

**1 Background**

Thuli Tau is a newly Registered Auditor (RA), with ambitions to build her own practice. With money she recently inherited, she acquired GM & Associates Inc. ('GMA') on 30 November 2021. The previous owner and sole partner of GMA, George Mwangi CA(SA), RA, sold the practice to Thuli upon his retirement.

GMA is a firm located in Gauteng. A few years ago, George acquired the Gauteng operations of the prominent United Kingdom audit firm, Wilson & Associates Inc., which was leaving South Africa.

At acquisition of the practice on 30 November 2021, GMA's staff comprised 30 full-time employees:

- 12 general accounting staff;
- 12 trainee accountants;
- Three senior managers (only two of whom are registered CAs(SA)); and
- Three office managers.

Unfortunately, due to the uncertainties surrounding the practice being sold to Thuli, Charleston Dube, one of the senior managers who is a qualified CA(SA) with ten years' post-qualification experience, resigned on 15 December 2021. Apart from this resignation, six experienced general accounting staff also resigned before 31 December 2021. Four of the 12 trainee accountants are due to complete their training contracts within the next six months. Only one of these trainee accountants has indicated that she would like to stay on at GMA.

**2 Notes and workpapers**

GMA has various external audit clients and the following are extracts of some of the audit clients' workpapers and notes, together with notes on GMA's own systems.

Document	Description
A	Thuli's high-level notes on the quality control systems at GMA
B	Information on the planning and execution phases – Transfrontier Steel Commodities (Pty) Ltd ('TSC')
B135-0	Inventory workpaper on TSC drafted by a trainee accountant and placed on audit file as complete
C300-0	Risk assessment for TSC performed by a trainee accountant for review

***Leadership arrangements***

- George and Charleston would normally have set aside a day to reflect on the past year and prepare a simple budget for the firm. The budget typically entailed using the previous year's revenue numbers adjusted upwards by 20%. Staff, office and IT equipment costs were increased by the annual average inflation rate for the previous year.
- Janine Werksmans (an office manager at GMA) was given the responsibility of promoting a quality control culture within the firm. When I discussed this with her, Janine confessed that she was not sure what this entailed. She stated that her focus was on managing client invoicing and collections. George did not like a large debtors' book.

***Ethics and independence arrangements***

- Every six months a trainee accountant is selected to perform the role of ethics and business conduct leader for GMA to achieve their SAICA ethics competency requirements.

***Acceptance and continuance of client relationships and specific engagements***

- Staff describe George as an excellent marketer, who promoted the firm wherever he went. George was always reluctant to turn down new clients. He felt that everyone has a right to professional services.
- George obtained a detailed policy document from Wilson & Associates, which provided practical guidance on the provision of non-audit services to audit clients and associated fee arrangements. However, George felt that most issues surrounding non-audit services could be dealt with by means of discussions with the audit client.

***Human resourcing***

- Since trainee accountants never seem to stay with the firm very long, George was reluctant to spend significant time or money training them. He believed 'on-the-job' training was the best approach. George did assign the responsibility to Charleston of ensuring that the trainee accountants met their competencies during their training contracts.
- Trainee accountants are assigned to clients when they join the firm and remain on those engagements until they have completed their training contracts. The balance of engagement teams is made up of general accountants allocated to clients based on whoever was free at the time.
- Performance appraisals take place as needed. George typically used to determine bonuses based on the level of fees and new clients each person gained for the firm.

***Engagement performance***

- George confirmed that he doubted whether there had ever been any policies in place that assessed or guided engagement performance.

**DOCUMENT B: Information on the planning and execution phases – Transfrontier Steel Commodities (Pty) Ltd ('TSC')**

***Company background***

TSC is a manufacturer and distributor of steel products. Over the years, TSC has grown from a company based in South Africa to a Pan-African company with operations in Mozambique and Namibia. On 20 December 2021, TSC signed and concluded a purchase agreement to acquire 100% of a competitor's shares, TZ Commodity Traders (Pty) Ltd, which also deals specifically in the manufacturing and distribution of steel products. Not much is currently known about the new acquisition, the management team or the rationale for TSC's acquisition of the company.

