

**QUESTION 2****50 marks**

You are a third-year audit trainee working at the audit firm, CFW Inc. ('CFW'). In May 2022, CFW was appointed as the external auditor of Meals 4 Me (Pty) Ltd ('M4M'). M4M has a 31 December year end.

M4M was incorporated in 2017 by two brothers, Steven and Michael Peters. M4M started off as a small business delivering frozen home-made meals. After the national lockdown regulations were implemented from March 2020, the demand for frozen meals grew significantly. M4M subsequently expanded its range of frozen meals and now has distribution centers nationwide. All operations of M4M take place from their facilities in Bloemfontein. Meals are distributed from the central kitchen to the distribution centers, and from the distribution centers to customers, via a third-party courier company.

M4M asked CFW to complete the financial audit by 28 February 2023. You are currently busy with the planning phase of the audit, which includes obtaining system descriptions for the various business cycles. These have been documented in the following audit workpapers:

<b>Workpaper reference</b>	<b>Subject of the workpaper</b>
A001	Accounting systems and internal controls
P001	Purchases cycle

<b>CFW Auditors Inc.</b>	<b>Workpaper reference:</b> A001
<b>Client:</b> Meals 4 Me (Pty) Ltd	<b>Prepared by:</b> A. Clark <b>Date:</b> 20 January 2023
<b>Year end:</b> 31 December 2022	<b>Reviewed by:</b> S. Mzamane <b>Date:</b> 24 January 2023
<b>Subject:</b> Accounting systems and internal controls	
<p>M4M uses an off-the-shelf accounting package, AccProf. AccProf processes value-added tax, has a built-in inventory management system, and offers the user a choice between the perpetual and periodic inventory systems. M4M makes use of the periodic inventory system. Free support is provided by the supplier of AccProf for five hours per month and changes to the system can only be made by the software supplier.</p> <p>The finance function consists of the following individuals:</p> <ul style="list-style-type: none"> <li>• Financial controller, Sarah Calitz CA(SA)</li> <li>• Senior accountant, Themba Sisulu CA(SA)</li> <li>• Accountant responsible for sales and tax, Aamira Abbasi CA(SA)</li> <li>• Zama Cele, a second-year part-time student in chartered accountancy. She was appointed in August 2021 to assist with managing the purchasing process and creditors.</li> </ul>	

<b>CFW Auditors Inc.</b>	<b>Workpaper reference:</b> P001
<b>Client:</b> Meals 4 Me (Pty) Ltd	<b>Prepared by:</b> T. Naidoo <b>Date:</b> 24 January 2023
<b>Year end:</b> 31 December 2022	<b>Reviewed by:</b> S. Mzamane <b>Date:</b> 24 January 2023
<b>Subject:</b> Purchases cycle	

**The purchasing and receiving team consists of the following staff members:**

- Head of purchasing – Lekwa Mabaso
- Ten buyers
- Two purchasing clerks: Victor Mashishi and Prudence Dlamini
- Four receiving clerks: Grace Symmons, Kagiso Nkosi, Themba Bhele and Nabeelah Bashir

**Important master documents**

- List of approved suppliers
- Standard price list

When a new supplier is considered, Lekwa presents the supplier's details to Steven and Michael. The approved supplier and standard price lists are updated once she receives approval from them.

**M4M makes use of three categories of suppliers**

- **Category 1: Fresh fruit and vegetables:** The ten buyers visit and negotiate with local farmers twice per week to ensure better prices and optimal quality of seasonal produce. If the required items are not available from the local farmers, it is sourced from retail stores at significantly higher prices. All fresh fruit and vegetables are paid for in cash.
- **Category 2: Meat, grains, spices, sauces, dairy, and other ingredients:** M4M has fixed contracts with suppliers. M4M negotiates the prices of products with its suppliers every month and standard price lists are updated as soon as negotiations have been completed.
- **Category 3: Packaging and logistics:** All packaging materials are imported from Beijing Pack Ltd ('Pack'), a supplier based in China. In terms of the contract, Pack pays the shipping costs on behalf of M4M when handing the goods to the courier and then adds the transport cost, plus a 10% service fee, to its invoice to M4M.

**Placing of orders**

The ordering function on AccProf is password protected, and only Victor and Prudence have access to this module. To initiate an order, the purchasing clerk responsible for placing the relevant order (either Victor or Prudence), enters their username and password, consisting of at least eight characters. The same purchasing clerk then enters the supplier code, which is obtained from the list of approved suppliers.

Once the supplier code has been entered into the system, a standard order form appears on the screen. The form includes standard details such as the supplier's e-mail address, business phone number, physical address and credit terms negotiated with the supplier. The relevant purchasing clerk compares these details with the list of approved suppliers. The purchasing clerk next selects the description of the items to be ordered from a pre-populated drop-down menu and types in the quantity of items to be ordered. The product code and price of the items are displayed automatically after the relevant item has been selected from the list.

The responsible purchasing clerk then compares these particulars with the most recently updated standard price list. The total amount of the order is calculated automatically by the system and the purchasing clerk re-performs the calculation to determine the total value of the order before releasing the order to the supplier by clicking the 'confirm order' button.

Victor pulls a report, listing all orders with no matching goods received notes (GRNs) from AccProf on a weekly basis, and follows up on any outstanding orders.

