

Part (a) Discuss the <u>factors</u> that increase the risk of material misstatement for the existence, completeness and accuracy, and valuation and allocation assertions for the cash and cash equivalents balance reflected in the statement of financial position of GreatSave at 31 December 2020.		Marks
General factors that could impact the risk of material misstatement		
1.1	The size of the 'cash and cash equivalents' balance with reference to the total assets is a factor that many of the below possible misstatements identified are likely to result in material misstatements.	1
1.2	At year-end there is R150 000 cash on hand for cash register float (for 6 cash registers) which translates to R25 000 worth of change that must be kept in the cash registers. Furthermore R100 000 is kept as Petty cash for "incidental expenses". This does not seem logical /reasonable and will increase the risk for fraud/errors.	1
1.3	This would be the first time the audit is performed and therefore management (Zach and Susan) have an opportunity to misstate the cash and cash equivalent balance.	1
1.4	Given that BigRetail wishes to invest in GreatSave and Mr Gary Turner is excited about this possible expansion, the shareholders / directors have an incentive to overstate the assets, including 'cash and cash equivalents'.	1
1.5	GreatSave is a small company (directors are working at and controlling the company) and must pay income tax. There is an inherent risk to understate cash and cash equivalents in an effort to pay less taxation.	1
1.6	Due to the significant growth / increase in the volume of transactions , Zach and Susan realised that the cash management system had to be enhanced with stronger controls and therefore without a commensurate improvement in the accounting and internal control system, there is an increased risk that errors can be made and misstatements arise as a result.	1
POS system		
2.1	Zach implemented a new integrated POS system called the Autosale system to record all transactions <u>processed</u> by the POS system electronically and without testing the General controls (including Masterfile amendments), this will result in consistent errors in the transaction listings journalised if the system is not functioning effectively. <ul style="list-style-type: none"> The transfer of the data from the POS system (terminals) to the Autosale system may be incorrect which will result in errors in the transaction listing (and the subsequent journal written to Cash and cash equivalents) 	1 1
2.2	If the customer pays in cash, the cashier could capture the wrong cash amount received (manual process) and/or count the wrong amount of change , which will result in errors.	1
2.3	The card payments machine system is connected to the internet and hence there is a risk that the POS system may be hacked or infected with a virus. <ul style="list-style-type: none"> The risk is further increased as no backups of the accounting information is made or stored in a location separate from Susan's computer, evident in the fact that Susan avoids cloud computing solutions due to concerns over security. 	1 1
Recording		

3.1	There are 6 cashiers who generates transaction listings and Susan downloads these that shows all the transactions for the day (to be recorded) . If there are no controls over ensuring that all transactions are on the list / all 6 listings are recorded, there will be errors in the accounting records.	1
3.2	GreatSave's bank charges a service fee of 2% on the transaction value on all card payments and these transactions may not be accounted for in the bank journals processed. (due to the possible lack of bank reconciliations)	1
3.3	Card payments take 3 business days to process, but the journal is already processed on the day of the transaction , there could be a difference (error) between the amount recorded and the amount in the bank account OR GreatSave might not receive the money at all. (due to the possible lack of bank reconciliations)	1
3.4	As there are no reconciliations done between cash and transaction listings there is a risk that management will not detect errors which occurred and might not correct these. <ul style="list-style-type: none"> • Bank reconciliations are not done and consequently the balance according to the accounting records and the bank account will possibly not be correct. 	1 1
Cash		
4.1	Cashiers, the security company and other staff (petty cash) have direct access to the cash (petty cash / float) and without proper controls, cash can be stolen. Due to the nature and susceptibility of being cash (in its various forms), there is a risk that the cash can be stolen .	1
4.2	GreatSave is a small business with a limited number of employees which do not provide for effective monitoring/supervision. <ul style="list-style-type: none"> • Susan is responsible for incompatible duties / with limited segregation of duties where she is responsible for various functions. If she has the right incentive, she can override the controls and understate / overstate Bank and cash. • No one reviews Susan's work / no independent reviews are done and therefore there could be errors in the cash and cash equivalents balance. • The only other person available for reviews seem to be Zach but as he is Susan's husband, independent reviews will not be possible / overriding of controls possible. • Furthermore, it is apparent that Susan is making errors in the journals being written and this could indicate that other errors may also be present within Cash and cash equivalents. 	1 1 1 1
4.3	Susan records 100% of the card/cash received to ' Bank – current account ' but then she retains a portion of the cash collected for the cash float / Petty cash which may not be recorded / possibly no proof .	1
4.4	Susan holds petty cash which is used for incidental expenses and these transactions may not be accounted for (cash received) and might not reflect the actual flow of cash .	1
Short-term deposit – money market		
5.1	Due to the nature of short-term deposits not having many transactions (not following the normal control activities in the company), there is a risk that this account is not reconciled and the transactions on the account are not accounted for in the accounting records.	1
Available		24
Maximum		17

