

SOLUTION AUDIT AND INTERNAL REVIEW NOVEMBER 2010

QUESTION 1

- (a)
 - i. Integrity and ethical values of management
 - ii. A commitment to competence
 - iii. Participation of the board of directors or audit committee
 - iv. Management philosophy and operating style
 - v. Organisational structure
 - vi. Assignment of authority and responsibility
 - vii. Human resource policies practices.
- (b)
 - i. Supervision – the system analysts who specify the system should exercise supervision over programming and testing of programs.
 - ii. Individual testing of programs – each computer program which goes towards making up a module of programmer should be individually tested by programmers prior to testing as a system.
 - iii. Authorisation – once testing of the system has been completed the data processing manager can authorise the operation of the system by user departments.
 - iv. Testing by users – the final stage will be testing of the system by the user departments who should ensure that it meets their requirements. Modifications may be necessary if the user requirements are not met in full.

Documents of the system should include:

- (a) - A draft manual produced prior to testing of the system
 - (b) - Listing of program instructions, flow charts, file layouts, input and output Documentation and the procedures which program module covers.
 - (c) - A final version of operating manual following testing of the system
 - (d) - Details of procedures to be followed if a system crash occurs.
- (c) The components of an internal control structure are
- i. The information system is the set of procedures established to identify, classify and record transactions and other events and the records maintained to record details of assets and liabilities.
 - ii. Control procedures are policies and procedures that help to ensure that necessary actions are taken to address the risks involved in the achievement of the entity's objectives.
 - iii. The control environment sets the tone of the organization influencing the control consciousness of its people. Control environment reflects the overall attitude, awareness and actions of management regarding internal control and its importance in the entity.

QUESTION 2

ABC & Co
P. O. Box GP 400
Accra

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Messrs Black and White
Black and Company
Tamale

Dear Sir,

INTERNAL CONTROL SYSTEMS

During the course of our audit we reviewed the systems of Internal Control operated by the company. We feel there are significant weaknesses in the system mainly created by the lack of division of duties between your staff. This could lead to significant errors remaining undetected for long periods.

In addition, without wishing to imply any dishonesty by the staff, we must bring to your attention the scope for fraud due to each employee having control of a complete accounting function.

We believe that if the tasks of the staff are reallocated as set out below it would be possible to improve greatly the internal control systems without incurring the additional expense of extra staff. The present staffs are competent and will have sufficient time to deal with all of the commended jobs.

We must also recommend that you become involved in the accounting function to the extent of authorizing certain transactions and periodically reviewing the work of your staff. This would considerably strengthen the overall control system.

Recommendations:

<u>PURCHASES</u>	<u>REPONSIBILITY</u>	<u>OTHER POINTS</u>
Ordering goods	Miss Abdulai	Major items should be authorised by a Director
- Checking invoices and posting to the ledger	Miss Damba	
- Payment of invoices and purchase ledger queries	Miss Chimsi	
2. SALES		
- Dealing with customers' orders	Miss Damba	Authorisation of credit notes by a Director

- Preparation of invoices Miss Abdulai
- Posting to sales ledger Miss Damba
- Receipt of cash and raising remittance advices Miss Chimsi
- Posting to sales ledger and dealing with queries Miss Damba

3. PAYROLL

- Preparation of payroll Miss Chimsi Checked periodically by a Director
- Preparation of pay packets Miss Abdulai
- Payout of wages Miss Damba

4. CASH BOOK

- Writing up receipts and payments Miss Chimsi Monthly bank reconciliation to be checked by a Director
- Petty cash Miss Chimsi

5. NOMINAL LEDGER

- Writing up Miss Abdulai Periodically reviewed by a Director

We would be pleased to discuss these recommendations with you and their implementation. Please do not hesitate to contact us if we can be of further assistance.

Yours faithfully,

ABC & Co
Chartered Accountants

QUESTION 3

- (a) Audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. A risk based audit approach is where the auditor obtains an understanding of an entity and its environment, and having assessed the risks of material misstatements in the financial statements at the assertion level, directs audit resources to the risky areas as appropriate. The risk of material misstatements may come from inherent risk and control risk.

Inherent risk and control risk are the entity's risks and they exist independently of the audit of the financial statements.

