



UNIVERSITY OF JOHANNESBURG

DEPARTMENT OF ACCOUNTANCY

**AUDITING 3A
ADIA003**

**SUPPLEMENTARY ASSESSMENT
July 2014**

**FIRST EXAMINER: Ms Rozanne Smith
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**TOTAL TIME: 2 hours and 30 minutes
TOTAL MARKS: 125 marks**

INSTRUCTIONS:

1. This paper consists of **NINE** pages. If your paper does not contain all the pages, please put up your hand so that a replacement paper can be handed to you.
2. Answer all the questions.
3. Calculate the time that you should spend on each question and part of a question by multiplying the number of marks by 1.2 to determine the time, in minutes, available for each question. Adhere to these time constraints in order to finish the paper in the given time.
4. Delete all (even single open lines) open spaces on your answer sheets with pen. Pages on your answer sheets that contain open spaces will be marked as such and those pages will not be eligible for a remark.
5. No tippex or pencil may be used on your answer sheets. Pages on your answer sheets that contain pencil or tippex will be marked as such and those pages will not be eligible for a remark.
6. All the examination regulations of the UJ and the policy document for students of the Department of Accounting will apply before, during and after this test.
7. Write your name/student number on this question paper and hand it in on completion thereof.
8. The neatness, disclosure and presentation of your answers will be taken into account when marking your paper.

QUESTION 1

(28 MARKS)

The South African Rugby Football Union ("SARFU") is currently finalising the arrangements for the 2015 World Cup Rugby. The tournament will take place over a period of a month and tickets will be sold at SARFU's head office. Tickets sales will commence in August.

SARFU has two major sources of revenue; ticket sales and corporate sponsorships. In return for sponsorships, corporate sponsors will be given free advertising in programmes. Programmes will be issued free to patrons and will not contain any other advertisements.

Mr Carel Robinson, the financial manager and the Chairman of the Union believes that the Union cannot afford any allegations of financial irregularities. SARFU is dependent on corporate sponsorships especially for the World Cup and subsequent to recent fraudulent sporting events, sport bodies are monitored more closely. He believes that it is particularly important for the company to ensure that all revenue is properly accounted for and has requested your firm to recommend a suitable system of internal control over revenue.

The administrative staff of SARFU includes:

- General Manager
- Financial Manager
- Marketing Manager
- Personal assistant to the above executives
- Bookkeeper
- Ticket sales Manager

Ticket sales:

Tickets are sold only through two sales counters located at the SARFU head office. Each counter is manned by one cashier at any time. As two shifts are worked each day, there are a total of four cashiers. The cashiers report to the ticket sales manager.

Tickets are never sold on credit and cheques are not accepted. Patrons are required to pay in cash or by credit card. Ticket prices vary according to the match that is played as well as to the seat in the stadium. SARFU also offers discounts on ticket prices to senior citizens, students and scholars.

Access control:

You have been advised of the following:

- All entrances to the stadium will be manned by security guards
- Security guards inspect patron's tickets before allowing entry, tear tickets in half to prevent re-use and hand back half to patrons. Security guards will retain the half

tickets, and will hand the half tickets to the general manager after each match so that he can determine attendance figures.

You are required to:

1. Discuss the control objectives in respect of the system over revenue earned by SARFU. (7)
2. Write a letter to Mr Robinson describing a suitable system of internal control over tickets sales and sponsorships earned by SARFU. (20)

(YOU ARE NOT REQUIRED TO DEAL WITH RECORDING IN THE ACCOUNTING RECORDS.)

Presentation (1)

QUESTION 2

(22 MARKS)

You were recently appointed as an HR consultant of a newly formed company, Picture Perfect (Pty) Ltd. You were going to provide the company with advisory services on their human resources function. The owner of the company is Cindy Moodley. Her company purchases paintings from novice artists which are then framed and sold. Initially, Cindy Moodley operated her business very informally as a sole trader, but her pictures have proved to be so popular that she has now expanded operations to a point where she has recognized the need for more formal structures and systems.

Cindy had received a large contract to supply a number of paintings to a development company, as part of their efforts to bring up the value of the homes that they were building. To cope with the sudden boost in sales and the significant amount of work required, Cindy had placed an advert in the paper for qualified artists to apply for the available positions that she now need to be filled in her company. A number of individuals responded to the advert, and being under pressure to meet the contract requirements, Cindy hired the applicants on the spot, without an interview, although she ensured that they had come to a common verbal agreement about their hours of work and the pay that they were going to receive once they were employed.

