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**UNIVERSITY OF JOHANNESBURG
DEPARTMENT OF ACCOUNTANCY**

Governance and Control

RHR03X7/RHR03X8/GAC8X00

FINAL ASSESSMENT

26 OCTOBER 2015

FIRST EXAMINERS:

Mrs Seabi Mokoena
Mrs Vanessa Van Dyk

MODERATOR

Mrs R Potgieter

TIME:

2 hours (excluding reading time)

Marks

100

1. This paper consists of 9 pages (excluding the required)
2. This documentation represents the scenario for the question
3. Twenty minutes (20) of reading time is given for the paper, making the assessment session 2 hours and 20 minutes.
4. During the 20 minutes reading time, you may:
 - Highlight the information presented in this document; and
 - Make such annotations on this document as you consider appropriate.
5. At the close of the 20 minute reading period, you will be given the question (required) and stationery packs.
6. You will have two (2) hours in which to answer the required section.
7. No questions may be asked during the assessment.
8. Please write your name and student number clearly on your answer sheet.
9. Make assumptions if you are uncertain regarding the interpretation of the scenario.

Question 1

You are a manager in the internal audit department of The Passenger Rail Company (Pty) Ltd (hereafter PRC). PRC operates in two of South Africa's provinces, namely Gauteng and the Western Cape. The regions operate independently of one another and report to the PRC head office in Johannesburg. PRC transports about 50,000 passengers per day, thereby accounting for roughly 3% of the people using public transport daily in South Africa. They operate at 10 stations, with the rolling stock fleet consisting of approximately twenty (20) train sets, and with train sets varying in size between 8 and 14 coaches per train set.

In light of an article recently published (see article below) as well as problems faced by the entity, both from the management side and operationally, you have been requested by the board to perform a review on the internal controls at PRC. The company reported a loss of R1million over the 2014 financial year.

Allegations of serious maladministration at PRC.

By [News24Wire](#) July 29, 2015

PRC's head of engineering services David Masondo appeared in the Johannesburg Magistrate's court on Wednesday on a charge of fraud and uttering relating to his qualification, the National Prosecuting Authority (NPA) in Gauteng said.

Uttering is the crime of using a forged document and is usually associated with the circulation of fake bank notes. He was released on R20 000 bail and has to return to court on August 25, NPA Gauteng spokesperson Phindi Mabena told News24.

Masondo's qualification became an issue following a report in the Afrikaans language newspaper Rapport, that new trains ordered by the entity from Spain were too high for South African rail infrastructure, and could damage overhead power cables. There have been at least two train crashes in the last four months, with the most recent accidents seeing 63 people injured in the same week. One of PRC's recently-purchased locomotives, an Afro-4000, derailed in the Western Cape, injuring several people, after alleged warnings that these trains were unsuitable for South African rail conditions and prone to derailment.

Masondo has since resigned from the Passenger Rail Company, shortly after PRC's CEO Hanna Monty's dismissal from the entity. Dodgy procurement practices, paying rent for vacant buildings and forking out millions for employees improperly dismissed are reportedly some of the allegations against the CEO.

One of the allegations was that payments totalling R1.1 million were made to contractors to provide stations with services and goods. The contracts were not only awarded improperly to this company after PRC's procurement policies were not followed, but the services and goods were never delivered to PRC.

Mrs Monty unlawfully engages yearly in a series of suspending employees perpetually with payment of salaries costing PRC an estimated R750,000.00 per annum in expenditure.

It was further alleged that PRC has not paid some of its employees' wages for a period of 6 months. After conducting an investigation into the matter, PRC determined that clock cards for the hours worked by these employees could not be found. The matter

will be resolved urgently.

The company has a centralised IT department. Data is processed on a mainframe computer which is located in the computer room at head office along with various other pieces of computer equipment. The various departments are linked to the mainframe by on-line terminals.

To assist you with your review, the financial manager arranged for you to obtain his secretary, Gugu Majola's password, should you want to gain access to the system and its various applications. The secretary gave you her user ID and informed you that her password was GM. She also informed you would be away the next day and that you could work at her terminal.

Although access to the IT department was controlled by a security key pad, it was not necessary for you to obtain the entry code as, the door was held open by a fire extinguisher to enable a stationery company to deliver paper.

