

**AUI2601**

May/June 2013

INTERNAL AUDITING. THEORY AND PRINCIPLES

Duration 2 Hours

100 Marks

EXAMINERS

FIRST

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SECOND

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Use of a non-programmable pocket calculator is permissible

Closed book examination

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THIS PAPER CONSISTS OF **EIGHT (8)** PAGES

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PLEASE NOTE:

Although the primary purpose of the examination is to test the candidate's knowledge of and ability to apply the subject matter, the examiners will also take into consideration the candidate's ability to organise and present such knowledge in acceptable written English

[TURN OVER]

QUESTION 1

15 marks

REQUIRED

For each subsection of this question, select only **one** alternative that you consider to be the most correct answer. Write down the number of the subsection and the letter that indicates the alternative you have selected. Answer the subsections of this question in numerical sequence. For example

1.1 A

1.2 B

Each question counts 1½ marks

1.1 Which of the following alternatives is **not** a specific principle which internal auditors are expected to apply and uphold, according to the Institute of Internal Auditors Code of Ethics?

A Integrity

B Responsibility

C Confidentiality

D Objectivity

1.2 Indicate the alternative that correctly completes the following sentence

The position of the chief audit executive is correctly defined as the

A auditor general

B external provider of internal audit assurance services

C person responsible for overseeing the contract of the external provider of internal audit services

D person employed by the organisation who is responsible for the internal audit activity

1.3 Which one of the following alternatives is **not** an internal audit procedure?

A Recalculating the depreciation of fixed assets

- B Verifying that there are two signatures of senior officials on all cheques
 - C Recommending improvements for the internal control system
 - D Observing the daily clocking in of employees
- 1.4 With whom does the primary responsibility for establishing and maintaining an internal control system rest?
- A The internal auditor
 - B The external auditor
 - C The management of the organisation
 - D Information system specialists
- 1.5 Which of the following alternatives is **not** one of the four functions of management?
- A Reviewing
 - B Organising
 - C Directing
 - D Planning
- 1.6 Indicate the alternative that **correctly** completes the following sentence
- In order to be sufficient, audit evidence must
- A bear a direct relationship to the audit finding and must include all the elements of an audit finding
 - B be well documented and cross-referenced in the audit working papers
 - C refer to information that helps the organisation meet its goals
 - D be adequate and convincing enough for a prudent person to reach the same conclusion

[TURN OVER]

- 1.7** The internal auditor prepares working papers primarily for the benefit of
- A The audit committee
 - B The executive management of the auditee
 - C The internal audit activity
 - D The chief audit executive
- 1.8** During the internal audit of sales representatives' travel expenses, the internal auditor calculates the average travel expenses per day for each of the sales representatives. He then examines the detailed receipts of sales representatives who have high daily averages. These audit procedures represent the use of which of the following types of audit evidence?
- A physical and oral evidence
 - B analytical and documentary evidence
 - C analytical and physical evidence
 - D documentary and physical evidence
- 1.9** An element of authority attributed to the internal audit activity that should be included in its charter is the
- A establishment of the internal audit activity's position within the organisation
 - B identification of the organisational units where internal audit engagements must be performed and the frequency of such engagements
 - C identification of the different types of disclosures that must be made to the audit committee
 - D access to the external auditor's working papers and engagement letter

1.10 Select the **incorrect** alternative regarding the required personal qualities of an internal auditor

- A Internal auditors should have insight into the technical influences of accounting, together with an interest in learning more about matters with which they are not proficient
- B Internal auditors must never allow practical experience or reasoning to distort their theoretical opinion
- C Internal auditors should always adhere to the ethical code that governs the internal audit profession, always acting in a sincere, honest and impartial manner
- D Internal auditors must have the ability to exercise patience. Repetitive and routine work, although monotonous, should not affect their vigilance and concentration negatively

QUESTION 2

15 marks

The International Professional Practices Framework (IPPF) contains three mandatory elements, namely (a) the Definition of Internal Auditing, (b) the Code of Ethics, and (c) the International Standards for the Professional Practice of Internal Auditing (Standards)

