

## **AUE2602**

May/June 2017

### **CORPORATE GOVERNANCE IN ACCOUNTANCY**

Duration 2 Hours

100 Marks

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**EXAMINATION PANEL AS APPOINTED BY THE DEPARTMENT**

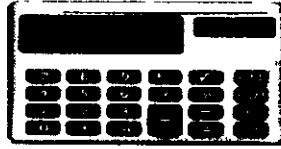
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**Use of a non-programmable pocket calculator is permissible**

**Closed book examination**

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**[TURN OVER]**

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THIS PAPER CONSISTS OF **EIGHT (8) PAGES**

This paper consists of the following questions and main topics

<b>QUESTION</b>	<b>MAIN TOPIC</b>	<b>MARKS</b>
<b>1</b>	Corporate governance and internal controls	50
<b>2</b>	Acquisition and payments cycle, inventory and production cycle and payroll and personnel cycle	50
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		<b><u>100</u></b>

**NOTE:**

Although the primary purpose of the examination is to test your knowledge and application of the subject matter, your ability to organise and present such knowledge in written language of an acceptable standard will be taken into consideration by the examiners

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## QUESTION 1

50 marks

You are an audit trainee at Vouch Inc a firm of registered auditors in Johannesburg. You were recently assigned to the audit of ScrewLoose Limited (hereafter referred to as "ScrewLoose"), a VAT-registered company that operates in the hardware sector in South Africa. ScrewLoose specialises in hardware, consumables, chemicals, tools and safety products. Mr C Ment founded the company 14 months ago. As this is the first time that ScrewLoose will be audited, Mr Ment requested that the audit firm provide value-adding comments regarding the corporate governance practices and internal controls at ScrewLoose. The integrated report is yet to be prepared.

The following information urgently requires your attention:

### 1. Corporate governance practices

	Position	Member of Governing Body (Board of Directors)	Member of Audit Committee
Charles Ment	Chief Executive Officer (CEO)	Chairperson	Chairperson
Danny Ndlovu	Operations Director	Yes	
Jonas Smith	Managing Director	Yes	Yes
Jessica Riley	Independent non-executive director	Yes	
Nadia Ismail	Independent non-executive director	Yes	Yes
Gertrude Molo	Independent non-executive director	Yes	
Thabiso Mudau	Independent non-executive director	Yes	
Note		1	2

**Note 1:** The board met twice during the first financial year.

**Note 2:** At the only meeting held by the audit committee during the first financial year, a decision was taken that the committee's only duty is to nominate the external auditor for appointment. The audit committee will have a first meeting with the external auditors next month.

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## 2. Continuity of operations

Mr Ment wants to develop an information technology (IT) disaster recovery plan as part of sound controls to minimise disruption should a disaster occur that could prevent processing and/or destroy financial data

## 3. Application controls

Your fellow audit trainee, Jack Newbie, was assigned to audit the payroll and personnel cycle at ScrewLoose. He has encountered the following application controls that are used in this cycle, but is not sure whether he has matched the correct descriptions to the respective application controls

#	Description	Application control
A	Identifies amounts that fall outside a predetermined limit after processing	Alphanumeric test
B	A final balance arrived at after processing is compared to the opening balance and the individual total of transactions	Check digits
C	Keying in will not continue until a particular field or fields have been entered	Limit test
D	Is a redundant (extra) character added to an account number, part number, etc	Mandatory field
E	Detect gaps or duplications in a sequence of numbers as the numbers are entered	Matching check
F	Data that has been processed is compared by the computer against data that is already in the database	Range test
G	Prevent or detect alphabetic fields that have been entered as numerals and vice versa	Run-to-run total
H	Data that has been processed is compared by the computer to other information for reasonableness	Sequence check

## 4. Source document design

Mr Ment has indicated his concerns to you regarding the design of the source documents at ScrewLoose. His main concern is whether or not the sales invoices that ScrewLoose issues comply with the requirements of the Consumer Protection Act 68 of 2008. You selected sales invoice 698, which is presented below

[TURN OVER]

## Sales Tax Invoice

Invoice number 698  
ScrewLoose Limited

Customer Black Velvet Design (Pty) Ltd  
PO BOX D  
Pretoria  
0037

Description	Amount (R)
XI52 3M Hearing Protection Caps with Green Cups	4 400 00
Bz17 35ℓ Compact Flammable Cabinet	12 600 00
<b>Total</b>	<b>17 000.00</b>



### REQUIRED

### Marks

- 1.1 **Comment** on the information that ScrewLoose Limited provided with reference to the requirements of **sound corporate governance** in terms of the King IV Report
- Present your answer under the following headings
- a) Governing Body (Board of directors) composition and appointments (five comments) (7½)
  - b) Audit committee composition and appointments (three comments) (4½)
  - c) Audit committee meetings (two comments) (3)
  - d) General remarks (two comments) (3)
- You should discuss issues in respect of both **compliance** and **non-compliance** with the King IV Report in your answer
  - Two presentation marks will be awarded if the answer is presented under the correct headings, and for communication, logical reasoning and structure (2)
- 1.2 Describe any **FOUR (4) duties** of the **audit committee** in terms of the provisions of section 94 of the **Companies Act 71 of 2008**. Exclude any duties relating to the external auditor from your answer (6)
- 1.3 Describe the **controls** that Mr C Ment should implement at ScrewLoose Limited to minimise information technology (IT) disruption as a result of some disaster. Limit your answer to the **disaster recovery plan** (6)

[TURN OVER]

**REQUIRED (continued)**

**Marks**

- 1.4** Assist Jack Newbie with his understanding of application controls by matching the correct **application control** to each **description**. Only **one** application control should be provided for each description.

