible | 3 293 163 | 466 500 | 3 759 663 | 823 500
Depreciation | 1 833 333 | – | 1 833 333 | –
Finance cost | 317 719 | 23 905 | 341 624 | 23 022
Severance pay payable to employees | – | – | – | 320 000
Direct costs of discontinuation | – | 40 000 | 40 000 | 17 500
Continuing operations

The profit after tax from continuing operations of Ilayimi, after all of the above events were taken into account, amounted to R12 523 500 for the year ended 31 December 2011.

Taxation

There is sufficient other taxable income for the recognition of deferred tax assets (subject to note 1.1 above).

Effective interest rate

The pre-tax discount rate for Ilayimi (applicable to all relevant transactions) is 10% per annum.