Payroll

As a result of the allegations surrounding the payroll department, you have decided to perform an extensive review of this process. Upon enquiry of the human resource head, you determined the following:

The company has a human resource department which is responsible for all matters pertaining to labour. The department is amongst other responsibilities responsible for maintaining the wage employee masterfile as well as hard copy records for each employee, e.g. employment contract, banking details, notification of grade changes, wage rate increases, etc. Hiring, dismissal and resignations are dealt with by this department in conjunction with the other heads of department.

All wage employees are located at the various PRC stations. Hours worked are controlled by a clocking system at the entry/ exit points of stations and employees are required to "clock" themselves into and out of their stations by passing their clock cards through the clocking machine. Employees work a 40 hour normal time week and overtime is worked as required. There are administration clerks located at each station.

At the conclusion of the wage period the clock cards are taken to the wages department at head office. The clerks in this department are responsible for entering the hours worked off the clock cards and producing the payroll using a reliable software package. To enter hours the clerk will access the payroll module. When accessed, the software will then bring up the first employee's records on the screen. Once the hours have been entered and confirmed, the software will automatically bring up the next employee's record.

Wages are paid every two weeks by EFT, directly into the employee's bank account.

Procurement

In light of the procurement issues highlighted by the article, you also decided to perform an extensive review of this process. You discovered that PRC uses the

same process to procure capital and operational goods. The documented procurement policy reads as follows:

When an order is placed with a supplier, a copy of the order is sent by the buying department to the accounting department where it is filed in numerical sequence.

For quality and reliability purposes, PRC only deals with approved suppliers.

All deliveries of goods are made by the suppliers themselves. When a delivery is made the receiving clerk at the stations agrees the number of goods physically delivered to the supplier's delivery note, signs it to acknowledge receipt, but does not check the contents of the packages at this point. The packages are later unpacked at the receiving department and checked against the order and supplier delivery note. Where there is a discrepancy in the contents of a package and the supplier delivery note, the receiving clerk makes out a "purchases discrepancy report" detailing the problem. He signs the report and faxes it to the supplier. The receiving clerk prepares a goods received note (GRN), signs it, attaches the supplier delivery note to a copy of the GRN, and attaches copy of the discrepancy report (if any) and sends the documents to the accounting department where the documents are matched to the order, and filed alphabetically by supplier name to await the supplier invoice.

When the supplier invoice arrives, the creditors clerk matches the invoice to the other documents and checks that all documents are present, details on the invoice agree with the order and GRN, prices charged agree with the supplier agreements and that all calculations are correct. He stamps the invoice "checked" and signs in the space provided. These invoices are then placed in a "pending" file to await the creditor's monthly statement. When the creditor's statement arrives, the creditors clerk agrees the supplier's invoice for the month to the statement, confirms that any payments made to the supplier during the month are recorded, and follows up on any adjustments e.g. credit notes passed. This enables him to draw up a reconciliation for each creditor which he attaches to the supplier statement and supporting documentation. He stamps the reconciliation "for payment", signs in the space provided and draws up a list of each creditor to be paid and the amount of the payment. This list is passed to the general administration clerk, who prepares a cheque for each creditor on the list. Payments to creditors are made only by cheque and all cheques are stamped "not transferable".

The creditors list, the cheque and supporting documentation are presented to the cheques signatories, who sign each cheque after having scrutinized the supporting documentation and agreed the payment to the list. They then stamp the documentation "first signatory" and "second signatory" respectively and sign the creditor's reconciliation once they are satisfied. The company has three authorised signatories and all cheques must be signed by the two of the three. The documents are filed by month in alphabetical order by supplier name

All documents are pre-printed, multi-part and numerically sequenced.

Question 2

Introduction

You are a newly appointed internal audit trainee at Global Market Resources (GMR). GMR Limited is a company that provides market reports to their clients based on retail data. These reports include information regarding the market share of their client within the industry and per product range, details selling prices of their products across different retail stores and movement of their products in relation to the same products of competitors. The company was started in Germany in 1960, where it is also listed and established a presence in South Africa in the early 1990's. The company grew steadily each year, listing on the Johannesburg Securities Exchange (JSE) in 1998.

The company's largest clients are those involved in the telecommunications industry, specifically the cellular telephone market. Such clients include Motorollo SA Limited and Knokea SA Limited the two largest telecommunications companies in South Africa and the major distributors of cellular telephones worldwide.