TSC has a December year end. The audit was initially scheduled to be concluded and signed off by 28 January 2022.

***Minutes of meeting***

Present: Thuli Tau (partner); Catherine Mashego (audit senior)

*Agenda item: Significant events noted during the 2021 financial year (FY2021) for TSC*

- TSC took over the entire physical aluminium inventory as a favour to the chief executive officer (CEO) of MuZi Commodity Traders (Pty) Ltd ('MuZi') towards the end of the financial year at no cost. He is a personal friend of TSC's CEO. MuZi is based in Mozambique and is currently in business rescue. TSC has never traded in aluminium before.
- TSC installed a new inventory management system six months into FY2021. The new inventory management system does not integrate with TSC's accounting system. The accounting system is 15 years old and was never designed to integrate with other systems. TSC has hired five temporary accounting staff to manually capture inventory transactions into the accounting system.

*Agenda item: Matters relating to audit staff and management*

- Thuli told Catherine that she believes that TSC's management is very honourable and law abiding. Therefore, Thuli does not believe that any areas of the annual financial statements are susceptible to fraud and no fraud procedures are necessary.
- Thuli stated that she would not hold fraud discussions with the other audit team members as she did not have any time to spend on that.
- Thuli stated that TSC's management is under a great deal of pressure because they are very busy dealing with potential takeover deals. Therefore, while conducting the audit, Catherine should only send queries to management if these were absolutely necessary.
- Further, all queries from the audit staff should first be sent to Thuli, because she wanted to check what questions were going to be asked of management.
- No other matters regarding fraud risk considerations were discussed or considered.

**Workpaper B135-0 Inventory workpaper on TSC drafted by a trainee accountant and placed on audit file as complete**

<b>Client:</b> Transfrontier Steel Commodities (Pty) Ltd	<b>Year end:</b> 31/12/2021	<b>B135-0</b>
<b>Prepared by:</b> Kethelo Khumalo (trainee accountant)	<b>Date:</b> 15/03/2022	
<b>Reviewed by:</b>	<b>Date:</b>	
<b>Audit area:</b> Inventory		
<b>Subject:</b>		

**Objective:** To determine the value of inventory

**Audit procedures**

- 1 For a sample of ten high-value steel inventory items, inspect the existence of the inventory item by visiting the large storage warehouses and confirming through inspection that the inventory items exist.
- 2 For each sampled inventory item, confirm the quantity on the inventory sheet at the warehouse to the recorded quantity on the stock count sheets and underlying inventory management system.
- 3 For the sample of ten high-value steel inventory items, confirm through inspection that each inventory item is not damaged and is in a saleable condition. Inspect each sampled steel inventory item for damage that could be an indicator of impairment.

<b>Results</b>						<b>Audit procedures</b>		
<b>No.</b>	<b>Inventory code</b>	<b>Inventory description</b>	<b>Quantity per inventory sheet (units)</b>	<b>Quantity per accounting system (units)</b>	<b>Difference</b>	<b>1</b>	<b>2</b>	<b>3</b>
1	WMTC1239	Steel slabs - rolling and billets	15 800	15 800	-	✓	✓	✓
2	MMTC8965	Reinforcing bars (rebar)	9 523	9 063	460	✓	✓	X
3	WHTC7861	Wire rods	5 036	4 958	78	✓	✓	✓
4	SBTC1002	Galvanised coils	18 520	18 520	-	X	X	X
5	GSTC1979	Corrugated sheets	11 569	11 005	564	X	X	✓
6		Perforated sheets				✓	✓	✓
7						✓	✓	✓
8						✓	✓	✓
9						✓	✓	✓
10						✓	✓	✓