You should present your answer in the following format

No marks will be awarded for the example below

Description	Application control
Example A	Example Limit test
B	
C	
D	
E	
F	
G	
H	

(7)

- Two presentation marks will be awarded if the answer is presented in the required format, and for communication, logical reasoning and structure

(2)

- 1.5** Indicate with reference to invoice 698 whether or not the design of the source document complies with the **minimum requirements for an invoice** as stipulated in the **Consumer Protection Act 68 of 2008**.

**Example.** The invoice does not state the date on which the transaction occurred

- You should discuss issues in respect of both **compliance** and **non-compliance** with the Consumer Protection Act in your answer

(9)

[TURN OVER]

## QUESTION 2

50 marks

Fantastic Four Furnishers (Pty) Ltd is a manufacturing company that produces beautiful wooden furniture for furniture retail stores

### 1. Ordering of wood

To enhance local employment rates, all wood is ordered from the local forestry department by the Senior Buyer, Ms S Storm

### 2 The manufacturing process

The factory floor is divided into five sections

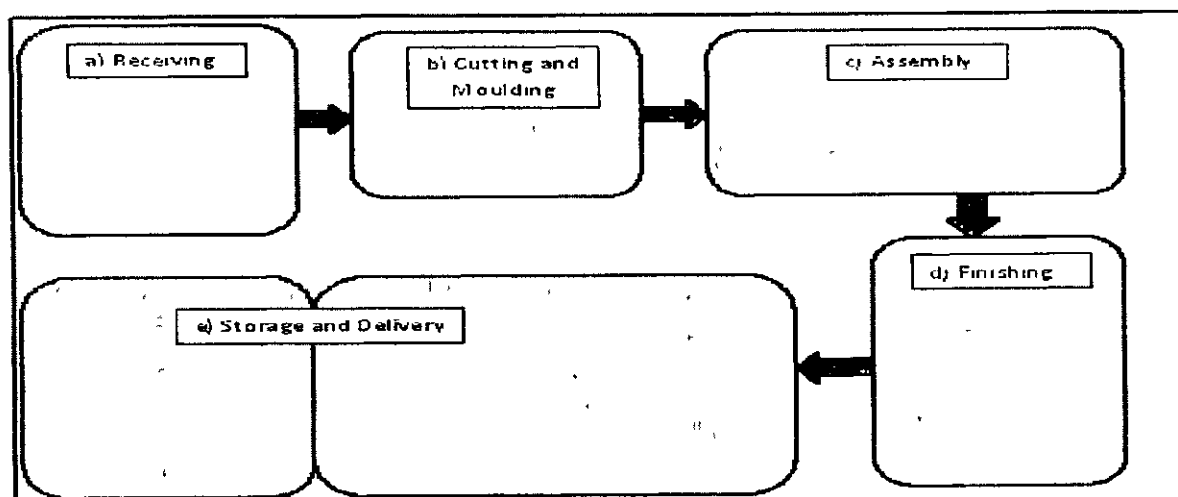


Figure 1: Factory floor layout

When the wood is received, it is checked and measured to ensure that the size and the moisture content of the wood pieces are within the specified requirements. Each bundle received is documented on a goods received note (GRN) before it is released to the cutting and moulding section for processing. When wood is transferred to a new section, for example, from cutting and moulding to assembly, a transfer note is completed by the foreman of the section releasing the inventory to the next section.

[TURN OVER]

### 3. Appointment of new staff

The foreman of the finishing section, Mr H Torch, has complained that the assembly section is always behind schedule and that the products are not of the required quality. Mr R Fantastic, the Chief Executive Officer, decided to appoint additional staff to the assembly section. Because he is a very busy man, he placed an advertisement in the local newspaper and immediately appointed the first five applicants. He then proceeded to capture the new employees' details in the computerised employee masterfile.

### 4. Employee masterfile

The employee masterfile can only be accessed through the use of an authorised username and password. To enhance accuracy and completeness of the keying in of the masterfile amendments and to detect invalid conditions, screen aids and programme checks were implemented. Any changes made to the masterfile are also automatically logged by the system on sequenced logs. Mr Thing, the Financial Director, regularly reviews the logs and checks the log sequence.

#### REQUIRED

#### Marks

- 2.1 Describe any **FIVE (5) risks** linked to the **ordering of goods function** of the **acquisition and payments cycle**. Explain why each risk is considered a risk.

Present your answer in the following format

No marks will be awarded for the example below

Risk	Explanation
<b>Example:</b> Paying unnecessarily high prices for goods	<b>Example:</b> This could result in liquidity problems and financial loss
1)	
2)	
3)	
4)	
5)	

(15)

- Two presentation marks will be awarded if the answer is presented in the required format, and for communication, logical reasoning and structure

(2)

[TURN OVER]



REQUIRED (continued)	Marks
2.2 Describe <b>FOUR (4) internal controls</b> that should be implemented to mitigate the risks associated with the <b>movement of inventory</b> from the Cutting and Moulding section to the Assembly section	(6)
2.3 Regarding the valuation of inventory	
2.3.1 Describe at what <b>value</b> the inventory should be presented in the financial statements of Fantastic Four Furnishers (Pty) Ltd	(3)
2.3.2 Indicate whether the following costs (a-f) should be <b>included or excluded</b> when valuing inventory  a) Delivery costs b) Commission paid on goods sold c) Cost of production material lost during a fire in the factory d) Administrative costs e) The salaries of production staff f) Variable production overheads	(6)
2.4 What <b>procedures</b> should Mr R Fantastic, the CEO, have followed <b>before making the new appointments</b> to address the risk of recruiting unsatisfactory or unnecessary employees?	(9)
2.5 Describe any <b>additional internal controls</b> that should be implemented to ensure that new employees' details added to the <b>employee masterfile</b> is accurate, complete and authorised	(9)