<i>Communication skills – layout and structure</i>	1
Total for part (a)	18

Part (b) Describe additional controls that should be implemented at GreatSave to prevent or detect the risks of material misstatement in the existence and completeness of the cash and cash equivalents balance.		Marks
1.	General / IT	
1.1	The POS system / Autosale <i>should be linked directly</i> to the accounting system in order to automatically record the transaction journals in order to avoid errors that can occur with manual recording of journals.	1
1.2	Based on the system description Susan is performing incompatible duties and more segregation of duties is encouraged. If it is cost effective, an independent person <i>should</i> be appointed / an accounting firm to perform certain checks/reviews on a monthly basis.	1
1.3	The data/software on Susan’s computer <i>should be</i> backed up regularly and the back-up copy should be stored off-site / in the cloud.	1
1.4	An appropriate anti-virus software program / firewalls etc. <i>should</i> be installed for the POS software, to reduce the risk of a virus corrupting the data, or hacking because it is linked to the bank via the internet/external network.	1
1.5	The POS terminals should only be accessed through the input of a valid username and password by the cashier and transactions should be recorded per cashier by shift.	1
1.6	The cashier should not leave the cash register unattended and <ul style="list-style-type: none"> • The system should shut down after a few seconds of inactivity / unsuccessful attempts • Cashiers can only scan and Supervisor should be limited to authorising transactions but cannot scan and obtain access to the cash (Least privilege / user profiles). 	1 1 1
1.7	A strong ethical and visible policy on ethics, and zero tolerance of fraud and theft (whistle blow procedures in place and visible to customers) should be implemented / Policies and enforcement of recruitment process for cashiers / persons to work with cash (no criminal records).	1
2.	Cashiers	
2.1	There should be limited exit points (preferably one) at the store.	1
2.2	The six cash registers should be strategically positioned and secured to limit the risk of theft.	1
2.3	The cashiers <i>should be</i> monitored by a store manager or Zach, or a CCTV camera system should be installed in the store to monitor the cashiers to ensure that they are performing their duties as required and are not misappropriating cash.	1
2.4	There should be a security guard that inspects customers’ receipts against the goods they have in their possession (or vice versa) as they leave the store to ensure that all transactions are processed through the POS system / Signage (visible to customers) should encourage customers to request a receipt and inspect the receipt and change received.	1
2.5	Cashiers should check and sign for the <u>float they receive</u> at the start of each shift.	1

2.6	All credit and debit card proof of payment slips (from the card machine) should be issued in duplicate and sequentially numbered . One should be given to the customer, and one should be kept by the cashier, OR A card payments listing should be generated (by the card machine) at the end of the shift (for record of payment methods to be used for reconciliation purposes).	1
3.	Cashing up	
3.1	All cashiers should 'cash up' (count the money in the till) at the end of their shift (can be done more frequently if necessary) under the supervision of Susan (she must review). <ul style="list-style-type: none"> There should be 2 individuals involved/present at all times (Susan and the cashier) and one of the 2 should never be left alone with the cash until the cashing up is completed and documented. 	1
3.2	The cash (after deducting the cash float received at the beginning of each cashier's shift) and the proof of payments slips in the till/ card payments listing extracted from the card machine should be reconciled to the transaction listing extracted from the POS system and documented on a cash-up sheet.	1
3.3	The cashier and Susan should sign a 'cashing-up sheet' to acknowledge the procedures that took place during the cashing up and that the two parties agree.	1
3.4	Any surpluses or shortages (large/frequent differences) in cash should be explained and indicated clearly on the 'cashing-up sheet" and acted upon in terms of a company policy (disciplinary actions).	1
3.5	After the reconciliation of the cash received compared with the transaction listing / shortages, the float must be accounted for on the cash-up sheet for the next day.	1
4.	Recording of transactions	
4.1	A sequential number <i>should</i> be allocated to all transactions by the Autosale system: <ul style="list-style-type: none"> Susan should on a daily basis inspect the sequence of transactions on the POS transaction listing to determine whether any transactions are missing / duplicated. (A sequence check can also be executed by the Autosale system and generate exception reports) 	1
4.2	Susan <i>should</i> also inspect the POS transaction listing to determine whether the first transaction number of the day follows on the last transaction number of the previous day to ensure that there are no duplicate / missing transactions.	1
5.	Banking / Security company	
5.1	The contract with the security company <i>should</i> stipulate that the security company is liable for any cash collected for depositing at the bank that is not deposited.	1
5.2	The security company should sign a register / document etc. as proof that they took custody of the cash (the container is secured, and it will not be cost-effective to count).	1
5.3	Cash for collection by the security company should be stored in a drop safe until collected by the security company, and only the security company should have the keys to that safe.	1
6.	Follow up afterwards	
6.1	A bank reconciliation <i>should</i> be prepared on a monthly basis: <ul style="list-style-type: none"> To agree the cash handed over to the security company with the receipt (cash deposit slip) from the bank to ensure that all 	1