- (b) The auditor may adopt the following approaches in the audit of an estimate
- Review and test the process used by management to develop the estimate
 - Use an independent estimate for comparison with that prepared by management
 - Obtain approval for the existence of the estimate
 - Review subsequent events which confirm the estimate made
 - Vouch estimate with other relevant records precipitating the estimate e.g. wage line of employee.
- (c) Information required on working papers
- Client's name e.g. Chocho Ltd.
 - The balance sheet date
 - The file reference of the working paper
 - Date the working paper was prepared
 - Subject of the working paper
 - The date the working paper was reviewed
 - The name or initials of the person preparing the working paper.
- (d) Reasons for obtaining evidence from an expert
- (i) Legal opinion e.g. interpretation of legal terms
 - (ii) Measurement of completed works
 - (iii) Determination of condition of property plant and equipment
 - (iv) Valuation of assets
 - (v) Determination of quantities of assets
 - (vi) Credibility to audit work.

QUESTION 4

- (a) Zelcom Ltd's internal audit department may be involved in the following
- (i) Review and monitoring of accounting and internal control systems and making regular recommendations to reduce theft, fraud etc.
 - (ii) Examination of financial and operating information including carrying out detailed testing of transactions and balances
 - (iii) Review of company's efficiency, economy and effectiveness
 - (iv) Review of compliance with regulatory requirements and all applicable laws
 - (v) Assessment of movement of stock and recommending purchases of items that are fast selling.
- (b) Benefits of computer-based accounting systems are
- (i) Performance of complex calculations and processing of large volumes of data or transactions
 - (ii) Availability and accuracy of information
 - (iii) Timeliness e.g. decision making
 - (iv) Additional analysis of data available
 - (v) Enhance monitoring of performance
 - (vi) Reduce risk of circumventing controls
 - (vii) Promote effective segregation.
- (c) Objectives of credit sales
- (i) All credit sales are authorised and approved within the specific period
 - (ii) Ensure only entities entitled to credit sales have access to the facility and standing data on credit sales is regularly matched with credit sales records
 - (iii) Ensure that the entity receives all cash due from the credit sales on the agreed date
 - (iv) Ensure that all credit sales proceeds are properly recorded
 - (v) Ensure that all receipts from credit sales are banked.
- (d) Limitations of relying on faxed confirmation
- (i) A fax is more susceptible to alteration than a letter received by the auditor through post.
 - (ii) Anyone with fax machine can send auditors fax allegedly from the debtor.
 - (iii) Faxes on any paper other than plain paper over time leading to loss of audit evidence.

The following additional procedures may be used

- Obtain independent confirmation that the debtor actually sent the fax
- Follow up with written confirmation is necessary.

QUESTION 5

a) The duties of auditor in respect of corporate governance are as follows:

- Include the extension to the directors' remuneration matter in the normal auditing and reporting duties.
- Review the directors' statement on going concern and the seven other items.
- Review the rest of the information included on corporate governance in the annual report.
- Auditors may need to report departures from the code by a statement in the auditors' report.

b) The circumstances that may give rise to disagreement are:

- In appropriate accounting policies
- Regarding fact or amount (example failure to provide a bad debt).
- Regarding manner or extent of disclosure or facts.
- Regarding compliance with legislation or other requirement.

c) The issues that may be included in a planning memorandum are:-

- Terms of the engagement: that is the work to be done (audit) precise accounting work to be done for the client, task etc.
- The clients and his background: that is history of the company, products locations especially noting factors like new managing director, new computer and new product.
- Important figures and ratios: that is from previous year and if available from management and draft account.
- Audit risk areas: this might include stock, work in progress
- List of all assets and liabilities revenues and expenses with summaries of the procedures to be adopted to verify them.
- Extent of involvement of internal audit
- Requirement for involvement of specialist\setting of materiality levels

- d) Clients assistance: this is, assistance from the client may be required in providing document and analysis providing computer time, among visits to branches.
- The audit approach: that is, the extent of reliance on internal controls the used of substantive test and analytical review procedures.
 - Time table: that is date of interim, year end and final audit and of deadlines to meet e.g. annual general meeting
 - Staff requirement
 - Budgeted fees.