

QUESTION 2

50 marks

1 Background

GreatSave (Pty) Ltd ('GreatSave') is a small family-owned store that sells groceries and assorted household goods. The store was opened 25 years ago by Mr Zach Andreas and his wife Susan, in the Alberton area in Gauteng. Zach and Susan are the sole owners and only directors of GreatSave. The store is ideally located close to a highway off-ramp which has resulted in significant growth in the business over time.

Zach, constantly looking for ways to enhance the shopping experience of his customers, has taken advantage of developments in the electronic payments industry over the years. Amongst others, he implemented an integrated point-of-sale (POS) system, called Autosale, that records all transactions processed by the POS system electronically and enables payment of transactions by means of debit and credit cards.

These changes resulted in a significant increase in foot traffic in the store during the financial year ended 31 December 2020 (FY2020). Zach and Susan realised that because of the increase in the volume of daily transactions, the cash management system in the store had to be enhanced with stronger controls.

At the end of FY2020, cash and cash equivalents reflected in the statement of financial position were as follows:

	R
POS cash register float (cash on hand)	150 000
Petty cash (cash on hand)	100 000
Bank – current account	498 500
Short-term deposit – money market	1 250 000
Total cash and cash equivalents	1 998 500

The total assets held at year end amounted to R4 501 700, and therefore cash and cash equivalents make up a significant portion of the assets on the statement of financial position.

2 Cash management system

The store does not extend credit facilities to customers, and customers need to pay for all purchases before exiting the store, at any of the store's six POS terminals. Each POS terminal is equipped with a POS cash register, screen, card swipe machine, receipt printer and a barcode scanner. Each POS terminal is also linked to the Autosale system, and is operated by a cashier. When customers present their shopping to the cashier, all the barcodes on their purchased items are scanned by the cashier. The Autosale system accesses the inventory masterfile, which contains a record of prices of all items. The POS terminal screen then displays the item description and price.

The total amount payable (including value-added tax (VAT), since GreatSave is a VAT vendor) is calculated after all the items have been scanned. The cashier next selects a payment option on the cash register based on the customer's payment preference (cash or card):

- If the customer pays in cash, the cashier captures the amount received from the customer and the cash drawer automatically opens and the amount of change, if any, is displayed on the screen. The cashier inserts the cash and takes out the necessary change.
- If the card option is selected, the transaction activates on a card machine connected to the POS terminal, and the customer inserts a credit or debit card into the card machine and enters a personal identification number (PIN) to effect payment.

Once payment is successful, a duplicate cash register slip is printed from the receipt printer; one copy is handed to the customer and one is kept by the cashier.

Card payments can take up to three business days to be processed and be reflected in the GreatSave bank account. GreatSave's bank charges a service fee of 2% of the transaction value on all card payments.

2.1 Accounting process

At the end of each business day, Susan downloads a transaction list from the Autosale system, which shows all the transactions that were recorded during the day. The list also shows whether the transactions were processed using cash or a card.

Susan uses this list to calculate the total revenue earned on the day. She then posts the following journal entry in GreatSave's accounting package:

Dr Bank – current account
Cr Revenue

GreatSave uses an off-the-shelf accounting package with strong built-in application controls to maintain its financial records from which annual financial statements are prepared. The accounting package has been installed on Susan's laptop computer, which is locked in the office in the store. Susan avoids cloud computing solutions because of her concerns about security. The computer as well as the accounting software are secured using logical access controls. Only Susan and Zach have access to the computer and software.

The cash collected during the day at each cash register from each cashier is processed by Susan at the end of each business day. She counts all the cash and places it in a secure container, together with a completed bank deposit slip which she prepared. The container is handed over to a security company that deposits the cash into GreatSave's bank account at a bank branch. Susan retains a portion of the daily cash takings for the next day's cash float (used to provide change to customers). Petty cash is also held, and is used to settle incidental expenses. The float, as well as petty cash, is locked in the store's safe. Only Susan and Zach have keys to the safe.

3 Potential investor

During January 2021, Zach and Susan was approached by Mr Gary Turner, the financial manager of Big Retail Ltd ('Big Retail'), who is interested in investing in GreatSave. Zach was excited about the possible investment as this would provide an opportunity for further expansion. One of the conditions of the offer is that audited financial statements be presented to Big Retail. GreatSave had never before been audited, because this was not a requirement of the Regulations in terms of the *Companies Act*.

Zach immediately contacted Nathan & Gauldie Inc. ('N&G'), to perform an audit for FY2020. N&G is a small auditing and accounting firm headed by two partners, Ms Phyllis Nathan and Mr Andrew Gauldie. N&G currently assists Zach on an annual basis with tax consultation services, which include completing GreatSave's annual tax returns, assisting with tax calculations, and performing payroll calculations based on the information recorded by means of the accounting software.

Zach originally decided to use N&G for the tax and payroll services as Phyllis is a friend of the Andreas family, and therefore he was comfortable trusting N&G with the financial matters of GreatSave.

The following is an email trail evidencing N&G's acceptance of the audit engagement:

To: Zach@GreatSave.co.za
From: Phyllis@N&G.co.za
Date: 20/01/2021 13:27
Subject: RE: RE: Audit of GreatSave December 2020 financial statements

Hi Zach

I am happy to start with the audit immediately. The engagement could not have come at a better time!

Kind regards
Phyllis

Audit Partner – N&G Inc.

To: Phyllis@N&G.co.za
From: Zach@GreatSave.co.za
Date: 20/01/2021 11:01
Subject: RE: Audit of GreatSave December 2020 financial statements

Hi Phyllis

I hope you and the family are well.

I just received the email below from Big Retail and need your assistance. It would help if you could start with the audit immediately; these guys are in a huge hurry and I don't want to keep them waiting!

I don't think the audit will take all that long – after all, you know the business by now from all the work you do for us. I know there is probably a bit of admin to complete before you start working, but in the interest of time, please send your audit clerks along in the meantime; we can complete the formalities at a later date.

I heard that Covid-19 has hit your practice quite hard. Hopefully this audit will help you keep your head above water for now.

Kind regards, Zach

CEO GreatSave

To: Zach@GreatSave.co.za
From: Gary@BigRetail.co.za
Date: 20/01/2021 10:15
Subject: Audit of GreatSave December 2020 financial statements

Dear Zach

With respect to our prior discussions on the requirement for providing audited financial statements, please ask your auditor to start with their audit procedures immediately. We need to finalise this transaction before our financial year end on 28 February 2021, and you know how long these auditors can take just to tick a few boxes.

Kind regards
Gary Turner

Financial Manager - Big Retail

INITIAL TEST OF COMPETENCE, SEPTEMBER 2021

PROFESSIONAL PAPER 4

PAPER 4 QUESTION 2 – REQUIRED		Marks	
		Sub-total	Total
(a)	Discuss the factors 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. <i>Communication skills – layout and structure</i>	17 1	 18
(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. <i>Communication skills – clarity of expression</i>	14 1	 15
(c)	Discuss, with specific reference to the information provided, the matters that N&G should consider before accepting the engagement to audit the FY2020 financial statements of GreatSave. • Exclude any recommendations for safeguards that N&G should implement. <i>Communication skills – logical argument</i>	16 1	 17
Total for question 2			50
TOTAL FOR PAPER 4			100