REQUIRED

Marks

With reference to the Institute of Internal Auditors (IIA) Code of Ethics, conclude and explain, whether each of the scenarios below is permissible or not. Please provide reasons for each of your conclusions

- 2.1** To save organisational costs, the chief audit executive has cancelled all staff training for the next two years on the basis that all internal audit staff is too new to benefit from such training **(3)**
- 2.2** An internal auditing team has made observations and recommendations that should significantly improve a department's operating efficiency. As a token of appreciation, the department manager presents James, the internal audit manager with a gift of moderate value. Since it shows appreciation for the work and because it is the holiday season, James accepts the gift **(3)**
- 2.3** Simon, an internal auditor has been assigned to audit the human resources department which is managed by his wife **(3)**

[TURN OVER]

- 2.4 Matthew, an internal auditor for a manufacturer of office products, has recently completed an engagement to evaluate the marketing function. Based on this experience, Matthew spends several hours one Saturday working as a paid consultant to a local hospital that intends conducting an engagement to evaluate its marketing function. (3)
- 2.5 An internal auditor did not report significant findings about illegal activity to the audit committee because management had indicated they would handle the issue. (3)

(Gleim and Wiley CIA Review adapted)

QUESTION 3

41 marks

You have recently been appointed as the chief audit executive (CAE) of a newly formed internal audit division at Data Magic (Pty) Limited. The company specialises in software training and has grown substantially over the last five years. The managing director, who appointed you, believes that your appointment and the establishment of an internal audit department would assist her to better improve control in this fast growing company.

After your first few weeks, the internal audit department is slowly shaping up. You are planning to present a workshop for all the departments of the organisation, to present the internal audit department and its workings.

REQUIRED

Marks

In your presentation, discuss the following topics:

- 3.1 Describe six (6) advantages of having an internal audit function in the organisation. (6)
- 3.2 An internal auditor is also an adviser in the organisation. Give seven (7) examples of how internal audit can assist management. (7)
- 3.3 Explain the aspects that should be included in the internal audit charter that grant internal audit the necessary authority. (5)
- 3.4 List seven (7) responsibilities of the internal audit activity as per the internal audit charter. (7)
- 3.5 List seven (7) practices that would enhance a good relationship between the audit committee and the internal audit activity. (7)

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- 3.6 Mention nine (9) actions which can contribute to good co-operation and co-ordination between the internal and external auditors (9)

QUESTION 4

10 marks

You recently attended a conference jointly organised by the Association of Certified Fraud Examiners and the Institute of Internal Auditors. The theme of the conference was **"The diverse roles of internal auditors in today's world"**

The Chief Audit Executive has asked you to prepare a brief presentation as a way of sharing with your colleagues what you learnt at the conference. He has asked that your presentation should cover at least a discussion of fraud and risk management.

REQUIRED

Marks

- 4.1 Explain the roles of management and the internal auditor with regard to risk management (5)
- 4.2 Explain the internal auditor's role in the **detection** of fraud (5)

QUESTION 5

19 marks

You have just been promoted to the position of senior internal auditor and your new responsibilities include providing training to internal audit trainees. As you go through the training file that was used by your predecessor you come across a comprehensive list of possible internal controls that can be performed in an organisation.

- 1 Payments received in the post are opened by two people. The payments are recorded in a remittance register by those responsible for opening the post.
- 2 The accounting clerk performs bank reconciliations monthly and the reconciliations are reviewed and signed by the supervisor.
- 3 At the wages payout, employees should provide proof of identification and acknowledge receipt of their wages by signing the payroll register.
- 4 The financial director reviews and signs exception reports every month before releasing payment to suppliers.
- 5 Cheque signatories cancel (by stamp or crossing) all supporting documentation so that these cannot be presented again for payment.

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REQUIRED

Marks

- 5.1** Explain to the trainees, the steps an auditor would follow when **planning** an audit **(4)**
- 5.2** For each of the internal controls listed in the scenario above
- (a) Describe **one (1)** audit procedure (test of control) that may be used to determine whether the control is working as intended, and **(10)**
- (b) Indicate the kind of audit evidence obtained **(5)**

Your solution to 5.2 should be structured as follows

Control number	Audit Procedure (5.2 (a))	Audit Evidence (5.2 (b))