	<p>cash has been banked; and to agree the deposit slips (cash deposits) with the bank statement to ensure that all cash has been accounted by the bank; and</p> <ul style="list-style-type: none"> To agree card payments on the POS transaction listing and the bank statement on a daily / weekly basis to ensure all card payments are received in the bank. 	1
7.	Petty cash	
7.1	Petty cash should be the sole responsibility of one person (only this person should have access to the keys).	1
7.2	<p>Cash <i>should</i> only be advanced from petty cash on production of a pre-authorized expense voucher.</p> <ul style="list-style-type: none"> The voucher should be authorised by an independent person / second person. 	1 1
7.3	The petty cash vouchers <i>should</i> be pre-numbered sequentially	1
7.4	All petty cash vouchers should have an original invoice / supporting document attached.	1
7.5	Cash received in the Petty cash must be limited to a specific maximum amount and the “top-up” amount must be exactly the amount of expenses from the previous “top-up”.	1
7.6	<p>Susan (or Zach) <i>should</i> regularly count the petty cash and the supporting invoices should be checked regularly and</p> <ul style="list-style-type: none"> Agreed to the balance reflected in the financial records to determine that no cash has been stolen/missing OR Perform a Reconciliation to the financial records. 	1 1
8.	Short-term deposit - Money market	
8.1	Susan <i>should</i> obtain monthly statements from the bank for the short-term deposit in the money market account and agree it to the balance reflected in the financial records, and ensure that any withdrawals / deposits / transactions are accounted for (bank reconciliation) in the accounting records.	1
8.2	Susan should follow up with the bank in the event where the bank has omitted interest or deposits / withdrawals.	1
	Available	40
	Maximum	14
	<i>Communication skills – clarity of expression</i>	<i>1</i>
	Total for part (b)	15

Part (c) Discuss, with reference to the information provided, the matters that N&G should consider before accepting the engagement to audit the FY2020 financial statements of GreatSave.		Marks
<ul style="list-style-type: none"> Exclude any recommendations for safeguards that N&G should implement. 		
CLIENT CONSIDERATIONS		
Independence considerations - COPC		
Relationships		
1	There is a possible familiarity threat to independence <u>because</u> : <ul style="list-style-type: none"> Zach and Phyllis are family friends which leads to Phyllis might be <u>too sympathetic</u> to Zach's concern of expanding the business whilst performing the audit (COPC 521). 	0.5 1
1.1	There is also a possible intimidation / self-interest threat to independence <u>because</u> : <ul style="list-style-type: none"> Phyllis might <u>not want to upset Zach</u> by pointing out errors in the financial records/weaknesses in the business. 	0.5 1
1.2	The <u>level of the threat</u> will not be at an acceptable level as the parties involved are family friends and they are the Engagement partner and the shareholder and director of the company (roles on audit team, position of client and nature of the relationship).	1
Dependency on audit fees		
2	There is a possible self-interest threat to independence <u>because</u> : <ul style="list-style-type: none"> N&G is currently experiencing financial difficulties, and this will create <u>concerns of receiving all the fees to address</u> these difficulties in which they hold an interest; and 	0.5 1
2.1	There is also a possible intimidation threat to independence <u>because</u> : <ul style="list-style-type: none"> the client (Zach) is aware that the auditors are struggling financially, and this may <u>use this information for his own benefit</u>. 	0.5 1
2.2	With limited information available it should be considered what the <u>level of the threat</u> will be depending on the current financial position of the audit firm and how severe the financial difficulties are and what the value of the fees (size) will be in comparison to the total fees / Material to the auditors.	1
Non-assurance services		
3.1	GreatSave is not classified as a public interest entity <u>because</u> GreatSave is not a listed entity ; and <ul style="list-style-type: none"> GreatSave would also not be considered a public interest entity because this is not an entity that would have significant public relevance (due to not having a large number and wide range of stakeholders due to its size / nature). 	1 1
3.2	Tax calculations (consulting): There is a possible self-review threat to independence <u>because</u> : <ul style="list-style-type: none"> N&G will be <u>biased</u> when auditing the tax calculation previously <u>performed by themselves</u>. 	0.5 1 1