**Key:**

✓ =

X =

**CONCLUSION:**

**Workpaper C300-0 Risk assessment for TSC performed by a trainee accountant for review**

<b>Client:</b> Transfrontier Steel Commodities (Pty) Ltd	<b>Year end:</b> 31/12/2021	<b>C300-0</b>
<b>Prepared by:</b> Kethelo Khumalo (trainee accountant)	<b>Date:</b> 16/03/2022	
<b>Reviewed by:</b>	<b>Date:</b>	
<b>Audit area:</b> Inventory		
<b>Subject:</b> Risk assessment – new aluminium products		
<b>Objective:</b> To determine the various risks that could affect the inventory balance for the new aluminium products.		
<b>Risk no.</b>	<b>Risk identification</b>	
A	TSC implemented a new inventory management system six months into the financial year. The new inventory management system does not integrate with TSC's accounting system.	
B	The accounting system is 15 years old and was never designed to integrate with other systems.	
C	TSC has hired five temporary accounting staff to manually capture inventory transactions into the accounting system.	
D	During the inventory count damaged inventory was identified by the trainee. There were piles of aluminium rods that were bent and skew and that did not seem to be in a usable state. The risk is that these damaged goods should be scrapped.	
E	During the inventory count the trainee accountant noticed that the team also had to count inventory that was in a container, separate from the main warehouse. Upon questioning this, the factory manager explained that it was consignment stock held on behalf of one of its suppliers, but it was nevertheless included in TSC's inventory balance.	
F	Upon inspecting the import and freight waybills, the trainee accountant noticed that the freight cost was not taken into account when calculating the inventory values, but rather just expensed through the statement of comprehensive income.	

**INITIAL TEST OF COMPETENCE, JUNE 2022**  
**PROFESSIONAL PAPER 2**

<b>PAPER 2 QUESTION 1 – REQUIRED</b>			<b>Marks</b>		
			<b>Sub-total</b>	<b>Total</b>	
(a)	(i)	Describe eight concerns evident from document A; and	8		
	(ii)	For each concern raised, provide an appropriate policy recommendation in terms of International Standard of Quality Control 1 <i>Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements</i> .	8		
	Use the following format for your answer, based on the example below:				
	<b>Element</b>	<b>(i) Concern</b>	<b>(ii) Appropriate policy recommendations</b>		
	<i>Leadership arrangements</i>	<i>'Promoting a culture of quality control' is not a clearly defined role. The scope of responsibilities and underlying duties related to roles are undefined.</i>		<i>Responsibility for development and documentation of the firm's quality control policies and procedures should be assigned to a designated quality control officer.</i>	
<i>Communication skills – layout and structure</i>			1	17	
(b)	Criticise audit workpaper B135-0 in terms of International Standards on Auditing (ISA) 230 <i>Audit Documentation</i> .		6	6	
(c)	Describe, with reference to Document B, non-compliance by the auditors with their responsibility with regard to fraud in terms of ISA 240 <i>The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements</i> .		12	12	

**Continued on p. 2**

**INITIAL TEST OF COMPETENCE, JUNE 2022**  
**PROFESSIONAL PAPER 2**

<b>PAPER 2 QUESTION 1 – REQUIRED (cont.)</b>		<b>Marks</b>									
		<b>Sub-total</b>	<b>Total</b>								
(d)	<p>Describe, for each of the risks listed in workpaper C300-0 –</p> <ul style="list-style-type: none"> <li>• whether the listed risk would be classified as a financial statement level risk or an assertion level risk;</li> <li>• when an assertion level risk is identified, which assertion(s) will be affected; and</li> <li>• one audit procedure that could be performed to mitigate the risk.</li> </ul> <p>○ Present your answer in the following tabular format:</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 10%;"><i><b>Risk no.</b></i></th> <th style="width: 20%;"><i><b>Financial statement OR assertion level risk</b></i></th> <th style="width: 20%;"><i><b>When assertion level risk, which assertion(s) will be affected</b></i></th> <th style="width: 50%;"><i><b>Describe ONE audit procedure that could be performed to mitigate the risk</b></i></th> </tr> </thead> <tbody> <tr> <td colspan="4" style="text-align: center;"><i>Communication skills – layout and structure</i></td> </tr> </tbody> </table>	<i><b>Risk no.</b></i>	<i><b>Financial statement OR assertion level risk</b></i>	<i><b>When assertion level risk, which assertion(s) will be affected</b></i>	<i><b>Describe ONE audit procedure that could be performed to mitigate the risk</b></i>	<i>Communication skills – layout and structure</i>				14	
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<i>Communication skills – layout and structure</i>											
<b>Total for question 1</b>		1	<b>50</b>								