Due to the general decline in the economy both in South Africa and worldwide as well as increase in interest rates and costs overall, GRM Limited experienced a situation where for the first time since inception, that some of their large clients were not renewing their long term contracts, but rather taking reports on an ad-hoc basis, if and when additional funds are available to these companies for discretionary spend on products such as those offered by GRM Limited. This has seen a decline in sales and drop in profitability for the company for the year ended 31 August 2015.

Annual General Meeting

Below is the notice of the general meeting was sent to shareholders via registered mail as well as electronically via email:

Global Market Resources Limited

Incorporated in the Republic of South Africa

Registration number 1991/104568/09

Sharecode: GMR ISIN: ZA000239854

Notice of annual meeting

Notice is hereby given that the annual general meeting of shareholders of the company will be held in the meeting room, first floor, GMR Building, 97 Central Street, Houghton, Johannesburg, on 15 October at 10:00 for the purpose of considering and, if deemed fit, passing, with or without modification, the following resolutions:

1. to receive, consider and adopt the annual financial statements of the company for the year ended 31 August 2015, together with the directors' and independent auditors' reports.
2. to re-elect Ms Chantal van Zyl who retires by rotation as she is eligible and available for re-election.

By order of the board

Jessica Chang

Human Resources Director

6 October 2015

Registered office

GMR Building
97 Central Street
Houghton
2179
Johannesburg

Registrars

Investor Services 2004 (Pty) Ltd
170 Eloff Street
Johannesburg
2001

Below are **certain extracts** from the annual report that was approved at the board meeting. Please note that you may assume that the company has the required number of sub-committees of the board, which have been appropriately constituted in terms of the King III recommendations, **unless otherwise stated**:

Directors' report

For the year ended 31 August 2015, total turnover was R2 014 million, showing a decrease from the prior year turnover of R 2 121 million. Total loss for the year amounted to R491 million in comparison to a prior year profit of R30 million. The board is confident that these decreases in sales and operating profit is as a result of the current recessive climate being experienced in the economy and overall increase in operating costs for both GMR Limited and its clients. The board is confident that this situation is short term and with appropriate corrective measures taken in the new year that this situation will be improved.

After making due enquiry, the directors consider that, as at the date of the approval of the financial statements, the Company has adequate resources to continue to operate for the foreseeable future. For this reason the directors continue to adopt the going concern basis in preparing the financial statements.

Corporate governance report

During the period the Board comprised the executive chairman and CEO, four further executive directors and 4 independent non-executive directors. However, Mr Myburgh, the HR director, resigned from the board in August 2015. The Board met 5 times during the past year.

Audit committee

The members of the audit committee for the period under review were as follows:

- Craig Bowen (Chairman)
- Molemo Moahloli (Marketing director)

The committee met twice during the last year, the last meeting being to approve the financial statements. Both meetings were conducted without the audit partner of Young & Ernest present and without invitation to other board members.

At the last meeting the members of the audit committee authorised the payment of dividends to shareholders of R1 for every share held. This results in R13.495 millions of dividends to be paid. It was also authorised that these dividends be paid out of the share capital account.

A summary of the audited and published financial results for the year ended 31 August 2015

Description	2015	2014
	R'000's	R'000's
Statement of Comprehensive Income		
Turnover	2 014 795	2 120 562
Operating (loss)/profit	(14 886)	563 331
Additional payment to Mr Myburgh	(11)	-
Loss on ordinary activities before tax	(462 937)	40 962
Tax on loss on ordinary activities	(27 737)	(11 111)
(Loss)/profit for the year	(490 674)	29 851
Statement of financial position		
ASSETS		
Fixed Assets*	172 474	504 178
Accounts receivable	762 342	565 236
Short-term investments	27 906	42 786
Cash at bank and in hand	-	372 566
Total Assets	962 722	1 484 766
EQUITY AND LIABILITIES		
Authorised share capital (shares)		
Issued share capital	13 495	13 070
Retained (loss)/income	(61 421)	518 511
Total equity	(47 926)	531 581
Current liabilities (due within 1 year)	753 561	545 658
Long term liabilities (due after 1 year)	129 372	17 045
Bank overdraft	128	
Provisions for liabilities and charges	127 587	390 482
Total Equity and liabilities	962 722	1 484 766

* The land and buildings of GRM Limited was sold to Motorollo Limited for a profit of R15 million and leased back from Motorollo Limited in terms of a sale-and-leaseback agreement.

