UNIVERSITY OF JOHANNESBURG

Department of Commercial Accounting

AUDITING AND INTERNAL CONTROL

AIC33A3 & AIC3AA3

Final Assessment Opportunity 2016

Date: June 2016

Time: 180 minutes **Marks: 100**

Assessors: Mr J Mamaile
Mrs K Esterhuizen
Mr A Peer

Internal Moderator: Mrs R Smith
External Moderator: Mr M Pete

INSTRUCTIONS:
This paper consists of **7** pages (including the cover page).
Answer all questions.
Show all calculations and workings clearly.
Start each question on a new page in your answer book.
Silent, non-programmable calculators may be used.
Where applicable, round all calculations to the nearest Rand.
All questions require the application of International Financial Reporting Standards.

Question	Topic	Marks	Time
1	Multiple choice	10	18 minutes
2	Receipts and Revenue cycle	20	36 minutes
3	Acquisition and payment cycle	20	36 minutes
4	Inventory and production cycle	15	27 minutes
5	Finance cycle	20	36 minutes
6	Investment cycle	15	27 minutes
		100	**180 minutes**

QUESTION 1 **MULTIPLE CHOICE** (10 marks)

1.1) Which of the following is the correct order of functions within the Revenue and Receipts cycle?

a) Customer order, Warehouse, Dispatch, accounting, collecting cash
b) Customer order, receiving, Warehouse, Dispatch, accounting, collecting cash
c) Purchase requisition, Purchase order, Receiving, accounting, payments to suppliers
d) Purchase order, Receiving, accounting, payments to suppliers

1.2) What is the purpose of the back-order note in the Revenue and Receipts cycle?

a) To indicate that the debtors account must be reduced for goods returned from the customer
b) To show that the goods have been delivered to the customer
c) To select the goods for shipment
d) To indicate requested goods are out of stock for follow up purposes (filling the order later)

1.3) Which one of the following is a key objective of the Inventory and Production cycle?

a) Increase loss of goods through theft
b) Purchase the goods from your uncle's company
c) Allow costs to be recorded once in while
d) Protect the inventory from damage, loss and theft, regardless of whether it is manufactured inventory or inventory purchased for resale

1.4) Which of the following is the correct order of functions within the Acquisition and Payment cycle?

a) Ordering, receiving, recording, despatching and actual payment
b) Ordering, receiving, recording, payment preparation and actual payment
c) Ordering, receiving, recording, warehousing and payment preparation
d) None of the above

1.5) Which of the following is NOT an item to be audited in the Finance cycle?

a) Provision, contingent liabilities and contingent assets
b) Long term loans, debentures and finance lease liabilities
c) Salary expense
d) Share capital

1.6) Which of the following risks is NOT a risk when it is audited as part of the Investment cycle?

a) Acquisition documentation may be lost or otherwise not communicated to proper personnel
b) Inadequate physical security over fixed assets
c) Incorrect depreciation lives or methods may be used
d) Return forms might be incorrectly completed

1.7) Which of the following risks is NOT a risk in the Inventory and Production cycle?

a) Company assets are being misappropriated
b) No record is created of goods or components physically moved
c) Failure to budget costs properly resulting in selling prices which are too low and subsequent losses
d) Inventory shortages are concealed

1.8) Select the correct statement:

a) Companies which have large quantities and numerous items of inventory will normally perform what are referred to as ***cycle counts***. Cycle counts amount to the ongoing comparison of physical quantities of inventory on hand, to theoretical quantities in the perpetual inventory records
b) For companies which do not operate perpetual inventory systems, the only way of ascertaining a closing inventory figure is to physically count the inventory and then to price it at the year-end inventory count
c) In most companies the systems which interface with the inventory and production cycle, will be computerised and will directly affect and be affected by the inventory Masterfile
d) All of the above are correct

1.9) Which of the following risks is NOT a risk in the Acquisition and Payment cycle?

a) No goods received notes are being issued
b) Invalid payment may be made
c) Failure to control the transfer of finished goods to the finished goods store
d) Payment of fictitious creditors

1.10) Which of the following financial statement assertions is NOT an assertion of the Acquisition and Payment cycle?

a) All creditors have been reflected at the appropriate amount (at the correct carrying value) - valuation
b) **All** payments (to creditors) that should have been recorded have been recorded - completeness
c) All purchases have been recorded in the proper accounts - classification
d) The company holds or controls the rights to all inventory reflected in the financial statements (any encumbrances must be disclosed) - rights

REQUIRED:

Choose the correct answer from four possible answers given. **[10]**

QUESTION 2 REVENUE AND RECEIPTS CYCLE (20 marks)

Pretorius (Pty) Ltd recognises that in addition to selling goods and services to individual consumers and employing many individuals as employees, the business sells large volumes of stock to its customers on an annual basis.

Many customers find Pretorius (Pty) Ltd accessible and selling best available quality goods to them.