When you arrived at Picture Perfect (Pty) Ltd to start performing the advisory work, you noticed a number of weaknesses with regards to the staff that were employed. There were a number of staff that were not performing any work, while you also noticed one of the staff members leaving the premises with an expensive frame, which Cindy did not even notice due to the pressures that she was dealing with.

On enquiry with one of the staff members who was resting at the back of the warehouse, about his qualifications, he mentioned that he was excellent at his previous job, where he was a janitor at a local school, but was forced to take "extended leave", because of some "misunderstanding with regard to a missing purse of one of the teachers".

When you brought this to Cindy's attention, she was shocked at what was happening, and did not understand where she had gone wrong with regards to employing these staff members

You are required to:

1. List the controls that should have been in place for the hiring of Cindy's new staff.
2. Identify the risks that these controls would mitigate.
3. Explain how you would test these controls.

(20)

Make use of the following table when answering this question:

Control	Risk	Test of control
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Presentation (2)

QUESTION 3

(20 MARKS)

You are the internal auditor employed at Merc Parts Ltd. You have reviewed the internal controls over the inventory cycle.

You have documented the following remarks on your working papers relating to the controls in inventory:

- Inventory is kept in a locked storeroom, and access is limited to authorised personnel only.
- Inventory is also safeguarded against the elements such as fire and floods
- Inventory is fully insured.
- Issue notes are made out for the issuing of raw materials to production after a requisition is authorised by the foreman.
- All issue notes are numerically numbered.
- Missing numbers are followed up.
- All issue notes are signed by the storeman and the production manager as proof of receipt.
- All inventories leaving the storeroom are accompanied by a delivery note.
- Continuous inventory records are maintained by personnel independent from the safeguarding function.
- Inventory is written up from the GRN or delivery notes.
- Regular inventory counts are held. Count totals are compared to inventory totals.
- Obsolete and slow moving inventory is identified timeously and written off according to the company policy.

You are required to:

1. List the control objectives that are affected by the internal controls above. (5)
2. Describe the test of controls that you will perform to test whether the controls that Merc Parts Ltd relies on over their inventory are effective. (14)

Presentation (1)

QUESTION 4

(15 MARKS)

Olivier's Computers (Pty) Ltd is a company situated in South Africa that is involved in the importing and exporting of business computer systems. The company imports these computers from a manufacturer in China under an internationally well known computer brand.

An investigation by the Scorpions during March 2014 revealed that these computers were in fact fake and had no connection with the well known brand. Upon further discussions with management regarding these computers, we were informed that these computers were "exactly the same as the well known brand, just different". Not being too sure of what management meant by this, some market research indicated that these fake computers being imported and exported were of a very low quality, yet were being sold to customers at almost the same price as the original well known brand type. Presently, one of the directors, Mr. Olivier, is serving time at the Leeukop Prison; awaiting trial for a court case against the company by the company's whose brand they are illegally using. Due to the delay in paperwork, a restriction has not yet been enforced to restrict the company from continuing its activities and is at this stage still importing these fake computers.

Once the computers arrive in South Africa, they are immediately exported to a number of South American countries including Brazil and Peru. There was a case a number of years ago where the company was sued by the South African Revenue Services for allegedly paying bribes to the customs officials in order to avoid paying customs duties on the computers imported.

The company is very secretive about the customers it has and has disallowed any form of contact between the auditors and the company's customers. The debtor's book of the company is material to the entity's operations.

In the past year, the company has been struggling to maintain its cash flow. It thus applied for and was granted a loan from a bank in China. The conditions of the loan are that the bank receives a copy of the annual financial statements of the company in order to re-evaluate on an annual basis, the conditions of the loan and whether or not the loan facility will be granted for the next year.