Remuneration report

Base salary

The base salary of the executive directors is subject to annual review and is set with reference to external market data, relating to similar companies based in South Africa.

Annual bonus plan

Each of the directors is entitled to participate in an annual bonus scheme based on the financial performance targets related to net profit, earnings per share and generation of cash together with an amount related to the achievement of personal key performance indicators set in accordance with the Company's performance management system.

Pension and other benefits

Pensions and other benefits such as life insurance benefits for executive directors reflect the practice of companies in similar industries.

Non-executive directors' fees

The executive directors determine the remuneration of non-executive directors annually. Consideration is given to fees payable to non-executive directors for comparable companies. Additional fees are paid to committee members and chairmen of board committees to take account of the additional work involved.

Directors' remuneration

Director	Directors fees	Basic Salary	Pension fund	Medical Aid	Life insurance	Bonus	2015 Total	2014 Total
	R'000	R'000	R'000	R'000	R'000	R'000	R'000	R'000
G Redwitz	560	6 450	300	90	80	20 000	27 480	21 870
C Bowen	100	2 920	80	90	30	12 750	15 970	9 600
M Moahloli	-	3 400	100	90	40	9 800	13 430	8 250
N Mbuli	-	3 750	250	90	30	5 000	9 120	6 840
A Myburgh	-	1 000	20	70	10	-	1 100	6 150
C van Zyl	810	-	-	-	-	1 000	1 810	500
S Seedat	640	-	-	-	-	-	640	230
J Chang	600	-	-	-	-	-	600	190
M Clark	100	-	-	-	-	-	100	20
TOTAL	2 810	17 520	750	430	190	48 550	70 250	53 650

A new director Roger Carson, attended the AGM and was introduced to the members by Mr Redwitz who personally nominated him for the position of executive director – operations. The board of directors voted in favour of the nomination at their first board meeting for the new year that was held on 18 September 2015 in terms of the conditions stated in the Memorandum of Incorporation of the company which states that the board of directors can appoint new directors.

A brief biography of Mr Carson includes:

- Completing a B.Com Accounting degree in 1987
- Completing a B Com Hons in Accounting in 1990
- Commencement of accounting training contract (SAIPA articles) in January 1991 at a small auditing firm, Amateur Auditors
- Completion of articles in December 1993
- Employed as financial manager for Ace (Pty) Ltd, a retail company, from 1994 – 1998
- Employed as financial manager for Barrow (Pty) Ltd, an construction company from 1998 – 2000
- Employed as financial manager for Deconstruct Limited, an engineering and project management company in 2000
- Employed as company secretary for Fine Furniture (Pty) Ltd a small furniture and fittings company in 2001
- Employed as company secretary for Echo (Pty) Ltd, an information technology company from 2002 - 2003
- Employed as financial director of Knokea SA Limited, a telecommunications company from 2003 – 2007
- Not employed from 2007 to current day.

You are intrigued as to why the new director's employment ends in 2007 and you decide to "Google" Mr Roger Carson and come across the following, very interesting article:

Carson to be incarcerated

By Ace Reporter

September 12, 2007

In a decision, that most would call fair, only to Mr Roger Carson, a judge sentenced Carson to three years in jail and found him guilty of fraud at Knokea Limited.

The fraud, which shocked the financial world in January this year, amounted to over R24 million, misappropriated by Carson for personal gain. During the investigation it was discovered that Carson had mounted large gambling debts that he could not settle personally, so began settling them with funds he had stolen from Knokea Limited. Previously, Carson had been hailed as the "wunderkind" of the telecommunications company as he turned the previously illiquid and loss making company into a profitable and cash flush enterprise.

Carson also had to file for bankruptcy in his personal capacity last year and it appears that many creditors are still awaiting payment. Nonetheless, Carson applied to the court just a month earlier to overturn his insolvency status, but the court would not re-habilitate him. Many feel that Carson should have received a far lengthier sentence for the acts committed by him. Not only have shareholders lost faith in Knokea Limited, but so have customers and suppliers and the company is facing severe financial difficulties. Another question on the lips of shareholders is whether Carson will even serve his full three year term. Another case has been brought against Carson in his personal capacity, being a director of Knokea Limited, but it appears that, based on his financial position, these shareholders will be in a long line of persons awaiting payment from Carson.