REQUIRED:

You are required to describe four control activities that can be performed for each of the functions listed below in the Revenue and Receipts cycle of a business. You can assume that the business operates in a manual environment.

2.1) Receiving customers' orders (4)
2.2) Despatch (4)
2.3) Warehousing (4)
2.4) Invoicing (4)
2.5) Recording of sales (4)

[20]

QUESTION 3 ACQUISITION AND PAYMENT CYCLE (20 marks)

You are auditing purchases at Honeybun (Pty) Ltd, a manufacturer of pastries for the catering and retail trade.

The following Acquisition and Payments system documentation has been confirmed:

Mr. Smith, the warehouse supervisor has sole responsibility for the ordering of the ingredients. He prepares a two-part order. The top copy is sent to the supplier and the second copy is temporarily filed pending delivery. As the shelf life of a number of these ingredients is limited, rush orders are often necessary and these are made telephonically.

When the goods are received, Mr. Smith checks the quantity and description to the order, if it exists, and makes out a pre-numbered three-part goods received note (GRN). Mr. Smith will not accept orders that are not complete. The top copy is filed numerically. Due to the rapid inventory turnover, the company has decided to do away with the perpetual inventory recording system. The second copy of the GRN accompanies the signed supplier's delivery note and the second copy of the order to Miss A, a clerk in the accounts department. The third copy of the GRN is returned to the supplier as evidence of receipt of the goods and to assist in the follow up of queries.

Miss A stamps the GRN with the outline:

Quantity agreed with delivery note
Quantity agreed with invoice
Account allocation

and signs the first block once she has reconciled the quantity of goods per the GRN to the supplier’s delivery note.

This package is then temporarily filed by supplier's name awaiting the supplier's invoice.

Once the invoice is received Miss A checks the supplier’s name and the quantity of goods received, enters the account allocation and signs the second and third blocks of the stamp. This package is then passed on to Miss B who prepares a pre-numbered journal voucher detailing supplier, description of goods, invoice total and account allocation. The package is then filed by supplier’s name and the journal vouchers batched daily and sent to data processing where the general ledger and accounts payable ledger are updated. You may assume that all journal vouchers are received by data processing and all controls over the input/output of data do exist.

On a monthly basis the accountant reconciles the total of the accounts payable ledger with the accounts payable control account in the general ledger and the accounts clerk reconciles the individual suppliers- accounts in the accounts payable ledger with the suppliers' statements before presenting them for payment. The accountant scrutinizes the reconciliation before adding his signature to the cheque.

REQUIRED:

3.1) Identify the internal control weaknesses in the above Acquisition and Payments system. (10)

3.2) Detail the possible consequences as a result of those weaknesses in this system. (10)

[20]

QUESTION 4 INVENTORY AND PRODUCTION CYCLE (15 marks)

Many of the tests which are carried out as tests of controls will be dual purpose tests and will supply some evidence relating to the accuracy of the inventory records. The performance of year-end procedures is usually broken down into two distinct phases namely attendance at the year-end inventory count and subsequent (post) inventory audit procedures.

REQUIRED:

List the test of controls and substantive procedures the auditor can execute at the **attendance of the year-end inventory count**.

[15]

QUESTION 5 FINANCE CYCLE (20 marks)

The finance cycle deals with those transactions which a company enters into to raise finance, for example by issuing shares, or borrowing money from a bank or investment company.

The transaction in this cycle will usually result in an account balance but may also give rise to cash inflows and outflows which are written off at the end of the financial year.

REQUIRED:

5.1) List and describe any five **characteristics** of the Finance cycle? (10)

5.2) Due to the nature of the Finance cycle, the transactions in this cycle will not be subjected to the routine day to day controls. List four **compensating controls** which should be implemented in the Finance cycle. (4)

5.3) What conditions must be met if the cost of an item of property, plant and equipment is to be recognised as an asset? (2)

5.4) In terms of IAS 16 - Property, Plant and Equipment, a company can choose to value its assets using the cost model for some assets and the revaluation method for other assets. True or False? (1)

5.5) What are the assertions which relate to transactions which take place in the Finance and Investment cycle? (3)

[20]

QUESTION 6 INVESTMENT CYCLE (15 marks)

During any given financial year, a company will invest in property, plant and equipment (PPE). These are normally large transactions which could give rise to an outflow of cash. The same PPE could be sold during a financial year giving rise to an asset disposal transaction. All these additions and disposal of PPE needs to be audited as transactions and primarily the occurrence, accuracy, cut-off and classification assertions should get the attention of the auditor.

The following line item was extracted from the fixed asset register:

Opening balance	Additions	Disposals	Closing balance
R 15 000	R 35 000	R10 000	R 40 000

<u>REQUIRED:</u>

6.1) With reference to the **additions** of R 35 000, list four audit procedures the auditor will execute to obtain evidence against the **occurrence** assertion. (4)

6.2) With reference to the **additions** of R 35 000, list any audit procedures the auditor will execute to obtain evidence against the accuracy, classification and **cut-off** assertions. (11)

[15]

Total: 100