You are required to:

To fully discuss the business risks you identify in Olivier's Computers (Pty) Ltd. (15)

QUESTION 5

(20 MARKS)

You have recently been appointed as the senior internal auditor at a firm called Sonny's Stationary, which is owned by Sonny Maloi. Sonny's Stationary is a small chain of six retail outlets of stationary in the Randburg area. The "head office" of Sonny's Stationary is situated at Sonny's home and he uses his triple garage as the central warehouse. He converted his garage so that there is only one entrance to it, but the entrance is also used as the backdoor to Sonny's house. Sonny has explained to you that he is concerned about the purchases system that he has in place at the moment and wants you to advise him on any weaknesses in the system. He explained to you that the system works as follows:

- Sonny personally negotiates with suppliers in order to obtain the best prices and payment discount structures for the firm and verbally informs the stationary buyer of those suppliers that she should buy stationary from.
- When purchases have to be made, the stationary buyer prepares a pre-numbered order for each purchase transaction. Each order reflects the supplier's name, the date, the price per item and quantity ordered as well as the appropriate totals. Each order is authorised by the accountant before it is sent to the supplier. A copy of each order is sent to the warehouse manager.
- The suppliers deliver the goods directly to the warehouse. At the time of delivery, the warehouse manager performs quality control tests on the stationary and agrees the quantity delivered to the information on the supplier's delivery note.
- The warehouse manager checks the goods to the relevant order and personally follows up on any short deliveries. Any goods received in excess of the order are returned to the supplier immediately after a pre-numbered form called a "request for credit" is completed. A copy thereof accompanies the goods sent back to the supplier. The warehouse manager then attaches the delivery note and the request for credit (where applicable) to the order. He sends these documents to the accounting department where it is filed.
- Sussie, Sonny's wife, who acts as the secretary of the firm, receives all of the mail, opens it and records it in a register. She then sends the suppliers invoices to the accounts clerk.
- The accounts clerk enters all invoices that have been received in an invoice register. The accounts clerk agrees the invoices to the delivery notes and orders, checking that the supplier, date, price and quantities agree. She stamps the documents with a rubber stamp that reads "checked for accuracy" and signs over the ink as evidence that she has completed the task. Invoices that have been checked in this manner are ticked off in the invoice register. Where the invoice is incorrect, the accounts clerk prepares a pre-numbered request for credit and sends a copy thereof to the supplier.
- The account clerk enters the detail from the invoices in the purchase journal.
- The accounts clerk enters the requests for credit immediately into the purchase journal as negative amounts.

- The accounts clerk posts the purchase journal entries to the creditor's ledger.
- At month end, the accounts clerk totals the purchase journal and hands it over to the accountant for processing in the general ledger. The accountant scrutinises the purchase journal for proper classification and summarisation and signs at the foot of each page as evidence that he has performed the procedure.
- Once the general ledger has been posted, the accounts clerk prints a list of the creditors and reconciles the total of the creditor list to the creditors control account in the general ledger.
- The accounts clerk reconciles the balance of each creditor in the creditor list to the statement received from each supplier and follows up on reconciling items.
- When payments have to be made to the suppliers, the accountant checks and sign the reconciliation of each creditor account as well as the reconciliation between the creditor list and the creditors control account in the general ledger.
- Copies of these signed creditor reconciliations are sent to the cash book clerk who makes out the cheques after considering payment discounts and sends the cheques, together with the copies of the reconciliation, to Sonny who is the only cheque signatory. Sonny glances through the reconciliations, signs the cheques and returns all of the documents to the accounts clerk who is responsible for mailing the cheques to the suppliers.
- The accounts clerk posts the cheque payments from the cash book to the creditor's ledger.
- Any adjusting journals are written out and posted by the accounts clerk after being approved in writing by the accountant.
- The cash book clerk prepares a monthly bank account reconciliation which is checked and signed by the accountant.
- Sussie is in control of the pre-numbered stationary that is stacked in a corner of the warehouse. Sussie maintains a stationary register and requires employees to sign the stationary register when taking new books of standard documents.

You are required to:

List, in detail, the weaknesses in the system described above.

(16)

Precision and Interpretation marks (4)

QUESTION 6**(20 MARKS)**

You are the internal audit manager of Steelworks Ltd, a listed company trading within the steel industry. The company has a 31 May period end. Steelworks Ltd has grown significantly over the past few years with a current turnover in excess of R 200 million per annum.

The company makes significant ongoing purchases of property, plant and equipment causing the company's fixed assets balance to be material. The Financial Manager of Steelworks Ltd informed you that the company's finance and investment cycle controls were somewhat neglected in the last few years. He approached you for advice on internal controls over property, plant and equipment.

YOU ARE REQUIRED TO:

1. Identify and list any five control objectives that are relevant in the finance and investment cycle above. (5)
2. List all the internal controls required for effective control over the property, plant and equipment of Steelworks Ltd. (15)