	<ul style="list-style-type: none"> The materiality of the tax calculation will have an impact on the <u>level of the threat and who</u> performed / was responsible for the calculation. 	
3.3	Tax Returns (consulting): In terms of COPC 604, assisting clients with drafting of tax returns does not usually create a threat.	1
3.4	Accounting services (payroll) Providing payroll services to the audit client will result in a self-review threat to independence <u>because</u> : <ul style="list-style-type: none"> N&G will be <u>biased</u> when auditing the payroll calculation previously <u>performed by themselves</u>. The <u>level of threat</u> will depend on whether the services are routine (we do not take on management responsibilities) and who performed the serviced payroll services initially and as the payroll calculations are performed based on the information provided by the GreatSave accounting software package, the service can be considered to be of a routine / mechanical nature (COPC 601.4 A1) (and can be accepted). 	0.5 1 1
Independence considerations – Companies Act		
4.1	N&G would have to consider the possible independence requirements in terms of section 90 of the Companies Act, but because this is a voluntary audit this does not apply.	1
Management integrity considerations		
5.1	It should be considered whether Zach’s statement about audit fees assisting the firm indicate that Zach might potentially attempt to unduly influence Phyllis later or whether this <u>was truthful</u> due to them being friends.	1
5.2	Management has an <u>incentive to manipulate</u> the AFS since they will be presenting the AFS to a potential investor .	1
Financial Responsibility		
6.1	It appears that the client is willing to pay the audit fee <u>because</u> they state the money will assist the audit firm with their financial position and <ul style="list-style-type: none"> able to settle the audit fee because they have a very healthy cash flow position. 	1 1
AUDITOR’S CONSIDERATIONS		
7.1	<u>Industry knowledge / understanding:</u> N&G has been providing various non-assurance services to GreatSave in the past and has a good understanding of the small retail industry .	1
7.3	<u>Resources / enough staff members:</u> It could be argued that because the audit firm is small with only 2 partners , there is a possibility that they may not have enough staff members to complete the audit on time.	1
7.4	<u>Time/Audit deadline:</u> <ul style="list-style-type: none"> It could be argued that there is a tight audit deadline because it is currently 20 January 2021 according to the email and the transaction need to be finalised by 28 February 2021 and therefore we do not have enough time to complete the additional audit in this time frame (with our other work planned for this period) and 	1

	<ul style="list-style-type: none"> • Apart from the 2020 audit the audit firm will need to perform additional audit procedures in terms of ISA510 on the opening balances and therefore they might struggle to meet the audit deadline, although • Auditing one small retail company, with one store, with a relatively simple accounting process could be reason to accept this engagement as one can easily meet this audit deadline if staff is available. 	1 1
7.2	<p><u>Potential need for an auditor's expert:</u> Since the input, processing and output occurs through barcodes being scanned (no input documents) and processing that happens in the Autosale system, the auditors need to be able to rely on the system to obtain sufficient appropriate audit evidence and therefore the auditor will possibly need the assistance of an IT expert to audit the POS system OR Software to perform CAATS.</p>	1
7.5	<p><u>Legal liability:</u> There may be a risk of legal claims resulting from accepting the engagement, especially as Big Retail will be using the audited financial statements to make an investment decision. (Sec 46 APA).</p>	1
TERMS OF ENGAGEMENT		
8.1	<p>Zach is requesting that the audit procedures start before the engagement letter is signed. This is in contravention of ISA 210 and the engagement letter must be signed beforehand.</p> <ul style="list-style-type: none"> • The firm would first need to determine whether the pre-conditions are present, which include that the relevant financial reporting framework is appropriate; and • Zach expects the audit to be a quick process since he is of the view that N&G already understands the business. This illustrates that he does not understand the full audit process, and should be explained in the engagement letter to set out each parties' responsibilities. 	1 1 1
8.2	<p>It is recommended that the audit fee must be agreed with the client beforehand because it seem that the client is under the impression that an audit can be performed quickly and possibly won't cost that much based on other work performed and because additional audit procedures (ISA510) also will need to be performed.</p>	1
8.3	<p>The appointment date is already 20 January 2021 and year-end was 31 December 2020 and therefore certain audit procedures like inventory counts, cash counts etc. should have been performed at year-end / alternative procedures must be considered but there are various weaknesses in the new system, there could be a possible limitation of scope in terms of ISA210.7 and consequently this engagement should not be accepted.</p>	1
Available		33
Maximum		16
<i>Communication skills – logical argument</i>		<i>1</i>
Total for part (c)		17