### **Delivery of goods**

All items are delivered to a dedicated receiving area. When receiving category 2 and 3 items, two of the four receiving clerks compare the quantity and description of the physical products with the delivery note received from the supplier and the original order form. The same receiving clerk checks the quality of the products, after which one of them completes a GRN on AccProf, indicating the quantity and description of the goods received. Both receiving clerks sign the form electronically by each clicking the 'signature' button. The receiving clerks then move the products into the storage area.

### **Recording of purchases**

All category 2 and 3 suppliers send their invoices directly to a dedicated M4M e-mail address. Zama monitors this inbox and captures these invoices on AccProf as they are received. Once the suppliers' invoices are captured, purchase journal entries are automatically posted to the creditor's account in the creditors ledger. The creditors control account in the general ledger is then updated to reflect the total amount owed to each individual creditor.

AccProf automatically matches the invoice captured with the relevant GRN and order form on the system. Once these documents have been matched, the system flags it as ready to be paid.

### **Payment of creditors**

Monthly supplier statements are e-mailed to the same e-mail address, and these statements are used to make payments to suppliers.

Zama prepares monthly creditors' reconciliations for all category 2 and 3 suppliers for this purpose, by comparing the balance payable according to the suppliers' statements received with the outstanding balance according to the creditors ledger, as reflected on AccProf. If Zama detects a difference, she investigates the matter and makes the appropriate adjustments to correct the creditor's balance on AccProf. She also adds a note next to the reconciling item explaining how the difference was resolved. Themba reviews the reconciliation and queries unresolved differences with the suppliers.

On the last business day of every month, Sarah prepares electronic payments on M4M's banking website and Steven releases the payments after reviewing the supplier statements and creditors' reconciliations. After payments have been made, cashbook journal entries are automatically posted to the creditor's account in the creditors ledger and the cashbook balance in the general ledger.

**INITIAL TEST OF COMPETENCE, JANUARY 2023**

**PROFESSIONAL PAPER 1**

**This paper consists of two questions.  
Answer each question in a separate answer book**

<b>PAPER 1 QUESTION 2 – REQUIRED</b>		<b>Marks</b>							
		<b>Sub-total</b>	<b>Total</b>						
(a)	(i) Identify and describe the risks of material misstatement related to the completeness, accuracy, and valuation and allocation of the creditors balance of M4M as at 31 December 2022; and	6							
	(ii) For each of the risks identified, indicate to which assertion the relevant risk relates.	6							
<ul style="list-style-type: none"> <li>Present your answer in a table format.</li> </ul> <p><i>Communication skills – clarity of expression</i></p>		1	13						
(b)	With reference to the placing of orders and delivery of goods from category 2 and 3 suppliers, as documented in workpaper P001 –								
	(i) identify and discuss the internal controls present in the systems description of M4M that you would rely on; and	12							
(ii) formulate the tests of control(s) the auditor should perform to assess the relevant internal controls for each control identified in (b)(i).		12							
<ul style="list-style-type: none"> <li>Present your answer in the following table format:</li> </ul> <table border="1" data-bbox="287 1473 1114 1653"> <thead> <tr> <th><b>(i) Internal control identified</b></th> <th><b>(ii) Test of control</b></th> </tr> </thead> <tbody> <tr> <td>Internal control 1...</td> <td>Test of control related to internal control 1...</td> </tr> <tr> <td>Etc...</td> <td>Etc...</td> </tr> </tbody> </table> <ul style="list-style-type: none"> <li>Assume that CFW will follow a combined audit approach.</li> <li>Do not include the following in your answer: <ul style="list-style-type: none"> <li>Changes to the list of approved suppliers and approved price list; and</li> <li>Segregation of duties between irreconcilable functions.</li> </ul> </li> </ul> <p><i>Communication skills – presentation</i></p>		<b>(i) Internal control identified</b>	<b>(ii) Test of control</b>	Internal control 1...	Test of control related to internal control 1...	Etc...	Etc...	1	25
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Internal control 1...	Test of control related to internal control 1...								
Etc...	Etc...								

**Continued on page 2**

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<b>PAPER 1 QUESTION 2 – REQUIRED (cont.)</b>		<b>Marks</b>	
		<b>Sub-total</b>	<b>Total</b>
(c)	<p>Formulate the substantive procedures that the audit team should perform to obtain sufficient appropriate evidence regarding the completeness of the creditors balance of M4M as at 31 December 2022.</p> <ul style="list-style-type: none"> <li>• Do not address the following in your answer: <ul style="list-style-type: none"> <li>○ The extent and timing of procedures; and</li> <li>○ Any procedures related to tax.</li> </ul> </li> <li>• Do not perform the following general substantive procedures: <ul style="list-style-type: none"> <li>○ Obtaining a creditors schedule and recalculating the mathematical accuracy of the schedule;</li> <li>○ Comparing the total creditors according to the creditors schedule with the creditors balance included in the trial balance and general ledger, the balance of the creditors control account and the creditors balance in the financial statements;</li> <li>○ Comparing the opening balance of creditors with the closing balance of the previous year's audited financial statements;</li> <li>○ Inspecting the creditors' accounts in the general ledger for any unusual journal entries and following up on any unusual entries identified; and</li> <li>○ Requesting a signed management representation letter to confirm the completeness of creditors.</li> </ul> </li> </ul>	12	12
<b>Total for question 2</b>			<b>50</b>
<b>TOTAL FOR PAPER 1</b>			<b>100</b>